

LIGHTBRIDGE INC  
Form 10-Q  
November 04, 2005

**Table of Contents**

**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, 2005**

**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: 000-21319**

**LIGHTBRIDGE, INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

(State or Other Jurisdiction of  
Incorporation or Organization)

**04-3065140**

(I.R.S. Employer Identification No.)

**30 Corporate Drive**

**Burlington, Massachusetts 01803**

(Address of Principal Executive Offices) (Zip Code)

**(781) 359-4000**

(Registrant's Telephone Number, Including Area Code)

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

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

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

As of October 31, 2005, there were 26,772,835 shares of the registrant's common stock, \$.01 par value, outstanding.

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**LIGHTBRIDGE, INC.**

**QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 30, 2005**

**TABLE OF CONTENTS**

	<b>Page</b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
<b><u>Item 1. UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS</u></b>	3
<b><u>Balance Sheets as of September 30, 2005 and December 31, 2004</u></b>	3
<b><u>Statements of Operations for the three and nine months ended September 30, 2005 and 2004</u></b>	4
<b><u>Statements of Cash Flows for the nine months ended September 30, 2005 and 2004</u></b>	6

<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	7
<u>Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	17
<u>Item 3. QUANTITATIVE AND QUALITATIVE MARKET RISK DISCLOSURES</u>	39
<u>Item 4. CONTROLS AND PROCEDURES</u>	40
<b><u>PART II. OTHER INFORMATION</u></b>	
<u>Item 1. LEGAL PROCEEDINGS</u>	40
<u>Item 2. CHANGES IN SECURITIES, USE OF PROCEEDS AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	40
<u>Item 6. EXHIBITS</u>	41
<b><u>SIGNATURE</u></b>	
<u>Ex-31.1 Section 302 Certification of CEO</u>	
<u>Ex-31.2 Section 302 Certification of CFO</u>	
<u>Ex-32.1 Section 906 Certification of CEO &amp; CFO</u>	
<u>Ex-99.1 First Amendment to the lease dated May 3, 2005</u>	

**Table of Contents**

**PART I. FINANCIAL INFORMATION**  
**ITEM 1. UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**LIGHTBRIDGE, INC. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**  
(Amounts in thousands, except share and per share amounts)

	<b>September 30, 2005</b>	<b>December 31, 2004</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 75,373	\$ 39,036
Short-term investments	3,056	12,589
Accounts receivable, net	12,159	14,368
Other current assets	1,860	2,189
Current assets retained after sale of INS assets	1,345	5,490
Current assets of discontinued operations		25
Total current assets	93,793	73,697
Property and equipment, net	11,008	15,819
Other assets, net	143	197
Restricted cash	2,100	600
Goodwill	57,628	57,628
Intangible assets, net	19,122	21,247
Non-current assets retained after sale of INS assets	300	753
Non-current assets of discontinued operations		545
Total assets	\$ 184,094	\$ 170,486

**LIABILITIES AND STOCKHOLDERS EQUITY**

Current liabilities:		
Accounts payable	\$ 3,415	\$ 4,530
Accrued compensation and benefits	3,592	4,697
Other accrued liabilities	5,440	3,861
Deferred rent	675	1,592
Deferred revenues	3,014	2,331
Funds due to merchants	6,919	5,558
Accrued restructuring	1,439	2,515
Current liabilities retained after sale of INS assets	963	5,318
Current liabilities of discontinued operations	34	298
Total current liabilities	25,491	30,700

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Deferred rent, less current portion	1,817	2,709
Other long-term liabilities	967	149
Non-current liabilities retained after sale of INS assets	720	
Total liabilities	28,995	33,558
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock, \$.01 par value; 5,000,000 shares authorized; no shares issued or outstanding at September 30, 2005 and December 31, 2004		
Common stock, \$.01 par value; 60,000,000 shares authorized; 30,171,171 and 29,951,826 shares issued and 26,732,128 and 26,512,783 shares outstanding at September 30, 2005 and December 31, 2004, respectively	302	300
Additional paid-in capital	169,111	167,465
Warrants		206
Foreign currency translation	129	(184)
Retained earnings (accumulated deficit)	6,344	(10,072)
Less: treasury stock, at cost	(20,787)	(20,787)
Total stockholders' equity	155,099	136,928
Total liabilities and stockholders' equity	\$ 184,094	\$ 170,486

See notes to unaudited condensed consolidated financial statements.

**Table of Contents**

**LIGHTBRIDGE, INC. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Amounts in thousands, except per share amounts)

	<b>Three Months Ended</b>	
	<b>September 30,</b>	
	<b>2005</b>	<b>2004</b>
Revenues:		
Transaction services	\$ 25,676	\$ 28,285
Consulting and maintenance services	1,556	2,126
Software licensing and hardware		10
Total revenues	27,232	30,421
Cost of revenues:		
Transaction services	11,691	14,074
Consulting and maintenance services	597	1,178
Software licensing and hardware		
Total cost of revenues	12,288	15,252
Gross profit:		
Transaction services	13,985	14,211
Consulting and maintenance services	959	948
Software licensing and hardware		10
Total gross profit	14,944	15,169
Operating expenses:		
Engineering and development	3,502	4,907
Sales and marketing	4,461	5,396
General and administrative	4,113	4,928
Restructuring charges and related asset impairments	1,544	1,969
Total operating expenses	13,620	17,200
Income (loss) from operations	1,324	(2,031)
Other income, net	489	164
Income (loss) from continuing operations before provision for (benefit from) income taxes	1,813	(1,867)

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Provision for (benefit from) income taxes	58	(622)
Income (loss) from continuing operations	1,755	(1,245)
Discontinued operations, net of income taxes	(268)	(3,055)
Net income (loss)	\$ 1,487	\$ (4,300)
Net income (loss) per common shares (basic):		
From continuing operations	\$ 0.07	\$ (0.05)
From discontinued operations	(0.01)	(0.11)
Net income (loss) per common share (basic)	\$ 0.06	\$ (0.16)
Net income (loss) per common share (diluted):		
From continuing operations	\$ 0.06	\$ (0.05)
From discontinued operations	(0.01)	(0.11)
Net income (loss) per common share (diluted):	\$ 0.05	\$ (0.16)
Basic weighted average shares	26,678	26,482
Diluted weighted average shares	27,345	26,482

See notes to unaudited condensed consolidated financial statements.

**Table of Contents**

**LIGHTBRIDGE, INC. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Amounts in thousands, except per share amounts)

	<b>Nine Months Ended September 30,</b>	
	<b>2005</b>	<b>2004</b>
Revenues:		
Transaction services	\$ 76,477	\$ 76,156
Consulting and maintenance services	4,492	8,189
Software licensing and hardware		1,628
Total revenues	80,969	85,973
Cost of revenues:		
Transaction services	35,881	40,422
Consulting and maintenance services	1,919	3,366
Software licensing and hardware		13
Total cost of revenues	37,800	43,801
Gross profit:		
Transaction services	40,596	35,734
Consulting and maintenance services	2,573	4,823
Software licensing and hardware		1,615
Total gross profit	43,169	42,172
Operating expenses:		
Engineering and development	10,978	13,747
Sales and marketing	13,375	13,290
General and administrative	11,734	12,098
Purchased in-process research and development		679
Restructuring charges and related asset impairments	1,920	2,458
Total operating expenses	38,007	42,272
Income (loss) from operations	5,162	(100)
Other income, net	1,079	464
Income from continuing operations before provision for income taxes	6,241	364



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Provision for income taxes	163	55
Income from continuing operations	6,078	309
Discontinued operations, net of income taxes:		
Gain on sale of INS assets	12,689	
Discontinued operations	(2,352)	(4,777)
Total discontinued operations, net of income taxes	10,337	(4,777)
Net income (loss)	\$ 16,415	\$ (4,468)
Net income (loss) per common shares (basic):		
From continuing operations	\$ 0.23	\$ 0.01
From discontinued operations	0.39	(0.18)
Net income (loss) per common share (basic)	\$ 0.62	\$ (0.17)
Net income (loss) per common share (diluted):		
From continuing operations	\$ 0.22	\$ 0.01
From discontinued operations	0.38	(0.18)
Net income (loss) per common share (diluted):	\$ 0.60	\$ (0.17)
Basic weighted average shares	26,631	26,689
Diluted weighted average shares	27,120	26,795

See notes to unaudited condensed consolidated financial statements.

**Table of Contents**

**LIGHTBRIDGE, INC. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Amounts in thousands)**

	<b>Nine Months Ended September 30,</b>	
	<b>2005</b>	<b>2004</b>
Cash flows from operating activities:		
Net income (loss)	\$ 16,415	\$ (4,468)
Income (loss) from discontinued operations	10,337	(4,777)
Income from continuing operations	6,078	309
Adjustments to reconcile net income to net cash provided by operating activities for continuing operations:		
Purchased in-process research and development		679
Depreciation and amortization	6,831	7,059
Deferred income taxes		406
Loss on disposal of property and equipment	8	12
Restructuring charge and related asset impairment	1,920	2,458
Stock compensation expense	414	
Gain on sale of INS assets, net of taxes	(12,689)	
Changes in assets and liabilities:		
Accounts receivable	2,209	3,865
Other assets	(1,301)	104
Accounts payable and accrued liabilities	(3,248)	(2,713)
Funds due to merchants	1,361	767
Deferred rent	(1,075)	
Deferred revenues	1,454	(583)
Other liabilities	818	368
Net cash provided by operating activities of continuing operations	2,780	12,731
Cash flows from investing activities of continuing operations:		
Purchases of property and equipment	(2,232)	(8,874)
Restricted cash	(1,500)	
Purchase of short-term investments	(3,928)	(28,491)
Proceeds from sales and maturities of short-term investments	13,461	83,778
Net cash proceeds from the sale of INS assets	15,017	
Acquisition of Authorize.Net, less cash received		(77,510)
Net cash provided by (used in) investing activities for continuing operations	20,818	(31,097)

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Cash flows from financing activities of continuing operations:		
Proceeds from issuance of common stock	1,028	517
Repurchase of common stock		(3,832)
Net cash provided by (used in) financing activities of continuing operations	1,028	(3,315)
Effects of foreign exchange rate changes on cash and cash equivalents	289	(73)
Net cash provided by (used in) operating activities of net assets retained after sale of INS assets and discontinued operations	11,422	(6,929)
Net cash provided by (used in) investing activities of net assets retained after sale of INS assets and discontinued operations		
Net cash provided by (used in) financing activities of net assets retained after sale of INS assets and discontinued operations		
Net increase (decrease) in cash and cash equivalents	36,337	(28,683)
Cash and cash equivalents, beginning of period	39,036	69,085
Cash and cash equivalents, end of period	\$ 75,373	\$ 40,402

See notes to unaudited condensed consolidated financial statements.

**Table of Contents****LIGHTBRIDGE, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****1. BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements include the accounts of Lightbridge, Inc. and its subsidiaries (collectively, Lightbridge or the Company, and sometimes referred to as we or us). Lightbridge believes that the unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of Lightbridge's financial position, results of operations and cash flows at the dates and for the periods indicated. Although certain information and disclosures normally included in Lightbridge's annual financial statements have been omitted, Lightbridge believes that the disclosures provided are adequate to make the information presented not misleading. Results of interim periods may not be indicative of results for the full year or any future periods. These financial statements should be read in conjunction with the consolidated financial statements and related notes included in Lightbridge's Annual Report on Form 10-K for the year ended December 31, 2004.

Certain prior year amounts in the condensed consolidated financial statements have been reclassified to conform to the current year presentation.

**2. DISCONTINUED OPERATIONS****Intelligent Network Solutions (INS) Business**

On April 25, 2005, the Company announced that it had entered into an asset purchase agreement for the sale of its INS business, which includes its PrePay IN product and related services, to VeriSign, Inc. The sale was completed on June 14, 2005 for \$17.45 million in cash plus assumption of certain contractual liabilities. Of the \$17.45 million in consideration, \$1.495 million is being held in escrow by VeriSign, and \$0.25 million is being held by the Company as a liability to VeriSign, until certain representations and warranties expire after an 18-month period after closing and will be recorded as a gain, net of possible indemnity claims at that time. In addition, a liability has been established of \$0.45 million in accordance with FASB Interpretation No. 45 (FIN 45), Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, based on the estimated cost if the Company were to purchase an insurance policy to cover up to \$5 million of indemnification obligations for certain potential breaches of its intellectual property representations and warranties in the asset purchase agreement with VeriSign. Such representations and warranties extend for a period of two years and expire on June 14, 2007. The operating results and financial condition of the INS segment have been reported as discontinued operations in the accompanying consolidated financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets, as the sale was completed during the second quarter of 2005. All comparative prior period amounts have been restated in a similar manner. The Company recorded a gain on the sale of its INS business of \$12.7 million during the second quarter of 2005, which has been presented as a gain on sale of discontinued operations.

We recorded a net loss from discontinued operations of \$0.3 million for the three months ended September 30, 2005 and recorded a net income from discontinued operations of \$10.3 million for the nine months ended September 30, 2005. The net income from discontinued operations includes the gain on the sale of INS of \$12.7 million and a \$1.4 million settlement of a lawsuit between Lucent Technologies, Inc. and the Company that was finalized in the second quarter of 2005.

The remaining assets and liabilities from the INS business that the Company retained are not significant to the Company's ongoing operations. Accordingly, we have classified the remaining assets and liabilities, principally consisting of accounts receivable, trade payables and restructuring accruals, from the INS business on the Balance Sheet as assets and liabilities related to assets sold. The Company anticipates that all accounts receivable and trade payables will be collected and paid by the end of 2005.

	<b>September 30, 2005</b>	<b>December 31, 2004</b>
Financial position:		
Current assets	\$ 1,345	\$ 5,490

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Other assets		300		753	
Current liabilities		(963)		(5,318)	
Other liabilities		(720)			
Net assets retained after sale of INS assets		\$	(38)	\$	925

**Table of Contents****Instant Conferencing Business**

In the first quarter of 2005, we made the decision to no longer actively market or sell our GroupTalk product and took actions to outsource the continuing operations of our Instant Conferencing segment. On August 17, 2005, we and America Online, Inc. mutually agreed to terminate our master services agreement under which we provided our GroupTalk instant conferencing services to America Online, Inc. We subsequently terminated all of the outsourcing agreements for our GroupTalk services and ceased operations of the Instant Conferencing segment in the third quarter of 2005. All comparative prior period amounts have been restated in a similar manner.

In accordance with SFAS 144, the operating results and financial condition of the Instant Conferencing segment have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements.

	<b>September 30, 2005</b>	<b>December 31, 2004</b>
Financial position:		
Current assets	\$	\$ 25
Other assets		545
Current liabilities	(34)	(298)
Net assets of discontinued operations	\$ (34)	\$ 272

Summarized financial information for the INS and Instant Conferencing discontinued operations are as follows (amounts in thousands):

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>
Results of operations:				
Total Gross Profit (loss)	\$ (134)	\$ 1,645	\$ 4,324	\$ 7,403
Total Operating Expenses	134	4,700	6,676	12,180
Net income (loss)	(268)	(3,055)	(2,352)	(4,777)
Gain on sale of INS			12,689	
Net income (loss) from discontinued operations	\$ (268)	\$ (3,055)	\$ 10,337	\$ (4,777)

**3. BUSINESS ACQUISITION**

On March 31, 2004, the Company acquired all of the outstanding stock of Authorize.Net Corp. ( Authorize.Net ) from InfoSpace, Inc. for \$81.6 million in cash. In addition, the Company incurred approximately \$2.0 million in acquisition related costs. Authorize.Net provides credit card and electronic check payment processing solutions to companies that process orders for goods and services over the Internet, by phone and mail, at retail locations and on wireless devices. Authorize.Net connects IP-enabled businesses to large credit card processors and banking organizations, allowing those businesses to accept electronic payments. The results of operations of Authorize.Net have been included in the Company's financial statements since the date of the acquisition. In connection with the Authorize.Net acquisition, the Company recorded a \$679,000 charge during the first quarter of 2004 for two

in-process research and development ( IPR&D ) projects. Please refer to the Company s 2004 Annual Report on Form 10-K for the year ended December 31, 2004 for a complete description of this acquisition. Please refer to Part II Other Information, Item 1, Legal Proceedings for a discussion of certain pending matters related to the intellectual property of Authorize.Net.

**Pro forma financial information**

The following table presents the unaudited pro forma financial information from continuing operations of the Company including Authorize.Net for the nine months ended September 30, 2004, as if the acquisition had occurred at the beginning of 2004, after giving effect to certain purchase accounting adjustments. The pro forma adjustments include elimination of revenue associated with pre-acquisition deferred revenue of Authorize.Net, amortization of intangible assets, elimination of interest income associated with the cash purchase price of the acquisition and related income tax effects.

**Table of Contents**

The pro forma net loss from continuing operations for the nine months ended September 30, 2004 excludes the expense of IPR&D of \$679,000 related to the Authorize.Net acquisition due to its non-recurring nature. These results are presented for illustrative purposes only and are not necessarily indicative of the actual operating results or financial position that would have occurred if the transaction had been consummated on January 1, 2004 (amounts in thousands, except per share amounts):

Pro forma net revenues	\$ 93,780
Pro forma net loss from continuing operations	\$ 1,711
Pro forma net loss per basic and diluted share from continuing operations	\$ 0.06
Shares used for basic and diluted computation	26,689

**Goodwill impairment analysis**

In accordance with Statement of Financial Accounting Standard No. 142 (SFAS 142), the Company is required to analyze the carrying value of goodwill and other intangible assets against the estimated fair value of those assets for possible impairment on an annual basis. If impairment has occurred, the Company will record a charge in the amount by which the carrying value of the assets exceeds their estimated fair value. Estimated fair value will generally be determined based on discounted cash flows. On March 31, 2005, the Company performed the annual impairment test for the goodwill balance of \$57.6 million related to the acquisition of Authorize.Net. The Company used the discounted cash flow and market methodologies to determine the fair value of the reporting unit related to these intangible assets. The discounted cash flow methodology is based upon converting expected cash flows to present value. A comparison of the resulting fair value of the reporting unit to its carrying amount, including goodwill, indicated that the goodwill balance was not impaired as of March 31, 2005. There have been no events during the quarter that would require us to perform an additional assessment of goodwill.

**4. DISCLOSURES ABOUT SEGMENTS OF AN ENTERPRISE AND RELATED INFORMATION**

Based upon the way financial information is provided to the Company's Chief Executive Officer for use in evaluating allocation of resources and assessing performance of the business, the Company reports its operations in two distinct operating segments, described as follows:

**Payment Processing Services (Payment Processing)** This segment provides a transaction processing system under the Authorize.Net® brand that allows businesses to authorize, settle and manage credit card, electronic check and other electronic payment transactions online.

**Telecom Decisioning Services (TDS)** This segment provides wireless subscriber qualification, risk assessment, fraud screening, consulting services and call center services to telecom and other companies.

In the Company's Annual Report on Form 10-K for the year ended December 31, 2004, and the Company's subsequently filed Quarterly Reports on Form 10-Q, the Company reported segment information for the Intelligent Network Solutions (INS) and the Instant Conferencing Services (Instant Conferencing) businesses as separate segments. The INS business, which the Company sold in the second quarter of 2005, provided wireless carriers with a real-time rating engine for voice, data and IN services for prepaid subscribers, as well as postpaid charging functionality and telecom calling card services. The Instant Conferencing business, the operations of which ceased in the third quarter of 2005, provided managed instant conferencing services through its Lightbridge GroupTalk™ product. The operating results and financial condition of the INS and Instant Conferencing segments have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements and, accordingly, the Company's segment information has been restated. Segment results for the INS and



Instant Conferencing business are no longer provided. All prior period segment financial information has been restated to conform with the current presentation. See Note 2, Discontinued Operations, for additional information about these businesses.

The Company also announced on April 25, 2005 that it would evaluate strategic alternatives for its TDS business and had engaged investment bankers to investigate a range of possibilities for the TDS business.

Within segments, performance is measured based on revenue, gross profit and operating income (loss) realized from each segment. There are no transactions between segments. The Company generally does not allocate corporate or centralized marketing and general and administrative expenses to its business unit segments, because these activities are managed separately from the business units. Also, the Company does not allocate restructuring expenses and other non-recurring gains or charges to its business unit segments because the Company's Chief Executive Officer evaluates the segment results exclusive of these items. Asset information by operating segment is not reported to or reviewed by the Company's Chief Executive Officer, and therefore the Company has not disclosed asset information for each operating segment.

**Table of Contents**

Financial information for each reportable segment from continuing operations as restated for the three and nine months ended September 30, 2005, and 2004 were as follows (amounts in thousands):

<b>Three Months Ended September 30, 2005</b>	<b>TDS</b>	<b>Payment Processing</b>	<b>Sub-total Reportable Segments</b>	<b>Reconciling Items</b>	<b>Consolidated Total</b>
Revenues	\$15,518	\$ 11,714	\$ 27,232	\$	\$ 27,232
Gross profit	5,776	9,168	14,944		14,944
Operating income (loss)	2,859	3,255	6,114	(4,790)(1)	1,324
Depreciation and amortization	992	1,035	2,027	166(2)	2,193

<b>Three Months Ended September 30, 2004</b>	<b>TDS</b>	<b>Payment Processing</b>	<b>Sub-total Reportable Segments</b>	<b>Reconciling Items</b>	<b>Consolidated Total</b>
Revenues	\$21,582	\$ 8,839	\$ 30,421	\$	\$ 30,421
Gross profit	8,969	6,200	15,169		15,169
Operating income (loss)	3,880	876	4,756	(6,787)(1)	(2,031)
Depreciation and amortization	1,353	1,009	2,362	213(2)	2,575

<b>Nine Months Ended September 30, 2005</b>	<b>TDS</b>	<b>Payment Processing</b>	<b>Sub-total Reportable Segments</b>	<b>Reconciling Items</b>	<b>Consolidated Total</b>
Revenues	\$48,408	\$ 32,561	\$ 80,969	\$	\$ 80,969
Gross profit	17,727	25,442	43,169		43,169
Operating income (loss)	8,538	7,805	16,343	(11,181)(1)	5,162
Depreciation and amortization	3,123	3,121	6,244	587(2)	6,831

<b>Nine Months Ended September 30, 2004</b>	<b>TDS</b>	<b>Payment Processing</b>	<b>Sub-total Reportable Segments</b>	<b>Reconciling Items</b>	<b>Consolidated Total</b>
Revenues	\$68,996	\$ 16,977	\$ 85,973	\$	\$ 85,973
Gross profit	30,027	12,145	42,172		42,172
Operating income (loss)	13,922	1,538	15,460	(15,560)(1)	(100)
Depreciation and amortization	4,279	2,039	6,318	741(2)	7,059

(1) Reconciling items from segment operating income (loss) to consolidated operating income (loss) include the following (amounts in thousands):

	<b>Three Months Ended September 30,</b>	
	<b>2005</b>	<b>2004</b>
Restructuring charges and related asset impairments	\$ 1,544	\$ 1,969
Unallocated corporate and centralized marketing, general and administrative expenses	3,246	4,818
<b>Total</b>	<b>\$ 4,790</b>	<b>\$ 6,787</b>

	<b>Nine Months Ended September 30,</b>	
	<b>2005</b>	<b>2004</b>
Restructuring charges and related asset impairments	\$ 1,920	\$ 2,458
Unallocated corporate and centralized marketing, general and administrative expenses	9,261	13,102
<b>Total</b>	<b>\$ 11,181</b>	<b>\$ 15,560</b>

(2) Represents depreciation and amortization included in the unallocated corporate or centralized marketing, general and administrative expenses.

**Table of Contents****5. COMMITMENTS AND CONTINGENCIES****Merchant Funds**

At September 30, 2005, the Company was holding funds in the amount of \$6.9 million due to merchants comprised of \$6.1 million held for Authorize.Net's eCheck.Net product, and \$0.8 million held for Authorize.Net's IPS product. The funds are included in cash and cash equivalents and funds due to merchants on the Company's consolidated balance sheet. The Company was holding funds in the amount of \$6.1 million on behalf of merchants utilizing Authorize.Net's eCheck.Net product. Authorize.Net typically holds eCheck.Net funds for approximately seven business days; the actual number of days depends on the contractual terms with each merchant. In addition, at September 30, 2005, the Company held funds in the amount of \$0.8 million on behalf of merchants processing credit card and Automated Clearing House (ACH) transactions using the Integrated Payment Solution (IPS) product. The funds are included in cash and cash equivalents and funds due to merchants on the Company's consolidated balance sheet. Credit card funds are held for approximately two business days; ACH funds are held for approximately four business days, according to the requirements of the IPS product and the contract between Authorize.Net and the financial institution through which the transactions are processed.

In addition, the Company currently has \$0.5 million on deposit with a financial institution to cover any deficit account balance that could occur if the amount of eCheck.Net transactions returned or charged back exceeds the balance on deposit with the financial institution. To date, the deposit has not been applied to offset any deficit balance, and management believes that the likelihood of incurring a deficit balance with the financial institution due to the amount of transactions returned or charged back is remote. The deposit will be held continuously for as long as Authorize.Net utilizes the ACH processing services of the financial institution, and the amount of the deposit may increase as processing volume increases.

**Legal Proceedings**

In 2001, Net MoneyIN, Inc. brought a patent infringement suit in the United States District Court for the District of Arizona, entitled *Net MoneyIN, Inc. v. VeriSign, Inc., et al.*, Case No. CIV 01-441 TUC RCC. Defendants in this case include InfoSpace, Inc. and E-Commerce Exchange, Inc.

On March 31, 2004, the Company acquired Authorize.Net from InfoSpace, Inc. In the purchase agreement, the Company agreed to indemnify and defend InfoSpace against this lawsuit. E-Commerce Exchange, Inc. was a reseller of services provided by Authorize.Net. The reseller agreement between the parties contains provisions regarding indemnification from Authorize.Net for claims against the reseller related to services provided under that agreement. Defendant Wells Fargo Bank, N.A. has also requested indemnification, including defense costs, from Authorize.Net based on certain contracts with Authorize.Net. Neither Lightbridge nor Authorize.Net is a party to the *Net MoneyIN* lawsuit, but because the Company is defending the litigation and providing indemnification to some of the defendants, the Company has potential exposure to liability (in an undetermined amount) as if the Company was party to the lawsuit. As with all major litigation, such liability could be significant and could, if the result of the lawsuit is adverse to the Company, materially adversely affect the Company's business, operations and financial condition. Lightbridge and Authorize.Net may be added as parties at a later date.

The lawsuit alleges infringement of certain patents involving payment processing over computer networks, and names a variety of defendants, including payment processing gateway providers and banks. Net MoneyIN alleges that numerous products or services infringe its patents, including the Authorize.Net Payment Gateway Service and eCheck.Net service, and seeks treble damages, permanent injunctive relief, attorneys' fees and costs. Injunctive relief adverse to the Company could materially adversely affect the Company's business operations and financial condition.

The defendants have denied the allegations of the plaintiff and have counterclaimed, seeking a declaration that plaintiff's patents have not been infringed and are invalid. The litigation is bifurcated, with separate liability and damages phases. The period designated for fact discovery during the liability phase has concluded. Following a claim construction hearing, the court issued an order on October 18, 2005 construing terms in one patent claim and finding other claims invalid. No liability-phase trial date has been set. The Company has incurred legal expenses in 2004 of approximately \$200,000 in connection with the defense of this lawsuit following the Company's acquisition of Authorize.Net, and expects to incur defense costs of approximately \$1.2 million to \$1.5 million in 2005. The Company intends to vigorously pursue available defenses to the lawsuit. The Company is not currently able to

estimate the possibility of loss or range of loss, relating to this claim.

**Leases**

As of September 30, 2005, the Company's primary contractual obligations and commercial commitments are under its operating leases and a letter of credit. The Company maintains a letter of credit in the amount of \$1.6 million, as required for security under the operating lease for its corporate headquarters.

The Company has non-cancelable operating lease agreements for office space and certain equipment. These lease agreements expire at various dates through 2011 and certain of them contain provisions for extension on substantially the same terms as are currently in effect.

**Table of Contents**

Future minimum payments under operating leases, including facilities affected by restructurings and the Company's new headquarters lease, consisted of the following at September 30, 2005 (amounts in thousands):

	<b>Operating Leases</b>
Remainder of 2005	\$ 1,113
2006	3,792
2007	3,463
2008	2,854
2009	2,208
2010	1,856
Thereafter	1,686
Total minimum lease payments	 \$ 16,972

**6. RESTRICTED CASH**

As of September 30, 2005, the Company has provided \$1.6 million of cash as collateral for a letter of credit, which is required for security under an operating lease for its corporate headquarters. The letter of credit and this related collateral agreement expire in January 2006. The Company is required to maintain this letter of credit throughout the term of the lease, which expires in 2011. In addition, as described in Note 5 above, the Company has \$0.5 million on deposit with a financial institution to cover any deficit account balance that could occur if the amount of transactions returned or charged back exceeds the balance on deposit with the financial institution.

**7. STOCK-BASED COMPENSATION**

The Company applies the intrinsic value method of accounting for stock options granted to employees. The Company accounts for stock options and awards to non-employees using the fair value method.

Under the intrinsic value method, compensation associated with stock awards to employees is determined as the difference, if any, between the current fair value of the underlying common stock on the date compensation is measured and the price an employee must pay to exercise the award. The measurement date for employee awards is generally the date of grant. Under the fair value method, compensation associated with stock awards to non-employees is determined based on the estimated fair value of the award itself, measured using either current market data or an established option pricing model. The measurement date for non-employee awards is generally the date performance of services is complete.

Had the Company used the fair value method to measure such compensation expense associated with grants of stock options to employees, reported net income (loss) and basic and diluted income (loss) per share would have been as follows (amounts in thousands, except per share amounts):

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>
Net income (loss) as reported	\$ 1,487	\$ (4,300)	\$ 16,415	\$ (4,468)
Stock-based compensation recorded in net income (loss)	(414)		(414)	
Stock-based compensation measured using the fair value method	645	(126)	1,780	404
Net income (loss) pro forma	\$ 1,256	\$ (4,174)	\$ 15,049	\$ (4,872)

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Basic net income (loss) per share pro forma	\$	0.05	\$	(0.16)	\$	0.57	\$	(0.18)
Diluted net income (loss) per share pro forma	\$	0.05	\$	(0.16)	\$	0.55	\$	(0.18)

**Table of Contents**

The fair value of options on their grant date was measured using the Black-Scholes Option Pricing Model. Key assumptions used to apply this pricing model for the nine-month periods ended September 30, 2005 and 2004 are as follows:

	<b>Nine Months Ended September 30,</b>	
	<b>2005</b>	<b>2004</b>
Risk-free interest rate	2.8%	2.9% 4.7%
Expected life of option grants	1 5 years	1 5 years
Expected volatility of underlying stock	60%	83%
Expected dividend payment rate, as a percentage of the stock price on the date of grant		

It should be noted that the option pricing model used was designed to value readily tradable stock options with relatively short lives. The options granted are not tradable and have contractual lives of up to ten years. Please refer to Note 12. Recent Accounting Pronouncements, for a discussion of future changes to accounting for stock-based compensation.

Stock-based compensation of \$0.4 million was recorded in the quarter ended September 30, 2005 related to the performance based vesting of certain executive s stock options. The compensation charge was in accordance with the achievement of certain stock price milestones determined in the option grants of the executives.

**8. EARNINGS (LOSS) PER SHARE (EPS)**

Basic EPS is computed by dividing income (loss) available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock.

A reconciliation of the shares used to compute basic income per share from continuing operations to those used for diluted income per share from continuing operations is as follows:

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>
	<b>(In thousands)</b>			
Shares for basic computation	26,678	26,482	26,631	26,689
Options and warrants (treasury stock method)	667		489	106
Shares for diluted computation	27,345	26,482	27,120	26,795

Stock options for which the exercise price exceeds the average market price over the period have an anti-dilutive effect on EPS and, accordingly, are excluded from the diluted computations for both periods presented. Had such shares been included, shares for the diluted computation would have increased by approximately 1,535,000 and 4,939,000 for the three months ended September 30, 2005 and 2004, respectively, and approximately 1,627,000 and 3,363,000 for the nine months ended September 30, 2005 and 2004, respectively. The EPS calculation has been restated to reflect the change in income from continuing operations due to the Company s INS segment now being accounted for as discontinued operations.

In addition, all other stock options and warrants convertible into common stock have been excluded from the diluted EPS computations for the three months ended September 30, 2004, as they are anti-dilutive due to the net loss recorded by the Company in those periods. Had such shares been included, the number of shares for the diluted computation would have increased by approximately 48,000 shares for the three months ended September 30, 2004.





**Table of Contents****9. RESTRUCTURING AND RELATED ASSET IMPAIRMENTS**

The following table summarizes the activity in the restructuring accrual for the three and nine months ended September 30, 2005 (amounts in thousands):

	Employee Severance and Termination Benefits	Facility Closing and Related Costs	Asset Impairment	Total
Accrued restructuring balance at December 31, 2004	\$ 2,229	\$ 286		\$ 2,515
Restructuring accrual Closing of Broomfield, Colorado Call Center	70	302		372
Cash payments	(1,050)	(117)		(1,167)
Restructuring charges	27			27
Restructuring adjustments	(12)	(3)		(15)
Accrued restructuring balance at March 31, 2005	1,264	468		1,732
Cash payments	(602)	(108)		(710)
Restructuring adjustments	(10)			(10)
Accrued restructuring balance at June 30, 2005	652	360		1,012
Restructuring accrual Existing Third Floor, Burlington, Massachusetts		890	\$ 654	1,544
Non-cash charge			(654)	(654)
Cash payments	(346)	(118)		(464)
Restructuring charges		1		1
Accrued restructuring balance at September 30, 2005	\$ 306	\$ 1,133	\$	\$ 1,439

In September 2005, the Company decided to consolidate its administrative facilities and vacated the third floor of its corporate headquarters at 30 Corporate Drive, Burlington Massachusetts. The Company recorded a restructuring charge and related asset impairments of \$1.5 million. This charge included \$0.9 million of lease obligations and \$0.6 million for the impairment of leasehold improvements and equipment. The lease obligation represents the fair value of future lease commitment costs, net of projected sublease rental income. The estimated future cash flows used in the fair value calculation are based on certain estimates and assumptions by management, including the projected sublease rental income, the amount of time the space will be unoccupied prior to sublease and the lengths of any sublease. The estimated future cash flows used were discounted using a credit adjusted risk-free interest rate and has a

maturity date that approximates the expected timing of future cash flows. The Company has lease obligations related to the facilities subject to its restructuring which extend to the year 2011. Management will review the sublease assumptions on a quarterly basis, until the outcome is finalized. Accordingly, management may modify these estimates to reflect any changes in circumstance in future periods. If modifications are made, the changes to the liability are measured using the same credit adjusted risk-free interest rate.

In January 2005, the Company announced the closing its Broomfield, Colorado call center in order to take advantage of its other existing call center infrastructure and operate more efficiently. This action resulted in the termination of approximately 40 employees associated with product service and delivery at this location. The Company recorded a restructuring charge of approximately \$0.4 million relating to facility closing costs and employee severance and termination benefits during the three months ended March 31, 2005. The Company anticipates that the severance costs related to this action will be paid by the end of 2005, and the Company anticipates that all other costs relating to this action, consisting principally of lease obligations on unused space, net of estimated sublease income, will be paid by the end of 2008.

In December 2004, the Company announced a restructuring of its business in order to lower overall expenses to better align them with future revenue expectations. This action followed the Company's announcement of an anticipated revenue reduction as a result of the acquisition of AT&T Wireless Services, Inc. (AT&T) by Cingular Wireless LLC (Cingular). This action resulted in the termination of 38 employees, in the Company's corporate offices in Burlington, Massachusetts as follows: 16 in product and service delivery, 11 in engineering and development, 10 in sales and marketing and 1 in general and administrative. The Company recorded a restructuring charge of approximately \$1.4 million relating to employee severance and termination benefits during the three months ended December 31, 2004. Additionally, subsequent to its acquisition of Authorize.Net the Company relocated its offices in Bellevue, Washington and the remaining rent paid of \$0.2 million on the vacated space was included in restructuring charges during the three months ended December 31, 2004. The Company anticipates that costs related to these actions will be paid by the end of 2005.

**Table of Contents**

In October 2004, the Company announced a restructuring of its business in accordance with the sale of the Fraud Centurion product suite to Subex Systems Limited NJ (Subex). This action, a continuation of the Company's emphasis on expense management, resulted in the termination of 9 employees in the Company's Broomfield, Colorado location as follows: 2 in product and service delivery, and 7 in engineering and development. The Company recorded a restructuring charge of approximately \$0.2 million relating to employee severance and termination benefits during the three months ended December 31, 2004. All costs related to this action were paid by the end of the second quarter of 2005.

In September 2004, the Company announced a restructuring of its business in order to lower overall expenses to better align them with future revenue expectations. This action, a continuation of the Company's emphasis on expense management, resulted in the termination of 64 employees and 2 contractors in the Company's corporate offices in Burlington, Massachusetts and its Broomfield, Colorado location as follows: 12 in product and service delivery, 16 in engineering and development, 25 in sales and marketing and 13 in general and administrative. The Company recorded a restructuring charge of approximately \$2.1 million relating to employee severance and termination benefits during the three months ended September 30, 2004. The Company anticipates that all costs related to this action will be paid by the end of 2005.

In January 2004, the Company announced a reorganization of its internal business operations. This action, a continuation of the Company's emphasis on expense management, resulted in the termination of 10 individuals in the Company's corporate office in Burlington, Massachusetts. The Company recorded a restructuring charge of approximately \$0.5 million relating to employee severance and termination benefits during the three months ended March 31, 2004. All costs related to this action were paid by the end of the first quarter of 2005.

In March 2003, the Company announced that it would be streamlining its existing Broomfield, Colorado call center operations into its Lynn, Massachusetts facility and a smaller facility in Broomfield, Colorado by the end of May 2003. In the quarter ended March 31, 2003, the Company recorded a restructuring charge of approximately \$0.1 million relating to employee severance and termination benefits. In the quarter ended June 30, 2003, the Company recorded an additional restructuring charge associated with this action of approximately \$1.0 million, consisting of approximately \$0.6 million in future lease obligations for unused facilities and approximately \$0.4 million for capital equipment write-offs. The capital equipment write-offs and all of the severance costs related to this restructuring were incurred by the end of 2003 and all other costs relating to this action were paid by the end of the first quarter of 2005.

In June 2002, the Company announced that it was reducing its workforce by seven percent and consolidating its Waltham, Massachusetts call center operations into its Lynn, Massachusetts and Broomfield, Colorado facilities by the end of 2002. The Company recorded a restructuring charge of approximately \$3.6 million, consisting of \$1.6 million relating to employee severance and termination benefits, \$1.3 million for facilities reductions including lease obligations, utilities and security costs on unused space and \$0.7 million for capital equipment write-offs associated with these measures. The restructuring plan resulted in the termination of 65 personnel as follows: 25 in product and service delivery, 22 in development, 11 in sales and marketing and 7 in general and administrative. The capital equipment write-offs and a majority of severance costs related to this action were incurred by the end of 2002, and the Company anticipates that all other costs relating to this action, consisting principally of lease obligations on unused space, will be paid by the end of 2005.

**10. PROVISION FOR (BENEFIT FROM) INCOME TAXES**

The Company provides for income taxes on an interim basis based on the full-year projected effective tax rate. The income tax provision for the nine months ended September 30, 2005 of \$0.16 million reflects a provision for state taxes of \$0.05 million and foreign taxes of \$0.11 million and includes a full valuation allowance after utilizing net operating loss carry-forwards to offset projected current taxable income. During the third quarter, the Company filed its 2004 US and state income tax returns and adjusted certain deferred tax asset items, which were also offset by a full valuation allowance. The income tax provision for the nine months ended September 30, 2004 of \$0.06 million reflects a state tax provision of \$0.08 plus an increase to the valuation allowance of \$0.09 million attributable to current year foreign tax credits, offset by a benefit of \$0.11 million to adjust certain deferred tax assets and includes a full valuation allowance on the current year net operating loss. At September 30, 2005, the Company continues to

believe a full valuation allowance is required until an appropriate level of profitability is sustained that would enable the Company to conclude that it is more likely than not that a portion of the Company's deferred taxes would be realizable.

**Table of Contents****11. COMPREHENSIVE LOSS**

The amounts that comprise comprehensive loss for the three and nine months ended September 30, 2005 and 2004 are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Net income (loss) as reported	\$ 1,487	\$ (4,300)	\$ 16,415	\$ (4,468)
Other comprehensive income:				
Foreign currency gain (loss)	88	(63)	313	(73)
Comprehensive income (loss)	\$ 1,575	\$ (4,363)	\$ 16,728	\$ (4,541)

**12. RECENT ACCOUNTING PRONOUNCEMENTS**

In December 2004, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards No. 123R, Share-Based Payment (SFAS No. 123R). This Statement is a revision of SFAS No. 123,

Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS No. 123R focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions. The Statement requires entities to recognize stock compensation expense for awards of equity instruments to employees based on the grant-date fair value of those awards (with limited exceptions). SFAS No. 123R is effective for the first interim or annual reporting period that begins after December 15, 2005. The Company is evaluating the two methods of adoption allowed by SFAS No. 123R: the modified-prospective transition method and the modified-retrospective transition method.

In March 2005, the SEC issued Staff Accounting Bulletin ( SAB ) No. 107 regarding the Staff's interpretation of SFAS No. 123R. This interpretation provides the Staff's views regarding interactions between SFAS No. 123R and certain SEC rules and regulations and provides interpretations of the valuation of share-based payments for public companies. The interpretive guidance is intended to assist companies in applying the provisions of SFAS No. 123R and investors and users of the financial statements in analyzing the information provided. The Company will follow the guidance prescribed in SAB No. 107 in connection with its adoption of SFAS No. 123R.

In June 2005, the FASB issued Statement No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20, Accounting Changes, and Statement No. 3, Reporting Accounting Changes in Interim Financial Statements (FAS 154). FAS 154 changes the requirements for the accounting for, and reporting of, a change in accounting principle. Previously, most voluntary changes in accounting principles were required to be recognized by way of a cumulative effect adjustment within net income during the period of the change. FAS 154 requires retrospective application to prior periods' financial statements, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. FAS 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005; however, the Statement does not change the transition provisions of any existing accounting pronouncements. We do not believe adoption of FAS 154 will have a material effect on our consolidated financial position, results of operations or cash flows.

In July 2005, the FASB issued an Exposure Draft of a proposed Interpretation Accounting for Uncertain Tax Positions an interpretation of FASB Statement No. 109. The proposed Interpretation proposes changes to the current accounting for uncertain tax positions. While we cannot predict with certainty the rules in the final Interpretation, there is risk that the final Interpretation could result in a cumulative effect charge to earnings upon adoption, increases in future effective tax rates, and/or increases in future inter-period effective tax rate volatility.

**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

*This Quarterly Report on Form 10-Q contains Forward-Looking Statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words believes, anticipates, plans, expects and similar expressions are intended to identify forward-looking statements. The forward-looking statements involve known and unknown risks, uncertainties and other factors, including the factors set forth under the heading Risk Factors below that may cause the actual results, performance and achievements of Lightbridge to differ materially from those indicated by the forward-looking statements. Lightbridge undertakes no obligation to update any forward-looking statements it makes.*

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**Critical Accounting Policies and Estimates**

Lightbridge has identified and discussed certain critical accounting policies and estimates in our Annual Report on Form 10-K for the year ended December 31, 2004. We did not modify our critical accounting policies during the nine months ended September 30, 2005. Those policies and estimates have been applied in the preparation of our financial statements included in this Quarterly Report on Form 10-Q.

**Overview and Revenue Recognition**

We develop, market and support a suite of products and services for merchants and communications providers, including payment processing, customer acquisition and qualification, risk management, and authentication.

A majority of our revenues historically have been derived from clients located in the United States. Our revenues are derived from transaction services, and consulting and maintenance services.

Transaction services revenues related to payment processing are derived from our credit card processing and Automated Clearing House (ACH) processing services, and other services (collectively, payment processing services), per-transaction fees, gateway fees and set-up fees. Payment processing services revenue is based on a fee per transaction and is recognized in the period in which the transaction occurs. Gateway fees are monthly subscription fees charged to our merchant customers for the use of our payment gateway. Gateway fees are recognized in the period in which the service is provided. Set-up fees represent one-time charges for initiating our payment processing services. Although these fees are generally paid to us at the commencement of the agreement, they are recognized ratably over the estimated average life of the merchant relationship, which is determined through a series of analyses of active and deactivated merchants. Commissions paid to outside sales partners are recorded in sales and marketing expense in our statements of operations.

Other transaction service revenues are derived primarily from the processing of applications for qualification of subscribers for telecommunications services and the activation of services for those subscribers. We have expanded our telecommunications transactions offerings from credit evaluation services to include screening for subscriber fraud, evaluating carriers' existing accounts, interfacing with carrier and third-party systems and providing call center services. We also offer transaction services to screen and authenticate the identity of users engaged in online transactions. Our transaction-based solutions provide multiple, remote, systems access for workflow management, along with centrally-managed client-specified business policies, and links to client and third-party systems. Transaction services are provided through contracts with carriers and others, which specify the services to be utilized

and the markets to be served. Our clients are charged for these services on a per transaction basis. Pricing varies depending primarily on the volume and type of transactions, the number and type of other products and services selected for integration with the services and the term of the contract under which services are provided. The volume of transactions processed varies depending on seasonal and retail trends, the success of the carriers and others utilizing our services in attracting subscribers and the markets served by our clients. Transaction revenues are recognized in the period in which the services are performed.



**Table of Contents**

We no longer offer instant voice conferencing transaction services through our GroupTalk offering. We never recognized any significant revenues from our GroupTalk offering and we ceased the operations of the Instant Conferencing business segment in the third quarter of 2005.

Our consulting revenues are derived primarily from providing solution development and deployment services and business advisory consulting in the areas of customer acquisition and retention, authentication, and risk management. The majority of consulting engagements are performed on a time-and-materials basis and revenues from these engagements are generally recognized as the services are performed. When we perform work under a fixed-fee arrangement, revenues are generally recognized as services are performed. Revenues from software maintenance contracts are recognized ratably over the term of the maintenance agreement.

Our software licensing revenues consist primarily of revenues attributable to the licensing of our CAS Application Modules. We sold our PrePay INS business to VeriSign in the second quarter of 2005. The PrePay billing system allowed carriers to market and manage prepaid wireless services to customers. Prepay was licensed as a packaged software product and each product generally required incidental customization or integration with other products and systems to varying degrees. Software licensing revenues are recognized when persuasive evidence of an arrangement exists, delivery of the product has been made, and a fixed fee and collectibility have been determined. Our hardware revenues historically have been derived in connection with sales of our PrePay and PhonePrint products. Revenue from hardware is recognized upon shipment, unless testing, integration or other services are required, in which case it is recognized upon commissioning and acceptance of the product. Revenue from hardware sold in conjunction with software is deferred until the software revenue is recognized.

**Recent Developments**

On August 17, 2005, we and America Online, Inc. mutually agreed to terminate our master services agreement under which we provided our GroupTalk instant conferencing service to America Online, Inc. We subsequently terminated all of the outsourcing agreements and ceased operations of the Instant Conferencing segment in the third quarter of 2005. In accordance with SFAS 144, the operating results and financial condition of the Instant Conferencing segment have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements.

Our services agreements with Sprint Spectrum L.P. (Sprint) and Nextel Operations, Inc (Nextel) expire on December 31, 2006. On December 15, 2004, Sprint and Nextel announced that their respective Boards of Directors had approved a definitive agreement for a merger of the two companies. On August 12, 2005, the merger transaction between Sprint and Nextel was completed to form Sprint Nextel Corporation (Sprint/Nextel). Following the merger, we decreased certain transaction fees to Sprint/Nextel commencing in the third quarter of 2005, and, as a result, we expect our future revenues for Sprint/Nextel to decrease in comparison to the historical levels for Sprint and Nextel when they were separate customers.

We are unable to predict the long term effect of the merger and on our relationship with Sprint/Nextel which represented a approximately 33% of our total revenues in the third quarter of 2005 including, without limitation, the timing or extent of any reductions in applications processed or other services provided under our contracts with those customers. It is possible that Sprint/Nextel could elect not to renew their agreements, to reduce the volume of products and services they purchase from us, or to request other significant changes to the pricing or other terms in any renewal agreement. A loss of one or more of our major clients, a decrease in orders by one or more of our clients or a change in the combination of products and services they obtain from us would adversely affect our revenues, margins and net income.

On April 25, 2005, we announced that we had entered into an asset purchase agreement for the sale of our INS business, which includes our PrePay IN product and related services, to VeriSign, Inc. The sale was completed on June 14, 2005 for \$17.45 million in cash plus assumption of certain contractual liabilities. Of the \$17.45 million in consideration, \$1.495 million is being held in escrow by VeriSign, and \$0.25 million is being held by us as a liability to VeriSign, until certain representations and warranties expire after an 18-month period after closing and will be recorded as a gain, net of possible indemnity claims at that time. In addition, a liability has been established of \$0.45 million in accordance with FASB Interpretation No. 45 (FIN 45), Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, based on the estimated cost if

we were to purchase an insurance policy to cover up to \$5 million of indemnification obligations for certain potential breaches of our intellectual property representations and warranties in the asset purchase agreement with VeriSign. Such representations and warranties extend for a period of two years and expire on June 14, 2007. The operating results and financial condition of the INS segment have been reported as discontinued operations in the accompanying consolidated financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 144,

Accounting for the Impairment or Disposal of Long-Lived Assets, as the sale was completed during the second quarter of 2005. All comparative prior period amounts have been restated in a similar manner. We have recorded a gain on the sale of our INS business of \$12.7 million, which has been presented as a gain on sale of discontinued operations. We recorded net loss from discontinued operations of \$0.3 million for the three months ended September 30, 2005 and recorded a net loss from discontinued operations of \$2.4 million for the nine months ended September 30, 2005. Income from discontinued operations included a \$1.4 million settlement of a lawsuit between Lucent Technologies, Inc. and us that was finalized in the second quarter of 2005.

**Table of Contents**

Also on April 25, 2005, we announced that we would evaluate strategic alternatives for our Telecom Decisioning Services ( TDS ) business and had engaged investment bankers to investigate a range of possibilities for our TDS business, including a sale or other disposition.

In November 2004, we announced that we expected that our future revenues from AT&T Wireless Services, Inc. (AT&T) will decline significantly as a result of the acquisition of AT&T by Cingular Wireless LLC (Cingular). As a result of the acquisition, AT&T customer activations will transition from our system to Cingular's internal system, and we do not expect that AT&T will be a significant customer in 2005.

In 2004, we determined that we would no longer actively market or sell our Retail Management System (RMS) product or our PhonePrint product. In October 2004, we completed the sale of certain assets related to our Fraud Centurion software product to Subex Systems Limited NJ (Subex). As a result of these actions, we do not expect to recognize significant future revenues from these products.

On March 31, 2004, we acquired all of the outstanding stock of Authorize.Net from InfoSpace Inc., for \$81.6 million in cash. We also incurred approximately \$2.0 million in acquisition-related transaction costs. Authorize.Net is a provider of payment solutions for online customer transactions. The Authorize.Net payment gateway provides credit card and electronic check solutions to companies that process orders for goods and services over the Internet, by phone and mail, at retail locations and on wireless devices. Authorize.Net connects small and medium sized businesses to large credit card processors and banking organizations, allowing those businesses to accept electronic payments.

**Operating Segments**

Based upon the way financial information is provided to our Chief Executive Officer for use in evaluating allocation of resources and assessing performance of the business, we report our operations in two distinct operating segments, described as follows:

**Payment Processing Services (Payment Processing)** This segment provides a transaction processing system, under the Authorize.Net® brand, that allows businesses to authorize, settle and manage credit card, electronic check and other electronic payment transactions online.

**Telecom Decisioning Services (TDS)** This segment provides wireless subscriber qualification, risk assessment, fraud screening, consulting services and call center services to telecom and other companies.

In our Annual Report on Form 10-K for the year ended December 31, 2004, and our previously filed Quarterly Reports on Form 10-Q, we reported separate segment information for the Intelligent Network Solutions (INS) and the Instant Conferencing Services (Instant Conferencing) businesses. The INS business, which we sold in the second quarter of 2005, provided wireless carriers with a real-time rating engine for voice, data and IN services for prepaid subscribers, as well as postpaid charging functionality and telecom calling card services. The Instant Conferencing business, the operations of which ceased in the third quarter 2005, provided managed instant conferencing services through our Lightbridge GroupTalk™ product. The operating results and financial condition of the INS and Instant Conferencing segment have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements and accordingly, our segment information has been restated. Segment results for the INS and Instant Conferencing business are no longer provided.

On April 25, 2005, we announced that we had entered into an asset purchase agreement for the sale of our INS business to VeriSign, which was completed on June 14, 2005. The operating results and financial condition of the INS segment have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements. Segment results for the INS business are no longer provided. All prior period segment financial information has been restated to conform with the current presentation. See Note 2, Discontinued Operations, for additional information about this sale.

We also announced on April 25, 2005 that we would evaluate strategic alternatives for our TDS business and had engaged investment bankers to investigate a range of possibilities for the TDS business.

Within segments, performance is measured based on revenue, gross profit and operating income (loss) realized from each segment. There are no transactions between segments. We do not allocate certain corporate or centralized marketing and general and administrative expenses to our business unit segments, because these activities are

managed separately from the business units. Also, we do not allocate restructuring expenses and other non-recurring gains or charges to our business unit segments because our Chief Executive Officer evaluates the segment results exclusive of these items. Asset information by operating segment is not reported to or reviewed by our Chief Executive Officer, and therefore we have not disclosed asset information for each operating segment.

The historical operating results associated with our RMS product, which we no longer actively market or sell, are included in our TDS segment.

**Table of Contents****Results Of Operations****Quarter Ended September 30, 2005 Compared with Quarter Ended September 30, 2004.**

**Revenues.** Revenues and certain revenue comparisons for the quarters ended September 30, 2005 and 2004 were as follows:

	Quarter Ended September 30, 2005	Quarter Ended September 30, 2004	\$ Difference	% Difference
(Dollars in thousands)				
Transaction services	\$ 25,676	\$ 28,285	\$ (2,609)	(9.2)%
Consulting and maintenance services	1,556	2,126	(570)	(26.8)
Software licensing and hardware		10	(10)	(100)
Total	\$ 27,232	\$ 30,421	\$ (3,189)	(10.5)%

The decrease in transaction services revenues was primarily due to a \$5.5 million decline in transactions services revenues from our TDS segment offset by a \$3.3 million increase in Authorize.Net's revenue. The decline in TDS transaction services revenues was primarily a result of a \$4.4 million reduction in transaction fees charged to AT&T, a decrease in transaction fees charged to Sprint/Nextel following the merger between Sprint and Nextel, and an unfavorable change in the mix of services provided to our TDS clients. Authorize.Net's revenues for the quarter increased 32.5% compared to the same period in 2004. The increased revenues were primarily the result of an increase in the number of merchant customers and the volume of transactions processed.

In the near term, we expect transaction services revenue from Authorize.Net to continue to increase. However, in the near term, we also expect transaction services revenue associated with our TDS segment to decline from the third quarter 2005 level as a result of declining revenues from AT&T, decreased pricing to Sprint/Nextel following the merger of the two companies, and continued pricing pressures. We do not expect AT&T to contribute significant revenues in the quarter ending December 31, 2005. We expect TDS transaction services revenues to continue to reflect the industry's rate of growth of new subscribers as well as the rate of switching among carriers by subscribers (subscriber churn). We believe that transaction revenue in future periods will continue to be impacted by changes in the demand for our transaction offerings, changes in the combination of services purchased by clients, carrier consolidation, and competitive pricing pressures.

The decrease in consulting and maintenance services revenues of \$0.6 million was principally due to a decline in consulting and maintenance revenues related to our decision to no longer actively market, sell or develop our RMS product. Consulting and maintenance services revenues associated with the RMS product was \$0.3 million lower in the quarter ended September 30, 2005 than in the same quarter of the preceding year. In addition, consulting and maintenance services revenues from AT&T declined \$0.5 million in the quarter ended September 30, 2005 as compared with the same period in the prior year.

There were no significant software licensing and hardware revenues in the quarter ended September 30, 2005 or in the same period in the prior year due to our decision to no longer actively market, sell or develop our RMS product.

**Cost of Revenues and Gross Profit.** Cost of revenues consists primarily of personnel costs, costs of maintaining systems and networks used in processing qualification and activation transactions (including depreciation and amortization of systems and networks) and amortization of capitalized software and acquired technology. Cost of revenues for Authorize.Net, included in transaction services cost of revenues, consists of expenses associated with the delivery, maintenance and support of Authorize.Net's products and services, including personnel costs, communication costs, such as high-bandwidth Internet access, server equipment depreciation, transactional processing fees, as well as

customer care costs. In the future, cost of revenues may vary as a percentage of total revenues as a result of a number of factors, including changes in the volume of transactions processed, changes in the mix of transaction revenues between those from automated transaction processing and those from processing transactions through our TeleServices call centers, changes in pricing to certain clients and changes in the mix of total revenues among transaction services revenues, consulting and maintenance services revenues.

**Table of Contents**

Cost of revenues, gross profit and certain comparisons for the quarters ended September 30, 2005 and 2004 were as follows:

	<b>Quarter Ended September 30, 2005</b>	<b>Quarter Ended September 30, 2004</b>	<b>\$ Difference</b>	<b>% Difference</b>
	<b>(Dollars in thousands)</b>			
Cost of revenues:				
Transaction services	\$ 11,691	\$ 14,074	\$ (2,383)	(16.9)%
Consulting and maintenance services	597	1,178	(581)	(49.3)
Software licensing and hardware				
<b>Total cost of revenues</b>	<b>\$ 12,288</b>	<b>\$ 15,252</b>	<b>\$ (2,964)</b>	<b>(19.4)%</b>
Gross profit:				
Transaction services \$	\$ 13,985	\$ 14,211	\$ (226)	(1.6)%
Transaction services %	54.5%	50.2%		
Consulting and maintenance services \$	\$ 959	\$ 948	\$ 11	1.2%
Consulting and maintenance services %	61.6%	44.6%		
Software licensing and hardware \$	\$	\$ 10	\$ (10)	(100.0)%
Software licensing and hardware %	%	100.0%		
<b>Total gross profit \$</b>	<b>\$ 14,944</b>	<b>\$ 15,169</b>	<b>\$ (225)</b>	<b>(1.5)%</b>
<b>Total gross profit %</b>	<b>54.9%</b>	<b>49.9%</b>		

Transaction services cost of revenues decreased by \$2.4 million in the quarter ended September 30, 2005 from the prior year. In our TDS business, spending decreased in our call centers as a result of the closing of our Broomfield, Colorado call center, and the staffing shift from that site to our Liverpool, Nova Scotia call center. We also realized reductions in third party data and services costs as a result of processing fewer transactions for AT&T, reduced costs for maintaining systems and networks used in processing qualification and activation transactions, and personnel-related savings resulting from our 2004 restructuring activities. Transaction services gross profit and gross profit percentage increased primarily as a result of Authorize.Net's higher contribution to the transaction services gross profit amount. Authorize.Net's percent of the transaction services gross profit amount was 66% in the quarter ended September 30, 2005 versus 44% in the same quarter of the preceding year as a result of higher revenues. This increase was partially offset by a decrease in the transaction services gross profit related to our TDS segment, where the revenue reduction exceeded the cost of sales expense reduction. Authorize.Net generated a higher gross profit percentage than our TDS segment, resulting in increased transaction services gross profit percentage in the quarter ended September 30, 2005 than in the same quarter of 2004.

Consulting and maintenance services cost of revenues decreased by \$0.6 million in the third quarter of 2005. This decrease was attributable to a reduction in personnel-related expenses as a result of the September and December 2004 restructurings. Consulting and maintenance services gross profit and gross profit percentage increased in the third quarter of 2005 due to the lower headcount partially offset by lower revenues related to our RMS product and from AT&T.





**Table of Contents**

**Engineering and Development.** Engineering and development expenses include software development costs, consisting primarily of personnel and outside technical service costs related to developing new products and services, enhancing existing products and services, and implementing and maintaining new and existing products and services. The \$1.4 million decrease in engineering and development expenses for the quarter ended September 30, 2005 as compared with the same quarter in 2004 was primarily due to cost savings associated with the 2004 restructuring activities and our decision to cease new development and enhancement of our RMS software product. Engineering and development expenses as a percentage of total revenues decreased for the third quarter of 2005 as a result of lower spending.

We expect engineering and development expenses for the quarter ending December 31, 2005 to continue to decline in comparison to the prior year level, primarily due to benefits of restructuring activities.

**Sales and Marketing.** Sales and marketing expenses consist primarily of salaries, commissions and travel expenses of direct sales and marketing personnel, as well as costs associated with advertising, trade shows and conferences. For Authorize.Net, sales and marketing expenses also include commissions paid to outside sales agents. The decrease of \$0.9 million in sales and marketing expenses in the quarter ended September 30, 2005 as compared with the same quarter in 2004, in absolute dollars and as a percentage of revenue, was due to lower personnel-related expenses as a result of our 2004 restructuring activities. Authorize.Net represented \$4.0 million of sales and marketing expenses in the third quarter of 2005 results compared to \$3.5 million in the third quarter of 2004. This increase was offset by reductions in marketing costs for the other portions of our business, restructuring activities, and reduced sales and marketing program spending as compared with the third quarter of 2004.

We expect that sales and marketing expenses for the quarter ending December 31, 2005 will be relatively unchanged from the third quarter of 2005. However, we expect sales and marketing expenses to increase with growth in Authorize.Net's revenues as a result of greater sales agent commissions associated with these revenues.

**General and Administrative.** General and administrative expenses consist principally of salaries of executive, finance, human resources and administrative personnel and fees for certain outside professional services. The decrease of \$0.8 million in general and administrative expenses, as compared to the same quarter in 2005, in absolute dollars and as a percentage of revenues, was due to savings associated with our 2004 restructuring activities and reduced program spending partially offset by higher spending associated with legal fees and other spending for professional services.

We do not expect significant changes in the level of general and administrative expenses in the quarter ending December 31, 2005 from the third quarter of 2005.

**Restructuring charges and related asset impairments.** Please refer to Note 9 in the Notes to Unaudited Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for a description of our restructuring activities and related asset impairment charges.

**Other Income, Net.** Other income, net primarily consists of interest income earned on our cash and short-term investment balances. Other income, net increased by \$0.3 million in the quarter ended September 30, 2005 in comparison with the same period in 2004 primarily due to an increase in our cash and short-term investments balance as a result of cost savings from the 2004 and 2005 restructurings and the cash received for the sale of our INS business.

**Provision for (Benefit from) Income Taxes.** We provide for income taxes on an interim basis based on the full-year projected effective tax rate. The income tax provision for the three months ended September 30, 2005 of \$0.06 million reflects a provision for state taxes of \$0.02 million and foreign taxes of \$0.04 million and includes a full valuation allowance after utilizing net operating loss carry-forwards to offset projected current taxable income. The income tax provision for the three months ended September 30, 2004 reflects a net benefit of \$0.62 million and includes a current state tax expense of \$0.03 million plus an increase to the valuation allowance of \$0.3 million attributable to foreign tax credits generated in the quarter, plus a provision of \$0.18 million to adjust certain deferred tax assets, offset by a \$0.86 million benefit to record a full valuation allowance on the current year net operating loss. At September 30, 2005, we continue to believe a full valuation allowance is required until an appropriate level of profitability is sustained that would enable us to conclude that it is more likely than not that a portion of our deferred tax assets would be realizable.

**Results by Operating Segment.** The operating results and financial condition of the INS and Instant Conferencing segments have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements. Segment results for the INS and Instant Conferencing business are no longer provided. All prior period segment financial information has been restated to conform with the current presentation.

**Table of Contents**

Certain operating results and comparisons by operating segment for the quarters ended September 30, 2005 and 2004 were as follows:

	<b>Quarter Ended September 30, 2005</b>	<b>Quarter Ended September 30, 2004</b>	<b>\$ Difference</b>	<b>% Difference</b>
	<b>(Dollars in thousands)</b>			
Revenues:				
TDS	\$ 15,518	\$ 21,582	\$ (6,064)	(28.1)%
Payment Processing	11,714	8,839	2,875	32.5
Total	\$ 27,232	\$ 30,421	\$ (3,189)	(10.5)%
Gross Profit (Loss):				
TDS \$	\$ 5,776	\$ 8,969	\$ (3,193)	(35.6)%
TDS %	37.2%	41.6%		
Payment Processing \$	\$ 9,168	\$ 6,200	\$ 2,968	47.9%
Payment Processing %	78.3%	70.1%		
Total gross profit \$	\$ 14,944	\$ 15,169	\$ (225)	(1.5)%
Total gross profit %	54.9%	49.9%		
Operating Income (Loss):				
TDS	\$ 2,859	3,880	\$ (1,021)	(26.3)%
Payment Processing	3,255	876	2,379	271.6
Total segment operating income	\$ 6,114	\$ 4,756	\$ 1,358	28.6%
Reconciling items(1)	(4,790)	(6,787)		
Total operating income (loss)	\$ 1,324	\$ (2,031)		

(1) Reconciling items consist of certain corporate or centralized marketing and

general and administrative expenses not allocated to our business unit segments, because these activities are managed separately from the business units. Also, we do not allocate restructuring expenses and other non-recurring gains or charges to our business unit segments because our Chief Executive Officer evaluates the segment results exclusive of these items.

***Revenues by Operating Segment***

***TDS.*** The decline in TDS revenues was primarily a result of a \$4.9 million reduction in revenue from AT&T, a decrease in certain transaction fees charged to Sprint/Nextel following the merger between Sprint and Nextel, and an unfavorable change in the mix of services provided.

***Payment Processing.*** Payment Processing revenues for the quarter have increased 32.5% compared to the same period in 2004. The increased revenues were primarily the result of an increase in the number of merchant customers and the volume of transactions processed.

***Gross Profit (Loss) by Operating Segment***

***TDS.*** The decline in TDS gross profit was a result of lower revenues of 28% as compared to the three months ended September 30, 2004. The impact of the revenue decline was partially offset by a \$2.9 million expense reduction. Spending decreased in our call centers as a result of the closing of our Broomfield, Colorado call center, and the staffing shift from that site to our Liverpool, Nova Scotia call center. We also realized reductions in third party data and services costs as a result of processing fewer transactions for AT&T Wireless, reduced costs for maintaining systems and networks used in processing qualification and activation transactions, and personnel-related savings resulting from our 2004 restructuring activities.

***Payment Processing.*** The increase in Payment Processing gross profit was due to the increase in Authorize.Net's revenue from the prior year.

**Table of Contents****Operating Income (Loss) by Operating Segment.**

**TDS.** The decline in TDS operating income reflects the impact of reduced revenues, partially offset by spending reductions resulting from our 2004 restructuring activities.

**Payment Processing.** The increase in Payment Processing operating income was due to the increase in Authorize.Net's revenue from the prior year.

**Nine Months Ended September 30, 2005 Compared with Nine Months Ended September 30, 2004.**

**Revenues.** Revenues and certain revenue comparisons for the nine months ended September 30, 2005 and 2004 were as follows:

	<b>Nine Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2004</b>	<b>\$ Difference</b>	<b>% Difference</b>
	<b>(Dollars in thousands)</b>			
Transaction services	\$ 76,477	\$ 76,156	\$ 321	0.4%
Consulting and maintenance services	4,492	8,189	(3,697)	(45.1)
Software licensing and hardware		1,628	(1,628)	(100.0)
<b>Total</b>	<b>\$ 80,969</b>	<b>\$ 85,973</b>	<b>\$ (5,004)</b>	<b>(5.8)%</b>

The increase in transaction revenues of \$0.3 million was mainly due to a full three quarters of Authorize.Net revenue during the nine months ended September 30, 2005. The results of Authorize.Net's operations were excluded from our first quarter 2004 results. As a result, Authorize.Net's revenues were \$15.6 million higher for the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004. A significant component of Authorize.Net's higher revenues were attributable to a 32.5% increase in revenues for the quarter ended September 30, 2005 as compared to the prior year. The increased revenues were primarily the result of an increase in the number of merchant customers and increased volume of transactions processed.

Our TDS business segment transaction revenues were \$15.3 million lower for the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004. The decline in TDS transaction services revenues was primarily a result of a \$11.9 million reduction in transaction fees charged to AT&T, a decrease in transaction fees charged to Sprint/Nextel as a result of the merger between Sprint and Nextel, and an unfavorable change in the mix of services provided.

The decrease in consulting and maintenance services revenues of \$3.7 million was principally due to lower revenues from AT&T and a decline in consulting and maintenance revenues related to our decision to no longer actively market, sell or develop our RMS product.

The decline in software licensing and hardware revenues of \$1.6 million was primarily due to a fee from the license of our RMS software product to Sprint for \$1.6 million in the nine months ended September 30, 2004.

**Cost of Revenues and Gross Profit**

Cost of revenues, gross profit and certain comparisons for the nine months ended September 30, 2005 and 2004 were as follows:

	<b>Nine Months Ended September 30,</b>	<b>Nine Months Ended September 30,</b>	<b>\$</b>	<b>%</b>
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	<b>2005</b>	<b>2004</b>	<b>Difference</b>	<b>Difference</b>
		<b>(Dollars in thousands)</b>		
<b>Cost of revenues:</b>				
Transaction services	\$ 35,881	\$ 40,422	\$ (4,541)	(11.2)%
Consulting and maintenance services	1,919	3,366	(1,447)	(43.0)
Software licensing and hardware		13	(13)	(100.0)
Total cost of revenues	\$ 37,800	\$ 43,801	\$ (6,001)	(13.7)%
<b>Gross profit:</b>				
Transaction services \$	\$ 40,596	\$ 35,734	\$ 4,862	13.6%
Transaction services %	53.1%	46.9%		
	24			

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**Table of Contents**

	<b>Nine Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2004</b>	<b>\$ Difference</b>	<b>% Difference</b>
			<b>(Dollars in thousands)</b>	
Consulting and maintenance services \$	\$ 2,573	\$ 4,823	\$ (2,250)	(46.7)%
Consulting and maintenance services %	57.3%	58.9%		
Software licensing and hardware \$	\$	\$ 1,615	\$ (1,615)	(100.0)%
Software licensing and hardware %	%	99.2%		
Total gross profit \$	\$ 43,169	\$ 42,172	\$ 997	2.4%
Total gross profit %	53.3%	49.1%		

Transaction services cost of revenues decreased by \$4.5 million for the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004. In our TDS business, spending decreased in our call centers as a result of the closing of our Broomfield, Colorado call center, and the staffing shift from that site to our Liverpool, Nova Scotia call center. We also realized reductions in third party data and services costs as a result of processing fewer transactions for AT&T, reduced costs for maintaining systems and networks used in processing qualification and activation transactions, and personnel-related savings resulting from our 2004 restructuring activities. Transaction services gross profit and gross profit percentage increased primarily as a result of Authorize.Net's results of operations not being included in our first quarter 2004 results. This resulted in Authorize.Net's higher contribution to the transaction services gross profit amount for the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004. Authorize.Net generated a higher gross profit percentage than our TDS segment, resulting in increased transaction services gross profit percentage. This was partially offset by a decrease in the transaction services gross profit related to our TDS segment, where the revenue reduction exceeded the cost of sales expense reduction.

Consulting and maintenance services cost of revenues decreased by \$1.4 million for the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004. This decrease was attributable to lower personnel-related expenses as a result of the September and December 2004 restructurings. Consulting and maintenance services gross profit and gross profit percentage decreased in the nine months ended September 30, 2005 due to lower revenues related to our RMS product and from AT&T.

Software licensing and hardware gross profit and gross profit percentage decreased by \$1.6 million for the nine months ended September 30, 2005 as compared to the nine months ended June 30, 2004. The decline is primarily due to a fee from the license of our RMS product to Sprint for \$1.6 million in the second quarter of 2004.

**Operating Expenses.** Operating expenses and certain operating expense comparisons for the nine months ended September 30, 2005 and 2004 were as follows:

	<b>Nine Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2004</b>	<b>\$ Difference</b>	<b>% Difference</b>
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	<b>(Dollars in thousands)</b>			
Engineering and development	\$ 10,978	\$ 13,747	\$ (2,769)	(20.1)%
Sales and marketing	13,375	13,290	85	0.6
General and administrative	11,734	12,098	(364)	(3.0)
Purchased in-process research and development		679	(679)	(100.0)
Restructuring charges	1,920	2,458	(538)	(21.9)
<b>Total</b>	<b>\$ 38,007</b>	<b>\$ 42,272</b>	<b>\$ (4,265)</b>	<b>(10.1)%</b>

**Engineering and Development.** The \$2.8 million decrease in engineering and development expenses for the nine months ended September 30, 2005 was primarily due to cost savings as a result of the 2004 restructurings. These savings were partially offset by the addition of engineering and development expenses for Authorize.Net which were included beginning in the three months ended June 30, 2004. Engineering and development expenses as a percentage of total revenues decreased for the nine months ended September 30, 2005 as a result of lower expense levels.

**Sales and Marketing.** The \$0.1 million increase in sales and marketing expenses for the nine months ended September 30, 2005 was due to the inclusion of Authorize.Net and the related sales agent commissions in sales and marketing expense for nine months in 2005 as compared to only the six months ended September 30, 2004.

**General and Administrative.** The \$0.4 million decrease in general and administrative costs for the nine months ended September 30, 2005 was primarily due to cost savings associated with the 2004 restructurings. These savings were partially offset by the addition of general and administrative expenses for Authorize.Net which were included beginning in the three months ended June 30, 2004.



**Table of Contents**

**Purchased In-Process Research and Development (IPR&D).** In connection with the Authorize.Net acquisition, we recorded a \$0.7 million charge during the first quarter of 2004 for two IPR&D projects. Please refer to our Annual Report on Form 10-K for the year ended December 31, 2004 for a complete description of this IPR&D charge. There were no IPR&D charges recorded during the nine months ended September 30, 2005.

**Restructuring charges and related asset impairments.** Please refer to Note 9 in the Notes to Unaudited Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for a complete description of these charges.

**Other Income, Net.** Other income, net primarily consists of interest income earned on our cash and short-term investment balances. Other income, net increased by \$0.6 million in the nine months ended September 30, 2005 in comparison with the same period in 2004 primarily due to an increase in our cash and short-term investments balances as a result of cost savings from the 2004 and 2005 restructurings and the cash received for the sale of our INS business.

**Provision for (Benefit from) Income Taxes.** We provide for income taxes on an interim basis based on the full-year projected effective tax rate. The income tax provision for the nine months ended September 30, 2005 of \$0.16 million reflects a provision for state taxes of \$0.05 million and foreign taxes of \$0.11 million and includes a full valuation allowance after utilizing net operating loss carry-forwards to offset projected current taxable income. During the third quarter, we filed our 2004 US and State income tax returns and adjusted certain deferred tax items, which were offset by a full valuation allowance. The income tax provision for the nine months ended September 30, 2004 of \$0.06 million reflects a state tax provision of \$0.08 plus an increase to the valuation allowance of \$0.09 million on the current year foreign tax credits, offset by a benefit of \$0.11 million to adjust certain deferred tax assets and includes a full valuation allowance on the current year net operating loss. At September 30, 2005, we continue to believe a full valuation allowance is required until an appropriate level of profitability is sustained that would enable us to conclude that it is more likely than not that a portion of our deferred tax assets would be realizable.

**Results by Operating Segment.** The operating results and financial condition of the INS and Instant Conferencing segments have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements. Segment results for the INS and Instant Conferencing businesses are no longer provided. All prior period segment financial information has been restated to conform with the current presentation. Certain operating results and comparisons by operating segment for the nine months ended September 30, 2005 and 2004 are as follows:

	<b>Nine Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2004</b>	<b>\$ Difference</b>	<b>% Difference</b>
	<b>(Dollars in thousands)</b>			
Revenues:				
TDS	\$ 48,408	\$ 68,996	\$ (20,588)	(29.8)%
Payment Processing	32,561	16,977	15,584	91.8
 Total	 \$ 80,969	 \$ 85,973	 \$ (5,004)	 (5.8)%
 Gross Profit (Loss):				
TDS \$	\$ 17,727	\$ 30,027	\$ (12,300)	(41.0)%
TDS %	36.6%	43.5%		
Payment Processing \$	\$ 25,442	\$ 12,145	\$ 13,297	109.5%

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Payment Processing %	78.1%	71.5%		
Total gross profit \$	\$ 43,169	\$ 42,172	\$ 997	2.4%
Total gross profit %	53.3%	49.1%		
Operating Income (Loss):				
TDS	\$ 8,538	13,922	\$ (5,384)	(38.7)%
Payment Processing	7,805	1,538	6,267	407.5
Total segment operating income	\$ 16,343	\$ 15,460	\$ 883	5.7%
Reconciling items(1)	(11,181)	(15,560)		
Total operating loss	\$ 5,162	\$ (100)		

26

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**Table of Contents**

- (1) Reconciling items consist of certain corporate or centralized marketing and general and administrative expenses not allocated to our business unit segments, because these activities are managed separately from the business units. Also, we do not allocate restructuring expenses and other non-recurring gains or charges to our business unit segments because our Chief Executive Officer evaluates the segment results exclusive of these items.

***Revenues by Operating Segment***

**TDS.** The decline in TDS revenues was primarily a result of a reduction in revenue from AT&T Wireless and a reduction in revenue from our RMS product. Other contributing factors were a decrease in certain transaction fees charged to Sprint/Nextel following the merger between Sprint and Nextel, and an unfavorable change in the mix of services provided for the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004.

**Payment Processing.** Lightbridge began recording Payment Processing revenues as of April 1, 2004 following the acquisition of Authorize.Net on March 31, 2004. The nine months ended September 30, 2004 includes revenue from April 1, 2004 through September 30, 2004. Authorize.Net revenue for the nine months ended September 30, 2005 increased 30% compared to the same period in 2004 as reported above by Authorize.Net's former owner, InfoSpace, Inc. The increased revenues were primarily the result of an increase in the number of merchant customers added and the volume of transactions processed.

***Gross Profit (Loss) by Operating Segment***

**TDS.** The decline in TDS gross profit was a result of lower revenue, primarily due to a reduction in revenue from AT&T, as well as a reduction in revenue from our RMS product, largely due to a fee from the license of that product

to Sprint in the second quarter of 2004. Other factors contributing to the decline in revenue as described above. The impact of the revenue decline was partially mitigated by an \$8.3 million expense reduction. Spending decreased in our call centers as a result of the closing of our Broomfield, Colorado call center, and the staffing shift from that site to our Liverpool, Nova Scotia call center.

We also realized reductions in third party data and services costs as a result of processing fewer transactions for AT&T, reduced costs for maintaining systems and networks used in processing qualification and activation transactions, and personnel-related savings resulting from our 2004 restructuring activities.

**Payment Processing.** The increase in Payment Processing gross profit was due to the acquisition of Authorize.Net on March 31, 2004.

**Operating Income (Loss) by Operating Segment.**

**TDS.** The decline in TDS operating income reflects the impact of reduced revenues, partially offset by spending reductions resulting from our 2004 restructuring activities.

**Payment Processing.** The increase in Payment Processing operating income was due to the acquisition of Authorize.Net on March 31, 2004.

**Discontinued Operations**

On April 25, 2005, we announced that we had entered into an asset purchase agreement for the sale of our INS business, which includes our PrePay IN product and related services, to VeriSign. The sale was completed on June 14, 2005 for \$17.45 million in cash plus assumption of certain contractual liabilities. Of the \$17.45 million in consideration, \$1.495 million is being held in escrow by VeriSign, and \$0.25 million is being held by us as a liability to VeriSign, until certain representations and warranties expire after an 18-month period after closing and will be recorded as a gain, net of possible indemnity claims at that time. In addition, a liability has been established of \$450,000 in accordance with FIN 45 based on the estimated cost if we were to purchase an insurance policy to cover up to \$5 million of indemnification obligations for certain potential breaches of our intellectual property representations and warranties in the asset purchase agreement with VeriSign. Such representations and warranties extend for a period of two years and expire on June 14, 2007. The operating results and financial condition of the INS segment have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements in accordance with SFAS No. 144, as the sale was completed during the second quarter of 2005. All comparative prior period amounts have been restated in a similar manner. We recorded a gain on the sale of our INS business during the second quarter of 2005 of \$12.7 million, which has been presented as a gain on sale of discontinued operations.

**Table of Contents**

In the first quarter of 2005, we made the decision to no longer actively market or sell our GroupTalk product and took actions to outsource the continuing operations of our Instant Conferencing segment. On August 17, 2005, we and America Online, Inc. mutually agreed to terminate our master services agreement under which we provided our GroupTalk instant conferencing services to America Online, Inc. We subsequently terminated all of the outsourcing agreements and ceased operations of the Instant Conferencing segment in the third quarter of 2005. In accordance with SFAS 144, the operating results and financial condition of the Instant Conferencing segment have been included as part of the financial results from discontinued operations in the accompanying consolidated financial statements.

We recorded net loss from discontinued operations of \$0.3 million for the three months ended September 30, 2005 and recorded a net income from discontinued operations of \$10.3 million for the nine ended September 30, 2005. The net income from discontinued operations includes the gain on the sale of INS of \$12.7 million and a \$1.4 million settlement of a lawsuit between Lucent Technologies, Inc. and us received in the second quarter of 2005.

**Liquidity and Capital Resources**

As of September 30, 2005, we had cash and cash equivalents, short-term investments and restricted cash of \$80.5 million. We believe that our current cash and short-term investment balances will be sufficient to finance our operations and capital expenditures for the next twelve months. Thereafter, the adequacy of our cash balances will depend on a number of factors that are not readily foreseeable such as the impact of general market conditions on our operations, additional acquisitions or investments, divestitures, restructuring or obligations associated with the closure of products or facilities, and the sustained profitability of the our operations. We may also require additional cash in the future to finance growth initiatives including acquisitions.

During the first nine months of 2005, we generated cash from operating activities of approximately \$2.0 million, cash from investing activities of approximately \$20.8 million, and cash from financing activities of approximately \$1.0 million. During the first nine months of 2005, we had a gain on sale of our PrePay assets of \$12.7 million and our accounts payable and accrued compensation and benefits decreased by a combined \$2.0 million primarily related to the payment of 2004 bonuses and the timing of payments to certain significant vendors. Included in cash provided by investing activities for the nine months ended September 30, 2005, was \$15.0 million in net cash proceeds from the sale of PrePay assets and \$1.5 million provided as restricted cash to collateralize a letter of credit supporting the operating lease for our corporate headquarters.

Our capital expenditures totaled \$2.2 million for the nine months ended September 30, 2005. The capital expenditures during this period were principally associated with our service delivery infrastructure and computer equipment for software development activities. We lease our facilities and certain equipment under non-cancelable operating lease agreements that expire at various dates through January 2011.

Future minimum payments under operating leases, including facilities affected by restructurings, consisted of the following at September 30, 2005 (amounts in thousands):

	<b>Operating Leases</b>
Remainder of 2005	\$ 1,113
2006	3,792
2007	3,463
2008	2,854
2009	2,208
2010	1,856
Thereafter	1,686
Total minimum lease payments	 \$ 16,972

We incurred legal expenses in 2004 of approximately \$200,000 in connection with the defense of a lawsuit entitled *Net Money IN, Inc. v. VeriSign, Inc., et. al.*, following our acquisition of Authorize.Net, and expect to incur defense

costs of approximately \$1.2 million to \$1.5 million in 2005. Please refer to Part II Other Information, Item 1, Legal Proceedings for a discussion of this lawsuit.

At September 30, 2005, we were holding funds in the amount of \$6.9 million due to merchants. The funds are included in cash and cash equivalents and funds due to merchants on our consolidated balance sheet. We were holding funds in the amount of \$6.1 million on behalf of merchants utilizing Authorize.Net's eCheck.Net product. Authorize.Net holds eCheck.Net funds for approximately seven business days; the actual number of days depends on the contractual terms with each merchant. In addition, at September 30, 2005, we held funds in the amount of \$0.8 million for and on behalf of merchants processing credit card and ACH transactions using the Integrated Payment Solution (IPS) product. The funds are included in cash and cash equivalents and funds due to merchants on our consolidated balance sheet. Credit card funds are held for approximately two business days; ACH funds are held for approximately four business days, according to the requirements of the IPS product and the contract between Authorize.Net and the financial institution through which the transactions are processed.

**Table of Contents**

In addition, we currently have \$0.5 million on deposit with a financial institution to cover any deficit account balance that could occur if the amount of eCheck.Net transactions returned or charged back exceeds the balance on deposit with the financial institution. To date, the deposit has not been applied to offset any deficit balance, and we believe that the likelihood of incurring a deficit balance with the financial institution due to the amount of transactions returned or charged back is remote. The deposit will be held continuously for as long as we utilize the ACH processing services of the financial institution, and the amount of the deposit may increase as processing volume increases.

Our primary contractual obligations and commercial commitments are under operating leases and a letter of credit. We maintain a letter of credit in the amount of \$1.6 million that extends through January 2006. In January 2005, we provided \$1.6 million of cash as collateral for that letter of credit.

**Inflation**

Although certain of our expenses increase with general inflation in the economy, inflation has not had a material impact on our financial results to date.

**Recent Accounting Pronouncements**

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 123R, Share-Based Payment (SFAS No. 123R). This Statement is a revision of SFAS No. 123, Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS No. 123R focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions. The Statement requires entities to recognize stock compensation expense for awards of equity instruments to employees based on the grant-date fair value of those awards (with limited exceptions). SFAS No. 123R is effective for the first interim or annual reporting period that begins after December 15, 2005. We are evaluating the two methods of adoption allowed by SFAS No. 123R: the modified-prospective transition method and the modified-retrospective transition method.

In March 2005, the SEC issued Staff Accounting Bulletin (SAB) No. 107 regarding the Staff's interpretation of SFAS No. 123R. This interpretation provides the Staff's views regarding interactions between SFAS No. 123R and certain SEC ruled and regulations and provides interpretations of the valuation of share-based payments for public companies. The interpretive guidance is intended to assist companies in applying the provisions of SFAS No. 123R and investors and users of the financial statements in analyzing the information provided. We will follow the guidance prescribed in SAB No. 107 in connection with our adoption of SFAS No. 123R.

In June 2005, the FASB issued Statement No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20, Accounting Changes, and Statement No. 3, Reporting Accounting Changes in Interim Financial Statements (FAS 154). FAS 154 changes the requirements for the accounting for, and reporting of, a change in accounting principle. Previously, most voluntary changes in accounting principles were required to be recognized by way of a cumulative effect adjustment within net income during the period of the change. FAS 154 requires retrospective application to prior periods' financial statements, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. FAS 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005; however, the Statement does not change the transition provisions of any existing accounting pronouncements. We do not believe adoption of FAS 154 will have a material effect on our consolidated financial position, results of operations or cash flows.

In July 2005, the FASB issued an Exposure Draft of a proposed Interpretation Accounting for Uncertain Tax Positions an interpretation of FASB Statement No. 109. The proposed Interpretation proposes changes to the current accounting for uncertain tax positions. While we cannot predict with certainty the rules in the final Interpretation, there is risk that the final Interpretation could result in a cumulative effect charge to earnings upon adoption, increases in future effective tax rates, and/or increases in future inter-period effective tax rate volatility.

**Table of Contents****Risk Factors****If One or More of Our Major Clients Stops Using Our Products or Services or Changes the Combination of Products and Services It Uses, Our Operating Results Would Suffer Significantly.**

On April 25, 2005, we announced that we engaged investment bankers to explore strategic alternatives for our TDS business. Our TDS revenues are concentrated among a few major clients. Our 10 largest clients accounted for approximately 55% and 58% of our total revenues in the quarter and nine months ended September 30, 2005, respectively. We have no significant merchant concentration in our Payment Processing business. Although our client concentration has declined, we expect that a majority of our revenues will continue to come from a relatively small number of clients for the foreseeable future. Consequently, our revenues, margins and net income may fluctuate significantly from quarter to quarter based on the actions of a single significant client. A client may take actions that significantly affect us for reasons that we cannot necessarily anticipate or control, such as reasons related to the client's financial condition, changes in the client's business strategy or operations, the introduction of alternative competing products or services, acquisitions, or as the result of the perceived quality or cost-effectiveness of our products or services. Our services agreements with Sprint Spectrum L.P. (Sprint), and Nextel Operations, Inc. (Nextel) expire on December 31, 2006. Our services agreement with AT&T Wireless Services, Inc. (AT&T) expires on April 1, 2009, but is subject to earlier termination upon twelve months' notice and designated services upon notice. In February 2004, Cingular Wireless LLC (Cingular) announced an agreement to acquire AT&T and in October 2004, Cingular announced that it had completed its merger with AT&T. Cingular is not presently a client of Lightbridge. As a result of the acquisition of AT&T, we do not expect that client to generate significant revenue in the remainder of 2005. On December 15, 2004, Sprint and Nextel announced that their respective Boards of Directors had approved a definitive agreement for a merger of the two companies. On August 12, 2005, the merger transaction between Sprint and Nextel was completed to form Sprint Nextel Corporation (Sprint/Nextel). Following the merger we decreased certain transaction fees to Sprint/Nextel commencing in the third quarter of 2005, and as a result, we expect our future revenues for Sprint/Nextel to decrease in comparison to the historical levels for Sprint and Nextel when they were separate customers. We are unable to predict the long term effect of the merger and on our relationship with Sprint/Nextel, which represented approximately 33% of our total revenues in the third quarter of 2005 including, without limitation, the timing or extent of any reductions in applications processed or other services provided under our contracts with those clients. It is possible that Sprint/Nextel could elect not to renew their agreement, to reduce the volume of products and services they purchase from us or to request significant changes to the pricing or other terms in any renewal agreement. The loss of Sprint/Nextel or any of our other major clients would cause sales to fall below expectations and materially reduce our revenues, margins and net income and adversely affect our business.

**Certain of Our Revenues Are Uncertain Because Our Clients May Reduce the Amounts of or Change the Combination of Our Products or Services They Purchase.**

Most of our communications client contracts extend for terms of between one and three years. During the terms of these contracts, our communications clients typically may elect to purchase any of several different combinations of products and services. The revenue that we receive for processing a transaction for such a client may vary significantly depending on the particular products and services used to process the transaction. In particular, transactions handled through our TeleServices Group generally result in significantly higher revenue than transactions that are submitted and processed electronically, but also result in higher cost of revenues. Therefore, our revenues or margins from a particular client may decline if the client changes the combination of products and services it purchases from us.

To the extent our client contracts contain minimum purchase or payment requirements, these minimums are typically at levels significantly below actual or historical purchase or payment levels. Therefore, our current clients may not continue to utilize our products or services at levels similar to previous years or at all, and may not generate significant revenues in future periods. If any of our major clients significantly reduces or changes the combination of products or services it purchases from us for any reason, our business would be seriously damaged.

**A Majority of Our Revenues Are Concentrated in the Wireless Telecommunications Industry, Which Is Experiencing Declining Growth Rates, Consolidation and Increasing Pressure to Control Costs.**



We currently derive a majority of our revenues from companies in the wireless telecommunications industry, and we expect that wireless telecommunications companies will continue to account for a majority of our revenues in 2005. In recent years, the growth rate of the domestic wireless industry has slowed. In addition, consolidation has affected the number of carriers to whom our products and services can be marketed and sold, and competition among wireless carriers has continued to increase, resulting in heightened efforts by carriers to control costs. Many of our carrier clients have sought, and may in the future seek, pricing concessions when they renew their services agreements with us or at other times, which could affect our revenues, margins and net income. In addition, certain of our carrier clients have sought bankruptcy protection in recent years, and we believe it is possible that additional clients may file for bankruptcy protection if current industry conditions continue. Bankruptcy filings by our clients or former clients such as WorldCom, Inc. may prevent us from collecting some or all of the amounts owing to us at the time of filing, may require us to return some or all of any payments received by us within 90 days prior to a bankruptcy filing and may also result in the termination of our service agreements. As a result of the foregoing conditions, our success depends on a number of factors:

**Table of Contents**

our ability to maintain our profit margins on sales of products and services to companies in the wireless telecommunications industry;

the financial condition of our clients and their continuing ability to pay us for services and products;

our ability to develop and market new or enhanced products and services to new and existing clients;

continued growth of the domestic wireless telecommunications markets;

the number of carriers seeking to implement prepaid billing services; and

our ability to increase sales of our products and services internationally.

**Our Exploration of Strategic Alternatives for Our TDS Business May Prove Unsuccessful or May Otherwise Have a Material Adverse Effect on Our Ability to Conduct Business, Our Operations and Our Financial Condition.**

We are taking steps to streamline operations and sharpen our strategic focus. On April 25, 2005, we announced our decision to explore strategic options for our TDS business.

We can offer no assurances that we will be able to locate potential strategic partners for the TDS business or will be able to consummate any transactions with potential strategic partners we do locate. Our pursuit of strategic initiatives may prove unsuccessful or may otherwise have a material adverse effect on our ability to conduct business, our operations and our financial condition. For example, we may not always be able to obtain the optimal price for assets and businesses we choose to sell or may receive a price that is substantially lower than the investments made for the assets or businesses being disposed of. In addition, our continuing operations may suffer as a result of losing synergies with the assets and businesses sold. Further, the inherent uncertainty in the process of seeking strategic alternatives could result in loss of customers or employees, which could impair the value of those assets.

Furthermore, changes to our business may not prove successful in the short or long term and may negatively impact our financial results. In particular, we expect to experience a decline in revenue in the short term, in the case of dispositions, and we may incur additional charges due to restructuring or impairment of assets.

**We and Our Clients Must Comply with Complex and Changing Laws and Regulations.**

Government regulation influences our activities and the activities of our current and prospective clients, as well as our clients' expectations and needs in relation to our products and services. Businesses that handle consumers' funds, such as our Payment Processing business, are subject to numerous state and federal regulations, including those related to banking, credit cards, electronic transactions and communication, escrow, fair credit reporting, privacy of financial records and others. State money transmitter regulations and federal anti-money laundering and money services business regulations can also apply under some circumstances. The application of many of these laws with regard to electronic commerce is currently unclear. In addition, it is possible that a number of laws and regulations may be applicable or may be adopted in the future with respect to conducting business over the Internet concerning matters such as taxes, pricing, content and distribution. If applied to us, any of the foregoing rules and regulations could require us to change the way we do business in a way that increases costs or makes our business more complex. In addition, violation of some statutes may result in severe penalties or restrictions on our ability to engage in e-commerce, which could have a material adverse effect on our business.

Our clients also include telecommunications companies that, to the extent that they extend consumer credit, may be subject to federal and state regulations. In making credit evaluations of consumers, performing fraud screening or user authentication, our clients are subject to requirements of federal law, including the Equal Credit Opportunity Act (ECOA), the Fair Credit Reporting Act (FCRA) and the Gramm-Leach-Bliley Act (GLBA) and regulations thereunder, as well as state laws which impose a variety of additional requirements. Privacy legislation may also affect the nature and extent of the products or services that we can provide to clients as well as our ability to collect, monitor and disseminate information subject to privacy protection. Although most of the products and services we provide to the telecommunications industry, other than our ProFile service, are not directly subject to these requirements, we

must take these extensive and evolving requirements into account in order to meet our clients' needs. In some cases, consumer credit laws require our clients to notify consumers of credit decisions made in connection with their applications for telecommunications services, and we have contracted with some of our clients, including Sprint, AT&T, Nextel, and Dobson Communications, Inc., to provide such notices on their behalf. Our software has in the past contained, and could in the future contain, undetected errors affecting compliance by our clients with one or more of these legal requirements. Failure to properly implement these requirements in our products and services in a timely, cost-effective and accurate manner could result in liability, either directly or as indemnitor of our clients, damage to our reputation and relationships with clients and a loss of business.

**Table of Contents**

Consumer protection laws in the areas of privacy, credit and financial transactions have been evolving rapidly at the state, federal and international levels. As the electronic transmission, processing and storage of financial information regarding consumers continues to grow and develop, it is likely that more stringent consumer protection laws may impose additional burdens on companies involved in such transactions. Uncertainty and new laws and regulations, as well as the application of existing laws to e-commerce, could limit our ability to operate in our markets, expose us to compliance costs and substantial liability and result in costly and time-consuming litigation.

Furthermore, the growth and development of the market for e-commerce may prompt more stringent consumer protection laws that may impose additional regulatory burdens on those companies, such as Lightbridge, that provide services to online business. The adoption of additional laws or regulations may affect the ability to offer, or cost effectiveness of offering, goods or services online, which could, in turn, decrease the demand for our products and services and increase our cost of doing business.

The Securities and Exchange Commission and the National Association of Securities Dealers, Inc. have also enacted regulations affecting our corporate governance, securities disclosure and compliance practices. We expect these regulations to increase our compliance costs and to make some of our activities more time-consuming. If we fail to comply with any of these regulations, we could be subject to legal actions by regulatory authorities or private parties.

**We May Become a Party to Intellectual Property Infringement Claims, Which Could Harm Our Business.**

From time to time, we have had and may be forced to respond to or prosecute other intellectual property infringement claims to protect our rights or defend a client's rights. These claims, regardless of merit, may consume valuable management time, result in costly litigation or cause product shipment delays, all of which could seriously harm our business and operating results. Furthermore, parties making such claims may be able to obtain injunctive or other equitable relief that could effectively block our ability to make, use, sell or otherwise practice our intellectual property, whether or not patented or described in pending patent applications, or to further develop or commercialize our products in the U.S. and abroad and could result in the award of substantial damages against us. We may be required to enter into royalty or licensing agreements with third parties claiming infringement by us of their intellectual property in order to settle these claims. These royalty or licensing agreements, if available, may not have terms that are acceptable to us. In addition, if we are forced to enter into a license agreement with terms that are unfavorable to us, our operating results would be materially harmed. We may also be required to indemnify our clients for losses they may incur under indemnification agreements if we are found to have violated the intellectual property rights of others. Please refer to Part II - Other Information, Item 1, Legal Proceedings for a discussion of certain pending matters related to our intellectual property.

In connection with the sale of our INS business to VeriSign on June 14, 2005, we agreed to indemnify VeriSign for up to \$5 million in damages incurred for potential breaches of our intellectual property representations and warranties in the asset purchase agreement. Such representations and warranties extend for two years from the date of closing.

**Our Future Revenues May Be Uncertain Because of Reliance on Third Parties for Marketing and Distribution.**

Authorize.Net distributes its service offerings primarily through outside sales partners. Authorize.Net's revenues are derived predominantly through relationships with distribution partners. In addition, we have entered into a business alliance with VeriSign to assist us in penetrating the online transaction market for authentication services.

We intend to continue to market and distribute our current and future products and services through existing and other relationships both in and outside of the United States. There are no minimum purchase obligations applicable to any existing distributor or other sales and marketing partners and we do not expect to have any guarantees of continuing orders. Failure by our existing and future distributors or other sales and marketing partners to generate significant revenues or our failure to establish additional distribution or sales and marketing alliances or changes in the industry that render third party distribution networks obsolete could have a material adverse effect on our business, operating results and financial condition.

In addition, distributors and other sales and marketing partners may become our competitors with respect to the products they distribute either by developing a competitive product themselves or by distributing a competitive offering. For example, resellers of Authorize.Net products and services are permitted to and generally do market and sell competing products and services; and VeriSign may elect to market or acquire alternative fraud and identity

verification products for authentication services. Competition from existing and future distributors or other sales and marketing partners could significantly harm sales of our products.

**Table of Contents****Changes to Credit Card Association Rules or Practices Could Adversely Impact Our Authorize.Net Business.**

Our Authorize.Net credit card payment gateway does not directly access the credit card associations. As a result, we must rely on banks and their service providers to process our transactions. We must comply with the operating rules of the credit card associations. The associations' member banks set these rules, and the associations interpret the rules. Some of those member banks compete with Authorize.Net. Visa, MasterCard, American Express or Discover could adopt new operating rules or interpretations of existing rules which we might find difficult or even impossible to comply with, resulting in our inability to give customers the option of using credit cards to fund their payments. If we were unable to provide a gateway for credit card transactions, our Authorize.Net business would be materially and adversely affected.

**We Could Be Subject to Liability as a Result of Security Breaches, Service Interruptions by Cyber Terrorists or Fraudulent or Illegal Use of Our Services.**

Because some of our activities involve the storage and transmission of confidential personal or proprietary information, such as credit card numbers and social security numbers, and because we are a link in the chain of e-commerce, security breaches, service interruptions and fraud schemes could damage our reputation and expose us to a risk of loss or litigation and possible monetary damages. Cyber terrorists have periodically interrupted, and may continue to interrupt, our payment gateway services in attempts to extort payments from us or disrupt commerce. Our payment gateway services may be susceptible to credit card and other payment fraud schemes, including unauthorized use of credit cards or bank accounts, identity theft or merchant fraud. We expect that technically sophisticated criminals will continue to attempt to circumvent our anti-fraud systems. If such fraud schemes become widespread or otherwise cause merchants to lose confidence in our services in particular, or in Internet systems generally, our business could suffer.

In addition, the large volume of payments that we handle for our clients makes us vulnerable to third-party or employee fraud or other internal security breaches. Further, we may be required to expend significant capital and other resources to protect against security breaches and fraud to address any problems they may cause.

Our payment system may also be susceptible to potentially illegal or improper uses. These uses may include illegal online gambling, fraudulent sales of goods or services, illicit sales of prescription medications or controlled substances, software and other intellectual property piracy, money laundering, bank fraud, child pornography trafficking, prohibited sales of alcoholic beverages and tobacco products and online securities fraud. Despite measures we have taken to detect and lessen the risk of this kind of conduct, we cannot ensure that these measures will succeed. In addition, regulations under the USA Patriot Act of 2001 may require us to revise the procedures we use to comply with the various anti-money laundering and financial services laws. Our business could suffer if clients use our system for illegal or improper purposes or if the costs of complying with regulatory requirements increase significantly.

Authorize.Net is compliant with Visa's Cardholder Information Security Program (CISP) and MasterCard's Site Data Protection (SDP) standard. However, there is no guarantee that we will maintain such compliance or that compliance will prevent illegal or improper use of our payment system.

We have expended, and may be required to continue to expend, significant capital resources to protect against security breaches, service interruptions and fraud schemes. Our security measures may not prevent security breaches, service interruptions and fraud schemes and the failure to do so may disrupt our business, damage our reputation and expose us to risk of loss or litigation and possible monetary damages.

**A Failure of, Error in or Damage to Our Computer and Telecommunications Systems Would Impair Our Ability to Conduct Transactions, Payment Processing and Support Services and Harm Our Business Operations.**

We provide TDS and payment processing transaction services, as well as support services, using complex computer and telecommunications systems. Our business could be significantly harmed if these systems fail or suffer damage from fire, natural disaster, terrorism including cyber terrorism, power loss, telecommunications failure, unauthorized access by hackers, electronic break-ins, intrusions or attempts to deny our ability to deploy our services, computer viruses or similar events. In addition, a growth of our client base, a significant increase in transaction volume or an expansion of our facilities may strain the capacity of our computers and telecommunications systems and lead to degradations in performance or system failure. Many of our agreements with telecommunications carriers

contain level of service commitments, which we might be unable to fulfill in the event of a natural disaster, an actual or threatened terrorist attack or a major system failure. Errors in our computer and telecommunications systems may adversely impact our ability to provide the products and services contracted for by our clients. We may need to expend significant capital or other resources to protect against or repair damage to our systems that occur as a result of malicious activities, cyber-terrorism, natural disasters or human error, but these protections and repairs may not be completely effective. Our property and business interruption insurance and errors and omissions insurance might not be adequate to compensate us for any losses that may occur as the result of these types of damage. It is also possible that such insurance might cease to be available to us on commercially reasonable terms, or at all.

**Table of Contents**

**The Demand for Our Payment Processing Products and Services Could Be Negatively Affected by a Reduced Growth of e-Commerce or Delays in the Development of the Internet Infrastructure.**

Sales of goods and services over the Internet do not currently represent a significant portion of overall sales of goods and services. We depend on the growing use and acceptance of the Internet as an effective medium of commerce by merchants and customers in the United States and as a means to grow our business. We cannot be certain that acceptance and use of the Internet will continue to develop or that a sufficiently broad base of merchants and consumers will adopt, and continue to use, the Internet as a medium of commerce.

It is also possible that the number of Internet users, or the use of Internet resources by existing users, will continue to grow, and may overwhelm the existing Internet infrastructure. Delays in the development or adoption of new standards and protocols required to handle increased levels of Internet activity could also have a detrimental effect on the Internet and correspondingly on our business. These factors would adversely affect usage of the Internet, and lower demand for our products and services.

**Our Reliance on Suppliers and Vendors Could Adversely Affect Our Ability to Provide Our Services and Products to Our Clients on a Timely and Cost-Efficient Basis.**

We rely to a substantial extent on third parties to provide some of our equipment, software, data, systems and services. In some circumstances, we rely on a single supplier or limited group of suppliers. For example, our Payment Processing business requires the services of third-party payment processors. If any of these processors cease to allow us to access their processing platforms, our ability to process credit card payments would be severely impacted. In addition, we depend on our Originating Depository Financial Institution partner to process ACH transactions, and our ability to process these transactions would be severely impacted if we were to lose such partner for any reason.

Our reliance on outside vendors and service providers also subjects us to other risks, including a potential inability to obtain an adequate supply of required components and reduced control over quality, pricing and timing of delivery of components. For example, in order to provide our credit verification service, we need access to third-party credit information databases provided to us by outside vendors. Similarly, delivery of our activation services often requires the availability and performance of billing systems which are also supplied by outside vendors. If for any reason we were unable to access these databases or billing systems, our ability to process credit verification transactions could be impaired.

In addition, our business is materially dependent on services provided by various telecommunications providers. A significant interruption in telecommunications services including, without limitation, a power loss could seriously harm our business.

From time to time, we must also rely upon third parties to develop and introduce components and products to enable us, in turn, to develop new products and product enhancements on a timely and cost-effective basis. We may not be able to obtain access, in a timely manner, to third-party products and development services necessary to enable us to develop and introduce new and enhanced products. We may not be able to obtain third-party products and development services on commercially reasonable terms and we may not be able to replace third-party products in the event such products become unavailable, obsolete or incompatible with future versions of our products.

**We Have Made and May Continue to Make Acquisitions, Which Involve Risks.**

We acquired Authorize.Net Corporation in March of 2004. We may also make additional acquisitions in the future if we identify companies, technologies or assets that appear to expand or complement our core business. Acquisitions involve risks that could cause the actual results of any acquisitions we make to differ from our expectations. If we are not able to make acquisitions, we may not be able to expand our business. For example:

We may experience difficulty in integrating and managing acquired businesses successfully and in realizing anticipated economic, operational and other benefits in a timely manner. The need to retain existing clients, employees, and sales and distribution channels of an acquired company and to integrate and manage differing corporate cultures can also present significant risks. If we are unable to successfully integrate and manage acquired businesses, we may incur substantial costs and delays or other operational, technical or financial problems.



Our acquisition of Authorize.Net significantly reduced our available cash and liquidity. In other future acquisitions, we may issue equity securities that could be dilutive to our shareholders or we may use our remaining cash, which may have an adverse effect on our liquidity. We also may incur additional debt and amortization expense related to intangible assets as a result of acquisitions. This additional debt and amortization expense, as well as the potential impairment of any purchased goodwill, may materially and adversely affect our business and operating results. We may also be required to make continuing investments in acquired products or technologies to bring them to market, which may negatively affect our cash flows and net income.

**Table of Contents**

We may also incur additional costs relating to the integration, review and evaluation and enhancement of our internal controls for Authorize.Net. In addition, we may assume contingent liabilities that may be difficult to estimate and costs and liabilities associated with assumed litigation matters.

Acquisitions may divert management's attention from our existing business and may damage our relationships with our key clients and employees.

Acquisitions may also result in liabilities for claims not known at the time of acquisition as well as for assumed obligations.

**The Success of Our Business Strategy Is Dependent on Our Ability to Expand into New or Complementary Markets.**

As part of our business strategy, we are seeking to expand our business into new markets or markets that are complementary to our existing core business. If we are not able to expand successfully into new markets, our financial results and future prospects may be harmed. Our ability to enter new markets depends on a number of factors, including:

growth in our targeted markets;

our ability to provide products and services to address the needs of those markets; and

competition in those markets.

**If We Do Not Continue to Enhance Our Existing Products and Services, and Develop or Acquire New Ones, We Will Not Be Able to Compete Effectively.**

The industries in which we do business or intend to do business have been changing rapidly as a result of increasing competition, technological advances, regulatory changes and evolving industry practices and standards, and we expect these changes will continue. Current and potential clients have also experienced significant changes as the result of consolidation among existing industry participants and economic conditions. In addition, the business practices and technical requirements of our clients are subject to changes that may require modifications to our products and services. In order to remain competitive and successfully address the evolving needs of our clients, we must commit a significant portion of our resources to:

identify and anticipate emerging technological and market trends affecting the markets in which we do business;

enhance our current products and services in order to increase their functionality, features and cost-effectiveness to clients that are seeking to control costs and to meet regulatory requirements;

develop or acquire new products and services that meet emerging client needs, such as products and services for the online market;

modify our products and services in response to changing business practices and technical requirements of our clients, as well as to new regulatory requirements;

integrate our current and future products with third-party products; and

create and maintain interfaces to changing client and third party systems.

We must achieve these goals in a timely and cost-effective manner and successfully market our new and enhanced products and services to clients. In the past, we have experienced errors or delays in developing new products and services and in modifying or enhancing existing products and services. If we are unable to expand or appropriately enhance or modify our products and services quickly and efficiently, our business and operating results will be adversely affected.

**We Need to Continue to Improve or Implement our Procedures and Controls.**

Requirements adopted by the Securities and Exchange Commission in response to the passage of the Sarbanes-Oxley Act of 2002 require annual review and evaluation of our internal control systems, and attestation of these systems by our registered independent public accounting firm. As permitted by the rules and regulations of the Securities and Exchange Commission, management determined that the internal control over financial reporting of Authorize.Net would be excluded from the final 2004 internal control assessment. Our disclosure controls and procedures as of June 30, 2005 were not fully effective as of that date to provide a reasonable level of assurance of reaching the Company's disclosure control objectives and, during the second quarter of 2005, we took certain steps to address that matter. We continue to evaluate such disclosure controls and procedures, including with regard to Authorize.Net, which was acquired in March 2004, and may modify, enhance or supplement them as appropriate in the future. Please refer to Part I, Item 4 below for a discussion on controls and procedures.

## **Table of Contents**

We need to periodically review our internal control procedures, modify, enhance or supplement them as may be necessary and consider the adequacy of the documentation of such procedures. There can be no assurance that we will be able to maintain compliance with all of the new requirements. Any modifications, enhancements or supplements to our internal control systems or in documentation of such internal control systems and the internal control assessment of Authorize.Net could be costly to prepare or implement, divert attention of management or finance staff, and may cause our operating expenses to increase over the ensuing year.

### **Our Business May Be Harmed by Errors in Our Software.**

The software that we develop and license to clients, and that we also use in providing our transaction processing and call center services, is extremely complex and contains hundreds of thousands of lines of computer code. Large, complex software systems such as ours are susceptible to errors. The difficulty of preventing and detecting errors in our software is compounded by the fact that we maintain multiple versions of our systems to meet the differing requirements of our major clients, and must implement frequent modifications to these systems in response to these clients' evolving business policies and technical requirements. Our software design, development and testing processes are not always adequate to detect errors in our software prior to its release or commercial use. As a result, we have from time to time discovered, and may likely in the future discover, errors in software that we have put into commercial use for our clients, including some of our largest clients. Because of the complexity of our systems and the large volume of transactions they process on a daily basis, we sometimes have not detected software errors until after they have affected a significant number of transactions. Software errors can have the effect of causing clients that utilize our products and services to fail to comply with their intended credit or business policies, or to fail to comply with legal requirements, such as those under the ECOA, FCRA, or GLBA.

Such errors, particularly if they affect a major client, can harm our business in several ways, including the following:

- we may suffer a loss of revenue if, due to software errors, we are temporarily unable to provide products or services to our clients;

- we may not be paid for the products or services provided to a client that contain errors, or we may be liable for losses or damages sustained by a client or its subscribers as a result of such errors;

- we may incur additional unexpected expenses to correct errors in our software, or to fund product development projects that we may undertake to minimize the occurrences of such errors in the future;

- we may damage our relationships with clients or suffer a loss of reputation within our industry;

- we may become subject to litigation or regulatory scrutiny; and

- our clients may terminate or fail to renew their agreements with us or reduce the products and services they purchase from us.

Our errors and omissions insurance may not adequately compensate us for losses that may occur due to software errors. It is also possible that such insurance might cease to be available to us on commercially reasonable terms or at all.

### **Our Initiatives to Improve Our Software Design and Development Processes May Not Be Successful.**

The development of our products has, in some cases, extended over a period of more than ten years. This incremental development process has resulted in systems which are extremely complex. Systems of the size and complexity of ours are inherently difficult to modify and maintain. We have implemented and are also evaluating changes in our product development, testing and control processes to improve the accuracy and timeliness of modifications that we make to our software, including the frequent modifications that we must make in response to changes in the business policies and technical requirements of our clients. We believe that our initiatives to implement a new product architecture and to improve our product development, test and control processes will be important to our future competitive position and success. If we are not successful in carrying out these initiatives on a timely basis

or in a manner that is acceptable to our clients, our business and future prospects could be harmed.

**We May Not Be Able to Successfully Manage Operational Changes.**

Over the last several years, our operations have experienced rapid growth in some areas and significant restructurings and cutbacks in others. These changes have created significant demands on our executive, operational, development and financial personnel and other resources. If we achieve future growth in our business, or if we are forced to make additional restructurings, we may further strain our management, financial and other resources. Our future operating results will depend on the ability of our officers and key employees to manage changing business conditions and to continue to improve our operational and financial controls and reporting systems. We cannot ensure that we will be able to successfully manage the future changes in our business.

## **Table of Contents**

### **Our Quarterly Operating Results May Fluctuate.**

Our operating results are difficult to predict and may fluctuate significantly from quarter to quarter. If our operating results fall below the expectations of investors or public market analysts, the price of our common stock could fall dramatically. Our common stock price could also fall dramatically if investors or public market analysts reduce their estimates of our future quarterly operating results, whether as a result of information we disclose, or based on industry, market or economic trends, or other factors.

Our revenues are difficult to forecast for a number of reasons:

Seasonal and retail trends affect our transaction revenues, in both our Payment Processing and TDS businesses, as well as our other products and services. Transaction revenues historically have represented the majority of our total revenues. As a result, our revenues can fluctuate. For example, our revenues generally have been highest in the fourth quarter of each calendar year, particularly in the holiday shopping season between Thanksgiving and Christmas. In addition, marketing initiatives undertaken by our clients or their competitors may significantly affect the number of transactions we process.

The sales process for our products and services offered to telecommunications clients is lengthy, sometimes exceeding twenty-four months. The length of the sales process makes our revenues difficult to predict. The delay of one or more large orders, could cause our quarterly revenues to fall substantially below expectations.

Our consulting services revenues can fluctuate based on the timing of product sales and projects we perform for our clients. Many of our consulting engagements are of a limited duration, so it can be difficult for us to forecast consulting services revenues or staffing requirements accurately more than a few months in advance.

The factors described above under the headings **If One or More of Our Major Clients Stops Using Our Products or Services or Changes the Combination of Products and Services It Uses, Our Operating Results Would Suffer Significantly**, **Certain of Our Revenues Are Uncertain Because Our Clients May Reduce the Amounts of or Change the Combination of Our Products or Services They Purchase**, and **A Majority of Our Revenues Are Concentrated in the Wireless Telecommunications Industry, Which Is Experiencing Declining Growth Rates, Consolidation and Increasing Pressure to Control Costs**.

Most of our expenses, particularly employee compensation, are relatively fixed. As a result, even relatively small variations in the timing of our revenues may cause significant variations in our quarterly operating results and may result in quarterly losses.

Our quarterly results may also vary due to the timing and extent of restructuring and other charges that may occur in a given quarter.

As a result of these factors, we believe that quarter-to-quarter comparisons of our results of operations are not necessarily meaningful. You should not rely on our quarterly results of operations to predict our future performance.

### **We Face Significant Competition for a Limited Supply of Qualified Software Engineers, Consultants and Sales and Marketing Personnel.**

Our business depends on the services of skilled software engineers who can develop, maintain and enhance our products, consultants who can undertake complex client projects and sales and marketing personnel. In general, only highly qualified, highly educated personnel have the training and skills necessary to perform these tasks successfully. In order to maintain the competitiveness of our products and services and to meet client requirements, we need to attract, motivate and retain a significant number of software engineers, consultants and sales and marketing personnel. Qualified personnel such as these are in short supply and we face significant competition for these employees, from not only our competitors but also clients and other enterprises. Other employers may offer software engineers, consultants and sales and marketing personnel significantly greater compensation and benefits or more attractive career paths than we are able to offer. Any failure on our part to hire, train and retain a sufficient number of qualified personnel would seriously damage our business.

### **Changes in Management Could Affect Our Ability to Operate Our Business.**

Our future success will depend to a significant degree on the skills, experience and efforts of our executive officers. The loss of any of our executive officers could impair our ability to successfully manage our current business or implement our planned business objectives and our future operations may be adversely affected.

**Table of Contents**

**We Face Competition from a Broad and Increasing Range of Vendors.**

The market for products and services offered to communications providers and participants in online transactions is highly competitive and subject to rapid change. Each of these markets is fragmented, and a number of companies currently offer one or more products or services competitive with ours. We anticipate continued growth and the formation of new alliances in each of the markets in which we compete, which will result in the entrance of new or the creation of bigger competitors in the future. For example, in October 2005, VeriSign, Inc. announced that PayPal, Inc. agreed to acquire VeriSign's payment gateway business and to form a strategic alliance with VeriSign, Inc. for on-line commerce and security. We face potential competition from several primary sources:

providers of online payment processing services, including VeriSign, Inc., CyberSource Corporation, Plug & Pay Technologies, Inc., PayPal, Inc. and LinkPoint International, Inc.

software vendors that provide one or more customer acquisition, customer relationship management and retention or risk management solutions, including ECtel Ltd., TSI Telecommunications Services Inc., Fair Isaac Corporation, Magnum Software Systems, Inc., American Management Systems, Incorporated and SLP Infoware;

service providers that offer customer acquisition, customer relationship management and retention, risk management or authentication services in connection with other services, including Choicepoint Inc., Visa U.S.A., Experian Information Solutions, Inc., Equifax, Inc., Lexis Nexis, Trans Union, L.L.C., Schlumberger Sema plc and Amdocs Ltd;

information technology departments within larger carriers that have the ability to provide products and services that are competitive with those we offer;

information technology vendors that offer wireless and internet software applications such as Oracle Corporation, Microsoft Corporation and International Business Machines Corporation;

consulting firms or systems integrators that may offer competitive services or the ability to develop customized solutions for customer acquisition and qualification, customer relationship management and retention or risk management, such as American Management Systems, Incorporated, Accenture Ltd., BearingPoint, Inc., PeopleSoft, Inc., Siebel Systems, Inc. and Cap Gemini Ernst & Young;

a number of alternative technologies, including profilers, personal identification numbers and authentication, provided by companies such as Verizon Communications, Inc., Authentix Network Inc. and Fair Isaac Corporation;

vendors that provide or resell products and services in the voice conferencing market such as Spectel, Inc., Polycom Inc., Raindance Communications, Inc., Ptek Holdings, Inc., and the major worldwide telecommunications providers such as AT&T, Sprint, and Global Crossing Limited.

Because competitors can easily penetrate one or more of our markets, we anticipate additional competition from other established and new companies. In addition, competition may intensify as competitors establish cooperative relationships among themselves or alliances with others.

Many of our current and potential competitors have significantly greater financial, marketing, technical and other competitive resources than we do. As a result, these competitors may be able to adapt more quickly to new or emerging technologies and changes in client requirements, or may be able to devote greater resources to the promotion and sale of their products and services. In addition, in order to meet client requirements, we must often work cooperatively with companies that are, in other circumstances, competitors. The need for us to work cooperatively with such companies may limit our ability to compete aggressively with those companies in other circumstances.



**Our Success Depends in Part on Our Ability to Obtain Patents for, or Otherwise Protect, Our Proprietary Technologies.**

We rely on a combination of copyright, patent, trademark and trade secret laws, license and confidentiality agreements, and software security measures to protect our proprietary rights. Much of our know-how and other proprietary technology is not covered by patent or similar protection, and in many cases cannot be so protected. If we cannot obtain patent or other protection for our proprietary software and other proprietary intellectual property rights, other companies could more easily enter our markets and compete successfully against us.

We have a limited number of patents in the U.S. and abroad, and have pending applications for additional patents, but we cannot be certain that any additional patents will be issued on those applications, that any of our current or future patents will protect our business or technology against competitors that develop similar technology or products or services or provide us with a competitive advantage, or that others will not claim rights in our patents or our proprietary technologies.

## **Table of Contents**

Patents issued and patent applications filed relating to products used in the wireless telecommunications and payment processing industry are numerous and it may be the case that current and potential competitors and other third parties have filed or will file applications for, or have received or will receive, patents or obtain additional proprietary rights relating to products used or proposed to be used by us. We may not be aware of all patents or patent applications that may materially affect our ability to make, use or sell any current or future products or services.

The laws of some countries in which our products are licensed do not protect our products and intellectual property rights to the same extent as U.S. laws. We generally enter into non-disclosure agreements with our employees and clients and restrict access to, and distribution of, our proprietary information. Nevertheless, we may be unable to deter misappropriation of our proprietary information or detect unauthorized use of and take appropriate steps to enforce our intellectual property rights. Our competitors also may independently develop technologies that are substantially equivalent or superior to our technology.

### **Our Foreign Operations Subject Us to Risks and Concerns Which Could Negatively Affect Our Business Overall.**

We have operations outside the U.S. at our call center located in Liverpool, Nova Scotia, Canada. In addition to the risks generally associated with operations in the U.S., operations in foreign countries present us with additional risks, including the following:

- the imposition of financial and operational controls and regulatory restrictions by foreign governments;

- the need to comply with a wide variety of complex U.S. and foreign import and export laws and treaties;

- fluctuations in interest and currency exchange rates; and

- difficulties in managing staffing and managing foreign subsidiary operations.

### **Our Business Could Require Additional Financing.**

Our future business activities, including our operation of Authorize.Net, the development or acquisition of new or enhanced products and services, the acquisition of additional computer and network equipment, the costs of compliance with government regulations and future expansions including acquisitions will require us to make significant capital expenditures. If our available cash resources prove to be insufficient, because of unanticipated expenses, revenue shortfalls or otherwise, we may need to seek additional financing or curtail our expansion activities. If we obtain equity financing for any reason, our existing stockholders may experience dilution in their investments. If we obtain debt financing, our business could become subject to restrictions that affect our operations or increase the level of risk in our business. It is also possible that, if we need additional financing, we will not be able to obtain it on acceptable terms, or at all.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE MARKET RISK DISCLOSURES.**

The market risk exposure inherent in our financial instruments and consolidated financial position represents the potential losses arising from adverse changes in interest rates. We are exposed to such interest rate risk primarily in our significant investment in cash and cash equivalents. Cash and cash equivalents include short-term, highly liquid instruments which consist primarily of money market accounts, purchased with remaining maturities of three months or less. Our short term investments also include debt securities maturing in one year or less that are classified as available for sale. These investments are carried at fair value. We do not execute transactions in or hold derivative financial instruments for trading or hedging purposes.

The amortized cost of available-for-sale debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Realized gains and losses, and declines in value judged to be other than temporary on available-for-sale debt securities, if any, are included in interest income, net. The cost of securities sold is based on the specific identification method. Interest and dividends on securities are included in interest income, net.

Market risk for cash and cash equivalents is estimated as the potential change in the fair value of the assets or obligations resulting from a hypothetical ten percent adverse change in interest rates, which would not have been significant to our financial position or results of operations during 2005.

We are not subject to any material market risk associated with foreign currency exchange rates.



**Table of Contents****ITEM 4. CONTROLS AND PROCEDURES**

The Company evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of September 30, 2005. The Company's Chief Executive Officer and its Chief Financial Officer supervised and participated in this evaluation. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2005, the Company's disclosure controls and procedures were effective to provide a reasonable level of assurance of reaching the Company's disclosure control objectives.

The effectiveness of a system of disclosure controls and procedures is subject to various inherent limitation, including cost limitations, judgments used in decision making, assumptions about the likelihood of future events, the soundness of internal controls, and fraud. Due to such inherent limitations, there can be no assurance that any system of disclosure controls and procedures will be successful in preventing all errors or fraud, or in making all material information known in a timely manner to the appropriate levels of management. The Company continues to evaluate its disclosure controls and procedures and may modify, enhance or supplement them as appropriate in the future.

There has not been any change in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) that occurred in the quarter ended September 30, 2005 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

In 2001, Net MoneyIN, Inc. brought a patent infringement suit in the United States District Court for the District of Arizona, entitled *Net MoneyIN, Inc. v. VeriSign, Inc., et al.*, Case No. CIV 01-441 TUC RCC. Defendants in this case include InfoSpace, Inc. and E-Commerce Exchange, Inc.

On March 31, 2004, we acquired Authorize.Net from InfoSpace, Inc. In the purchase agreement, we agreed to indemnify and defend InfoSpace, Inc. against this lawsuit. E-Commerce Exchange, Inc. was a reseller of services provided by Authorize.Net. The reseller agreement between the parties contains provisions regarding indemnification from Authorize.Net for claims against the reseller related to services provided under that agreement. Defendant Wells Fargo Bank, N.A. has also requested indemnification, including defense costs, from Authorize.Net based on certain contracts with Authorize.Net. Neither Lightbridge nor Authorize.Net is a party to the *Net MoneyIN* lawsuit, but because we are defending the litigation and providing indemnification to some of the defendants, we have potential exposure to liability (in an undetermined amount) as if we were party to the lawsuit. As with all major litigation, such liability could be significant and could, if the result of the lawsuit is adverse to us, materially adversely affect our business, operations and financial condition. We and Authorize.Net may be added as parties at a later date.

The lawsuit alleges infringement of certain patents involving payment processing over computer networks, and names a variety of defendants, including payment processing gateway providers and banks. Net MoneyIN alleges that numerous products or services infringe its patents, including the Authorize.Net Payment Gateway Service and eCheck.Net service, and seeks treble damages, permanent injunctive relief, attorneys' fees and costs. Injunctive relief adverse to us could materially adversely affect our business operations and financial condition.

The defendants have denied the allegations of the plaintiff and have counterclaimed, seeking a declaration that plaintiff's patents have not been infringed and are invalid. The litigation is bifurcated, with separate liability and damages phases. The period designated for fact discovery during the liability phase has concluded. Following a claim construction hearing, the court issued an order on October 18, 2005 construing terms in one patent claim and finding other claims invalid. No liability-phase trial date has been set. We incurred legal expenses in 2004 of approximately \$200,000 in connection with the defense of this lawsuit following our acquisition of Authorize.Net, and expect to incur defense costs of approximately \$1.2 million to \$1.5 million in 2005. We intend to vigorously pursue available defenses to the lawsuit.

**Item 2. Changes in Securities, Use of Proceeds and Issuer Purchases of Equity Securities**

*Stock Repurchases* On October 4, 2001, we announced that our board of directors authorized the repurchase of up to 2 million shares of our common stock at an aggregate price of up to \$20 million. The shares may be purchased from time to time on or after October 8, 2001, depending on market conditions. On April 23, 2003, the board approved an

expansion of the plan to authorize us to purchase up to 4 million shares of our common stock at an aggregate price of up to \$40 million through September 26, 2005. As of September 30, 2005, we had purchased approximately 2.5 million shares at a total cost of approximately \$17.9 million since the inception of its repurchase program. There were no repurchases during the first nine months of 2005. The maximum number of shares that could yet be purchased under the plan was 1,452,862 at September 30, 2005.

**Table of Contents**

**Item 6. Exhibits**

**(a) Exhibits**

<b>No.</b>	<b>Description</b>
31.1	Certification of Robert E. Donahue dated November 4, 2005
31.2	Certification of Timothy C. O'Brien dated November 4, 2005
32.1	Certification of Robert E. Donahue and Timothy C. O'Brien dated November 4, 2005 (furnished but not filed with the Securities and Exchange Commission)
99.1	First Amendment to the lease between EOP Operating Limited Partnership, and Lightbridge, Inc. dated May 3, 2005

**Table of Contents**

**SIGNATURE**

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

LIGHTBRIDGE, INC.

Date: November 4, 2005

By: /s/ Timothy C. O Brien  
Timothy C. O Brien  
Vice President, Finance and  
Administration,  
Chief Financial Officer and Treasurer  
(Principal Financial and Chief  
Accounting  
Officer)