

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

Form 10-K

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

For the fiscal year ended December 31, 2004

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

For the transition period from to

Commission File Number 000-50327

iPass Inc.

(Exact name of Registrant as specified in its charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

93-1214598
(I.R.S. Employer
Identification No.)

3800 Bridge Parkway
Redwood Shores, California 94065
(Address, including zip code, of principal executive offices)

(650) 232-4100
(Registrant's telephone number, including area code)

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

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, \$0.001 Par Value

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

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

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

Aggregate market value of the registrant's common stock held by non-affiliates of the registrant, based upon the closing price of a share of the registrant's common stock on June 30, 2004 as reported by the Nasdaq National Market on that date: \$466,202,024. The determination of affiliate status for the purposes of this calculation is not necessarily a conclusive determination for other purposes. The calculation excludes approximately 18,186,994 shares held by directors, officers and stockholders whose ownership exceeded five percent of the registrant's outstanding Common Stock as of June 30, 2004. Exclusion of these shares should not be construed to indicate that such person controls, is controlled by or is under common control with the registrant.

The number of shares outstanding of the Registrant's Common Stock, \$0.001 par value, as of February 28, 2005 was 62,907,510.

iPASS INC.

FORM 10-K

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2004

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Disclosure Regarding Forward-Looking Statements

This annual report on Form 10-K contains forward-looking statements regarding future events and our future results that are based on current expectations, estimates, forecasts, and projections about the industries in which we operate and the beliefs and assumptions of our management. Words such as “expects,” “anticipates,” “targets,” “goals,” “projects,” “intends,” “plans,” “believes,” “seeks,” “estimates,” variations of such words, and similar expressions are intended to identify such forward-looking statements. In addition, any statements which refer to projections of our future financial performance, our anticipated growth and trends in our business, and other characterizations of future events or circumstances, are forward-looking statements. Readers are cautioned that these forward-looking statements are only predictions and are subject to risks, uncertainties, and assumptions that are difficult to predict. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. Readers are directed to risks and uncertainties identified below, under “Factors Affecting Operating Results” in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and elsewhere herein, for factors that may cause actual results to be different than those expressed in these forward-looking statements. Any forward-looking statement speaks only as of the date on which it is made, and except as required by law, we undertake no obligation to revise or update publicly any forward-looking statements for any reason.

PART I

Item 1. **Business**

Overview

We are a global provider of software-enabled enterprise connectivity services for mobile workers. Our flagship service offering, iPass Corporate Access, is designed to enable enterprises to provide their employees with secure access from over 150 countries to the enterprise's internal networks through an easy-to-use interface. In addition, we provide policy management services that extend our secure offering to enable better protection of user identities, the integrity of an enterprises' remote and mobile computer systems, or endpoints, as well as an enterprises' network. These services can be used in conjunction with iPass Corporate Access or over non-iPass network connections.

As opposed to telecommunications companies that own and operate physical networks, we provide our services through a virtual network. Our virtual network is enabled by our software-based architecture and our relationships with over 300 telecommunications carriers, Internet service providers and other network service providers around the globe. Our architecture allows our customers to both gain better control over remote and mobile connectivity by configuring and enforcing policies around network access usage and security, as well as receive centralized and detailed billing, reporting and management tools.

We derive revenues from usage of our networks and from fees. Our usage revenues are generated by providing enterprise connectivity services to customers using narrowband access technologies, such as modem dial-up, and from broadband access technologies, including Ethernet and Wireless-Fidelity (Wi-Fi). Revenues pertaining to usage represented 92% of our total revenues in 2004. Additionally, we receive revenue from fees and other services, including session and endpoint reporting and policy management services. In 2004 we generated approximately 8% of our revenues from fees and other services. We market and sell our services directly, as well as indirectly through channel partners, which consist of network service providers, systems integrators and value-added resellers. We were incorporated in California in July 1996 and reincorporated in Delaware in June 2000.

Our Strategy

Our objective is to use our software-enabled virtual network to become the leading provider of secure enterprise connectivity services worldwide. The key elements of our strategy to achieve this objective include:

Expand our Customer Base. We seek to increase the number of enterprises that use our services by leveraging our direct sales professionals and channel partners who focus on generating new accounts. We also seek to expand our indirect sales capabilities by building additional relationships with channel partners, such as systems integrators, and providers of security products (i.e. VPN, personal firewalls, intrusion detection) and broadband access service equipment. We also intend to build and maintain iPass brand awareness through the promotion of our brand through marketing campaigns, our web presence, and our large installed base of branded client software, and by increasing our market credibility through integrating our back-end software and co-branding our client software with the offerings of our channel partners.

Increase Penetration within our Existing Customer Base. We seek to accelerate the adoption of our services by increasing the number of mobile workers who connect to our virtual network, increasing usage by existing customers of both dial and broadband, as well as promoting our new policy management services into our existing customer base. Our sales force assists our customers with the adoption and integration of our services with their organizations, assesses their needs and usage and provides support. In addition, we do not have exclusive arrangements with any particular vendor of connectivity, VPN or security services, so our account representatives can work with our enterprise customers to provide the technical solution that best meets their needs.

Expand our Wired and Wireless Broadband Service Offerings. We believe that the ease of use, security functionality and our ability to aggregate and integrate providers into our virtual network together with the other benefits of our services can address many of the challenges presented by the emerging broadband

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markets, such as security concerns, the lack of unified roaming standards and complexity driven by the high degree of fragmentation of the wireless broadband market. As such, we seek to expand the scope and coverage of our virtual network to venues focused on business travelers, such as airports, hotels and convention centers, and more recently, cafes and restaurants. We intend to continue increasing the number of these venues by establishing relationships with network service providers that provide access to these hotspots. We also seek to continue developing authentication, settlement and clearinghouse capabilities, client software and other services for Wi-Fi service providers to expand their broadband capabilities through our virtual network.

Continue to Enhance our Virtual Network. We intend to continue to establish new relationships with network service providers to increase the coverage and redundancy of our virtual network. We intend to enhance the functionality and features of our software and to address changing customer requirements and technologies through internal development, strategic partnerships and/or acquisitions. We also seek to expand our service offerings by supporting and integrating new access methods, devices, applications and operating systems, and by building additional relationships with systems integrators and technology providers. We also intend to explore additional managed services that enhance our competitive advantage and provide us with new growth opportunities.

Leverage and Extend our Policy Management Capabilities. We intend to continue to improve the policy management and enforcement capabilities of our services through both extension of our platform to new functions that serve to protect identities, endpoints, the network, and user data as well as integration with technology partners in the enterprise security industry.

Our Core Capabilities

Our services are designed to enable enterprises to provide their employees with secure access from over 150 countries to the enterprise's internal networks through an easy-to-use interface. We provide our services through a virtual network that is enabled by our software, our scalable network architecture, and our relationships with over 300 network service providers around the globe.

Our core capabilities include:

Global Virtual Network. Our virtual network aggregates over 35,000 access points in over 150 countries. As of December 31, 2004, over 19,000 of these access points were dial-up connections and approximately 17,000 were broadband connections, including approximately 15,000 Wi-Fi hotspots and approximately 2,000 wired hotspots. As a result, enterprises that use our services can provide their mobile workers with access from these countries, in most instances with a local telephone or broadband connection.

Redundant and Scalable Virtual Network. Our relationships with over 300 network service providers enable us to provide connectivity through multiple networks in approximately 120 out of the over 150 countries on our virtual network. As a result, our virtual network reduces the risk of service interruptions associated with depending on only one service provider. Furthermore, our geographically distributed transaction centers, which operate as collection points for user transactional information, are organized to provide efficient, reliable processing through our built-in redundancy and fail-over capabilities.

This architecture also makes our virtual network scalable, allowing us to handle many connections and users without a proportionate increase in capital expenditure.

Secure Connectivity. Our software is designed to enable integration between an enterprise's network connectivity infrastructure and a wide variety of enterprise security applications. Our services integrate a wide variety of security software and systems, including VPNs, personal firewall, anti-virus policy enforcement and authentication systems, enabling enterprises to rapidly deploy our services while leveraging their existing and future investments in security infrastructure.

Unlike many network service providers, we securely route all credentials relating to our end users with 128-bit Secure Socket Layer, or SSL, ensuring the confidentiality of sensitive user information as it traverses the Internet.

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Robust Policy Management Software. Our virtual network also offers policy management capabilities, which enable customers to allow or deny access to their network based on specific user and session characteristics. The characteristics may be based on the user's location, the user's identity and role within the organization, the type of network being used, and the compliance of the user's computer with enterprise security policies.

Centralized Billing and Reporting. We integrate multiple network service providers to create one global virtual network, eliminating the need for enterprises to negotiate agreements with multiple network service providers to provide network connectivity to their mobile workers. Our virtual network creates call-detail records for each network session, including user, date, time, duration of usage, and other parameters. We are also able to provide detailed transaction-level billing in a single invoice for all services provided to enterprises and network service providers and can tailor the invoice to provide the level of detail and the format that our customers desire. We also offer the ability for information technology managers to gain a comprehensive and near real-time view of their employees' network connectivity usage patterns, enabling faster identification and resolution of user-related issues.

Our technology enables us to monitor and manage our virtual network by producing near real-time updates of connection success rates, client configurations, authentication times and other information critical to diagnosing network health and troubleshooting user connection problems.

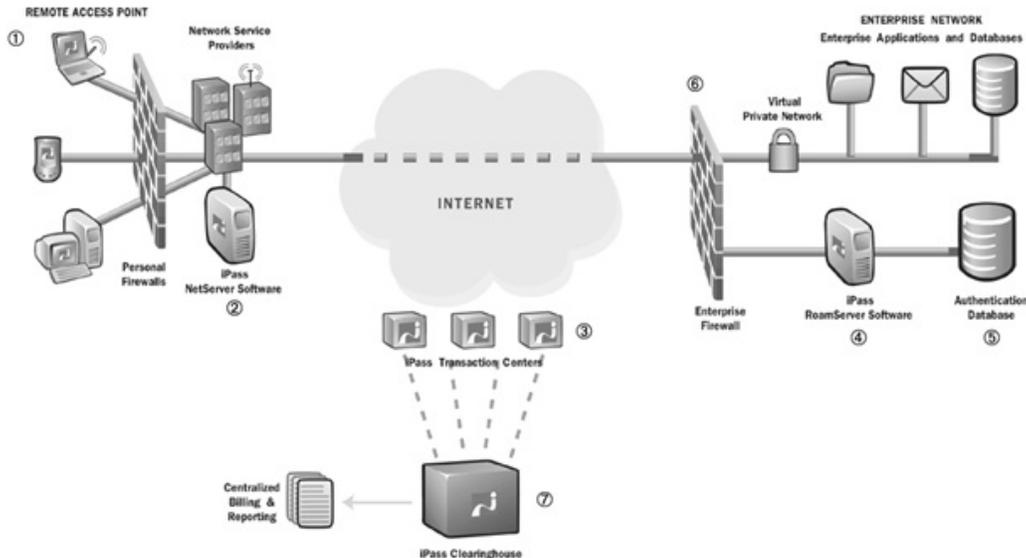
Integration of New Technologies. We actively evaluate and integrate new access methods, devices, applications and operating systems into our service offering. For example, we support wired broadband, wireless broadband based on the current and emerging Wi-Fi standards, as well as 3G mobile data services. End users can access our virtual network using desktop and laptop computers, wireless PDAs and other Internet protocol-enabled electronic devices. Our network integrates with our enterprise customers' existing VPN and security applications, and our software supports a wide range of computer operating systems, including various Windows, Mac OS, Pocket PC and Palm OS versions. As new access methods, devices, applications and operating systems emerge, we intend to integrate these new technologies into our service offerings.

Services

iPass Corporate Access

iPass Corporate Access is our primary service, offering our customers the ability to provide global dial-up, wired broadband, and wireless access to their mobile workers through our universal client, iPassConnect™ and for the IT department to have a single point of management and billing. We generally bill customers on a usage basis, based on negotiated rates. The process by which a mobile worker accesses the enterprise's

network through iPass Corporate Access is illustrated in the following diagram and described through the following steps:



1. The iPassConnect universal client software installed on a mobile worker's laptop computer or other electronic device enables the mobile worker to connect to our virtual network. The mobile worker indicates the city in which he or she is located, and then selects a local network access point (dial-up, ISDN, wired high-speed internet, Wi-Fi wireless broadband, GSM, or 3G) or has the client software select one automatically. The client software automatically detects and displays any available Wi-Fi hotspots or mobile data services. It can also be used to connect via the user's home broadband connection. A feature called SecureConnect allows the enterprise to set policies that detect whether the user's personal firewall or anti-virus software is active, auto-launch this software if it is not, and disallow the connection attempt if the proper software cannot be launched.

2. The iPass NetServer software, installed in a network service provider's network, provides the interface between the network service provider and the iPass network. The NetServer recognizes that the end user belongs to the iPass network and securely transmits the username and password to the nearest iPass transaction center using 128-bit SSL.

3. The transaction center to which the authentication request is routed looks up the enterprise to which the user belongs and securely transmits the user name and password to the iPass RoamServer software residing on the enterprise's servers. Our ten transaction centers are located in California, New York, Georgia, Hong Kong, Australia, the United Kingdom, Germany, The Netherlands, Japan and Brazil.

4. The RoamServer receives the request from the transaction center, converts it to the local authentication protocol used at the enterprise, and passes it to the enterprise authentication database. Enterprises can manage their own user lists and authentication databases and control users' access to their internal network through the authentication system of their choice.

5. The enterprise authentication database then grants or denies authorization. The RoamServer securely sends a yes/no response back to the network service provider via a transaction center.

6. Once we authorize the network service provider to allow access to the Internet, the iPassConnect universal client software can invoke the Endpoint Policy Management services to assess and remediate the mobile device before the end user can continue with accessing the Internet or attaching to the

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corporate LAN. Once remediation is complete, iPassConnect can automatically launch the user's VPN to securely connect to the enterprise network.

7. When the mobile worker terminates the Internet session, the VPN connection is also terminated and a record of the transaction is forwarded to the iPass clearinghouse. The enterprise receives one or more detailed monthly invoices, as requested. Using the Auto-Tear-down feature, the enterprise can also set policies to disconnect the internet usage session if the VPN, personal firewall, or anti-virus software is terminated during the session.

Additional Services

In addition to iPass Corporate Access, we currently offer the following services:

iIQ. We have developed our iIQ service to allow our customers' in-house or outsourced help desk personnel to quickly identify issues and troubleshoot connection problems. With our iIQ service, enterprises can generate records and reports regarding access locations, client configuration, error codes, connection speeds, time to authenticate and other critical information. We generally charge a monthly fee for our iIQ service. We periodically update the iIQ software in order to provide improved reporting for our internal support organization and our customers. These upgrades are downloaded to the user's computer or other electronic device when the user logs in, at no additional cost to the customer.

ExpressConnect. Our ExpressConnect service is designed to enable enterprises to realize the benefits of our enterprise connectivity services while avoiding the cost of installing and managing additional authentication infrastructure. We manage an enterprise's authentication server at an off-site secure data center, but the enterprise's information technology manager retains full control. We generally charge a monthly fee for our ExpressConnect service.

Wireless LAN Roaming. Our Wireless LAN Roaming service is an add-on option to the iPass Corporate Access service, which allows enterprise IT departments to offer a single user experience for all remote and local wireless connections while extending centralized management of security policies to potentially vulnerable corporate owned wireless networks. We generally charge a monthly fee for our Wireless LAN Roaming service.

Device ID. The DeviceID service strengthens network security through device authentication. The service creates a digital fingerprint for every device by gathering unique identifying numbers from select hardware components and uses this information when interrogating the device to provide access to the corporate LAN via a VPN. DeviceID helps protect against replay attacks, reverse engineering and spoofing by checking different hardware attributes during each authentication request. This service is designed to ensure that only corporate-issued or authorized machines access the network as well as validate device identity as an additional factor for VPN authentication.

Endpoint Policy Management — Online. This iPass-hosted service links automated security assessment, remediation and patch management capabilities into the iPass Corporate Access service. When users attempt to use the iPassConnect universal client to connect to the internet and the corporate VPN, the Endpoint Policy Management — Online service will check to see that the user's computer is running the proper versions of Microsoft Windows OS patches and anti-virus definition file updates for endpoint devices — before allowing Internet access and launching the VPN. This helps mitigate the effects of viruses and worms.

Mobile Lifecycle Management Suite. This service helps enterprise customers to discover, secure, and manage their laptops, desktops and handheld devices from any location via a single management console. This service is driven by iPass server software and resides on the enterprise network. It is sold either on a per-seat fee-based model or through a perpetual license model with annually occurring maintenance fees.

Mobile Lifecycle Management Suite includes the following features:

- allows IT to discover all mobile assets by gathering detailed hardware and software inventory on all mobile devices.

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- provides high-performance, policy-driven distribution of new software and updates to remote and mobile devices, automatically distributing software applications and system updates to all PCs and handheld devices via LAN, WAN and wireless networks.
- patch automation features that speed the process of deploying Microsoft Windows OS and application patches across large populations of remote and mobile devices. IT staffs receive patches directly from Microsoft and apply them with no intermediate handling during the process. This minimizes the risk of inadvertent or intentional tampering with a patch, avoiding potential problems.
- a Web-based view of user configurations and inventory information for rapid call resolution, all integrated with a customer's existing Windows NT Domain, NDS or Active Directory security system.

Technology

Principal Components

The technology incorporated in our service is designed to provide our customers with reliability, quality of service, network security, policy enforcement, consolidated billing and scalability. Our technology consists of the following four principal components, each of which was designed and developed internally: iPassConnect universal client; distributed authentication system; iPass Clearinghouse; and service quality management.

iPassConnect Universal Client. The iPassConnect universal client software is installed on mobile workers' laptop computers or other devices, and allows them to securely and reliably connect to the Internet using a variety of access methods including narrowband, integrated services digital network, or ISDN, wired and wireless broadband, GSM and 3G. The iPassConnect universal client is designed to be easy-to-use and to be a flexible and scalable network connectivity platform for enterprises. The key features of iPassConnect include:

- *Intuitive User Interface.* iPassConnect universal client was designed with over five years of experience and customer feedback, resulting in a user-friendly interface with many features.
- *Automatic Updates.* iPassConnect universal client also provides enterprises with the ability to schedule periodic software modifications or updates to their end users without handling each end user device separately. These upgrades are securely downloaded to the user's computer or other electronic device when the user logs in, at no additional cost to the customer.
- *Central Policy Control.* iPassConnect universal client enables an enterprise to define a set of criteria, such as length of session or idle timeouts, once and apply those criteria to manage its remote access policies across its entire workforce.
- *Dynamic Phonebook.* iPassConnect universal client enables enterprises to adjust the order of narrowband access points that are displayed to the end user, based on service quality. Customers also have the flexibility of integrating in-house access numbers with iPass' access points in cases where both networks are being utilized.
- *Third Party Application Integration.* iPassConnect universal client can be configured to automatically launch a variety of third party VPNs upon successful connection to the Internet.
- *Support for multiple operating systems and languages.* iPassConnect universal client supports a wide range of computer operating systems, including Windows 95, 98, NT, 2000, Me, XP, CE, Mac OS 8.x, 9.x, 10.x, Pocket PC2000, Pocket PC2002 and Palm OS. Additionally, iPassConnect is localized in Brazilian Portuguese, Simplified Chinese, Traditional Chinese, French, German, Japanese, Korean, Portuguese and Spanish.

Distributed Authentication System. Our distributed authentication system, which is comprised of iPass NetServer software, iPass RoamServer software and iPass transaction server software, is designed to enable the reliable, scalable and secure initiation and termination of a remote access session on our virtual network. NetServer is installed on the servers of our network service providers. RoamServer is installed on our

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enterprise customer's internal networks, typically located on their premises. Our ten transaction centers, each of which is comprised of two or more transaction servers, are located in third party co-location facilities.

The software components of NetServer, RoamServer and the transaction server operate on third party single-or multi-processor servers based on Unix, Linux, or Windows. We send our enterprise customers updates to NetServer, RoamServer and the transaction server electronically on an as needed basis to support new authentication and management needs.

iPass NetServer software receives end user authentication requests for Internet connectivity and securely forwards the request to a transaction server across a 128-bit SSL connection. The iPass transaction server validates the request and securely forwards this request to a RoamServer located at the enterprise. The RoamServer receives the authentication request for Internet connectivity and forwards the request in a format compatible with the enterprise's authentication database. Once the enterprise authentication database has allowed or denied the end user's request for access, this reply is returned along the same route.

We have recently developed and are presently deploying an additional security enhancement to our authentication system designed to further ensure the confidentiality of sensitive user credentials.

iPass Clearinghouse. Our iPass Clearinghouse software, collects, filters, resolves, analyzes and summarizes the accounting details necessary to bill for the iPass Corporate Access and ExpressConnect services. Once an end user session is terminated, the Clearinghouse retrieves accounting records for each customer from each transaction server. Once received by the Clearinghouse, the records are filtered to eliminate duplicate records and reviewed for completeness and integrity of the data. The Clearinghouse then determines the identities of both the customer and the network service provider and generates two billing records to reflect the revenues and network access expenses based on the details contained in the original accounting record. The Clearinghouse then summarizes the records of each network service provider and generates and distributes customer call detail records and invoices. The Clearinghouse software is run internally on servers residing at a secure data center in Redwood City, California, with a fail-over and disaster recovery in a separate location.

Service Quality Management. Our iPass service quality management, or SQM, software consists of several quality of service monitoring and management elements that we incorporated into our services. These tools and processes are comprised of the following:

- *Client-Side SQM.* Client-side SQM captures detailed status and usage information from connection attempts and uploads this information to a central iPass database when a successful connection is made. SQM records and reports access points from which connections are made, client configuration, error codes, connection speeds, time to authenticate and other information important in diagnosing network health. Our SQM software is deployed on networks worldwide to gather data on local access points and network conditions and allows us to monitor our virtual network from a customer's point of view.
- *SQM Reporting.* Our SQM infrastructure enables our iOQ service and provides information such as detailed access point performance, individual and corporate connection success rates, and other connection data to our customers and to us. With this data, our customer support and development teams can monitor service quality and continue to improve the reliability and performance of our service offering. Through our iOQ service, our customers benefit from this SQM technology because it enables them to diagnose problems their users are experiencing.
- *Phonebook.* Based on input from the SQM infrastructure, the phonebook tool within the iPassConnect universal client places the highest quality access point at the top of the directory in order to enhance the experience for our customers' end users.

Co-location Facilities

Our ten transaction centers are located in third-party co-location facilities in California, New York, Georgia, Hong Kong, Australia, the United Kingdom, The Netherlands, Germany, Japan and Brazil. Three

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additional co-location facilities are utilized to host our primary Clearinghouse and Finance systems, and corporate web services, which are located in California. Three out of our ten transaction centers also run the standby and disaster recovery Clearinghouse environments, our ExpressConnect service and the phonebook distribution servers. We maintain standard contractual agreements with the third parties that host our co-location facilities which generally provide for a term of between one and three years. If our relationships with these providers terminate, we believe that we will be able to secure relationships with alternative providers without any significant disruption to our operations.

Customers

We sell our service offering directly to enterprise customers and indirectly through our channel partners.

International revenue accounted for approximately 41% of total revenues for the year ended December 31, 2004 and 39% for the years ended December 31, 2003 and 2002. Revenues generated in the United Kingdom accounted for 11% of total revenues for the year ended December 31, 2004. No individual foreign country represented 10% or more of total revenues for the years ended December 31, 2003 and 2002. International revenue is determined by the location of the customer's headquarters.

Substantially all of our long-lived assets are located in the United States.

Agreements with Network Service Providers

We have relationships with over 300 telecommunications carriers, Internet service providers and other network service providers that enable us to offer our services in over 150 countries around the world. We pay network service providers for access to their network access points on a usage basis, in some cases, subject to minimum purchase commitments. Most of these contracts have a term of one year, after which either party can terminate the contract with six months notice. In 2004, two network service providers, MCI and Equant, accounted for approximately 17% and 7% of our network access expenses, respectively. The contracts we have entered into with these providers are non-exclusive and contain minimum commitments for the purchase of network access. The initial term of our contract with Equant expires in February 2006. The term of our contract with MCI expires in November 2005. The contract is automatically renewed for successive periods of one or 12 month periods unless terminated by either party. In countries in which we have contracted with multiple network service providers, if one network service provider is no longer available, we can obtain alternative network access without significant disruption to our business. We are also able to direct users to the network of particular service providers to fulfill minimum purchase commitments.

Sales and Marketing

We sell our services directly through our sales force and indirectly through our channel partners. Our sales organization is organized into regional account teams, which include sales directors, sales managers, account executives, account managers, inside sales representatives and sales engineers. We maintain sales offices or personnel in a number of cities in the United States as well as Australia, the United Kingdom, Hong Kong, Japan, Korea, Germany, France, Singapore, Denmark, Sweden and the Netherlands. As of December 31, 2004, our sales organization was comprised of 99 individuals in North America, 28 individuals in Asia Pacific, and 34 individuals in Europe. We intend to increase the size of our sales organization and establish additional sales offices as needed.

Our channel partners include network service providers, systems integrators and value added resellers. A channel partner typically signs a one to two year agreement with us through which we appoint the partner as a nonexclusive reseller of our services. Channel partners are responsible for implementing and managing billing and promotional activities for their customers. Selling through channel partners allows us to offer our services without incurring the cost of maintaining a direct sales force in each target market. Our channel partners typically sell related networking products and bundle our services with their core offerings. Once an enterprise has signed a contract for our services through a channel partner, our post-sales team works with the channel partner to ensure successful implementation of our services. However, the enterprise remains the channel partner's customer and has no direct relationship with us.

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We focus our marketing efforts on creating awareness for our services and their applications, educating potential customers and generating new sales opportunities. We conduct a variety of marketing programs to educate our target market and enhance brand awareness, including advertising, press relations, telemarketing, direct marketing, seminars and trade shows.

Competition

We compete primarily with large, facilities-based carriers and non-facilities-based software-enabled network operators. We compete based on geographic coverage, reliability, quality of service, ease of implementation, ease of use and cost. We believe that we compete favorably in terms of geographical coverage, reliability, quality of service, ease of implementation and ease of use.

Facilities-based carriers against whom we compete, such as AT&T and MCI, generally have substantially greater resources, larger customer bases, longer operating histories, and greater name recognition than we have. Carriers may have the ability to offer a broad range of services and may be willing to reduce the price for remote access that is bundled with their other services. In some cases, potential customers are also suppliers to these carriers, and may be more inclined to purchase enterprise connectivity services from these carriers rather than from us. We believe that we compete favorably against facilities-based carriers when the potential customer is not a supplier to the carrier, and when the customer requires global access rather than access only within a limited geographic region.

We also compete with other non-facilities-based software-enabled network operators, such as GoRemote Internet Communications and Fiberlink. In some cases, our service offerings may not be as attractively priced as those offered by our competitors, which may put us at a competitive disadvantage. Non-facilities-based network operators that provide managed services such as VPNs and firewalls, may also provide, as a package, additional services such as local exchange and long distance services, voicemail and DSL services. Although our channel partners may offer these services in conjunction with our service, we do not offer these additional services directly, which may put us at a competitive disadvantage when competing for potential customers. Also, we believe we compete favorably against these competitors in terms of the coverage, redundancy, security, quality and ease of use of our service offerings.

For a discussion of the possible effects that competition could have on our business, see "Factors Affecting Operating Results — We face strong competition in our market, which could make it difficult for us to succeed."

Research and Development

We believe that to compete favorably we must continue to invest in research and development of our services. Our research and development efforts are focused on improving and enhancing our existing service offerings as well as developing new proprietary products and services. As of December 31, 2004, our research and development organization consisted of 78 employees. Our research and development expenses were \$13.8 million, \$9.9 million and \$7.1 million in 2004, 2003, and 2002, respectively.

Intellectual Property

We rely on a combination of trademark, copyright, trade secret laws and disclosure restrictions to protect our intellectual property rights. We also enter into confidentiality and proprietary rights agreements with our employees, consultants and other third parties and control access to software, documentation and other proprietary information. iPass®, iQQ® and the iPass logo are our U.S. registered trademarks. iPassConnect™, ExpressConnect™, iPassNet™, RoamServer™, NetServer™, and iPass Corporate Access™ are designations that we use. We have 18 U.S. patent applications pending relating to our service. On January 21, 2003, we were issued a U.S. patent for a method and a technology relating to our SQM technology. We also obtained two U.S. patents in 2004 through the acquisition of Safe3w and Mobile Automation. The duration of a patent is 20 years from the date of issuance. We have also applied for or registered company trademarks in over 50 other countries. If a claim is asserted that we have infringed the intellectual property of a third party, we may be required to seek licenses to that technology. In addition, we license third-party technologies that are

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incorporated into our services, including our license for encryption granted by RSA Security. The license agreement with RSA Security expires in February 2006 and automatically renews for additional three-year periods unless terminated by us or by RSA Security. Licenses from third party technologies, including our license with RSA Security, may not continue to be available to us at a reasonable cost, or at all. Additionally, the steps we have taken to protect our intellectual property rights may not be adequate. Third parties may infringe or misappropriate our proprietary rights. Competitors may also independently develop technologies that are substantially equivalent or superior to the technologies we employ in our services. If we fail to protect our proprietary rights adequately, our competitors could offer similar services, potentially significantly harming our competitive position and decreasing our revenues.

Employees

As of December 31, 2004, we had 402 employees, consisting of 80 in network operations, 78 in research and development, 192 in sales and marketing and 52 in general and administrative. We consider our relationship with our employees to be good.

Trademarks

iPass®, iOQ® and the iPass logo are our U.S. registered trademarks. iPassConnect™, ExpressConnect™, iPassNet™, RoamServer™, NetServer™, iPass Corporate Access™, DeviceID™, EPM™, iSEEL™ and iPass Alliance™ are designations that we use. We have also applied for or registered company trademarks in over 50 other countries.

Available Information

Our Internet address is www.ipass.com. We make available free of charge through our Internet website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities and Exchange Act, as amended, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

Further, a copy of this annual report is located at the SEC's Public Reference Room at 450 Fifth Street, NW, Washington, D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding our filings at www.sec.gov.

Item 2. Properties

We lease approximately 74,000 square feet of space in our headquarters in Redwood Shores, California under a lease that expires in 2010. We also lease sales and support offices in other parts of the United States and abroad. We believe that our principal facility in Redwood Shores will be adequate for our needs for at least the next several years, and we might expect that additional facilities will be available in other jurisdictions to the extent we add new offices.

Item 3. Legal Proceedings

On January 14, 2005, a lawsuit entitled *Palumbo v. iPass, Inc., et al.*, Case No. C 05 228 MHP was filed in the United States District Court for the Northern District of California, purportedly on behalf of a class of investors who purchased the Company's stock between April 22, 2004 and June 30, 2004. The complaint alleges claims under Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934 against the Company and certain of its officers and directors. Several similar lawsuits were subsequently filed in the same court. The Company expects that all of the cases will be consolidated into a single action. This matter is at an early stage; no lead plaintiff has been selected, no response to the complaint has been filed, no discovery has taken place and no trial date has been set. The Company and the individual defendants intend to take all appropriate actions to defend the suit.

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We may be subject to various other claims and legal actions arising in the ordinary course of business from time to time.

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

No matters were submitted to a vote of our stockholders during the fiscal quarter ended December 31, 2004.

PART II

Item 5. Market For Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Price Range of Common Stock

Our common stock is traded on the Nasdaq National Market under the symbol "IPAS" since our initial public offering on July 24, 2003.

The following table sets forth the high and low sale price of our common stock, based on the last daily sale, in each of the quarters since our initial public offering:

	<u>Low Sale Price</u>	<u>High Sale Price</u>
Fiscal year ended December 31, 2004:		
First Quarter	\$ 10.70	\$ 16.25
Second Quarter	9.86	13.37
Third Quarter	4.78	6.91
Fourth Quarter	5.75	7.77
Fiscal year ended December 31, 2003:		
Third Quarter	\$ 17.60	\$ 28.22
Fourth Quarter	15.25	26.90

We had 62,907,510 shares of our common stock outstanding held by 216 stockholders of record as of February 28, 2005.

Dividend Policy

We have never paid any cash dividends on our common stock. Our board of directors currently intends to retain future earnings to support operations and to finance the growth and development of our business and does not intend to pay cash dividends on our common stock in the foreseeable future. Any future determination related to dividend policy will be made at the discretion of the board.

Recent Sales of Unregistered Securities

We have not made any sales of unregistered securities following the date of our initial public offering.

Item 6. Selected Financial Data

The following selected consolidated financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" following this section and our consolidated financial statements and related notes included elsewhere in this report. The historical results are not necessarily indicative of results to be expected in any future period.

	Year Ended December 31,				
	2004	2003	2002	2001	2000
	(In thousands, except per share data)				
Statement of Operations Data					
Revenues	\$ 166,319	\$ 136,078	\$ 92,830	\$ 53,164	\$ 35,281
Total operating expenses	137,353	113,721	86,178	80,898	69,316
Operating income (loss)	28,966	22,357	6,652	(27,734)	(34,035)
Net income (loss)	19,068	13,902	29,759(1)	(27,801)	(34,964)
Net income (loss) per share:					
Basic	0.31	0.26	2.34	(2.43)	(3.60)
Diluted	0.29	0.23	0.57	(2.43)	(3.60)

(1) Of this amount, \$24.3 million was due to a tax benefit, resulting from the reversal of deferred tax valuation allowances.

	As of December 31,				
	2004	2003	2002	2001	2000
	(In thousands, except per share data)				
Balance Sheet Data					
Total assets	\$ 230,513	\$ 190,117	\$ 75,442	\$ 37,421	\$ 52,232
Line of credit and loans payable	—	—	10,375	8,932	2,726
Total stockholders' equity	207,222	171,722	49,600	16,262	38,294

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**Company Overview**

We deliver simple, secure and manageable enterprise mobility services, maximizing the productivity of workers as they move between office, home and remote locations. Our policy management services close the gaps in protecting computers, network assets, user identities and data whenever users connect over the Internet. Our connectivity services utilize the iPass global virtual network, a unified network of hundreds of dial-up, wireless, and broadband providers in over 150 countries.

Overview of 2004

In 2004, we increased revenues and end users over 2003, although not at the rate we had anticipated as growth from our traditional dial-up business slowed substantially to rates below those we had historically experienced. We continued to expand both our dial-up and broadband global footprints in 2004, which enabled our users to remotely access their corporate networks from more locations, with increased redundancy than in any previous year.

Another goal in 2004 was to improve upon our existing service offerings as well as add new products and services in order to drive revenue growth and to expand our existing customer base. We accelerated our timetable for the development and improvement of new and existing products and services through increased spending on research and development. We also added to our product offering through the acquisitions of Safe3w and Mobile Automation in September and October, respectively. For additional information on the acquisitions, please see Note 7 in the Notes to the Consolidated Financial Statements.

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Going forward, we will continue to focus on delivering innovative services and solutions for our customers, increasing the number of end users of our services for both dial-up and broadband access, as well as focus on generating revenues from our endpoint policy management products and services. In 2005, we expect to see continued growth in our business. However, our success could be limited by several factors, including the timely release of new products, continued market acceptance of our products and the introduction of new products by existing or new competitors. For a further discussion of these and other risk factors, see the section below entitled "Factors Affecting Operating Results."

Sources of Revenues

We derive our revenues primarily from providing enterprise connectivity services through our virtual network. We sell these services directly, as well as indirectly through our channel partners. We bill substantially all customers on a time basis for usage based on negotiated rates. We bill the remaining customers based on a fixed charge per active user per month with additional charges for excess time. Substantially all enterprise customers commit to a one to three year contract term. Most of our contracts with enterprise customers contain minimum usage levels. Our usage-based revenues represented 92% and 93% of our revenues for the years ended December 31, 2004 and 2003, respectively.

Although we have incurred expenses to expand our broadband coverage and are seeking to generate additional revenues from our broadband wired and wireless coverage, we have generated less than 2% of our usage revenues from broadband coverage in 2004 and 2003. We cannot determine when, if ever, we will generate any substantial revenues from broadband.

With the acquisition of Mobile Automation in October of 2004, we also began generating license and maintenance revenue through software licensing agreements.

We bill customers for minimum commitments when actual usage is less than their monthly minimum commitment amount. We recognize the difference between the minimum commitment and actual usage as fee revenue once the cash for such fee has been collected. We also provide customers with deployment services and technical support throughout the term of the contract. We typically charge fees for these services on a one-time or annual basis, depending on the service provided and the nature of the relationship. In addition, we also offer customers additional services for which we generally bill on a monthly basis. Fees for these services, together with revenues generated from license and maintenance fees, represented approximately 8% and 7% of our revenues for the years ended December 31, 2004 and 2003, respectively.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to revenue recognition, income taxes, and allowance for doubtful accounts. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable, the results of which form the basis of making judgments about the carrying values of assets and liabilities.

We believe the following critical accounting policies and estimates are important in understanding our consolidated financial statements.

Revenue Recognition

Services and Fees

The Company derives substantially all of its revenues from usage fees. The Company recognizes revenues when persuasive evidence of an arrangement exists, service has been provided to the customer, the price to the customer is fixed or determinable, and collectibility is probable.

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Revenues are recognized during the period the services are rendered to end users based on usage at negotiated rates. The Company typically requires its customers to commit to minimum usage levels. Minimum usage levels can be based on an annual term, monthly term or over the term of the arrangement. If actual usage in a given period is less than the minimum commitment, the Company recognizes the difference between the actual usage and the minimum commitment as revenue when cash is collected because the Company cannot reasonably estimate the amount of the difference that will be collected. The Company cannot reasonably estimate the amount of the difference to be collected because it has from time to time renegotiated minimum commitments in cases where customers have sought renegotiation of their contract for reasons such as a significant downturn in their business or where the Company has determined that it would be in its best interest to do so. Customers are not contractually entitled to use or otherwise receive benefit for unused service in subsequent periods.

The Company typically provides its customers with deployment services, technical support and additional optional services. Depending on the service provided and the nature of the arrangement, the Company may charge a one-time, annual or monthly fee. Revenues relating to one-time fees are recognized on a straight-line basis over the term of the initial contract, generally one to three years. Revenues relating to annual fees are recognized on a straight-line basis. Revenues for monthly services are recognized during the month that these services are provided.

License and Maintenance

License revenue consists principally of revenue earned under software license agreements. License revenue is generally recognized when a signed contract or other persuasive evidence of an arrangement exists, the software has been shipped or electronically delivered, the license fee is fixed or determinable, and collection of the resulting receivable is reasonably probable. We enter into revenue arrangements in which a customer may purchase a combination of software, upgrades and maintenance and support (multiple-element arrangements). When vendor-specific objective evidence ("VSOE") of fair value exists for all elements, we allocate revenue to each element based on the relative fair value of each of the elements. VSOE of fair value is established by the price charged when that element is sold separately. When contracts contain multiple elements wherein vendor specific objective evidence exists for all undelivered elements, we account for the delivered elements in accordance with the "residual method" prescribed by AICPA Statement of Position ("SOP") 98-9. Revenue from subscription license agreements, which include software, rights to future products and maintenance, is recognized ratably over the term of the subscription period. Revenue on shipments to resellers, which is generally subject to certain rights of return and price protection, is recognized when the products are sold by the resellers to the end-user customer.

Maintenance revenue consists of fees for providing software updates on a when and if available basis and technical support for software products (post-contract support or "PCS"). Maintenance revenue is recognized ratably over the term of the agreement.

Payments received in advance of services performed are deferred. Allowances for estimated future returns and discounts are provided for upon recognition of revenue.

The Company generally performs credit reviews to evaluate the customers' ability to pay. If the Company determines that collectibility is not probable, revenue is recognized as cash is collected.

Accounting for Income Taxes

In preparing our consolidated financial statements, we assess the likelihood that our deferred tax assets will be realized from future taxable income. We establish a valuation allowance if we determine that it is more likely than not that some portion of the net deferred tax assets will not be realized. Changes in the valuation allowance are included in our consolidated statements of income as a provision for (benefit from) income taxes. We exercise significant judgment in determining our provisions for income taxes, our deferred tax assets and liabilities and our future taxable income for purposes of assessing our ability to utilize any future tax benefit from our deferred tax assets.

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During the year ended December 31, 2002, we determined that it was more likely than not that we would realize all of our available net deferred tax assets in the carryforward period of up to 19 years. As a result, we determined that it was no longer necessary or appropriate to maintain a valuation allowance related to our deferred tax assets. Accordingly, we recorded a \$24.3 million tax benefit in our consolidated statement of operations for the year ended December 31, 2002.

Although we believe it is more likely than not that we will realize our net deferred tax assets, there is no guarantee this will be the case as our ability to use the net operating losses is contingent upon our ability to generate sufficient taxable income in the carryforward period. At each period end, we reassess our ability to realize our net operating losses. If we conclude it is more likely than not that we would not realize the benefit of our net operating losses, we may have to re-establish the valuation allowance and therefore record a significant charge to our results of operations.

Allowance for Doubtful Accounts

Our allowance for doubtful accounts is based on a detailed assessment of accounts receivable for specific, as well as anticipated, uncollectible accounts receivable. Our estimate for the allowance for doubtful accounts is based on credit profiles of our customers, current economic trends, contractual terms and conditions, and historical payment experience. We have an allowance for doubtful accounts of \$2.1 million, \$2.3 million and \$1.5 million as of December 31, 2004, 2003 and 2002, respectively, for estimated losses resulting from the inability of our customers to make their required payments. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, or if we underestimated the allowances required, additional allowances may be required, which would result in an increased general and administrative expense in the period such determination was made.

RESULTS OF OPERATIONS

Revenue

	December 31,						2002
	2004	Change		2003	Change		
		\$	%		\$	%	
Total Revenue	\$ 166,319	\$ 30,241	22.2%	\$ 136,078	\$ 43,248	46.6%	\$ 92,830

The growth in total revenue in 2004 over 2003 was due to an increase in the usage of our services resulting from an increased number of end users of our services at new and existing customers. Distinct end users of our service increased to 518,000 in the month of December of 2004, compared to 447,000 for the same period in 2003. No individual customer accounted for 10% or more of total revenues for the years ended December 31, 2004, 2003 or 2002. Fees represented approximately 8%, 7% and 5% of our revenue in 2004, 2003, and 2002, respectively.

The growth in total revenue in 2003 over 2002 was due to an increase in the usage of our services resulting from an increased number of end users of our services at new and existing customers. Distinct end users of our service increased to 447,000 in the month of December of 2003 from 286,000 for the same period in 2002.

International revenues, which are revenues generated from customers domiciled outside the United States, accounted for approximately 41% of total revenues in 2004 and 39% of total revenues in 2003 and 2002. Substantially all of our international revenues are generated in the EMEA (Europe, Middle East and Africa) and Asia Pacific regions. Revenues in the EMEA region represented 24%, 21% and 17% of total revenues in 2004, 2003 and 2002, respectively. The increase in EMEA as a percent of revenues has been driven by the expansion of our sales force in the region. Revenues in the Asia Pacific region represented 13%, 14% and 15% of total revenues in 2004, 2003 and 2002, respectively. Revenues in the United Kingdom accounted for 11% of total revenues in 2004. No individual foreign country accounted for 10% or more of total revenues in 2003 or

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2002 to 2003 was due primarily to our ability to scale our network operations infrastructure without a proportionate increase in network operations expenses.

Research and Development

Research and development expenses consist of compensation and benefits for our research and development personnel, consulting, and certain allocated overhead costs.

	December 31,						
	2004	Change		2003	Change		2002
		\$	%		\$	%	
Research and development expenses	\$ 13,804	\$ 3,860	38.8%	\$ 9,944	\$ 2,874	40.7%	\$ 7,070
As a percent of revenue	8.3%	—	1.0%	7.3%	—	(0.3)%	7.6%

The increase in research and development expenses in 2004 over 2003 was due primarily to an additional \$2.3 million of compensation and benefits expenses related to an increase in headcount, and approximately \$1.2 million in fees paid to consultants to further develop our service. The increase as a percentage of revenues was due to the acceleration of our development of new products as well as the increase in research and development personnel as a result of the two acquisitions that occurred in 2004. We expect that our research and development expenses will continue to increase in absolute dollars as we develop and enhance new and existing service offerings as well as integrate newly acquired products and technologies into our existing products. We also expect research and development expenses to increase slightly as a percentage of revenues as we continue to increase headcount and bring new and upgraded products and services to market.

The increase in research and development expenses in 2003 over 2002 was due primarily to an additional \$1.8 million of compensation and benefits expenses related to an increase in headcount, and approximately \$540,000 in fees paid to consultants to further develop our service. The decrease as a percentage of revenues was due to revenues increasing at a faster pace than research and development expenses.

Sales and Marketing

Sales and marketing expenses consist of compensation, benefits, advertising, promotion expenses, and certain allocated overhead costs.

	December 31,						
	2004	Change		2003	Change		2002
		\$	%		\$	%	
Sales and marketing expenses	\$ 46,580	\$ 5,531	13.5%	\$ 41,049	\$ 8,118	24.7%	\$ 32,931
As a percent of revenue	28.0%	—	(2.2)%	30.2%	—	(5.3)%	35.5%

The increase in sales and marketing expenses in 2004 over 2003 in absolute dollars was due primarily to an additional \$2.3 million in compensation and benefits expenses resulting from the expansion of the sales organization in the EMEA and Asia Pacific regions, as well as the additional sales personnel from the acquisition of Mobile Automation in the last quarter of 2004. The increase also included \$1.2 million of additional advertising and public relations expenses, as well as a \$410,000 increase in compensation and benefits expenses for additional marketing personnel. The remaining portion of the increase was due to individually insignificant items. We expect that sales and marketing expenses will increase in absolute dollars to the extent revenues increase and/or we expand our sales force and increase marketing activities, but will remain relatively constant as a percentage of revenues.

The increase in sales and marketing expenses in 2003 over 2002 in absolute dollars was due primarily to an additional \$3.7 million in compensation and benefits expenses resulting from the expansion of the sales organization and increased commissions expense as a result of sales growth in 2003 over 2002. The increase also included \$1.3 million of additional advertising and public relations expenses, as well as a \$930,000

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increase in compensation and benefits expenses for additional marketing personnel. The remaining portion of the increase was due to individually insignificant items.

General and Administrative

General and administrative expenses consist of compensation and benefits of general and administrative personnel, legal and accounting expenses, bad debt expense, and certain allocated overhead costs.

	December 31,						2002
	2004	Change		2003	Change		
		\$	%		\$	%	
			(In thousands, except percentages)				
General and administrative expenses	\$ 17,790	\$ 3,558	25.0%	\$ 14,232	\$ 4,602	47.8%	\$ 9,630
As a percent of revenue	10.7%	—	0.2%	10.5%	—	0.1%	10.4%

A significant part of the increase in general and administrative expenses in 2004 over 2003 was \$1.7 million in compensation and benefits expenses for additional personnel and \$1.0 million for directors and officers insurance premiums. There was also a \$1.0 million increase in legal and accounting fees. These increases were offset in part by decreases in various individually insignificant accounts. We expect that our general and administrative expenses will increase in absolute dollars to the extent that we expand our operations, but to remain relatively constant as a percentage of revenues.

A significant part of the increase in general and administrative expenses in 2003 over 2002 was \$1.2 million in compensation and benefits expenses for additional personnel. There was also an increase of \$1.0 million for directors and officers insurance, as well as \$930,000 for consulting, and an \$800,000 increase in rent expense. General and administrative expenses increased in absolute dollars in 2003 over 2002 due to incurring additional costs associated with becoming a public company.

Amortization of Stock-Based Compensation

We record stock-based compensation charges in the amount by which the option exercise price or the restricted stock purchase price is less than the deemed fair value of our common stock at the date of grant. We amortize this compensation expense on an accelerated basis over the vesting period of the applicable agreements, generally four years. Amortization of stock-based compensation expense relates to stock options granted to employees prior to our initial public offering in July of 2003.

	December 31,						2002
	2004	Change		2003	Change		
		\$	%		\$	%	
			(In thousands, except percentages)				
Amortization of stock-based compensation expense	\$ 2,342	\$ (1,727)	(42.4)%	\$ 4,069	\$ 1,304	47.2%	\$ 2,765
As a percent of revenue	1.4%	—	(1.6)%	3.0%	—	—	3.0%

We expect to incur amortization of stock-based compensation expense of at least \$1.2 million in 2005 and \$518,000 in 2006. The amount of amortization of stock-based compensation expense to be recognized in future periods could decrease if stock options for which accrued but unvested compensation expense has been recorded are forfeited.

Non-Operating Expenses

Other Income (Expense), Net

Other income (expense) consists of the net total of interest income and interest expense for the period.

Interest income includes interest income on cash, cash equivalents, and short-term investment balances. Interest income and other was \$2.3 million, \$1.1 million and \$440,000 for the years ended December 31, 2004,

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2003 and 2002, respectively. The increase in interest income was due to an increase in the average cash, cash equivalents, and short-term investment balances for the period, resulting primarily from proceeds received from the initial public offering in July 2003.

Interest expense consists of interest paid on our line of credit and loans, as well as amortization of a loan discount associated with the fair value of warrants issued in connection with our financing activities. Interest expense was \$620,000 and \$1.0 million in 2003 and 2002, respectively. There was no interest expense for the year ended December 31, 2004. The decrease in interest expense from 2002 to 2003 was the result of paying off our line of credit and all outstanding loans payable in July and August 2003.

Provision for (benefit from) Income Taxes

The provision for income taxes was \$12.2 million in 2004 compared to a provision of \$9.0 million in 2003. The increase is due to an increase in taxable income in 2004 over 2003.

We incurred net operating losses in 2001 and consequently paid insignificant amounts of federal, state and foreign income taxes. As of December 31, 2001, we had recorded a valuation allowance of \$27.2 million, which was equal to the amount of our deferred tax assets. These assets relate to net operating loss carryforwards and other tax credit carryforwards and temporary differences between items recorded for financial reporting and tax return purposes. We established this valuation allowance because we determined that it was more likely than not that some portion or all of the deferred tax assets would not be realized. We reversed the valuation allowance totaling \$27.2 million during fiscal year 2002, of which \$2.9 million was due to taxable earnings generated during 2002, and \$24.3 million because we determined that it is more likely than not that we will generate enough taxable income to use our net operating losses.

Liquidity and Capital Resources

From our inception in July 1996 through our initial public offering of our common stock in July 2003, we funded our operations primarily through issuances of preferred stock, which provided us with aggregate net proceeds of approximately \$86.5 million. In July 2003, we completed the sale of 8,050,000 shares of common stock in an initial public offering, including the underwriters' exercise of an over-allotment option, and realized net proceeds of \$102.7 million. We used \$10.9 million of the net proceeds to pay off all outstanding balances on loans payable and line of credit.

Net cash provided by operating activities was \$37.5 million for the year ended December 31, 2004, compared to \$23.7 million for the year ended December 31, 2003 and \$10.6 million for the year ended December 31, 2002. This increase is primarily due to the expansion of our business, as reflected in the increase in net income before taxes from 2002 to 2004.

Net cash used in investing activities in 2004 was \$59.6 million compared to \$99.2 million and \$3.5 million in 2003 and 2002, respectively. Net cash used in investing activities in 2004 was from the purchases of \$156.0 million in short-term investments, offset by the maturities of short-term investments in the amount of \$131.1 million. Net cash used in investing activities also included \$28.5 million for the acquisition of Safe3w and Mobile Automation as well as \$6.2 million for the purchases of property and equipment. Net cash used in investing activities in 2003 was from the purchases of property and equipment, with the exception of a net investment of \$93.5 million in short-term investments as a result of the receipt of the proceeds from our initial public offering.

Net cash provided by financing activities in 2004 was \$10.9 million, compared to \$93.2 million and \$2.1 million in 2003 and 2002, respectively. Cash provided by financing activities in 2004 was the result of proceeds from the issuance of common stock for employee stock options plus the repayment of shareholder notes receivable. In comparison, cash provided by financing activities in 2003 was primarily due to net proceeds from our initial public offering, offset in part by the payment of all outstanding balances on our line of credit and loans payable. Net cash provided by financing activities in 2002 were primarily due to net proceeds from loans payable as well as proceeds from payments on stockholder notes receivable.

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We anticipate that our operating expenses, as well as planned capital expenditures, will constitute a material use of our cash resources for the foreseeable future in order to execute our business plan. In addition, we may utilize cash resources to fund acquisitions of complementary businesses, technologies or product lines. We believe that our cash and cash equivalents and short-term investments on hand will be sufficient to meet our cash requirements for at least the next 18 months, including working capital requirements and planned capital expenditures.

As of December 31, 2004, our principal source of liquidity was \$152.3 million of cash, cash equivalents and short-term investments.

Commitments

At December 31, 2004, we had no material commitments for capital expenditures.

We have signed contracts with some network service providers under which we have minimum purchase commitments that expire on various dates through February 2006. Other than in the approximately 29 countries in which our sole network provider is Equant, we have contracted with multiple network service providers to provide alternative access points in a given geographic area. In those geographic areas where we have access through multiple providers, we are able to direct users to the network of particular service providers. Consequently, we believe we have the ability to fulfill our minimum purchase commitments in these geographic areas. Future minimum purchase commitments under all agreements as of December 31, 2004 are as follows (in thousands):

Year ending December 31:	
2005	\$ 3,042
2006	208
	<u>\$ 3,250</u>

We lease our facilities under non-cancelable operating leases that expire at various dates through February 2010. Future minimum lease payments under these operating leases as of December 31, 2004 are as follows (in thousands):

Year ending December 31:	
2005	\$ 3,799
2006	3,927
2007	4,055
2008	4,183
2009	4,311
2010	1,453
	<u>\$ 21,728</u>

Tabular Disclosure of Contractual Obligations

Contractual Obligations	Payments Due By Period				
	Total	Less than 1 Yr	1-3 Years	3-5 Years	More than 5 Yrs
Operating Lease Obligations	\$ 21,728	\$ 3,799	\$ 7,982	\$ 8,494	\$ 1,453
Purchase Obligations	3,250	3,042	208	—	—
Total Contractual Obligations	<u>\$ 24,978</u>	<u>\$ 6,841</u>	<u>\$ 8,190</u>	<u>\$ 8,494</u>	<u>\$ 1,453</u>

FACTORS AFFECTING OPERATING RESULTS

Set forth below and elsewhere in this report are risks and uncertainties that could cause actual results to differ materially from the results contemplated by the forward-looking statements contained in this report.

Risks Relating to Our Business

If we are unable to meet the challenges posed by broadband access, our ability to grow our business will be impaired.

We have generated substantially all of our usage revenues to date from the sale of enterprise connectivity services using narrowband technologies such as modem dial-up. In some countries, including the United States, the use of narrowband as a primary means of enterprise connectivity has declined and is expected to continue to decline over time as broadband access technologies, such as cable modem, DSL, and Wi-Fi, become more broadly used. Although we have not generated substantial revenues from broadband access, a substantial portion of the growth of our business may depend upon our ability to expand the broadband elements of our virtual network. Such an expansion may not result in additional revenues to us. Key challenges in expanding the broadband elements of our virtual network include:

The broadband access market is at an early stage of development. Although we derive revenues from wired and wireless broadband “hotspots”, such as particular airports, hotels and convention centers, the broadband access market, particularly for wireless access, is at an early stage of development and demand at levels we anticipate may not develop. In particular, the market for enterprise connectivity services through broadband is characterized by evolving industry standards and specifications and there is currently no uniform standard for wireless access. We have developed and made available Wi-Fi specifications that are directed at enabling Wi-Fi access points to become ready for use by enterprise customers. If this specification is not widely adopted, market acceptance of our wireless broadband services may be significantly reduced or delayed and our business could be harmed. Furthermore, although the use of wireless frequencies generally does not require a license in the United States and abroad, if Wi-Fi frequencies become subject to licensing requirements, or are otherwise restricted, this would substantially impair the growth of wireless access. Some large telecommunications providers and other stakeholders that pay large sums of money to license other portions of the wireless spectrum may seek to have the Wi-Fi spectrum become subject to licensing restrictions. If the broadband wireless access market does not develop, we will not be able to generate revenues from broadband wireless access.

The broadband service provider market is highly fragmented. Due to the early stage of development of the broadband access market, there are currently many wired and wireless broadband service providers that provide coverage in only one or a small number of hotspots. We have entered into contractual relationships with numerous broadband service providers. These contracts generally have an initial term of two years or less. As this process is in the early stages, we must continue to develop relationships with many providers on terms commercially acceptable to us in order to provide adequate coverage for our customers’ mobile workers and to expand our broadband coverage. We may also be required to develop additional technologies in order to integrate new broadband services into our service offering. If we are unable to develop these relationships or technologies, our ability to grow our business could be impaired. In addition, if broadband service providers consolidate, our negotiating leverage with providers may decrease, resulting in increased rates for access, which could harm our operating results.

We do not generate revenues from broadband home access. We do not generate revenues when mobile workers access their enterprise networks from the home using subscription-based broadband access because they do not connect through our virtual network. If subscription-based broadband access from the home increases and fewer home workers use narrowband access, our revenues may decline.

If demand for broadband access does not materially increase, or if demand increases but we do not meet the challenges outlined above, our ability to grow our business may suffer.

Our customers require a high degree of reliability in our services, and if we cannot meet their expectations, demand for our services will decline.

Any failure to provide reliable network access, uninterrupted operation of our network and software infrastructure, or a satisfactory experience for our customers and their mobile workers, whether or not caused by our own failure, could reduce demand for our services. In 2002, we experienced three outages affecting our clearinghouse system, which handles invoicing to our customers and network service providers, resulting in five days of outages and eight days of work to confirm data integrity in response to the outages. Although these problems did not affect the ability of mobile workers to access our services or impact our revenues, one of these outages caused a delay in our invoicing of approximately one week. If additional outages occur, or if we experience other hardware or software problems, our business could be harmed.

We face strong competition in our market, which could make it difficult for us to succeed.

We compete primarily with facilities-based carriers as well as with other non-facilities-based network operators. Some of our competitors have substantially greater resources, larger customer bases, longer operating histories or greater name recognition than we have. Also, with the recent introduction of our policy management services, we face additional competition from companies that provide security and policy-based services and software. In addition, we face the following challenges from our competitors:

Many of our competitors can compete on price. Because many of our facilities-based competitors own and operate physical networks, there may be little incremental cost for them to provide additional telephone or Internet connections. As a result, they may offer dial-up remote access services at little additional cost, and may be willing to discount or subsidize remote access services to capture other sources of revenue. In contrast, we have traditionally purchased network access from facilities-based network service providers to enable our dial-up remote access service. As a result, large carriers may sell their remote access services at a lower price. In addition, new non-facilities-based carriers may enter our market and compete on price. In either case, we may lose business or be forced to lower our prices to compete, which could reduce our revenues.

Many of our competitors offer additional services that we do not, which enables them to compete favorably against us. Some of our competitors provide services that we do not, such as local exchange and long distance services, voicemail and digital subscriber line, or DSL, services. Potential customers that desire these services on a bundled basis may choose to obtain remote access and policy management services from the competitor that provides these additional services.

Our potential customers may have other business relationships with our competitors and consider those relationships when deciding between our services and those of our competitors. Many of our competitors are large facilities-based carriers that purchase substantial amounts of products and services, or provide other services or goods unrelated to remote access services. As a result, if a potential customer is also a supplier to one of our large competitors, or purchases unrelated services or goods from our competitor, the potential customer may be motivated to purchase its remote access services from our competitor in order to maintain or enhance its business relationship with that competitor.

If our security measures are breached and unauthorized access is obtained to a customer's internal network, our virtual network may be perceived as not being secure and enterprises may curtail or stop using our services.

It is imperative for our customers that access to their mission critical data is secure. A key component of our ability to attract and retain customers is the security measures that we have engineered into our network for the authentication of the end user's credentials; on a going forward basis, we expect an additional key component in this regard to be our policy management services. These measures are designed to protect against unauthorized access to our customers' networks. Because techniques used to obtain unauthorized access or to sabotage networks change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures against unauthorized access or sabotage. If an actual or perceived breach of network security occurs, regardless of whether the breach is attributable to our services, the market perception of the effectiveness of

our security measures could be harmed. To date, we have not experienced any significant security breaches to our network.

If enterprise connectivity demand does not continue to expand, we may experience a shortfall in revenues or earnings or otherwise fail to meet public market expectations.

The growth of our business is dependent, in part, upon the increased use of enterprise connectivity services and our ability to capture a higher proportion of this market. If the demand for enterprise connectivity services does not continue to grow, then we may not be able to grow our business, maintain profitability or meet public market expectations. Increased usage of enterprise connectivity services depends on numerous factors, including:

- the willingness of enterprises to make additional information technology expenditures;
- the availability of security products necessary to ensure data privacy over the public networks;
- the quality, cost and functionality of these services and competing services;
- the increased adoption of wired and wireless broadband access methods; and
- the proliferation of electronic devices and related applications.

If we are unable to meet the challenges related to the market acceptance and provision of our policy management services, our ability to grow the business may be harmed.

We expect that the growth of our business may depend in part upon whether our policy management services will achieve and sustain expected levels of demand and market acceptance. If enterprises do not perceive the benefits of our policy management services, then the market for these services may not develop at all, or it may develop more slowly than we expect, either of which could significantly and adversely affect our growth. In addition, if demand for our policy management services does not materialize as expected, our ability to recover our investment in Safe3w, Inc. and Mobile Automation, Inc. may be impaired or delayed. In addition, because of our limited operating history relating to policy management services, we cannot predict our revenue and operating results from the provision of these services. Key challenges that we face related to our provision of these services include the risk that we may encounter unexpected technical and other difficulties in developing our policy management services which could delay or prevent the development of these services or certain features of these services; the risk that the rate of adoption by enterprises of network security software or integrated secure connectivity solutions will not be as we anticipate, which if slow would reduce or eliminate the purchase of these services; and the risk that security breaches may occur, notwithstanding the use of our policy management services, by hackers that develop new methods of avoiding security software. If we do not adequately address these challenges, our growth and operating results may be negatively impacted.

Our long sales and service deployment cycles require us to incur substantial sales costs that may not result in related revenues.

Our business is characterized by a long sales cycle between the time a potential customer is contacted and a customer contract is signed. In addition, the downturn in the economy and the resulting reduction in corporate spending on Internet infrastructure have further lengthened the average sales cycle for our services. Furthermore, once a customer contract is signed, there is typically an extended period before the customer's end users actually begin to use our services, which is when we begin to realize revenues. As a result, we may invest a significant amount of time and effort in attempting to secure a customer which may not result in any revenues. Even if we enter into a contract, we will have incurred substantial sales-related expenses well before we recognize any related revenues. If the expenses associated with sales increase, we are not successful in our sales efforts, or we are unable to generate associated offsetting revenues in a timely manner, our operating results will be harmed.

There are approximately 29 countries in which we provide dial-up access only through Equant. The loss of Equant as a dial-up network service provider would substantially diminish our ability to deliver global network access.

In approximately 29 countries, our sole dial-up network service provider is Equant. Network usage from access within these countries accounted for less than 2% of our revenues for the years ended December 31, 2004 and 2003. If we lose access to Equant's network and are unable to replace this access in some or all of these countries, our revenues would decline. In addition, our ability to market our services as being global would be impaired, which could cause us to lose customers. Although our agreement with Equant does not expire until February 2006, Equant may terminate the agreement earlier if we materially breach the contract and fail to cure the breach, or if we become insolvent. In addition, Equant has no obligation to continue to provide us with access to its network after February 2006. If Equant were to cease operations or terminate its arrangements with us, we would be required to enter into arrangements with other dial-up network service providers, which may not be available. This process could be costly and time consuming, and we may not be able to enter into these arrangements on terms acceptable to us.

If our channel partners do not successfully market our services to their customers or corporate end users, then our revenues and business may be adversely affected.

We sell our services directly through our sales force and indirectly through our channel partners, which include network service providers, systems integrators and value added resellers. Our business depends on the efforts and success of these channel partners in marketing our services to their customers. Our own ability to promote our services directly to their customers is often limited. Many of our channel partners may offer services to their customers that may be similar to, or competitive with, our services. Therefore, these channel partners may be reluctant to promote our services. If our channel partners fail to market our services effectively, our ability to grow our revenue would be reduced and our business will be impaired.

If we fail to address evolving standards and technological changes in the enterprise connectivity and policy management services industry, our business could be harmed.

The market for enterprise connectivity and policy management services is characterized by evolving industry standards and specifications and rapid technological change, including new access methods, devices, applications and operating systems. In developing and introducing our services, we have made, and will continue to make, assumptions with respect to which features, security standards, performance criteria, access methods, devices, applications and operating systems will be required or desired by enterprises and their mobile workers. If we implement technological changes or specifications that are different from those required or desired, or if we are unable to successfully integrate required or desired technological changes or specifications into our wired or wireless services, market acceptance of our services may be significantly reduced or delayed and our business could be harmed.

The telecommunications industry has experienced a dramatic decline, which may cause consolidation among network service providers and impair our ability to provide reliable, redundant service coverage and negotiate favorable network access terms.

The telecommunications industry has experienced dramatic technological change and increased competition that have led to significant declines in network access pricing. In addition, the revenues of network service providers have declined as a result of the general economic slowdown. As a result, network service providers have experienced operating difficulties in the last several years, resulting in poor operating results and a number of these providers declaring bankruptcy. As these conditions have continued, some of these service providers have consolidated and are working to consolidate or otherwise cease operations, which would reduce the number of network service providers from which we are able to obtain network access. As this occurs, while we expect that we will still be able to maintain operations and provide enterprise connectivity services with a small number of network service providers, we would potentially not be able to provide sufficient redundant access points in some geographic areas, which could diminish our ability to provide broad, reliable,

redundant coverage. Further, our ability to negotiate favorable access rates from network service providers could be impaired, which could increase our network access expenses and harm our operating results.

Our software is complex and may contain errors that could damage our reputation and decrease usage of our services.

Our software may contain errors that interrupt network access or have other unintended consequences. If network access is disrupted due to a software error, or if any other unintended negative results occur, such as the loss of billing information, a security breach or unauthorized access to our virtual network, our reputation could be harmed and our business may suffer. Although we generally attempt by contract to limit our exposure to incidental and consequential damages, if these contract provisions are not enforced or enforceable for any reason, or if liabilities arise that are not effectively limited, our operating results could be harmed.

Because much of our business is international, we encounter additional risks, which may reduce our profitability.

We generate a substantial portion of our revenues from business conducted internationally. Revenues from customers domiciled outside of the United States were 41% of our revenues for 2004, of which approximately 24% and 13% were generated in our EMEA (Europe, Middle East and Africa) and Asia Pacific regions, respectively. In 2003, revenues from customers domiciled outside of the United States were 39% of our total revenues, of which approximately 21% and 14% were generated in our EMEA and Asia Pacific regions, respectively. Although we currently bill for our services in U.S. dollars, our international operations subject our business to specific risks. These risks include:

- longer payment cycles for foreign customers, including delays due to currency controls and fluctuations;
- the impact of changes in foreign currency exchange rates on the attractiveness of our pricing;
- high taxes in some foreign jurisdictions;
- difficulty in complying with Internet-related regulations in foreign jurisdictions;
- difficulty in staffing and managing foreign operations; and
- difficulty in enforcing intellectual property rights and weaker laws protecting these rights.

Any of these factors could negatively impact our business.

Completed or future acquisitions or investments could dilute the ownership of our existing stockholders, cause us to incur significant expenses or harm our operating results.

Integrating any newly acquired businesses, technologies or services may be expensive and time-consuming. For example, we completed the acquisitions of Safe3w, Inc. in September 2004 and Mobile Automation, Inc. in October 2004. To finance any acquisitions, it may be necessary for us to raise additional funds through public or private financings. Additional funds may not be available on terms that are favorable to us and, in the case of equity financings, would result in dilution to our stockholders. In the case of completed or future acquisitions, we may be unable to operate any acquired businesses profitably or otherwise implement our strategy successfully. If we are unable to integrate any newly acquired entities, such as Safe3w, Inc. and Mobile Automation, Inc., or technologies effectively, our operating results could suffer. Completed acquisitions by us, such as the aforementioned Safe3w, Inc. and Mobile Automation, Inc. transactions, or future acquisitions by us could also result in large and immediate write-offs or assumption of debt and contingent liabilities, either of which could harm our operating results.

If we are unable to effectively manage future expansion, our business may be adversely impacted.

We have experienced, and in the future may experience, rapid growth in operations which has placed and could continue to place, a significant strain on our network operations, development of services, internal

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controls and other managerial, operating, and financial resources. If we do not manage future expansion effectively, our business will be harmed. To effectively manage any future expansion, we will need to improve our operational and financial systems and managerial controls and procedures, which include the following:

- managing our research and development efforts for new and evolving technologies;
- expanding the capacity and performance of our network and software infrastructure;
- developing our administrative, accounting and management information systems and controls; and
- effectively maintaining coordination among our various departments, particularly as we expand internationally.

We currently are, and in the future may be, subject to securities class action lawsuits due to decreases in our stock price.

We are at risk of being subject to securities class action lawsuits if our stock price declines substantially. Securities class action litigation has often been brought against a company following a decline in the market price of its securities. For example, in June 2004, we announced that we would not meet market expectations regarding our financial performance in the second quarter, and our stock price declined. On January 14, 2005, a lawsuit entitled *Palumbo v. iPass, Inc., et al.*, Case No. C 05 228 MHP was filed in the United States District Court for the Northern District of California, purportedly on behalf of a class of investors who purchased the Company's stock between April 22, 2004 and June 30, 2004. The complaint alleges claims under Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934 against the Company and certain of its officers and directors. Several similar lawsuits were subsequently filed in the same court. We cannot predict the outcome of the lawsuits. If our stock price declines substantially in the future, we may be the target of similar litigation. The current, and any future, securities litigation could result in substantial costs and divert management's attention and resources, and could seriously harm our business.

Litigation arising from disputes involving third parties could disrupt the conduct of our business.

Because we rely on third parties to help us develop, market and support our service offerings, from time to time we have been, and we may continue to be, involved in disputes with these third parties. If we are unable to resolve these disputes favorably, our development, marketing or support of our services could be delayed or limited, which could materially and adversely affect our business.

If licenses to third party technologies, including our license with RSA Security, do not continue to be available to us at a reasonable cost, or at all, our business and operations may be adversely affected.

We license technologies from several software providers that are incorporated in our services. We anticipate that we will continue to license technology from third parties in the future. In particular, we license encryption technology from RSA Security. The license agreement with RSA Security expires in February 2006 and automatically renews for additional three-year periods unless terminated by us or by RSA Security. Licenses from third party technologies, including our license with RSA Security, may not continue to be available to us at a reasonable cost, or at all. The loss of these technologies or other technologies that we license could have an adverse effect on our services and increase our costs or cause interruptions or delays in our services until substitute technologies, if available, are developed or identified, licensed and successfully integrated into our services.

Litigation arising out of intellectual property infringement could be expensive and disrupt our business.

We cannot be certain that our products do not, or will not, infringe upon patents, trademarks, copyrights or other intellectual property rights held by third parties, or that other parties will not assert infringement claims against us. From time to time we have been, and we may continue to be, involved in disputes with these third parties. Any claim of infringement of proprietary rights of others, even if ultimately decided in our favor, could result in substantial costs and diversion of our resources. Successful claims against us may result in an injunction or substantial monetary liability, in either case which could significantly impact our results of

operations or materially disrupt the conduct of our business. If we are enjoined from using a technology, we will need to obtain a license to use the technology, but licenses to third-party technology may not be available to us at a reasonable cost, or at all.

New and Potential New Accounting Pronouncements May Impact Our Future Financial Position and Results of Operations.

There may be potential new accounting pronouncements or regulatory rulings, which may have an impact on our future financial position and results of operations. In particular, in December 2004, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standards 123R (SFAS 123R), "Share-Based Payment — An Amendment of FASB Statements No. 123 and 95, which eliminated the ability to account for share-based compensation transactions using Accounting Principles Board Opinion No. 25 (APB 25), "Accounting for Stock Issued to Employees." SFAS 123R will instead require companies to recognize compensation expense, using a fair-value based method, for costs related to share-based payments including stock options and employee stock purchase plans. SFAS 123R is effective for public companies in periods beginning after June 15, 2005. We will be required to implement the standard no later than the quarter that begins July 1, 2005. The cumulative effect of adoption, if any, applied on a modified prospective basis, would be measured and recognized on July 1, 2005. The adoption of FAS 123R and other potential changes could materially impact our results of operations.

Risks Relating to Our Industry

Security concerns may delay the widespread adoption of the Internet for enterprise communications, or limit usage of Internet-based services, which would reduce demand for our products and services.

The secure transmission of confidential information over public networks is a significant barrier to further adoption of the Internet as a business medium. The Internet is a public network and information is sent over this network from many sources. Advances in computer capabilities, new discoveries in the field of code breaking or other developments could result in compromised security on our network or the networks of others. Security and authentication concerns with respect to the transmission over the Internet of confidential information, such as corporate access passwords and the ability of hackers to penetrate online security systems may reduce the demand for our services. Further, new access methods, devices, applications and operating systems have also introduced additional vulnerabilities which have been actively exploited by hackers. Internet-based worms and viruses, computer programs that are created to slow Internet traffic or disrupt computer networks or files by replicating through software or operating systems, are examples of events or computer programs that can disrupt users from using our Internet-based services and reduce demand for our services, potentially affecting our business and financial performance. In particular, certain Internet worms and viruses affected some of our customers and their mobile users, which may have negatively impacted our revenues. Furthermore, any well-publicized compromises of confidential information may reduce demand for Internet-based communications, including our services.

Financial, political or economic conditions could adversely affect our revenues.

Our revenues and profitability depend on the overall demand for enterprise connectivity services. The general weakening of the global economy in the last few years led to decreased corporate spending on Internet infrastructure. In addition, if there are further acts of terrorism, if hostilities involving the United States and other countries continue or escalate, or if other future financial, political, economic and other uncertainties or natural disasters arise, this could lead to a reduction in travel, including by business travelers who are substantial users of our services, and continue to contribute to a climate of economic and political uncertainty that could adversely affect our revenue growth and financial results.

Government regulation of, and legal uncertainties regarding, the Internet could harm our business.

Internet-based communication services generally are not subject to federal fees or taxes imposed to support programs such as universal telephone service. Changes in the rules or regulations of the U.S. Federal

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Communications Commission or in applicable federal communications laws relating to the imposition of these fees or taxes could result in significant new operating expenses for us, and could negatively impact our business. Any new law or regulation, U.S. or foreign, pertaining to Internet-based communications services, or changes to the application or interpretation of existing laws, could decrease the demand for our services, increase our cost of doing business or otherwise harm our business. There are an increasing number of laws and regulations pertaining to the Internet. These laws or regulations may relate to taxation and the quality of products and services. Furthermore, the applicability to the Internet of existing laws governing intellectual property ownership and infringement, taxation, encryption, obscenity, libel, employment, personal privacy, export or import matters and other issues is uncertain and developing and we are not certain how the possible application of these laws may affect us. Some of these laws may not contemplate or address the unique issues of the Internet and related technologies. Changes in laws intended to address these issues could create uncertainty in the Internet market, which could reduce demand for our services, increase our operating expenses or increase our litigation costs.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Foreign Currency

Although we currently bill our services in U.S. dollars, our financial results could be affected by factors such as changes in foreign currency rates or weak economic conditions in foreign markets. A strengthening of the dollar could make our services less competitive in foreign markets and therefore could reduce our revenues. We are billed by and pay substantially all of our network service providers in U.S. dollars. In the future, some portion of our revenues and costs may be denominated in foreign currencies. To date, exchange rate fluctuations have had little impact on our operating results.

Interest Rate Sensitivity

As of December 31, 2004, we had cash, cash equivalents, and short-term investments totaling \$152.3 million. Our investment portfolio consists of money market funds and securities, asset backed securities, corporate securities, and government securities, generally due within one to two years. All of our instruments are held other than for trading purposes. We place investments with high quality issuers and limit the amount of credit exposure to any one issuer. These securities are subject to interest rate risks. Based on our portfolio content and our ability to hold investments to maturity, we believe that, a hypothetical 10% increase or decrease in current interest rates would not materially affect our interest income, although there can be no assurance of this.

As of December 31, 2003, we had cash and cash equivalents of \$139.3 million, which consisted of cash and highly liquid short-term investments with original maturities of three months or less at the date of purchase, which we held solely for non-trading purposes. A hypothetical increase or decrease in market interest rates by 10% from the market interest rates would have caused the interest generated by, and the fair value of, these short-term investments to change by an immaterial amount.

The following is a chart of the principal amounts of short-term investments by expected maturity (in thousands):

	Expected Maturity Date for Par Value Amounts For the Year Ended December 31,		Total Cost Value	As of
	2005	2006		Dec. 31, 2004
				Total Fair Value
U.S. Government agencies	\$ 59,600	\$ 43,500	\$ 103,357	\$ 102,989
Corporate notes	—	14,415	15,007	14,951
Total	\$ 59,600	\$ 57,915	\$ 118,364	\$ 117,940

Our general policy is to limit the risk of principal loss and ensure the safety of invested funds by limiting market and credit risk. We consider all investments to be short-term investments, which are classified in the

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balance sheet as current assets, because (1) the investments can be readily converted at any time into cash or into securities with a shorter remaining time to maturity and (2) the investments are selected for yield management purposes only and we are not committed to holding the investments until maturity. We determine the appropriate classification of our investments at the time of purchase and re-evaluate such designations as of each balance sheet date. All short-term investments and cash equivalents in our portfolio are classified as "available-for-sale" and are stated at fair market value, with the unrealized gains and losses reported as a component of accumulated other comprehensive income (loss). The amortized cost of debt securities is adjusted for amortization of premiums and accretion of unrealized discounts to maturity. Such amortization and accretion is included in interest income and other, net. The cost of securities sold is based on the specific identification method.

Item 8. Financial Statements and Supplementary Data**Financial Statements**

Our financial statements required by this item are set forth as a separate section of this report. See Item 15(a)(1) for a listing of financial statements provided in the section titled "Financial Statements."

Supplementary Data

The following tables set forth unaudited quarterly supplementary data for each of the years in the two-year period ended December 31, 2004 (in thousands, except per share amounts):

	Quarter Ended			
	March 31	June 30	September 30	December 31
Year Ended December 31, 2004				
Revenues	\$ 40,695	\$ 40,394	\$ 41,912	\$ 43,318
Operating income	7,140	7,194	7,950	6,682
Net income	4,697	4,489	5,206	4,676
Basic net income per share	\$ 0.08	\$ 0.07	\$ 0.08	\$ 0.08
Diluted net income per share	\$ 0.07	\$ 0.07	\$ 0.08	\$ 0.07

	Quarter Ended			
	March 31	June 30	September 30	December 31
Year Ended December 31, 2003				
Revenues	\$ 30,498	\$ 33,103	\$ 34,989	\$ 37,488
Operating income	4,390	5,638	6,163	6,166
Net income	2,310	2,952	4,461	4,179
Basic net income per share	\$ 0.17	\$ 0.21	\$ 0.08	\$ 0.07
Diluted net income per share	\$ 0.04	\$ 0.05	\$ 0.07	\$ 0.06

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures**Controls and Procedures**

We carried out an evaluation, under the supervision and with the participation of our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Securities Exchange Act Rules 13a-15(e) and 15d-15(e)), as of the end of the period covered by this report. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures are effective to provide reasonable assurance that

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the information required to be disclosed by us in our periodic SEC reports are recorded, processed, summarized and reported within the time periods specified in the in the SEC's rules and the SEC reports.

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended). Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2004. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control-Integrated Framework. Our management has concluded that, as of December 31, 2004, our internal control over financial reporting is effective based on these criteria. Our independent registered public accounting firm, KPMG LLP, have issued an audit report on our assessment of our internal control over financial reporting, which is included herein.

Changes in Internal Control Over Financial Reporting

In addition, there have been no changes in our internal controls over financial reporting during the quarter ended December 31, 2004 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within iPass have been detected.

Item 9B. Other Information

None.

PART III

Item 10. Directors and Executive Officers of the Registrant

Information relating to our executive officers and directors will be presented under the captions "Proposal 1 — Election of Directors" and "Executive Officers and Directors" in our definitive proxy statement in connection with our 2005 Annual Meeting of Stockholders to be held in June 2005 to be filed with the Securities and Exchange Commission not later than April 30, 2005 (the "Proxy Statement"). That information is incorporated into this report by reference.

Information concerning compliance with Section 16(a) of the Securities Exchange Act of 1934 will be presented under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement. That information is incorporated into this report by reference.

Code of Ethics

We have adopted a code of conduct and ethics that applies to all of our employees, including the principal executive officer, principal financial officer and principal accounting officer. This code of conduct and ethics is posted on our Website. The Internet address for our Website is <http://www.ipass.com>, and the code of conduct and ethics may be found as follows:

1. From our main Web page, first click on "Investors."
2. Next, click on "Corporate Governance."

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3. Then, click on "Code of Conduct."
4. Finally, click on "Code of Conduct and Ethics."

We intend to satisfy the disclosure requirement under Item 5.05 of Form 8-K regarding an amendment to, or waiver from, a provision of this code of conduct and ethics by posting such information on our website, at the address and location specified above.

Item 11. *Executive Compensation*

Information relating to director and executive compensation required by this Item 11 will be presented under the captions "Compensation of Directors," "Compensation of Executive Officers," and "Compensation Committee Interlocks and Insider Participation" in the Proxy Statement. That information is incorporated into this report by reference.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters*

Information relating to the security ownership of our common stock by our management and other beneficial owners will be presented under the caption "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement. That information is incorporated into this report by reference.

Information relating to securities authorized for issuance under equity compensation plans will be presented under the caption "Securities Authorized for Issuance Under Equity Compensation Plans" in the Proxy Statement. That information is incorporated into this report by reference.

Item 13. *Certain Relationships and Related Transactions*

Information relating to certain relationships of our directors and executive officers and related transactions will be presented under the caption "Certain Relationships and Related Transactions" in the Proxy Statement. That information is incorporated into this report by reference.

Item 14. *Principal Accountant Fees and Services*

The information required by this item will be included under the captions "Proposal No. 2 — Ratification of Independent Auditors—Principal Accountant Fees and Services" in the Proxy Statement. That information is incorporated into this report by reference.

PART IV

Item 15. *Exhibits and Financial Statement Schedules*

- (a) The following financial statements are filed as part of this report:

1. Financial Statements

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Consolidated Financial Statements:	
Balance Sheets as of December 31, 2004 and 2003	38
Statements of Operations for the years ended December 31, 2004, 2003 and 2002	39
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2. Financial Statement Schedules

None. All schedules are omitted because they are not required or the required information is shown in the financial statements or notes thereto.

3. Exhibits

<u>Exhibit Number</u>	<u>Description of Document</u>
2.1	Agreement and Plan of Merger dated October 26, 2004 by and among iPass Inc., Montage Acquisition Corp., Mobile Automation, Inc. and David Strohm, as Stockholders' Agent.
3.1	Amended and Restated Certificate of Incorporation.(1)
3.2	Bylaws, as amended.(1)
4.1	Reference is made to Exhibits 3.1 and 3.2.
4.2	Specimen stock certificate.(1)
10.1	2003 Equity Incentive Plan and form of related agreements, as amended.(1)
10.2	2003 Non-Employee Directors Plan.(1)
10.3	1999 Stock Option Plan and form of related agreements.(1)
10.4	1997 Stock Option Plan and form of related agreements.(1)
10.5	Interim 1999 Stock Option Plan.(1)
10.6	Restricted Stock Purchase Agreement by and between the Registrant and Anurag Lal dated November 8, 1999.(1)
10.7	2003 Employee Stock Purchase Plan and form of related agreements, as amended.(1)
10.8	Lease Agreement, dated October 26, 1999 between Registrant and Westport Joint Venture (as amended).(1)
10.9	Amended and Restated Investor Rights Agreement dated August 8, 2000 between Registrant, founders and holders of the Registrant's Preferred Stock.(1)
10.10	Form of Indemnity Agreement.(1)
10.11	Employment Agreement, dated November 13, 2001 between Registrant and Kenneth D. Denman.(1)
10.12	Form of Offer Letter to Executive Officers.(1)
10.13	OEM Service Provider License Agreement, dated February 29, 2000, between RSA Security, Inc. and the Registrant, and amendments thereto.(1)(3)
10.14	Support Agreement, dated February 29, 2000, by and between RSA Security, Inc. and the Registrant.(1)(3)
10.15	Managed Data Network Services Agreement, dated September 17, 1996, between Equant, (formerly Scitor International Telecommunication Services, Inc.), and the Registrant, and amendments thereto.(1)(3)
10.16	Loan and Security Agreement dated September 4, 2001 between Silicon Valley Bank and the Registrant and modifications thereto.(1)
10.17	Internet Service Agreement dated April 25, 2001, by and between UUNET Technologies, Inc. and the Registrant, and amendment thereto.(1)(3)
10.18	Virtual Internet Provider (VIP) Agreement dated January 9, 1997, by and between UUNET Technologies, Inc. and the Registrant and amendments thereto.(1)(3)
10.19	Management Bonus Structure 2005 Plan (4)
10.20	Outside Director Compensation Arrangement (5)
10.21	Executive Officer Cash Compensation Arrangement (6)
21.1	Subsidiaries of the Registrant.
23.1	Consent of Independent Registered Public Accounting Firm.
24.1	Power of Attorney.(reference is made to the signature page of this Form 10-K)



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Exhibit Number	Description of Document
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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- (1) Previously filed as the like-numbered exhibit to our Registration Statement on Form S-1, as amended, originally filed with the Securities and Exchange Commission on January 24, 2003, as amended, and incorporated by reference herein.
 - (2) Previously filed as the like-numbered exhibit to our Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 13, 2003, and incorporated by reference herein.
 - (3) Confidential treatment has been granted for a portion of the exhibit. The information omitted pursuant to such confidential treatment order had been filed separately with the Securities and Exchange Commission.
 - (4) Previously filed as the file-numbered exhibit on our Current Report on Form 8-K filed with the Securities and Exchange Commission on February 17, 2005, and incorporated by reference herein.
 - (5) Previously disclosed under the caption "Compensation of Directors" in our Definitive Proxy Statement on Schedule 14A filed with the Securities and Exchange Commission on April 26, 2004, and incorporated by reference herein.
 - (6) Previously disclosed under the caption "Compensation of Executive Officers" in our Definitive Proxy Statement on Schedule 14A filed with the Securities and Exchange Commission on April 26, 2004, and incorporated by reference herein.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
iPass Inc.:

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

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of iPass Inc. and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of iPass Inc.'s internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 15, 2005 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

/S/ KPMG LLP

Mountain View, CA
March 15, 2005

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
iPass Inc.:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control Over Financial Reporting, that iPass Inc. maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). iPass' management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

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

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

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that iPass maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Also, in our opinion, iPass maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of iPass Inc. and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2004, and our report dated March 15, 2005 expressed an unqualified opinion on those consolidated financial statements.

/S/ KPMG LLP

Mountain View, CA
March 15, 2005

iPASS INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	As of December 31,	
	2004	2003
	(In thousands, except share and per share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 34,395	\$ 45,646
Short-term investments	117,940	93,639
Accounts receivable, net of allowance for doubtful accounts of \$2,071 and \$2,348, respectively	23,884	20,658
Prepaid expenses and other current assets	3,161	3,310
Deferred income tax assets	8,642	17,341
Total current assets	188,022	180,594
Property and equipment, net	10,111	8,288
Other assets	1,224	1,235
Acquired intangibles, net	11,143	—
Goodwill	20,013	—
Total assets	<u>\$ 230,513</u>	<u>\$ 190,117</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 9,154	\$ 7,421
Accrued liabilities	14,137	10,974
Total current liabilities	23,291	18,395
Total liabilities	23,291	18,395
Commitments (Note 9)		
Stockholders' equity:		
Common stock, \$.001 par value; authorized 250,000,000 and 120,000,000 shares, respectively; issued and outstanding 62,756,718 and 60,483,432 shares, respectively	63	60
Additional paid-in capital	240,629	229,026
Notes receivable from stockholders	—	(2,831)
Deferred stock-based compensation	(1,782)	(4,326)
Accumulated other comprehensive income (loss)	(424)	125
Accumulated deficit	(31,264)	(50,332)
Total stockholders' equity	207,222	171,722
Total liabilities and stockholders' equity	<u>\$ 230,513</u>	<u>\$ 190,117</u>

The accompanying notes are an integral part of these consolidated financial statements.

iPASS INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	For the Year Ended December 31,		
	2004	2003	2002
	(In thousands, except share and per share amounts)		
Revenues	\$ 166,319	\$ 136,078	\$ 92,830
Operating expenses:			
Network access	37,339	30,121	23,323
Network operations	19,041	14,306	10,459
Research and development	13,804	9,944	7,070
Sales and marketing	46,580	41,049	32,931
General and administrative	17,790	14,232	9,630
Amortization of stock-based compensation(1)	2,342	4,069	2,765
Amortization of intangibles	457	—	—
Total operating expenses	<u>137,353</u>	<u>113,721</u>	<u>86,178</u>
Operating income	<u>28,966</u>	<u>22,357</u>	<u>6,652</u>
Other income (expense):			
Interest income and other	2,298	1,133	440
Interest expense	—	(620)	(1,026)
Total other income (expense)	<u>2,298</u>	<u>513</u>	<u>(586)</u>
Income before income taxes	31,264	22,870	6,066
Provision for (benefit from) income taxes	12,196	8,968	(23,693)
Net income	<u>\$ 19,068</u>	<u>\$ 13,902</u>	<u>\$ 29,759</u>
Net income per share:			
Basic	\$ 0.31	\$ 0.26	\$ 2.34
Diluted	\$ 0.29	\$ 0.23	\$ 0.57
Number of shares used in per share calculations:			
Basic	60,770,680	53,474,537	12,742,068
Diluted	65,645,757	60,622,040	51,873,067
(1) Amortization of stock-based compensation consists of:			
Network operations	\$ 335	\$ 551	\$ 302
Research and development	352	468	219
Sales and marketing	554	984	571
General and administrative	1,101	2,066	1,673
Total amortization of stock-based compensation	<u>\$ 2,342</u>	<u>\$ 4,069</u>	<u>\$ 2,765</u>

The accompanying notes are an integral part of these consolidated financial statements.

iPASS INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME

	<u>Convertible Preferred Stock</u>		<u>Common Stock</u>		<u>Additional Paid-In Capital</u>	<u>Notes Receivable from Stockholders</u>	<u>Deferred Stock-Based Compensation</u>	<u>Accumulated Deficit</u>	<u>Accumulated Comprehensive Income (Loss)</u>	<u>Total Stockholders' Equity</u>	<u>Comprehensive Income</u>
	<u>Shares</u>	<u>Amount</u>	<u>Shares</u>	<u>Amount</u>							
Balances, December 31, 2001	35,273	\$ 35	13,191	\$ 13	\$ 115,870	\$ (1,785)	\$ (3,878)	\$ (93,993)	—	\$ 16,262	—
Exercise of stock options	—	—	3,240	3	1,673	(1,485)	—	—	—	191	—
Payment of stockholder notes receivable	—	—	—	—	—	625	—	—	—	625	—
Repurchase of unvested common stock	—	—	(418)	—	(109)	87	—	—	—	(22)	—
Warrants	—	—	—	—	46	—	—	—	—	46	—
Interest earned on stockholder note receivable	—	—	—	—	—	(86)	—	—	—	(86)	—
Cancellation of unvested stock options	—	—	—	—	(572)	—	572	—	—	—	—
Deferred stock-based compensation	—	—	—	—	2,300	—	(2,300)	—	—	—	—
Amortization of stock-based compensation	—	—	—	—	—	—	2,765	—	—	2,765	—
Fair value of options for accelerated vesting	—	—	—	—	44	—	—	—	—	44	—
Fair value of options issued to non-employees	—	—	—	—	16	—	—	—	—	16	—
Net income	—	—	—	—	—	—	—	29,759	—	29,759	29,759
Balances, December 31, 2002	35,273	35	16,013	16	119,268	(2,644)	(2,841)	(64,234)	—	49,600	\$ 29,759
Issuance of common stock in initial public offering, net of issuance costs of \$10,043	—	—	8,050	8	102,649	—	—	—	—	102,657	—
Conversion of convertible preferred stock into common stock	(35,273)	(35)	35,273	35	—	—	—	—	—	—	—
Exercise of stock options	—	—	662	1	962	—	—	—	—	963	—
Exercise of warrants	—	—	485	—	—	—	—	—	—	—	—
Interest earned on stockholder note receivable	—	—	—	—	—	(187)	—	—	—	(187)	—
Cancellation of unvested stock options	—	—	—	—	(282)	—	282	—	—	—	—
Deferred stock-based compensation	—	—	—	—	5,836	—	(5,836)	—	—	—	—
Amortization of stock-based compensation	—	—	—	—	—	—	4,069	—	—	4,069	—
Fair value of options issued to non-employees	—	—	—	—	392	—	—	—	—	392	—
Tax benefit from employee stock option plans	—	—	—	—	201	—	—	—	—	201	—
Unrealized gain on available-for-sale investments, net	—	—	—	—	—	—	—	—	125	125	125

Net income	—	—	—	—	—	—	—	13,902	—	13,902	13,902
Balances, December 31, 2003	—	—	60,483	60	\$ 229,026	\$ (2,831)	\$ (4,326)	\$ (50,332)	\$ 125	\$ 171,722	\$ 14,027
Exercise of stock options	—	—	1,886	2	5,239	—	—	—	—	5,241	—
Employee stock purchase plan — common stock issued	—	—	388	1	2,735	—	—	—	—	2,736	—
Payment of stockholder notes receivable	—	—	—	—	—	2,887	—	—	—	2,887	—
Interest earned on stockholder note receivable	—	—	—	—	—	(56)	—	—	—	(56)	—
Cancellation of unvested stock options	—	—	—	—	(202)	—	202	—	—	—	—
Amortization of stock-based compensation	—	—	—	—	—	—	2,342	—	—	2,342	—
Tax benefit from employee stock option plans	—	—	—	—	3,831	—	—	—	—	3,831	—
Unrealized loss on available-for- sale investments, net	—	—	—	—	—	—	—	—	(549)	(549)	(549)
Net income	—	—	—	—	—	—	—	19,068	—	19,068	19,068
Balances, December 31, 2004	—	—	<u>62,757</u>	<u>63</u>	<u>\$ 240,629</u>	<u>—</u>	<u>\$ (1,782)</u>	<u>\$ (31,264)</u>	<u>\$ (424)</u>	<u>\$ 207,222</u>	<u>\$ 18,519</u>

The accompanying notes are an integral part of these consolidated financial statements.

iPASS INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Year Ended December 31,		
	2004	2003	2002
	(In thousands)		
Cash flows from operating activities:			
Net income	\$ 19,068	\$ 13,902	\$ 29,759
Adjustments to reconcile net income to net cash provided by operating activities:			
Amortization of stock-based compensation for employees	2,342	4,069	2,765
Amortization of warrants issued	—	8	64
Amortization of acquired intangibles	457	—	—
Depreciation and amortization	4,386	3,810	3,549
Stock-based compensation	—	392	60
Tax benefit from employee stock option plans	3,831	201	—
Deferred income taxes	6,473	6,958	(24,299)
Interest on shareholder notes receivable	(56)	(187)	(86)
Provision for doubtful accounts	1,100	1,176	1,250
Loss on disposals of property and equipment	—	45	—
Realized loss on investments, net	98	—	—
Changes in operating assets and liabilities:			
Accounts receivable	(3,433)	(7,607)	(5,961)
Prepaid expenses and other current assets	250	(1,991)	183
Other assets	30	(22)	52
Accounts payable	1,733	442	1,521
Accrued liabilities	1,185	2,486	1,719
Net cash provided by operating activities	<u>37,464</u>	<u>23,682</u>	<u>10,576</u>
Cash flows from investing activities:			
Purchases of short-term investments	(156,020)	(98,854)	—
Maturities of short-term investments	131,072	5,340	—
Purchases of property and equipment	(6,186)	(5,683)	(3,533)
Acquisition of Safe3w, net of cash acquired	(8,481)	—	—
Acquisition of Mobile Automation, net of cash acquired	(19,964)	—	—
Net cash used in investing activities	<u>(59,579)</u>	<u>(99,197)</u>	<u>(3,533)</u>
Cash flows from financing activities:			
Net proceeds from initial public offering	—	102,657	—
Proceeds from loans payable	—	1,483	2,418
Payments on loans payable	—	(5,064)	(1,128)
Payments on line of credit, net	—	(6,794)	—
Proceeds from issuance of common stock	7,977	963	191
Proceeds from payment of stockholder notes receivable	2,887	—	625
Payments for repurchase of unvested restricted stock	—	—	(22)
Net cash provided by financing activities	<u>10,864</u>	<u>93,245</u>	<u>2,084</u>
Net increase (decrease) in cash and cash equivalents	(11,251)	17,730	9,127
Cash and cash equivalents at beginning of year	<u>45,646</u>	<u>27,916</u>	<u>18,789</u>
Cash and cash equivalents at end of year	<u>\$ 34,395</u>	<u>\$ 45,646</u>	<u>\$ 27,916</u>
Supplemental disclosures of cash flow information:			
Cash paid for interest	\$ —	\$ 486	\$ 799
Cash paid for taxes	\$ 1,485	\$ 1,362	\$ 378
Non-cash investing and financing activities:			
Issuance of stockholder notes receivable for exercise of stock options	\$ —	\$ —	\$ 1,485
Cancellation of stockholder notes receivable for unvested restricted stock repurchases	\$ —	\$ —	\$ 87

The accompanying notes are an integral part of these consolidated financial statements.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Description of Business

iPass, Inc. (the "Company") provides software-enabled enterprise connectivity services for mobile workers. Its primary service offering, iPass Corporate Access, is designed to enable enterprises to provide their employees with secure access from over 150 countries to the enterprise's internal networks through an easy-to-use interface. As opposed to telecommunications companies that own and operate physical networks, iPass provides its services through a virtual network. iPass' virtual network is enabled by its software, its scalable network architecture and its relationships with over 300 telecommunications carriers, internet service providers and other network service providers around the globe. The Company's software is designed to provide enterprises with a high level of security, the ability to affect and control policy management, and to receive centralized billing and detailed reporting. iPass was incorporated in California in July 1996 and reincorporated in Delaware in June 2000.

In July 2003, the Company closed the sale of 8,050,000 shares of common stock, including the underwriters' exercise of an over-allotment option, at a price of \$14 per share in an initial public offering (IPO). A total of \$112.7 million in gross proceeds was raised from these transactions. After deducting the underwriting discount of approximately \$7.9 million, and offering expenses of approximately \$2.1 million, net proceeds were \$102.7 million.

Upon the closing of the Company's IPO, 35,273,169 shares of the Company's convertible preferred stock converted into common shares.

Note 2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Principles of Consolidation

The accompanying consolidated financial statements include the financial statements of iPass Inc. and its wholly owned subsidiaries after elimination of intercompany accounts and transactions.

Foreign Currency Translation

All revenues and substantially all network access expenses are denominated in U.S. dollars. Therefore, the Company considers all functional currency of its foreign subsidiaries to be the U.S. dollar. Foreign currency transaction gains and losses are included in the accompanying consolidated statements of income. Foreign currency transaction gains and losses were not significant for the years ended December 31, 2004, 2003 and 2002.

Comprehensive Income

Comprehensive income is a measure of all changes in equity of an enterprise that result from transactions and other economic events of the period other than transactions with stockholders. Comprehensive income is the total of net income and all other non-owner changes in equity. Comprehensive income includes net income and unrealized gains and losses on available-for-sale securities.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Comprehensive income is comprised of the following (in thousands):

	Year Ended December 31,		
	2004	2003	2002
Net income	\$ 19,068	\$ 13,902	\$ 29,759
Comprehensive income:			
Change in accumulated unrealized gain (loss) on available-for-sale securities	(549)	125	—
Total comprehensive income	<u>\$ 18,519</u>	<u>\$ 14,027</u>	<u>\$ 29,759</u>

Cash Equivalents and Short-term Investments

Cash equivalents consist of highly liquid investments including money market funds and corporate debt securities with maturities of 90 days or less from the date of purchase.

The Company has the ability to convert its short-term investments into cash or into securities with a shorter remaining time to maturity without penalty and is not committed to holding the investments until maturity. As such, all short-term investments in the Company's portfolio are classified as "available-for-sale" and are stated at fair market value, with the unrealized gains and losses reported as a component of accumulated comprehensive income (loss). The amortized cost of debt securities is adjusted for amortization of premiums and accretion of unrealized discounts to maturity. Such amortization and accretion is included in interest income and other, net. The cost of securities sold is based on the specific identification method.

Concentrations of Risk

Substantially all of the Company's cash, cash equivalents and short-term investments are held by two financial institutions.

The Company provides credit to its customers in the normal course of business, performs ongoing credit evaluations of its customers, and maintains an adequate allowance for doubtful accounts. As of December 31, 2004 and 2003, no individual customer represented 10% or more of accounts receivable.

For the three years ended December 31, 2004, 2003 and 2002, suppliers representing greater than 10% of network access expenses were as follows:

<u>Access Provider:</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
A	6.8%	14.2%	19.0%
B	16.8%	21.3%	21.1%

In addition, the some of the contracts the Company has entered into with these access providers contain minimum purchase commitments (see Note 9).

Fair Value of Financial Instruments

For the Company's financial instruments, including cash, cash equivalents, accounts receivable, accounts payable, and accrued liabilities, carrying amounts approximate fair value due to the relatively short maturities of the financial instruments.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Property and Equipment

Property and equipment are recorded at cost less accumulated depreciation and amortization. Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the related assets as follows:

- Equipment (Three years)
- Furniture and fixtures (Five years)
- Computer software and equipment (Three years)
- Leasehold improvements (Shorter of useful life or lease term)

Impairment of Long-Lived Assets

The Company periodically evaluates the carrying amount of its property and equipment, annually or when events or changes in business circumstances have occurred, which indicate the carrying amount of such assets may not be fully realizable. Determination of impairment is based on an estimate of undiscounted future cash flows resulting from the use of the assets and their eventual disposition. If the Company determines these assets have been impaired, the impairment charge is recorded based on a comparison of the net book value of the fixed assets and the discounted future cash flows resulting from the use of the assets over their remaining useful lives. There have been no such impairment charges during any of the periods presented.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized as income in the period that includes the enactment date. A valuation allowance is recorded against deferred tax assets if it is more likely than not that all or a portion of the deferred tax assets will not be realized.

Stock-Based Compensation

Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation — Transition and Disclosure an Amendment of FASB Statement No. 123", amends the disclosure requirements of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), to require more prominent disclosures in both interim and annual financial statements regarding the method of accounting for stock-based employee compensation and the effect of the method used on reported results.

The Company accounts for stock-based awards to employees and directors using the intrinsic value method of accounting in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). Under the intrinsic value method, when the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized in the Company's Consolidated Statements of Operations.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The Company is required under SFAS 123, to disclose pro forma information regarding option grants made to its employees based on specified valuation techniques that produce estimated compensation charges. The pro forma information is as follows (in thousands, except per-share amounts):

	For the Year Ended December 31,		
	2004	2003	2002
Net income — as reported	\$ 19,068	\$ 13,902	\$ 29,759
Add: Stock-based employee compensation expense included in the reported net income, net of related tax effects	1,429	2,523	1,714
Deduct: Stock-based employee compensation expense using the fair value method, net of related tax effects	(3,699)	(3,029)	(2,265)
Pro forma net income	<u>\$ 16,798</u>	<u>\$ 13,396</u>	<u>\$ 29,208</u>
Basic net income per common share:			
As reported	\$ 0.31	\$ 0.26	\$ 2.34
Pro forma	\$ 0.28	\$ 0.25	\$ 2.29
Diluted net income per common share:			
As reported	\$ 0.29	\$ 0.23	\$ 0.57
Pro forma	\$ 0.26	\$ 0.22	\$ 0.56

The weighted average fair value of options granted during fiscal 2004, 2003 and 2002 was \$6.10, \$4.35 and \$1.35, respectively.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants for the twelve months ended December 31, 2004, 2003 and 2002:

	Employee Stock Options For the Year Ended December 31,			Employee Stock Purchase Plan For the Year Ended December 31,		
	2004	2003	2002	2004	2003	2002
Risk-free rate	3.0%	2.0%	3.0%	1.6%	—	—
Expected dividend yield	0%	0%	0%	0%	—	—
Expected volatility	41-47%	43%	0%*	32-52%	—	—
Expected life	3 Years	3 Years	3 Years	.5 Years	—	—

* Note that all stock option grants issued during the year ended December 31, 2002 were issued prior to the Company's initial public offering, therefore 0% volatility has been used. The employee stock purchase plan commenced on July 23, 2003 with the first purchase occurring on April 30, 2004.

Computation of Net Income per Share

Basic net income per share is computed by dividing net income by the weighted daily average number of shares of common stock outstanding during the period. Diluted net income per share is computed using the weighted daily average number of shares of common stock outstanding for the period plus dilutive potential common shares, including stock options and warrants using the treasury-stock method and from convertible preferred stock using the "if converted" method.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Revenue Recognition

Services and Fees

The Company derives substantially all of its revenues from usage fees. The Company recognizes revenues when persuasive evidence of an arrangement exists, service has been provided to the customer, the price to the customer is fixed or determinable, and collectibility is probable.

Revenues are recognized during the period the services are rendered to end users based on usage at negotiated rates. The Company typically requires its customers to commit to minimum usage levels. Minimum usage levels can be based on an annual term, monthly term or over the term of the arrangement. If actual usage in a given period is less than the minimum commitment, the Company recognizes the difference between the actual usage and the minimum commitment as revenue when cash is collected because the Company cannot reasonably estimate the amount of the difference that will be collected. The Company cannot reasonably estimate the amount of the difference to be collected because it has from time to time renegotiated minimum commitments in cases where customers have sought renegotiation of their contract for reasons such as a significant downturn in their business or where the Company has determined that it would be in its best interest to do so. Customers are not contractually entitled to use or otherwise receive benefit for unused service in subsequent periods.

The Company typically provides its customers with deployment services, technical support and additional optional services. Depending on the service provided and the nature of the arrangement, the Company may charge a one-time, annual or monthly fee. Revenues relating to one-time fees are recognized on a straight-line basis over the term of the initial contract, generally one to three years. Revenues relating to annual fees are recognized on a straight-line basis. Revenues for monthly services are recognized during the month that these services are provided.

License and Maintenance

License revenue consists principally of revenue earned under software license agreements. License revenue is generally recognized when a signed contract or other persuasive evidence of an arrangement exists, the software has been shipped or electronically delivered, the license fee is fixed or determinable, and collection of the resulting receivable is reasonably probable. We enter into revenue arrangements in which a customer may purchase a combination of software, upgrades and maintenance and support (multiple-element arrangements). When vendor-specific objective evidence ("VSOE") of fair value exists for all elements, we allocate revenue to each element based on the relative fair value of each of the elements. VSOE of fair value is established by the price charged when that element is sold separately. When contracts contain multiple elements wherein vendor specific objective evidence exists for all undelivered elements, we account for the delivered elements in accordance with the "Residual Method" prescribed by AICPA Statement of Position ("SOP") 98-9. Revenue from subscription license agreements, which include software, rights to future products and maintenance, is recognized ratably over the term of the subscription period. Revenue on shipments to resellers, which is generally subject to certain rights of return and price protection, is recognized when the products are sold by the resellers to the end-user customer.

Maintenance revenue consists of fees for providing software updates on a when and if available basis and technical support for software products (post-contract support or "PCS"). Maintenance revenue is recognized ratably over the term of the agreement.

Payments received in advance of services performed are deferred. Allowances for estimated future returns and discounts are provided for upon recognition of revenue.

The Company generally performs credit reviews to evaluate the customers' ability to pay. If the Company determines that collectibility is not probable, revenue is recognized as cash is collected.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Network Access

Network access expenses represent the amounts paid to network access providers for the usage of their networks. The Company has minimum purchase commitments with some network service providers for access that it expects to utilize during the term of the contracts. Costs of minimum purchase contracts are recognized as network access expenses at the greater of the minimum commitment or actual usage.

If the Company estimates that the revenues derived from the purchase commitment will be less than the purchase commitment, the Company recognizes a loss on that purchase commitment to the extent of that difference. No such loss has been recognized through December 31, 2004.

Advertising

Advertising and promotional costs are expensed as incurred. For the years ended December 31, 2004, 2003 and 2002 were approximately \$989,000, \$1.4 million and \$370,000, respectively.

Software Development Costs

Costs related to the research and development of new software and enhancements to existing software are expensed as incurred until technological feasibility has been established. To date, the Company's software has been available for general release concurrent with the establishment of technological feasibility, and accordingly, no costs have been capitalized.

The Company capitalizes the costs of computer software developed or obtained for internal use. During the years ended December 31, 2004, 2003 and 2002, the Company had no capitalized software development costs. Development costs are amortized over the estimated useful life of the software developed, which is generally six years. As of December 31, 2004 and 2003, the Company had no capitalized software development costs.

Recent Accounting Pronouncements

In December of 2004, the Financial Accounting Standards Board ("FASB") issued a revised version of Statement No. 123 *Accounting for Stock-Based Compensation* ("SFAS 123R"), which supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and its related implementation guidance. SFAS 123R requires recognition of the cost of employee services received in share-based payment transactions, thereby reflecting the economic consequences of those transactions in the financial statements. The accounting provisions for SFAS 123 are effective beginning with the first interim or annual reporting period that begins after June 15, 2005, and we will be required to adopt SFAS 123R in the third quarter of 2005. The pro forma disclosures previously permitted under SFAS 123 will no longer be an alternative to financial statement recognition. See "*Stock-Based Compensation*" above for the pro forma net income and net income per share amounts, for fiscal 2002 through 2004, as if we had used a fair-value-based method similar to the methods required under SFAS 123R to measure compensation expense for employee stock incentive awards. Although we have not yet determined whether the adoption of SFAS 123R will result in amounts that are similar to the current pro forma disclosures under SFAS 123, we are evaluating the requirements under SFAS 123R and expect the adoption of SFAS 123R to have a significant adverse impact on our consolidated statements of operations and net income per share.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 3. Short-Term Investments

The following tables summarize the Company's short-term investments as of December 31, 2004 and 2003 (in thousands):

December 31, 2004	Short-term Investments			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. Government agencies	103,357	—	(368)	102,989
Corporate notes	15,007	—	(56)	14,951
	<u>118,364</u>	<u>—</u>	<u>(424)</u>	<u>117,940</u>

December 31, 2003	Short-term Investments			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. Government agencies	80,551	110	—	80,661
Corporate notes	9,157	17	(2)	9,172
Asset backed	3,806	—	—	3,806
	<u>93,514</u>	<u>127</u>	<u>(2)</u>	<u>93,639</u>

The following table summarizes the principal amounts of the Company's short-term investments by expected maturity date (in thousands):

	Expected Maturity Date for Par Value Amounts For the Year Ended December 31,			As of Dec. 31, 2004
	2005	2006	Total Cost Value	Total Fair Value
	U.S. Government agencies	\$ 59,600	\$ 43,500	\$ 103,357
Corporate notes	—	14,415	15,007	14,951
Total	<u>\$ 59,600</u>	<u>\$ 57,915</u>	<u>\$ 118,364</u>	<u>\$ 117,940</u>

The Company recognized gross realized gains of \$17,000 and gross realized losses of \$115,000 for the year ended December 31, 2004. There were no recognized gains or losses on short-term investments for the year ended December 31, 2003. The Company has not recorded any impairment loss relating to an other-than-temporary impairment in the fair value of its short-term investments as the Company has the ability to hold the security until maturity.

Note 4. Allowance for Doubtful Accounts

Changes in the Company's allowance for doubtful accounts for the year ended December 31, 2002, 2003 and 2004 are as follows (in thousands):

	Beginning Balance	Provisions	Charge Offs	Ending Balance
Year ended December 31, 2002	\$ 1,114	\$ 1,250	\$ (864)	\$ 1,500
Year ended December 31, 2003	\$ 1,500	\$ 1,176	\$ (328)	\$ 2,348
Year ended December 31, 2004	\$ 2,348	\$ 1,100	\$ (1,377)	\$ 2,071

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 5. Property and Equipment

Property and equipment consisted of:

	<u>December 31,</u> <u>2004</u>	<u>December 31,</u> <u>2003</u>
	(In thousands)	
Equipment	\$ 17,906	\$ 13,694
Furniture and fixtures	2,538	2,456
Computer software and equipment	4,312	2,213
Leasehold improvements	1,620	1,443
	<u>26,376</u>	<u>19,806</u>
Less: Accumulated depreciation and amortization	(16,265)	(11,518)
Property and equipment, net	<u>\$ 10,111</u>	<u>\$ 8,288</u>

Depreciation expense was \$4,386,000, \$3,711,000 and \$3,396,000 for the years ended December 31, 2004, 2003 and 2002, respectively.

Note 6. Accrued Liabilities

Accrued liabilities consisted of:

	<u>December 31,</u> <u>2004</u>	<u>December 31,</u> <u>2003</u>
	(In thousands)	
Accrued commissions	\$ 2,928	\$ 2,979
Deferred rent	1,630	1,504
Deferred revenues	2,984	1,852
Paid time off payable	1,631	1,274
Other accrued liabilities	4,964	3,365
	<u>\$ 14,137</u>	<u>\$ 10,974</u>

Note 7. Business Combinations**Safe3w**

In September 2004, the Company completed its acquisition of Safe3w, Inc., a privately-held Woodbury, NY company that has developed patented dynamic device "fingerprinting" technology. The Company acquired 100% of the interest in Safe3w in a cash transaction for approximately \$8.5 million. The Company plans to incorporate Safe3w's technology into its existing products. The total purchase price includes \$300,000 in direct transactions costs, including legal and valuation fees.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The results of operations of Safe3w are included in the Company's Consolidated Statement of Operations beginning September 16, 2004, the date of the transaction closing. The following table summarizes the allocation of the purchase price based on the estimated fair values of the tangible assets acquired and the liabilities assumed at the date of acquisition (in thousands).

Cash acquired	\$ 7
Other tangible assets acquired	96
Amortizable intangible assets:	
Existing technology	2,900
Patent/core technology	1,100
Goodwill	<u>5,785</u>
Total assets acquired	9,888
Deferred tax liability, net	(953)
Liabilities assumed	(135)
Transaction costs	<u>(300)</u>
Net assets acquired	<u>\$ 8,500</u>

Identifiable intangible assets, including existing technology and patents/core technology are being amortized over their useful lives of eight years.

Developed technology was identified and valued through interviews, analysis of data provided by Safe3w concerning development projects, their stage of development, the time and resources needed to complete them, if applicable, and their expected income generating ability and associated risks. All development projects had reached technological feasibility and were classified as developed technology with the value assigned to existing technology capitalized. The income approach, which includes an analysis of the cash flows and risks associated with achieving such cash flows, was the primary technique utilized in valuing acquired intangible assets. Key assumptions included a discount rate of 21.0% and estimates of revenue growth, operating expenses and taxes.

The following unaudited pro forma information represents the results of operations for iPass and Safe3w for the twelve months ended December 31, 2004 and 2003 as if the acquisition had been consummated as of January 1, 2004 and 2003, respectively. This pro forma information does not purport to be indicative of what may occur in the future (in thousands, except per share amounts):

	Twelve Months Ended December 31,	
	2004	2003
Total revenue	\$ 166,444	\$ 136,223
Net income	16,187	10,893
Net income per share:		
Basic	\$ 0.27	\$ 0.20
Diluted	\$ 0.25	\$ 0.18
Number of shares used in per share calculations:		
Basic	60,770,680	53,474,537
Diluted	65,645,757	60,622,040

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Mobile Automation

In October 2004, the Company completed its acquisition of Mobile Automation, a privately-held Westlake Village, CA company that has developed solutions that help enterprise IT departments protect and manage their remote and mobile devices such as computers and personal data assistants (PDAs). The Company acquired 100% of the interest in Mobile Automation in a cash transaction for approximately \$20.0 million. The Company plans to enhance its product offering to its customers who use remote and mobile devices. The total purchase price includes \$187,000 in direct transactions costs, including legal and valuation fees.

The results of operations of Mobile Automation are included in the Company's Consolidated Statement of Operations beginning October 29, 2004, the date of the transaction closing. The following table summarizes the allocation of the purchase price based on the estimated fair values of the tangible assets acquired and the liabilities assumed at the date of acquisition (in thousands).

Cash acquired	\$	37
Accounts receivable		893
Other tangible assets acquired		52
Amortizable intangible assets:		
Existing technology		5,000
Patent/core technology		1,700
Maintenance agreements and certain relationships		400
Customer relationships		500
Goodwill		<u>14,228</u>
Total assets acquired		22,810
Deferred tax liability, net		(1,297)
Liabilities assumed		(1,326)
Transaction costs		(187)
Net assets acquired	\$	<u>20,000</u>

Identifiable intangible assets, including existing technology, patents/core technology and customer relationships are being amortized over their useful lives of four years. Maintenance agreements and certain relationships are being amortized over their useful lives of six years.

Developed technology was identified and valued through interviews, analysis of data provided by Mobile Automation concerning development projects, their stage of development, the time and resources needed to complete them, if applicable, and their expected income generating ability and associated risks. All development projects had reached technological feasibility and were classified as developed technology with the value assigned to existing technology capitalized. The income approach, which includes an analysis of the cash flows and risks associated with achieving such cash flows, was the primary technique utilized in valuing acquired intangible assets. Key assumptions included a discount rate of 21.2% and estimates of revenue growth, operating expenses and taxes.

The following unaudited pro forma information represents the results of operations for iPass and Mobile Automation for the twelve months ended December 31, 2004 and 2003 as if the acquisition had been

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

consummated as of January 1, 2004 and 2003, respectively. This pro forma information does not purport to be indicative of what may occur in the future (in thousands, except per share amounts):

	Twelve Months Ended December 31,	
	2004	2003
Total revenue	\$ 169,545	\$ 139,682
Net income	17,682	13,579
Net income per share:		
Basic	\$ 0.29	\$ 0.25
Diluted	\$ 0.27	\$ 0.22
Number of shares used in per share calculations:		
Basic	60,770,680	53,474,537
Diluted	65,645,757	60,622,040

Note 8. Acquired Intangibles, net

Acquired intangibles with finite lives as of December 31, 2004 are classified as follows:

	As of December 31, 2004		Weighted Average Remaining Useful Life
	Gross Carrying Amount	Accumulated Amortization (In thousands)	
Existing technology	\$ 7,900	\$ (314)	5.3 Years
Patent/ Core technology	2,800	(111)	5.4 Years
Maintenance agreements and certain relationships	400	(11)	5.8 Years
Customer relationships	500	(21)	3.8 Years
Total acquired intangibles	<u>\$ 11,600</u>	<u>\$ (457)</u>	5.2 Years

Aggregate amortization expense for the fiscal years (in thousands):

2004	\$ 457
Estimated amortization expense for the fiscal years (in thousands):	
2005	\$ 2,367
2006	2,367
2007	2,367
2008	2,067
2009	567
Thereafter	1,408
Total estimated amortization expense	<u>\$ 11,143</u>

Prior to the acquisition of Safe3w and Mobile Automation in 2004, the Company had no acquired intangibles balances or expenses relating to the amortization of acquired intangibles.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 9. Commitments and Contingencies

The Company leases its facilities under non-cancelable operating lease agreements that expire at various dates through February 2010. Future minimum lease payments under all non-cancelable operating leases as of December 31, 2004 are as follows (in thousands):

Year ending December 31:	
2005	\$ 3,799
2006	3,927
2007	4,055
2008	4,183
2009	4,311
2010	1,453
	<u>\$ 21,728</u>

Rent expense under operating leases for the years ended December 31, 2004, 2003, and 2002 was \$5,701,000, \$4,349,000 and \$4,210,000, respectively (net of sublease income of \$111,000 and \$415,000 in 2003 and 2002, respectively).

As of December 31, 2004, the Company had minimum purchase commitments with network service providers that expire at various dates through 2006. Future minimum purchase commitments under all agreements are as follows (in thousands):

Year ending December 31:	
2005	\$ 3,042
2006	208
	<u>\$ 3,250</u>

Legal Actions

On January 14, 2005, a lawsuit entitled *Palumbo v. iPass, Inc., et al.*, Case No. C 05 228 MHP was filed in the United States District Court for the Northern District of California, purportedly on behalf of a class of investors who purchased the Company's stock between April 22, 2004 and June 30, 2004. The complaint alleges claims under Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934 against the Company and certain of its officers and directors. Several similar lawsuits were subsequently filed in the same court. The Company expects that all of the cases will be consolidated into a single action. This matter is at an early stage; no lead plaintiff has been selected, no response to the complaint has been filed, no discovery has taken place and no trial date has been set. The Company and the individual defendants intend to take all appropriate actions to defend the suit. We cannot estimate any possible loss at this time.

Note 10. 401(k) Plan

Substantially all of the Company's employees are eligible to participate in the Company's 401(k) plan, which provides for discretionary Company matching contributions. There were no matching contributions for the years ended December 31, 2004, 2003 or 2002.

Note 11. Income Taxes

Income before income taxes includes net income from foreign operations of approximately \$968,000, \$736,000 and \$245,000 for the years ended December 31, 2004, 2003 and 2002, respectively.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The provision for (benefit from) income taxes consisted of the following for the years ended December 31, 2004, 2003 and 2002 (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Current			
U.S. federal	\$ 584	\$ 518	\$ —
State	583	1,285	531
Foreign	187	207	75
	<u>1,354</u>	<u>2,010</u>	<u>606</u>
Deferred			
U.S. federal	9,371	7,451	(22,245)
State	1,471	(493)	(2,054)
	<u>10,842</u>	<u>6,958</u>	<u>(24,299)</u>
Total provision for (benefit from) income taxes	<u>\$ 12,196</u>	<u>\$ 8,968</u>	<u>\$ (23,693)</u>

Deferred income taxes reflect the net tax effects of temporary differences between carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes and net loss carryforwards. A partial valuation allowance was placed on the deferred tax assets relating to the net operating loss carryforwards obtained as a result of the acquisition of Safe3w and Mobile Automation in 2004. The components of deferred tax assets (liabilities) consisted of the following as of December 31, 2004 and 2003 (in thousands):

	<u>2004</u>	<u>2003</u>
Deferred tax liabilities:		
Acquired intangibles	\$ (4,520)	\$ —
Deferred tax assets:		
Net operating loss carryforwards	11,461	13,104
Reserves and accruals	3,293	3,082
Other	1,624	1,155
Total deferred tax assets	<u>16,378</u>	<u>17,341</u>
Valuation allowance	<u>(3,216)</u>	<u>—</u>
Net deferred tax assets	<u>13,162</u>	<u>17,341</u>
Total net deferred income tax assets	<u>\$ 8,642</u>	<u>\$ 17,341</u>

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

For the years ended December 31, 2004, 2003 and 2002, the provision for (benefit from) income taxes differed from the amounts computed by applying the U.S. federal income tax rate to pretax income before income taxes as a result of the following:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Federal statutory rate	34%	34%	34%
State taxes, net of federal benefit	6	2	6
Foreign taxes	—	—	1
Amortization of stock-based compensation	(1)	6	14
Research and development benefit	(2)	(3)	—
Other	2	—	1
Change in valuation allowance	—	—	(447)
Provision for (benefit from) income taxes	<u>39%</u>	<u>39%</u>	<u>(391)%</u>

As of December 31, 2004, the Company had cumulative net operating loss carryforwards for federal and state tax reporting purposes of approximately \$11.7 million and \$3.6 million, respectively, which expire in various periods through 2021. Under current tax law, net operating loss carryforwards available in any given year may be limited upon the occurrence of certain events, including significant changes in ownership interest such as an IPO.

As of December 31, 2002, the Company determined that it was more likely than not that it would realize all of the available net deferred income tax assets in the carry forward period of up to 19 years. As a result, the Company determined that it was no longer necessary or appropriate to maintain a valuation allowance, and accordingly, during the year ended December 31, 2002 recorded a benefit from income taxes of \$24.3 million which is included in the Consolidated Statement of Operations.

Note 12. Common Stock

Stock Option Plans

In February 1997, the Company adopted the 1997 Stock Option Plan (1997 Plan). In June 1999, the Company adopted two option plans, the 1999 Stock Option Plan (1999 Plan) and the 1999 Interim Stock Option Plan (1999 Interim Plan). The 1997 Plan, the 1999 Plan, and the 1999 Interim Plan are collectively referred to as the Plans. Under the Plans, as amended, the Company is authorized to issue shares to employees, directors and consultants. The board of directors may grant incentive and nonqualified stock options to employees, directors, and consultants of the Company. The exercise price per share for nonstatutory stock options cannot be less than 85% of the fair market value, as determined by the board of directors, on the date of grant. The exercise price per share for incentive stock options cannot be less than the fair market value, as determined by the board of directors on the date of grant. Options generally vest over a four-year period and generally expire 10 years after the date of grant. Certain options can be exercised prior to vesting in exchange for restricted stock. Should the option holder subsequently terminate employment prior to vesting, the Company has the right to repurchase unvested shares at the lower of original exercise price or fair value. At December 31, 2004, 635,113 shares of common stock were subject to repurchase at a weighted average exercise price of \$0.50 per share.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Stock option activity under the Plans for the three years ended December 31, 2004 is summarized below:

	Shares Available for Grant	Number of Shares	Weighted Average Exercise Price
Balance as of December 31, 2001	1,614,664	9,783,296	\$ 2.32
Granted	(1,800,000)	1,800,000	0.83
Exercised	—	(3,240,697)	0.52
Cancelled	1,334,281	(1,334,281)	3.19
Balance as of December 31, 2002	1,148,945	7,008,318	2.60
Authorized	8,859,026	—	—
Granted	(1,792,200)	1,792,200	6.00
Exercised	—	(661,550)	4.55
Cancelled	251,395	(251,395)	2.79
Balance as of December 31, 2003	8,467,166	7,887,573	3.46
Authorized	3,024,171	—	—
Granted	(4,497,933)	4,497,933	6.10
Exercised	—	(1,885,253)	2.75
Cancelled	385,267	(385,267)	3.11
Balance at December 31, 2004	<u>7,378,671</u>	<u>10,114,986</u>	<u>\$ 4.78</u>
Exercisable as of December 31, 2002		2,576,460	\$ 3.75
Exercisable as of December 31, 2003		3,891,821	\$ 3.45
Exercisable as of December 31, 2004		4,055,123	\$ 3.83

The following table summarizes the options outstanding as of December 31, 2004:

Exercise Prices	Options Outstanding			Options Exercisable	
	Number of Options	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
\$0.06-1.50	2,360,425	6.74	\$ 0.66	1,444,084	\$ 0.64
\$2.00-4.75	2,450,903	5.46	\$ 3.75	1,784,600	\$ 4.12
\$5.05-5.35	3,175,091	9.58	\$ 5.26	234,465	\$ 5.33
\$5.50-20.02	2,128,567	8.04	\$ 9.83	591,974	\$ 10.13
	<u>10,114,986</u>	7.60	\$ 4.78	<u>4,055,123</u>	\$ 3.83

As of December 31, 2004, 635,113 options ranging in exercise price from \$0.50 to \$0.85 were exercised and are currently unvested and subject to repurchase by the Company.

The Company's board of directors adopted the 2003 Employee Stock Purchase Plan, the 2003 Equity Incentive Plan and the 2003 Non-employee Directors Plan on January 15, 2003.

Stock-Based Compensation

The Company records stock-based compensation charges in the amount, if any, by which the option exercise price or the restricted stock purchase price is less than the deemed fair value of common stock at the

iPASS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

date of grant. Prior to the Company's IPO, the Company's board of directors determined the fair value of our common stock based upon several factors, including operating performance, issuances of convertible preferred stock, liquidation preferences of preferred stockholders, and valuations of other publicly-traded companies. The Company recorded deferred stock-based compensation totaling approximately \$0, \$5,836,000 and \$2,300,000 for the years ended December 31, 2004, 2003 and 2002, that is being amortized on an accelerated basis over the corresponding vesting period, using the method outlined in FASB Interpretation No. 28. Deferred stock-based compensation was decreased by approximately \$202,000, \$282,000 and \$572,000 for the years ended December 31, 2004, 2003 and 2002, due to forfeiture of accrued but unvested deferred stock-based compensation arising from the termination of employees. Amortization of deferred compensation expense for the years ended December 31, 2004, 2003 and 2002, was approximately \$2,342,000, \$4,069,000 and \$2,765,000, respectively. Non-employee equity transactions were accounted for at fair value at each grant date pursuant to SFAS No. 123. The amount of deferred stock-based compensation expense to be recorded in future periods could decrease if options for which accrued but unvested compensation has been recorded are forfeited.

Note 13. Segment Information

SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information* establishes standards for the reporting by business enterprises of information about operating segments, products and services, geographic areas, and major customers. The method for determining what information is reported is based on the way that management organizes the operating segments within the Company for making operational decisions and assessments of financial performance. The Company's chief operating decision maker is considered to be the Company's chief executive officer (CEO). The CEO reviews financial information presented on a consolidated basis for purposes of making operating decisions and assessing financial performance. The consolidated financial information reviewed by the CEO is similar to the information presented in the accompanying consolidated financial statements of operations. Therefore, the Company has determined that it operates in a single reportable segment.

International revenue is determined by the location of the customer's headquarters. International revenue accounted for approximately 41%, 39% and 39% of total revenues for the years ended December 31, 2004, 2003, and 2002, respectively. Revenues in the United Kingdom accounted for 11% of total revenues in 2004. No individual foreign country accounted for 10% or more of total revenues in 2003 or 2002.

Substantially all of the Company's long-lived assets are located in the United States.

Note 14. Net Income Per Common Share

In accordance with SFAS 128, "Earnings Per Share," basic net income per share is computed by dividing net income by the weighted daily average number of shares of common stock outstanding during the period. The weighted daily average number of shares of common stock excludes shares that have been exercised prior to vesting and are subject to repurchase by the company. As such, basic net income per share excludes 635,113, 1,467,190 and 2,271,651 shares subject to repurchase for the years ended December 31, 2004, 2003 and 2002, respectively. These shares have been included in diluted net income per share to the extent that the inclusion of such shares is not anti-dilutive. Diluted net income per share is based upon the weighted daily average number of shares of common stock outstanding for the period plus dilutive potential common shares, including stock options using the treasury-stock method and from convertible stock using the "if converted" method.

iPASS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table sets forth the computation of basic and diluted net income per share (in thousands, except share and per share amounts):

	For the Year Ended December 31,		
	2004	2003	2002
Numerator:			
Net income	\$ 19,068	\$ 13,902	\$ 29,759
Denominator:			
Denominator for basic net income per common share			
Weighted average shares outstanding	60,770,680	53,474,537	12,742,068
Effect of dilutive securities:			
Preferred stock	—	—	35,273,169
Stock options	4,875,077	7,147,503	3,835,170
Warrants	—	—	22,660
Denominator for diluted net income per common share — adjusted			
	65,645,757	60,622,040	51,873,067
Basic net income per common share	\$ 0.31	\$ 0.26	\$ 2.34
Diluted net income per common share	\$ 0.29	\$ 0.23	\$ 0.57

The following potential shares of common stock have been excluded from the computation of diluted net income per share because the effect of including these shares would have been anti-dilutive:

	For the Year Ended December 31,		
	2004	2003	2002
Options to purchase common stock	804,250	351,200	2,914,281
Common stock subject to repurchase	—	—	27,500
Warrants	—	—	535,601
Total	804,250	351,200	3,477,382

The weighted-average exercise price of options to purchase common stock excluded from the computation was \$14.56, \$18.12 and \$5.30 for the years ended December 31, 2004, 2003 and 2002, respectively. The weighted-average repurchase price of common stock excluded was \$2.00 for the year ended December 31, 2002. The weighted-average exercise price of warrants excluded was \$4.88 for the year ended December 31, 2002.

Note 15. Related Party Transactions

During 2002, the Company entered into two full recourse notes receivable for \$1,484,675 with two executive officers for the exercise of stock options. The notes as well as any accrued interest were paid in full during 2004.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

iPass Inc.

By: /s/ Donald C. McCauley

Donald C. McCauley
Vice President and Chief Financial Officer
(duly authorized officer and principal financial officer)

Date: March 15, 2005

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENT, that each person whose signature appears below constitutes and appoints Donald C. McCauley and Bruce K. Posey, and each or any one of them, his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments (including post-effective amendments) to this Report, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his substitutes or substitute, may lawfully do or cause to be done by virtue hereof.

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

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ KENNETH D. DENMAN</u> Kenneth D. Denman	Chairman, President, Chief Executive Officer and Director	March 15, 2005
<u>/s/ DONALD C. MCCAULEY</u> Donald C. McCauley	Vice President, Finance, and Chief Financial Officer (Principal Financial Officer)	March 15, 2005
<u>/s/ FRANK E. VERDECANNA</u> Frank E. Verdecanna	Vice President and Corporate Controller (Principal Accounting Officer)	March 15, 2005
<u>/s/ A. Gary Ames</u> A. Gary Ames	Director	March 15, 2005
<u>/s/ Cregg B. Baumbaugh</u> Cregg B. Baumbaugh	Director	March 15, 2005

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Signature	Title	Date
<hr/> <i>/s/ John D. Beletic</i> John D. Beletic	Director	March 15, 2005
<hr/> <i>/s/ Peter G. Bodine</i> Peter G. Bodine	Director	March 15, 2005
<hr/> <i>/s/ Arthur C. Patterson</i> Arthur C. Patterson	Director	March 15, 2005
<hr/> <i>/s/ Allan R. Spies</i> Allan R. Spies	Director	March 15, 2005

INDEX TO EXHIBITS

<u>Exhibit Number</u>	<u>Description of Document</u>
2.1	Agreement and Plan of Merger dated October 26, 2004 by and among iPass Inc., Montage Acquisition Corp., Mobile Automation, Inc. and David Strohm, as Stockholders' Agent.
3.1	Amended and Restated Certificate of Incorporation.(1)
3.2	Bylaws, as amended.(1)
4.1	Reference is made to Exhibits 3.1 and 3.2.
4.2	Specimen stock certificate.(1)
10.1	2003 Equity Incentive Plan and form of related agreements, as amended.(1)
10.2	2003 Non-Employee Directors Plan.(1)
10.3	1999 Stock Option Plan and form of related agreements.(1)
10.4	1997 Stock Option Plan and form of related agreements.(1)
10.5	Interim 1999 Stock Option Plan.(1)
10.6	Restricted Stock Purchase Agreement by and between the Registrant and Anurag Lal dated November 8, 1999.(1)
10.7	2003 Employee Stock Purchase Plan and form of related agreements, as amended.(1)
10.8	Lease Agreement, dated October 26, 1999 between Registrant and Westport Joint Venture (as amended).(1)
10.9	Amended and Restated Investor Rights Agreement dated August 8, 2000 between Registrant, founders and holders of the Registrant's Preferred Stock.(1)
10.10	Form of Indemnity Agreement.(1)
10.11	Employment Agreement, dated November 13, 2001 between Registrant and Kenneth D. Denman.(1)
10.12	Form of Offer Letter to Executive Officers.(1)
10.13	OEM Service Provider License Agreement, dated February 29, 2000, between RSA Security, Inc. and the Registrant, and amendments thereto.(1)(3)
10.14	Support Agreement, dated February 29, 2000, by and between RSA Security, Inc. and the Registrant.(1)(3)
10.15	Managed Data Network Services Agreement, dated September 17, 1996, between Equant, (formerly Scitor International Telecommunication Services, Inc.), and the Registrant, and amendments thereto.(1)(3)
10.16	Loan and Security Agreement dated September 4, 2001 between Silicon Valley Bank and the Registrant and modifications thereto.(1)
10.17	Internet Service Agreement dated April 25, 2001, by and between UUNET Technologies, Inc. and the Registrant, and amendment thereto.(1)(3)
10.18	Virtual Internet Provider (VIP) Agreement dated January 9, 1997, by and between UUNET Technologies, Inc. and the Registrant and amendments thereto.(1)(3)
10.19	Management Bonus Structure 2005 Plan (4)
10.20	Outside Director Compensation Arrangement (5)
10.21	Executive Officer Cash Compensation Arrangement (6)
21.1	Subsidiaries of the Registrant.
23.1	Consent of Independent Registered Public Accounting Firm.
24.1	Power of Attorney.(reference is made to the signature page of this Form 10-K)
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

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Exhibit Number	Description of Document
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

- (1) Previously filed as the like-numbered exhibit to our Registration Statement on Form S-1, as amended, originally filed with the Securities and Exchange Commission on January 24, 2003, as amended, and incorporated by reference herein.
- (2) Previously filed as the like-numbered exhibit to our Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 13, 2003, and incorporated by reference herein.
- (3) Confidential treatment has been granted for a portion of the exhibit. The information omitted pursuant to such confidential treatment order has been filed separately with the Securities and Exchange Commission.
- (4) Previously filed as the file-numbered exhibit on our Current Report on Form 8-K filed with the Securities and Exchange Commission on February 17, 2005, and incorporated by reference herein.
- (5) Previously disclosed under the caption "Compensation of Directors" in our Definitive Proxy Statement on Schedule 14A filed with the Securities and Exchange Commission on April 26, 2004, and incorporated by reference herein.
- (6) Previously disclosed under the caption "Compensation of Executive Officers" in our Definitive Proxy Statement on Schedule 14A filed with the Securities and Exchange Commission on April 26, 2004, and incorporated by reference herein.

AGREEMENT AND PLAN OF MERGER

among:

iPass Inc.,
a Delaware corporation;

Montage Acquisition Corp.,
a Delaware corporation;

Mobile Automation, Inc.,
a Delaware corporation;

and

David Strohm,
as **Stockholder's Agent.**

Dated as of October 26, 2004

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EXHIBITS

Exhibit A	-	Certain Definitions
Exhibit B	-	Form of Proprietary Information and Inventions Agreement
Exhibit C-1	-	Form of Offer Letter
Exhibit C-2	-	Continuing Employees from the Company
Exhibit D	-	Escrow Agreement
Exhibit E-1	-	Form of Release
Exhibit E-2	-	List of Individuals Signing Release
Exhibit F	-	Form of Legal Opinion of Stradling Yocca Carlson & Rauth
Schedule I	-	Specified Payment Obligations

AGREEMENT AND PLAN OF MERGER

This Agreement and Plan of Merger (this “**Agreement**”) is made and entered into as of October 26, 2004, by and among: **iPass Inc.**, a Delaware corporation (“**Parent**”); **Montage Acquisition Corp.**, a Delaware corporation and a wholly owned subsidiary of Parent (“**Merger Sub**”); **Mobile Automation, Inc.**, a Delaware corporation (the “**Company**”); and, for the limited purpose of agreeing to and becoming bound by the provisions of Section 10.1, David Strohm, as Stockholder’s Agent. Certain other capitalized terms used in this Agreement are defined in **Exhibit A**.

Recitals

A. Parent, Merger Sub and the Company intend to effect a merger of Merger Sub with and into the Company in accordance with this Agreement and the Delaware General Corporation Law (the “**DGCL**”) (the “**Merger**”). Upon consummation of the Merger, Merger Sub will cease to exist, and the Company will become a wholly owned subsidiary of Parent.

B. This Agreement has been approved by the respective boards of directors of Parent, Merger Sub and the Company.

C. In order to induce Parent to enter into this Agreement and to consummate the transactions contemplated by this Agreement, contemporaneously with the execution and delivery of this Agreement, the individuals listed on **Exhibit C-2** are each executing a proprietary information and inventions agreements of even date substantially in the form of **Exhibit B**.

Agreement

The parties to this Agreement agree as follows:

SECTION 1. Description of Transaction

1.1 Merger of Merger Sub with and into the Company. Upon the terms and subject to the conditions set forth in this Agreement, at the Effective Time (as defined in Section 1.3), Merger Sub shall be merged with and into the Company, and the separate existence of Merger Sub shall cease. The Company will continue as the surviving corporation in the Merger (the “**Surviving Corporation**”).

1.2 Effect of the Merger. The Merger shall have the effects set forth in this Agreement and in the applicable provisions of the DGCL.

1.3 Closing; Effective Time. The consummation of the transactions contemplated by this Agreement (the “**Closing**”) shall take place at the offices of Cooley Godward llp, 3175 Hanover Street, Palo Alto, California 94306 at 10:00 a.m. on a date to be mutually agreed to by Parent and the Company after the satisfaction (or, to the extent permitted, waiver) of the conditions set forth in Sections 6 and 7. The date on which the Closing actually takes place is

referred to in this Agreement as the “**Closing Date**.” Contemporaneously with or as promptly as practicable after the Closing, a properly executed certificate of merger conforming to the requirements of the DGCL shall be filed with the Secretary of State of the State of Delaware. The Merger shall become effective at the time such certificate of merger is filed with the Secretary of State of the State of Delaware (the “**Effective Time**”).

1.4 Certificate of Incorporation and Bylaws; Directors and Officers. Unless otherwise determined by Parent and the Company prior to the Effective Time:

(a) the certificate of incorporation of the Surviving Corporation shall be the Certificate of Incorporation of Merger Sub as in effect immediately prior to the Effective Time;

(b) the bylaws of the Surviving Corporation shall be the bylaws of Merger Sub as in effect immediately prior to the Effective Time; and

(c) the directors and officers of the Surviving Corporation immediately after the Effective Time shall be the respective individuals who are directors and officers of Merger Sub immediately prior to the Effective Time.

1.5 Conversion of Shares.

(a) Immediately prior to the Effective Time, each share of Company Preferred Stock shall be converted into one (1) share of Company Common Stock.

(b) The aggregate consideration to be paid by Parent and Merger Sub in the Merger to holders of Company Common Stock, the Converted Option Holders (as defined in Section 1.6 below) and the Converted Warrant Holders (as defined in Section 1.6 below) shall be U.S. \$20,000,000, less the amount of (1) specified payment obligations of the Company as set forth on **Schedule I** hereto (as may be updated prior to the Closing) that would be assumed by Parent (the “**Specified Payment Obligations**”) and (2) fees, costs and expenses for which the Company Stockholders, the Converted Option Holders and the Converted Warrant Holders are responsible pursuant to Section 10.3 (the “**Merger Consideration**”).

(c) Subject to the other subsections of this Section 1.5 and Sections 1.6, 1.8, 1.9 and 1.10, at the Effective Time, by virtue of the Merger and without any further action on the part of Parent, Merger Sub, the Company or any stockholder, Converted Option Holder or Converted Warrant Holder of the Company:

(i) each share of the common stock (par value \$0.001 per share) of Merger Sub then outstanding shall remain outstanding and each certificate therefor shall be converted into one share of common stock of the Surviving Corporation;

(ii) each share of Company Common Stock held in the Company’s treasury as of the Effective Time shall be cancelled and retired and all rights in respect thereof shall cease to exist, without any conversion thereof or payment of any consideration therefor; and

(iii) each share of Company Common Stock outstanding immediately prior to the Effective Time shall be converted into the right to receive from Parent, upon surrender of the certificate representing such share of Company Capital Stock, an amount of cash, without interest, equal to (i) the Merger Consideration divided by (ii) the sum of (a) the number of shares of Common Stock outstanding immediately prior to the Effective Time and (b) the number of Net Option Shares (as set forth in the definition of Option Consideration in **Exhibit A**) and Net Warrant Shares (as set forth in the definition of Warrant Consideration in **Exhibit A**) outstanding immediately prior to the Effective Time.

(d) Notwithstanding anything to the contrary contained in Section 1.5 or elsewhere in this Agreement, at or promptly after the Closing, \$4,000,000 of the aggregate consideration otherwise payable to the holders of Company Common Stock, Converted Option Holders and Converted Warrant Holders pursuant to Section 1.5 (the "**Escrow Amount**") shall be withheld from such stockholders Converted Option Holders and Converted Warrant Holders and deposited with the Escrow Agent in an escrow account (the "**Escrow Account**"), to be held and distributed in accordance with the terms of that certain Escrow Agreement, substantially in the form of **Exhibit D** (the "**Escrow Agreement**").

(e) If, between the date of this Agreement and the Effective Time, the outstanding shares of Company Capital Stock are changed into a different number or class of shares by reason of any stock split, division or subdivision of shares, stock dividend, reverse stock split, consolidation of shares, reclassification, recapitalization or other similar transaction, then the Merger Consideration shall be appropriately adjusted.

1.6 Stock Options; Warrants.

(a) The Company shall take such action as is necessary or required, including action necessary or required under the Company's Amended and Restated Certificate of Incorporation and any Company Stock Plan and each outstanding option grant thereunder ("**Company Option**"), to accelerate the vesting of such Company Options effective immediately prior to the Effective Time. Prior to the Effective Time, the Company may enter into an agreement, in a form reasonably satisfactory to Parent (each a "Stock Option Cancellation Agreement"), with each holder (each a "Converted Option Holder") of an outstanding Company Option providing for a termination of such Company Option effective as of the Effective Time, in exchange for the payment (an subject to the provisions of Section 1.8) of the Option Consideration; provided, that the Option Consideration shall be reduced by any applicable federal and state withholding taxes. Each outstanding Company Option that remains unexercised or outstanding immediately prior to the Effective Time shall be terminated in accordance with the terms of such Company Option and not be assumed by Parent, and all rights with respect to Company Capital Stock under outstanding Company Option shall thereupon be terminated.

(b) Prior to the Effective Time, the Company may enter into an agreement, in a form reasonably satisfactory to Parent, with each holder (each a "Converted Warrant Holder") of an outstanding warrant to purchase or acquire Company Capital Stock ("**Company Warrant**") providing for a termination of such Company Warrant effective as of the Effective Time, in exchange for the payment (subject to the provisions of Section 1.8) of the Warrant

Consideration; provided, that the Warrant Consideration shall be reduced by any applicable federal and state withholding taxes. Each Company Warrant that remains unexercised or outstanding immediately prior to the Effective Time shall be terminated in accordance with the terms of such Company Warrant and not be assumed by Parent, and all rights with respect to Company Capital Stock under outstanding Company Warrants shall thereupon be terminated.

(c) At the Effective Time, the Company shall take all action that may be necessary (under the Company's Stock Plan and related stock option agreements, the Company Warrants, applicable law or regulation and otherwise) to effectuate the provisions of this Section 1.6.

1.7 Closing of the Company's Transfer Books. At the Effective Time, holders of certificates representing shares of the Company's capital stock that were outstanding immediately prior to the Effective Time shall cease to have any rights as stockholders of the Company, and the stock transfer books of the Company shall be closed with respect to all shares of such capital stock outstanding immediately prior to the Effective Time. No further transfer of any such shares of the Company's capital stock shall be made on such stock transfer books after the Effective Time. If, after the Effective Time, a valid certificate previously representing any of such shares of the Company's capital stock (a "**Company Stock Certificate**") is presented to the Surviving Corporation or Parent, such Company Stock Certificate shall be cancelled.

1.8 Balance Sheet Adjustment.

(a) Notwithstanding anything to the contrary contained elsewhere in this Agreement, in addition to the Escrow Amount withheld pursuant to Section 1.5(d), a portion of the aggregate consideration otherwise payable to the Company Common Stockholders, Converted Option Holders and Converted Warrant Holders pursuant to Section 1.5(a)(ii) of this Agreement equal to \$300,000 (the "**Adjustment Amount**") shall be withheld. In the event that at any time within thirty (30) days following the Closing Date (the "**Determination Deadline**") it is determined by Parent in good faith and based on documentation shared with the Stockholders' Agent that (i) the outstanding debt of the Company as of the Closing is greater than the amounts listed on **Schedule I** hereto; or (ii) the amount of Current Net Assets of the Company as of the Closing (excluding any fees, costs and expenses of the Company described in Section 10.3 of this Agreement) are less than the Current Net Assets of the Company set forth in the Unaudited Interim Balance Sheet (as defined in Section 2.4(a)(ii)) (the aggregate amount of any difference under clause (i) and (ii) being the "**Shortfall**"), then Parent shall have the right to recover from the Escrow Amount the extent of the Shortfall.

(b) Within five (5) business days following the Determination Deadline, Parent shall distribute on a pro rata basis to the Company Common Stockholders, Converted Option Holders and Converted Warrant Holders the Adjustment Amount, less any Shortfall. With respect to distribution of the Adjustment Amount, if any, to the Company Common Stockholders, Converted Option Holders and Converted Warrant Holders, Parent's sole obligation is to deliver the balance of the Adjustment Amount, if any. The Company Common Stockholders, Converted Option Holders or Converted Warrant Holders will not be entitled to any interest on the Adjustment Amount. The parties hereto agree that the Adjustment Amount is

intended to secure Parent partially against any Shortfall and is not the sole or exclusive remedy for Parent or any other Indemnitee for recovery of any payments or losses arising from any inaccuracy or breach of representations, warranties and covenants, and Parent shall be entitled to recover any such losses or payments exceeding the Adjustment Amount through the Escrow Amount or other available remedy.

1.9 Dissenting Shares.

(a) Notwithstanding anything to the contrary contained in this Agreement, to the extent that the provisions of Section 262 of the DGCL or Chapter 13 of the CGCL are or prior to the Effective Date may become applicable to the Merger, any shares of Company Common Stock that, as of the Effective Time, may carry appraisal rights under Section 262 of the DGCL or Chapter 13 of the CGCL shall not be converted into or represent the right to receive the Merger Consideration, and the holder or holders of such shares shall be entitled only to such rights as may be granted to such holder or holders in Section 262 of the DGCL or Chapter 13 of the CGCL; *provided, however*, that if shares carrying appraisal rights shall not be perfected, or if any such shares shall lose their status as shares carrying appraisal rights, then, as of the later of the Effective Time or the time of the failure to perfect such status or the loss of such status, such shares shall automatically be converted into and shall represent only the right to receive (upon the surrender of the certificate or certificates representing such shares) the Merger Consideration in accordance with Section 1.5.

(b) The Company shall give Parent (i) prompt notice of any written demand received by the Company prior to the Effective Time to require the Company to purchase shares of Company Common Stock pursuant to Section 262 of the DGCL or Chapter 13 of the CGCL and of any other demand, notice or instrument delivered to the Company prior to the Effective Time pursuant to the DGCL or CGCL, and (ii) the opportunity to participate in all negotiations and proceedings with respect to any such demand, notice or instrument. The Company shall not make any payment or settlement offer prior to the Effective Time with respect to any such demand unless Parent shall have consented in writing to such payment or settlement offer.

1.10 Further Action. If, at any time after the Effective Time, any further action is determined by Parent to be necessary or desirable to carry out the purposes of this Agreement or to vest the Surviving Corporation or Parent with full right, title and possession of and to all rights and property of Merger Sub and the Company, the officers and directors of the Surviving Corporation and Parent shall be fully authorized (in the name of Merger Sub, in the name of the Company and otherwise) to take such action.

SECTION 2. Representations and Warranties of the Company

The Company represents and warrants, to and for the benefit of the Indemnitees, that each statement set forth in each of the sections and subsections of this Section 2 (each such statement being a “representation and warranty” of the Company) is accurate and complete, except as set forth in the Disclosure Schedule delivered separately to Parent by the Company on the date of this Agreement corresponding to the particular section or subsection of this Section 2 in which such representation and warranty appears (it being understood, however, that a disclosure in a particular Disclosure Schedule will also be deemed to qualify a representation and

warranty that does not appear in the corresponding section or subsection of this Section 2 if it is readily apparent on the face of such disclosure that such disclosure qualifies such representation and warranty).

2.1 Due Organization; No Subsidiaries; Etc.

(a) The Company is a corporation duly organized, validly existing and in good standing under the laws of the jurisdiction of its incorporation and has all necessary power and authority: (i) to conduct its business in the manner in which its business is currently being conducted; (ii) to own and use its assets in the manner in which its assets are currently owned and used; and (iii) to perform its obligations under all Company Contracts.

(b) Except as set forth in Part 2.1 of the Disclosure Schedule, the Company has not conducted any business under or otherwise used, for any purpose or in any jurisdiction, any fictitious name, assumed name, trade name or other name, other than the name "Mobile Automation, Inc."

(c) The Company is not and has not been required to be qualified, authorized, registered or licensed to do business as a foreign corporation in any jurisdiction, except where the failure to be so qualified, authorized, registered or licensed has not had and would not reasonably be expected to have a Material Adverse Effect on the Company.

(d) Part 2.1 of the Disclosure Schedule accurately sets forth (i) the names of the members of the board of directors of the Company, (ii) the names of the members of each committee of the board of directors of the Company, and (iii) the names and titles of the officers of the Company.

(e) The Company does not directly or indirectly own any controlling interest in any Entity and, except for the equity interests identified in Part 2.1 of the Disclosure Schedule, the Company has never owned, beneficially or otherwise, any shares or other securities of, or any direct or indirect equity interest in, any Entity. The Company has neither agreed to nor is obligated to make any future investment in or capital contribution to any Entity. The Company has neither guaranteed nor is responsible or liable for any obligation of any of the Entities in which it owns or has owned any equity interest.

2.2 Certificate of Incorporation and Bylaws; Records. The Company has delivered to Parent accurate and complete copies of: (a) the Company's certificate of incorporation and bylaws, including all amendments thereto; (b) the stock records of the Company; and (c) except as set forth in Part 2.2 of the Disclosure Schedule, the minutes and other records of the meetings and other proceedings (including any actions taken by written consent or otherwise without a meeting) of the stockholders of the Company, the board of directors of the Company and all committees of the board of directors of the Company. There have been no formal meetings or other proceedings of the stockholders of the Company, the board of directors of the Company or any committee of the board of directors of the Company that are not reflected in all material respects in such minutes or other records. There has not been any violation of any of the provisions of the Company's certificate of incorporation or bylaws, and the Company has not taken any action that is inconsistent in any material respect with any

resolution adopted by each the Company's stockholders, the board of directors of the Company or any committee of the Company's board of directors. The books of account, stock records, minute books and other records of the Company are accurate, up-to-date and complete in all material respects, and have been maintained in accordance with prudent business practices.

2.3 Capitalization, Etc.

(a) The authorized capital stock of the Company consists of: (i) 50,000,000 shares of Company Common Stock, of which 7,009,003 shares have been issued and are outstanding as of the date of this Agreement; and (ii) 30,000,000 shares of Preferred Stock (A) 1,000,000 of which have been designated "Series A Preferred Stock," of which 735,294 shares have been issued and are outstanding as of the date of this Agreement and (B) 16,000,000 of which have been designated "Series B Preferred Stock," of which 15,941,179 shares have been issued and are outstanding as of the date of this Agreement. Each outstanding share of Series A Preferred Stock is convertible into one share of Company Common Stock. Each outstanding share of Series B Preferred Stock is convertible into one share of Company Common Stock. All of the outstanding shares of Company Capital Stock have been duly authorized and validly issued, and are fully paid and non-assessable. Part 2.3(a) of the Disclosure Schedule (i) provides an accurate and complete description of the terms of each repurchase option which is held by the Company and to which any of such shares is subject and (ii) sets forth all issued and outstanding shares of the Company Capital Stock as of the date of this Agreement.

(b) The Company has reserved 7,319,635 shares of Company Common Stock for issuance under its Stock Plan, of which options to purchase 6,670,353 shares are outstanding as of the date of this Agreement. The Company has reserved an additional (i) 147,060 shares of Company Common Stock for issuance upon exercise of Common Stock Company Warrants; and (ii) 683,125 shares of Series B Preferred Stock for issuance upon exercise of Series B Company Warrants. The Company has delivered to Parent accurate and complete copies of the Company Warrants. The exercise price of the Common Stock Company Warrants is \$0.34 per share. The exercise price of the Series B Company Warrants is between \$0.05 and \$0.20 per share. Part 2.3 of the Disclosure Schedule accurately sets forth, with respect to each Company Option and Company Warrant that is outstanding as of the date of this Agreement: (i) the name of the holder of such Company Option or Company Warrant; (ii) the total number of shares of Company Common Stock or Series B Preferred Stock, as applicable, that are subject to such Company Option or Company Warrant and the number of shares of Company Common Stock or Series B Preferred Stock with respect to which such Company Option or Company Warrant is immediately exercisable; (iii) the date on which such Company Option or Company Warrant was granted and the term of such Company Option or Company Warrant; (iv) the vesting schedule for such Company Option or Company Warrant; (v) the exercise price per share of Company Common Stock or Series B Preferred Stock purchasable under such Company Option or Company Warrant; and (vi) whether such Company Option has been designated an "incentive stock option" as defined in Section 422 of the Code. Except for the Company Options and Company Warrants and except as set forth in Part 2.3(b) of the Disclosure Schedule, there is no: (A) outstanding subscription, option, call, warrant or right (whether or not currently exercisable) to acquire any shares of the capital stock or other securities of the Company; (B) outstanding security, instrument or obligation that is or may become convertible into or exchangeable for any

shares of the capital stock or other securities of the Company; (C) Contract under which the Company is or may become obligated to sell or otherwise issue any shares of its capital stock or any other securities; or (D) to the best Knowledge of the Company, condition or circumstance that may give rise to or provide a basis for the assertion of a claim by any Person to the effect that such Person is entitled to acquire or receive any shares of capital stock or other securities of the Company.

(c) All outstanding shares of Company Capital Stock and all outstanding Company Options and Company Warrants, have been issued and granted in compliance with (i) all applicable securities laws and other applicable Legal Requirements, and (ii) all requirements set forth in applicable Contracts.

(d) Except as set forth in Part 2.3(d) of the Disclosure Schedule, the Company has never repurchased, redeemed or otherwise reacquired any shares of capital stock or other securities of the Company. All securities so reacquired by the Company were reacquired in compliance with (i) the applicable provisions of the DGCL and all other applicable Legal Requirements, and (ii) all requirements set forth in applicable restricted stock purchase agreements and other applicable Contracts.

(e) Immediately prior to the Effective Time, and following: (i) the filing of a Certificate of Amendment of Amended and Restated Certificate of Incorporation with the Secretary of State of Delaware to increase the authorized number of shares of Series B Preferred Stock from 16,000,000 to 29,000,000, (ii) conversion of all principal and accrued interest on certain indebtedness of Greylock IX, Limited Partnership into shares of Series B Preferred Stock, and (iii) conversion of all issued and outstanding shares of Preferred Stock into shares of Company Common Stock, the authorized capital stock of the Company shall consist of: (A) 50,000,000 shares of Company Common Stock, of which 34,775,725 shares shall be issued and are outstanding; and (B) 30,000,000 shares of Preferred Stock (x) 1,000,000 of which have been designated "Series A Preferred Stock," none of which shall be issued and outstanding and (y) 29,000,000 of which have been designated "Series B Preferred Stock," none of which shall be issued and outstanding.

2.4 Financial Statements; Financial Controls.

(a) The Company has delivered to Parent the following financial statements and notes (collectively, the "Company Financial Statements"):

(i) The unaudited balance sheets of the Company as of December 31, 2003, and the related unaudited income statements, statements of stockholders' equity and statements of cash flows of the Company for the year then-ended; and

(ii) the unaudited balance sheet and unaudited statements of cashflows of the Company, as of August 31, 2004 (the "Unaudited Interim Balance Sheet"), and the related unaudited income statement of the Company for the eight months then ended.

(b) The Company Financial Statements are accurate and complete in all material respects and present fairly the financial position of the Company as of the respective

dates thereof and the results of operations and (in the case of the financial statements referred to in Section 2.4(a)(i)) cash flows of the Company for the periods covered thereby. The Company Financial Statements have been prepared in accordance with United States generally accepted accounting principles applied on a consistent basis throughout the periods covered (except that the financial statements referred to in Section 2.4(a)(ii) do not contain footnotes and are subject to normal and recurring year-end audit adjustments, which will not, individually or in the aggregate, be material in magnitude).

(c) Part 2.4(c) of the Disclosure Schedule provides an accurate and complete breakdown and aging of all accounts receivable, notes receivable and other receivables of the Company. Except as set forth on Part 2.4(c) of the Disclosure Schedule, all existing accounts receivable of the Company (i) represent valid obligations of customers of the Company arising from bona fide transactions entered into in the ordinary course of business, (ii) are current, and (iii) to the Knowledge of the Company, will be collected in full, without any counterclaim or set off, when due, except to the extent such accounts receivable become uncollectible as a result of an action taken by Parent following the Effective Time.

(d) Part 2.4(d) of the Disclosure Schedule (i) identifies the revenues received from each customer of the Company and from each other Person from whom the Company generated revenues in the fiscal year ended December 31, 2003, and (ii) identifies the revenues received from each customer of the Company and from each other Person from whom the Company generated revenues in the first eight (8) months of 2004. The Company has not received any notice or other communication indicating that any customer or other Person identified on Part 2.4(d) of the Disclosure Schedule intends or expects to cease dealing with the Company or to effect a material reduction in the volume of business transacted by such Person with the Company below historical levels.

(e) Part 2.4(e) of the Disclosure Schedule lists, and the Company has delivered to Parent accurate and complete copies of all documentation creating or governing, any securitization transaction and "off-balance sheet arrangements" (as defined in Item 303(c) of Regulation S-K of the United States Securities and Exchange Commission) effected or maintained in effect by the Company since its inception.

(f) The Company maintains books and records reflecting its assets and liabilities that are accurate and complete in all material respects and maintains adequate internal accounting controls so that: (i) transactions are executed with management's authorization; (ii) transactions are recorded as necessary to permit preparation of the financial statements of the Company and to maintain accountability for the assets of the Company; (iii) access to the assets of the Company is permitted only in accordance with management's authorization; (iv) the reporting of the assets of the Company is compared with existing assets at regular intervals; and (v) accounts, notes and other receivables are recorded accurately.

(g) The Company has not entered into any oral Contract that may be materially inconsistent with the terms of any of its written sales Contracts or related Contracts. Since its inception, the Company has not entered into any barter transaction. No reseller,

distributor or other customer that is not the end-user of a product sold by the Company has any return right, right to price protection or similar right with respect to such product.

(h) Part 2.4(h) of the Disclosure Schedule contains an accurate and complete list of all outstanding loans and advances made by the Company to any Company employee, other than routine travel advances made to current employees in the ordinary course of business.

2.5 Absence of Changes. Except as set forth in Part 2.5 of the Disclosure Schedule, since August 31, 2004:

(a) there has not been any material adverse change in the Company' business, condition, assets, liabilities, operations, financial performance or prospects, and, to the best Knowledge of the Company, no event has occurred that will, or could reasonably be expected to, have a Material Adverse Effect on the Company;

(b) there has not been any material loss, damage or destruction to, or any material interruption in the use of, any of the Company' assets (whether or not covered by insurance);

(c) the Company has not declared, accrued, set aside or paid any dividend or made any other distribution in respect of any shares of capital stock, and has not repurchased, redeemed or otherwise reacquired any shares of its capital stock or other securities;

(d) the Company has not sold, issued or authorized the issuance of (i) any capital stock or other security (except for Company Common Stock issued upon the exercise of outstanding Company Options), (ii) any option or right to acquire any capital stock or any other security (except for Company Options described in Part 2.3 of the Disclosure Schedule) or (iii) any instrument convertible into or exchangeable for any capital stock or other security of the Company;

(e) except as described in Section 1.6 of this Agreement, the Company has not amended or waived any of its rights under, or permitted the acceleration of vesting under, (i) any provision of the Stock Plan, (ii) any provision of any agreement evidencing any outstanding Company Option or Company Warrant, or (iii) any restricted stock purchase agreement;

(f) there has been no amendment to the Company's certificate of incorporation or bylaws, and the Company has not effected or been a party to any Acquisition Transaction, recapitalization, reclassification of shares, stock split, reverse stock split or similar transaction;

(g) the Company has not formed any subsidiary or acquired any equity or other interest in any other Entity;

(h) the Company has not made any capital expenditure that exceeds \$5,000;

(i) the Company has not amended or prematurely terminated, or waived any material right or remedy under, any such Contract that is or would constitute a Material Contract (as defined in Section 2.10(a));

(j) the Company has not (i) acquired, leased or licensed any right or other asset from any other Person, (ii) sold or otherwise disposed of, or leased or licensed, any right or other asset to any other Person or (iii) waived or relinquished any right, except in each case for rights or other assets acquired, leased, licensed or disposed of in the ordinary course of business and consistent with the Company's past practices;

(k) the Company has not written off as uncollectible, or established any extraordinary reserve with respect to, any account receivable or other indebtedness;

(l) the Company has not made any pledge of any of its assets or otherwise permitted any of its assets to become subject to any Encumbrance, except for pledges of immaterial assets made in the ordinary course of business and consistent with the Company's past practices;

(m) the Company has not (i) lent money to any Person or (ii) incurred or guaranteed any indebtedness;

(n) the Company has not (i) established or adopted any Employee Benefit Plan, (ii) paid any bonus or made any profit-sharing or similar payment to, or increased the amount of the wages, salary, commissions, fringe benefits or other compensation or remuneration payable to, any of its directors, officers or employees, or (iii) hired any new employee;

(o) the Company has not changed any of its methods of accounting or accounting practices in any material respect;

(p) the Company has not made any Tax election other than in the ordinary course of business and pursuant to past practices;

(q) the Company has not commenced or settled any Legal Proceeding;

(r) the Company has not entered into any material transaction or taken any other material action outside the ordinary course of business or inconsistent with its past practices; and

(s) the Company has not agreed or committed to take any of the actions referred to in clauses "(c)" through "(r)" above.

2.6 Title to Assets; Equipment.

(a) The Company owns, and has good, valid and marketable title to, all assets purported to be owned by it, including: (i) all assets reflected on the Unaudited Interim Balance Sheet; (ii) all assets referred to in Parts 2.1, 2.7(b) and 2.9 of the Disclosure Schedule and all of

the Company' rights under the Contracts identified in Part 2.10 of the Disclosure Schedule; and (iii) all other assets reflected in the Company's books and records as being owned by the Company. Except as set forth in Part 2.6(a) of the Disclosure Schedule, all of the assets purported to be owned by the Company are owned by the Company free and clear of any liens or other Encumbrances, except for (i) any lien for current Taxes not yet due and payable and (ii) minor liens that have arisen in the ordinary course of business and that do not (in any individual case or in the aggregate) materially detract from the value of the assets subject thereto or materially impair the operations of the Company.

(b) Part 2.6(b) of the Disclosure Schedule identifies all assets that are material to the business of the Company and that are being leased or licensed to the Company.

(c) All material items of equipment and other tangible assets owned by or leased to the Company are reasonably adequate for the uses to which they are being put, are in good condition and repair (ordinary wear and tear excepted) and are reasonably adequate for the conduct of the Company' business in the manner in which such business is currently being conducted and is currently being proposed to be conducted.

2.7 Bank Accounts; Receivables.

(a) Part 2.7(a) of the Disclosure Schedule provides accurate information with respect to each account maintained by or for the benefit of the Company at any bank or other financial institution.

(b) Part 2.7(b) of the Disclosure Schedule provides an accurate and complete breakdown and aging of all accounts receivable, notes receivable and other receivables of the Company as of June 30, 2004. Except as set forth in Part 2.7(b) of the Disclosure Schedule, all existing accounts receivable of the Company (including those accounts receivable reflected on the Unaudited Interim Balance Sheet that have not yet been collected and those accounts receivable that have arisen since June 30, 2004 and have not yet been collected) (i) represent valid obligations of customers of the Company arising from bona fide transactions entered into in the ordinary course of business, and (ii) are current and, to the best Knowledge of the Company, will be collected in full when due, without any counterclaim or set off.

2.8 Title to Real Property. The Company does not own any real property or interests in real property other than leasehold interests in real property. Part 2.8 of the Disclosure Schedule sets forth a complete list of all real property and interests in real property leased by the Company ("**Leased Real Property**"). The Company has good and valid title to the leasehold interests in all Leased Real Property, in each case free and clear of all Encumbrances, except leases, subleases and similar agreements set forth in Part 2.8 of the Disclosure Schedule.

2.9 Intellectual Property

(a) Disclosures

(i) Products and Services. Part 2.9(a)(i) of the Disclosure Schedule accurately identifies and describes each Company Product developed, distributed, licensed,

leased, manufactured, marketed, provided, or sold, directly or indirectly, by or on behalf of the Company at any time since January 1, 2001, and any Company Product currently under development by the Company, whether or not in collaboration with any Person, including an identification of each version thereof, the general release date of each such version, the primary designers and developers of each such version, and any material components of each such version that were not developed by people who were, when they were developing such components, employees of the Company.

(ii) Registered IP. Part 2.9(a)(ii) of the Disclosure Schedule accurately identifies (A) each item of Registered IP in which the Company has or purports to have an ownership interest of any nature (whether exclusively, jointly with another Person, or otherwise); (B) the jurisdiction in which such item of Registered IP has been registered or filed and the applicable registration or serial number; (C) any other Person that has an ownership interest in such item of Registered IP and the nature of such ownership interest; and (D) each component of the Company Products that embodies, utilizes, or is based upon or derived from (or, with respect to Company Products under development, that is expected to embody, utilize, or be based upon or derived from) such item of Registered IP. The Company has provided to Parent complete and accurate copies of all applications, correspondence, and other material documents (including correspondence with the U.S. PTO, U.S. Copyright Office, and similar authorities in other jurisdictions) related to each such item of Registered IP.

(iii) Third Party IP and Inbound Licenses. Part 2.9(a)(iii) of the Disclosure Schedule accurately identifies (A) all Intellectual Property Rights or Intellectual Property licensed to the Company (other than any non-customized software that (1) is so licensed solely in executable or object code form pursuant to a non-exclusive, internal use software license, (2) is not incorporated into, or used directly in the development, manufacturing, or distribution of, the Company Products, and (3) is generally available on standard terms for less than \$1,000); (B) the corresponding Contract or Contracts pursuant to which such Intellectual Property Rights or Intellectual Property is licensed to the Company; and (C) whether the license or licenses granted to the Company are exclusive or non-exclusive.

(iv) Outbound Licenses. Part 2.9(a)(iv) of the Disclosure Schedule accurately identifies each Contract pursuant to which any Person has been granted any license under, or otherwise has received or acquired any right (whether or not currently exercisable) or interest in, the Company IP (other than non-exclusive, internal use, object code software licenses granted to end user customers in the ordinary course of business pursuant to the Company's standard form of end user license agreement).

(v) Standard Form IP Agreements. The Company has provided to Parent a complete and accurate copy of each standard form of Company IP Contract used by the Company at any time since January 1, 2001, including each standard form of (A) end user license agreement; (B) maintenance or support agreement; (C) development agreement; (D) distributor, reseller agreement, sales representative, or referral agreement; (E) application service provider, hosting services, managed services, outsourcing services, or service bureau agreement, (F) employee agreement containing intellectual property assignment or license of Intellectual Property or Intellectual Property Rights or any confidentiality provision; (G) consulting or

independent contractor agreement containing intellectual property assignment or license of Intellectual Property or Intellectual Property Rights or any confidentiality provision; and (H) confidentiality or nondisclosure agreement. Part 2.9(a)(v) of the Disclosure Schedule accurately identifies each Company IP Contract that deviates in any material respect from the corresponding standard form agreement provided to Parent.

(b) Company IP

(i) Ownership Free and Clear. The Company exclusively owns all right, title, and interest to and in the Company IP (other than Intellectual Property Rights exclusively licensed to the Company, as identified in Part 2.9(b)(i) of the Disclosure Schedule) free and clear of any Encumbrances (other than non-exclusive licenses granted pursuant to the Contracts listed in Part 2.9(a)(iv) of the Disclosure Schedule). Without limiting the generality of the foregoing:

(A) Perfection of Rights. All documents and instruments necessary to perfect the rights of the Company in the Company IP have been validly executed, delivered, and filed in a timely manner with the appropriate Governmental Body.

(B) Employees and Contractors. Each Person who is or was an employee or contractor of the Company and who is or was involved in the creation or development of any Company IP has signed a valid, enforceable agreement containing an assignment of Intellectual Property Rights to the Company and confidentiality provisions protecting the Company IP. No current or former shareholder, officer, director, or employee of the Company has any claim, right (whether or not currently exercisable), or interest to or in any Company IP. No employee of the Company is (a) bound by or otherwise subject to any Contract restricting him or her from performing his or her duties for the Company or any of its Subsidiaries or (b) in breach of any Contract with any former employer or other Person concerning Intellectual Property Rights or confidentiality.

(C) Government Rights. No funding, facilities, or personnel of any Governmental Body were used, directly or indirectly, to develop or create, in whole or in part, any Company IP.

(D) Protection of Proprietary Information. The Company has taken all reasonable steps to maintain the confidentiality of and otherwise protect and enforce their rights in all Company Source Code and other proprietary information, that the Company holds, or purports to hold, as a trade secret.

(E) Past IP Dispositions. Since January 1, 2001, the Company has not assigned or otherwise transferred ownership of, or agreed to assign or otherwise transferred ownership of, any Intellectual Property Right to any other Person.

(F) Standards Bodies. The Company is not nor was ever a member or promoter of, or a contributor to, any industry standards body or similar organization that could require or obligate the Company to grant or offer to any other Person any license or right to any Company IP.

(G) Sufficiency. The Company owns or otherwise has, and after the Closing will have, all Intellectual Property Rights needed to conduct its business as currently conducted and planned to be conducted.

(H) Limitations. The Company is not bound by, and no Company IP is subject to, any Contract containing any covenant or other provision that in any way limits or restricts the ability of the Company to use, exploit, assert, or enforce any Company IP anywhere in the world.

(ii) Valid and Enforceable. All Company, all Company IP is valid, subsisting, and enforceable. Without limiting the generality of the foregoing:

(A) Patents. Each U.S. patent application and U.S. patent in which the Company has or purports to have an ownership interest was filed within one year of a printed publication, public use, or offer for sale of each invention described in the U.S. patent application or U.S. patent. Each foreign patent application and foreign patent in which the Company has or purports to have an ownership interest was filed or claims priority to a patent application filed prior to each invention described in the foreign patent application or foreign patent being made available to the public.

(B) Trademarks. No trademark or trade name owned, used, or applied for by the Company conflicts or interferes with any trademark or trade name owned, used, or applied for by any other Person. No event or circumstance (including a failure to exercise adequate quality controls and an assignment in gross without the accompanying goodwill) has occurred or exists that has resulted in, or could reasonably be expected to result in, the abandonment of any trademark (whether registered or unregistered) owned, used, or applied for by the Company.

(C) Legal Requirements and Deadlines. Each item of Company IP that is Registered IP is and at all times has been in compliance with all legal requirements and all filings, payments, and other actions required to be made or taken to maintain such item of Company IP in full force and effect have been made by the applicable deadline. No application for a patent or a copyright, mask work, or trademark registration or any other type of Registered IP filed by or on behalf of the Company has been abandoned, allowed to lapse, or rejected. Part 2.9(b)(ii)(C) of the Disclosure Schedule accurately identifies and describes each action, filing, and payment that must be taken or made on or before the date that is ninety (90) days after the Closing Date in order to maintain such item of Company IP in full force and effect.

(D) Interference Proceedings and Similar Claims. No interference, opposition, reissue, reexamination, or other Legal Proceeding is or since the Company's inception has been pending or, to the best of the Company's Knowledge, threatened, in which the scope, validity, or enforceability of Company IP is being, has been, or could reasonably be expected to be contested or challenged. There is no basis for a claim that any Company IP is invalid or unenforceable.

(iii) Third-Party Infringement of Company IP. No Person has infringed, misappropriated, or otherwise violated, and no Person is currently infringing,

misappropriating, or otherwise violating, any Company IP. Part 2.9(b)(iii) of the Disclosure Schedule accurately identifies (and the Company has provided to Parent a complete and accurate copy of) each letter or other written or electronic communication or correspondence that has been sent or otherwise delivered since the Company's inception by or to the Company or any representative of the Company regarding any actual, alleged, or suspected infringement or misappropriation of any Company IP, and provides a brief description of the current status of the matter referred to in such letter, communication, or correspondence.

(iv) Effects of This Transaction. Neither the execution, delivery, or performance of this Agreement (or any of the ancillary agreements) nor the consummation of any of the transactions contemplated by this Agreement (or any of the ancillary agreements) will, with or without notice or lapse of time, result in, or give any other Person the right or option to cause or declare, (A) a loss of, or Encumbrance on, any Company IP; (B) a breach of any Company IP Contract; (C) the release, disclosure, or delivery of any source code or other Company IP by or to any escrow agent or other Person; (D) the grant, assignment, or transfer to any other Person of any license or other right or interest under, to, or in any of the Company IP; or (E) any limitation or restriction on the ability of Parent, Merger Sub, or the Company to use, exploit, assert, or enforce any Intellectual Property or Intellectual Property Rights owned or exclusively licensed to them anywhere in the world.

(c) Infringement Claims and Liability

(i) No Infringement of Third Party IP Rights. The Company has never infringed (directly, contributorily, by inducement, or otherwise), misappropriated, or otherwise violated any Intellectual Property Right of any other Person.

(ii) Infringing Acts. No product, information, or service ever manufactured, produced, distributed, published, used, provided, or sold by or on behalf of the Company has infringed, misappropriated, or otherwise violated the Intellectual Property Rights of any other Person.

(iii) Infringement Claims. No infringement, misappropriation, or similar claim or Legal Proceeding is pending or, to the best of the Company's Knowledge, threatened against the Company or against any other Person who may be entitled to be indemnified, defended, held harmless, or reimbursed by the Company with respect to such claim or Legal Proceeding. The Company has never received any notice or other communication (in writing or otherwise) relating to any actual, alleged, or suspected infringement, misappropriation, or violation of any Intellectual Property Rights of another Person.

(iv) Other Infringement Liability. Except as set forth in Part 2.9(c)(iv) of the Disclosure Schedule, the Company is not bound by any Contract to indemnify, defend, hold harmless, or reimburse any other Person with respect to any intellectual property infringement, misappropriation, or similar claim. The Company has never assumed, or agreed to discharge or otherwise take responsibility for, any existing or potential liability of another Person for infringement, misappropriation, or violation of any Intellectual Property Right.

(v) Infringement Claims Affecting In-Licensed IP Licensed. To the best of the Company's Knowledge, no claim or Legal Proceeding involving any Intellectual Property or Intellectual Property Right licensed to the Company is pending or has been threatened, except for any such claim or Legal Proceeding that, if adversely determined, would not adversely affect (A) the use or exploitation of such Intellectual Property or Intellectual Property Right by the Company, or (B) the development, distribution, licensing, leasing, manufacturing, marketing, provision, or sale of any Company Product by the Company.

(d) Software; and Services

(i) Bugs. None of the software (including firmware and other software embedded in hardware devices) owned, developed (or currently being developed), used, marketed, distributed, licensed, or sold by the Company (other than non-customized third-party software licensed to the Company for internal use on a non-exclusive basis) (collectively, "Company Software") (a) contains any bug, defect, or error (including any bug, defect, or error relating to or resulting from the display, manipulation, processing, storage, transmission, or use of data data) that materially and adversely affects the use, functionality, or performance of such Company Software or any product or system containing or used in conjunction with such Company Software; or (b) fails (or when sold, licensed, or otherwise made available did fail) to comply with any applicable warranty or other contractual commitment relating to the use, functionality, or performance of such Company Software or any product or system containing or used in conjunction with such Company Software. The Company has provided to Parent a complete and accurate list of all known bugs, defects, and errors in each version and component of the Company Software.

(ii) Harmful Code. No Company Software contains any "back door," "drop dead device," "time bomb," "Trojan horse," "virus," or "worm" (as such terms are commonly understood in the software industry) or any other code designed or intended to have, or capable of performing, any of the following functions: (A) disrupting, disabling, harming, or otherwise impeding in any manner the operation of, or providing unauthorized access to, a computer system or network or other device on which such code is stored or installed; or (B) damaging or destroying any data or file without the user's consent.

(iii) Source Code. No Company Source Code has been delivered, licensed, or made available to any escrow agent or other Person who is not, as of the date of this Agreement, an employee of the Company. Except as set forth in Part 2.9(d)(iii) of the Disclosure Schedule, the Company has no duty or obligation (whether present, contingent, or otherwise) to deliver, license, or make available the Company Source Code to any escrow agent or other Person who is not, as of the date of this Agreement, an employee of the Company. No event has occurred, and no circumstance or condition exists, that (with or without notice or lapse of time) will, or could reasonably be expected to, result in the delivery, license, or disclosure of any Company Source Code to any other Person who is not, as of the date of this Agreement, an employee of the Company.

(iv) Open Source Code. No Company Software is subject to any "copyleft" or other obligation or condition (including any obligation or condition under any

“open source” license such as the GNU Public License, Lesser GNU Public License, or Mozilla Public License) that (a) could require, or could condition the use or distribution of such Company Software on, the disclosure, licensing, or distribution of any Company Source Code, or (b) could otherwise impose any limitation, restriction, or condition on the right or ability of the Company to use or distribute any Company Software.

(v) All installation services, programming services, integration services, repair services, maintenance services, support services, training services, upgrade services and other services that have been performed by the Company were performed properly and in conformity with the terms and requirements of all applicable warranties and other Contracts and with all applicable Legal Requirements.

(vi) Except as set forth in Part 2.9(d)(vi) of the Disclosure Schedule, since January 1, 2001, no customer or other Person has asserted or, to the best Knowledge of the Company, threatened to assert any claim against the Company: (i) under or based upon any warranty provided by or on behalf of any of the Company; or (ii) based upon any services performed by the Company.

2.10 Contracts.

(a) Part 2.10(a) of the Disclosure Schedule identifies:

(i) each Company Contract (A) relating to the employment of, or the performance of services by, any employee, consultant or independent contractor, (B) pursuant to which the Company is or may become obligated to make any severance, termination or similar payment to any Person, or (C) pursuant to which the Company is or may become obligated to make any bonus or similar payment) in excess of \$5,000 to any Person;

(ii) each Company Contract imposing any restriction on the Company’s right or ability (A) to compete with any other Person, (B) to solicit, hire or retain any Person as an employee, consultant or independent contractor, (C) to develop, sell, supply, distribute, offer, support or service any product or technology to or for any other Person or (D) to transact business or deal in any other manner with any other Person;

(iii) each Company Contract creating or involving any agency relationship, distribution arrangement or franchise relationship;

(iv) each Company Contract (other than Company Contracts evidencing Company Options and Company Warrants) relating to the acquisition, issuance or transfer of any securities;

(v) each Company Contract creating or relating to any partnership or joint venture or any sharing of revenues, profits, losses, costs or Liabilities;

(vi) each Company Contract with any Related Party (as defined in Section 2.17);

(vii) each Company Contract with a corporate or similar sponsor;

(viii) each Company Contract relating to the acquisition, transfer, use, development, sharing or license of any Intellectual Property or any Intellectual Property Right;

(ix) each Company Contract relating to the creation of any Encumbrance with respect to any asset of the Company;

(x) each Company Contract relating to the grant of rights to manufacture, produce, assemble, license, market, or sell any of the Company's current or future products to any other Person or otherwise affecting the Company's exclusive right to develop, manufacture, assemble, distribute, market or sell its current or future products;

(xi) each Company Contract relating to indemnification by any of the Company with respect to infringements of Intellectual Property Rights;

(xii) each Company Contract (A) to which any Governmental Body is a party or under which any Governmental Body has any rights or obligations, or (B) directly or indirectly benefiting any Governmental Body;

(xiii) each Company Contract that contemplates or involves (A) the payment or delivery of cash or other consideration in an amount or having a value in excess of \$10,000 in the aggregate or (B) the performance of services having a value in excess of \$5,000 in the aggregate, in each case other than Contracts that have a term of less than 60 days or that may be terminated by the Company (without penalty) within 60 days after the delivery of a termination notice by the Company;

(xiv) each Company Contract that is material to the business of the Company; and

(xv) any Contract relating to the acquisition, sale, spin-off, outsourcing or disposition of any business operation or unit or any product line of the Company, including any right of first offer, right of first refusal or any similar or related right;

(Contracts in the respective categories described in clauses "(i)" through "(xiv)" above are referred to in this Agreement as "**Material Contracts.**")

(b) The Company has delivered to Parent accurate and complete copies of all written Contracts identified in Part 2.10 of the Disclosure Schedule, including all amendments thereto. Part 2.10 of the Disclosure Schedule provides an accurate description of the terms of each Material Contract that is not in written form. Each Contract identified in Part 2.10 of the Disclosure Schedule is valid and in full force and effect and is enforceable by the Company in

accordance with its terms, subject to (i) laws of general application relating to bankruptcy, insolvency and the relief of debtors and (ii) rules of law governing specific performance, injunctive relief and other equitable remedies.

(c) Except as set forth in Part 2.10 of the Disclosure Schedule:

(i) the Company has not violated or breached, or committed any default under, any Material Contract, and, to the best Knowledge of the Knowledge of the Company, no other Person has violated or breached, or committed any default under, any Material Contract;

(ii) no event has occurred, and no circumstance or condition exists, that (with or without notice or lapse of time) will, or could reasonably be expected to, (A) result in a violation or breach of any of the provisions of any Material Contract, (B) give any Person the right to declare a default or exercise any remedy under any Material Contract, (C) give any Person the right to accelerate the maturity or performance of any Material Contract or (D) give any Person the right to cancel, terminate or modify any Material Contract;

(iii) the Company has not received any notice or other communication regarding any actual or possible violation or breach of, or default under, any Material Contract and the Company is not aware of any basis therefore; and

(iv) the Company has not waived any of its material rights under any Material Contract.

(d) No Person is renegotiating, or has a right pursuant to the terms of any Company Contract to renegotiate, any amount paid or payable to the Company under any Material Contract or any other material term or provision of any Material Contract.

(e) The Contracts identified in Part 2.10 of the Disclosure Schedule collectively constitute all of the Contracts necessary to enable the Company to conduct its business in the manner in which its business is currently being conducted.

2.11 Liabilities.

(a) The Company has no accrued, contingent or other liabilities of any nature, either matured or unmatured (whether or not required to be reflected in financial statements in accordance with generally accepted accounting principles, and whether due or to become due), except for: (i) liabilities identified as such in the "liabilities" column of the Unaudited Interim Balance Sheet; and (ii) the liabilities identified on Part 2.11(a) of the Disclosure Schedule, in excess of \$5,000 in the aggregate.

(b) Part 2.11(b) of the Disclosure Schedule provides an accurate and complete breakdown and aging of (i) all accounts payable of the Company, and (ii) all notes payable of the Company and all indebtedness of the Company for borrowed money.

(c) No event has occurred, and no circumstance or condition exists, that has resulted in, or that will or would reasonably be expected to result in, any claim for indemnification or reimbursement by any Company employee pursuant to (i) the terms of the Company's certificate of incorporation or bylaws, (ii) any indemnification agreement or other Contract between the Company and any such Company employee, or (iii) any applicable Legal Requirement.

2.12 Compliance with Legal Requirements. The Company is, and has at all times been, in compliance in all material respects with all applicable Legal Requirements. Except as set forth in Part 2.12 of the Disclosure Schedule, the Company has not received any notice or other communication from any Governmental Body regarding any actual or possible violation of, or failure to comply with, any Legal Requirement.

2.13 Governmental Authorizations. Part 2.13 of the Disclosure Schedule identifies each material Governmental Authorization held by the Company as of the date of this Agreement. The Company has delivered to Parent accurate and complete copies of all Governmental Authorizations identified in Part 2.13 of the Disclosure Schedule. The Governmental Authorizations identified in Part 2.13 of the Disclosure Schedule are valid and in full force and effect, and collectively constitute all Governmental Authorizations necessary to enable the Company to conduct its business in the manner in which its business is currently being conducted and is currently proposed to be conducted. The Company is, and at all times has been, in compliance in all material respects with the terms and requirements of the respective Governmental Authorizations identified in Part 2.13 of the Disclosure Schedule. The Company has not received any notice or other communication from any Governmental Body regarding (a) any actual or possible violation of or failure to comply with any term or requirement of any Governmental Authorization or (b) any actual or possible revocation, withdrawal, suspension, cancellation, termination or modification of any Governmental Authorization.

2.14 Tax Matters.

(a) Each of the Tax Returns required to be filed by or on behalf of the Company with any Governmental Body with respect to any taxable period ending on or before the Closing Date (the "**Company Returns**") (i) has been or will be filed on or before the applicable due date (including any extensions of such due date), and (ii) has been, or will be when filed, prepared in all material respects in compliance with all applicable Legal Requirements. All amounts shown on the Company Returns to be due on or before the Closing Date have been or will be paid on or before the Closing Date. The Company has delivered to Parent accurate and complete copies of all Company Returns filed by the Company.

(b) The Unaudited Interim Balance Sheet accrues all actual and contingent liabilities for Taxes with respect to all periods through June 30, 2004 in accordance with generally accepted accounting principles. The Company will establish, in the ordinary course of business and consistent with its past practices, reserves adequate for the payment of all Taxes for the period from June 30, 2004 through the Closing Date.

(c) No Company Return has ever been examined or audited by any Governmental Body. No extension or waiver of the limitation period applicable to any of the

Company Returns has been granted (by the Company or any other Person), and no such extension or waiver has been requested from the Company.

(d) No claim or Legal Proceeding is pending or has been threatened against or with respect to the Company in respect of any material Tax. There are no unsatisfied liabilities for material Taxes with respect to any notice of deficiency or similar document received by the Company with respect to any material Tax (other than liabilities for Taxes asserted under any such notice of deficiency or similar document which are being contested in good faith by the Company and with respect to which adequate reserves for payment have been established on the Unaudited Interim Balance Sheet). There are no liens for material Taxes upon any of the assets of the Company except liens for current Taxes not yet due and payable. The Company has not been, and will not be, required to include any adjustment in taxable income for any tax period (or portion thereof) pursuant to Section 481 or 263A of the Code (or any comparable provision of state or foreign Tax laws) as a result of transactions or events occurring, or accounting methods employed, prior to the Closing. The Company has not made any distribution of stock of any controlled corporation, as that term is defined in Code Section 355(a)(1).

(e) There is no agreement, plan, arrangement or other Contract covering any employee or independent contractor or former employee or independent contractor of the Company that, considered individually or considered collectively with any other such Contracts, will, or could reasonably be expected to, give rise directly or indirectly to the payment of any amount that would not be deductible pursuant to Section 280G or Section 162 of the Code (or any comparable provision under state or foreign Tax laws). The Company is not, and has never been, a party to or bound by any tax indemnity agreement, tax sharing agreement, tax allocation agreement or similar Contract.

2.15 Employee and Labor Matters; Benefit Plans.

(a) Part 2.15(a) of the Disclosure Schedule identifies each salary, bonus, vacation, deferred compensation, incentive compensation, stock purchase, stock option, severance pay, termination pay, death and disability benefits, hospitalization, medical, life or other insurance, flexible benefits, supplemental unemployment benefits, profit-sharing, pension or retirement plan, program or agreement and each other employee benefit plan or arrangement (collectively, the “**Employee Plans**”) sponsored, maintained, contributed to or required to be contributed to by the Company for the benefit of any current or former employee of the Company.

(b) Except as set forth in Part 2.15(a) of the Disclosure Schedule, the Company does not maintain, sponsor or contribute to, and the Company has not at any time in the past maintained, sponsored or contributed to, any employee pension benefit plan (as defined in Section 3(2) of the Employee Retirement Income Security Act of 1974, as amended (“**ERISA**”), or any similar pension benefit plan under the laws of any foreign jurisdiction, whether or not excluded from coverage under specific Titles or Subtitles of ERISA for the benefit of employees or former employees of the Company (a “**Pension Plan**”).

(c) Except as set forth in Part 2.15(a) of the Disclosure Schedule, the Company does not maintain, sponsor or contribute to any employee welfare benefit plan (as

defined in Section 3(1) of ERISA or any similar welfare benefit plan under the laws of any foreign jurisdiction, whether or not excluded from coverage under specific Titles or Subtitles of ERISA), for the benefit of any current or former employees or directors of the Company (a “**Welfare Plan**”).

(d) With respect to each Employee Plan, the Company has delivered to Parent: (i) an accurate and complete copy of such Employee Plan (including all amendments thereto); (ii) an accurate and complete copy of the annual report, if required under ERISA, with respect to such Employee Plan for the last two years; (iii) an accurate and complete copy of the most recent summary plan description, together with each summary of material modifications, if required under ERISA, with respect to such Employee Plan, (iv) if such Employee Plan is funded through a trust or any third party funding vehicle, an accurate and complete copy of the trust or other funding agreement (including all amendments thereto) and accurate and complete copies the most recent financial statements thereof; (v) accurate and complete copies of all Contracts relating to such Employee Plan, including service provider agreements, insurance contracts, minimum premium contracts, stop-loss agreements, investment management agreements, subscription and participation agreements and recordkeeping agreements; and (vi) an accurate and complete copy of the most recent determination letter received from the Internal Revenue Service with respect to such Employee Plan (if such Employee Plan is intended to be qualified under Section 401(a) of the Code).

(e) The Company neither is or has ever been required to be treated as a single employer with any other Person under Section 4001(b)(1) of ERISA or Section 414(b), (c), (m) or (o) of the Code. The Company has never been a member of an “affiliated service group” within the meaning of Section 414(m) of the Code. None of the Employee Plans identified in the Disclosure Schedule is a multiemployer plan (within the meaning of Section 3(37) of ERISA). The Company has never made a complete or partial withdrawal from a multiemployer plan, as such term is defined in Section 3(37) of ERISA, resulting in “withdrawal liability,” as such term is defined in Section 4201 of ERISA (without regard to subsequent reduction or waiver of such liability under either Section 4207 or 4208 of ERISA).

(f) The Company has no plan or commitment to create any Welfare Plan or any Pension Plan, or to modify or change any existing Welfare Plan or Pension Plan (other than to comply with applicable law) in a manner that would affect any current or former employee or director of the Company.

(g) No Employee Plan provides death, medical or health benefits (whether or not insured) with respect to any current or former employee or director of the Company after any termination of service of such employee or director (other than benefit coverage mandated by applicable law, including coverage provided pursuant to Section 4980B of the Code).

(h) With respect to any Employee Plan constituting a group health plan within the meaning of Section 4980B(g)(2) of the Code, the provisions of Section 4980B of the Code (“**COBRA**”) have been complied with in all material respects. Part 2.15(h) of the Disclosure Schedule describes all obligations of the Company as of the date of this Agreement under any of the provisions of COBRA.

(i) Each of the Employee Plans has been operated and administered in all material respects in accordance with its terms and with applicable Legal Requirements, including ERISA, the Code and applicable foreign Legal Requirements. The Company has performed all of its obligations under the Employee Plans.

(j) Each of the Employee Plans intended to be qualified under Section 401(a) of the Code has received a favorable determination letter from the Internal Revenue Service, and nothing has occurred that would adversely affect such determination.

(k) Except as may be set forth in Part 2.15 (k) of the Disclosure Schedule, neither the execution, delivery or performance of this Agreement, nor the consummation of the Merger or any of the other transactions contemplated by this Agreement, will result in any bonus, golden parachute, severance or other payment or obligation to any current or former employee or director of the Company (whether or not under any Employee Plan), or materially increase the benefits payable or provided under any Employee Plan, or, except as contemplated by Section 1.6 of this Agreement, result in any acceleration of the time of payment or vesting of any such benefits. Without limiting the generality of the foregoing (and except as set forth in Part 2.15(k) of the Disclosure Schedule), the consummation of the Merger will not result in the acceleration of vesting of any unvested Company Options.

(l) Part 2.15 (l) of the Disclosure Schedule contains a list of all employees of the Company as of the date of this Agreement, and correctly reflects, in all material respects, their salaries or hourly compensation, any other compensation payable to them (including compensation payable pursuant to bonus, deferred compensation or commission arrangements), their dates of employment and their positions. The Company is not a party to any collective bargaining contract or other Contract with a labor union involving any of its employees. All of the employees of the Company are "at will" employees.

(m) Part 2.15(m) of the Disclosure Schedule identifies each employee of the Company who is not fully available to perform work because of disability or other leave and sets forth the basis of such disability or leave and the anticipated date of return to full service.

(n) The Company is in compliance in all material respects with all applicable Legal Requirements and Contracts relating to employment, employment practices, wages, bonuses and terms and conditions of employment, including employee compensation matters.

(o) The Company has good labor relations, and the Company has no Knowledge of any facts indicating that (i) the consummation of the Merger or any of the other transactions contemplated by this Agreement will have a material adverse effect on the labor relations of the Company, or (ii) any of the employees of the Company intends to terminate his or her employment with the Company.

2.16 Insurance. Part 2.16 of the Disclosure Schedule identifies all insurance policies maintained by, at the expense of or for the benefit of the Company, identifies any material claims made thereunder, and includes a summary of the amounts and types of coverage and the deductibles under each such insurance policy. Each of the insurance policies identified in Part 2.16 of the Disclosure Schedule is in full force and effect. The Company has not received any

notice or other communication regarding any actual or possible (a) cancellation or invalidation of any insurance policy, (b) refusal of any coverage or rejection of any claim under any insurance policy or (c) material adjustment in the amount of the premiums payable with respect to any insurance policy.

2.17 Related Party Transactions. Except as set forth in Part 2.17 of the Disclosure Schedule: (a) no Related Party has, and no Related Party has at any time had, any direct or indirect interest in any material asset used in or otherwise relating to the business of the Company; (b) no Related Party is, or has at any time been, indebted to the Company; (c) no Related Party has entered into, or has had any direct or indirect financial interest in, any material Contract, transaction or business dealing involving the Company; (d) no Related Party is competing, or has at any time competed, directly or indirectly, with the Company; and (e) no Related Party has any claim or right against the Company (other than rights to receive compensation for services performed as an employee of the Company). (For purposes of this Section 2.18 each of the following shall be deemed to be a “**Related Party**”: (i) each of the stockholders of the Company; (ii) each individual who is, or who has at any time been, an officer of the Company; (iii) each member of the immediate family of each of the individuals referred to in clauses “(i)” and “(ii)” above; and (iv) any trust or other Entity (other than the Company) in which any one of the individuals referred to in clauses “(i),” “(ii)” and “(iii)” above holds (or in which more than one of such individuals collectively hold), beneficially or otherwise, a material voting, proprietary or equity interest.)

2.18 Legal Proceedings; Orders.

(a) Except as set forth in Part 2.18(a) of the Disclosure Schedule, there is no pending Legal Proceeding, and to the Knowledge of the Company, no Person has threatened to commence any Legal Proceeding: (i) that involves the Company or any of the assets owned or used by the Company; (ii) that involves any Person whose liability the Company has or may have retained or assumed, either contractually or by operation of law; or (iii) that challenges, or that may have the effect of preventing, delaying, making illegal or otherwise interfering with, the Merger or any of the other transactions contemplated by this Agreement. Except as set forth in Part 2.18(a) of the Disclosure Schedule, to the Knowledge of the Company, no event has occurred, and no claim, dispute or other condition or circumstance exists, that will, or that could reasonably be expected to, give rise to or serve as a basis for the commencement of any such Legal Proceeding.

(b) Except as set forth in Part 2.18(b) of the Disclosure Schedule, no Legal Proceeding has ever been commenced by or has ever been pending against the Company.

(c) There is no order, writ, injunction, judgment or decree to which the Company, or any of the assets owned or used by the Company, is subject. To the Knowledge of the Company, none of the stockholders of the Company is subject to any order, writ, injunction, judgment or decree that relates to the business of the Company or to any of the assets owned or used by the Company.

2.19 Authority; Binding Nature of Agreement. Subject to obtaining the Required Vote, the Company has the absolute and unrestricted right, power and authority to enter into and

to perform its obligations under this Agreement; and the execution, delivery and performance by the Company of this Agreement have been duly authorized by all necessary action on the part of the Company and its board of directors. This Agreement constitutes the legal, valid and binding obligation of the Company, enforceable against the Company in accordance with its terms, subject to (a) laws of general application relating to bankruptcy, insolvency and the relief of debtors, and (b) rules of law governing specific performance, injunctive relief and other equitable remedies.

2.20 Non-Contravention; Consents. Except as set forth in Part 2.20 of the Disclosure Schedule, neither (1) the execution, delivery or performance of this Agreement or any of the other agreements referred to in this Agreement, nor (2) the consummation of the Merger or any of the other transactions contemplated by this Agreement, will directly or indirectly (with or without notice or lapse of time):

(a) contravene, conflict with or result in a violation of (i) any of the provisions of the Company's certificate of incorporation or bylaws, or (ii) any resolution adopted by the Company's stockholders, the Company's board of directors or any committee of the Company's board of directors;

(b) contravene, conflict with or result in a violation of, or give any Governmental Body or other Person the right to challenge any of the transactions contemplated by this Agreement or to exercise any remedy or obtain any relief under, any Legal Requirement or any order, writ, injunction, judgment or decree to which the Company, or any of the assets owned or used by the Company, is subject;

(c) contravene, conflict with or result in a violation of any of the terms or requirements of, or give any Governmental Body the right to revoke, withdraw, suspend, cancel, terminate or modify, any Governmental Authorization that is held by the Company or that otherwise relates to the Company's business or to any of the assets owned or used by the Company;

(d) contravene, conflict with or result in a violation or breach of, or result in a default under, any provision of any Company Contract that is or would constitute a Material Contract, or give any Person the right to (i) declare a default or exercise any remedy under any such Company Contract, (ii) accelerate the maturity or performance of any such Company Contract, or (iii) cancel, terminate or modify any such Company Contract; or

(e) result in the imposition or creation of any lien or other Encumbrance upon or with respect to any asset owned or used by the Company (except for minor liens that will not, in any case or in the aggregate, materially detract from the value of the assets subject thereto or materially impair the operations of the Company).

Except as set forth in Part 2.20 of the Disclosure Schedule, the Company is not and will not be required to make any filing with or give any notice to, or to obtain any Consent from, any Person in connection with (x) the execution, delivery or performance of this Agreement or any of the other agreements referred to in this Agreement, or (y) the consummation of the Merger or any of the other transactions contemplated by this Agreement.

2.21 Full Disclosure.

(a) This Agreement (when taken together with the Disclosure Schedule) does not, and the Closing Certificate will not, (i) contain any representation, warranty or information that is false or misleading with respect to any material fact, or (ii) omit to state any material fact necessary in order to make the representations, warranties and information contained and to be contained herein and therein (in the light of the circumstances under which such representations, warranties and information were or will be made or provided) not false or misleading.

(b) The information supplied by the Company for inclusion in the Information Statement (as defined in Section 5.2) will not, as of the date of the Information Statement or as of the date of the Company Stockholders' Meeting (as defined in Section 5.2), (i) contain any statement that is inaccurate or misleading with respect to any material fact, or (ii) omit to state any material fact necessary in order to make such information (in the light of the circumstances under which it is provided) not false or misleading.

2.22 Vote Required. The affirmative vote of the holders of a majority of the outstanding shares of Company Common Stock, voting as a single class, a majority of the outstanding shares of Series A Preferred Stock, voting as a single class and a majority of the outstanding shares of Series B Preferred Stock, voting as a single class (the "**Required Vote**"), is the only vote of the holders of any class or series of the Company Capital Stock necessary to adopt this Agreement.

2.23 No Brokers. Except for Sequoia Partners, which will be entitled only to the amount set forth in Schedule I, no broker, finder or investment banker is entitled to any brokerage, finder's or other fee or commission in connection with the transactions contemplated by this Agreement based on arrangements made by or on behalf of the Company.

2.24 Certain Business Practices. Neither the Company, nor, to the Knowledge of the Company, any Representative of the Company or Company employee, has (i) used any funds for unlawful contributions, gifts, entertainment or other unlawful expenses relating to political activity, (ii) made any unlawful payment to foreign or domestic government officials or employees or to foreign or domestic political parties or campaigns, violated any provision of the Foreign Corrupt Practices Act of 1977, as amended, or (iii) taken any action that would constitute a violation of the Foreign Corrupt Practices Act of 1977, as amended, if the Company were publicly held.

2.25 No Discussions. The Company nor any Representative of the Company is engaged, directly or indirectly, in any discussions or negotiations with any other Person relating to any Acquisition Proposal.

SECTION 3. Representations and Warranties of Parent and Merger Sub

Parent and Merger Sub jointly and severally represent and warrant to the Company as follows:

3.1 Due Organization; Corporate Power. Each of the Parent and the Merger Sub is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware. Parent has all requisite corporate power and authority to carry on the businesses in which it is engaged and to own and use the properties owned and used by it.

3.2 Authority; Binding Nature of Agreement. Parent and Merger Sub have the absolute and unrestricted right, power and authority to perform their obligations under this Agreement; and the execution, delivery and performance by Parent and Merger Sub of this Agreement have been duly authorized by all necessary corporate action on the part of Parent and Merger Sub and their respective boards of directors. No vote of Parent's stockholders is needed to adopt this Agreement. This Agreement constitutes the legal, valid and binding obligation of Parent and Merger Sub, enforceable against them in accordance with its terms, subject to (a) laws of general application relating to bankruptcy, insolvency and the relief of debtors, and (b) rules of law governing specific performance, injunctive relief and other equitable remedies.

3.3 No Brokers. No broker, finder or investment banker is entitled to any brokerage, finder's or other fee or commission in connection with the transactions contemplated by this Agreement based on arrangements made by or on behalf of Parent.

SECTION 4. Certain Covenants of the Company

4.1 Access and Investigation. During the period from the date of this Agreement through the Effective Time (the "**Pre-Closing Period**"), the Company shall, and shall cause its Representatives to: (a) provide Parent and Parent's Representatives with reasonable access to the Company's Representatives, personnel and assets and to all existing books, records, Tax Returns, work papers and other documents and information relating to the Company; and (b) provide Parent and Parent's Representatives with copies of such existing books, records, Tax Returns, work papers and other documents and information relating to the Company, and with such additional financial, operating and other data and information regarding the Company, as Parent may reasonably request.

4.2 Operation of the Company's Business. During the Pre-Closing Period:

(a) the Company shall conduct its business and operations in the ordinary course and in substantially the same manner as such business and operations have been conducted prior to the date of this Agreement;

(b) the Company shall use its best efforts to preserve intact its current business organization, keep available the services of its current officers and employees and maintain its relations and goodwill with all suppliers, customers, landlords, creditors, licenses, employees and other Persons having business relationships with the Company;

(c) the Company shall keep in full force all insurance policies identified in Part 2.16 of the Disclosure Schedule;

(d) the Company shall not sell, issue or authorize the issuance of (i) any capital stock or other security, (ii) any option or right to acquire any capital stock or other

security or (iii) any instrument convertible into or exchangeable for any capital stock or other security (except that the Company shall be permitted (A) to issue Company Common Stock to employees upon the exercise of outstanding Company Options, (B) to issue shares of Company Common Stock upon the conversion of shares of Series A Preferred Stock or Series B Preferred Stock or (C) to issue shares of Company Capital Stock upon the exercise of Company Warrants);

(e) the Company shall not declare, accrue, set aside or pay any dividend or make any other distribution in respect of any shares of capital stock, and shall not repurchase, redeem or otherwise reacquire any shares of capital stock or other securities (except that the Company may repurchase Company Capital Stock from former employees pursuant to existing restricted stock purchase agreements);

(f) except to the extent contemplated by Section 1.6 of this Agreement, the Company shall not amend or waive any of its rights under, (i) any provision of the Stock Plan, (ii) any provision of any agreement evidencing any outstanding Company Option or Company Warrant, or (iii) any provision of any restricted stock purchase agreement, (except that the Company may modify the vesting schedules of outstanding Company Options and may modify the terms of repurchase rights of the Company to the extent that such modifications would not alter the Merger Consideration);

(g) the Company shall not amend or permit the adoption of any amendment to the certificate of incorporation or bylaws of the Company, or effect or permit the Company to become a party to any Acquisition Transaction, recapitalization, reclassification of shares, stock split, reverse stock split or similar transaction;

(h) the Company shall not form any subsidiary or acquire any equity interest or other interest in any other Entity;

(i) the Company shall not make any capital expenditure;

(j) the Company shall not (i) enter into, or permit any of the assets owned or used by it to become bound by, any Contract that is or would constitute a Material Contract or (ii) amend or prematurely terminate, or waive any material right or remedy under, any such Material Contract;

(k) the Company shall not (i) acquire, lease or license any right or other asset from any other Person or sell or otherwise dispose of, or lease or license, any right or other asset to any other Person or (ii) waive or relinquish any material right;

(l) the Company shall not (i) lend money to any Person or (ii) incur or guarantee any indebtedness;

(m) the Company shall not (i) establish, adopt or amend any Employee Plan or (ii) pay any bonus or make any profit-sharing payment, cash incentive payment or similar payment to, or increase the amount of the wages, salary, commissions, fringe benefits or other compensation or remuneration payable to, any of its directors, officers or employees, in a manner that is inconsistent with its past business practices;

- (n) the Company shall not change any of its methods of accounting or accounting practices;
- (o) the Company shall not make any Tax election except in the ordinary course of business and pursuant to past practices;
- (p) the Company shall not commence or settle any Legal Proceeding; and
- (q) the Company shall not agree or commit to take any of the actions described in clauses "(d)" through "(p)" above.

4.3 Notification; Updates to Disclosure Schedule.

(a) During the Pre-Closing Period, the Company shall promptly notify Parent in writing of: (i) the discovery by the Company of any event, condition, fact or circumstance that occurred or existed on or prior to the date of this Agreement and that caused or constitutes an inaccuracy in or a breach of any representation or warranty made by the Company in this Agreement; (ii) any event, condition, fact or circumstance that occurs, arises or exists after the date of this Agreement and that would cause or constitute an inaccuracy in or a breach of any representation or warranty made by the Company in this Agreement if (A) such representation or warranty had been made as of the time of the occurrence, existence or discovery of such event, condition, fact or circumstance or (B) such event, condition, fact or circumstance had occurred, arisen or existed on or prior to the date of this Agreement; (iii) any breach of any covenant or obligation of the Company; and (iv) any event, condition, fact or circumstance that would make the timely satisfaction of any of the conditions set forth in Section 6 or Section 7 impossible or unlikely.

(b) If any event, condition, fact or circumstance that is required to be disclosed pursuant to Section 4.3(a) requires any change in the Disclosure Schedule, or if any such event, condition, fact or circumstance would require such a change assuming the Disclosure Schedule were dated as of the date of the occurrence, existence or discovery of such event, condition, fact or circumstance, then the Company shall promptly deliver to Parent an update to the Disclosure Schedule specifying such change. No such update shall be deemed to supplement or amend the Disclosure Schedule for the purpose of (i) determining the accuracy of any of the representations and warranties made by the Company in this Agreement or (ii) determining whether any of the conditions set forth in Section 6 has been satisfied.

4.4 No Negotiation. During the Pre-Closing Period, the Company shall not, directly or indirectly:

- (a) solicit or encourage the submission of any expression of interest, proposal, plan or offer from, or provide any non-public information to, any Person (other than Parent) relating to a possible Acquisition Transaction;
- (b) engage in any discussions or negotiations or enter into any agreement, understanding or arrangement with any Person (other than Parent) relating to, or in connection with, a possible Acquisition Transaction; or

(c) consider, entertain or accept any proposal or offer from any Person (other than Parent) relating to a possible Acquisition Transaction;

(d) permit any Representative of the Company or any stockholder of the Company to do any of the foregoing.

The Company shall, and shall cause each of its Representatives to, immediately discontinue any ongoing discussions or negotiations (other than any ongoing discussions with Parent) relating to a possible Acquisition Transaction. The Company shall promptly provide Parent with an oral and a written description of any expression of interest, inquiry, proposal or offer relating to a possible Acquisition Transaction that is received by the Company or any of its Representatives or stockholders during the Pre-Closing Period.

4.5 Conversion of Preferred Stock. The Company shall obtain the consent of the holders of Company Preferred Stock to convert all of the Company Preferred Stock into shares of Company Common Stock pursuant to the terms of the Company's Amended and Restated Certificate of Incorporation, such conversion to be effective immediately prior to the Effective Time.

SECTION 5. Additional Covenants of the Parties

5.1 Filings and Consents. As promptly as practicable after the execution of this Agreement, (a) each party to this Agreement shall make all filings (if any) and give all notices (if any) required to be made and given by such party in connection with the Merger and the other transactions contemplated by this Agreement, and (b) the Company shall use all commercially reasonable efforts to obtain all Consents (if any) required to be obtained (pursuant to any applicable Legal Requirement or Contract, or otherwise) by the Company in connection with the Merger and the other transactions contemplated by this Agreement. The Company shall (upon request) promptly deliver to Parent a copy of each such filing made, each such notice given and each such Consent obtained by the Company during the Pre-Closing Period.

5.2 Company Stockholders' Meeting; Written Consents; Delivery of Certificates.

(a) As promptly as practicable after the execution of this Agreement, the Company shall prepare an Information Statement relating to the adoption of this Agreement by the Company's stockholders (the "**Information Statement**"). The Company shall, in accordance with its certificate of incorporation and bylaws and the applicable requirements of the DGCL, call and hold a special meeting of its stockholders as promptly as practicable for the purpose of permitting them to consider and to vote upon and adopt this Agreement (the "**Company Stockholders' Meeting**"). In lieu of calling and holding the Company Stockholders' Meeting, the Company may solicit written consents of the stockholders of the Company in accordance with the applicable requirements of the DGCL for the purpose of permitting the stockholders of the Company to vote upon and adopt this Agreement. The Company shall cause a copy of the Information Statement to be delivered to each stockholder of the Company who is entitled to vote at the Company Stockholders' Meeting or to act by written consent. As promptly as practicable after the delivery of copies of the Information Statement to all stockholders entitled to vote at the Company Stockholders' Meeting or to act by written

consent, the Company shall use its best efforts to solicit from each such stockholder a proxy or written consent (in the event the Company has elected to solicit written consents in lieu of a meeting) in favor of the adoption of this Agreement.

(b) The board of directors of the Company shall unanimously recommend that the Company's stockholders vote in favor of and adopt this Agreement at the Company Stockholders' Meeting or by written consent; (ii) the Information Statement shall include a statement to the effect that the board of directors of the Company has unanimously recommended that the Company's stockholders vote in favor of and adopt this Agreement at the Company Stockholders' Meeting or by written consent; and (iii) neither the board of directors of the Company nor any committee thereof shall withdraw, amend or modify, or propose or resolve to withdraw, amend or modify, in a manner adverse to Parent, the unanimous recommendation of the board of directors of the Company that the Company's stockholders vote in favor of and adopt this Agreement. For purposes of this Agreement, said recommendation of the board of directors of the Company shall be deemed to have been modified in a manner adverse to Parent if said recommendation shall no longer be unanimous.

(c) The Company shall use its best efforts to cause each Company Stockholder to surrender to Parent at the Closing all certificates representing Company Capital Stock (properly endorsed for transfer) together with an accurately and fully completed letter of transmittal in a form to be provided to each Company Stockholder by Parent.

5.3 Public Announcements. During the Pre-Closing Period, the Company shall not (nor shall it permit any of its Representatives to) issue any press release or make any public statement regarding this Agreement or the Merger, or regarding any of the other transactions contemplated by this Agreement (other than to stockholders or Representatives of the Company), without the Parent's prior written consent.

5.4 Reasonable Efforts. During the Pre-Closing Period, (a) the Company shall use its reasonable efforts to cause the conditions set forth in Section 6 to be satisfied on a timely basis, and (b) Parent and Merger Sub shall use their reasonable efforts to cause the conditions set forth in Section 7 to be satisfied on a timely basis.

5.5 Termination of Agreements. Prior to the Closing, the Company shall use commercially reasonable efforts to cause the following agreements to be terminated:

- (a) All agreements under which Douglas Neal is entitled to receive royalty or similar payments relating to the Company's products or service offerings;
- (b) The Company's 1998 Stock Option/Stock Issuance Plan;
- (c) Workers Compensation and Employers Liability Insurance from Great American Insurance Company of New York;
- (d) Commercial Automobile Insurance Policy from Chubb Group of Insurance Companies — Federal Insurance Company;

(e) Commercial Excess and Umbrella Insurance Policy from Chubb Group of Insurance Companies - Federal Insurance Company; and

(f) Customary Classic Insurance Program from Chubb Group of Insurance Companies — Federal Insurance Company, for Property, Liability, Crime and Common Policy.

5.6 FIRPTA Matters. At the Closing, (a) the Company shall deliver to Parent a statement (in such form as may be reasonably requested by counsel to Parent) conforming to the requirements of Section 1.897 — 2(h)(1)(i) of the United States Treasury Regulations, and (b) the Company shall deliver to the Internal Revenue Service the notification required under Section 1.897 — 2(h)(2) of the United States Treasury Regulations.

5.7 Termination of Employment; Termination of Employee Plans. Prior to the Closing, the Company shall terminate the employment of all employees of the Company other than the Retained Employees. At the Closing, the Company shall have obtained the necessary consents and approvals to terminate its 401(k) plan, and shall terminate its stock option plans and other incentive plans, and shall ensure that no employee or former employee of the Company has any rights under any of such Plans and that any liabilities of the Company under such Plans (including any such liabilities relating to services performed prior to the Closing) are, or will be, fully extinguished at no cost to the Company.

5.8 Continuing Indemnification of Directors & Officers. The indemnification provisions contained in the Certificate of Incorporation or bylaws of the Surviving Corporation shall not substantially reduce or impair the rights to indemnification now existing in the Certificate of Incorporation or bylaws of the Company for the officers and directors of the Company as of the date of this Agreement for acts or omissions of such individuals occurring prior to the Effective Time, except to the extent such changes may reasonably be determined by the Surviving Corporation to be required to conform with changes in applicable law and any changes which do not adversely affect the application of such provisions to acts or omissions of such individuals prior to the Closing.

SECTION 6. Conditions Precedent to Obligations of Parent and Merger Sub

The obligations of Parent and Merger Sub to effect the Merger and otherwise consummate the transactions contemplated by this Agreement are subject to the satisfaction, at or prior to the Closing, of each of the following conditions:

6.1 Accuracy of Representations. Each of the representations and warranties made by the Company in this Agreement and in each of the other agreements and instruments delivered to Parent in connection with the transactions contemplated by this Agreement shall have been accurate in all material respects as of the date of this Agreement (without giving effect to any “Material Adverse Effect” or other materiality qualifications, or any similar qualifications, contained or incorporated directly or indirectly in such representations and warranties), and shall be accurate in all material respects as of the Closing Date as if made on the Closing Date (without giving effect to any “Material Adverse Effect” or other materiality qualifications, or any similar qualifications, contained or incorporated directly or indirectly in such representations and warranties).

6.2 Performance of Covenants. All of the covenants and obligations that the Company is required to comply with or to perform at or prior to the Closing shall have been complied with and performed in all material respects.

6.3 Stockholder Approval. This Agreement shall have been duly adopted by the Required Vote. On or prior to the date which is five (5) business days following the date of this Agreement, the Company shall have delivered written consents by such holders of the Company's capital stock as is required to approve the Merger under the provisions of applicable law.

6.4 Board Approval. This Agreement and all related agreements and transactions shall have been duly adopted by the Board of Directors of the Company and Parent.

6.5 Consents. All Consents required to be obtained in connection with the Merger and the other transactions contemplated by this Agreement (including the Consents identified in Part 2.20 of the Disclosure Schedule) shall have been obtained and shall be in full force and effect.

6.6 Employees. Parent shall have executed offer letters in the form set forth on **Exhibit C-1**, and proprietary information and inventions agreements in the form set forth on **Exhibit B** with the employees of the Company identified on **Exhibit C-2**.

6.7 Assignment of Intellectual Property Rights. Doug Neal shall have terminated all royalty rights and assigned all Intellectual Property Rights to the Company relating to the Company IP.

6.8 Agreements and Documents. Parent and the Company shall have received the following agreements and documents, each of which shall be in full force and effect:

(a) Stock Option Cancellation Agreements, executed by each of the Converted Option Holders;

(b) a Release in the form of **Exhibit E-1**, executed by each of the individuals identified on **Exhibit C-2**;

(c) legal opinion of Stradling Yocca Carlson & Rauth, the Company's legal counsel, (reasonably satisfactory to Parent) in the United States, dated as of the Closing Date, in the form of **Exhibit F**;

(d) confidential invention and assignment agreements, reasonably satisfactory in form and content to Parent, executed by all employees and former employees of the Company and by all consultants and independent contractors and former consultants and former independent contractors to the Company who have not already signed such agreements (including the individuals identified in Part 2.9(f) of the Disclosure Schedule and each of the Retained Employees);

(e) an estoppel certificate, dated as of a date not more than five days prior to the Closing Date and satisfactory in form and content to Parent, executed by Sheffield Properties of Illinois, Inc.;

(f) a statement (in such form as may be reasonably requested by counsel to Parent) conforming to the requirements of Section 1.897 — 2(h)(1)(i) of the United States Treasury Regulations;

(g) written resignations of all directors and officers of the Company, effective as of the Effective Time;

(h) a certificate executed by the Company containing the representation and warranty of the Company that each of the representations and warranties set forth in Section 2 is accurate in all respects as of the Closing Date as if made on the Closing Date and that the conditions set forth in Section 6 have been duly satisfied (the “Closing Certificate”).

6.9 Absence of Material Adverse Effect. Since the date of this Agreement, there shall not have occurred any Material Adverse Effect on the Company, and no event shall have occurred or circumstance shall exist that, in combination with any other events or circumstances, could reasonably be expected to have a Material Adverse Effect on the Company; provided, however, that an increase of the Company’s outstanding debt (including costs and expenses incurred in connection with the transactions contemplated by this Agreement) to an amount not exceeding \$1,500,000 shall not constitute a Material Adverse Effect.

6.10 FIRPTA Compliance. The Company shall have filed with the Internal Revenue Service the notification required under Section 1.897 — 2(h)(2) of the United States Treasury Regulations.

6.11 No Restraints. No temporary restraining order, preliminary or permanent injunction or other order preventing the consummation of the Merger shall have been issued by any court of competent jurisdiction and remain in effect, and there shall not be any Legal Requirement enacted or deemed applicable to the Merger that makes consummation of the Merger illegal.

6.12 No Legal Proceedings. There shall not be pending or threatened any suit, action, proceeding other than the matters set forth in Part 2.18(a) of the Disclosure Schedule. There shall not be pending or threatened any suit, action, proceeding or investigation: (i) challenging or seeking to restrain or prohibit the consummation of the Merger or any of the other transactions contemplated by this Agreement; (ii) relating to the Merger and seeking to obtain from Parent any damages (iii) seeking to prohibit or limit in any material respect Parent’s ability to vote, receive dividends with respect to or otherwise exercise ownership rights with respect to the stock of the Surviving Corporation; (iv) which would materially and adversely affect the right of the Surviving Corporation to own the assets or operate the business of the Company; or (v) which, if adversely determined, could have a Material Adverse Effect on the Company or Parent.

6.13 Termination of Employee Plans. The Company shall have provided Parent with evidence, reasonably satisfactory to Parent, (a) as to the termination of the Stock Plan and

additional Employee Plans to be terminated (if any), (b) that no employee or former employee of the Company has any rights under any of such Employee Plans and (c) that any Liabilities of the Company under such Employee Plans (including any such Liabilities relating to services performed prior to the Closing) are fully extinguished at no cost to the Company.

6.14 Termination of Agreements. The Company shall have provided Parent with evidence, reasonably satisfactory to Parent, of the termination of the agreements set forth in Section 5.5 of this Agreement.

6.15 Company Warrants. Parent shall have received evidence reasonably satisfactory to it that all Company Warrants shall have been exercised or terminated.

6.16 Dissenters Rights. Any Company stockholders exercising dissenters rights pursuant to Section 1.10 must collectively hold less than five percent (5%) of the Company's outstanding capital stock.

6.17 Conversion of Preferred Stock. The Company shall have obtained the consent of the holders of Company Preferred Stock to convert all of the Company Preferred Stock into shares of Company Common Stock pursuant to the terms of the Company's Amended and Restated Certificate of Incorporation with such conversion to be effective immediately prior to the Effective Time.

6.18 Delivery of Supplement to Opinion Letters. Parent and the Company shall have received a supplement to each of the October 2004 opinion letters of Stradling Yocca Carlson & Rauth delivered to the Company, which supplements shall be in a form reasonably acceptable to Parent.

SECTION 7. Conditions Precedent to Obligations of the Company

The obligations of the Company to effect the Merger and otherwise consummate the transactions contemplated by this Agreement are subject to the satisfaction, at or prior to the Closing, of the following conditions:

7.1 Accuracy of Representations. Each of the representations and warranties made by Parent and Merger Sub in this Agreement shall have been accurate in all material respects as of the date of this Agreement (without giving effect to any materiality or similar qualifications contained in such representations and warranties), and shall be accurate in all material respects as of the Closing Date as if made on the Closing Date (without giving effect to any materiality or similar qualifications contained in such representations and warranties).

7.2 Performance of Covenants. All of the covenants and obligations that Parent and Merger Sub are required to comply with or to perform at or prior to the Closing shall have been complied with and performed in all material respects.

7.3 Documents. The Company shall have received a certificate executed by Parent and Merger Sub containing the representations and warranties of Parent and Merger Sub that the conditions set forth in Sections 7.1, 7.2 and 7.4 have been duly satisfied.

7.4 No Restraints. No temporary restraining order, preliminary or permanent injunction or other order preventing the consummation of the Merger shall have been issued by any court of competent jurisdiction and remain in effect, and there shall not be any Legal Requirement enacted or deemed applicable to the Merger that makes consummation of the Merger illegal.

SECTION 8. Termination

8.1 Termination Events. This Agreement may be terminated prior to the Closing:

(a) by Parent if the Closing has not taken place on or before October 31, 2004 (other than as a result of any failure on the part of Parent or Merger Sub to comply with or perform any covenant or obligation of Parent or Merger Sub set forth in this Agreement or in any other agreement or instrument delivered to the Company);

(b) by the Company if the Closing has not taken place on or before October 31, 2004 (other than as a result of the failure on the part of the Company to comply with or perform any covenant or obligation set forth in this Agreement or in any other agreement or instrument delivered to Parent);

(c) by mutual written consent of Parent and the Company; or

(d) by either Parent or the Company if a court of competent jurisdiction or other Governmental Body shall have issued a final and nonappealable order, decree or ruling, or shall have taken any other action, having the effect of permanently restraining, enjoining or otherwise prohibiting the Merger.

8.2 Termination Procedures. If Parent wishes to terminate this Agreement pursuant to Section 8.1(a) or Section 8.1(d), Parent shall deliver to the Company a written notice stating that Parent is terminating this Agreement and setting forth a brief description of the basis on which Parent is terminating this Agreement. If the Company wishes to terminate this Agreement pursuant to Section 8.1(b) or Section 8.1(d), the Company shall deliver to Parent a written notice stating that the Company is terminating this Agreement and setting forth a brief description of the basis on which it is terminating this Agreement.

8.3 Effect of Termination. If this Agreement is terminated pursuant to Section 8.1, all further obligations of the parties under this Agreement shall terminate; *provided, however*, that notwithstanding such termination: (i) neither the Company nor Parent shall be relieved of any obligation or liability arising from any prior material breach by such party of any representation, warranty or covenant contained in, or other provision of, this Agreement; (ii) the parties shall, in all events, remain bound by and continue to be subject to the provisions set forth in Section 10; and (iii) the Company shall, in all events, remain bound by and continue to be subject to Section 5.3.

SECTION 9. Indemnification, Etc.

9.1 Survival of Representations, Etc.

(a) Other than the representations and warranties set forth in Sections 2.3, 2.4, 2.6, 2.7, 2.9, 2.11, 2.12, 2.14, 2.15, 2.18, 2.19 and 2.20 (the “**Specified Representations**”), the representations and warranties made by the Company (including the representations and warranties set forth in Section 2 and the representations and warranties set forth in the Closing Certificate) shall survive the Closing for a period of one (1) year. The Specified Representations shall survive Closing for a period of eighteen (18) months; *provided, however*, that if, at any time prior to the termination of the representation or warranty in question, if any Indemnitee (acting in good faith) delivers to the Stockholders’ Agent a written notice alleging the existence of an inaccuracy in or a breach of any of the representations and warranties made by the Company (and setting forth in reasonable detail the basis for such Indemnitee’s belief that such an inaccuracy or breach may exist) and asserting a claim for recovery under this Section 9 based on such alleged inaccuracy or breach, then the claim asserted in such notice shall survive until such time as such claim is fully and finally resolved. All representations and warranties made by Parent and Merger Sub shall terminate and expire as of the Effective Time, and any liability of Parent or Merger Sub with respect to such representations and warranties shall thereupon cease. Notwithstanding anything to the contrary contained in Section 9.1(a), the limitations set forth in Sections 9.1(a) shall not apply in the case of claims based upon intentional misrepresentation or fraud.

(b) The representations, warranties, covenants and obligations of the Company, and the rights and remedies that may be exercised by the Indemnitees, shall not be limited or otherwise affected by or as a result of any information furnished to, or any investigation made by or Knowledge of, any of the Indemnitees or any of their Representatives.

(c) For purposes of this Agreement, each statement or other item of information set forth in the Disclosure Schedule or in any update to the Disclosure Schedule shall be deemed to be a representation and warranty made by the Company in this Agreement.

9.2 Indemnification by Company.

(a) From and after the Effective Time (but subject to Section 9.1(a)), the Company (the “**Indemnitors**”), shall hold harmless and indemnify each of the Indemnitees from and against, and shall compensate and reimburse each of the Indemnitees for, any Damages which are directly or indirectly suffered or incurred by any of the Indemnitees or to which any of the Indemnitees may otherwise become subject (regardless of whether or not such Damages relate to any third-party claim) and which arise from or as a result of, or are directly or indirectly connected with: (i) any inaccuracy in or breach of any representation or warranty of the Company set forth in this Agreement, the Disclosure Schedule or the Closing Certificate (without giving effect to any “Material Adverse Effect” or other materiality qualification or any similar qualification contained or incorporated directly or indirectly in such representation or warranty); (ii) any inaccuracy in or breach of any representation or warranty of the Company set forth in this Agreement, the Disclosure Schedule or the Closing Certificate as if such representation and warranty had been made on and as of the Closing Date, except to the extent

that such representations and warranties relate to a specific date, in which case such representations and warranties shall be accurate on and as of such specific date, (without giving effect to any "Material Adverse Effect" or other materiality qualification or any similar qualification contained or incorporated directly or indirectly in such representation or warranty); (iii) any breach of any covenant or failure to perform any obligation of the Company set forth in this Agreement, the Disclosure Schedule or the Closing Certificate; (iv) the failure of the Company to comply with local, state or federal labor and employment laws, rules and regulations, including without limitation all laws, rules or regulations dealing with employee wages and hours, on or before the Closing; (v) any matter or correspondence described in Part 2.9 of the Disclosure Schedule or (vi) any Legal Proceeding relating to any breach or inaccuracy of the type referred to in clause "(i)," "(ii)," "(iii)," (iv) or "(iv)" above (including any Legal Proceeding commenced by any Indemnitee for the purpose of enforcing any of its rights under this Section 9).

(b) With the exception of inaccuracies or breaches of representations, warranties and covenants involving intentional misrepresentation or fraud, the Parent shall be entitled to be indemnified solely from the Escrow Amount not yet released by Parent pursuant to Section 1.8 for any Damages actually incurred by an Indemnitee as set forth in Section 9.2(a).

(c) Except in the case of intentional misrepresentation or fraud, and without limiting the effect of any other limitation contained in this Section 9, the indemnification provided for in this Section 9.2 shall not apply, and an Indemnitee shall not be entitled to exercise any indemnification rights under this Section 9.2, except to the extent that the aggregate amount of the Damages against which all Indemnitees would otherwise be entitled to be indemnified under this Section 9.2 exceeds \$200,000. At such time as the cumulative amount of such Damages exceeds \$200,000 in the aggregate, then the Indemnitees shall be entitled to be indemnified against and compensated and reimbursed for the cumulative amount of such Damages (and not merely the portion of such Damages exceeding \$200,000).

(d) In the case of intentional misrepresentation or fraud by the Company or any Company Stockholder, the following provisions shall apply:

(i) the Indemnitees shall have recourse to the Escrow Amount with respect to any Damages to which an Indemnitee is entitled to be held harmless, indemnified, compensated or reimbursed pursuant to Section 9.2 and which arise from or as a result of, or are connected with, such intentional misrepresentation or fraud (irrespective of the Person who actually participated in or had knowledge of such intentional misrepresentation or fraud); and

(ii) in addition to the rights and remedies referred to in clause "(i)" of this sentence, with respect to any Company Stockholder who participated in or had knowledge of such intentional misrepresentation or fraud, there shall be no limit on such Company Stockholder's liability for such intentional misrepresentation or fraud.

(e) Nothing in this Agreement shall limit any remedy an Indemnitee may have against any Person for intentional misrepresentation or fraud under applicable tort laws.

9.3 Defense of Third Party Claims. In the event of the assertion or commencement by any Person of any claim or Legal Proceeding (whether against Merger Sub, the Company, Parent or any other Person) with respect to which any of the Indemnitors may become obligated to hold harmless, indemnify, compensate or reimburse any Indemnitee pursuant to this Section 9, Parent shall have the right, at its election, to proceed with the defense of such claim or Legal Proceeding on its own. If Parent so proceeds with the defense of any such claim or Legal Proceeding:

(a) all reasonable expenses relating to the defense of such claim or Legal Proceeding shall be borne and paid from the Escrow Amount;

(b) each Indemnitor shall make available to Parent any documents and materials in his or its possession or control that may be necessary to the defense of such claim or Legal Proceeding; and

(c) Parent shall have the right to settle, adjust or compromise such claim or Legal Proceeding with the consent of the Stockholders' Agent; *provided, however,* that such consent shall not be unreasonably withheld or delayed.

Parent shall (i) give the Stockholders' Agent notice of the commencement of any such claim or Legal Proceeding against Parent, Merger Sub or the Company promptly after Parent becomes aware of such claims or Legal Proceeding and (ii) use reasonable efforts to notify the Stockholders' Agent of all material developments relating to such claims or Legal Proceeding; *provided, however,* that any failure on the part of Parent to so notify the Stockholders' Agent shall not limit any of the obligations of the Indemnitors under this Section 9 (except to the extent such failure materially prejudices the defense of such Legal Proceeding). If Parent does not elect to proceed with the defense of any such claim or Legal Proceeding, the Stockholders' Agent may proceed with the defense of such claim or Legal Proceeding with counsel reasonably satisfactory to the Parent; *provided, however,* that the Stockholders' Agent (i) will use reasonable efforts to notify Parent of all material developments relating to such claim or Legal Proceeding and (ii) may not settle, adjust or compromise any such claim or Legal Proceeding without the prior written consent of Parent (which consent may not be unreasonably withheld or delayed).

9.4 Exercise of Remedies by Indemnitees Other Than Parent. No Indemnitee (other than Parent or any successor thereto or assign thereof) shall be permitted to assert any indemnification claim or exercise any other remedy under this Agreement unless Parent (or any successor thereto or assign thereof) shall have consented to the assertion of such indemnification claim or the exercise of such other remedy.

SECTION 10. Miscellaneous Provisions

10.1 Stockholders' Agent. If this Agreement is duly adopted by the Company's stockholders, the Company's stockholders shall be deemed to have irrevocably appointed David Strohm as their agent for purposes of Section 9 and for purposes of acting on behalf of the Company's stockholders pursuant to the indemnity and holdback terms of this Agreement (the "**Stockholders' Agent**"). Mr. Strohm hereby accepts his appointment as the Stockholders' Agent. Parent shall be entitled to deal exclusively with the Stockholders' Agent on all matters

relating to Section 9 and such indemnity and holdback provisions, and shall be entitled to rely conclusively (without further evidence of any kind whatsoever) on any document executed or purported to be executed on behalf of any Indemnitor by the Stockholders' Agent, and on any other action taken or purported to be taken on behalf of any Indemnitor by the Stockholders' Agent, as fully binding upon such Indemnitor. If the Stockholders' Agent shall die, become disabled or otherwise be unable to fulfill his responsibilities as agent of the Indemnitors, then the Indemnitors shall, within ten days after such death or disability, appoint a successor agent and, promptly thereafter, shall notify Parent of the identity of such successor. Any such successor shall become the "Stockholders' Agent" for purposes of Section 9, and such indemnity and holdback provisions, and this Section 10.1. If for any reason there is no Stockholders' Agent at any time, all references herein to the Stockholders' Agent shall be deemed to refer to the Indemnitors.

10.2 Further Assurances. Each party hereto shall execute and cause to be delivered to each other party hereto such instruments and other documents, and shall take such other actions, as such other party may reasonably request (prior to, at or after the Closing) for the purpose of carrying out or evidencing any of the transactions contemplated by this Agreement.

10.3 Fees and Expenses. Each party to this Agreement shall bear and pay all fees, costs and expenses (including legal fees and accounting fees) that have been incurred or that are incurred in the future by such party in connection with the transactions contemplated by this Agreement, including all fees, costs and expenses incurred by such party in connection with or by virtue of (a) the negotiation, preparation and review of this Agreement (including the Disclosure Schedule) and all agreements, certificates, opinions and other instruments and documents delivered or to be delivered in connection with the transactions contemplated by this Agreement, (b) the preparation and submission of any filing or notice required to be made or given in connection with any of the transactions contemplated by this Agreement, and the obtaining of any Consent required to be obtained in connection with any of such transactions, and (c) the consummation of the Merger; provided, however, that, notwithstanding anything to the contrary contained in this Agreement, the total amount of all such fees, costs and expenses incurred by or for the benefit of the Company, including all fees and expenses to be paid to the Escrow Agent in connection with the Escrow Amount, shall be borne and paid solely by the stockholders of the Company, the Converted Option Holders and Converted Warrant Holders, Converted Option Holders and Converted Warrant Holders, and not by the Company. Such fees, costs and expenses incurred by or for the benefit of the Company shall be deducted from the Merger Consideration in accordance with Section 1.5(a) above.

10.4 Attorneys' Fees. If any action or proceeding relating to this Agreement or the enforcement of any provision of this Agreement is brought against any party hereto, the prevailing party shall be entitled to recover reasonable attorneys' fees, costs and disbursements (in addition to any other relief to which the prevailing party may be entitled).

10.5 Notices. Any notice or other communication required or permitted to be delivered to any party under this Agreement shall be in writing and shall be deemed properly delivered, given and received (a) upon receipt when delivered by hand, or (b) two business days after sent by registered mail or by courier or express delivery service, or by facsimile, provided

that in each case the notice or other communication is sent to the address or facsimile telephone number set forth beneath the name of such party below (or to such other address or facsimile telephone number as such party shall have specified in a written notice given to the other parties hereto):

if to Parent or Merger Sub:

iPass Inc.

3800 Bridge Parkway
Redwood Shores, CA
Attention: Bruce Posey, Esq.
Facsimile No.: (650) 232-0250

with a copy to:

Cooley Godward LLP

3000 El Camino Real
Five Palo Alto Square
Palo Alto, CA 94306
Attention: Timothy J. Moore, Esq.
Facsimile No.: (650) 849-7400

if to the Company:

Mobile Automation, Inc.

310 North Westlake Blvd.
Westlake Village, CA 91362
Attention:
Facsimile No.: (310) 914-9703

with a copy to:

Stradling Yocca Carlson & Rauth

660 Newport Center Drive, Suite 1600
Newport Beach, CA 92660
Attention: Steven R. Pacelli, Esq.
Facsimile No.: (949) 725-4100

if to the Stockholders' Agent:

David Strohm
Greylock
2929 Campus Dr., Suite 400
San Mateo, CA 94403
Facsimile No.: (650) 493-5575

10.6 Time of the Essence. Time is of the essence of this Agreement.

10.7 Headings. The headings contained in this Agreement are for convenience of reference only, shall not be deemed to be a part of this Agreement and shall not be referred to in connection with the construction or interpretation of this Agreement.

10.8 Counterparts. This Agreement may be executed in several counterparts, each of which shall constitute an original and all of which, when taken together, shall constitute one agreement.

10.9 Governing Law; Venue. This Agreement shall be construed in accordance with, and governed in all respects by, the internal laws of the State of Delaware (without giving effect to principles of conflicts of laws). In any action between any of the parties arising out of or relating to this Agreement or any of the transactions contemplated by this Agreement: (a) each of the parties irrevocably and unconditionally consents to and submits to the exclusive jurisdiction and venue of the state and federal courts located in Santa Clara County, California; (b) if any such action is commenced in a state court, then, subject to applicable law, no party shall object to the removal of such action to any federal court located in the Northern District of California; and (c) each of the parties irrevocably consents to service of process by first class certified mail, return receipt requested, postage prepaid, to the address at which such party is to receive notice in accordance with Section 10.5.

10.10 Successors and Assigns. This Agreement shall be binding upon each of the parties hereto and each of their respective successors and assigns, if any. This Agreement shall inure to the benefit of: the Company; Parent; Merger Sub; the other Indemnitees; and the respective successors and assigns (if any) of the foregoing. Parent may freely assign any or all any of its rights under this Agreement (including its indemnification rights under Section 9), in whole or in part, to any other Person without obtaining the consent or approval of any other party hereto or of any other Person.

10.11 Remedies Cumulative; Specific Performance. The rights and remedies of the parties hereto shall be cumulative (and not alternative). The parties to this Agreement agree that, in the event of any breach or threatened breach by any party to this Agreement of any covenant, obligation or other provision set forth in this Agreement for the benefit of any other party to this Agreement, such other party shall be entitled (in addition to any other remedy that may be available to it) to (a) a decree or order of specific performance or mandamus to enforce the observance and performance of such covenant, obligation or other provision, and (b) an injunction restraining such breach or threatened breach.

10.12 Waiver.

(a) No failure on the part of any Person to exercise any power, right, privilege or remedy under this Agreement, and no delay on the part of any Person in exercising any power, right, privilege or remedy under this Agreement, shall operate as a waiver of such power, right, privilege or remedy; and no single or partial exercise of any such power, right, privilege or remedy shall preclude any other or further exercise thereof or of any other power, right, privilege or remedy.

(b) No Person shall be deemed to have waived any claim arising out of this Agreement, or any power, right, privilege or remedy under this Agreement, unless the waiver of such claim, power, right, privilege or remedy is expressly set forth in a written instrument duly executed and delivered on behalf of such Person; and any such waiver shall not be applicable or have any effect except in the specific instance in which it is given.

10.13 Waiver of Jury Trial. Each of the parties hereto hereby irrevocably waives any and all right to trial by jury in any Legal Proceeding arising out of or related to this Agreement or the transactions contemplated hereby.

10.14 Amendments. This Agreement may not be amended, modified, altered or supplemented other than by means of a written instrument duly executed and delivered on behalf of all of the parties hereto.

10.15 Severability. In the event that any provision of this Agreement, or the application of any such provision to any Person or set of circumstances, shall be determined to be invalid, unlawful, void or unenforceable to any extent, the remainder of this Agreement, and the application of such provision to Persons or circumstances other than those as to which it is determined to be invalid, unlawful, void or unenforceable, shall not be impaired or otherwise affected and shall continue to be valid and enforceable to the fullest extent permitted by law.

10.16 Parties in Interest. Except for the provisions of Sections 1.5 and 9, none of the provisions of this Agreement is intended to provide any rights or remedies to any Person other than the parties hereto and their respective successors and assigns (if any).

10.17 Entire Agreement. This Agreement and the other agreements referred to herein set forth the entire understanding of the parties hereto relating to the subject matter hereof and thereof and supersede all prior agreements and understandings among or between any of the parties relating to the subject matter hereof and thereof; *provided, however,* that the “no-shop” agreement executed on behalf of Parent and the Company on September 3, 2004 shall not be superseded by this Agreement and shall remain in effect in accordance with its terms until the earlier of (a) the Effective Time, or (b) the date on which such agreement is terminated in accordance with its terms.

10.18 Construction.

(a) For purposes of this Agreement, whenever the context requires: the singular number shall include the plural, and vice versa; the masculine gender shall include the feminine and neuter genders; the feminine gender shall include the masculine and neuter genders; and the neuter gender shall include the masculine and feminine genders.

(b) The parties hereto agree that any rule of construction to the effect that ambiguities are to be resolved against the drafting party shall not be applied in the construction or interpretation of this Agreement.

(c) As used in this Agreement, the words “include” and “including,” and variations thereof, shall not be deemed to be terms of limitation, but rather shall be deemed to be followed by the words “without limitation.”

(d) Except as otherwise indicated, all references in this Agreement to “Sections” and “Exhibits” are intended to refer to Sections of this Agreement and Exhibits to this Agreement.

The parties hereto have caused this Agreement to be executed and delivered as of the date first written above.

iPass Inc.,
a Delaware corporation

By: _____

Printed Name: _____

Title: _____

Montage Acquisition Corp.
a Delaware corporation

By: _____

Printed Name: _____

Title: _____

Mobile Automation, Inc.,
a Delaware corporation

By: _____

Printed Name: _____

Title: _____

Stockholder's Agent

By: _____

Printed Name: _____

Exhibit A

CERTAIN DEFINITIONS

For purposes of the Agreement (including this **Exhibit A**):

Acquisition Transaction. “Acquisition Transaction” shall mean any transaction involving any (a) merger, consolidation, business combination, or similar transaction involving the Company, (b) sale, license on an exclusive basis, lease or other disposition directly or indirectly by merger, consolidation, business combination, share exchange, joint venture, or otherwise of assets of the Company representing 50% or more of the assets of the Company, (c) issuance, sale, or other disposition of (including by way of merger, consolidation, business combination, share exchange, joint venture, or any similar transaction) securities (or options, rights or warrants to purchase, or securities convertible into or exchangeable for such securities) representing 50% or more of the voting power of the Company, (d) transaction in which any person shall acquire beneficial ownership, or the right to acquire beneficial ownership or any group shall have been formed which beneficially owns or has the right to acquire beneficial ownership of 50% or more of the outstanding voting capital stock of the Company or (e) any combination of the foregoing (other than the Merger).

Acquisition Proposal. “Acquisition Proposal” shall mean any offer, proposal, inquiry or indication of interest (other than an offer, proposal, inquiry or indication of interest by Parent) contemplating or otherwise relating to any Acquisition Transaction.

Agreement. “Agreement” shall mean the Agreement and Plan of Merger to which this **Exhibit A** is attached, as it may be amended from time to time.

CGCL. “CGCL” shall mean the California General Corporation Law.

Code. “Code” shall mean the Internal Revenue Code of 1986, as amended.

Company. “Company” shall mean the Company and all of the Subsidiaries.

Company Capital Stock. “Company Capital Stock” shall mean the Company Common Stock and the Company Preferred Stock.

Company Common Stock. “Company Common Stock” shall mean the common stock (\$0.001 par value per share) of the Company.

Company Common Stock Warrants. “Company Common Stock Warrants” shall mean warrants to purchase shares of Company Common Stock.

Company Contract. “Company Contract” shall mean any Contract: (a) to which the Company is a party; (b) by which the Company or any of its assets is or may become bound or under which the Company has, or may become subject to, any obligation; or (c) under which the Company has or may acquire any right or interest.

Company IP. “Company IP” means (a) all Intellectual Property Rights in the Company Products and Company Software and (b) all Intellectual Property Rights and Intellectual Property

in which the Company has (or purports to have) an ownership interest or an exclusive license or similar exclusive right.

Company Options. “Company Options” shall have the meaning set forth in Section 1.6.

Company Preferred Stock. “Company Preferred Stock” shall mean the Series A Preferred Stock and Series B Preferred Stock.

Company Series A Warrants. “Company Series A Warrants” shall mean warrants to purchase shares of Series A Preferred Stock.

Company Series B Warrants. “Company Series B Warrants” shall mean warrants to purchase shares of Series B Preferred Stock.

Company Product. “Company Product” means any product or service developed, distributed, licensed, leased, manufactured, marketed, provided, or sold, directly or indirectly, by or on behalf of the Company at any time, and any product or service currently under development by the Company, whether or not in collaboration with any Person.

Company Software. “Company Software” shall mean any software (including firmware and other software embedded in hardware devices) owned, developed (or currently being developed), used, marketed, distributed, licensed or sold by the Company at any time (other than non-customized third-party software licensed to the Company solely for internal use on a non-exclusive basis).

Company Source Code. “Company Source Code” shall mean the human-readable source code version of any Company Software, including all calculation formulae embodied in the Company Software, descriptions or details of any algorithms embodied in the Company Software, and all annotations, commentary, instructions, specifications (including design, functional, and other technical specifications), programmer notes (technical or otherwise), logic diagrams, flowcharts, input and output layouts, field descriptions, sort sequences, data dictionaries, and file layouts relating to any Company Software.

Company Stockholder. “Company Stockholder” shall mean each stockholder of the Company that does not perfect its dissenters’ rights or rights of appraisal and is otherwise entitled to receive the Merger Consideration pursuant to Section 1.5.

Company Stock Plan. “Company Stock Plan” means the Company’s 1998 Stock Option/Stock Issuance Plan.

Company Warrants. “Company Warrants” shall have the meaning set forth in Section 1.6.

Consent. “Consent” shall mean any approval, consent, ratification, permission, waiver or authorization (including any Governmental Authorization).

Contract. “Contract” shall mean any written, oral or other agreement, contract, subcontract, lease, understanding, instrument, note, warranty, insurance policy, benefit plan or legally binding commitment or undertaking of any nature.

Current Net Assets. “Current Net Assets” means the total current assets of the Company as of a certain balance sheet date less the total current liabilities of the Company as of the same balance sheet date, in each case as determined in accordance with GAAP.

Damages. “Damages” shall include any loss, damage, injury, decline in value, lost opportunity, Liability, claim, demand, settlement, judgment, award, fine, penalty, Tax, fee (including reasonable attorneys’ fees), charge, cost (including costs of investigation) or expense of any nature.

Disclosure Schedule. “Disclosure Schedule” shall mean the schedule (dated as of the date of the Agreement) delivered separately to Parent on behalf of the Company.

Encumbrance. “Encumbrance” shall mean any lien, pledge, hypothecation, charge, mortgage, security interest, encumbrance, claim, infringement, interference, option, right of first refusal, preemptive right, community property interest or restriction of any nature (including any restriction on the voting of any security, any restriction on the transfer of any security or other asset, any restriction on the receipt of any income derived from any asset, any restriction on the use of any asset and any restriction on the possession, exercise or transfer of any other attribute of ownership of any asset).

Entity. “Entity” shall mean any corporation (including any non-profit corporation), general partnership, limited partnership, limited liability partnership, joint venture, estate, trust, company (including any limited liability company or joint stock company), firm or other enterprise, association, organization or entity.

Escrow Agent. “Escrow Agent” shall mean U.S. Bank National Association.

Governmental Authorization. “Governmental Authorization” shall mean any: (a) permit, license, certificate, franchise, permission, clearance, registration, qualification or authorization issued, granted, given or otherwise made available by or under the authority of any Governmental Body or pursuant to any Legal Requirement; or (b) right under any Contract with any Governmental Body.

Governmental Body. “Governmental Body” shall mean any: (a) nation, state, commonwealth, province, territory, county, municipality, district or other jurisdiction of any nature; (b) federal, state, local, municipal, foreign or other government; or (c) governmental or quasi-governmental authority of any nature (including any governmental division, department, agency, commission, instrumentality, official, organization, unit, body or Entity and any court or other tribunal).

Indemnitees. “Indemnitees” shall mean the following Persons: (a) Parent; (b) Parent’s current and future affiliates (including the Surviving Corporation); (c) the respective Representatives of the Persons referred to in clauses “(a)” and “(b)” above; and (d) the respective successors and assigns of the Persons referred to in clauses “(a)”, “(b)” and “(c)” above; *provided, however*, that the stockholders of the Company shall not be deemed to be “Indemnitees.”

Intellectual Property. “Intellectual Property” means and includes all algorithms, APIs, apparatus, databases and data collections, diagrams, formulae, inventions (whether or not

patentable), know-how, logos, marks (including brand names, product names, logos, and slogans), methods, network configurations and architectures, processes, proprietary information, protocols, schematics, specifications, software, software code (in any form including source code and executable or object code), subroutines, user interfaces, techniques, URLs, web sites, works of authorship, and other forms of technology (whether or not embodied in any tangible form and including all tangible embodiments of the foregoing such as instruction manuals, laboratory notebooks, prototypes, samples, studies, and summaries).

Intellectual Property Rights. “Intellectual Property Rights” means and includes all past, present, and future rights of the following types, which may exist or be created under the laws of any jurisdiction in the world: (a) rights associated with works of authorship, including exclusive exploitation rights, copyrights, moral rights, and mask works; (b) trademark and trade name rights and similar rights; (c) trade secret rights; (d) patents and industrial property rights; (e) other proprietary rights in Intellectual Property of every kind and nature; and (f) all registrations, renewals, extensions, combinations, divisions, or reissues of, and applications for, any of the rights referred to in clauses (a) through (f) above.

Knowledge. Information shall be deemed to be known to or to the “Knowledge” of the Company or a Company Stockholder if that information is actually known or should be known by any officer or director of the Company or such Company Stockholder after due inquiry.

Legal Proceeding. “Legal Proceeding” shall mean any action, suit, litigation, arbitration, proceeding (including any civil, criminal, administrative, investigative or appellate proceeding), hearing, inquiry, audit, examination or investigation commenced, brought, conducted or heard by or before, or otherwise involving, any court or other Governmental Body or any arbitrator or arbitration panel.

Legal Requirement. “Legal Requirement” shall mean any federal, state, local, municipal, foreign or other law, statute, constitution, principle of common law, resolution, ordinance, code, edict, decree, rule, regulation, ruling or requirement issued, enacted, adopted, promulgated, implemented or otherwise put into effect by or under the authority of any Governmental Body.

Liability. “Liability” shall mean any debt, obligation, duty or liability of any nature (including any unknown, undisclosed, unmatured, unaccrued, unasserted, contingent, indirect, conditional, implied, vicarious, derivative, joint, several or secondary liability), regardless of whether such debt, obligation, duty or liability would be required to be disclosed on a balance sheet prepared in accordance with generally accepted accounting principles and regardless of whether such debt, obligation, duty or liability is immediately due and payable.

Material Adverse Effect. An event, violation, inaccuracy, circumstance or other matter will be deemed to have a “Material Adverse Effect” on the Company if such event, violation, inaccuracy, circumstance or other matter (considered together with all other matters that would constitute exceptions to the representations and warranties set forth in the Agreement or in the Closing Certificate but for the presence of “Material Adverse Effect” or other materiality qualifications, or any similar qualifications, in such representations and warranties) would have a material adverse effect on (i) the business, condition, capitalization, assets, liabilities, operations or financial performance of the Company, (ii) the ability of the Company to consummate the

Merger or any of the other transactions contemplated by the Agreement or to perform any of its obligations under the Agreement, or (iii) Parent's ability to vote, receive dividends with respect to or otherwise exercise ownership rights with respect to the stock of the Surviving Corporation.

Option Consideration. "Option Consideration" shall mean an amount in cash equal to the product of (i) the excess of the Merger Consideration per share of Company Common Stock underlying such Company Option over the exercise price per share of Company Common Stock of such Company Option and (ii) the number of shares of Company Common Stock (the "Net Option Shares") computed using the following formula:

$$X = Y(A-B)/A$$

Where:

X = the Net Option Shares

Y = number of shares of Company Common Stock for which such Company Option is exercisable immediately prior to the Effective Time after giving effect to any acceleration of vesting resulting from the Merger

A = the Merger Consideration per share of Company Common Stock underlying such Company Option

B = Exercise price per share of Company Common Stock of such Company Option

Person. "Person" shall mean any individual, Entity or Governmental Body.

Registered IP. "Registered IP" means all Intellectual Property Rights that are registered, filed, or issued under the authority of any Governmental Body, including all patents, registered copyrights, registered mask works, and registered trademarks and all applications for any of the foregoing.

Representatives. "Representatives" shall mean officers, directors, employees, agents, affiliates, attorneys, accountants, advisors and other representatives.

Series A Preferred Stock. "Series A Preferred Stock" shall mean the preferred stock of the Company (\$0.005 par value per share) designated as "Series A."

Series B Preferred Stock. "Series B Preferred Stock" shall mean the preferred stock of the Company (\$0.005 par value per share) designated as "Series B."

Subsidiary. Any Entity shall be deemed to be a "Subsidiary" of another Person if such Person directly or indirectly (a) has the power to direct the management or policies of such Entity or (b) owns, beneficially or of record, (i) an amount of voting securities or other interest of such Entity that is sufficient to enable such Person to elect at least a majority of the members of such Entity's board of directors or other governing body, or (ii) at least 50% of the outstanding equity or financial interests of such Entity.

Tax. "Tax" shall mean any tax (including any income tax, franchise tax, capital gains tax, gross receipts tax, value-added tax, surtax, excise tax, ad valorem tax, transfer tax, stamp

tax, sales tax, use tax, property tax, business tax, withholding tax or payroll tax), levy, assessment, tariff, duty (including any customs duty), deficiency or fee, and any related charge or amount (including any fine, penalty or interest), imposed, assessed or collected by or under the authority of any Governmental Body.

Tax Return. "Tax Return" shall mean any return (including any information return), report, statement, declaration, estimate, schedule, notice, notification, form, election, certificate or other document or information filed with or submitted to, or required to be filed with or submitted to, any Governmental Body in connection with the determination, assessment, collection or payment of any Tax or in connection with the administration, implementation or enforcement of or compliance with any Legal Requirement relating to any Tax.

Warrant Consideration. "Warrant Consideration" shall mean an amount in cash equal to the product of (a) the excess of the Merger Consideration per share of Company Common Stock underlying such Company Warrant over the exercise price per share of Company Common Stock of such Company Warrant and (b) the number of shares of Company Common Stock (the "Net Warrant Shares") computed using the following formula:

$$X = Y(A-B)/A$$

Where:

X = the Net Warrant Shares

Y = number of shares of Company Common Stock for which such Company Warrant is exercisable immediately prior to the Effective Time

A = the Merger Consideration per share of Company Common Stock underlying such Company Warrant

B = Exercise price per share of Company Common Stock of such Company Warrant

Exhibit B

FORM OF PROPRIETARY INFORMATION AND INVENTIONS AGREEMENT

7.

Exhibit C-1
FORM OF OFFER LETTER

8.

Exhibit C-2

CONTINUING EMPLOYEES OF THE COMPANY

Mark Bell

Bruce Temesy

Steve Recker

Jay Steidle

Hank Nowak

Ryan Thomas

Lisa Cell

Mike Teplinsky

Chad Sanders

Geoff Schemel

Jack Homer

Alan Hand

Alex Chernyakhovsky

Michael Russell

Dale Schroeder

Justin Killen

Alex Balint

Marc Farer

David Adkins

Steve Rogers

Douglas Neal

Kay Buell

Exhibit D
ESCROW AGREEMENT

10.

Exhibit E-1
FORM OF RELEASE

11.

Exhibit E-2

LIST OF INDIVIDUALS SIGNING RELEASE

Greylock IX Limited Partnership

David Strohm

Silicon Valley Bank

Douglas Neal

The Peter Norton Living Trust

Safi Qureshey

Safi U. Qureshey Family Trust

Uns Safi Qureshey Investment Trust

Zeshan Qureshey Investment Trust

Rod Turner

Exhibit F

FORM OF LEGAL OPINION FROM STRADLING YOCCA CARLSON & ROTH

Schedule I

SPECIFIED PAYMENT OBLIGATIONS

14.

Subsidiaries

<u>Name</u>	<u>Jurisdiction</u>
iPass U.K., Limited	United Kingdom
iPass Asia, Pte., Ltd.	Singapore
iPass Holdings, Pty, Ltd.	Australia
iPass France, SAS	France
iPass Japan, K.K.	Japan
iPass, Ltd.	Israel
Safe3w, Inc.	Delaware
Mobile Automation, Inc.	Delaware

Consent of Independent Registered Public Accounting Firm

The Board of Directors
iPass Inc.:

We consent to the incorporation by reference in the Registration Statements (Nos. 333-107315 and 333-118295) on Form S-8 of iPass, Inc., of our reports dated March 15, 2005, relating to the consolidated balance sheets of iPass, Inc. and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2004, and management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2004, and the effectiveness of internal controls over financial reporting as of December 31, 2004, which reports appear in the December 31, 2004 annual report on Form 10-K of iPass, Inc.

/s/ KPMG LLP

Mountain View, California
March 15, 2005

CERTIFICATION

I, Kenneth D. Denman, certify that:

1. I have reviewed this Annual Report on Form 10-K of iPass Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 15, 2005

/s/ Kenneth D. Denman

Kenneth D. Denman
Chairman and Chief Executive Officer
(Principal Executive Officer)

CERTIFICATION

I, Donald C. McCauley, certify that:

1. I have reviewed this Annual Report on Form 10-K of iPass Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 15, 2005

/s/ Donald C. McCauley

Donald C. McCauley
Vice President and Chief Financial Officer
(Principal Financial Officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002, 18 U.S.C SECTION 1350**

In connection with the Annual Report of iPass Inc. (the "Company") on Form 10-K for the period ended December 31, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Kenneth D. Denman, Chairman and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 15, 2004

/s/ Kenneth D. Denman

Kenneth D. Denman
Chairman and Chief Executive Officer
(Principal Executive Officer)

This certification accompanies the Form 10-K to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of iPass Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Form 10-K), irrespective of any general incorporation language contained in such filing.

**CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002, 18 U.S.C SECTION 1350**

In connection with the Annual Report of iPass Inc. (the "Company") on Form 10-K for the period ended December 31, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Donald C. McCauley, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 15, 2005

/s/ Donald C. McCauley

Donald C. McCauley
Chief Financial Officer
(Principal Financial Officer)

This certification accompanies the Form 10-K to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of iPass Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Form 10-K), irrespective of any general incorporation language contained in such filing.