

LEAP WIRELESS INTERNATIONAL INC

Form 10-Q

November 13, 2001

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2001

OR

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

For the transition period from _____ to _____ .

Commission File Number 0-29752

Leap Wireless International, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)
10307 Pacific Center Court, San Diego, CA
(Address of principal executive offices)

33-0811062
(I.R.S. Employer
Identification No.)
92121
(Zip Code)

(858) 882-6000

(Registrant's telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last reported)

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

The number of shares of registrant's common stock outstanding on November 8, 2001 was 36,863,156.

TABLE OF CONTENTS

PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

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

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

PART II OTHER INFORMATION

Item 1. Legal Proceedings.

Item 2. Changes in Securities and Use of Proceeds.

Item 3. Defaults Upon Senior Securities.

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

Item 5. Other Information.

Item 6. Exhibits and Reports on Form 8-K.

SIGNATURES

EXHIBIT INDEX

EXHIBIT 10.24.1

EXHIBIT 10.24.2

EXHIBIT 10.25.2

EXHIBIT 10.26.1

EXHIBIT 10.27.3

Table of Contents

LEAP WIRELESS INTERNATIONAL, INC.

QUARTERLY REPORT ON FORM 10-Q

For the Quarter Ended September 30, 2001

TABLE OF CONTENTS

	Page
PART I FINANCIAL INFORMATION	
Item 1. Financial Statements	3
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	20
Item 3. Quantitative and Qualitative Disclosures About Market Risk	43
PART II OTHER INFORMATION	
Item 1. Legal Proceedings	44
Item 2. Changes in Securities and Uses of Proceeds	44
Item 3. Defaults Upon Senior Securities	44
Item 4. Submission of Matters to a Vote of Security Holders	44
Item 5. Other Information	44
Item 6. Exhibits and Reports on Form 8-K	44

Table of Contents**PART I****FINANCIAL INFORMATION****Item 1. Financial Statements.****LEAP WIRELESS INTERNATIONAL, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share data)**

	September 30, 2001	December 31, 2000
	(Unaudited)	
Assets		
Cash and cash equivalents	\$ 300,303	\$ 338,878
Restricted cash equivalents		13,575
Short-term investments	42,189	199,106
Inventories	34,831	9,032
Notes receivable, net	33,284	138,907
Other current assets	15,833	12,746
	<hr/>	<hr/>
Total current assets	426,440	712,244
Property and equipment, net	858,258	430,193
Investment in unconsolidated wireless operating company		34,691
Wireless licenses, net	687,634	265,635
Goodwill and other intangible assets, net	45,298	30,297
Restricted investments	54,182	51,896
Deposits for wireless licenses	85,000	91,772
Other assets	31,458	30,679
	<hr/>	<hr/>
Total assets	\$2,188,270	\$1,647,407
	<hr/>	<hr/>
Liabilities and Stockholders Equity		
Accounts payable and accrued liabilities	\$ 72,922	\$ 58,735
Other current liabilities	103,234	65,690
	<hr/>	<hr/>
Total current liabilities	176,156	124,425
Long-term debt	1,510,161	897,878
Other long-term liabilities	66,173	41,846
	<hr/>	<hr/>
Total liabilities	1,752,490	1,064,149
	<hr/>	<hr/>
Commitments and contingencies (Notes 2, 3 and 6)		
Stockholders equity:		
Preferred stock authorized 10,000,000 shares; \$.0001 par value, no shares issued and outstanding		
Common stock authorized 300,000,000 shares; \$.0001 par value, 36,752,478 and 28,348,694 shares issued and outstanding at September 30, 2001 and December 31, 2000, respectively	3	3
Additional paid-in capital	1,147,032	893,401
Unearned stock-based compensation	(6,201)	(10,019)

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

Accumulated deficit	(706,555)	(302,898)
Accumulated other comprehensive income	1,501	2,771
	<u> </u>	<u> </u>
Total stockholders' equity	435,780	583,258
	<u> </u>	<u> </u>
Total liabilities and stockholders' equity	\$2,188,270	\$1,647,407
	<u> </u>	<u> </u>

See accompanying notes to condensed consolidated financial statements.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
Revenues:				
Service revenues	\$ 57,240	\$ 5,296	\$ 122,449	\$ 31,542
Equipment revenues	9,453	2,244	28,843	4,513
Total revenues	66,693	7,540	151,292	36,055
Operating expenses:				
Cost of service	(27,297)	(5,506)	(57,003)	(14,270)
Cost of equipment	(53,197)	(4,883)	(116,632)	(30,851)
Selling and marketing	(32,181)	(4,113)	(70,982)	(15,730)
General and administrative	(39,290)	(15,061)	(96,691)	(57,445)
Depreciation and amortization	(33,494)	(3,573)	(68,792)	(17,251)
Total operating expenses	(185,459)	(33,136)	(410,100)	(135,547)
Operating loss	(118,766)	(25,596)	(258,808)	(99,492)
Equity in net loss of investments in and loans receivable from unconsolidated wireless operating companies	(14,264)	(25,249)	(57,562)	(72,001)
Interest income	4,850	16,934	23,623	33,938
Interest expense	(44,258)	(28,437)	(123,709)	(80,908)
Foreign currency transaction gains (losses), net	136	1,378	(1,139)	13,099
Gain on sale of subsidiary				313,432
Gain on issuance of stock by unconsolidated wireless operating company		6,898		32,602
Other income, net	12,405		15,981	1,978
Income (loss) before income taxes and extraordinary items	(159,897)	(54,072)	(401,614)	142,648
Income taxes	(845)		(2,043)	(34,548)
Income (loss) before extraordinary items	(160,742)	(54,072)	(403,657)	108,100
Extraordinary loss on early extinguishment of debt				(4,737)
Net income (loss)	\$ (160,742)	\$ (54,072)	\$ (403,657)	\$ 103,363
Other comprehensive income (loss):				
Foreign currency translation gains (losses), net	(628)	(3,327)	(1,233)	(2,433)
Unrealized holding gains (losses) on investments, net	(164)		(37)	
Comprehensive income (loss)	\$ (161,534)	\$ (57,399)	\$ (404,927)	\$ 100,930

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

Basic net income (loss) per common share:				
Income (loss) before extraordinary items	\$ (4.43)	\$ (2.04)	\$ (12.27)	\$ 4.35
Extraordinary loss				(0.19)
Net income (loss)	\$ (4.43)	\$ (2.04)	\$ (12.27)	\$ 4.16
Diluted net income (loss) per common share:				
Income (loss) before extraordinary items	\$ (4.43)	\$ (2.04)	\$ (12.27)	\$ 3.36
Extraordinary loss				(0.15)
Net income (loss)	\$ (4.43)	\$ (2.04)	\$ (12.27)	\$ 3.21
Shares used in per share calculations:				
Basic	36,310	26,524	32,909	24,826
Diluted	36,310	26,524	32,909	32,134

See accompanying notes to condensed consolidated financial statements.

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(UNAUDITED)****(In thousands)**

	Nine Months Ended September 30,	
	2001	2000
Operating activities:		
Net cash used in operating activities	\$ (239,899)	\$ (32,942)
Investing activities:		
Purchase of property and equipment	(132,818)	(43,686)
Loans to subsidiary and unconsolidated wireless operating company	(20,542)	(18,533)
Acquisitions, net of cash acquired	(2,900)	(1,327)
Purchase of wireless licenses	(230,876)	(39,364)
Net proceeds from disposal of subsidiaries		214,455
Purchase of investments	(117,199)	(163,117)
Sale and maturity of investments	275,870	45,490
Restricted cash equivalents and investments, net	12,736	(57,893)
Sale and repayment of notes receivable	108,138	
Other	(3,468)	
Net cash used in investing activities	(111,059)	(63,975)
Financing activities:		
Proceeds from issuance of senior and senior discount notes		550,102
Proceeds from loans payable to banks and long-term debt	191,782	59,324
Repayment of notes payable and long-term debt	(49,408)	(247,820)
Issuance of common stock	170,009	336,957
Payment of debt financing costs		(15,222)
Other		822
Net cash provided by financing activities	312,383	684,163
Effect of exchange rate changes on cash and cash equivalents		(8,119)
Net increase (decrease) in cash and cash equivalents	(38,575)	579,127
Cash and cash equivalents at beginning of period	338,878	44,109
Cash and cash equivalents at end of period	\$ 300,303	\$ 623,236

See accompanying notes to condensed consolidated financial statements.

Table of Contents

LEAP WIRELESS INTERNATIONAL, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. The Company and Basis of Presentation

The Company and Nature of Business

Leap Wireless International, Inc., a Delaware corporation, together with its wholly owned subsidiaries (the Company or Leap) is a wireless communications carrier that offers digital wireless service in the United States under the brand Cricket. The Company also has a 20.1% interest in Pegaso Telecomunicaciones, S.A. de C.V. (Pegaso), a Mexican corporation that operates a wireless network in Mexico. From April 1999 to the date of sale on June 2, 2000, the Company owned 100% of Smartcom, S.A. (Smartcom), a Chilean corporation that operates a nationwide wireless network in Chile.

Interim Financial Statements

The accompanying interim condensed consolidated financial statements have been prepared by the Company without audit, in accordance with the instructions to Form 10-Q and, therefore, do not include all information and footnotes necessary for a fair presentation of its financial position, results of operations, cash flows and stockholders' equity in accordance with generally accepted accounting principles. In the opinion of management, the unaudited financial information for the interim periods presented reflects all adjustments (which include only normal, recurring adjustments) necessary for a fair presentation. These condensed consolidated financial statements and notes thereto should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2000 filed with the Securities and Exchange Commission (SEC) on March 2, 2001 and Amendment No. 1 thereto filed on Form 10-K/A with the SEC on June 28, 2001. Operating results for interim periods are not necessarily indicative of operating results for an entire fiscal year. The Company recognizes its share of net earnings or losses of its foreign operating companies on a three-month lag.

Revenues and Cost of Revenues

Wireless services are provided on a month-to-month basis and are generally paid in advance. The Company does not charge fees for the initial activation of service. Revenues from wireless services are recognized as services are rendered. Amounts received in advance are recorded as deferred revenue. Cost of service generally includes direct costs and related overhead, excluding depreciation and amortization, of operating the Company's networks.

Equipment revenues arise from the sale of handsets and accessories. Revenues and related costs from the sale of handsets are recognized when service is activated by customers. Revenues and related costs from the sale of accessories are recognized at the point of sale. The costs of handsets and accessories sold are recorded in cost of equipment. Handsets sold to third party dealers and distributors are recognized as inventory until they are sold to and activated by customers. Amounts due from third party dealers and distributors for handsets are recorded as deferred revenue upon shipment by the Company and are recognized as equipment revenues when service is activated by customers. Sales incentives offered without charge to customers related to the sale of handsets are recognized as a reduction of revenue when the related equipment revenue is recognized. Customers have limited rights to return handsets and accessories based on time and/or usage. The Company records an estimate for returns at the time of recognizing revenue. Returns have historically been insignificant.

Basic and Diluted Net Income (Loss) Per Common Share

Basic earnings per common share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the reporting period. Diluted earnings per common share reflects the potential dilutive effect of additional common shares that are issuable upon exercise of outstanding

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

stock options and warrants calculated using the treasury stock method. A reconciliation of weighted average shares outstanding used in calculating basic and diluted income (loss) per share is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
	(Unaudited)			
Weighted average shares outstanding basic earnings per share	36,310	26,524	32,909	24,826
Effect of dilutive securities:				
Employee stock options				3,046
Qualcomm warrant				4,085
Chase Telecommunications Holdings warrant				74
Qualcomm Trust Convertible Preferred Securities				103
Adjusted weighted average shares outstanding diluted earnings per share	36,310	26,524	32,909	32,134

The following shares were not included in the computation of diluted earnings per share as their effect would be antidilutive (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
	(Unaudited)			
Employee stock options	8,161	7,448	8,161	808
Qualcomm warrant	3,375	4,500	3,375	
Senior and senior discount unit warrants	2,830	2,830	2,830	2,830
Chase Telecommunications Holdings warrant	95	203	95	

Basic and diluted net loss per common share are the same for the three and nine months ended September 30, 2001, respectively, as a result of the exclusion of these shares.

Recent Accounting Requirements

In July 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 141 Business Combinations and No. 142 Goodwill and Other Intangible Assets. SFAS No. 141 replaces Accounting Principles Board (APB) Opinion No. 16 and eliminates pooling-of-interests accounting prospectively. It also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS No. 142 changes the accounting for goodwill and intangible assets that are deemed to have indefinite lives from an amortization method to an impairment-only approach. Under SFAS No. 142, goodwill and intangible assets that are deemed to have indefinite lives are required to be tested annually and whenever events or circumstances occur indicating that goodwill might be impaired. SFAS No. 141 and SFAS No. 142 are effective for all business combinations completed after September 30, 2001. Upon adoption of SFAS No. 142, amortization of goodwill recorded for business combinations consummated prior to July 1, 2001 will cease, and intangible assets acquired prior to July 1, 2001 that do not meet the criteria for recognition under SFAS No. 141 will be reclassified to goodwill. Companies are required to adopt SFAS No. 142 for fiscal years beginning after December 15, 2001. The Company

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

will adopt SFAS No. 142 on January 1, 2002. In connection with the adoption of SFAS No. 142, the Company will be required to perform a transitional goodwill impairment

Table of Contents

LEAP WIRELESS INTERNATIONAL, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

assessment. The Company is currently assessing the impact these standards will have on its results of operations and financial position.

In October 2001, the FASB issued SFAS No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets. SFAS No. 144 replaces SFAS No. 121 Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of. SFAS No. 144 applies to all long-lived assets (including discontinued operations) and consequently amends APB Opinion No. 30, Reporting Results of Operations Reporting the Effects of Disposal of a Segment of a Business. SFAS No. 144 develops one accounting model for long-lived assets that are to be disposed of by sale. SFAS No. 144 requires that long-lived assets that are to be disposed of by sale be measured at the lower of book value or fair value less cost to sell. Additionally, SFAS No. 144 expands the scope of discontinued operations to include all components of an entity with operations that (1) can be distinguished from the rest of the entity and (2) will be eliminated from the ongoing operations of the entity in a disposal transaction. SFAS No. 144 is effective for fiscal years beginning after December 15, 2001 and interim periods within those fiscal years. The Company will adopt SFAS No. 144 on January 1, 2002. The Company is currently assessing the impact this standard will have on its results of operations and financial position.

Note 2. Recent and Pending Acquisition, Exchange and Sale of Wireless Licenses

From January 2001 through September 2001, the Company completed the purchase and exchange of wireless licenses in various areas covered by an individual wireless license issued by the Federal Communications Commission (FCC), also known as a basic trading area or BTA and certain wireless information assets for an aggregate of \$230.2 million in cash, net of proceeds, the assumption of debt and other liabilities totaling \$110.2 million (including (1) a promissory note in the principal amount of \$86.5 million with interest at the rate of 10% per annum, with principal and interest payable in quarterly installments, with the first installment of \$48.0 million plus interest paid July 6, 2001, and the final of the three remaining quarterly installments due April 6, 2002, and (2) a convertible note in the principal amount of \$18.0 million with interest at the rate of 8.5% per annum, with principal and interest payable at maturity on June 15, 2002 and the right to convert \$11.0 million of the note at maturity into shares of the Company s common stock for \$45.825 per share, or 240,043 shares), and the issuance of 2,778,534 shares of the Company s common stock with a fair value at the time of purchase of approximately \$82.7 million. Approximately 265,083 shares issued in connection with two of the acquisitions are being held in an escrow account to satisfy potential indemnification obligations of the sellers. The promissory note and convertible note are secured by pledges of the outstanding stock of three wholly owned subsidiaries of the Company, which together own 11 wireless licenses. The Company was the high bidder on 22 wireless licenses in the FCC s broadband PCS auction completed in January 2001 for an aggregate purchase price of \$350.0 million. NextWave Telecommunications, Inc. (NextWave), the former holder of the 22 licenses for which the Company was the high bidder, is a party to litigation challenging the validity of their reacution. On June 22, 2001, the United States Court of Appeals for the D.C. Circuit released a decision supporting NextWave s contention that the FCC violated the U.S. Bankruptcy Code in revoking and reacutioning NextWave s licenses. The FCC has stated that it will seek further judicial review of the D.C. Circuit s decision in the U.S. Supreme Court. There are ongoing discussions surrounding a settlement that, if concluded, would result in the Company acquiring all of these licenses from the FCC for the original bid price. The Company cannot predict what effect the D.C. Circuit s decision, further judicial review, or the settlement discussions will have on it or its ability to obtain the 22 reacutioned licenses.

In July 2001, the Company entered into an agreement to sell wireless licenses for 15 MHz of spectrum in Salt Lake City and Provo, Utah to Cingular Wireless LLC for \$140.0 million in cash. The agreement is subject to customary closing conditions, including the FCC s approval, which was granted on October 4, 2001, becoming a final order and no assurance can be given that the transaction will be completed. If the transaction

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

is completed, the Company will retain wireless licenses for 15 MHz of spectrum in each of Salt Lake City and Provo, Utah to operate existing voice and planned information services products.

Note 3. Investments in and Loans Receivable from Wireless Operating Companies

Prior to the Company's acquisition of substantially all the assets of Chase Telecommunications Holdings, Inc. (Chase Telecommunications Holdings) in March 2000, Chase Telecommunications Holdings was accounted for under the equity method. The Company recorded equity losses from Chase Telecommunications Holdings of \$10.4 million during the three months ended March 31, 2000.

At September 30, 2001, the Company had a 20.1% interest in Pegaso. The Company invested \$100.0 million in Pegaso from June to September 1998 as a founding shareholder. In June, July and August 2001, the Company invested an additional \$10.0 million, \$9.7 million and \$0.9 million, respectively, in Pegaso by purchasing convertible subordinated notes (the Pegaso Notes) pursuant to a \$29.4 million funding commitment that preserved the Company's interest of 20.1%. The Pegaso Notes, due in January 2008, do not accrue interest and are subordinate to other indebtedness of Pegaso. The Pegaso Notes convert into equity of Pegaso on the earlier of December 31, 2002 or immediately prior to the consummation of an acquisition transaction as outlined in the Pegaso Notes. The Company recorded equity losses from Pegaso of \$14.3 million and \$57.6 million during the three and nine months ended September 30, 2001, respectively, and \$25.2 million and \$61.6 million during the three and nine months ended September 30, 2000, respectively.

Condensed combined financial information for the operating companies accounted for under the equity method is summarized as follows (in thousands):

	September 30, 2001	December 31, 2000
	(Unaudited)	
Current assets	\$ 179,475	\$ 106,751
Non-current assets	813,395	678,628
Current liabilities	(542,858)	(300,424)
Non-current liabilities	(569,842)	(312,489)
	<u> </u>	<u> </u>
Total stockholders' capital (deficit)	(119,830)	172,466
Other stockholders' share of capital (deficit)	(95,726)	137,775
	<u> </u>	<u> </u>
Company's share of capital (deficit)	(24,104)	34,691
Convertible subordinated notes	20,542	
	<u> </u>	<u> </u>
Investment in and loans receivable from (committed to) unconsolidated wireless operating company	\$ (3,562)	\$ 34,691
	<u> </u>	<u> </u>

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
	(Unaudited)			
Operating revenues	\$ 51,849	\$ 24,394	\$ 110,047	\$ 51,052
Operating expenses	(135,454)	(89,121)	(363,801)	(242,394)
Other expense, net	(31,536)	(13,337)	(69,158)	(38,663)
Foreign currency transaction gain (losses), net	44,228	(34,857)	36,744	(25,195)
Net loss	(70,913)	(112,921)	(286,168)	(255,200)
Other stockholders' share of net loss	(56,649)	(87,672)	(228,606)	(181,701)
Company's share of net loss	(14,264)	(25,249)	(57,562)	(73,499)
Elimination of intercompany transactions				1,498
Equity in net loss of investments in and loans receivable from and committed to unconsolidated wireless operating companies	\$ (14,264)	\$ (25,249)	\$ (57,562)	\$ (72,001)

Note 4. Long-Term Debt

Long-term debt is summarized as follows (in thousands):

	September 30, 2001	December 31, 2000
	(Unaudited)	
12.5% senior notes, due 2010, effective interest rate of 15.8%	\$ 167,948	\$ 162,939
14.5% senior discount notes, face amount of \$668.0 million, due 2010, effective interest rate of 16.3%	319,902	274,776
Vendor financing agreements, weighted average interest rate of 8.3%	939,460	378,668
U.S. government financing, weighted average effective interest rate of 9.9%	84,598	83,140
Qualcomm term loan, effective interest rate of 12.4%	194	
	1,512,102	899,523
Less current portion	(1,941)	(1,645)
	\$ 1,510,161	\$ 897,878

Qualcomm Term Loan

In January 2001, the Company entered into a secured loan agreement with Qualcomm Incorporated (Qualcomm) under which Qualcomm agreed to loan the Company approximately \$125.3 million to finance its acquisition of wireless licenses in the FCC's broadband PCS auction completed in January 2001. In March 2001, Qualcomm funded borrowings of the full amount available under the agreement by transferring to the Company an FCC auction discount voucher, and the Company issued promissory notes in favor of Qualcomm for an aggregate principal amount of \$126.6 million, representing \$125.3 million for the value of the auction discount voucher and \$1.3 million for a commitment fee due to Qualcomm at the initial borrowing. On August 1, 2001, at the request of Qualcomm, the Company agreed to return the auction discount voucher to Qualcomm and reestablish the availability for either a cash loan or a re-borrowing of the auction discount voucher in the future. The FCC confirmed its consent to the return of the auction discount voucher to Qualcomm on August 8, 2001 and the indebtedness under the \$125.3 million note was canceled.

Table of Contents

LEAP WIRELESS INTERNATIONAL, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 5. Stockholders Equity

Common Stock Purchase Agreement

In December 2000, the Company entered into a common stock purchase agreement with Acqua Wellington North American Equities Fund, Ltd. (Acqua Wellington) under which the Company may, at its discretion, sell up to a maximum of \$125.0 million of registered common stock from time to time over the succeeding 28-month period. Under the agreement, the Company may require Acqua Wellington to purchase between \$10.0 and \$25.0 million of common stock, depending on the market price of its common stock, during each of one or more 18 trading day periods. The Company cannot require Acqua Wellington to purchase its common stock if the market price of the Company's common stock is less than \$15 per share. In addition, the Company may grant to Acqua Wellington an option to purchase up to an equal amount of common stock during the same 18 trading day period. Acqua Wellington purchases the common stock at a discount to its then current market price, ranging from 4.0% to 5.5%, depending on the Company's market capitalization at the time the Company requires Acqua Wellington to purchase its common stock. A special provision in the agreement (as amended and restated) allowed the first sale of common stock under the agreement to be up to \$55.0 million. In January 2001, the Company completed the first sale of its common stock under the agreement, issuing 1,564,336 shares to Acqua Wellington in exchange for \$55.0 million. In July 2001, the Company completed the second sale of its common stock under the agreement, issuing 521,396 shares to Acqua Wellington in exchange for \$15.0 million.

Stockholder Rights Plan

In April 2001, the Company's Board of Directors authorized and approved an increase in the number of shares designated as Series A Junior Participating Preferred Stock from 75,000 to 300,000 shares.

2001 Non-Qualified Stock Option Plan

In April 2001, the Company's Board of Directors adopted the 2001 Non-Qualified Stock Option Plan (the 2001 Non-Qualified Plan) that allows the Board of Directors to grant options to employees, directors and consultants to purchase shares of the Company's common stock. A total of 2,500,000 shares of common stock were reserved for issuance under the 2001 Non-Qualified Plan. Terms of the 2001 Non-Qualified Plan are comparable to the Company's 1998 Stock Option Plan, except that only non-qualified stock options may be granted and the number of options that may be granted to officers and directors is limited under the 2001 Non-Qualified Plan.

Employee Stock Purchase Plan

In April 2001, the Company's stockholders approved an amendment to the Company's 1998 Employee Stock Purchase Plan to increase the number of shares of common stock reserved for issuance under the plan from 200,000 to 500,000.

2001 Executive Officer Deferred Bonus Stock Plan

In April 2001, the Company's stockholders approved the adoption of the Company's 2001 Executive Officer Deferred Bonus Stock Plan, under which 275,000 shares of common stock were reserved for issuance. Terms of the plan are comparable to the Company's Executive Officer Deferred Stock Plan.

Table of Contents

LEAP WIRELESS INTERNATIONAL, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Equity Offering

In May 2001, the Company completed an underwritten public offering of 3,000,000 shares of its common stock at a price of \$33.50 per share. The Company received proceeds of approximately \$97.9 million, net of underwriting discounts and commissions and other offering expenses, from the offering.

Note 6. Commitments and Contingencies

Pegaso has significant financing under two equipment loans and a bridge facility. The Company has guaranteed \$33.0 million of Pegaso's outstanding indebtedness under the bridge facility from Qualcomm. On October 31, 2001, Pegaso failed to make scheduled payments of approximately \$5.7 million under the equipment loans and also failed to meet covenants related to the completion of a strategic sale or merger with a third party under all three of the facilities. Qualcomm has reported that it is currently working with Pegaso and a third party to complete a transaction that would likely result in a sale of the equity the Company has in Pegaso or, alternatively, to assist Pegaso in raising additional funds. The transaction and additional financing are not certain. Pegaso has limited cash available to meet its operating and financing commitments and is therefore dependent on securing additional financing or completing a strategic arrangement with an existing carrier.

On June 2, 2000, the Company completed the sale of Smartcom to Endesa S.A (Endesa). The Company has a \$35.0 million promissory note receivable from Endesa that is subject to a right of set-off to secure indemnification claims under the share purchase agreement for the sale. Endesa has asserted claims against the Company for breach of representations and warranties under the share purchase agreement and has notified the Company that it is offsetting the claims against the entire unpaid balance of the note. The note matured on June 2, 2001 and will remain unpaid until the issues related to the claims are resolved. The Company is contesting Endesa's claims. Management of the Company believes that the ultimate outcome of this matter will not have a material adverse effect on the Company's financial position or results of operations.

In connection with one of the Company's recently completed acquisitions of wireless licenses, the seller has asserted that, based on the results of the FCC auction of wireless licenses completed in January 2001, it is entitled to a purchase price adjustment that would effectively double the purchase price. The parties are in the early stages of an arbitration concerning this claim. Under the terms of the agreement, if the Company is obligated to pay a purchase price adjustment, the Company is entitled to pay such additional amounts in cash or its common stock, at the Company's discretion. The Company believes the seller's position is without merit, and the Company will vigorously defend against the claim of the seller. Management of the Company believes that the ultimate outcome of this matter will not have a material adverse effect on the Company's financial position or results of operations.

Various claims arising in the course of business, seeking monetary damages and other relief, are pending. The amount of the liability, if any, from such claims cannot be determined with certainty; however, management of the Company believes that the ultimate liability for such claims will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Note 7. Supplementary Cash Flow Information (in thousands):**

	Nine Months Ended September 30,	
	2001	2000
	(Unaudited)	
Supplementary disclosure of cash flow information:		
Cash paid for interest	\$ 21,520	\$ 21,322
Cash paid for income taxes	\$ 38,419	\$
Supplementary disclosure of non-cash investing and financing activities:		
Long-term financing to purchase equipment	\$ 349,330	\$ 296,141
Long-term and short-term financing to purchase wireless licenses	105,920	10,467
Long-term financing for auction discount voucher	125,274	
Cancellation of long-term financing for auction discount voucher	(130,216)	
Facility fee due on long-term debt	1,253	1,800
Issuance of common stock for minority interest in subsidiary		45,961
Long-term financing for loans to unconsolidated wireless operating company		10,338
Issuance of common stock to purchase wireless licenses	71,990	10,725
Issuance of notes receivable for sale of Smartcom		143,173
Supplementary disclosure of cash used for acquisitions:		
Total purchase price	\$ 18,675	\$ 152,946
Common stock issued	(10,712)	
Warrant issued for subsidiary company common stock		(15,353)
Liabilities assumed at present value	(5,063)	(131,293)
Cash acquired		(4,973)
	<u> </u>	<u> </u>
Cash used for acquisitions	\$ 2,900	\$ 1,327
	<u> </u>	<u> </u>

Note 8. Segment Data

The Company's current reportable segments are Cricket in the United States and the Company's unconsolidated interest in Pegaso in Mexico. These reportable segments are evaluated separately because each geographic region in which they operate presents different service offerings, marketing strategies and operational issues, as well as distinct economic climates and regulatory constraints. As a result of the Company's June 2000 sale of Smartcom, segment data excludes Smartcom.

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Summary information by segment is as follows (in thousands):

	As of and for the Three Months Ended September 30,		As of and for the Nine Months Ended September 30,	
	2001	2000	2001	2000
(Unaudited)				
Cricket:				
Revenues	\$ 66,693	\$ 7,540	\$ 151,292	\$ 17,381
Operating loss	(105,120)	(20,190)	(226,482)	(48,827)
Depreciation and amortization	(30,637)	(3,389)	(65,203)	(12,151)
Capital expenditures	(199,349)	(207,429)	(477,270)	(291,518)
Purchase of wireless licenses		(37,355)	(410,345)	(110,509)
Total assets	1,714,496	914,090	1,714,496	914,090
Pegaso:				
Revenues	51,849	24,394	110,047	48,081
Operating loss	(83,605)	(64,727)	(253,754)	(181,012)
Depreciation and amortization	(19,869)	(12,613)	(49,703)	(27,228)
Capital expenditures	(41,755)	(35,253)	(205,589)	(122,681)
Total assets	992,870	754,727	992,870	754,727

A reconciliation of the Company's segment revenues, operating losses and depreciation and amortization to the corresponding consolidated amounts is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
(Unaudited)				
Segment revenues	\$ 118,542	\$ 31,934	\$ 261,339	\$ 65,462
Revenues of unconsolidated wireless operating companies	(51,849)	(24,394)	(110,047)	(51,052)
Smartcom				21,645
Consolidated revenues	\$ 66,693	\$ 7,540	\$ 151,292	\$ 36,055
Segment operating losses	\$(188,725)	\$(84,917)	\$(480,236)	\$(229,839)
Operating losses of unconsolidated wireless operating companies	83,605	64,727	253,754	191,342
Smartcom				(38,137)
Corporate and other	(13,646)	(5,406)	(32,326)	(22,858)
Consolidated operating loss	\$(118,766)	\$(25,596)	\$(258,808)	\$ (99,492)
Segment depreciation and amortization	\$ (50,506)	\$ (16,002)	\$(114,906)	\$ (39,379)
Depreciation and amortization of unconsolidated wireless operating companies	19,869	12,613	49,703	32,371

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

Smartcom				(15,033)
Corporate and other	(2,857)	(184)	(3,589)	4,790
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Consolidated depreciation and amortization	\$ (33,494)	\$ (3,573)	\$ (68,792)	\$ (17,251)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Note 9. Subsidiary Guarantee**

The Company's senior notes and senior discount notes are guaranteed by its wholly owned subsidiary, Cricket Communications Holdings, Inc. (Cricket Communications Holdings). Condensed consolidating financial information of Leap, Cricket Communications Holdings and non-guarantor subsidiaries of Leap as of September 30, 2001 and December 31, 2000 and for the three and nine months ended September 30, 2001 and 2000, respectively, is presented below. The subsidiaries of Cricket Communications Holdings are not guarantors of the senior notes and senior discount notes and are therefore reflected as investments accounted for under the equity method of accounting in the Cricket Communications Holdings financial information.

Balance Sheet Information as of September 30, 2001 (unaudited, in thousands):

	Leap	Cricket Communications Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Assets					
Cash and cash equivalents	\$ 211,480	\$	\$ 88,823	\$	\$ 300,303
Short-term investments	15,020		27,169		42,189
Inventories			34,831		34,831
Note receivable, net			33,284		33,284
Other current assets	4,574		11,259		15,833
Total current assets	231,074		195,366		426,440
Property and equipment, net	3,163		855,095		858,258
Investment in and loans receivable from subsidiaries and unconsolidated wireless operating company	593,991	(16,584)		(577,407)	
Wireless licenses, net	18,822		668,812		687,634
Goodwill and other intangible assets, net	180		80,485	(35,367)	45,298
Restricted investments	54,182				54,182
Deposits for wireless licenses	85,000				85,000
Other assets	22,684		8,774		31,458
Total assets	\$ 1,009,096	\$ (16,584)	\$ 1,808,532	\$ (612,774)	\$ 2,188,270
Liabilities and Stockholders' Equity					
Accounts payable and accrued liabilities	\$ 4,848	\$	\$ 112,208	\$ (44,134)	\$ 72,922
Other current liabilities	79,669		27,127	(3,562)	103,234
Total current liabilities	84,517		139,335	(47,696)	176,156
Long-term debt	488,044		1,022,117		1,510,161
Other long-term liabilities	755		65,418		66,173
Total liabilities	573,316		1,226,870	(47,696)	1,752,490
Stockholders' Equity:					
Common stock	3		7	(7)	3
Additional paid-in capital	1,147,032	454,667	1,168,688	(1,623,355)	1,147,032
	(6,201)		(6,201)	6,201	(6,201)

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

Unearned stock-based compensation					
Accumulated deficit	(706,555)	(471,251)	(582,301)	1,053,552	(706,555)
Accumulated other comprehensive income	1,501		1,469	(1,469)	1,501
Total stockholders equity	435,780	(16,584)	581,662	(565,078)	435,780
Total liabilities and stockholders equity	\$ 1,009,096	\$ (16,584)	\$ 1,808,532	\$ (612,774)	\$ 2,188,270

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Balance Sheet Information as of December 31, 2000 (in thousands):**

	Leap	Cricket Communications Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Assets					
Cash and cash equivalents	\$ 106,504	\$	\$ 232,374	\$	\$ 338,878
Restricted cash equivalents and short-term investments	13,575				13,575
Short-term investments	16,237		182,869		199,106
Inventories			9,032		9,032
Notes receivable, net			138,907		138,907
Other current assets	1,631		11,115		12,746
	<u>137,947</u>		<u>574,297</u>		<u>712,244</u>
Property and equipment, net	5,763		424,430		430,193
Investments in subsidiaries and unconsolidated wireless operating companies	705,455	338,418	34,691	(1,043,873)	34,691
Wireless licenses, net	25,107		240,528		265,635
Goodwill and other intangible assets, net	3,800		61,162	(34,665)	30,297
Restricted investments	51,896				51,896
Deposits for wireless licenses	91,772				91,772
Other assets	22,268		8,411		30,679
	<u>\$ 1,044,008</u>	<u>\$ 338,418</u>	<u>\$ 1,343,519</u>	<u>\$ (1,078,538)</u>	<u>\$ 1,647,407</u>
Liabilities and Stockholders Equity					
Accounts payable and accrued liabilities	\$ 8,618	\$	\$ 57,150	\$ (7,033)	\$ 58,735
Other current liabilities	12,319		53,371		65,690
	<u>20,937</u>		<u>110,521</u>	<u>(7,033)</u>	<u>124,425</u>
Long-term debt	438,143		459,735		897,878
Other long-term liabilities	1,670		40,176		41,846
	<u>460,750</u>		<u>610,432</u>	<u>(7,033)</u>	<u>1,064,149</u>
Stockholders Equity:					
Common stock	3				3
Additional paid-in capital	893,401	539,578	812,863	(1,352,441)	893,401
Unearned stock-based compensation	(10,019)		(10,019)	10,019	(10,019)
Accumulated deficit	(302,898)	(201,160)	(72,470)	273,630	(302,898)
Accumulated other comprehensive income	2,771		2,713	(2,713)	2,771
	<u>583,258</u>	<u>338,418</u>	<u>733,087</u>	<u>(1,071,505)</u>	<u>583,258</u>

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

Total liabilities and stockholders equity	\$ 1,044,008	\$ 338,418	\$ 1,343,519	\$ (1,078,538)	\$ 1,647,407
---	--------------	------------	--------------	----------------	--------------

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Statement of Operations Information for the Three Months Ended September 30, 2001 (unaudited, in thousands):**

	Leap	Cricket Communications Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues:					
Service revenues	\$	\$	\$ 57,240	\$	\$ 57,240
Equipment revenues			9,453		9,453
Total revenues			66,693		66,693
Operating expenses:					
Cost of service			(29,871)	2,574	(27,297)
Cost of equipment			(53,197)		(53,197)
Selling, general and administrative	(7,478)		(63,993)		(71,471)
Depreciation and amortization	(488)		(33,006)		(33,494)
Total operating expenses	(7,966)		(180,067)	2,574	(185,459)
Operating loss	(7,966)		(113,374)	2,574	(118,766)
Equity in net loss of subsidiaries and unconsolidated wireless operating company	(145,409)	(124,446)	(14,264)	269,855	(14,264)
Interest income	3,601		1,249		4,850
Interest expense	(23,372)		(20,886)		(44,258)
Foreign currency transaction losses, net			136		136
Other income, net	12,405		2,574	(2,574)	12,405
Loss before income taxes	(160,741)	(124,446)	(144,565)	269,855	(159,897)
Income taxes	(1)		(844)		(845)
Net loss	\$(160,742)	\$(124,446)	\$(145,409)	\$269,855	\$(160,742)

Statement of Operations Information for the Three Months Ended September 30, 2000 (unaudited, in thousands):

	Leap	Cricket Communications Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues:					
Service revenues	\$	\$	\$ 5,296	\$	\$ 5,296
Equipment revenues			2,244		2,244
Total revenues			7,540		7,540
Operating expenses:					
Cost of service			(5,845)	339	(5,506)
Cost of equipment			(4,883)		(4,883)
Selling, general and administrative	(4,231)		(14,943)		(19,174)
Depreciation and amortization	(184)		(3,389)		(3,573)

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

Total operating expenses	<u>(4,415)</u>	<u></u>	<u>(29,060)</u>	<u>339</u>	<u>(33,136)</u>
Operating loss	(4,415)		(21,520)	339	(25,596)
Equity in net loss of subsidiaries and unconsolidated wireless operating company	(32,428)	(19,367)	(25,249)	51,795	(25,249)
Interest income	5,161		11,773		16,934
Interest expense	(22,423)		(6,014)		(28,437)
Foreign currency transaction gains, net	3		1,375		1,378
Gain on issuance of stock by unconsolidated wireless operating company			6,898		6,898
Other income (expense), net	30		309	(339)	
Net loss	<u>\$(54,072)</u>	<u>\$(19,367)</u>	<u>\$(32,428)</u>	<u>\$51,795</u>	<u>\$(54,072)</u>

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Statement of Operations Information for the Nine Months Ended September 30, 2001 (unaudited, in thousands):**

	Leap	Cricket Communications Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues:					
Service revenues	\$	\$	\$ 122,449	\$	\$ 122,449
Equipment revenues			28,843		28,843
Total revenues			151,292		151,292
Operating expenses:					
Cost of service			(62,551)	5,548	(57,003)
Cost of equipment			(116,632)		(116,632)
Selling, general and administrative	(19,928)		(147,745)		(167,673)
Depreciation and amortization	(1,031)		(67,761)		(68,792)
Total operating expenses	(20,959)		(394,689)	5,548	(410,100)
Operating loss	(20,959)		(243,397)	5,548	(258,808)
Equity in net loss of subsidiaries and unconsolidated wireless operating company	(337,489)	(270,091)	(57,562)	607,580	(57,562)
Interest income	12,147		11,476		23,623
Interest expense	(72,833)		(50,876)		(123,709)
Foreign currency transaction losses, net			(1,139)		(1,139)
Other income, net	15,987		5,542	(5,548)	15,981
Loss before income taxes	(403,147)	(270,091)	(335,956)	607,580	(401,614)
Income taxes	(510)		(1,533)		(2,043)
Net loss	\$(403,657)	\$(270,091)	\$(337,489)	\$607,580	\$(403,657)

Statement of Operations Information for the Nine Months Ended September 30, 2000 (unaudited, in thousands):

	Leap	Cricket Communications Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues:					
Service revenues	\$	\$	\$ 31,542	\$	\$ 31,542
Equipment revenues			4,513		4,513
Total revenues			36,055		36,055
Operating expenses:					
Cost of service			(14,863)	593	(14,270)
Cost of equipment			(30,851)		(30,851)
Selling, general and administrative	(12,814)		(60,361)		(73,175)
Depreciation and amortization	(528)		(16,723)		(17,251)

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

Total operating expenses	(13,342)		(122,798)	593	(135,547)
Operating loss	(13,342)		(86,743)	593	(99,492)
Equity in net income (loss) of subsidiaries and unconsolidated wireless operating companies	164,215	(60,933)	(72,001)	(103,282)	(72,001)
Interest income	19,132		14,806		33,938
Interest expense	(58,338)		(22,570)		(80,908)
Foreign currency transaction gains, net	3		13,096		13,099
Gain on sale of subsidiary	(4,484)		317,916		313,432
Gain on issuance of stock by unconsolidated wireless operating company			32,602		32,602
Other income, net	599		1,972	(593)	1,978
Income (loss) before income taxes and extraordinary items	107,785	(60,933)	199,078	(103,282)	142,648
Income taxes			(34,548)		(34,548)
Income (loss) before extraordinary items	107,785	(60,933)	164,530	(103,282)	108,100
Extraordinary loss on early extinguishment of debt	(4,422)		(315)		(4,737)
Net income (loss)	\$ 103,363	\$ (60,933)	\$ 164,215	\$ (103,282)	\$ 103,363

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Cash Flow Information for the Nine Months Ended September 30, 2001 (unaudited, in thousands):**

	Leap	Cricket Communications Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Operating activities:					
Net cash provided by (used in) operating activities	\$ 308,805	\$	\$ (548,704)	\$	\$ (239,899)
Investing activities:					
Purchase of property and equipment	(4,878)		(127,940)		(132,818)
Investment in loans to subsidiary and unconsolidated wireless operating company	(100,542)			80,000	(20,542)
Acquisitions, net of cash acquired	(2,900)				(2,900)
Purchase of wireless licenses	(230,876)				(230,876)
Purchase of investments	(14,901)		(102,298)		(117,199)
Sale and maturity of investments	18,285		257,585		275,870
Restricted cash equivalents and investments, net	12,736				12,736
Sale and collection of notes receivable			108,138		108,138
Other	(1,354)		(2,114)		(3,468)
Net cash provided by (used in) investing activities	(324,430)		133,371	80,000	(111,059)
Financing activities:					
Proceeds from long-term debt			191,782		191,782
Repayment of short-term and long-term debt	(49,408)				(49,408)
Parent's investment			80,000	(80,000)	
Issuance of common stock	170,009				170,009
Net cash provided by financing activities	120,601		271,782	(80,000)	312,383
Net increase (decrease) in cash and cash equivalents	104,976		(143,551)		(38,575)
Cash and cash equivalents at beginning of period	106,504		232,374		338,878
Cash and cash equivalents at end of period	\$ 211,480	\$	\$ 88,823	\$	\$ 300,303

Cash Flow Information for the Nine Months Ended September 30, 2000 (unaudited, in thousands):

	Leap	Cricket Communications Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Operating activities:					

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

Net cash provided by (used in) operating activities	\$ (52,899)	\$ _____	\$ 19,957	\$ _____	\$ (32,942)
Investing activities:					
Purchase of property and equipment	(1,916)		(41,770)		(43,686)
Loans to subsidiary and unconsolidated wireless operating company	(378,558)	(368,658)	(8,633)	737,316	(18,533)
Acquisitions, net of cash acquired			(1,327)		(1,327)
Purchase of wireless licenses	(39,364)				(39,364)
Net proceeds from disposal of subsidiary	4,311		210,144		214,455
Purchase of investments	(129,030)		(34,087)		(163,117)
Sale and maturity of investments	43,222		2,268		45,490
Restricted cash equivalents and investments, net	(57,893)				(57,893)
Net cash provided by (used in) investing activities	(559,228)	(368,658)	126,595	737,316	(63,975)
Financing activities:					
Proceeds from issuance of senior and senior discount notes	550,102				550,102
Proceeds from loans payable to banks and long-term debt	31,022		28,302		59,324
Repayment of long-term debt	(229,120)		(18,700)		(247,820)
Issuance of common stock	336,957				336,957
Payment of debt financing costs	(15,222)				(15,222)
Parent company investment		368,658	368,658	(737,316)	
Other			822		822
Net cash provided by financing activities	673,739	368,658	379,082	(737,316)	684,163
Effect of exchange rate changes on cash and cash equivalents			(8,119)		(8,119)
Net increase in cash and cash equivalents	61,612		517,515		579,127
Cash and cash equivalents at beginning of period	35,713		8,396		44,109
Cash and cash equivalents at end of period	\$ 97,325	\$ _____	\$525,911	\$ _____	\$ 623,236

Table of Contents

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

The words Leap, we, our, ours and us refer to Leap Wireless International, Inc. and, unless the context otherwise requires, its consolidated subsidiaries. Unless otherwise specified, information relating to population and potential customers, or POPs, is based on 2001 population estimates provided by Easy Analytic Software Incorporated.

The following information should be read in conjunction with the condensed consolidated financial statements and notes thereto included in Item 1 of this Quarterly Report and the audited consolidated financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Annual Report on Form 10-K for the year ended December 31, 2000, filed with the Securities and Exchange Commission on March 2, 2001 and Amendment No. 1 thereto filed with the SEC on Form 10-K/A on June 28, 2001.

Except for the historical information contained herein, this report, including Management's Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements reflecting management's current forecast of certain aspects of Leap's future. Some forward-looking statements can be identified by forward-looking words such as believe, may, could, will, estimate, continue, anticipate, intend, seek, plan, expect, should, would and similar expressions. This report is based on current information, which we have assessed but by its nature is dynamic and subject to rapid and even abrupt changes. Our actual results could differ materially from those stated or implied by such forward-looking statements due to risks and uncertainties associated with our business. Factors that could cause actual results to differ include, but are not limited to: changes in the economic conditions of the various areas covered by an individual wireless license issued by the Federal Communications Commission and also known as a basic trading area or BTA our subsidiaries serve which could adversely affect the market for wireless services; our ability to access capital markets; a failure to meet the operational, financial or other covenants contained in our credit facilities; our ability to rollout networks in accordance with our plans, including receiving equipment and backhaul and interconnection facilities on schedule from third parties; failure of network systems to perform according to expectations; the effect of competition; the acceptance of our product offering by our target customers; our ability to retain customers; our ability to maintain our cost, market penetration and pricing structure in the face of competition; uncertainties relating to our ability to close pending transactions described in this report; technological challenges in developing wireless information services and customer acceptance of such services if developed; our ability to integrate the businesses and technologies we acquire; rulings by courts or the FCC adversely affecting our rights to own and/or operate certain wireless licenses; the impacts on the global and domestic economies and the financial markets of recent terrorist activities, the ensuing declaration of war on terrorism and the continued threat of terrorist activity and other acts of war or hostility; and other factors detailed in the section entitled Risk Factors included elsewhere in this report and in our other SEC filings. The forward-looking statements should be considered in the context of these risk factors. Investors and prospective investors are cautioned not to place undue reliance on such forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Overview

Leap is a wireless communications carrier that is providing innovative, affordable, simple wireless services designed to accelerate the transformation of wireless service into a mass consumer product. We generally seek to address a much broader population segment than traditional wireless providers have addressed to date. In the U.S., we are offering wireless service under the brand name CricketSM. Our innovative Cricket strategy is designed to extend the benefits of mobility to the mass market by offering wireless service that is as simple to understand and use as, and priced competitively with, traditional landline service. In each of our markets, we are deploying 100% digital, Code Division Multiple Access, or CDMA, networks that we believe provide higher capacity and more efficient deployment of capital than competing technologies. This, when combined with our efforts to streamline operation and distribution systems, allows us to be a low-cost provider of wireless services in each of our markets.

Table of Contents

Cricket service allows customers to make and receive virtually unlimited calls within a local calling area for a low, flat monthly rate compared with traditional wireless services. Cricket customers pay in advance each month's service from a simple, straightforward bill. We offer Cricket service without a term contract, and because service is paid in advance, we currently require no credit check. The simplicity of the Cricket service allows us to sustain lower operating costs per minute of use compared to traditional wireless providers. Our networks are designed and built to provide coverage in the local calling area where our target customers live, work and play. As a result, we believe that our network operating costs are less per minute of use than those of traditional wireless providers.

As of September 30, 2001, we had launched Cricket service in markets covering a total population of approximately 19.5 million potential customers and had approximately 724,000 Cricket customers across the U.S. To date we have acquired or have rights to acquire wireless licenses covering approximately 76.8 million potential customers in 36 states. We plan to continue launching new Cricket markets during the remainder of 2001 and the early part of 2002. Under what we refer to as our 40 market plan, we expect to launch 15 additional markets in the six months after October 1, 2001. Rights to acquire wireless licenses covering approximately 23.8 million potential customers for which we were the high bidder in the FCC's broadband PCS auction completed in January 2001 (Auction 35) are subject to uncertainty as to when and if they will be issued as described below under Recent and Pending Acquisitions and Sale of Wireless Licenses.

We plan to expand our service offerings to include wireless information services designed to appeal to a broad segment of the population. We believe that wireless information services, like our innovative Cricket service, need to be simple, easy to use and affordable for all consumers. In furtherance of this objective, we completed our first purchase of wireless information technology in December 2000 through the acquisition of a proprietary, personalized, location-based technology, and in March and April 2001 we completed two additional acquisitions to support our future offering of wireless information services. We have several new services in development. The first of these services, marketed under the brand name SlicSM, is an information service designed to provide wireless information and advertising to customers' mobile phones. This service was launched in Chattanooga and Nashville, Tennessee in May and June 2001, respectively, in Albuquerque, New Mexico in July 2001, and in Phoenix, Arizona in August 2001.

In Mexico, we were a founding shareholder and have made investments in and have loans and loan commitments to Pegaso Telecomunicaciones, S.A. de C.V. totaling \$129.4 million. Pegaso is a company that is providing a wireless service in Mexico that is more traditional in approach than our Cricket service. Pegaso holds wireless licenses covering all of Mexico, representing approximately 99 million potential customers. At the end of September 2001, Pegaso reported approximately 791,000 customers. We currently own 20.1% of Pegaso.

While we expect our emphasis for the next few years will be on our U.S.-based operations, if presented with attractive opportunities, we may invest in international markets where we believe the combination of unfulfilled demand and our attractive wireless service offerings can fuel rapid growth.

As is typical for start-up telecommunications networks, we expect to incur operating expenses significantly in excess of revenues in each of our markets in their initial period of operation. Operating losses are likely to continue for the next several years as we expand service in new markets and seek to increase our customer base in new and existing markets. We believe, however, that with our simple, easy to understand approach to wireless, we can attract new customers more quickly, maintain lower customer acquisition costs, and sustain lower operating costs per minute of use compared to traditional wireless providers, which will allow us to generate profits in each of our markets sooner than is typical for a traditional wireless provider.

Recent and Pending Acquisition, Exchange and Sale of Wireless Licenses

In April and May 2001, we acquired wireless licenses in various basic trading areas from CenturyTel, Inc. for an aggregate of \$118.7 million in cash and an \$86.5 million secured promissory note with interest at the rate of 10% per annum. Principal and accrued interest under this note are payable in quarterly installments, with the first installment of \$48.0 million plus interest paid July 6, 2001, and the final of the three remaining quarterly installments due April 6, 2002. In addition, from January 2001 through September 2001, we

Table of Contents

completed the purchase and exchange of wireless licenses in various other basic trading areas and certain wireless information assets for an aggregate of \$111.5 million in cash, net of proceeds, the assumption of debt and other liabilities totaling \$23.7 million (including a convertible note in the principal amount of \$18.0 million with interest at the rate of 8.5% per annum, with principal and interest payable at maturity on June 15, 2002 and the right to convert \$11.0 million of the note at maturity into shares of our common stock for \$45.825 per share, or 240,043 shares), and the issuance of 2,778,534 shares of our common stock with a fair value at the time of purchase of approximately \$82.7 million. Approximately 265,083 shares issued in connection with two of the acquisitions are being held in an escrow account to satisfy potential indemnification obligations of the sellers. In connection with one of our recently completed wireless license acquisitions, the seller has asserted that based on the results of the FCC's broadband PCS auction completed in January 2001, it is entitled to a purchase price adjustment that would effectively double the purchase price. The parties are in the early stages of an arbitration concerning this claim. Under the terms of the agreement, if we are obligated to pay a purchase price adjustment, we are entitled to pay such additional amounts in cash or Leap common stock, at our discretion. We believe the seller's position is without merit, and we will vigorously defend against the claim of the seller. Management of Leap believes that the ultimate outcome of this matter will not have a material adverse effect on our financial position or results of operations. We were the high bidder on 22 wireless licenses covering 23.8 million potential customers in the FCC's broadband PCS auction completed in January 2001 for an aggregate purchase price of \$350.0 million. NextWave Telecommunications, Inc., the former holder of the 22 licenses for which we were the high bidder, is a party to litigation challenging the validity of their reacution. On June 22, 2001, the United States Court of Appeals for the D.C. Circuit released a decision supporting NextWave's contention that the FCC violated the U.S. Bankruptcy Code in revoking and reacutioning NextWave's licenses. The FCC has stated that it will seek further judicial review of the D.C. Circuit's decision in the U.S. Supreme Court. There are ongoing discussions surrounding a settlement that, if concluded, would result in our acquiring all of these licenses from the FCC for the original bid price. We cannot predict what effect the D.C. Circuit's decision, further judicial review or the settlement discussions will have on us or our ability to obtain access to the 22 reacutioned licenses. See Risk Factors It May Be More Difficult for Us to Acquire C-Block and F-Block Licenses in the Future described below.

In July 2001, we entered into an agreement to sell wireless licenses for 15MHz of spectrum in Salt Lake City and Provo, Utah to Cingular Wireless LLC for \$140.0 million in cash. The agreement is subject to customary closing conditions, including the FCC's approval, which was granted on October 4, 2001, becoming a final order, and no assurance can be given that the transaction will be completed. If the transaction is completed, we will retain wireless licenses for 15MHz of spectrum in each of Salt Lake City and Provo, Utah to operate existing voice and planned information services products.

Smartcom Disposition

On June 2, 2000, we completed the sale of Smartcom to Endesa S.A. Under the terms of our agreement with Endesa, Endesa purchased all of the outstanding capital stock of Smartcom from our subsidiary, Inversiones Leap Wireless Chile, S.A., and its designated shareholder nominee, in exchange for gross consideration of approximately \$381.5 million, consisting of cash, three promissory notes, the repayment of intercompany debt due to Leap by Smartcom, and the release of cash collateral. In February 2001, we sold one of the promissory notes, with an original principal amount of \$58.2 million plus accrued interest, to a third party for \$60.7 million. In June 2001, Endesa repaid \$47.5 million of principal and accrued interest for the second promissory note. The final remaining promissory note of \$35.0 million is subject to a right of set-off to secure indemnification claims under the share purchase agreement for the sale. Endesa has asserted claims against Leap and Inversiones for breach of representations and warranties under the share purchase agreement and has notified us that it is offsetting the claims against the unpaid balance of the note. The note matured on June 2, 2001 and will remain unpaid until the issues related to the claims are resolved. We are contesting Endesa's claims. Management of Leap believes that the ultimate outcome of this matter will not have a material adverse effect on our financial position or results of operations. We recognized a gain on sale of Smartcom of \$313.4 million before related income tax expense of \$34.5 million during the quarter ended June 30, 2000.

Table of Contents

Presentation

Foreign Subsidiaries

We have recognized our share of net earnings or losses of our foreign operating companies on a three-month lag. The financial statements of Smartcom are included in our consolidated financial statements from June 1, 1999 to March 31, 2000 as a result of our acquisition of the remaining 50% of Smartcom that we did not already own in April 1999 and our sale of 100% of Smartcom on June 2, 2000. The accounts of Smartcom were consolidated using a three-month lag, and as a result of the sale in June 2000, the results of Smartcom for April and May 2000 have been reflected in accumulated deficit during the year ended December 31, 2000. We currently own 20.1% of Pegaso and account for our interest in Pegaso under the equity method of accounting.

Revenues and Cost Recognition

For our Cricket business, revenues include wireless services and the sale of handsets and accessories. Wireless services are provided on a month-to-month basis and are generally paid in advance. We do not charge fees for the initial activation of service. Revenues from wireless services are recognized as services are rendered. Amounts received in advance are recorded as deferred revenue. Cost of service generally includes direct costs and related overhead, excluding depreciation and amortization, of operating our networks. Equipment revenues arise from the sale of handsets and accessories. Revenues and related costs from the sale of handsets are recognized when service is activated by customers. Revenues and related costs from the sale of accessories are recognized at the point of sale. The costs of handsets and accessories sold are recorded in cost of equipment. Handsets sold to third party dealers and distributors are recognized as inventory until they are sold to and activated by customers. Amounts due from third party dealers and distributors for handsets are recorded as deferred revenue upon shipment by us and are recognized as equipment revenues when service is activated by customers. Sales incentives offered without charge to customers related to the sale of handsets are recognized as a reduction of revenue when the related equipment revenue is recognized. Customers have limited rights to return handsets and accessories based on time and/or usage. Returns have historically been insignificant.

Handsets sold through our indirect dealers and distributors are subject to a mark-up which is not included in our equipment revenues. We also deduct from equipment revenues the value of the first month's service, which is included in the price of the handset. We generate revenues from features, including call waiting, caller identification and voicemail. Service revenue is also generated from the customer's usage of long-distance minutes purchased from Cricket and directory assistance.

Results of Operations

Three and Nine Months Ended September 30, 2001 Compared to Three and Nine Months Ended September 30, 2000

At September 30, 2001, customers of our Cricket service rose to approximately 724,000, compared to approximately 62,000 at September 30, 2000. We added approximately 252,000 and 534,000 customers in the three and nine months ended September 30, 2001, respectively, due to increased penetration in existing markets and the launch of new markets, bringing the total potential customer base covered by our networks in 25 markets across the U.S. to approximately 19.5 million. Gross customer additions were approximately 301,000 and 644,000 in the three and nine months ended September 30, 2001, respectively. Weighted average customers were approximately 561,000 for the three months ended September 30, 2001.

During the three and nine months ended September 30, 2001, we generated \$57.2 million and \$122.4 million in service revenues and \$9.5 million and \$28.8 million in equipment revenues, respectively, compared to \$5.3 million and \$10.0 million in service revenues and \$2.2 million and \$4.4 million in equipment revenues, excluding Smartcom, in the corresponding periods of the prior year. The increase in service and equipment revenues over the corresponding periods of the prior year related to the increase in our customer base and the launch of network service in new markets in the U.S. During the three months ended

Table of Contents

September 30, 2001, we launched network service in Phoenix, Arizona and Denver, Colorado, our two largest markets.

During the three and nine months ended September 30, 2001, we incurred \$27.3 million and \$57.0 million in cost of service and \$53.2 million and \$116.6 million in cost of equipment, respectively. During the three and nine months ended September 30, 2000, we incurred \$5.5 million and \$7.3 million in cost of service and \$4.9 million and \$9.1 million in cost of equipment, respectively, excluding Smartcom. We sell our handsets to customers and third party dealers and distributors at prices below cost to grow and maintain our customer base, which is typical of wireless providers. During the three and nine months ended September 30, 2001, \$42.1 million and \$83.8 million of our losses on equipment sales were to acquire new customers, respectively.

Prior to March 17, 2000, we did not report any revenues and related cost of revenues from our Cricket business because Chase Telecommunications, which introduced Cricket service in Chattanooga, Tennessee in March 1999 and Nashville, Tennessee in January 2000, was accounted for under the equity method of accounting.

Selling and marketing expenses were \$32.2 million and \$71.0 million for the three and nine months ended September 30, 2001, respectively, compared to \$4.1 million and \$6.2 million, excluding Smartcom, in the corresponding periods of the prior year. General and administrative expenses were \$39.3 million and \$96.7 million for the three and nine months ended September 30, 2001, respectively, compared to \$15.1 million and \$45.9 million, excluding Smartcom, in the corresponding periods of the prior year. The increase in selling and marketing and general and administrative expenses was due primarily to higher expenses associated with the development and launch of network service in additional markets and the development of new service offerings. For the three and nine months ended September 30, 2001, \$31.2 million and \$68.7 million of selling and marketing expenses were to acquire new customers, respectively. Selling and marketing expenses for the three and nine months ended September 30, 2001 consisted primarily of advertising and public relations and related payroll expenses. General and administrative expenses for the three and nine months ended September 30, 2001 included customer service and billing expenses, costs for business development associated with negotiations for and acquisitions of wireless licenses, government relations, public reporting and investor relations, legal expenses and development of our wireless information service offerings. In addition, we incurred stock-based compensation expense of \$1.2 million and \$4.4 million for the three and nine months ended September 30, 2001, respectively, primarily related to the exchange of stock options from our June 2000 acquisition of the remaining interest in Cricket Communications Holdings that we did not already own. We expect that selling and marketing and general and administrative expenses will continue to increase in the future as a result of our planned network development and launch of Cricket service in additional U.S. markets and the development and launch of our wireless information services.

Depreciation and amortization was \$33.5 million and \$68.8 million for the three and nine months ended September 30, 2001, respectively, compared to \$3.6 million and \$7.3 million, excluding Smartcom, in the corresponding periods of the prior year. The increase in depreciation and amortization resulted from a larger base of equipment and wireless licenses in service compared to the prior year, in addition to amortization of goodwill from our June 2000 acquisition of the remaining interest in Cricket Communications Holdings that we did not already own.

During the three and nine months ended September 30, 2001, our equity share in the net loss of unconsolidated wireless operating company was \$14.3 million and \$57.6 million, respectively, and related only to Pegaso. During the three and nine months ended September 30, 2000, our equity share in the net loss of unconsolidated wireless operating companies was \$25.2 million and \$72.0 million, respectively, and related to Pegaso and Chase Telecommunications Holdings prior to March 2000. In June, July and August 2001, we invested an additional \$10.0 million, \$9.7 million and \$0.9 million, respectively, in Pegaso by purchasing convertible subordinated notes pursuant to a \$29.4 million funding commitment. Our equity share of future net losses of Pegaso will be limited to the extent of our investment, loans and funding commitment.

Interest income was \$4.9 million and \$23.6 million for the three and nine months ended September 30, 2001, respectively, compared to \$16.9 million and \$33.8 million, excluding Smartcom, in the corresponding

Table of Contents

periods of the prior year. The decrease in interest income for the three and nine months ended September 30, 2001 compared to the corresponding periods of the prior year related to decreased average cash and cash equivalents and investment balances following our equity offering and units offering in February 2000, offset by cash and notes receivable related to the sale of Smartcom in June 2000 and proceeds from the sale of stock in our May 2001 underwritten public offering and under our common stock purchase agreement with Acqua Wellington.

Interest expense was \$44.3 million and \$123.7 million for the three and nine months ended September 30, 2001, respectively, compared to \$28.4 million and \$72.4 million, excluding Smartcom, in the corresponding periods of the prior year. The increase in interest expense related primarily to interest on our senior notes and senior discount notes issued in our February 2000 units offering, increased vendor financing of our wireless networks, seller financing of wireless license acquisitions and financing of our auction discount voucher. We expect interest expense to increase substantially in the future due to expected additional borrowings to finance the construction of wireless networks in various markets across the U.S. and the purchase of wireless licenses.

Foreign currency transaction gains (losses) primarily reflected unrealized exchange gains (losses) recognized by Leap and Smartcom on cash balances, payables and loans as a result of changes in the exchange rate between the U.S. dollar and the Chilean peso.

Other income, net, for the three months ended September 30, 2001 includes \$4.9 million related to the reversal of previously recorded interest expense upon the return of an auction discount voucher to Qualcomm and cancellation of related indebtedness in August 2001 and \$7.4 million related to the exchange of wireless licenses. For the nine months ended September 30, 2000, we reported an extraordinary loss on early extinguishment of debt of \$4.7 million, consisting of the write-off of unamortized debt issuance costs in connection with the repayment of our credit agreement with Qualcomm in February 2000 and the repayment of bank loans due to the sale of Smartcom in June 2000.

Consolidation of Smartcom

As a result of the consolidation of Smartcom for the nine months ended September 30, 2000, we recorded \$21.6 million of additional revenues, \$7.0 million of additional cost of service, \$21.8 million of additional cost of equipment, \$9.5 million of additional selling and marketing, \$11.6 million of additional general and administrative, \$10.0 million of additional depreciation and amortization, \$8.4 million of additional net interest expense, and \$10.8 million of additional foreign currency transaction gains, respectively.

Liquidity and Capital Resources

For the 12 months beginning October 1, 2001, we expect to spend a total of approximately \$1,331 million for the following requirements:

approximately \$610 million for capital expenditures for the buildout of our networks and approximately \$250 million to fund operating losses for our voice and wireless information service offerings;

approximately \$422 million in connection with our pending acquisitions and deferred payments of completed acquisitions of wireless licenses and certain wireless information assets, including \$350 million for Auction 35 wireless licenses;

approximately \$9 million to purchase convertible subordinated notes from Pegaso; and

approximately \$40 million for general corporate overhead and other expenses, including increased expenditures for our wireless information service offerings.

Over those 12 months, interest under our senior notes, senior discount notes, vendor facilities and the Qualcomm Term Loan is either deferred and added to principal or otherwise paid from our restricted investment accounts and is therefore not included in this liquidity and capital resources discussion. Our facility with Lucent requires payment of cash interest beginning in November 2002 and principal amortization beginning in December 2002.

Table of Contents

Our planned expenditures may vary over the next 12 months if we determine that we can expand our business more rapidly than currently planned based on the availability of additional capital and our ability to amend the terms of our vendor financing arrangements. Our actual expenditures may also vary significantly depending upon whether we purchase additional wireless licenses, the progress of the buildout of our networks and wireless information services and other factors, including unforeseen delays, cost overruns, unanticipated expenses, regulatory expenses, engineering design changes and other risks. In addition, as our business grows, our net expenditures for operating losses may vary significantly due to variability in our gross revenues and operating expenses, which are affected by various factors including, but not limited to, our subscriber growth, churn, and cost per gross additional customer. On October 31, 2001, Pegaso failed to make scheduled payments of approximately \$5.7 million under two equipment loans and also failed to meet covenants related to the completion of a strategic sale or merger with a third party under those loans and a bridge facility from Qualcomm. We have guaranteed \$33 million of Pegaso's outstanding indebtedness under the bridge facility. We have not included the contingent obligation under this guarantee in our planned expenditures; however, we cannot assure you that it will not become due in the next twelve months.

We have a total of approximately \$1,424 million in unused capital resources for our future cash needs as follows:

approximately \$431 million in consolidated unrestricted cash, cash equivalents, investments and deposits on wireless licenses as of September 30, 2001, including \$85 million on deposit for wireless licenses for which we were the high bidder in the FCC's Auction 35 completed in January 2001;

approximately \$125 million committed under a senior secured financing arrangement with Qualcomm to pay for Auction 35 wireless licenses;

approximately \$726 million in commitments (net of capitalized interest and fees we expect to incur over the next 12 months) under vendor financing arrangements with Lucent Technologies, Inc., Nortel Networks, Inc. and Ericsson Wireless Communications Inc., with availability based on (i) a ratio of the total amounts of products and services purchased and (ii) certain covenants restricting our growth, including but not limited to a covenant on maximum capital expenditures (our current plans are to borrow approximately \$680 million on these facilities in the next twelve months); and

approximately \$142 million in net cash proceeds we expect to receive from agreements to sell wireless licenses, including a July 2001 agreement to sell two wireless licenses to Cingular Wireless LLC (which sale is subject to the FCC's approval, which was granted on October 4, 2001, becoming a final order and other closing conditions).

We also have a \$35 million promissory note receivable from the sale of Smartcom, subject to a right of set-off to secure indemnification claims under the share purchase agreement for the sale. Endesa has asserted claims against Leap and Inversiones for breach of the representations and warranties under the share purchase agreement and has notified us that it is offsetting the claims against the unpaid balance of the note. The note matured on September 2, 2001 and will remain unpaid until the issues related to the claims are resolved. We are contesting Endesa's claims.

According to our estimates, we believe we have sufficient capital resources to build and launch networks and fund operating losses in markets with approximately 38.4 million total potential customers under our 40 market plan. Our networks in these markets are expected to cover approximately 25.2 million potential customers. However, we will need to refinance or extend the amortization schedule of our vendor indebtedness prior to January 2003 or raise additional capital to fund a portion of the principal amortization of our vendor indebtedness. We plan to refinance our vendor indebtedness if market conditions permit. Our ability to refinance our indebtedness will depend on, among other things, our financial condition, the state of the public and private debt and equity markets, the restrictions in the instruments governing our indebtedness and other factors. In addition, if we fail to comply with the covenants governing our indebtedness, we may need additional financing in order to service or extinguish our indebtedness. We may not be able to obtain financing or refinancing on terms that are acceptable to us, or at all.

Table of Contents

Although we expect some of our markets to be cash flow positive during 2001, we expect to incur significant operating losses and to generate significant negative cash flow from operating activities in the future while we continue to buildout our networks and build our customer base. Our ability to satisfy our debt repayment obligations and covenants depends upon our future performance, which is subject to a number of factors, many of which are beyond our control.

If we engage in significant activities in addition to those described above, including launching additional markets, investing in new voice or information services or ventures, or completing additional license purchases for cash, we will need to raise additional capital to fund those activities and amend our vendor financing arrangements to permit additional capital expenditures. We expect that we will require significant additional financing over the next several years to substantially complete the buildout of additional planned wireless networks in the U.S., the acquisition of additional licenses, the buildout of markets related to those additional licenses and the development and launch of additional wireless information services. These capital requirements include license acquisition costs, capital expenditures for network construction, operating cash flow losses and other working capital costs, debt service and closing fees and expenses. Additionally, our existing vendor financing does not allow significant additional growth and we will need to either refinance or amend those facilities to allow for such planned wireless networks. As is typical for start-up wireless communications networks, we expect our networks to incur operating expenses significantly in excess of revenues in their early years of operations. We are exploring potential sales of spectrum assets and public and private debt and equity financing alternatives, including the sale from time to time of convertible preferred stock, convertible debentures and other debt and equity securities. However, we may not be able to sell assets, raise additional capital or refinance or restructure our existing financing facilities on terms that are acceptable to us, or at all.

Credit Facilities and Other Financing Arrangements

Units Offering. In February 2000, we completed an offering of 225,000 senior units, each senior unit consisting of one 12.5% senior note due 2010 (Senior Note) and one warrant to purchase our common stock, and 668,000 senior discount units, each senior discount unit consisting of one 14.5% senior discount note due 2010 (Senior Discount Note) and one warrant to purchase our common stock. The total gross proceeds from the sale of the senior units and senior discount units were \$225.0 million and \$325.1 million, respectively, of which \$164.4 million of the total proceeds was allocated to the fair value of the warrants, estimated using the Black-Scholes option pricing model. The warrants issued in the units offering are exercisable for an aggregate of 2,829,854 shares of our common stock at an exercise price of \$96.80 per share from February 23, 2001 to prior to April 15, 2010. The terms and conditions of the warrants are more fully described in the warrant agreement for the warrants, which is filed as an exhibit to our Annual Report on Form 10-K.

Interest on the Senior Notes is payable semi-annually. The Senior Discount Notes begin accruing cash interest on April 15, 2005, with the first semi-annual interest payment due October 15, 2005. Each Senior Discount Note has an initial accreted value of \$486.68 and a principal amount at maturity of \$1,000. We may redeem any of the notes beginning April 15, 2005. The initial redemption price of the Senior Notes is 106.25% of their principal amount plus accrued interest. The initial redemption price of the Senior Discount Notes is 107.25% of their principal amount at maturity plus accrued interest. In addition, before April 15, 2003, Leap may redeem up to 35% of both the Senior Notes and the Senior Discount Notes using proceeds from certain qualified equity offerings at 112.5% of their principal amount and 114.5% of their accreted value, respectively. The notes are guaranteed by Cricket Communications Holdings. The terms of the notes include certain covenants that restrict Leap's ability to, among other things, incur additional indebtedness, create liens, pay dividends, make investments, sell assets and effect a consolidation or merger. The terms and conditions of the notes are more fully described in the indenture for the notes, which is filed as an exhibit to our Annual Report on Form 10-K.

Common Stock Purchase Agreement. In December 2000, we entered into a common stock purchase agreement with Acqua Wellington North American Equities Fund, Ltd. under which we may, at our discretion, sell up to a maximum of \$125.0 million of registered common stock from time to time over the succeeding 28-month period. Under the agreement, we may require Acqua Wellington to purchase between \$10.0 and \$25.0 million of common stock, depending on the market price of our common stock, during each of

Table of Contents

one or more 18 trading day periods. We cannot require Acqua Wellington to purchase our common stock if the market price of our common stock is less than \$15 per share. In addition, we may grant to Acqua Wellington an option to purchase up to an equal amount of common stock during the same 18 trading day period. Acqua Wellington purchases the common stock at a discount to its then current market price, ranging from 4.0% to 5.5%, depending on our market capitalization at the time we require Acqua Wellington to purchase our common stock. A special provision in the agreement (as amended and restated) allowed the first sale of common stock under the agreement to be up to \$55.0 million. In January 2001, we completed the first sale of our common stock under the agreement, issuing 1,564,336 shares to Acqua Wellington in exchange for \$55.0 million. In July 2001, we completed the second sale of our common stock under the agreement, issuing 521,396 shares of our common stock to Acqua Wellington in exchange for \$15.0 million.

Equity Offering. In May 2001, we completed an underwritten public offering of 3,000,000 shares of our common stock at a price of \$33.50 per share. We received proceeds of approximately \$97.9 million, net of underwriting discounts and commissions and other offering expenses, from the offering.

Vendor Financing. Cricket Communications has entered into purchase agreements and credit facilities with each of Lucent Technologies, Inc., Nortel Networks, Inc. and Ericsson Wireless Communications, Inc. for the purchase of network infrastructure products and services and the financing of these purchases plus additional working capital. Cricket Communications has agreed to purchase up to \$900.0 million of infrastructure products and services from Lucent. The five-year purchase agreement with Lucent is subject to early termination at Cricket Communications' convenience subject to payment for products and services purchased from Lucent. The Lucent credit facility permits up to \$1,350.0 million in total borrowings by Cricket Communications, however, Lucent is not required to make additional loans under the facility if the total of the loans held directly or supported by Lucent exceeds \$815.0 million. In August 2000, Cricket Communications entered into a three-year supply agreement with Nortel for the purchase of infrastructure products and services, and a related credit facility that permits up to \$525.0 million in total borrowings. However, Nortel is not required to make additional loans under the facility if the total of the loans held directly or supported by Nortel exceeds \$300.0 million. In October 2000, Cricket Communications entered into a three-year supply agreement with Ericsson for the purchase of up to \$330.0 million of infrastructure products and services, and a related credit facility with Ericsson Credit AB that permits up to \$495.0 million in total borrowings. Lucent, Nortel and Ericsson have agreed to share collateral and limit total loans by the three vendors to \$1,845.0 million.

Borrowing availability under each credit agreement is generally based on a ratio of the total amount of products and services purchased from the vendor. Each of the credit agreements contain various covenants and conditions typical for loans of this type, including minimum levels of customers and covered potential customers that must increase over time, minimum revenues, limits on annual capital expenditures, dividend restrictions (other than the Nortel agreement) and other financial ratio tests. The obligations under the credit agreements are secured by all of the stock of Cricket Communications, its subsidiaries and the stock of each special purpose subsidiary of Leap formed to hold wireless licenses used in Cricket Communications' business, and all of their respective assets. Although we believe we have sufficient availability under our vendor credit facilities to complete the 40 market plan, we will not be able to draw all of the availability under the vendor credit facilities during the next twelve months because of restrictions imposed by the covenants in these credit agreements and our expectations with respect to product and service purchases from the vendors. Borrowings under each of the credit facilities accrue interest at a rate equal to LIBOR plus 3.5% to 4.25% or a bank base rate plus 2.5% to 3.25%, in each case with the specific rate based on the ratio of total indebtedness to EBITDA. Cricket Communications must pay a commitment fee equal to 1.25% per annum on the unused commitment under the facilities, decreasing to 0.75% per annum. Principal payments under each credit agreement are scheduled to begin three years after the effective date for such credit agreement with a final maturity eight years after such effective date. Repayment is weighted to the later years of the repayment schedule. We plan to refinance these loans if market conditions permit; however, we may not be able to refinance these loans at such time, or at all. At September 30, 2001, Cricket Communications had \$939.5 million outstanding under the vendor credit agreements, at a weighted-average interest rate of 8.3%. In

Table of Contents

addition, at September 30, 2001, we had amounts payable to the vendors that will be financed under the vendor credit agreements of \$59.2 million, which have been included in other long-term liabilities.

Because our new Cricket markets were launched later in the fourth quarter of 2000 than anticipated and because of reduced equipment sales revenues as a result of holiday promotions, Cricket revenue for the quarter ended December 31, 2000 was below the minimum required level contained in the financial covenants in the vendor loan facilities. We received waivers of our failure to meet this revenue target from all of the required lenders. We made up this revenue shortfall and were in compliance with the revenue covenant for the quarters ended March 31, June 30, and September 30, 2001, respectively. In September 2001, we entered into credit agreement amendments that reduced the minimum gross revenue covenant for the third quarter of fiscal 2001 and subsequent quarters. The amendment also reallocated the maximum capital expenditures that Cricket Communications and its subsidiaries can incur in fiscal years 2000 through 2002, reallocating permitted expenditures that are not utilized in fiscal 2000 to fiscal 2001 and providing that permitted expenditures that are not utilized in fiscal 2001 can be carried forward to and utilized in fiscal 2002. There can be no assurance that various circumstances (including additional delays in market launches and/or other adverse results in our business) will not result in a failure to meet our financial or operating covenants in the future. See Risk Factors Our Debt Instruments Contain Provisions and Requirements that Could Limit Our Ability to Pursue Borrowing Opportunities described below.

Qualcomm Term Loan. In January 2001, we entered into a secured loan agreement with Qualcomm under which Qualcomm agreed to loan us approximately \$125.3 million to finance our acquisition of wireless licenses in the FCC's broadband PCS auction completed in January 2001. In March 2001, Qualcomm funded our borrowings of the full amount available under the agreement by transferring to us an FCC auction discount voucher, and we issued promissory notes in favor of Qualcomm for an aggregate principal amount of \$126.6 million, representing \$125.3 million for the value of the auction discount voucher and \$1.3 million for a commitment fee due to Qualcomm at the initial borrowing. On August 1, 2001, at the request of Qualcomm, we agreed to return the auction discount voucher to Qualcomm and reestablish the availability for either a cash loan or a re-borrowing of the auction discount voucher in the future. The FCC confirmed its consent to the return of the auction discount voucher to Qualcomm on August 8, 2001 and the indebtedness under the \$125.3 million note was canceled. Under the terms of the agreement, we must repay to Qualcomm the outstanding principal and accrued interest that may be borrowed under these notes in a single payment no later than five years after the date of the initial borrowing. Loans are subject to mandatory prepayments in certain circumstances, including as a result of our receiving net cash proceeds in excess of \$400.0 million from issuances of debt or equity securities by Leap or its subsidiaries (other than certain excluded issuances such as equipment vendor financing and sales under the Acqua Wellington common stock purchase agreement which are used to acquire wireless licenses). Loans under the agreement bear interest at a variable rate depending on the collateral we provide. We expect this rate to be at LIBOR plus 7.5%. Interest on the loans is payable semi-annually. However, we may elect to defer interest payments through September 2002 and capitalize the deferred interest under the promissory notes. Loans under the agreement will begin to accrue interest from the date we either borrow cash or the date the FCC applies the auction discount voucher against amounts we owe for licenses we acquire through the January 2001 FCC auction. As security for the loans, we have agreed to pledge in favor of Qualcomm the stock of subsidiaries holding licenses that we acquire through the January 2001 FCC auction with an aggregate purchase price of at least 150% of the outstanding principal amount of the loans. The loans are subject to the same covenants that are contained in the Indenture for the high-yield notes issued in our February 2000 units offering, and other customary covenants and conditions.

Debt Obligations to the FCC. We have assumed \$94.8 million (\$85.9 million, net of discount) in debt obligations to the FCC as part of the purchase price for wireless licenses through September 2001. The terms of the notes include interest rates ranging from 6.25% to 9.75% per annum and quarterly principal and interest payments until maturity through July 2007. The notes were discounted using management's best estimate of the prevailing market interest rate to us at the time of purchase of the wireless licenses ranging from 9.75% to 10.75% per annum.

CenturyTel Note. In April and May 2001, we acquired wireless licenses in various basic trading areas from CenturyTel, Inc. for an aggregate of \$118.7 million in cash and an \$86.5 million secured promissory note

Table of Contents

with interest at the rate of 10% per annum. Principal and accrued interest under this note are payable in quarterly installments, with the first installment of \$48.0 million plus interest paid July 6, 2001 and the final of the three remaining quarterly installments due April 6, 2002. The note is secured by a pledge of the outstanding stock of two wholly owned subsidiaries of Leap which together own 10 wireless licenses.

MCG Note. In June 2001, we acquired wireless licenses in Buffalo and Syracuse, New York from MCG PCS, Inc. for an aggregate of \$18.3 million in cash and an \$18.0 million promissory note with interest at the rate of 8.5% per annum, with principal and interest payable at maturity on June 15, 2002. MCG PCS has the right to convert \$11.0 million of the note at maturity into shares of our common stock at \$45.825 per share, or 240,043 shares. The note is secured by a pledge of the outstanding stock of a wholly owned subsidiary of Leap that owns one wireless license.

Pegaso Guarantee. Pegaso has significant financing under two equipment loans and a bridge facility. We have guaranteed \$33.0 million of Pegaso's outstanding indebtedness under the bridge facility from Qualcomm. On October 31, 2001, Pegaso failed to make scheduled payments of approximately \$5.7 million under the equipment loans and also failed to meet covenants related to the completion of a strategic sale or merger with a third party under all three of the facilities. Qualcomm has reported that it is currently working with Pegaso and a third party to complete a transaction that would likely result in a sale of the equity we have in Pegaso or, alternatively, to assist Pegaso in raising additional funds. The transaction and additional financing are not certain. Pegaso has limited cash available to meet its operating and financing commitments and is therefore dependent on securing additional financing or completing a strategic arrangement with an existing carrier.

Pegaso Funding. In June, July and August 2001, we invested an additional \$10.0 million, \$9.7 million and \$0.9 million, respectively, in Pegaso by purchasing convertible subordinated notes pursuant to a \$29.4 million funding commitment that preserved our percentage interest of 20.1%. Our equity share of future net losses of Pegaso will be limited to the extent of our investment, loans and funding commitment. Pegaso requires substantial additional capital to continue its operations and planned growth. As a result, Pegaso is seeking additional debt and equity financing, including additional vendor financing. Leap may contribute capital to Pegaso in the future. If Leap does not contribute additional capital to Pegaso, Leap's ownership interest in Pegaso may be diluted due to additional capital contributions of other investors.

Operating Activities

We used \$239.9 million in cash for operating activities during the nine month period ended September 30, 2001 compared to \$32.9 million in the corresponding period of the prior year. The increase was primarily attributable to increased operating expenses associated with the launch of network service in additional markets in the U.S. We expect that cash used in operating activities is likely to continue to increase for the next several years as we expand service in new markets and seek to increase our customer base in new and existing markets and develop new wireless information services.

Investing Activities

Cash used in investing activities was \$111.1 million during the nine month period ended September 30, 2001 compared to \$64.0 million in the corresponding period of the prior year. Investing activities during the nine month period ended September 30, 2001 consisted primarily of \$108.2 million in proceeds from the sale and repayment of notes receivable from the sale of Smartcom and the sale and maturity of investments of \$275.9 million and restricted cash equivalents of \$12.7 million, offset by the purchase of investments of \$117.2 million, equipment purchases for the continued buildout of planned networks of \$132.8 million, the purchase of wireless licenses of \$230.9 million and the purchase of convertible subordinated promissory notes from Pegaso of \$20.5 million. Investing activities in the corresponding period of the prior year consisted primarily of \$214.5 million in net proceeds from the disposal of Smartcom and other investee companies, offset by \$175.5 million in net purchases of investments and restricted cash equivalents and investments with proceeds from our equity and units offerings, in addition to equipment purchases of \$43.7 million, including purchases related to our Smartcom operations, purchases of wireless licenses of \$39.4 million, and loans to Smartcom and to Chase Telecommunications Holdings.

Table of Contents

Financing Activities

Cash provided by financing activities during the nine month period ended September 30, 2001 was \$312.4 million and consisted of \$170.0 million in proceeds from the sale of common stock, primarily from our May 2001 underwritten public offering and under our common stock purchase agreement with Acqua Wellington, in addition to cash proceeds from loans under our vendor loan facilities for the purchase of property and equipment and wireless licenses of \$191.8 million, partially offset by repayments of notes payable and long-term debt of \$49.4 million. Cash provided by financing activities in the corresponding period of the prior year was \$684.2 million, and consisted primarily of proceeds from our February 2000 public equity offering and units offering and loans from equipment vendors and banks totaling \$931.2 million, partially offset by the repayment of our credit agreements with Qualcomm and other debt totaling \$247.8 million.

Inflation

Inflation has had and may continue to have negative effects on the economies and securities markets of emerging market countries and could have negative effects on Pegaso, including its ability to obtain financing. Mexico, for example, has periodically experienced relatively high rates of inflation. We expect that our foreign subsidiaries, where permitted and subject to competitive pressures, would increase their tariffs to account for the effects of inflation. However, in those jurisdictions where tariff rates are regulated or specified in the wireless license, they may not successfully mitigate the impact of inflation on their operations.

Recent Accounting Requirements

In July 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 141 Business Combinations and No. 142 Goodwill and Other Intangible Assets. SFAS No. 141 replaces Accounting Principles Board (APB) Opinion No. 16 and eliminates pooling-of-interests accounting prospectively. It also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS No. 142 changes the accounting for goodwill and intangible assets that are deemed to have indefinite lives from an amortization method to an impairment-only approach. Under SFAS No. 142, goodwill and intangible assets that are deemed to have indefinite lives are required to be tested annually and whenever events or circumstances occur indicating that goodwill might be impaired. SFAS No. 141 and SFAS No. 142 are effective for all business combinations completed after June 30, 2001. Upon adoption of SFAS No. 142, amortization of goodwill recorded for business combinations consummated prior to July 1, 2001 will cease, and intangible assets acquired prior to July 1, 2001 that do not meet the criteria for recognition under SFAS No. 141 will be reclassified to goodwill. Companies are required to adopt SFAS No. 142 for fiscal years beginning after December 15, 2001. We will adopt SFAS No. 142 on January 1, 2002. In connection with the adoption of SFAS No. 142, we will be required to perform a transitional goodwill impairment assessment. We are currently assessing the impact these standards will have on our results of operations and financial position.

In October 2001, the FASB issued SFAS No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets. SFAS No. 144 replaces SFAS No. 121 Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of. SFAS No. 144 applies to all long-lived assets (including discontinued operations) and consequently amends APB Opinion No. 30, Reporting Results of Operations Reporting the Effects of Disposal of a Segment of a Business. SFAS No. 144 develops one accounting model for long-lived assets that are to be disposed of by sale. SFAS No. 144 requires that long-lived assets that are to be disposed of by sale be measured at the lower of book value or fair value less cost to sell. Additionally, SFAS No. 144 expands the scope of discontinued operations to include all components of an entity with operations that (1) can be distinguished from the rest of the entity and (2) will be eliminated from the ongoing operations of the entity in a disposal transaction. SFAS No. 144 is effective for fiscal years beginning after December 15, 2001 and interim periods within those fiscal years. We will adopt SFAS No. 144 on January 1, 2002. We are currently assessing the impact this standard will have on its results of operations and financial position.

Table of Contents

RISK FACTORS

We Have a Limited Operating History

We have operated as an independent company since September 1998, and we acquired and/or launched all of our existing Cricket markets beginning in January 2000. Because we are at an early stage of development, we face risks generally associated with establishing a new business enterprise. When considering our prospects, investors must consider the risks, expenses and difficulties encountered by companies in their early stages of development. These risks include possible disruptions and inefficiencies associated with rapid growth and workplace expansion, the difficulties associated with raising money to finance new enterprises and the difficulties of establishing a significant presence in highly competitive markets.

Recent Terrorist Activity in the United States and the Military Action to Counter Terrorism Could Adversely Impact our Business.

The September 11, 2001 terrorist attacks in the United States, the ensuing declaration of war on terrorism and the continued threat of terrorist activity and other acts of war or hostility appear to be having an adverse effect on business, financial and general economic conditions in the U.S. These effects may, in turn, result in reduced demand for our products and services, which would have a material adverse effect on our business and results of operations. These circumstances may also adversely affect our ability to attract and retain customers, our ability to raise capital and the operation and maintenance of our networks. The events of September 11, 2001 and use of the term war thereafter could also affect the availability of insurance for various adverse circumstances in the future. At this time, however, we are not able to predict the nature, extent or duration of these effects on overall economic conditions or on our business and operating results.

Our Business Strategy Is Unproven

Our business strategy in the U.S., marketed under the brand name Cricket, is to offer consumers a service plan that allows them to make and receive virtually unlimited local calls for an affordable, flat monthly rate. This strategy, which has been introduced in a limited number of markets, is a new approach to marketing wireless services and may not prove to be successful. Our marketing efforts may not draw the volume of customers necessary to sustain our business plan, our capital and operating costs may exceed planned levels, and we may be unable to compete effectively with landline and other wireless service providers in our markets. In addition, potential customers may perceive the Cricket service to be less appealing than other wireless plans, which offer more features and options, including the ability to roam outside of the home service area. If our business strategy proves to be successful, other wireless providers are likely to adopt similar pricing plans and marketing approaches. Should our competitors choose to adopt a strategy similar to the Cricket strategy, some of them may be able to price their services more aggressively or attract more customers because of their stronger market presence and geographic reach and their larger financial resources. Similarly, we currently have several new services that have either recently been introduced to selected markets or are in development, including a service designed to provide wireless information and advertising to consumers' mobile phones. These new and planned services are innovative and unproven. They may not attract or retain customers at a rate necessary to make them profitable and otherwise may not prove to be successful.

We Have a History of Losses and Anticipate Future Losses

Leap experienced net losses of \$403.7 million in the nine month period ended September 30, 2001, \$269.3 million (excluding the gain on the sale of Smartcom, net of related taxes and foreign currency impact) in the year ended December 31, 2000, \$75.8 million in the transition period from September 1, 1999 to December 31, 1999, \$164.6 million in the year ended August 31, 1999, \$46.7 million in the year ended August 31, 1998 and \$5.2 million in the year ended August 31, 1997. Losses are likely to be significant for the next several years as we launch service in new markets and seek to increase our customer bases in new and existing markets. We may not generate profits in the short term or at all. If we fail to achieve profitability, that failure could have a negative effect on the market value of our common stock.

Table of Contents

If We Experience a High Rate of Customer Turnover, Our Costs Could Increase

Many providers in the U.S. personal communications services, or PCS, industry have experienced a high rate of customer turnover. The rate of customer turnover may be the result of several factors, including limited network coverage, reliability issues such as blocked or dropped calls, handset problems, inability to roam onto cellular networks, affordability, customer care concerns and other competitive factors. Our strategy to address customer turnover may not be successful, or the rate of customer turnover may be unacceptable. In some markets, our competitors have chosen to provide a service plan with pricing similar to the Cricket service, and these competitive factors could also cause increased customer turnover. A high rate of customer turnover could reduce revenues and increase marketing costs in order to attract the minimum number of replacement customers required to sustain our business plan, which, in turn, could have a material adverse effect on our business and financial condition.

We Face Significant Competition

The wireless telecommunications industry generally is very competitive and competition is increasing. Unlike many wireless providers, we also intend to compete directly with landline service providers in the telecommunications industry. Many competitors have substantially greater resources than we have, and we may not be able to compete successfully. Some competitors have announced rate plans substantially similar to the Cricket service plan in markets in which we have launched or expect to launch service. These competitive plans could adversely affect our ability to maintain our pricing, market penetration and customer retention.

In the U.S., we will compete directly with other wireless providers and traditional landline carriers in each of our markets, many of which have greater resources than we do and entered the markets before us. A few of our competitors operate wireless telecommunications networks covering most of the U.S. Our competitors' earlier entry and broader presence in the U.S. telecommunications market may have a negative effect on our ability to successfully implement our strategy. Furthermore, the FCC is actively pursuing policies designed to increase the number of wireless competitors in each of our markets. For example, the FCC has announced that it will auction licenses that will authorize the entry of two additional wireless providers in each market. In addition, other wireless providers in the U.S. either have or could attempt to implement plans substantially similar to our domestic strategy of providing unlimited local service at a low, flat monthly rate. The landline services with which we compete are already used by many of our potential customers, and we may not be successful in our efforts to persuade potential customers to adopt our wireless service in addition to, or in replacement of, their current landline service.

Although the deployment of advanced telecommunications services is in its early stages in many developing countries, we believe competition is increasing as businesses and foreign governments realize the market potential of telecommunications services. In Mexico, a number of international telecommunications companies, including Verizon, AT&T, MCI, Telefonica, Nextel and SBC, as well as local competitors such as Telmex and other Mexican telecommunications companies, continue to actively engage in developing telecommunications services. Pegaso also competes against landline carriers, including government-owned telephone companies. We also expect the prices that Pegaso may charge for its products and services in some regions will decline over the next few years as competition increases. Our competitors in Mexico have greater financial resources and more established operations than Pegaso. Pegaso is at an early stage of development and may not be able to compete successfully.

We compete with companies that use other communications technologies, including paging and digital two-way paging, enhanced specialized mobile radio and domestic and global mobile satellite service. These technologies may have advantages over the technology we use and may ultimately be more attractive to customers. We may compete in the future with companies that offer new technologies and market other services, including cable television access, landline telephone service and Internet access, that we do not currently intend to market. Some of our competitors offer these other services together with their wireless communications service, which may make their services more attractive to customers. In addition, we expect that, over time, providers of wireless communications services will compete more directly with providers of

Table of Contents

traditional landline telephone services. In addition, energy companies, utility companies and cable operators may expand their services to offer communications services.

Leap May Fail to Raise Required Capital

We require significant additional capital to buildout and operate planned networks and for general working capital needs. We also require additional capital to invest in any new wireless opportunities, including capital for license acquisition costs, network buildout of newly acquired licenses and the planned development and rollout of our wireless information services. Capital markets have recently been volatile and uncertain. These markets may not improve, and we may not be able to access these markets to raise additional capital. If we fail to obtain required new financing, that failure would have a material adverse effect on our business and our financial condition. For example, if we are unable to access capital markets, we may have to restrict our activities or sell our interests in licenses, or in one or more of our subsidiaries or other ventures earlier than planned or at a distressed sale price.

Your Ownership Interest in Leap Will Be Diluted Upon Issuance of Shares We Have Reserved for Future Issuance

On November 2, 2001, 36,860,068 shares of our common stock were outstanding, and 19,658,984 additional shares of our common stock were reserved for issuance. The issuance of these additional shares will reduce your percentage ownership in Leap.

The following shares were reserved for issuance as of November 2, 2001:

3,375,000 shares reserved for issuance upon exercise of a warrant issued to Qualcomm in connection with the spin-off of Leap, which is exercisable in whole or in part at any time between now and September 2008;

10,323,467 shares reserved for issuance upon the exercise of options or awards granted or available for grant to employees, officers, directors and consultants under Leap's equity incentive plans;

2,795,621 shares reserved for issuance upon exercise of options to purchase Leap common stock granted to holders of Qualcomm options in connection with the distribution of Leap's common stock to the stockholders of Qualcomm;

240,043 shares reserved for issuance under a convertible promissory note issued in connection with our acquisition of wireless licenses in Buffalo and Syracuse, New York, a portion of which may be converted, at the option of the holder, into shares of common stock in June 2002;

94,999 shares of common stock reserved for issuance upon exercise of a warrant held by Chase Telecommunications Holdings, Inc.; and

2,829,854 shares of common stock reserved for issuance upon exercise of the warrants issued in connection with our February 2000 units offering.

In connection with our recent acquisition of wireless licenses in Buffalo and Syracuse, New York that closed in June 2001, the seller has asserted that based on the results of the FCC auction of wireless licenses completed in January 2001, it is entitled to a purchase price adjustment that would result in the purchase price for such wireless licenses being effectively doubled. The parties are in the early stages of an arbitration concerning this claim. Under the terms of the agreement, if we are obligated to pay a purchase price adjustment, we are entitled to pay such additional amounts in cash or Leap common stock, at our discretion. We believe the seller's position is without merit, and we will vigorously defend against the claim of the seller.

In December 2000, we entered into a common stock purchase agreement with Acqua Wellington under which we may, at our discretion, sell up to a maximum of \$125.0 million of registered common stock from time to time over the succeeding 28-month period. Under the agreement, we may require Acqua Wellington to purchase between \$10.0 million and \$25.0 million of common stock, depending on the market price of our common stock, during each of one or more 18 trading day periods. We cannot require Acqua Wellington to

Table of Contents

purchase our common stock if the market price of our common stock is less than \$15 per share. In addition, we may grant to Acqua Wellington an option to purchase up to an equal amount of common stock during the same 18 trading day period. Acqua Wellington purchases the common stock at a discount to its then current market price, ranging from 4.0% to 5.5%, depending on our market capitalization at the time we require Acqua Wellington to purchase our common stock. A special provision in the agreement (as amended and restated) allowed the first sale of common stock under the agreement to be up to \$55.0 million. In January 2001, we completed the first sale of our common stock under the agreement, issuing 1,564,336 shares to Acqua Wellington in exchange for \$55.0 million. In July 2001, we completed the second sale of our common stock under the agreement, issuing 521,396 shares of our common stock to Acqua Wellington in exchange for \$15.0 million.

An increase in the outstanding number of shares of our common stock could adversely affect prevailing market prices for our common stock and our ability to raise capital through an offering of equity securities.

High Levels of Debt Could Adversely Affect Our Business and Financial Condition

We have obtained and expect to continue to obtain much of our required capital through debt financing. A substantial portion of the debt financing, including all of our vendor financing, bears or is likely to bear interest at a variable rate, exposing us to interest rate risk.

Our high leverage could have important consequences, including the following:

- our ability to obtain additional financing may be impaired;
 - a substantial portion of our future cash flows from operations must be dedicated to the servicing of our debt, thus reducing the funds available for operations and investments;
 - our leverage may reduce our ability to adjust rapidly to changing market conditions and may make us more vulnerable to future downturns in the general economy; and
 - high levels of debt may reduce the value of stockholders' investments in Leap because debt holders have priority regarding our assets in the event of a bankruptcy or liquidation.
- We may not have sufficient future cash flows to meet our debt payments, and may not be able to refinance any of our debt at maturity.

In addition, our vendors have sold outstanding debt under our vendor financing agreements to third parties at a discount and may choose to do so in the future. Such sales could affect the prices at which our outstanding notes trade and could adversely affect the market's perception of Leap's creditworthiness.

Our Debt Instruments Contain Provisions and Requirements that Could Limit Our Ability to Pursue Borrowing Opportunities

The restrictions contained in the indenture governing the notes issued in our February 2000 units offering, and the restrictions contained in our vendor facilities, may limit our ability to implement our business plan, finance future operations, respond to changing business and economic conditions, secure additional financing, if needed, and engage in opportunistic transactions, such as the acquisition of wireless licenses. Such senior debt, among other things, restricts our ability and the ability of our subsidiaries and our future subsidiaries to do the following:

- incur additional indebtedness;
- create liens;
- make certain payments, including payments of dividends and distributions in respect of capital stock;
- consolidate, merge and sell assets;
- engage in certain transactions with affiliates; and
- fundamentally change our business.

Table of Contents

In addition, such senior debt requires us to maintain certain ratios, including:

leverage ratios;

interest coverage ratios; and

fixed charges ratios;

and to satisfy certain tests, including tests relating to:

maximum annual capital expenditures;

minimum covered population;

minimum number of subscribers to our services; and

minimum quarterly revenues and, commencing in 2004, minimum annual revenues.

We expect to make capital expenditures during 2001 and 2002 at or near the maximum annual amount permitted by our vendor loan facilities. Our ability to expand beyond the buildout of networks covering 25 million potential customers planned for launch in 2001 and early 2002 will be significantly restricted if we are not able to obtain additional amendments to the maximum annual capital expenditure covenant contained in our vendor loan facilities. If our growth is so restricted, management of Leap believes that it will not adversely affect our ability to successfully operate the markets we have launched or will launch throughout the remainder of 2001 and early 2002.

We may not satisfy the financial ratios, tests and other covenants under our vendor loan facilities due to events that are beyond our control. If we fail to satisfy any of the financial ratios, tests, or other covenants, we could be in default under our senior debt or may be limited in our ability to access additional funds under our senior debt, which could result in our being unable to make payments on our outstanding notes. In addition, if we fail to meet performance requirements, our equipment financing may be restricted or cancelled. Because Leap's new Cricket markets were launched later in the fourth quarter of 2000 than anticipated and because of reduced equipment sales revenues as a result of holiday promotions, Cricket revenue was below the minimum required level contained in the financial covenants in the vendor loan facilities. Leap received waivers of its failure to meet this revenue target from all of the required lenders. We made up this revenue shortfall in the quarter ended March 31, 2001 and were in compliance with the revenue covenant for the quarters ended June 30, 2001 and September 30, 2001. There can be no assurance that various circumstances (including additional delays in market launches and/or other adverse results in our business) will not result in a failure to meet our financial or operating covenants in the future. Any defaults that result in a suspension of further borrowings under the vendor facilities or acceleration of our obligations to repay the outstanding balances under the vendor facilities would have a material adverse effect on our business and our financial condition.

Because principal amortization of our vendor indebtedness begins in December 2002, we will need to refinance or extend the amortization schedule of our vendor indebtedness prior to January 2003 or raise additional capital to fund a portion of the principal amortization of our vendor indebtedness. In addition, if we fail to comply with the covenants governing our indebtedness, we may need additional financing in order to service or extinguish our indebtedness. We plan to refinance our vendor indebtedness as soon as market conditions permit. However, our ability to refinance our indebtedness will depend on, among other things, our financial condition, the state of the public and private debt and equity markets, the restrictions in the instruments governing our indebtedness and other factors. We may not be able to obtain financing or refinancing on terms that are acceptable to us, or at all.

We May Experience Difficulties in Constructing and Operating Our Telecommunications Networks

We will need to construct new telecommunications networks and expand existing networks. We will depend heavily on suppliers and contractors to successfully complete these complex construction projects. We may experience quality deficiencies, cost overruns and delays on these construction projects, including deficiencies, overruns and delays not within our control or the control of our contractors. We also will depend on third parties not under our control or the control of our contractors to provide backhaul and interconnection facilities on a timely basis. In addition, the construction of new telecommunications networks requires the receipt of permits and approvals from numerous governmental bodies including municipalities and zoning

Table of Contents

boards. There are pressures to limit growth and tower and other construction in many of our markets. Failure to receive these approvals in a timely fashion can delay system rollouts and can raise the costs of completing construction projects. Pegaso's launch of commercial service in Mexico City was delayed several months due to delays in obtaining the required permits from local authorities for cell site construction and some planned 2000 launches were delayed. Some of our planned Cricket launches were delayed and launched with fewer cell sites than desirable and therefore, reduced coverage as well.

We may not complete construction projects within budget or on a timely basis. A failure to satisfactorily complete construction projects could jeopardize wireless licenses and customer contracts. As a result, a failure of this type could have a material adverse effect on our business and financial condition.

Even if we complete construction in a timely and cost effective manner, we will also face challenges in managing and operating our telecommunications systems. These challenges include operating and maintaining the telecommunications operating equipment and managing the sales, advertising, customer support, billing and collection functions of the business. Our failure in any of these areas could undermine customer satisfaction, increase customer turnover, reduce revenues and otherwise have a material adverse effect on our business and financial condition.

We Have Encountered Reliability Problems During the Initial Deployment of Our Networks

As is typical with newly constructed and rapidly expanding wireless networks, we have experienced reliability problems with respect to network infrastructure equipment, reliability of third party suppliers and capacity limitations of our networks. If our networks ultimately fail to perform as expected, that failure could have a material adverse effect on our business and financial condition.

Call Volume Under Cricket Flat Price Plans Could Exceed the Capacity of Our Wireless Networks

Our Cricket strategy in the U.S. is to offer consumers a service plan that allows them to make virtually unlimited local calls for a low, flat monthly rate. Our business plans for this strategy assume that Cricket customers will use their wireless phones for substantially more minutes per month than customers who purchase service from other providers under more traditional plans. Our current plans assume, and our experience has shown, that our Cricket customers use their phones approximately 1,100 minutes per month. We design our U.S. networks to accommodate this expected high call volume. Although we believe CDMA-based networks will be well suited to support high call volumes, if wireless use by Cricket customers exceeds the capacity of our future networks, service quality may suffer, and we may be forced to raise the price of Cricket service to reduce volume or otherwise limit the number of new customers, or incur substantial capital expenditures to expand network capacity. If our planned networks cannot handle the call volumes they experience, our competitive position and business prospects in the U.S. could be materially adversely affected.

We Must Remain Qualified to Hold C-Block and F-Block Licenses

Our business plan depends on our acquisition and operation of C-Block and F-Block licenses in the U.S. We may acquire and operate C-Block and F-Block licenses only if we qualify as a designated entity under FCC rules.

In July 1999, the FCC issued an opinion and order that found that we were entitled to acquire C-Block and F-Block licenses. The order approved our acquisition of the 36 C-Block licenses for which we were the highest bidder in the FCC's 1999 spectrum re-auction, and the transfer of three F-Block licenses which cover portions of North Carolina from AirGate Wireless, L.L.C. to one of our subsidiaries, in each case subject to the fulfillment of certain conditions. In October 1999, the FCC issued to us the 36 re-auctioned licenses. In addition, in March 2000, the FCC approved the transfer to us of 11 C-Block licenses from Chase Telecommunications and one F-Block license from PCS Devco. Subsequently, the FCC has approved the transfer to us of various other C-Block and F-Block licenses.

The FCC's grants of our C-Block and F-Block licenses are subject to certain conditions. Each of the conditions imposed by the FCC in the opinion and order has been satisfied. We have a continuing obligation, during the designated entity holding period for our C-Block and F-Block licenses, to limit our debt to

Table of Contents

Qualcomm to 50% or less of our outstanding debt and to ensure that persons who are or were previously officers or directors of Qualcomm do not comprise a majority of our board of directors or a majority of our officers. If we fail to continue to meet any of the conditions imposed by the FCC or otherwise fail to maintain our qualification to own C-Block and F-Block licenses, that failure could have a material adverse effect on our business and financial condition.

Various parties previously challenged our qualification to hold C-Block and F-Block licenses, which challenges were rejected in the FCC's July 1999 order. One of these parties, a wireless operating company, requested that the FCC review its order, as well as the order consenting to the transfer of licenses to us from Chase Telecommunications and PCS Devco. That wireless operating company also opposed subsequent assignment or transfer applications at the FCC. In July 2000, the FCC affirmed its July 1999 order as well as the order consenting to the transfer of licenses to us from Chase Telecommunications and PCS Devco, and the wireless operating company subsequently appealed the FCC's decision with the U.S. Court of Appeals for the D.C. Circuit. In November 2000, the wireless operating company and Leap executed a settlement agreement that resolves all pending agency or court proceedings brought by the wireless operating company against Leap applications. This agreement was approved by the FCC on March 1, 2001. The wireless operating company has withdrawn all pending agency and judicial challenges to Leap's applications. On March 15, 2001, the U.S. Court of Appeals for the D.C. Circuit issued an order dismissing the wireless operating company's appeal. On April 13, 2001, the FCC issued a public notice officially approving the withdrawal of the wireless operating company's pending petitions to deny and applications for review of our applications. While we believe further review is unlikely, this action may still be subject to additional judicial or administrative review.

Further judicial review of the FCC's orders granting us licenses is possible. In addition, licenses awarded to us at auction may be subject to the outcome of pending judicial proceedings by parties challenging the auction process or the FCC's decision or authority to auction or reacquire certain C-Block and F-Block licenses. We may also be affected by other pending or future FCC, legislative or judicial proceedings that generally affect the rules governing C-Block and F-Block licensees or other designated entities. For example, recent FCC rules changes have made it easier for large companies to acquire C-Block and F-Block licenses at auction and in the aftermarket. The FCC in a pending proceeding has announced that it will modify the cap on the amount of commercial mobile radio services spectrum that any particular carrier may acquire in a wireless market to immediately allow carriers to acquire up to 55 MHz of such spectrum in a market. The FCC also announced that it will phase this cap out entirely effective January 1, 2003, as well as immediately eliminate its cellular cross-interest rule in metropolitan cellular markets. These rule modifications may make it easier for large wireless carriers to consolidate spectrum assets and to acquire smaller wireless carriers, and could adversely affect our entry into new wireless markets.

We may not prevail in connection with any such challenges, appeals or proceedings. If the FCC or a court determines that we are not qualified to hold C-Block or F-Block licenses, it could take the position that some or all of our licenses should be divested, cancelled or reacquired, or that we should pay certain financial penalties.

It May Be More Difficult For Us to Acquire C-Block and F-Block Licenses in the Future

Regulatory changes or requirements, or market circumstances, could make it more difficult to acquire C-Block or F-Block PCS licenses, either at auction or in the aftermarket.

The FCC held a reacquisition of 422 C-Block and F-Block licenses that closed in January 2001. In connection with that reacquisition, the FCC made a number of changes to its wireless and PCS licensing rules, and to the size of the licenses being sold. Specifically, the FCC subdivided the C-Block licenses slated for reacquisition into three 10 MHz licenses. For this reacquisition, the FCC also subdivided the basic trading area, or BTA, service areas to which C-Block and F-Block eligibility restrictions would continue to apply into two tiers according to population. In so-called Tier 1 BTAs, service areas with a population equal to or greater than 2.5 million, the FCC removed all eligibility restrictions on two of the newly-created 10 MHz C-Block licenses, and sold them in open bidding to any entity that could afford to purchase them, no matter how large. In these

Table of Contents

Tier 1 BTAs, one 10 MHz C-Block license remained subject to a closed bidding process, such that only entities meeting C-Block and F-Block eligibility requirements were permitted to bid. In Tier 2 BTAs, service areas with a population less than 2.5 million, two of the 10 MHz C-Block licenses remained subject to C-Block and F-Block eligibility rules and thus were reserved for closed bidding by designated entities, while one 10 MHz C-Block license per BTA was sold at open bidding. Several 15 MHz C-Block licenses and a number of F-Block licenses slated for reauction also were sold at open bidding, such that previous C-Block and F-Block eligibility requirements no longer applied.

The FCC's reauction that closed in January 2001 represented a compromise that made some additional spectrum available to large carriers, but also continued to preserve C-Block and F-Block spectrum for designated entities. The FCC's C-Block and F-Block rules, the recent reauction, and FCC actions taken in connection with previous C-Block auctions and reauctions, remain subject to pending FCC and judicial proceedings. These proceedings, and continuing changes to the C-Block and F-Block rules, could have a material adverse effect on our business and financial condition, including our ability to continue acquiring C-Block and F-Block licenses. In the reauction, we were named the high bidder on 22 licenses covering 23.8 million potential customers.

NextWave Telecommunications, Inc., the former holder of the 22 licenses for which we were the high bidder in the January 2001 reauction, is a party to litigation challenging the validity of their reauction. On June 22, 2001, the United States Court of Appeals for the D.C. Circuit released a decision supporting NextWave's contention that the FCC violated the U.S. Bankruptcy Code in revoking and reauctioning NextWave's licenses. The FCC has sought further judicial review of the D.C. Circuit's decision in the U.S. Supreme Court. We cannot predict what effect the D.C. Circuit's decision or further judicial review will have on us or our ability to retain access to the 22 reauctioned licenses. The FCC is also actively seeking to settle the NextWave litigation, and Congress may attempt to address the litigation legislatively. We cannot predict what effect such actions would have on us or our ability to retain access to the 22 reauctioned licenses for which we were named the high bidder.

While we are in compliance with the terms of our C-Block and F-Block licenses, as a result of the expansion of our business, we have now grown beyond certain designated entity size thresholds specified in FCC rules. This growth will likely preclude our ability to obtain additional C-Block or F-Block licenses that may be auctioned by the FCC in the future. This growth does not preclude us from continuing to acquire C-Block and F-Block licenses in the aftermarket, but we may be subject to unjust enrichment penalties if we seek to acquire C-Block or F-Block licenses from entities that qualify as very small businesses under FCC rules.

We May Not Satisfy the Buildout Deadlines and Geographic Coverage Requirements Applicable to Our Licenses, Which May Result in the Revocation of Some of Our Licenses or the Imposition of Fines and/or Other Sanctions

Each of our licenses is subject to an FCC mandate that we construct PCS networks that provide adequate service to specified percentages of the population in the areas covered by that license, or make a showing of substantial service in that area, within five and ten years after the license grant date. For 30 MHz C-Block licenses, this initial requirement is met when adequate service is offered to at least one-third of the population of the licensed service area. For 15 MHz and 10 MHz C-Block licenses and 10 MHz F-Block licenses, the initial requirement is met when adequate service is provided to at least one-quarter of the population in the licensed service area. Because we obtained many of our wireless licenses from third parties subject to existing buildout requirements, some of our licenses have buildout deadlines in 2001 and several other licenses have buildout deadlines in the first half of 2002. We are unable to predict whether the required coverage will be achieved. For a number of these licenses, we applied for and received from the FCC a limited waiver of the construction requirements; however, failure to comply with the terms of this waiver will mean that the licenses revert back to their original construction deadlines. Failure to comply with FCC buildout requirements could cause the revocation of some of our licenses or the imposition of fines and/or other sanctions.

Table of Contents

Failure to Comply with Regulations or Adverse Regulatory Changes Could Impair Our Ability to Maintain Existing Licenses and Obtain New Licenses

We must maintain our existing telecommunications licenses and those we acquire in the future to continue offering wireless telecommunications services. Changes in regulations or failure to comply with regulations or the terms of a license or failure to have the license renewed could result in a loss of the license, penalties and fines. For example, we could lose a license, or be subject to fines, if we fail to construct or operate a wireless network as required by the license, or if we fail to comply with FCC regulations or compliance deadlines. One such deadline is the requirement that we deploy the capability to identify the precise location of wireless 911 calls by October 1, 2001. Like virtually every other major carrier in the PCS industry, we have sought a waiver from the FCC of this requirement. The loss of a license or the imposition of significant fines or penalties could have a material adverse effect on our business and financial condition.

State regulatory agencies, the FCC, the U.S. Congress, the courts and other governmental bodies regulate the operation of wireless telecommunications systems and the use of licenses in the U.S. The FCC, Congress, the courts or other federal, state or local bodies having jurisdiction over our operating companies may take actions that could have a material adverse effect on our business and financial condition.

Foreign governmental authorities regulate the operation of wireless telecommunications systems and the use of licenses in the foreign countries in which we operate. In some cases, the regulatory authorities also operate our competitors. Changes in the current regulatory environment of these markets could have a negative effect on us. In addition, the regulatory frameworks in some of these countries are relatively new, and the interpretation of regulations is uncertain.

We believe that the process of acquiring new telecommunications licenses will be highly competitive. If we are not able to obtain new licenses, or cannot otherwise participate in companies that obtain new licenses, our ability to expand our operations would be limited.

Risks Associated with Pegaso Could Adversely Affect Our Business

Pegaso has significant financing under two equipment loans and a bridge facility. We have guaranteed \$33.0 million of Pegaso's outstanding indebtedness under the bridge facility from Qualcomm. On October 31, 2001, Pegaso failed to make scheduled payments of approximately \$5.7 million under the equipment loans and also failed to meet covenants related to the completion of a strategic sale or merger with a third party under all three of the facilities. Qualcomm has reported that it is currently working with Pegaso and a third party to complete a transaction that would likely result in a sale of the equity we have in Pegaso or, alternatively, to assist Pegaso in raising additional funds. The transaction and additional financing are not certain. Pegaso has limited cash available to meet its operating and financing commitments and is therefore dependent on securing additional financing or completing a strategic arrangement with an existing carrier.

We face many risks from our international activities. Pegaso in Mexico largely depends on the Mexican economy. The Mexican market is subject to rapid fluctuations in currency exchange rates, consumer prices, inflation, employment levels and gross domestic product.

Mexico's currency and financial markets continue to experience volatility. The impact on the Mexican economy of the economic crisis in Latin America has affected the ability of Mexican companies to access the capital markets. The ability of Mexican companies to access the capital markets may not improve and may deteriorate further in the future. The economy of Mexico historically is affected by fluctuations in the price of oil and petroleum products. Fluctuations in the prices of these products and continuing political tensions in Mexico could negatively impact our prospects in Mexico.

In addition, foreign laws and courts govern many of the agreements of Pegaso. Other parties may breach or may make it difficult to enforce these agreements.

Pegaso requires substantial additional capital to continue its operations and planned growth. If Leap does not contribute additional capital to Pegaso, Leap's ownership interest in Pegaso may be diluted due to additional capital contributions of other investors.

Table of Contents

If presented with attractive opportunities, Leap may invest in additional international markets in the future. Any such international investment would create risks associated with the applicable foreign country's economic condition, including but not limited to currency exchange rates, inflation, employment levels and gross domestic product.

Our Results of Operations May be Harmed by Foreign Currency Fluctuations

We are exposed to risk from fluctuations in foreign currency rates, which could impact our results of operations and financial condition. Although we report our financial statements in U.S. dollars, Pegaso reports its results in Mexican pesos. Consequently, fluctuations in currency exchange rates between the U.S. dollar and the Mexican peso will affect our results of operations as well as the value of our ownership interest in Pegaso. We do not currently hedge against foreign currency exchange rate risks.

Pegaso generates revenues that are paid in Mexican pesos. However, many of Pegaso's major contracts, including financing agreements and contracts with equipment suppliers, are denominated in U.S. dollars. As a result, a significant change in the value of the U.S. dollar against the Mexican peso could significantly increase Pegaso's expenses and could have a material adverse effect on our business and financial condition. For example, Pegaso may be unable to satisfy its obligations under equipment supply agreements denominated in U.S. dollars in the event of currency devaluations. In some developing countries, including Mexico, significant currency devaluations relative to the U.S. dollar have occurred and may occur again in the future. In such circumstances, Leap and Pegaso may experience economic loss with respect to the collectability of payments from their business partners and customers and the recoverability of their investments.

If we invest in other foreign ventures in the future, we will face similar risks relating to the applicable foreign currency of the foreign venture as well as other country-specific risks.

The Technologies that We Use May Become Obsolete, Which Would Limit Our Ability to Compete Effectively

We have employed digital wireless communications technology based on CDMA technology. We are required under an agreement entered into with Qualcomm in connection with our spin-off to use only cdmaOne systems in international operations through January 2004. Other digital technologies may ultimately prove to have greater capacity or features and be of higher quality than CDMA. If another technology becomes the preferred industry standard in any of the countries in which we operate, we may be at a competitive disadvantage, and competitive pressures may require us to change our digital technology at substantial cost. We may not be able to respond to those pressures or implement new technology on a timely basis, or at an acceptable cost. If CDMA technology becomes obsolete at some time in the future, and we are unable to effect a cost-effective migration path, it could materially and adversely affect our business and financial condition.

If Wireless Handsets Pose Health and Safety Risks, We May Be Subject to New Regulations, and Demand for Our Services May Decrease

Media reports have suggested that certain radio frequency emissions from wireless handsets may be linked to various health concerns, including cancer, and may interfere with various electronic medical devices, including hearing aids and pacemakers. Concerns over radio frequency emissions may have the effect of discouraging the use of wireless handsets, which would decrease demand for our services. In recent years, the FCC and foreign regulatory agencies have updated the guidelines and methods they use for evaluating radio frequency emissions from radio equipment, including wireless handsets. In addition, interest groups have requested that the FCC investigate claims that wireless technologies pose health concerns and cause interference with airbags, hearing aids and other medical devices. There also are some safety risks associated with the use of wireless handsets while driving. Concerns over these safety risks and the effect of any legislation that has been and may be adopted in response to these risks could limit our ability to market and sell our wireless service.

Table of Contents

The Loss of Key Personnel Could Harm Our Business

We believe our success depends on the contributions of a number of our key personnel. These key personnel include but are not limited to Harvey P. White, Chairman of the Board and Chief Executive Officer, and Susan G. Swenson, President and Chief Operating Officer. If we lose the services of key personnel, that loss could materially harm our business. We do not maintain key person life insurance on any employee.

Our Stock Price is Volatile

The stock market in general, and the stock prices of telecommunications companies and other technology-based companies in particular, have experienced significant volatility that often has been unrelated to the operating performance of any specific public companies. The market price of Leap common stock has fluctuated widely in the past quarter and calendar year and is likely to continue to fluctuate in the future. Factors that may have a significant impact on the market price of Leap common stock include:

- future announcements concerning Leap or its competitors, including the announcement of joint development efforts;
- changes in the prospects of our business partners or equipment suppliers;
- delays in the construction of planned Cricket networks and in general implementation of our business plan;
- failure to achieve planned levels of subscriber growth and other operating targets;
- deficiencies in our networks;
- results of technological innovations;
- government regulation, including the FCC's review of our acquisition of wireless licenses;
- changes in recommendations of securities analysts and rumors that may be circulated about Leap or its competitors;
- the impact of an economic slowdown on existing and future customers; and
- public perception of risks associated with our international operation.

Our future earnings and stock price may be subject to significant volatility, particularly on a quarterly basis. Shortfalls in our revenues, earnings or subscriber growth or delays in network buildout in any given period relative to the levels and schedule expected by securities analysts could immediately, significantly and adversely affect the trading price of Leap common stock. In the past, following periods of volatility in the market price of a company's securities, class action litigation has often been instituted against the subject company. Litigation of this type could result in substantial costs and a diversion of our management's attention and resources which could, in turn, have a material adverse effect on our business and financial condition.

We Do Not Intend to Pay Dividends in the Foreseeable Future

We do not anticipate paying any cash dividends on our common stock in the foreseeable future. The terms of the indenture governing the notes issued in our February 2000 units offering restrict our ability to declare or pay dividends. We intend to retain future earnings to fund our growth. Accordingly, you will not receive a return on your investment in our common stock through the payment of dividends in the foreseeable future and may not realize a return on your investment even if you sell your shares. Any future payment of dividends to our stockholders will depend on decisions that will be made by our board of directors and will depend on then existing conditions, including our financial condition, contractual restrictions, capital requirements and business prospects.

Table of Contents

We Have Implemented or Are Subject to Anti-Takeover Provisions that Could Prevent or Delay an Acquisition of Leap that Is Beneficial to Our Stockholders

Our charter and bylaws could make it more difficult for a third party to acquire us, even if doing so would benefit our stockholders. Our charter and bylaw provisions could diminish the opportunities for a stockholder to participate in tender offers. The charter and bylaws may also restrain volatility in the market price of our common stock resulting from takeover attempts. In addition, our Board of Directors may issue Preferred Stock that could have the effect of delaying or preventing a change in control of Leap. The issuance of Preferred Stock could also negatively affect the voting power of holders of our common stock. The provisions of the charter and bylaws may have the effect of discouraging or preventing an acquisition of Leap or a sale of our businesses. In addition, Section 203 of the Delaware General Corporation Law imposes restrictions on mergers and other business combinations between us and any holder of 15% or more of our common stock.

We have adopted a rights plan that could discourage, delay or prevent an acquisition of Leap at a premium price. The rights plan provides for Preferred Stock purchase rights attached to each share of our common stock which will cause substantial dilution to a person or group acquiring 15% or more of our stock if the acquisition is not approved by our Board of Directors.

The transfer restrictions imposed on the U.S. wireless licenses we own also adversely affect the ability of third parties to acquire us. Our licenses may only be transferred with prior approval by the FCC. In addition, we are prohibited from voluntarily assigning or transferring control of our C-Block and F-Block licenses for five years after the grant date except to assignees or transferees that satisfy the financial criteria established by the FCC for designated entities, unless we have met the first network buildout deadline applicable to such license. Accordingly, the number of potential transferees of our licenses is limited, and any acquisition, merger or other business combination involving us would be subject to regulatory approval.

In addition, the documents governing our indebtedness contain limitations on our ability to enter into a change of control transaction. Under these documents, the occurrence of a change of control transaction, in some cases after notice and grace periods, would constitute an event of default permitting acceleration of the indebtedness.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Currency Fluctuation and Foreign Exchange Market Risk. We report our financial statements in U.S. dollars. Pegaso reports its results in Mexican pesos. Consequently, fluctuations in currency exchange rates between the U.S. dollar and the Mexican peso may affect our results of operations as well as the value of our ownership interest in Pegaso. Generally, Pegaso generates revenues that are paid in Mexican pesos, but its major contracts, including financing agreements and contracts with equipment suppliers, are denominated in U.S. dollars. As a result, a significant change in the value of the U.S. dollar against the Mexican peso could result in a significant increase in its expenses and could have a material adverse effect on Pegaso and on us. In some emerging markets, including Mexico, significant devaluations of the local currency have occurred and may occur again in the future.

Interest Rate Risk. Our exposure to market risk for changes in interest rates relates primarily to our variable rate long-term debt obligations. The general level of U.S. interest rates and/or LIBOR affect the interest expense that we recognize on our variable rate long-term debt obligations. As of September 30, 2001, the principal amounts of our variable rate long-term debt obligations amounted to approximately \$940.8 million. An increase of 10% in interest rates would increase our interest expense for the next 12 months by approximately \$7.8 million. This hypothetical amount is only suggestive of the effect of changes in interest rates on our results of operations for the next 12 months.

Hedging Policy. As required by our vendor loan agreements, Leap will maintain hedging agreements which fix or limit the interest cost to Cricket Communications and the Leap subsidiaries that guarantee the vendor loans (other than Cricket Communications Holdings, Inc.) to a portion of their long-term indebtedness sufficient to cause 50% of their consolidated long-term indebtedness to be comprised of a combination of (a) indebtedness bearing interest at a fixed rate and (b) indebtedness covered by such hedging agreements. These agreements do not qualify as hedges and to date have been immaterial. In addition, Leap does not engage in hedging activities against foreign currency exchange rate or interest rate risks.

Table of Contents

PART II

OTHER INFORMATION

Item 1. Legal Proceedings.

Various claims arising in the course of business, seeking monetary damages and other relief, are pending. The amount of the liability, if any, from such claims cannot be determined with certainty; however, in the opinion of Leap's management, the ultimate liability for such claims will not have a material adverse effect on Leap's consolidated financial position, results of operations or cash flows.

Item 2. Changes in Securities and Use of Proceeds.

(c) On July 31, 2001, Chase Telecommunications Holdings, Inc. net-exercised a portion of a warrant Leap issued to Chase Telecommunications Holdings in connection with Leap's acquisition of substantially all of its assets in March 2000, and Leap issued 89,345 shares of common stock to Chase Telecommunications Holdings, with Chase Telecommunications Holdings surrendering warrants to purchase 18,222 shares of common stock in payment of the exercise price. The issuance of these shares was deemed to be exempt from registration under the Securities Act in reliance on Section 3(a)(9) of the Securities Act.

Item 3. Defaults Upon Senior Securities.

None.

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

None.

Item 5. Other Information.

On October 23, 2001, Alejandro Burillo Azcárraga resigned from the Board of Directors of Leap to devote his full attention to his business interests in Mexico.

Item 6. Exhibits and Reports on Form 8-K.

(a) *Index to Exhibits:*

Exhibit Number	Description of Exhibit
10.24.1	Amendment No. 1 to System Equipment Purchase Agreement, effective as of December 26, 2000, by and between Cricket Communications, Inc. and Nortel Networks Inc. Portions of this exhibit (indicated by asterisks) have been omitted pursuant to a request for confidential treatment pursuant to Rule 24b-2 under the Securities Exchange Act of 1934.
10.24.2	Amendment No. 2 to System Equipment Purchase Agreement, effective as of September 17, 2001, by and between Cricket Communications, Inc. and Nortel Networks Inc. Portions of this exhibit (indicated by asterisks) have been omitted pursuant to a request for confidential treatment pursuant to Rule 24b-2 under the Securities Exchange Act of 1934.
10.25.2	

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

Second Amendment, dated as of September 17, 2001, to the Credit Agreement, dated as of August 28, 2000, among Cricket Communications Holdings, Inc., Cricket Communications, Inc., the Lenders party thereto and Nortel Networks Inc., as Administrative Agent.

Table of Contents

Exhibit Number	Description of Exhibit
10.26.1	First Amendment, dated as of September 17, 2001, to the Credit Agreement, dated as of September 20, 1999, as Amended and Restated as of October 20, 2000 (the Credit Agreement), among Cricket Communications Holdings, Inc., Cricket Communications, Inc., the Lenders party thereto and Lucent Technologies Inc., as Administrative Agent. The Credit Agreement was filed as an exhibit to Leap s Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2000, as filed with the SEC on November 14, 2000.
10.27.3	Third Amendment, dated as of September 17, 2001, to the Credit Agreement, dated as of October 20, 2000, among Cricket Communications Holdings, Inc., Cricket Communications, Inc., Ericsson Credit AB, the other Lenders party thereto and the Administrative Agent thereunder.
10.30.1(1)	First Amendment to Loan Agreement, dated August 1, 2001, by and among the Registrant, Qualcomm Incorporated, the other lenders party thereto, and Citibank, N.A., as administrative agent for the lenders and as collateral agent for the lenders.
10.30.2(1)	ADV Assignment and Acceptance, dated as of August 1, 2001, between the Registrant and Qualcomm Incorporated.
10.41(1)	Agreement for Purchase and Sale of Licenses, entered into as of July 30, 2001, by and among the Registrant, Cricket Licensee IX, Inc. and Cingular Wireless LLC.

(1) Filed as an exhibit to Leap s Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2001, as filed with the SEC on August 14, 2001, and incorporated herein by reference.

(b) *Reports on Form 8-K.*

(1) Current Report on Form 8-K, dated July 25, 2001, filed with the SEC on July 26, 2001. Item 5 reported, relating to Leap having announced its earnings for the fiscal quarter ended June 30, 2001.

(2) Current Report on Form 8-K, dated September 19, 2001, filed with the SEC on September 20, 2001. Item 5 reported, relating to Leap having entered into amendments to its credit agreements with each of Lucent Technologies Inc., Ericsson Credit AB and Nortel Networks Inc. to, among other things, reduce the requirements for minimum gross revenues and reallocate permitted capital expenditures during fiscal years 2000 through 2002.

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

LEAP WIRELESS INTERNATIONAL, INC.

Date: November 12, 2001

By: /s/ HARVEY P. WHITE

Harvey P. White
Chairman and Chief Executive Officer

Date: November 12, 2001

By: /s/ MANFORD LEONARD

Manford Leonard
Vice President and Corporate Controller
(Chief Accounting Officer)

Table of Contents**EXHIBIT INDEX**

Exhibit Number	Description of Exhibit
10.24.1	Amendment No. 1 to System Equipment Purchase Agreement, effective as of December 26, 2000, by and between Cricket Communications, Inc. and Nortel Networks Inc. Portions of this exhibit (indicated by asterisks) have been omitted pursuant to a request for confidential treatment pursuant to Rule 24b-2 under the Securities Exchange Act of 1934.
10.24.2	Amendment No. 2 to System Equipment Purchase Agreement, effective as of September 17, 2001, by and between Cricket Communications, Inc. and Nortel Networks Inc. Portions of this exhibit (indicated by asterisks) have been omitted pursuant to a request for confidential treatment pursuant to Rule 24b-2 under the Securities Exchange Act of 1934.
10.25.2	Second Amendment, dated as of September 17, 2001, to the Credit Agreement, dated as of August 28, 2000, among Cricket Communications Holdings, Inc., Cricket Communications, Inc., the Lenders party thereto and Nortel Networks Inc., as Administrative Agent.
10.26.1	First Amendment, dated as of September 17, 2001, to the Credit Agreement, dated as of September 20, 1999, as Amended and Restated as of October 20, 2000 (the Credit Agreement), among Cricket Communications Holdings, Inc., Cricket Communications, Inc., the Lenders party thereto and Lucent Technologies Inc., as Administrative Agent. The Credit Agreement was filed as an exhibit to Leap's Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2000, as filed with the SEC on November 14, 2000.
10.27.3	Third Amendment, dated as of September 17, 2001, to the Credit Agreement, dated as of October 20, 2000, among Cricket Communications Holdings, Inc., Cricket Communications, Inc., Ericsson Credit AB, the other Lenders party thereto and the Administrative Agent thereunder.
10.30.1(1)	First Amendment to Loan Agreement, dated August 1, 2001, by and among the Registrant, Qualcomm Incorporated, the other lenders party thereto, and Citibank, N.A., as administrative agent for the lenders and as collateral agent for the lenders.
10.30.2(1)	ADV Assignment and Acceptance, dated as of August 1, 2001, between the Registrant and Qualcomm Incorporated.
10.41(1)	Agreement for Purchase and Sale of Licenses, entered into as of July 30, 2001, by and among the Registrant, Cricket Licensee IX, Inc. and Cingular Wireless LLC.

- (1) Filed as an exhibit to Leap's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2001, as filed with the SEC on August 14, 2001, and incorporated herein by reference.