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

FORM 10-Q

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

For the quarterly period ended September 30, 2005

Commission File Number 000-30229

SONUS NETWORKS, INC.
(Exact name of Registrant as specified in its charter)

DELAWARE	**04-3387074**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)

250 Apollo Drive, Chelmsford, Massachusetts 01824
(Address of principal executive offices, including zip code)

(978) 614-8100
(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 x No o

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

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

As of October 31, 2005, there were 249,378,820 shares of $0.001 par value per share, common stock outstanding.

SONUS NETWORKS, INC.
FORM 10-Q
QUARTER ENDED SEPTEMBER 30, 2005
TABLE OF CONTENTS

PART I—FINANCIAL INFORMATION

Item 1: Financial Statements

SONUS NETWORKS, INC.

Condensed Consolidated Balance Sheets

(In thousands, except share data)

(Unaudited)

	September 30, 2005	December 31, 2004
Assets		
Current assets:		
Cash and cash equivalents	$ 134,789	$ 121,931
Marketable debt securities	182,735	170,145
Accounts receivable, net	42,690	32,486
Inventory, net	30,288	28,346
Other current assets	12,637	10,891
Total current assets	403,139	363,799
Property and equipment, net	14,894	8,217
Long-term investments	7,363	21,029
Other assets	720	783
Total	$ 426,116	$ 393,828
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 12,697	$ 8,654
Accrued expenses	14,489	18,240
Accrued restructuring expenses	193	186
Current portion of deferred revenue	80,968	65,105
Convertible subordinated note	10,000	—
Current portion of long-term liabilities	45	30
Total current liabilities	118,392	92,215
Long-term deferred revenue, less current portion	32,392	25,960
Long-term liabilities, less current portion	538	613
Convertible subordinated note	—	10,000
Total liabilities	151,322	128,788
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock, $0.01 par value; 5,000,000 shares authorized, none issued and outstanding	—	—
Common stock, $0.001 par value; 600,000,000 shares authorized, 251,601,576 and 249,755,118 shares issued and 249,304,666 and 247,458,208 shares outstanding at September 30, 2005 and December 31, 2004	252	250
Additional paid-in capital	1,055,548	1,049,142
Accumulated deficit	(780,739)	(784,085)
Treasury stock, at cost; 2,296,910 common shares at September 30, 2005 and December 31, 2004	(267)	(267)
Total stockholders' equity	274,794	265,040
Total	$ 426,116	$ 393,828

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

SONUS NETWORKS, INC.

Condensed Consolidated Statements of Operations

(In thousands, except per share data)

(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2005	2004	2005	2004
Revenues:				
Product	$ 29,107	$ 36,064	$ 92,904	$ 92,896
Service	16,550	10,698	44,456	32,759
Total revenues	45,657	46,762	137,360	125,655
Cost of revenues (1):				
Product	17,410	6,296	39,657	24,151
Service	6,073	4,173	16,993	12,659
Total cost of revenues	23,483	10,469	56,650	36,810
Gross profit	22,174	36,293	80,710	88,845
Operating expenses:				
Research and development (1)	11,787	8,975	33,902	26,826
Sales and marketing (1)	10,834	10,539	31,365	26,034
General and administrative (1)	5,455	6,638	18,732	17,210

Stock-based compensation	11	91	15	606
Amortization of purchased intangible assets	—	601	—	1,801
Total operating expenses	28,087	26,844	84,014	72,477
(Loss) income from operations	(5,913)	9,449	(3,304)	16,368
Interest expense	(121)	(117)	(370)	(360)
Interest income	2,690	1,150	6,787	2,806
(Loss) income before income taxes	(3,344)	10,482	3,113	18,814
(Benefit) provision for income taxes	(640)	214	(233)	598
Net (loss) income	$ (2,704)	$ 10,268	$ 3,346	$ 18,216
Net (loss) income per share—basic and diluted	$ (0.01)	$ 0.04	$ 0.01	$ 0.07
Weighted average shares outstanding:				
Basic	248,801	246,198	248,312	245,394
Diluted	248,801	251,707	253,221	252,776

(1) Excludes non-cash, stock-based compensation expense as follows:

Cost of revenues	$ —	$ 5	$ —	$ 15
Research and development	—	38	—	200
Sales and marketing	11	32	15	295
General and administrative	—	16	—	96
	$ 11	$ 91	$ 15	$ 606

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

SONUS NETWORKS, INC.
Condensed Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Nine months ended September 30,	
	2005	2004
Cash flows from operating activities:		
Net income	$ 3,346	$ 18,216
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	5,256	4,179
Stock-based compensation	15	606
Amortization of purchased intangible assets	—	1,801
Changes in operating assets and liabilities:		
Accounts receivable	(10,204)	(11,648)
Inventory	(1,942)	(13,827)
Other current assets	(1,155)	(5,926)
Accounts payable	4,043	7,851
Accrued expenses and accrued restructuring expenses	(4,390)	(4,528)
Deferred revenue	22,295	989
Net cash provided by (used in) operating activities	17,264	(2,287)
Cash flows from investing activities:		
Purchases of property and equipment	(11,271)	(6,308)
Maturities of available-for-sale marketable debt securities	146,400	152,761
Purchases of available-for-sale marketable debt securities	(151,660)	(154,229)
Maturities of held-to-maturity marketable debt securities and long-term investments	38,316	20,672
Purchases of held-to-maturity marketable debt securities and long-term investments	(31,980)	(30,583)
Increase in restricted cash	(591)	—
Other assets	63	430
Net cash used in investing activities	(10,723)	(17,257)
Cash flows from financing activities:		
Sale of common stock in connection with employee stock purchase plan	4,516	1,721
Proceeds from exercise of stock options	1,877	1,104
Payments of long-term liabilities	(76)	(151)
Net cash provided by financing activities	6,317	2,674
Net increase (decrease) in cash and cash equivalents	12,858	(16,870)
Cash and cash equivalents, beginning of period	121,931	133,715
Cash and cash equivalents, end of period	$ 134,789	$ 116,845
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 244	$ 241
Cash paid for taxes	$ 713	$ 668
Tax refunds received	$ 454	$ —
Non-cash purchases of property and equipment	$ 662	$ —

SONUS NETWORKS, INC.

Notes to Condensed Consolidated Financial Statements

(Unaudited)

(1) Description of Business

Sonus Networks, Inc. (Sonus) was incorporated on August 7, 1997 and is a leading provider of packet voice infrastructure solutions for wireline and wireless service providers. Sonus offers a new generation of carrier-class switching equipment and software that enables telecommunications service providers to deliver voice services over packet-based networks.

(2) Summary of Significant Accounting Policies

The accompanying condensed consolidated financial statements reflect the application of certain significant accounting policies as described in this note and elsewhere in the accompanying condensed consolidated financial statements and notes.

(a) Basis of Presentation and Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements have been prepared by Sonus pursuant to the rules and regulations of the United States Securities and Exchange Commission (SEC) regarding interim financial reporting. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements and should be read in conjunction with the audited financial statements included in Sonus' Annual Report on Form 10-K for the year ended December 31, 2004.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements have been prepared on the same basis as the audited financial statements, and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results of the interim periods presented. The operating results for the interim periods presented are not necessarily indicative of the results expected for the full fiscal year.

The accompanying consolidated financial statements include the accounts of Sonus and its wholly owned subsidiaries. All material intercompany transactions and balances have been eliminated.

Certain balances in the condensed consolidated financial statements as of December 31, 2004 and for the period ended September 30, 2004 have been adjusted to conform to the current year presentation.

(b) Use of Estimates and Judgments

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant estimates and judgments relied upon in preparing these financial statements include revenue recognition for multiple element arrangements, allowances for doubtful accounts, estimated fair value of investments, inventory reserves, expected future cash flows used to evaluate the recoverability of long-lived assets, restructuring and other related charges, contingencies associated with revenue contracts, contingent liabilities, and recoverability of Sonus' net deferred tax assets and related valuation allowance. Although Sonus regularly assesses these estimates, actual results could differ materially from these estimates. Changes in estimates are recorded in the period in which they become known. Sonus bases its estimates on historical experience and various other assumptions that it believes to be reasonable under the

(2) Summary of Significant Accounting Policies (Continued)

circumstances. Actual results may differ from Sonus' estimates if past experience or other assumptions do not turn out to be substantially accurate.

(c) Cash Equivalents, Marketable Securities and Long-Term Investments

Cash equivalents are stated at cost, which approximates market value, and have remaining maturities of three months or less at the date of purchase.

Cash equivalents and marketable debt securities are invested in high quality debt instruments, primarily U.S. Government, municipal and corporate obligations. Investments in U.S. Government and corporate obligations are classified as held-to-maturity, as Sonus has the intent and ability to hold them to maturity. Held-to-maturity marketable debt securities are reported at amortized cost. Investments in municipal obligations are classified as available-for-sale and are reported at fair value. Unrealized gains and losses from available-for-sale marketable debt securities were not material for all periods presented. The unrealized losses related to these securities at September 30, 2005 are not considered to be a permanent decline in the market value of such securities. There have been no material realized gains or losses to date. Current marketable debt securities include held-to-maturity investments with remaining maturities of

less than one year at the date of purchase and available-for-sale investments that are expected to be sold in the current period or to be used in current operations. Long-term investments have remaining maturities of one to five years as of the balance sheet date.

As of September 30, 2005 and December 31, 2004, marketable debt securities consisted of the following, in thousands:

	September 30, 2005			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value
Short-term marketable debt securities				
Available-for-sale:				
State municipal obligations	$ 150,175	$ —	$ —	$ 150,175
Held-to-maturity:				
U.S. government agency notes	6,552	—	(8)	6,544
Corporate debt securities	18,914	—	(132)	18,782
Commercial paper	7,094	—	(3)	7,091
	$ 182,735	$ —	$ (143)	$ 182,592
Long-term marketable debt securities				
Held-to-maturity:				
U.S. government agency notes	$ 5,568	$ —	$ (75)	$ 5,493
Corporate debt securities	1,795	—	(22)	1,773
	$ 7,363	$ —	$ (97)	$ 7,266

SONUS NETWORKS, INC.

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

(2) Summary of Significant Accounting Policies (Continued)

	December 31, 2004			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value
Short-term marketable debt securities				
Available-for-sale:				
State municipal obligations	$ 144,548	$ —	$ —	$ 144,548
Held-to-maturity:				
U.S. government agency notes	5,600	1	—	5,601
Corporate debt securities	19,997	—	(103)	19,894
Commercial paper	—	—	—	—
	$ 170,145	$ 1	$ (103)	$ 170,043
Long-term marketable debt securities				
Held-to-maturity:				
U.S. government agency notes	$ 5,566	$ —	$ (9)	$ 5,557
Corporate debt securities	15,463	—	(190)	15,273
	$ 21,029	$ —	$ (199)	$ 20,830

As of September 30, 2005, Sonus had $591,000 in restricted cash, which is used to collateralize standby letters of credit. Restricted cash is included in Other Current Assets on the Condensed Consolidated Balance Sheet.

(d) Concentrations of Credit and Off-Balance Sheet Risk, Significant Customers and Limited Suppliers

The financial instruments that potentially subject Sonus to concentrations of credit risk are cash, cash equivalents, marketable securities, accounts receivables and long-term investments. Sonus has no off-balance sheet arrangements such as foreign exchange contracts, options contracts or other foreign hedging arrangements as of September 30, 2005. During the three months ended September 30, 2005, Sonus entered into foreign exchange contracts to hedge against currency fluctuations related to a particular account receivable denominated in Japanese Yen which were completed by September 30, 2005. Sonus' cash, cash equivalent and investment portfolio holdings are diversified among five financial institutions.

The following customers contributed 10% or more of Sonus' revenues in the three and nine months ended September 30, 2005 and 2004:

	Three months ended September 30,		Nine months ended September 30,	
Customer:	2005	2004	2005	2004
A	33%	*	29%	10%
B	*	38%	*	16
C	*	*	*	10
D	*	*	*	10
E	*	27%	*	18

* Represents less than 10% of revenues.

(2) Summary of Significant Accounting Policies (Continued)

One customer at September 30, 2005 and two customers at December 31, 2004, each accounted for 10% or more of Sonus' accounts receivable balance, representing an aggregate of 49% and 53% of total accounts receivable, respectively. Sonus performs ongoing credit evaluations of its customers and generally does not require collateral on accounts receivable. Sonus maintains allowances for potential credit losses and such losses have been within management's expectations.

International revenues, primarily attributable to Japan and Europe, were 21% and 6% of total revenues for the three months ended September 30, 2005 and 2004, respectively, and were 20% and 15% of total revenues for the nine months ended September 30, 2005 and 2004, respectively. All international sales are denominated in U.S. dollars. The effect of foreign currency gains or losses is not material as of September 30, 2005 and December 31, 2004.

Certain components and software licenses from third parties used in Sonus' products are procured from single sources of supply. The failure of a supplier, including a subcontractor, to deliver on schedule could delay or interrupt Sonus' delivery of products and thereby materially adversely affect Sonus' revenues and operating results.

(e) Accounts Receivable

Accounts receivable consist of the following, in thousands:

	September 30, 2005	December 31, 2004
Earned accounts receivable	$ 28,572	$ 9,088
Unearned accounts receivable	14,474	23,807
Accounts receivable, gross	43,046	32,895
Allowance for doubtful accounts	(356)	(409)
Accounts receivable, net	$ 42,690	$ 32,486

Unearned accounts receivable represent products shipped to customers where Sonus has a contractual right to bill the customer and collectibility is probable under ordinary collection terms prior to satisfying Sonus' revenue recognition criteria. The allowance for doubtful accounts is based on Sonus' detailed assessment of the collectibility of specific customer accounts.

(f) Inventory

Inventory consists of the following, in thousands:

	September 30, 2005	December 31, 2004
On-hand final assemblies and finished goods inventory	$ 15,446	$ 18,725
Unearned inventory	17,483	14,054
Evaluation inventory	3,907	6,107
Inventory, gross	36,836	38,886
Excess, obsolete and evaluation reserve	(6,548)	(10,540)
Inventory, net	$ 30,288	$ 28,346

SONUS NETWORKS, INC.
Notes to Condensed Consolidated Financial Statements (Continued)
(Unaudited)

(2) Summary of Significant Accounting Policies (Continued)

Unearned inventory represents deferred cost of revenues for product shipments prior to satisfaction of Sonus' revenue recognition criteria.

Sonus values inventory at the lower of cost on a first-in, first-out basis or fair market value and provides inventory reserves based on excess and obsolete inventory determined primarily by future demand forecasts and records adjustments to such reserves through charges to cost of revenues. Sonus also records a full inventory reserve for evaluation equipment at the time of shipment to customers as a charge to sales and marketing expense as Sonus' experience with this type of inventory indicates it is probable that the value of the inventory will not be realizable. If these evaluation shipments should convert to revenue, Sonus records a benefit to sales and marketing expense and records the full cost of revenues in the period of revenue recognition.

(g) Deferred Revenue

Deferred revenue consists of the following, in thousands:

	September 30, 2005	December 31, 2004
Maintenance and support contracts	$ 65,543	$ 44,859
Customer deposits	33,343	22,399
Unearned revenue	14,474	23,807

Total deferred revenue	113,360	91,065
Less current portion	(80,968)	(65,105)
	$ 32,392	$ 25,960

Maintenance and support contracts are recognized ratably over the life of the maintenance and support period. Customer deposits represent payments received in advance of revenue recognition. Unearned revenue represents billings for which payment has not been received and revenue recognition criteria have not been met. As of September 30, 2005 and December 31, 2004, deferred revenue and accounts receivable excluded $7.7 million and $6.5 million related to products shipped and billed to customers which are collectible under extended payment terms or for which revenue is recognized as cash is collected.

(h) Revenue Recognition

Sonus recognizes revenue from product sales when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collectibility of the related receivable is probable under ordinary payment terms. When Sonus has future obligations, including a requirement to deliver additional elements which are essential to the functionality of the delivered elements or for which vendor specific objective evidence of fair value (VSOE) does not exist or customer acceptance is required, Sonus defers revenue recognition and related costs until those obligations are satisfied. The ordering patterns and sales lead times associated with customer orders may vary significantly from period to period.

Many of Sonus' sales involve complex contractual, multiple element arrangements. When a sale includes multiple elements, such as products, maintenance and/or professional services, Sonus recognizes

(2) Summary of Significant Accounting Policies (Continued)

revenue using the residual method. Revenues associated with undelivered elements that are considered not essential to the functionality of the product and for which VSOE has been established, are deferred based on the VSOE value and any remaining arrangement fee is then allocated to, and recognized as, product revenue. VSOE is determined based upon the price charged when the same element is sold separately or established by the relevant pricing authority. If Sonus cannot establish VSOE for each undelivered element, including specified upgrades, it defers revenue on the entire arrangement until VSOE for all undelivered elements is known or all elements are delivered and all other revenue recognition criteria are met.

Maintenance and support services are recognized ratably over the life of the service period, ranging from one to five years. Maintenance and support services include telephone support, return and repair support and unspecified rights to product upgrades and enhancements.

Installation service revenues which are considered to be perfunctory are generally recognized when the service is complete. Other professional services for which VSOE has been established are typically recognized based on the proportional performance method as the services are delivered.

Consulting, custom development and other professional service only engagements are recognized as services are rendered.

Sonus sells the majority of its products directly to end-users. For products sold by resellers and distributors, Sonus typically recognizes revenue on a sell-through basis utilizing information provided to Sonus from its resellers and distributors. To date, no revenues have been recognized on a sell-in basis due to the limited history of shipments to resellers and distributors.

Sonus records deferred revenue for product delivered or services performed for which collection of the amount billed is either probable or has been collected but other revenue recognition criteria have not been satisfied. Deferred revenues include customer deposits and amounts associated with maintenance contracts. Deferred revenues expected to be recognized as revenue more than one year of the balance sheet date are classified as long-term deferred revenues.

Sonus defers recognition of incremental direct costs, such as cost of goods, royalties, commissions and third-party installation costs, until satisfaction of the criteria for recognition of the related revenue.

(i) Stock-based Compensation

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

(2) Summary of Significant Accounting Policies (Continued)

The following table shows Sonus' pro forma net (loss) income and net (loss) income per share if accounted under SFAS 123 for the three and nine months ended September 30, 2005 and 2004, in thousands except per share data:

	Three months ended September 30,		Nine months ended September 30,	
	2005	2004	2005	2004
Net (loss) income, as reported	$ (2,704)	$ 10,268	$ 3,346	$ 18,216
Plus: Employee stock-based compensation expense included in net (loss) income under intrinsic value method related to options	11	65	15	530
Less: Employee stock-based compensation under fair value method	(8,458)	(12,104)	(26,696)	(35,137)
Pro forma net loss	$ (11,151)	$ (1,771)	$ (23,335)	$ (16,391)
Basic and diluted net (loss) income per share—				
As reported	$ (0.01)	$ 0.04	$ 0.01	$ 0.07
Pro forma	$ (0.04)	$ (0.01)	$ (0.09)	$ (0.07)

(j) Comprehensive Net Income (Loss)

Sonus applies SFAS No. 130, *Reporting Comprehensive Income*. The comprehensive net (loss) income for the three and nine months ended September 30, 2005 and 2004 does not significantly differ from the reported net (loss) income.

(k) Disclosures about Segments of an Enterprise

SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, established standards for reporting information regarding operating segments and established standards for related disclosures about products and services and geographic areas. Operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision maker in making decisions regarding resource allocation and assessing performance. To date, the chief operating decision maker has made such decisions and assessed performance at the company level as one segment.

(l) Net (Loss) Income Per Share

Basic net (loss) income per share is computed by dividing the net income for the period by the weighted average number of shares of unrestricted common stock outstanding during the period. Diluted net (loss) income per share is computed by dividing the net (loss) income for the period by the weighted average number of shares of unrestricted common stock and dilutive potential common shares outstanding based on the average market price of Sonus' common stock (under the treasury stock method). Dilutive potential common shares consist of restricted common stock and common stock issuable upon the exercise of stock options and conversion of a convertible subordinated note.

(2) Summary of Significant Accounting Policies (Continued)

The following table sets forth the computation of shares used in calculating the basic and diluted net (loss) income per share, in thousands:

	Three months ended September 30,		Nine months ended September 30,	
	2005	2004	2005	2004
Weighted average common shares outstanding	248,801	246,322	248,312	245,849
Less weighted average restricted common shares outstanding	—	124	—	455
Weighted average shares used in basic per share calculation	248,801	246,198	248,312	245,394
Add effect of dilutive potential common shares	—	5,509	4,909	7,382
Weighted average shares used in diluted per share calculation	248,801	251,707	253,221	252,776

Excluded from the shares used in the calculations above are options to purchase shares of common stock and shares of common stock issuable upon conversion of a convertible subordinated note representing an aggregate of 9,422,290 shares for the three months ended September 30, 2004, and 11,145,862 shares and 5,529,290 shares for the nine months ended September 30, 2005 and 2004 as their effects would have been anti-dilutive.

(m) Warranty Reserve

Sonus' products are covered by a standard warranty of 90 days for software and one year for hardware or a warranty of longer periods under certain customer contracts. In addition, certain customer contracts include warranty-type provisions for epidemic or similar product failures, generally for the contractual period or the life of the product in accordance with published telecommunications standards. Sonus accrues for warranty obligations when the occurrence of such obligation is probable and the amount of such obligation is reasonably estimable. Sonus has not incurred significant costs related to such obligations. Sonus' customers typically purchase maintenance and support contracts, which encompass its warranty obligations. Sonus' estimates of anticipated rates of warranty claims and costs are primarily based on historical information and future forecasts.

In addition, certain of Sonus' customer contracts include provisions under which Sonus may be obligated to pay penalties generally for the contractual period or for the life of the product if Sonus' products fail or do not perform in accordance with specifications. Sonus accrues for such contingent obligations when the occurrence of such obligation is probable and the amount of such obligation is reasonably estimable. Sonus has not incurred significant costs related

to such provisions. Sonus periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary. Increases in product failure rates, material usage or service delivery costs may result in increases to Sonus' warranty reserve and its gross profit could be adversely affected. As of September 30, 2005 and December 31, 2004 Sonus had $330,000 and $0 of warranty reserves recorded.

(2) Summary of Significant Accounting Policies (Continued)

(n) Recent Accounting Pronouncements

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs, an amendment of Accounting Research Bulletin (ARB) No. 43, Chapter 4.* SFAS No. 151 amends the guidance in ARB No 43, Chapter 4, "Inventory Pricing" to clarify that abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage) should be recognized as current-period charges. In addition, SFAS No. 151 requires that allocation of fixed production overhead to the costs of conversion be based on the normal capacity of the production facilities. The provisions of SFAS No. 151 are effective for fiscal years beginning after June 15, 2005. Sonus is evaluating the provisions of SFAS No. 151 and presently does not believe that its adoption will have a material impact on its financial condition, results of operations or cash flows.

In December 2004, the FASB issued SFAS 123(R), *Share-Based Payment*, which revises SFAS No. 123, *Accounting for Stock-Based Compensation*. supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees* and its related interpretations, and amends SFAS No. 95, *Statement of Cash Flows*. SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values at the date of grant. Pro forma disclosure is no longer an alternative. SFAS 123(R) is effective for fiscal years beginning after June 15, 2005. Sonus is required to adopt SFAS 123(R) on January 1, 2006. SFAS 123(R) permits public companies to adopt its requirements using one of two methods: a "modified prospective" method, in which compensation cost is recognized beginning with the effective date (a) based on the requirements of SFAS 123(R) for all share-based payments granted after the effective date, and (b) based on the requirements of SFAS 123 for all awards granted to employees prior to the effective date of SFAS 123(R) that remain unvested on the effective date; or a "modified retrospective" method, which includes the requirements of the modified prospective method described above, but also permits entities to restate based on the amounts previously recognized under SFAS 123 for purposes of pro forma disclosures either (a) all prior periods presented or (b) prior interim periods of the year of adoption. Sonus has not yet determined which method to use in adopting SFAS 123(R). Sonus is evaluating SFAS 123(R) and has not yet determined the amount of stock option expense that will be incurred in future periods as a result of the adoption of SFAS 123(R). The adoption of SFAS 123(R) will have no impact on Sonus' net cash flows or overall financial position.

(3) Restructuring Charges

Commencing in the third quarter of fiscal 2001 and extending through fiscal 2002, in response to unfavorable business conditions primarily caused by significant declines in capital spending by telecommunications service providers, Sonus implemented restructuring plans designed to reduce expenses and align its cost structure with its revised business outlook. The restructuring plans included worldwide workforce reductions, consolidation of excess facilities and the write-off of excess inventory and purchase commitments.

(3) Restructuring Charges (Continued)

2002 Restructuring Accrual

The following table summarizes the activity during the nine months ended September 30, 2005 relating to Sonus' accrual for fiscal 2002 restructuring actions, in thousands:

	December 31, 2004 accrual balance	Cash payments	September 30, 2005 accrual balance	Current portion	Long-term portion
Consolidation of facilities	$ 799	$ (138)	$ 661	$ 193	$ 468

The remaining cash expenditures relating to the consolidation of excess facilities are expected to be paid through 2008.

(4) Contingencies

In November 2001, a purchaser of Sonus' common stock filed a complaint in the United States District Court for the Southern District of New York against Sonus, two of its officers and the lead underwriters alleging violations of the federal securities laws in connection with Sonus' initial public offering (IPO) and seeking unspecified monetary damages. The purchaser seeks to represent a class of persons who purchased Sonus' common stock between the IPO on May 24, 2000 and December 6, 2000. An amended complaint was filed in April 2002. The amended complaint alleges that Sonus' registration statement contained false or misleading information or omitted to state material facts concerning the alleged receipt of undisclosed compensation by the underwriters

and the existence of undisclosed arrangements between underwriters and certain purchasers to make additional purchases in the after market. The claims against Sonus are asserted under Section 10(b) of the Securities Exchange Act of 1934 and Section 11 of the Securities Act of 1933 and against the individual defendants under Sections 11 and 15 of the Securities Act and Sections 10(b) and 20(a) of the Exchange Act. Other plaintiffs have filed substantially similar class action cases against approximately 300 other publicly traded companies and their IPO underwriters which, along with the actions against Sonus, have been transferred to a single federal judge for purposes of coordinated case management. On July 15, 2002, Sonus, together with the other issuers named as defendants in these coordinated proceedings, filed a collective motion to dismiss the consolidated amended complaints on various legal grounds common to all or most of the issuer defendants. The plaintiffs voluntarily dismissed the claims against many of the individual defendants, including those Sonus officers named in the complaint. On February 19, 2003, the court granted a portion of the motion to dismiss by dismissing the Section 10(b) claims against certain defendants including Sonus, but denied the remainder of the motion as to the defendants. In June 2003, a special committee of Sonus' Board of Directors authorized Sonus to enter into a proposed settlement with the plaintiffs on terms substantially consistent with the terms of a Memorandum of Understanding negotiated among representatives of the plaintiffs, the issuer defendants and the insurers for the issuer defendants. On February 15, 2005, the court preliminarily approved the terms of the proposed settlement contingent on modifications to the proposed settlement. On August 31, 2005, the court approved the terms of the proposed settlement, as modified. The settlement is subject to class certification and final approval by the court. A hearing has been scheduled on April 24, 2006 for final approval. The proposed settlement would

(4) Contingencies (Continued)

not require any settlement payment by Sonus, therefore Sonus does not expect that the settlement would have a material impact on its business or financial results.

Beginning in July 2002, several purchasers of Sonus' common stock filed complaints in the United States District Court for the District of Massachusetts against Sonus, certain officers and directors and a former officer under Sections 10(b) and 20(a) and Rule 10b-5 of the Securities Exchange Act of 1934 (Class Action Complaints). The purchasers seek to represent a class of persons who purchased Sonus' common stock between December 11, 2000 and January 16, 2002, and seek unspecified monetary damages. The Class Action Complaints were essentially identical and alleged that Sonus made false and misleading statements about its products and business. On March 3, 2003, the plaintiffs filed a Consolidated Amended Complaint. On April 22, 2003, Sonus filed a motion to dismiss the Consolidated Amended Complaint on various grounds. On May 11, 2004, the court held oral argument on the motion, at the conclusion of which the court denied Sonus' motion to dismiss. The plaintiffs filed a motion for class certification on July 30, 2004. . On February 16, 2005, the court certified the class and appointed a class representative. On March 9, 2005, the court appointed the law firm of Moulton & Gans as lead counsel. After the court requested additional briefing on the adequacy of the class representative, the class representative withdrew. Lead counsel then filed a motion to substitute a new plaintiff as the class representative. On May 19, 2005, the court held a hearing on the motion and took the matter under advisement. On August 15, 2005, the court issued an order decertifying the class and requiring the parties to submit a joint report informing the court whether the cases have been settled and whether defendants would be seeking to recover attorney's fees from the plaintiffs. On September 30, 2005, the plaintiffs filed motions to voluntarily dismiss their complaints with prejudice. On October 5, 2005, the court entered an order dismissing the cases. On October 21, 2005, the defendants filed a motion seeking the recovery of attorneys' fees from plaintiffs. The plaintiffs have until December 5, 2005 to respond to the motion.

Beginning in February 2004, a number of purported shareholder class action complaints were filed in the United States District Court for the District of Massachusetts against Sonus and certain of its current officers and directors. On June 28, 2004, the court consolidated the claims. On December 1, 2004, the lead plaintiff filed a consolidated amended complaint. The complaint asserts claims under the federal securities laws, specifically Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Sections 11, 12(a), and 15 of the Securities Act of 1933, relating to Sonus' restatement of its financial results for 2001, 2002, and the first three quarters of 2003. Specifically, the complaint alleges that Sonus issued a series of false or misleading statements to the market concerning Sonus' revenues, earnings and financial condition. Plaintiffs contend that such statements caused Sonus' stock price to be artificially inflated. The complaint seeks unspecified damages on behalf of a purported class of purchasers of Sonus' common stock during the period from March 28, 2002, through March 26, 2004. On January 28, 2005, Sonus filed a motion to dismiss the Section 10(b) and 12(a) claims and joined the motion to dismiss the Section 11 claim filed by the individual defendants. On June 1, 2005, the court held a hearing on the motion and allowed the plaintiff to file an amended complaint. The plaintiff filed an Amended Complaint that included the same claims and substantially similar allegations as set forth in the prior Complaint. On September 12, 2005, the defendants filed motions to dismiss this Amended Complaint. The Court has scheduled a hearing on the motions for December 10, 2005. Sonus believes that it has substantial legal and factual defenses to the claims, which it intends to pursue vigorously. There is no assurance Sonus will prevail in defending these actions. A

(4) Contingencies (Continued)

judgment or a settlement of the claims against the defendants could have a material impact of Sonus' financial results.

In February 2004, three purported shareholder derivative lawsuits were filed in the United States District Court for the District of Massachusetts against Sonus and certain of its officers and directors, naming Sonus as a nominal defendant. Also in February 2004, two purported shareholder derivative lawsuits were filed in the business litigation session of the superior court of Suffolk County of Massachusetts against Sonus and certain of its directors and officers,

also naming Sonus as a nominal defendant. The suits claim that certain of Sonus' officers and directors breached their fiduciary duties to Sonus' stockholders and to the company. The complaints are derivative in nature and do not seek relief from Sonus. However, Sonus has entered into indemnification agreements in the ordinary course of business with certain of the defendant officers and directors and may be obligated throughout the pendency of these actions to advance payment of legal fees and costs incurred by the defendants pursuant to Sonus' obligations under the indemnification agreements or applicable Delaware law. On September 27, 2004, the state court granted Sonus' motion to dismiss. On October 26, 2004, the plaintiffs filed a notice appealing the state court's dismissal of the actions. On June 24, 2005, the plaintiffs withdrew the appeal and dismissed the case with prejudice. In the federal actions, on June 28, 2004, the court consolidated and stayed the three actions. On October 12, 2004, the lead plaintiff filed a consolidated amended complaint. On June 1, 2005, the court held a hearing on the motion and allowed the plaintiff to file an amended complaint. On July 1, 2005, the plaintiff filed an amended complaint. The defendants renewed their motions to dismiss. The court has scheduled a hearing on the motions for December 10, 2005. There is no assurance Sonus will prevail in defending these actions. Sonus does not expect these shareholder derivative claims will have a material impact on its financial results.

In December 2004, a purchaser of Sonus' common stock filed a complaint in the circuit court in Will County, Illinois, against Sonus, one of its officers, and a former officer alleging misrepresentation and fraud in connection with the plaintiff's purchase of Sonus stock. The Complaint seeks unspecified damages. Sonus filed a motion to dismiss the complaint. On May 5, 2005, the plaintiff filed an amended complaint. On October 26, 2005, the court held a hearing on the motion during which he dismissed the federal claims without prejudice and dismissed the state claims without prejudice and leave to refile within 28 days. If the plaintiff does not refile within 28 days then the state claims will be dismissed with prejudice. The court scheduled a status hearing for December 1, 2005. Sonus does not expect that this claim will have a material impact on its financial results.

Sonus includes standard intellectual property indemnification provisions in its product agreements in the ordinary course of business. Pursuant to Sonus' product agreements, Sonus will indemnify, hold harmless, and reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally business partners or customers, in connection with certain patent, copyright or other intellectual property infringement claims by third parties with respect to Sonus' products. Other agreements with Sonus' customers provide indemnification for claims relating to property damage or personal injury resulting from the performance of services by Sonus or its subcontractors. Historically, Sonus' costs to defend lawsuits or settle claims relating to such indemnity agreements have been insignificant. Accordingly, the estimated fair value of these indemnification provisions is immaterial.

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

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements, which are subject to a number of risks and uncertainties. These forward-looking statements are based on our current expectations, assumptions, estimates and projections about our industry and ourselves, and we do not undertake an obligation to update our forward-looking statements to reflect future events or circumstances. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including the factors set forth in "Cautionary Statements" in the Quarterly Report on Form 10-Q. This discussion should be read in conjunction with the unaudited condensed consolidated financial statements and related notes for the periods specified. Further reference should be made to our Annual Report on Form 10-K for the year ended December 31, 2004 and our Quarterly Report on Form 10-Q for the quarter ended June 30, 2005, both on file with the SEC.

Overview

We are a leading supplier of packet voice infrastructure solutions for wireline and wireless service providers. Our products are a new generation of carrier-class switching equipment and software that enable voice services to be delivered over packet-based networks.

In 2004 and continuing into 2005, there was increased interest and activity in the market for packet-based voice infrastructure products. While it remains uncertain as to the speed and extent of the adoption of carrier packet voice infrastructure products by large carriers, we believe that over time the market opportunity for packet voice solutions is substantial. This has shown in our order activity as in the fourth quarter of fiscal 2004 we achieved record orders and in the first nine months of fiscal 2005 orders were consistent with revenue. For the three and nine months ended September 30, 2005, revenues were $45.7 million and $137.4 million, respectively, compared to $46.8 million and $125.7 million for the three and nine months ended September 30, 2004, respectively, and total deferred revenue increased to $113.4 million at September 30, 2005 from $91.1 million at December 31, 2004. This variability in our quarterly revenue and operating results is caused primarily by the uneven ordering pattern of our customers and the timing of revenue recognition, including network installations, product delays and customer acceptance.

We sell our products primarily through a direct sales force and, in some markets, through or with the assistance of resellers and distributors. Customers' decisions to purchase our products to deploy in commercial networks involve a significant commitment of resources and a lengthy evaluation, testing and product qualification process. Our revenues and results of operations may vary significantly and unexpectedly from quarter to quarter as a result of long sales cycles, our expectation that customers will periodically place large orders with short lead times and the application of complex revenue recognition rules to certain transactions, which may result in customer shipments and orders from multiple quarters being recognized as revenue in one quarter. We expect to recognize revenues from a limited number of customers for the foreseeable future.

From our inception through December 31, 2003, we incurred significant losses. As of September 30, 2005, we had an accumulated deficit of $780.7 million. Although we achieved profitability in the second quarter of 2005 and in each quarter and on an annual basis in fiscal year 2004, we incurred a net loss for the first and third quarters of 2005 and may incur additional losses in future quarters and years. We have a lengthy sales cycle for our products and, accordingly, we expect to incur sales and other expenses before we realize the related revenues. We expect to continue to incur significant sales and marketing, research and development and general and administrative expenses, many of which are fixed prior to the beginning of any particular fiscal period and, as a result, we will need to generate significant revenues to maintain profitability.

Critical Accounting Policies and Estimates

Management's discussion and analysis of the financial condition and results of operations is based upon the consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We base our estimates and judgments on historical experience, knowledge of current conditions and beliefs of what could

occur in the future given available information. We consider the following accounting policies to be both those most important to the portrayal of our financial condition and those that require the most subjective judgment. If actual results differ significantly from management's estimates and projections, there could be a material effect on our financial statements. The significant accounting policies that we believe are the most critical to aid in fully understanding and evaluating our reported financial results include the following:

- Revenue recognition
- Deferred revenue
- Allowance for doubtful accounts
- Inventory reserves
- Warranty, litigation, and other loss contingency reserves
- Stock-based compensation, and
- Accounting for income taxes

A full discussion of these accounting policies is included in our 2004 Annual Report on Form 10-K filed with the Securities and Exchange Commission and we refer the reader to that discussion. The following information regarding critical accounting policies has been updated since our 10-K:

Revenue Recognition. We recognize revenue from product sales when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collectibility of the related receivable is probable under ordinary payment terms. When we have future obligations, including a requirement to deliver additional elements which are essential to the functionality of the delivered elements or for which vendor specific objective evidence of fair value (VSOE) does not exist or customer acceptance is required, we defer revenue recognition and related costs until those obligations are satisfied. The ordering patterns and sales lead times associated with customer orders may vary significantly from period to period.

Many of our sales involve complex contractual, multiple element arrangements. When a sale includes multiple elements, such as products, maintenance and/or professional services, we recognize revenue using the residual method. Revenues associated with undelivered elements that are considered not essential to the functionality of the product and for which VSOE has been established, are deferred based on the VSOE value and any remaining arrangement fee is then allocated to, and recognized as, product revenue. VSOE is determined based upon the price charged when the same element is sold separately or established by the relevant pricing authority. If we cannot establish VSOE for each undelivered element, including specified upgrades, we defer revenue on the entire arrangement until VSOE for all undelivered elements is known or all elements are delivered and all other revenue recognition criteria are met.

Maintenance and support services are recognized ratably over the life of the service period, ranging from one to five years. Maintenance and support services include telephone support, return and repair support and unspecified rights to product upgrades and enhancements.

Installation service revenues which are considered to be perfunctory are generally recognized when the service is complete. Other professional services for which VSOE has been established are typically recognized based on the proportional performance as the services are delivered.

Consulting, custom development and other professional services only engagements are recognized as services are rendered.

We sell the majority of our products directly to end-users. For products sold through resellers and distributors, we typically recognize revenue on a sell-through basis utilizing information provided to us from our resellers and distributors. To date, no revenues have been recognized on a sell-in basis due to the limited history of shipments to resellers and distributors.

We record deferred revenue for product delivered or services performed for which collection of the amount billed is either probable or has been collected but other revenue recognition criteria have not been satisfied. Deferred revenues include customer deposits and amounts associated with maintenance contracts. Deferred revenues expected to be recognized as revenue more than one year of the balance sheet date are classified as long-term deferred revenues.

We defer recognition of incremental direct costs, such as cost of goods, royalties, commissions and third-party installation costs, until satisfaction of the criteria for recognition of the related revenue.

Loss Contingencies and Reserves. We are subject to ongoing business risks arising in the ordinary course of business that affect the estimation process of the carrying value of assets, the recording of liabilities and the possibility of various loss contingencies. Under SFAS No. 5, *Accounting for Contingencies*, an estimated loss contingency is accrued when it is probable that a liability has been incurred or an asset has been impaired and the amount of loss can be reasonably estimated. We regularly evaluate current information available to determine whether such amounts should be adjusted and record changes in estimates in the period they become known.

Allowance for Doubtful Accounts. We establish billing terms at the time we negotiate purchase agreements with our customers. We continually monitor for timely payments and potential collection issues. Allowance for doubtful accounts is estimated based on our detailed assessment of the collectibility of specific customer accounts. While we believe that our allowance for doubtful accounts is adequate and that the judgment applied is appropriate, if there is a deterioration of a customer's creditworthiness or actual defaults are higher than our historical experience, the actual results could differ from these estimates. While such credit losses have historically been within our expectations and the allowances we established, we can provide no assurance that we will continue to experience the same credit loss rates that we have in the past. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payment, additional allowances may be required. We defer revenue recognition for customers for which we believe collection is less than probable. Our failure to accurately estimate the losses for doubtful accounts or receive payments on a timely basis could have a material adverse effect on our business, financial condition and results of operations.

Inventory Reserves. Inventory purchases and commitments are based upon estimated future demand for our products. We value inventory at the lower of cost on a first-in, first-out basis or net realizable value. We provide inventory reserves based on excess and obsolete inventory determined primarily by future demand forecasts and returns of defective product, and record charges to cost of revenues. We assess such demand forecasts and return history on at least a quarterly basis. If we record a charge to reduce inventory to its estimated net realizable value, we do not increase its carrying value due to subsequent changes in demand forecasts or product repairs. Accordingly, if inventory previously reserved for is subsequently sold, we may realize improved gross profit margins on those transactions in the period the related revenue is recognized.

We also record a full inventory reserve for evaluation equipment at the time of shipment to our customers as a charge to sales and marketing expense as it is probable that the inventory value will not be realizable. If these evaluation shipments are later purchased by our customers, we reclassify amounts previously charged to sales and marketing expenses to cost of revenues in the period all revenue recognition criteria are met.

We have experienced significant changes in our product demand and, as a result, our required inventory reserves have fluctuated in recent periods. It is possible that significant changes in required inventory reserves may continue to occur in the future if there is a sudden and significant change in the demand for our products, changes in the amount of customer evaluation inventory or higher risks of inventory obsolescence because of rapidly changing technology.

Warranty Reserve. Our products are covered by a standard warranty of 90 days for software and one year for hardware or a warranty for longer periods under certain customer contracts. In addition, certain customer contracts include warranty-type provisions for epidemic or similar product failures, generally for the contractual period or the life of the product in accordance with published telecommunications standards**.** We accrue for warranty obligations when the occurrence of such obligation is probable and the amount of such obligation is reasonably estimable. We have not incurred significant costs related to such obligations. Our customers typically purchase maintenance and support contracts, which encompass our warranty obligations. Our estimates of anticipated rates of warranty claims and costs are primarily based on historical information and future forecasts.

In addition, certain of our customer contracts include provisions under which we may be obligated to pay penalties generally for the contractual period or for the life of the product if our products fail or do not perform in accordance with specifications. We accrue for such contingent obligations when the occurrence of such obligation is probable and the amount of such obligation is reasonably estimable. We have not incurred significant costs related to such provisions. We periodically assess the adequacy of our recorded warranty liabilities and adjust the amounts as necessary. Increases in product failure rates, material usage or service delivery costs may result in increases to our warranty reserve and our gross profit could be adversely affected. As of September 30, 2005 and December 31, 2004 we had $330,000 and $0 of warranty reserves recorded.

Royalty Accrual. We accrue for royalties for technology we license from vendors based on established royalty rates and usage. In certain cases, we have been contacted by third parties who claim that our products infringe on certain intellectual property of the third party. We evaluate these claims and accrue for royalties when the amounts are probable and reasonably estimable. While we believe that the amounts accrued for estimated royalties are adequate, the amounts required to ultimately settle royalty obligations may be different.

Reserve for Litigation and Legal Fees. We are subject to various legal claims, including securities litigation. We reserve for legal contingencies and legal fees when the amounts are probable and reasonably estimable. Our director and officer liability insurance policies provide only limited liability protection relating to the securities class action and derivative lawsuits against us and certain of our officers and directors. We intend to defend these matters vigorously, although the ultimate outcome of these items is uncertain and the potential loss, if any, may be significantly different than the amounts we have previously accrued.

Accounting for Income Taxes. As a result of net operating losses incurred in prior years in most jurisdictions in which we operate, a net operating loss in the first and third fiscal quarters of 2005, and uncertainty as to the extent, jurisdiction and timing of profitability in future periods, we have continued to record a full valuation allowance against net deferred tax assets, which was approximately $94 million as of September 30, 2005. The establishment and amount of the valuation allowance requires significant estimates and judgment and can materially affect our results of operations. If the realization of deferred

tax assets in the future is considered more likely than not, an adjustment to the valuation reserve for the deferred tax asset would be made. A portion of the release of the valuation allowance will increase net income in the period such determination was made. In addition, approximately $26 million of the valuation allowance relates to tax benefits from stock option compensation. A substantial portion of the tax benefit of that item, when realized, will result in an increase in additional paid-in capital. Our effective tax rate may vary from period to period based on changes in estimated taxable income or loss in each jurisdiction, changes to the valuation allowance, statutory minimum tax rates or changes to federal, state or foreign tax laws, future expansion into areas with varying country, state, and local income tax rates including statutory minimum tax rates, deductibility of certain costs and expenses by jurisdiction and as a result of acquisitions.

Stock-based Compensation. In October 1995, the FASB issued SFAS No. 123, *Accounting for Stock-Based Compensation*. SFAS No. 123 provides that companies may account for stock-based compensation under either the fair value-based method of accounting under SFAS No. 123 or the intrinsic value-based method provided by APB No. 25, *Accounting for Stock Issued to Employees*. We use the intrinsic value based method of APB No. 25 to account for all of our employee stock-based compensation plans and use the fair value method of SFAS No. 123 to account for all non-employee stock-based compensation. We follow FIN 28, and amortize the intrinsic value as measured under APB No. 25 on an accelerated basis. SFAS No. 123, as amended by SFAS No. 148, *Accounting for Stock-Based Compensation—Transition and Disclosure—an amendment of FASB Statement No. 123*, requires companies following APB No. 25 to make pro forma disclosure in the notes to the consolidated financial statements using the measurement provisions of SFAS No. 123.

Beginning on January 1, 2006, we will adopt SFAS 123(R), *Share-Based Payment*, which is a revision of SFAS No. 123 and supersedes APB Opinion No. 25. SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values at the date of grant in fiscal years beginning after June 15, 2005, and eliminates pro forma disclosure in the notes to the financial statements.

Restructuring and Other Related Charges. We established exit plans for each of the restructuring activities which took place in 2001 and 2002 and accounted for these plans in accordance with Emerging Issues Task Force (EITF) Issue No. 94-3, *Liability Recognition for Certain Employee Benefits and Other Costs to Exit an Activity (including Certain Costs incurred in a Restructuring)*. These exit plans required that we make estimates as to the nature, timing and amount of the exit costs that we specifically identified. The consolidation of facilities required us to make estimates, which included contractual rental commitments or lease buy-outs for office space being vacated and related costs and leasehold improvement write-downs, offset by estimated sub-lease income. We have remaining accrued exit costs of $661,000 as of September 30, 2005, which relate to remaining lease payments. SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*, was effective for exit or disposal activities that are initiated after December 31, 2002. SFAS No. 146 requires that a liability for a cost that is associated with an exit or disposal activity be recognized when the liability is incurred. A liability is recognized when the severance amounts relate to prior services rendered, the payment of the amount is probable and the amount can be reasonably estimated.

Three and Nine Months Ended September 30, 2005 and 2004

Revenues. Revenues for the three and nine months ended September 30, 2005 and 2004 were as follows, in thousands:

	Three months ended September 30,		Nine months ended September 30,	
	2005	2004	2005	2004
Revenues:				
Product	$ 29,107	$ 36,064	$ 92,904	$ 92,896
Service	16,550	10,698	44,456	32,759
Total revenues	$ 45,657	$ 46,762	$ 137,360	$ 125,655

Product revenues comprise sales of our voice infrastructure products, including our GSX9000™ Open Services Switch, PSX, SGX, ASX, Sonus Insight™ Management System and related product offerings. Product revenues for the three months ended September 30, 2005 decreased 19% from the comparable period in fiscal 2004. Product revenues for the nine months ended September 30, 2005 were consistent with the comparable period in fiscal 2004. The decrease for the three months ended September 30, 2005 is primarily due to the renegotiation of bundled maintenance and support arrangements with two customers resulting in a deferral of product revenue of $4.7 million for the three months ended September 30, 2005. The maintenance and support renegotiation also resulted in a decrease in gross margin in the amount of $4.7 million and earnings per share of $0.02. The $4.7 million of deferred revenue will be recognized as service revenue over subsequent quarters as services are delivered. The consistency for the nine months ended September 30, 2005 is primarily due to the timing of revenue recognition, which in part is dependent upon completion of certain customer deployments and obligations as of the end of a fiscal quarter and the impact of an increase in orders in the fourth quarter of 2004 and first quarter of 2005, offset by the $4.7 reduction of revenue noted above.

Service revenues primarily comprise hardware and software maintenance, network design, installation and other professional services. Service revenues for the three and nine months ended September 30, 2005 increased 55% and 36%, respectively, from the comparable periods in fiscal 2004. These increases were primarily a result of higher maintenance revenues due to our growing installed product base and an increase in installation revenue. For the nine months ended September 30, 2005, service revenues were partially offset by lower resident engineering revenue.

Cingular Wireless, Global Crossing, Qwest Communications, Softbank Broadband and Verizon Global Networks each contributed 10% or more of our revenues during one or more of the periods for the three and nine months ended September 30, 2005 and 2004.

International revenues, primarily attributable to Japan and Europe, were 21% and 6% of total revenues for the three months ended September 30, 2005 and 2004, respectively, and were 20% and 15% of total revenues for the nine months ended September 30, 2005 and 2004, respectively.

Our deferred product revenue was $47.8 million and $46.2 million as of September 30, 2005 and December 31, 2004, respectively. Our deferred service revenue was $65.6 million and $44.9 million as of September 30, 2005 and December 31, 2004, respectively. Our deferred revenue balance may fluctuate as a result of the timing of revenue recognition, customer payments, maintenance contract renewals, contractual billing rights, customer creditworthiness and maintenance revenue deferrals included in multiple element arrangements. As of September 30, 2005 and December 31, 2004, deferred revenue and accounts receivable excluded $7.7 million and $6.5 million, respectively, related to products shipped and billed to customers which are collectible under extended payment terms or for which revenue is recognized as cash is collected.

Cost of Revenues/Gross Profit. Our cost of revenues consists primarily of amounts paid to third-party manufacturers for purchased materials and services, royalties, manufacturing and professional services personnel and related costs, and inventory obsolescence. Cost of revenues and gross profit as a percentage of revenues for the three and nine months ended September 30, 2005 and 2004 were as follows (in thousands, except percentages):

	Three months ended September 30,		Nine months ended September 30,	
	2005	2004	2005	2004
Cost of revenues:				
Product	$ 17,410	$ 6,296	$ 39,657	$ 24,151
Service	6,073	4,173	16,993	12,659
Total cost of revenues	$ 23,483	$ 10,469	$ 56,650	$ 36,810
Gross profit margin (% of respective revenues):				
Product	40%	83%	57%	74%
Service	63	61	62	61
Total gross profit margin	49%	78%	59%	71%

The decreases in product gross profit as a percentage of product revenues for the three and nine months ended September 30, 2005 were primarily due to customer and product mix and a renegotiation of maintenance and support arrangements with two customers resulting in a reduction in product revenue and gross margin of $4.7 million in the third quarter of 2005. We expect that over time our product gross margins will be consistent with our long-term financial model of 58-62%. The increase in service gross profit as a percentage of service revenues was primarily due to an increase in our service revenues, partially offset by increased investment in our service organization to support the expansion of our installed base. Our service cost of revenues is predominantly fixed in nature and, therefore, changes in service revenue will have a significant impact on service gross profit percentage.

Research and Development Expenses. Research and development expenses consist primarily of salaries and related personnel costs and prototype costs related to the design, development, testing and enhancement of our products. Research and development expenses were $11.8 million for the three months ended September 30, 2005, an increase of $2.8 million, or 31%, from $9.0 million for the same period in fiscal 2004. Research and development expenses were $33.9 million for the nine months ended September 30, 2005, an increase of $7.1 million, or 26%, from $26.8 million for the same period in fiscal 2004. These increases primarily reflect an increase in salary and related expenses associated with increased headcount and additional depreciation expenses associated with new capital expenditures. Some aspects of our research and development efforts require significant short-term expenditures, the timing of which can cause significant variability in our expenses. We believe that rapid technological innovation is critical to our long-term success and we intend to continue to make substantial investments to enhance our products and technologies to meet the requirements of our customers and market. We believe that our research and development expenses for the fourth quarter of fiscal 2005 will increase from the third quarter of fiscal 2005 primarily as a result of increases in salary and related expenses associated with increased headcount, and depreciation expenses associated with new capital expenditures. The

additional investments are directed primarily toward the growth of our access, wireless and international businesses as well as the expansion of our research and development operations in India.

Sales and Marketing Expenses. Sales and marketing expenses consist primarily of salaries and related personnel costs, commissions, travel and entertainment expenses, promotions, customer evaluations and other marketing and sales support expenses. Sales and marketing expenses were $10.8 million for the three months ended September 30, 2005, an increase of $295,000, or 3%, from $10.5 million for the same period in fiscal 2004. Sales and marketing expenses were $31.4 million for the nine months ended September 30, 2005, an increase of $5.4 million, or 20%, from $26.0 million for the same period in fiscal 2004. The

increases for the three and nine months ended September 30, 2005 primarily reflect an increase in salaries and travel expenses associated with increased headcount related to the expansion of our access, wireless and international sales opportunities, partially offset by a decrease in evaluation equipment expenses. We believe that our sales and marketing expenses for the fourth quarter of fiscal 2005 will increase from the third quarter of fiscal 2005 related to commission and evaluation equipment expenses. The magnitude of the increase will be dependent upon our level of revenues in the fourth quarter as commission expenses fluctuate primarily based on revenue levels.

General and Administrative Expenses. General and administrative expenses consist primarily of salaries and related personnel costs for executive and administrative personnel, recruiting expenses, professional fees and directors and officers insurance. General and administrative expenses were $5.5 million for the three months ended September 30, 2005, a decrease of $1.2 million, or 18%, from $6.6 million for the same period in fiscal 2004. General and administrative expenses were $18.7 million for the nine months ended September 30, 2005, an increase of $1.5 million, or 9%, from $17.2 million for the same period in fiscal 2004. The decrease for the three months ended September 30, 2005 primarily reflects a decrease in directors and officers insurance costs and a reduction in bonus expenses, partially offset by an increase in salary and related expenses associated with increased headcount. The increase for the nine months ended September 30, 2005 primarily reflects an increase in professional fees incurred to perform the assessment and audit of our internal control over financial reporting required under Section 404 of the Sarbanes-Oxley Act of 2002 for 2005 and to remedy identified material weaknesses in our internal control environment and an increase in salary and related expenses associated with increased headcount, partially offset by a decrease in directors and officers insurance costs. We believe that our general and administrative expenses for the fourth quarter of fiscal 2005 will increase from the third quarter due to continued costs associated with improvements we are making in our internal control environment to address material weaknesses.

Stock-based Compensation Expenses. Stock-based compensation expenses include the amortization of stock compensation charges resulting from the granting of stock options, including the telecom technologies, inc. (TTI) stock options assumed by us, stock awards to TTI employees under the 2000 Retention Plan, sales of restricted common stock and granting of stock options to non-employees. Stock-based compensation expenses were $11,000 and $15,000 for the three and nine months ended September 30, 2005, respectively, compared to $91,000 and $606,000 for the three and nine months ended September 30, 2004, respectively. The decreases are due to deferred stock-based compensation being fully amortized as of December 31, 2004, partially offset by expense for a grant to a non-employee in the second quarter of 2005.

Amortization of Purchased Intangible Assets. In fiscal 2001, we acquired certain intellectual property, in-process research and development and intangible assets in connection with our acquisitions of TTI and Linguateq, Inc. As of December 31, 2004, the purchased intangible assets were fully amortized, therefore there was no amortization expense for the three and nine months ended September 30, 2005. Amortization of purchased intangible assets was $601,000 and $1.8 million for the three and nine months ended September 30, 2004, respectively.

Interest Income, net. Interest income consists of interest earned on our cash equivalents, marketable debt securities and long-term investments. Interest expense consists of interest incurred on a convertible subordinated note and capital lease arrangements. Interest income, net of interest expense, was $2.6 million for the three months ended September 30, 2005, an increase of $1.6 million from $1.0 million for the same period in fiscal 2004. Interest income, net of interest expense, was $6.4 million for the nine months ended September 30, 2005, an increase of $4.0 million from $2.4 million for the same period in fiscal 2004. These increases primarily reflect the benefit of an increase in the yield on our portfolio due to an increasing interest rate environment.

Income Taxes. (Benefit) provision for income taxes was $(640,000) and $214,000 for the three months ended September 30, 2005 and 2004, respectively, and $(233,000) and $598,000 for the nine months ended September 30, 2005 and 2004, respectively. The income tax (benefit) provision in all periods is primarily attributable to foreign income taxes and state income taxes in the U.S. During the three months ended September 30, 2005, we received a refund of approximately $450,000 related to foreign income taxes paid in prior years that was recorded as a reduction to expense.

Liquidity and Capital Resources

At September 30, 2005, our principal sources of liquidity were our cash, cash equivalents, marketable debt securities and long-term investments that totaled $324.9 million.

Our cash generated from operating activities was $17.3 million for the nine months ended September 30, 2005 as compared to net cash used in operating activities of $2.3 million for the same period in fiscal 2004. This increase was primarily due to an increase in deferred revenue and decreases in inventory and other current assets, partially offset by lower net income for the nine months ended September 30, 2005 as compared to the prior year and a decrease in accounts payable.

Net cash used in investing activities was $10.7 million for the nine months ended September 30, 2005, as compared to $17.3 million for the same period in fiscal 2004. Net cash used in investing activities for the nine months ended September 30, 2005 primarily reflects capital expenditures of $11.3 million. Net cash used in investing activities for the nine months ended September 30, 2004 primarily reflects net purchases of marketable debt securities and long-term investments of $11.4 million and capital expenditures of $6.3 million. We expect to incur approximately $3-4 million in additional capital expenditures in the remainder of 2005.

Net cash provided by financing activities was $6.3 million for the nine months ended September 30, 2005, as compared to $2.7 million for the same period in fiscal 2004. The net cash provided by financing activities for both periods resulted primarily from the sale of common stock in connection with our employee stock purchase plan and proceeds from the exercise of stock options.

Based on our current expectations, we believe our current cash, cash equivalents, marketable debt securities and long-term investments will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for at least 12 months. Although it is difficult to predict future liquidity requirements with certainty, the rate at which we will consume cash will be dependent on the cash needs of future operations, including changes in working capital, which will, in turn, be directly affected by the levels of demand for our products, the timing and rate of expansion of our business, the resources we devote to developing our products and any litigation settlements. We anticipate devoting substantial capital resources to continue our research and development efforts, to maintain our sales, support and marketing operations, to improve our controls environment and for other general corporate activities, as well as to vigorously defend against existing and potential litigation.

Recent Accounting Pronouncements

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs, an Amendment of Accounting Research Bulletin (ARB) No. 43, Chapter 4.* SFAS No. 151 amends the guidance in ARB No. 43, Chapter 4, "Inventory Pricing" to clarify that abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage) should be recognized as current-period charges. In addition, SFAS No. 151 requires that allocation of fixed production overhead to the costs of conversion be based on the normal capacity of the production facilities. The provisions of SFAS No. 151 are effective for fiscal years beginning after June 15, 2005. We are evaluating the provisions of SFAS No. 151 and presently do not believe that its adoption will have a material impact on our financial condition, results of operations or cash flows.

In December 2004, the FASB issued SFAS 123(R), *Share-Based Payment*, which revises SFAS No. 123, *Accounting for Stock-Based Compensation*. supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees* and its related interpretations, and amends SFAS No. 95, *Statement of Cash Flows*. SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values at the date of grant. Pro forma disclosure is no longer an alternative. SFAS 123(R) is effective for fiscal years beginning after June 15, 2005. Sonus is required to adopt SFAS 123(R) on January 1, 2006. SFAS 123(R) permits public companies to adopt its requirements using one of two methods: a "modified prospective" method, in which compensation cost is recognized beginning with the effective date (a) based on the requirements of SFAS 123(R) for all share-based payments granted after the effective date, and (b) based on the requirements of SFAS 123 for all awards granted to employees prior to the effective date of SFAS 123(R) that remain unvested on the effective date; or a "modified retrospective" method, which includes the requirements of the modified prospective method described above, but also permits entities to restate based on the amounts previously recognized under SFAS 123 for purposes of pro forma disclosures either (a) all prior periods presented or (b) prior interim periods of the year of adoption. Sonus has not yet determined which method to use in adopting SFAS 123(R). Sonus is evaluating SFAS 123(R) and has not yet determined the amount of stock option expense that will be incurred in future periods as a result of the adoption of SFAS 123(R). The adoption of SFAS 123(R) will have no impact on Sonus' net cash flows or overall financial position.

Cautionary Statements

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Securities Litigation Reform Act of 1995 that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of a number of factors, including those set forth in the following cautionary statements and elsewhere in this Quarterly Report on Form 10-Q. If any of the following risks were to occur, our business, financial condition or results of operations would likely suffer and the trading price of our common stock would likely decline. Investing in our common stock involves a high degree of risk. You should carefully consider the risks described below before buying our common stock.

We have identified material weaknesses in our disclosure controls and procedures and our internal control over financial reporting, which, if not remedied effectively, could have an adverse effect on the trading price of our common stock and otherwise seriously harm our business.

Management has concluded that our disclosure controls and procedures and our internal control over financial reporting had material weaknesses as of December 31, 2004. Although we have taken certain actions during 2005 to address those material weaknesses, our inability to remedy such material weaknesses promptly and effectively could have a material adverse effect on our business, results of operations and financial condition, as well as impair our ability to meet our quarterly and annual reporting requirements in a timely manner. These effects could in turn adversely affect the trading price of our common stock. Prior to the remediation of these material weaknesses, there remains risk that the transitional controls on which we currently rely will fail to be sufficiently effective, which could result in a material misstatement of our financial position or results of operations. In addition, even if we are successful in strengthening our controls and procedures, such controls and procedures may not be adequate to prevent or identify irregularities or fraud or facilitate the fair presentation of our financial statements, SEC reporting or other disclosures.

Failure or circumvention of our controls and procedures could seriously harm our business.

We are making significant changes in our internal control over financial reporting and our disclosure controls and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, and not absolute, assurances that the objectives of the system are met. The failure or circumvention of our controls, policies and procedures could have a material adverse effect on our business, results of operations and financial position.

We face risks related to securities litigation that could have a material adverse effect on our business, financial position and results of operations.

We have been named as a defendant in a number of securities class action and derivative lawsuits. We are generally obliged, to the extent permitted by law, to indemnify our current and former directors and officers who are named as defendants in some of these lawsuits. Defending against existing and potential litigation may require significant attention and resources of management. Regardless of the outcome, such litigation will result in significant legal expenses. If our defenses are ultimately unsuccessful, or if we are unable to achieve a favorable settlement, we could be liable for large damage awards that could have a material adverse effect on our business, results of operations and financial position.

The limitations of our director and officer liability insurance may materially harm our business and financial condition.

Our director and officer liability insurance policies provide only limited liability protection relating to the securities class action and derivative lawsuits against us and certain of our officers and directors. If these policies do not adequately cover expenses and certain liabilities relating to these lawsuits, our results of operations and our financial position could be materially harmed. The facts underlying the lawsuits have made director and officer liability insurance extremely expensive for us, and may make such insurance coverage unavailable for us in the future. Increased premiums could materially harm our financial results in future periods. The inability to obtain this coverage due to its unavailability or prohibitively expensive premiums would make it more difficult to retain and attract officers and directors and expose us to potentially self-funding any potential future liabilities ordinarily mitigated by director and officer liability insurance.

If we are not current in our SEC filings, we will face several adverse consequences.

If we are unable to remain current in our SEC filings, we will not be able to file a registration statement under the Securities Act of 1933, covering a public offering of securities, declared effective by the SEC, and we will not be able to make offerings pursuant to existing registration statements (including registration statements on Form S-8 covering employee stock plans), or pursuant to certain "private placement" rules of the SEC under Regulation D to any purchasers not qualifying as "accredited investors." In addition, our affiliates will not be able to sell our securities pursuant to Rule 144 under the Securities Act. Finally, we will not be eligible to use a "short form" registration statement on Form S-3 for a period of 12 months after the time we become current in our filings. These restrictions may impair our ability to raise capital in the public markets should we desire to do so, and to attract and retain key employees.

If we fail to keep current in our SEC filings, our common stock may be delisted from the NASDAQ National Market and subsequently would trade on the Pink Sheets. The trading of our common stock on the Pink Sheets may reduce the price of our common stock and the levels of liquidity available to our stockholders. Our delisting from the NASDAQ National Market and transfer to the Pink Sheets may also result in other negative implications, including the potential loss of confidence by suppliers, customers and employees, the loss of institutional investor interest and fewer business development opportunities.

Our business has been adversely affected by developments in the telecommunications industry and these developments may continue to affect our revenues and operating results.

From our inception through the year 2000, the telecommunications market experienced rapid growth spurred by a number of factors, including deregulation in the industry, entry of a large number of new emerging service providers, growth in data traffic and the availability of significant capital from the financial markets. Commencing in 2001 and continuing into 2005, the telecommunications industry experienced a reversal of some of these trends, marked by dramatic reductions in capital expenditures, financial difficulties, and, in some cases, bankruptcies experienced by service providers. These conditions caused a substantial, unexpected reduction in demand for telecommunications equipment, including our products.

We expect the developments described above to continue to affect our business in the following manner:

- our ability to accurately forecast revenue and plan our business is diminished;
- our revenues could be unexpectedly reduced; and
- we may incur losses because a high percentage of our operating expenses are expected to continue to be fixed in the short-term.

Any one or a combination of the above could materially and adversely affect our business, operating results and financial position.

Consolidation in the telecommunications industry could harm our business.

The industry has experienced consolidation and we expect this trend to continue. Consolidation among our customers may cause delays or reductions in capital expenditure plans and/or increased competitive pricing pressures as the number of available customers declines and their relative purchasing power increases in relation to suppliers. Any of these factors could adversely affect our business.

We expect that a majority of our revenues will be generated from a limited number of customers and we will not be successful if we do not grow our customer base.

To date, we have shipped our products to a limited number of customers. We expect that in the foreseeable future, the majority of our revenues will continue to depend on sales of our products to a limited number of customers. One customer contributed more than 10% of our revenues for the first nine months of fiscal 2005, which represented an aggregate of 29% of total revenues. Two and four customers each contributed more than 10% of our revenues for fiscal 2004 and 2003, respectively, which represented an aggregate of 29% and 57% of total revenues, respectively. Our future success will depend on our ability to attract additional customers beyond our current limited number. The growth of our customer base could be adversely affected by:

- acquisition of or by our customers;
- customer unwillingness to implement our new voice infrastructure products or renew contracts as they expire;
- potential customer concerns with selecting an emerging telecommunications equipment vendor;
- delays or difficulties that we may incur in completing the development and introduction of our planned products or product enhancements;
- further deterioration in the general financial condition of service providers, including additional bankruptcies, or inability to raise capital;

- new product introductions by our competitors;
- failure of our products to perform as expected; or
- difficulties we may incur in meeting customers' delivery requirements.

The loss of any of our significant customers or any substantial reduction in orders or contractual commitments from these customers could materially adversely affect our financial position and results of operations. If we do not expand our customer base to include additional customers that deploy our

products in operational commercial networks, our business, operating results and financial position could be materially and adversely affected.

The market for voice infrastructure products for the new public network is new and evolving and our business will suffer if it does not develop as we expect.

The market for our products continues to evolve. In particular, wireless, cable and broadband access networks are emerging to become important markets for our products. Packet-based technology may not become widely accepted as a platform for voice and a viable market for our products may not be sustainable. If this market does not develop, or develops more slowly than we expect, we may not be able to sell our products in significant volume.

If we do not anticipate and meet specific customer requirements or if our products do not interoperate with our customers' existing networks, we may not retain current customers or attract new customers.

To achieve market acceptance for our products, we must effectively anticipate, and adapt in a timely manner to, customer requirements and offer products and services that meet changing customer demands. Prospective customers may require product features and capabilities that our current products do not have. The introduction of new or enhanced products also requires that we carefully manage the transition from older products in order to minimize disruption in customer ordering patterns and ensure that adequate supplies of new products can be delivered to meet anticipated customer demand. If we fail to develop products and offer services that satisfy customer requirements, or to effectively manage the transition from older products, our ability to create or increase demand for our products would be seriously harmed and we may lose current and prospective customers.

Many of our customers will require that our products be designed to interface with their existing networks, each of which may have different specifications. Issues caused by an unanticipated lack of interoperability may result in significant warranty, support and repair costs, divert the attention of our engineering personnel from our hardware and software development efforts and cause significant customer relations problems. If our products do not interoperate with those of our customers' networks, installations could be delayed or orders for our products could be cancelled, which would seriously harm our gross margins and result in loss of revenues or customers.

Our large customers have substantial negotiating leverage, which may require that we agree to terms and conditions that may have an adverse effect on our business.

Large telecommunications providers have substantial purchasing power and leverage negotiating contractual arrangements with us. These customers may require us to develop additional features and require penalties for failure to deliver such features. As we seek to sell more products to this class of customer, we may be required to agree to such terms and conditions, which may affect the timing of revenue recognition and amount of deferred revenues and may impact our financial position in the period affected.

We rely on distribution partners to sell our products in certain markets, and disruptions to or our failure to effectively develop and manage our distribution channel and the processes and procedures that support it could adversely affect our ability to generate revenues from the sale of our products in those markets.

Our future success is highly dependent upon establishing and maintaining successful relationships with a variety of value-added reseller and distribution partners. A portion of our revenues is derived through distributors, many of which sell competitive products. Our revenues depend in part on the performance of these distributors. The loss of or reduction in sales by these distributors could materially reduce our revenues. If we fail to maintain relationships with these distribution partners, fail to develop new relationships with distributors in new markets, fail to manage, train, or provide incentives to existing distributors effectively or if these partners are not successful in their sales efforts, sales of our products may decrease and our operating results could suffer.

In addition, we recognize a portion of our revenue based on a sell-through model using information provided by our distributors. If those distributors provide us with inaccurate or untimely information, the amount or timing of our revenues could be adversely impacted.

We may face risks associated with our international expansion that could impair our ability to grow our revenues abroad.

International revenues, primarily attributable to Japan and Europe, were approximately $26.8 million for the first nine months of fiscal 2005, and $28.8 million for fiscal 2004 and we intend to expand our sales in international markets. This expansion will require significant management attention and financial resources to successfully develop direct and indirect international sales and support channels. In addition, we may not be able to develop international market demand for our products, which could impair our ability to grow our revenues. We have limited experience marketing, distributing and supporting our products internationally and, to do so, we expect that we will need to develop versions of our products that comply with local standards. Furthermore, international operations are subject to other inherent risks, including:

- reliance on distributors and resellers;
- greater difficulty collecting accounts receivable and longer collection cycle;
- difficulties and costs of staffing and managing international operations;
- the impact of differing technical standards outside the United States;
- the impact of recessions in economies outside the United States;
- changes in regulatory requirements and currency exchange rates;
- certification requirements;
- reduced protection for intellectual property rights in some countries;
- potentially adverse tax consequences; and
- political and economic instability.

We may not return to or sustain profitability.

We have incurred significant losses since inception and, as of September 30, 2005, had an accumulated deficit of $780.7 million. Although we achieved profitability in the second quarter of fiscal 2005 and in each quarter and on an annual basis in fiscal year 2004, we incurred a net loss in the first and third

quarters of fiscal 2005 and may incur additional losses in future quarters and years. Our revenues may not grow and we may never generate sufficient revenues to return to or sustain profitability.

The unpredictability of our quarterly results may adversely affect the trading price of our common stock.

Our revenues and operating results may vary significantly from quarter to quarter due to a number of factors, many of which are outside of our control and any of which may cause our stock price to fluctuate. Generally, purchases by service providers of telecommunications equipment from manufacturers have been unpredictable and clustered, rather than steady, as the providers build out their networks. The primary factors that may affect our revenues and operating results include the following:

- fluctuation in demand for our voice infrastructure products and the timing and size of customer orders;
- the cancellation or deferral of existing customer orders or the renegotiation of existing contractual commitments;
- the failure of certain of our customers to successfully and timely reorganize their operations, including emerging from bankruptcy;
- the length and variability of the sales cycle for our products;
- the timing of revenue recognition;
- new product introductions and enhancements by our competitors or by us;
- changes in our pricing policies, the pricing policies of our competitors and the prices of the components of our products;
- our ability to develop, introduce and ship new products and product enhancements that meet customer requirements in a timely manner;
- the mix of product configurations sold;
- our ability to obtain sufficient supplies of sole or limited source components;
- our ability to attain and maintain production volumes and quality levels for our products;
- costs related to acquisitions of complementary products, technologies or businesses;
- general economic conditions, as well as those specific to the telecommunications, networking and related industries;
- consolidation within the telecommunications industry, including acquisitions of or by our customers, and
- the application of complex revenue recognition accounting rules to our customer arrangements.

As with other telecommunications product suppliers, we may recognize a substantial portion of our revenue in a given quarter from sales booked and shipped in the last weeks of that quarter. As a result, delays in customer orders may result in delays in shipments and recognition of revenue beyond the end of a given quarter.

A significant portion of our operating expenses is fixed in the short-term. If revenues for a particular quarter are below expectations, we may not be able to reduce operating expenses proportionally for the quarter. Any such revenue shortfall would, therefore, have a significant effect on our operating results for the quarter.

We believe that quarter-to-quarter comparisons of our operating results are not a good indication of our future performance. It is likely that in some future quarters, our operating results may be below the expectations of public market analysts and investors, which may adversely affect our stock price.

We are entirely dependent upon our voice infrastructure products and our future revenues depend upon their commercial success.

Our future growth depends upon the commercial success of our voice infrastructure products. We intend to develop and introduce new products and enhancements to existing products in the future. We may not successfully complete the development or introduction of these products. If our target customers do not adopt, purchase and successfully deploy our current or planned products, our revenues will not grow.

If we do not respond rapidly to technological changes or to changes in industry standards, our products could become obsolete.

The market for packet voice infrastructure products is likely to be characterized by rapid technological change and frequent new product introductions. We may be unable to respond quickly or effectively to these developments. We may experience difficulties with software development, hardware design, manufacturing or marketing that could delay or prevent our development, introduction or marketing of new products and enhancements. The introduction of new products by our competitors, the market acceptance of products based on new or alternative technologies or the emergence of new industry standards could render our existing or future products obsolete. If the standards adopted are different from those that we have chosen to support, market acceptance of our products may be significantly reduced or delayed. If our products become technologically obsolete, we may be unable to sell our products in the marketplace and generate revenues.

If we fail to compete successfully, our ability to increase our revenues or return to profitability will be impaired.

Competition in the telecommunications market is intense. This market has historically been dominated by large companies, such as Lucent Technologies, NEC, Nortel Networks, Siemens and Ericsson, all of which are our direct competitors. We also face competition from other large telecommunications and networking companies, including Cisco Systems, some of which have entered our market by acquiring companies that design competing products. Because this market is rapidly evolving, additional competitors with significant financial resources may enter these markets and further intensify competition.

Many of our current and potential competitors have significantly greater selling and marketing, technical, manufacturing, financial and other resources. Further, some of our competitors sell significant amounts of other products to our current and prospective customers. Our competitors' broad product

portfolios, coupled with already existing relationships, may cause our customers to buy our competitors' products or harm our ability to attract new customers.

To compete effectively, we must deliver innovative products that:

- provide extremely high reliability and voice quality;
- scale easily and efficiently;
- interoperate with existing network designs and other vendors' equipment;
- provide effective network management;
- are accompanied by comprehensive customer support and professional services; and
- provide a cost-effective and space efficient solution for service providers.

If we are unable to compete successfully against our current and future competitors, we could experience price reductions, order cancellations, loss of customers and revenues and reduced gross profit margins.

Because our products are sophisticated and designed to be deployed in complex environments, they may have errors or defects that we find only after full deployment, which could seriously harm our business.

Our products are sophisticated and are designed to be deployed in large and complex networks. Because of the nature of our products, they can only be fully tested when substantially deployed in very large networks with high volumes of traffic. Some of our customers have only recently begun to commercially deploy our products and they may discover errors or defects in the software or hardware, or the products may not operate as expected. As we continue to expand our distribution channel through distributors and resellers, we will need to rely on and support their service and support organizations. If we are unable to fix errors or other performance problems that may be identified after full deployment of our products, we could experience:

- loss of, or delay in, revenues;
- loss of customers and market share;
- a failure to attract new customers or achieve market acceptance for our products;
- increased service, support and warranty costs and a diversion of development resources; and
- costly and time-consuming legal actions by our customers.

Because our products are deployed in large, complex networks around the world, failure to establish a support infrastructure and maintain required support levels could seriously harm our business.

Our products are deployed in large and complex networks around the world. Our customers expect us to establish a support infrastructure and maintain demanding support standards to ensure that their networks maintain high levels of availability and performance. To support the continued growth of our business, our support organization will need to provide service and support at a high level throughout the world. If we are unable to provide the expected level of support and service to our customers, we could experience:

- loss of customers and market share;
- a failure to attract new customers in new geographies;
- increased service, support and warranty costs and a diversion of development resources; and
- network performance penalties.

We have experienced changes in our senior management recently, which could affect our business and operations.

We have made significant changes in our senior management team recently including the hiring of a Vice President, Corporate Controller and Principal Accounting Officer in August 2005, a Vice President of Internal Operations in March 2005, and a Chief Financial Officer in December 2004. Because of these significant changes, our management team may not be able to work together effectively to successfully develop and implement our business strategies and financial operations. In addition, management will need to devote significant attention and resources to preserve and strengthen relationships with employees, customers and the investor community. If our new management team is unable to achieve these goals, our ability to grow our business and successfully meet operational challenges could be impaired.

If we fail to hire and retain needed personnel, the implementation of our business plan could slow or our future growth could halt.

Our business depends upon highly skilled engineering, sales, marketing and customer support personnel. Any failure to hire or retain needed qualified personnel could impair our growth. Our future success depends upon the continued services of our executive officers who have critical industry experience and relationships that we rely on to implement our business plan. None of our officers or key employees is bound by an employment agreement for any specific term. The loss of the services of any of our officers or key employees could delay the development and introduction of, and negatively impact our ability to sell, our products.

If we are subject to employment claims, we could incur substantial costs in defending ourselves.

We may become subject to employment claims in connection with employee terminations. In addition, companies in our industry whose employees accept positions with competitors frequently claim that their competitors have engaged in unfair hiring practices. These claims may result in material

litigation. We could incur substantial costs defending ourselves or our employees against those claims, regardless of their merits. In addition, defending ourselves from those types of claims could divert our management's attention from our operations. If we are found liable in connection with any employment claim, we may incur significant costs that could adversely impact our financial position and results of operations.

We depend upon contract manufacturers and any disruption in these relationships may cause us to fail to meet the demands of our customers and damage our customer relationships.

We rely on a small number of contract manufacturers to manufacture our products according to our specifications and to fill orders on a timely basis. Our contract manufacturers provide comprehensive manufacturing services, including assembly of our products and procurement of materials. Each of our contract manufacturers also builds products for other companies and may not always have sufficient quantities of inventory available to fill our orders or may not allocate their internal resources to fill these orders on a timely basis. We do not have long-term supply contracts with our manufacturers and they are not required to manufacture products for any specified period. We do not have internal manufacturing capabilities to meet our customers' demands. Qualifying a new contract manufacturer and commencing commercial scale production is expensive and time consuming and could result in a significant interruption in the supply of our products. If a change in contract manufacturers results in delays in our fulfillment of customer orders or if a contract manufacturer fails to make timely delivery of orders, we may lose revenues and suffer damage to our customer relationships.

We and our contract manufacturers rely on single or limited sources for supply of some components of our products and if we fail to adequately predict our manufacturing requirements or if our supply of any of these components is disrupted, we will be unable to ship our products.

We and our contract manufacturers currently purchase several key components of our products, including commercial digital signal processors, from single or limited sources. We purchase these components on a purchase order basis. If we overestimate our component requirements, we could have excess inventory, which would increase our costs. If we underestimate our requirements, we may not have an adequate supply, which could interrupt manufacturing of our products and result in delays in shipments and revenues.

We currently do not have long-term supply contracts with our component suppliers and they are not required to supply us with products for any specified periods, in any specified quantities or at any set price, except as may be specified in a particular purchase order. In the event of a disruption or delay in supply, or inability to obtain products, we may not be able to develop an alternate source in a timely manner or at

favorable prices, or at all. A failure to find acceptable alternative sources could hurt our ability to deliver high-quality products to our customers and negatively affect our operating margins. In addition, reliance on our suppliers exposes us to potential supplier production difficulties or quality variations. Our customers rely upon our ability to meet committed delivery dates, and any disruption in the supply of key components would seriously adversely affect our ability to meet these dates and could result in legal action by our customers, loss of customers or harm our ability to attract new customers.

If we are not able to obtain necessary licenses of third-party technology at acceptable prices, or at all, our products could become obsolete.

We have incorporated third-party licensed technology into our current products. From time to time, we may be required to license additional technology from third parties to develop new products or product enhancements. Third-party licenses may not be available or continue to be available to us on commercially reasonable terms. The inability to maintain or re-license any third-party licenses required in our current products or to obtain any new third-party licenses to develop new products and product enhancements could require us to obtain substitute technology of lower quality or performance standards or at greater cost, and delay or prevent us from making these products or enhancements, any of which could seriously harm the competitiveness of our products.

Failures by our strategic partners or by us in integrating products provided by our strategic partners could seriously harm our business.

Our solutions include the integration of products supplied by strategic partners, who offer complementary products and services. We rely on these strategic partners in the timely and successful deployment of our solutions to our customers. If the products provided by these partners have defects or do not operate as expected or if we do not effectively integrate and support products supplied by these strategic partners, then we may have difficulty with the deployment of our solutions that may result in:

- loss of, or delay in, revenues;
- increased service, support and warranty costs and a diversion of development resources; and
- network performance penalties.

In addition to cooperating with our strategic partners on specific customer projects, we also may compete in some areas with these same partners. If these strategic partners fail to perform or choose not to cooperate with us on certain projects, in addition to the effects described above, we could experience:

- loss of customers and market share; and
- a failure to attract new customers or achieve market acceptance for our products.

Our ability to compete and our business could be jeopardized if we are unable to protect our intellectual property or become subject to intellectual property rights claims, which could require us to incur significant costs.

We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain and use our products or technology. Monitoring unauthorized use of our products is difficult and we cannot be certain that the steps we have taken will prevent unauthorized use of our technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States. If competitors are able to use our technology, our ability to compete effectively could be harmed.

In addition, we have received inquiries from other patent holders and may become subject to claims that we infringe their intellectual property rights. Any parties asserting that our products infringe upon

their proprietary rights could force us to license their patents for substantial royalty payments or to defend ourselves and possibly our customers or contract manufacturers in litigation. These claims and any resulting licensing arrangement or lawsuit, if successful, could subject us to significant royalty payments or liability for damages and invalidation of our proprietary rights. Any potential intellectual property litigation also could force us to do one or more of the following:

- stop selling, incorporating or using our products that use the challenged intellectual property;
- obtain from the owner of the infringed intellectual property right a license to sell or use the relevant technology, which license may not be available on reasonable terms, or at all; or
- redesign those products that use any allegedly infringing technology.

Any lawsuits regarding intellectual property rights, regardless of their success, would be time-consuming, expensive to resolve and would divert our management's time and attention.

Any investments or acquisitions we make could disrupt our business and seriously harm our financial condition.

We intend to consider investing in, or acquiring, complementary products, technologies or businesses. In the event of future investments or acquisitions, we could:

- issue stock that would dilute our current stockholders' percentage ownership;
- incur debt or assume liabilities;
- incur significant impairment charges related to the write-off of goodwill and purchased intangible assets;
- incur significant amortization expenses related to purchased intangible assets; or
- incur large and immediate write-offs for in-process research and development and stock based compensation.

Our integration of any acquired products, technologies or businesses will also involve numerous risks, including:

- problems and unanticipated costs associated with combining the purchased products, technologies or businesses;
- diversion of management's attention from our core business;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have limited or no prior experience; and
- potential loss of key employees, particularly those of the acquired organizations.

We may be unable to successfully integrate any products, technologies, businesses or personnel that we might acquire in the future without significant costs or disruption to our business.

Recent rulemaking by the Financial Accounting Standards Board will require us to expense equity compensation given to our employees and may reduce our ability to effectively utilize equity compensation to attract and retain employees.

We historically have used stock options as a significant component of our employee compensation program in order to align employees' interests with the interests of our stockholders, encourage employee retention, and provide competitive compensation packages. The Financial Accounting Standards Board has adopted changes that will require companies to record a charge to earnings for employee stock option

grants and other equity incentives beginning January 1, 2006. By causing us to incur significantly increased compensation costs, such accounting changes may cause us to reduce the availability and amount of equity incentives provided to employees, which may make it more difficult for us to attract, retain and motivate key personnel.

Regulation of the telecommunications industry could harm our operating results and future prospects.

The telecommunications industry is highly regulated and our business and financial condition could be adversely affected by the changes in the regulations relating to the telecommunications industry. Currently, there are few laws or regulations that apply directly to access to or delivery of voice services on IP networks. We could be adversely affected by regulation of IP networks and commerce in any country, including the United States, where we operate. Such regulations could include matters such as voice over the Internet or using Internet protocol, encryption technology, and access charges for service providers. The adoption of such regulations could decrease demand for our products, and at the same time increase the cost of selling our products, which could have a material adverse effect on our business, operating results and financial condition.

We may seek to raise additional capital in the future, which may not be available to us, and if it is available, may dilute the ownership of our common stock.

In April and September 2003, we completed public offerings of 20,000,000 and 17,000,000 shares, respectively, of our common stock resulting in the dilution of our existing investors' percentage ownership of our common stock. In the future, we may seek to raise additional funds through public or private debt or equity financings in order to:

- fund ongoing operations and capital requirements;
- take advantage of opportunities, including more rapid expansion or acquisition of complementary products, technologies or businesses;
- develop new products; or
- respond to competitive pressures.

Any additional capital raised through the sale of convertible debt or equity may further dilute an investor's percentage ownership of our common stock. Furthermore, additional financings may not be available on terms favorable to us, or at all. A failure to obtain additional funding could prevent us from

making expenditures that may be required to grow or maintain our operations.

Our stock price has been and may continue to be volatile.

The market for technology stocks has been and will likely continue to be extremely volatile. The following factors could cause the market price of our common stock to fluctuate significantly:

- changes in our listing status on the NASDAQ Stock Market;
- the addition or loss of any major customer;
- consolidation in the telecommunications industry;
- changes in the financial condition or anticipated capital expenditure purchases of any existing or potential major customer;
- quarterly variations in our operating results;
- changes in financial estimates by securities analysts;

- speculation in the press or investment community;
- announcements by us or our competitors of significant contracts, new products or acquisitions, distribution partnerships, joint ventures or capital commitments;
- sales of common stock or other securities by us or by our stockholders in the future;
- securities and other litigation;
- announcement of a stock split, reverse stock split, stock dividend or similar event;
- economic conditions for the telecommunications, networking and related industries; and
- worldwide economic instability.

Sales of a substantial amount of our common stock in the future could cause our stock price to fall.

Some stockholders hold a substantial number of shares of our common stock that have not yet been sold in the public market. Further, additional shares may become available for sale upon the conversion or redemption of our convertible subordinated note. Sales of a substantial number of shares of our common stock within a short period of time in the future could impair our ability to raise capital through the sale of additional debt or stock and /or cause our stock price to fall.

Provisions of our charter documents and Delaware law may have anti-takeover effects that could prevent a change of control.

Provisions of our amended and restated certificate of incorporation, our amended and restated by-laws and Delaware law could make it more difficult for a third party to acquire us, even if doing so would be beneficial to our stockholders.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

We are exposed to a variety of market risks, including changes in interest rates affecting the return on its investments and foreign currency fluctuations. We have established procedures to manage our exposure to fluctuations in interest rates and foreign currency exchange rates.

We generally place our marketable debt securities in high-quality debt instruments, primarily U.S. Government, state government and corporate obligations with contractual maturities of less than one year. Beginning in the third quarter of 2005, we entered into foreign exchange contracts to hedge against currency fluctuations related to a particular account receivable denominated in Japanese Yen which were closed as of September 30, 2005. We have not experienced any material losses from our marketable security investments and therefore believe that our potential interest rate exposure is not material. As we continue to expand internationally, we will continue to evaluate the impact of foreign currency exchange risk on our results of operations.

Item 4: Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the Exchange Act)) as of September 30, 2005, which included an evaluation of disclosure controls and procedures applicable to the period covered by the filing of this periodic report. We previously reported ten material weaknesses in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act), which were described in Item 9A and Management's Report on Internal Control Over Financial Reporting in our Annual Report on Form 10-K for the year ended December 31, 2004. As a result of these material weaknesses in our internal control

over financial reporting, we have concluded that our disclosure controls and procedures were not effective as of September 30, 2005.

During the fiscal quarter ended September 30, 2005, we made changes that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. These changes consist of the following:

- We implemented system-based detail sub-ledgers related to revenue, deferred revenue, cost of revenue and inventory transactions to help ensure that balances are properly summarized and posted to our general ledger.
- We implemented a quote and proposal review and approval process intended to provide an enhanced level of management and cross-functional review for customer quotes and proposals before submission to our customers, capture the relevant data to identify all commitments made to customers for

our financial reporting and define, automate and document the required approvals.

- We enhanced our controls over cash receipts, including the implementation of a lockbox and reassignment of responsibilities to help ensure that all cash is accurately and timely recorded.
- We established an IT Audit and Security function to help provide assurance that changes to financial applications are properly authorized and tested and that access to our information systems and financial applications are appropriately restricted.
- We continued to enhance the level of analysis and supporting documentation for amounts reported in the financial statements.
- We continued to enhance our processes and procedures to help ensure that inventory valuation accounts are properly analyzed and that any resulting adjusting entries are accurately and timely recorded in our general ledger.
- We continued with the design and implementation of our information systems enhancement project to further address control deficiencies.

We continue to plan and expect to implement additional changes to our infrastructure and related processes that we believe are reasonably likely to strengthen and materially affect our internal control over financial reporting.

The changes in our internal control over financial reporting implemented by us to date will not in and of themselves remediate the material weaknesses, and certain of these remedial measures will require some time to be fully implemented or to take full effect. Prior to the remediation of these material weaknesses, there remains risk that the transitional controls, described below, on which we currently rely will fail to be sufficiently effective, which could result in material misstatement of our financial position or results of operations and require a restatement.

We are currently implementing an enhanced internal controls environment intended to address the material weaknesses in our internal control over financial reporting and to remedy the ineffectiveness of our disclosure controls and procedures. While this implementation phase is underway, we are relying on extensive manual procedures, including regular reviews and the significant utilization of external professionals, to assist us with meeting the objectives otherwise fulfilled by an effective internal controls environment. We expect to establish and implement a policy-based system of internal controls. While we are undertaking the implementation of this new internal controls environment, there remains risk that the transitional controls on which we are currently relying will fail to be sufficiently effective. We also note, however, that an internal control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the internal control system are met. Further, the design of an internal control system must include an assessment of the costs and related risks associated

with the control and the purpose for which it was intended. Because of the inherent limitations in all internal control systems, no evaluation of internal controls can provide absolute assurance that all control issues including instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and breakdowns can occur because of simple error or mistake. Additionally, internal controls can be circumvented by the individual acts of some person, by collusion of two or more people, or by management override of the controls. The design of any system of internal controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, our internal control systems, as we develop them, may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected and could be material to our financial statements.

The certifications of our Chief Executive Officer and Chief Financial Officer required in accordance with Rule 13a-14(a) under the Exchange Act are attached as exhibits to this Quarterly Report on Form 10-Q. The disclosures set forth in this Item 4 contain information concerning the evaluation of our disclosure controls and procedures, and changes in our internal control over financial reporting, referred to in paragraph 4 of those certifications. Those certifications should be read in conjunction with this Item 4 for a more complete understanding of the matters covered by the certifications.

PART II—OTHER INFORMATION

Item 1: Legal Proceedings

In November 2001, a purchaser of our common stock filed a complaint in the United States District Court for the Southern District of New York against us, two of our officers and the lead underwriters alleging violations of the federal securities laws in connection with our initial public offering (IPO) and seeking unspecified monetary damages. The purchaser seeks to represent a class of persons who purchased our common stock between the IPO on May 24, 2000 and December 6, 2000. An amended complaint was filed in April 2002. The amended complaint alleges that our registration statement contained false or misleading information or omitted to state material facts concerning the alleged receipt of undisclosed compensation by the underwriters and the existence of undisclosed arrangements between underwriters and certain purchasers to make additional purchases in the after market. The claims against us are asserted under Section 10(b) of the Securities Exchange Act of 1934 and Section 11 of the Securities Act of 1933 and against the individual defendants under Sections 11 and 15 of the Securities Act and Sections 10(b) and 20(a) of the Exchange Act. Other plaintiffs have filed substantially similar class action cases against approximately 300 other publicly traded companies and their IPO underwriters which, along with the actions against us, have been transferred to a single federal judge for purposes of coordinated case management. On July 15, 2002, we, together with the other issuers named as defendants in these coordinated proceedings, filed a collective motion to dismiss the consolidated amended complaints on various legal grounds common to all or most of the issuer defendants. The plaintiffs voluntarily dismissed the claims against many of the individual defendants, including our officers named in the complaint. On February 19, 2003, the court granted a portion of the motion to dismiss by dismissing the Section 10(b) claims against certain defendants including us, but denied the remainder of the motion as to the defendants. In June 2003, a special committee of our Board of Directors authorized us to enter into a proposed settlement with the plaintiffs on terms substantially consistent with the terms of a Memorandum of Understanding negotiated among representatives of the plaintiffs, the issuer defendants and the insurers for the issuer defendants. On February 15, 2005, the court preliminarily approved the terms of the proposed settlement contingent on modifications to the proposed settlement. On August 31, 2005, the court approved the terms of the proposed settlement, as modified. The settlement is subject to class certification and final approval by the court. A hearing has been scheduled on April 24, 2006 for final approval. The proposed settlement would not require any settlement payment by Sonus, therefore Sonus does not expect that the settlement would have a material impact on its business or financial results.

Beginning in July 2002, several purchasers of our common stock filed complaints in the United States District Court for the District of Massachusetts against us, certain officers and directors and a former officer under Sections 10(b) and 20(a) and Rule 10b-5 of the Securities Exchange Act of 1934 (Class Action Complaints). The purchasers seek to represent a class of persons who purchased our common stock between December 11, 2000 and January 16, 2002, and seek unspecified monetary damages. The Class Action Complaints were essentially identical and alleged that we made false and misleading statements about our products and business. On March 3, 2003, the plaintiffs filed a Consolidated Amended Complaint. On April 22, 2003, we filed a motion to dismiss the Consolidated Amended Complaint on various grounds. On May 11, 2004, the court held oral argument on the motion, at the conclusion of which the court denied our motion to dismiss. The plaintiffs filed a motion for class certification on July 30, 2004, . On February 16, 2005, the court certified the class and appointed a class representative. On March 9, 2005, the court appointed the law firm of Moulton & Gans as lead counsel. After the court requested additional briefing on the adequacy of the class representative, the class representative withdrew. Lead counsel then filed a motion to substitute a new plaintiff as the class representative. On May 19, 2005 the court held a hearing on the motion and took the matter under advisement. On August 15, 2005, the court issued an order decertifying the class and requiring the parties to submit a joint report informing the court whether the cases have been settled and whether defendants

would be seeking to recover attorney's fees from the plaintiffs. On September 30, 2005, the plaintiffs filed motions to voluntarily dismiss their complaints with prejudice. On October 5, 2005, the court entered an order dismissing the cases. On October 21, 2005, the defendants filed a motion seeking the recovery of attorneys' fees from plaintiffs. The plaintiffs have until December 5, 2005 to respond to the motion.

Beginning in February 2004, a number of purported shareholder class action complaints were filed in the United States District Court for the District of Massachusetts against us and certain of our current officers and directors. On June 28, 2004, the court consolidated the claims. On December 1, 2004, the lead plaintiff filed a consolidated amended complaint. The complaint asserts claims under the federal securities laws, specifically Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Sections 11, 12(a), and 15 of the Securities Act of 1933, relating to our restatement of our financial results for 2001, 2002, and the first three quarters of 2003. Specifically, the complaint alleges that we issued a series of false or misleading statements to the market concerning our revenues, earnings, and financial condition. Plaintiffs contend that such statements caused our stock price to be artificially inflated. The complaint seeks unspecified damages on behalf of a purported class of purchasers of our common stock during the period from March 28, 2002, through March 26, 2004. On January 28, 2005, we filed a motion to dismiss the Section 10(b) and 12(a) claims and joined the motion to dismiss the Section 11 claim filed by the individual defendants. On June 1, 2005, the court held a hearing on the motion and allowed the plaintiff to file an amended complaint. The plaintiff filed an Amended Complaint that included the same claims and substantially similar allegations as set forth in the prior Complaint. On September 12, 2005, the defendants filed motions to dismiss this Amended Complaint. The Court has scheduled a hearing on the motions for December 10, 2005. We believe that we have substantial legal and factual defenses to the claims, which we intend to pursue vigorously. There is no assurance we will prevail in defending these actions. A judgment or a settlement of the claims against the defendants could have a material impact of Sonus' financial results.

In February 2004, three purported shareholder derivative lawsuits were filed in the United States District Court for the District of Massachusetts against us and certain of our officers and directors, naming us as a nominal defendant. Also in February 2004, two purported shareholder derivative lawsuits were filed in the business litigation session of the superior court of Suffolk County of Massachusetts against us and certain of our directors and officers, also naming us as a nominal defendant. The suits claim that certain of our officers and directors breached their fiduciary duties to our stockholders and to us. The complaints are derivative in nature and do not seek relief from us. However, we have entered into indemnification agreements in the ordinary course of business with certain of the defendant officers and directors and may be obligated throughout the pendency of these actions to advance payment of legal fees and costs incurred by the defendants pursuant to our obligations under the indemnification agreements or applicable Delaware law. On September 27, 2004, the state court granted our motion to dismiss. On October 26, 2004, the plaintiffs filed a notice appealing the state court's dismissal of the actions. On June 24, 2005, the plaintiffs withdrew the appeal and dismissed the case with prejudice. In the federal actions, on June 28, 2004, the court consolidated and stayed the three actions. On October 12, 2004, the lead plaintiff filed a consolidated amended complaint. On June 1, 2005, the court held a hearing on the motion and allowed the plaintiff to file an amended complaint. On July 1, 2005, the plaintiff filed and amended complaint. The defendants renewed their motions to dismiss. The court has scheduled a hearing on the motions for December 10, 2005. There is no assurance we will prevail in defending these actions. Sonus does not expect these shareholder derivative claims will have a material impact on its financial results.

In December 2004, a purchaser of our common stock filed a complaint in the circuit court in Will County, Illinois, against us, one of our officers, and a former officer alleging misrepresentation and fraud in connection with the plaintiff's purchase of our stock. The Complaint seeks unspecified damages. We filed a motion to dismiss the complaint. On May 5, 2005, the plaintiff filed an amended complaint. On October 26, 2005, the court held a hearing on the motion during which he dismissed the federal claims

without prejudice and dismissed the state claims without prejudice and leave to refile within 28 days. If the plaintiff does not refile within 28 days then the state claims will be dismissed with prejudice. The court scheduled a status hearing for December 1, 2005. Sonus does not expect that this claim will have a material impact on its financial results.

Sonus includes standard intellectual property indemnification provisions in its product agreements in the ordinary course of business. Pursuant to Sonus' product agreements, Sonus will indemnify, hold harmless, and reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally business partners or customers, in connection with certain patent, copyright or other intellectual property infringement claims by third parties with respect to Sonus' products. Other agreements with Sonus' customers provide indemnification for claims relating to property damage or personal injury resulting from the performance of services by Sonus or its subcontractors. Historically, Sonus' costs to defend lawsuits or settle claims relating to such indemnity agreements have been insignificant. Accordingly, the estimated fair value of these indemnification provisions is immaterial.

Item 6: Exhibits

Exhibit Number	Description
10.28	Office Lease Agreement, dated July 19, 2005, between Sonus Networks, Inc. and Pearson Fund III, L.P. with respect to property located at 1130 East Arapaho Road, Richardson, Texas.
10.29(a)	Employment letter dated August 11, 2005, by and between the Registrant and Paul K. McDermott.

31.1	Certification of Sonus Networks, Inc. Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
31.2	Certification of Sonus Networks, Inc. Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
32.1	Certification of Sonus Networks, Inc. Chief Executive Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934.
32.2	Certification of Sonus Networks, Inc. Chief Financial Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934.

(a) Incorporated by reference from the Registrant's Form 8-K (file No. 000-30229) filed August 15, 2005 with the SEC.

SIGNATURES

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

Dated: November 8, 2005

SONUS NETWORKS, INC.

By: /s/ ELLEN B. RICHSTONE
Ellen B. Richstone
Chief Financial Officer (Principal Financial Officer)

SONUS NETWORKS, INC.

By: /s/ PAUL K. MCDERMOTT
Paul K. McDermott
Vice President of Finance, Corporate Controller and Principal Accounting Officer (Principal Accounting Officer)

EXHIBIT INDEX

Exhibit Number	Description
10.28	Office Lease Agreement, dated July 19, 2005, between Sonus Networks, Inc. and Pearson Fund III, L.P. with respect to property located at 1130 East Arapaho Road, Richardson, Texas.
10.29(a)	Employment letter dated August 11, 2005, by and between the Registrant and Paul K. McDermott.
31.1	Certification of Sonus Networks, Inc. Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
31.2	Certification of Sonus Networks, Inc. Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
32.1	Certification of Sonus Networks, Inc. Chief Executive Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934.
32.2	Certification of Sonus Networks, Inc. Chief Financial Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934.

(a) Incorporated by reference from the Registrant's Form 8-K (file No. 000-30229) filed August 15, 2005 with the SEC.

LEASE PACKAGE:

RESPECTING LEASE BY AND BETWEEN

PEARSON FUND III, L.P., a Texas limited partnership ("LANDLORD"),

And

SONUS NETWORKS, INC, a Delaware corporation ("TENANT")

RESPECTING LEASE OF PREMISES SITUATED AT 1130 EAST ARAPAHO ROAD, RICHARDSON, TEXAS 75081:

1. BASIC LEASE INFORMATION

2. STANDARD LEASE, INCLUDING EXHIBITS THERETO AS FOLLOWS:

Exhibit A-l	-	Legal Description of the Land
Exhibit A-2	-	General Depiction of the Premises – 1st Floor
Exhibit A-3	-	General Depiction of the Premises – 2nd Floor
Exhibit B	-	Building Rules and Regulations
Exhibit C	-	Operating Expense Escalator
Exhibit D	-	Special Provisions
Exhibit D-l	-	ADA Compliance Matters
Exhibit E	-	Parking
Exhibit F	-	Intentionally Deleted
Exhibit G	-	Subordination Non-Disturbance and Attornment Agreement
Exhibit H	-	Intentionally Deleted
Exhibit I	-	Janitorial Specifications

BASIC LEASE INFORMATION

Lease Date/Effective Date: Effective, but not necessarily signed, July 19, 2005.

Commencement Date: The earlier of (a) November 15, 2005 (provided that Landlord delivers possession of the Premises to Tenant on the Lease Date; otherwise, such date shall be extended one day for each day of delay in delivering possession of the Premises to Tenant) or (b) the date on which Tenant occupies any portion of the Premises and begins conducting business therein, as may be adjusted to the date set forth in that certain letter agreement between Landlord and Tenant described in Section 3 of this Lease.

Tenant:

Sonus Networks, Inc., a Delaware corporation

Tenant's Address:

Sonus Networks, Inc.
1130 East Arapaho Road
Suite 200
Richardson, Texas 75081
Attention: Mike Eastep
Telephone: 972.301.4930
Facsimile: 972.680.6329

with a copy to:
Sonus Networks, Inc.
250 Apollo Drive
Chelmsford, MA 01824
Attention: General Counsel
Telephone: 978.614.8505
Facsimile: 978.614.8651

Landlord: Pearson Fund III, L.P., a Texas limited partnership

Landlord's Address:

Pearson Fund III, L.P.
9000 Mountbatten Circle
Austin, TX 78730
Attention: Craig Nemec, President
Telephone: 512.342.1700
Facsimile: 512.233.5280

with a copy to:
Pearson Group, Inc.
1130 East Arapaho Road
Suite 190
Attention: Craig Nemec, Pres.
Richardson, Texas 75081

Telephone:
972.234.3743
Facsimile:
972.664.1084

Premises: Suite 200, containing approximately **26,537** rentable square feet, as outlined on the floor plans attached hereto as Exhibits A-2 and A-3 (**"Premises"**), comprising a portion of the 1st and 2nd floors of the six-story office building (the **"Building"**) located on that certain real property commonly known as Two Richardson Center, Richardson, Dallas County, Texas, with a street address of 1130 East Arapaho Road, Richardson, Texas 75081 (Dallas County, Texas), comprised of a stipulated **119,169** rentable square feet, as more particularly described on Exhibit A-l (the **"Land"**), together with the non-exclusive use of the Common Area of the first floor of the Building, including, without limitation, the loading dock area and the front lobby (collectively the **"First Floor Common Area"**). The Premises and the First and Second Floor Common Areas are generally depicted and shown on Exhibits A-2 and A-3; said exhibits being attached for identification purposes only, and such depictions are expressly made WITHOUT WARRANTY, EXPRESS OR IMPLIED, OF ANY KIND. The First and Second Floor Common Areas do not include the elevator closets and mechanical rooms on the first and second floors of the Building as depicted and shown on Exhibit A-2 and A-3.

Measurement and calculation of rentable area has been performed in accordance with the Building Owners and Managers Association (**"BOMA"**) guidelines using no more than a 15.0% load factor with respect to each multi-tenant floor of the Building and a 8.0% load factor with respect to each single tenant floor of the Building (i.e., the 2nd floor); it being agreed that, at no time during the Term, shall such load factors exceed such percentages. Landlord and Tenant hereby stipulate that notwithstanding anything herein to the contrary, the Premises shall be deemed to consist of **19,478** rentable square feet on the 2nd Floor and **7,059** rentable square feet on the 1st Floor, and that no shortage or overage in the rentable square feet of the Premises purported by either party shall be the basis for changing the number of rentable square feet herein stipulated, other than in the event of Tenant's exercise of its Expansion Option, if any, as provided in the Lease.

Term: 60 full calendar months, plus any partial month from the Commencement Date to the end of the month in which the Commencement Date occurs, beginning on the Commencement Date and ending at 5:00 p.m. local time on the last day of the 60th full calendar month following the Commencement Date, subject to adjustment and earlier termination as provided in the Lease.

Basic Rental:

LEASE MONTHS:	ANNUAL BASIC RENTAL PER RENTABLE SQUARE FOOT:	MONTHLY BASIC RENTAL:
1-3*	$ 0.00	$ 0.00
4-12	$ 10.00	$ 22,114.17
13-60	$ 18.50	$ 40,911.21

As used herein, the term **"Lease Month"** means each calendar month during Term (and if the Commencement Date does not occur on the first day of the calendar month, the period from the Commencement Date to the first day of the next calendar month shall be included in the first Lease Month for purposes of determining the duration of the Term and the monthly Basic Rental applicable for such partial month.

*Notwistanding the foregoing, the Basic Rent shall be $0.00 with respect to the first 92 days of the Term and any remaining portion of the calendar month after such initial 92-day period expires shall be prorated based on the number of days remaining in such month, the total number of days in such month and a monthly Basic Rental of $22,114.17.

Security Deposit **$30,000.00.**

Rent: Basic Rental, Electricity Costs, Excess (as defined in Exhibit C), and all other sums that Tenant may owe to Landlord under the Lease.

Permitted Use: General business and professional offices, research and development, training, demonstration and sales and service of telephony equipment.

Expense Stop: Basic Cost (as defined in Exhibit C) per rentable square foot in the Building for calendar year 2006 (the "Base Stop Year") as more fully set forth on Exhibit C.

Initial Liability Insurance $1,000,000.00 per occurrence, and $2,000,000.00 in the aggregate.

Amount:

Tenant's Pro Rata Share 22.27%, being the percentage obtained by dividing (a) the number of rentable square feet in the Premises as stated above by (b) the 119,169 rentable square feet in the Building.

SIGNATURES ON FOLLOWING PAGE

The foregoing Basic Lease Information is incorporated into and made a part of the Lease identified above. If any conflict exists between any Basic Lease Information (as set forth herein) and the Lease, then the Basic Lease Information shall control.

LANDLORD:

PEARSON FUND III, L.P.
a Texas limited partnership

By: Pearson Group Capital Management III, Inc.
General Partner

By: /s/ Craig Nemec
Name: Craig Nemec
Title: President

Signed the 31st day of July 2005

TENANT:

SONUS NETWORK INC.,
a Delaware corporation

By: /s/ Ellen B. Richstone
Name: Ellen B. Richstone
Title: CFO
Signed the 29th day of July, 2005

STANDARD LEASE PROVISIONS

THIS LEASE (this **"Lease"**) is entered into effective, but not necessarily signed July 19, 2005, by and between Pearson Fund III, L.P., a Texas limited partnership (**"Landlord"**), and Sonus Networks, Inc., a Delaware corporation (**"Tenant"**).

DEFINITIONS AND BASIC PROVISIONS

1. The definitions and basic provisions set forth in the Basic Lease information (the **"Basic Lease Information"**) executed by Landlord and Tenant contemporaneously herewith are incorporated herein by reference for all purposes.

LEASE GRANT

2. Subject to the terms of this Lease, Landlord leases to Tenant, and Tenant leases from Landlord, the Premises. Except as may be expressly provided elsewhere in this Lease, Tenant hereby accepts the Premises in their **"AS-IS"** condition. Landlord shall have no obligation to perform any work therein (including demolition of any improvements existing therein or construction of any tenant finish-work or other improvements therein), and shall not, except as provided in Exhibit D, be obligated to reimburse Tenant or provide an allowance for any costs related to the demolition or construction of improvements therein. Landlord shall deliver possession and permit early occupancy immediately upon complete execution hereof and receipt of proof of Tenant's insurance as required in this Lease. Occupancy of the Premises by Tenant prior to the Commencement Date shall be subject to all provisions of this Lease excepting only those requiring the payment of Basic Rent. Notwithstanding anything to the contrary contained in this Lease, if Landlord does not deliver possession of the Premises to Tenant on or before the later of the date this Lease is executed by Tenant or August 1, 2005, Tenant may terminate this Lease by delivering to Landlord written notice thereof.

TERM

3. The Term of the Lease shall commence as of the Commencement Date. By occupying the Premises, Tenant shall be deemed to have accepted the Premises in their condition as of the date of such occupancy, subject to the performance of punch-list items that remain to be performed by Landlord pursuant to the express provisions hereof, if any. Tenant shall execute and deliver to Landlord, within ten days after Landlord has requested same, a letter confirming (i) that Tenant has accepted the Premises, and (ii) that Landlord has performed all of its obligations with respect to the Premises.

RENT

4. (a) **Payment**. Tenant shall timely pay to Landlord the Basic Rental without demand and all additional sums to be paid by Tenant to Landlord under this Lease, including the amounts set forth in Section 4(b) below (Tenant's Share of Electricity Costs) and in Exhibit C (Operating Expense Escalator) after receipt of a monthly invoice therefor, without further demand, deduction or set off, at Landlord's Address (or such other address within the continental

United States as Landlord may from time to time designate in writing to Tenant). Basic Rental, adjusted as herein provided, shall be payable monthly in advance. The first monthly installment of Basic Rental shall be payable contemporaneously with the Commencement Date of this Lease, which installment shall be prorated if such date does not fall on the first day of the month, and thereafter, monthly installments of Basic Rental shall be due on the first day of the first calendar month immediately following the Commencement Date. Monthly installments shall continue on the first day of each succeeding calendar month during the Term. Basic Rental for any fractional month at the beginning of the Term shall be prorated based on 1/365 of the current annual Basic Rental for each day of the partial month from the Commencement Date to the first day of the first calendar month immediately following the Commencement Date.

(b) **Electricity Costs**. In addition to Basic Rental and any other amounts to be paid by Tenant to Landlord under this Lease, Tenant will pay to Landlord, concurrently with each monthly installment of Basic Rental, Tenant's Share (as hereinafter defined) of all electricity (including the cost of electricity for Landlord to provide HVAC) used by the Building (**"Electricity Costs"**) the prior month. The term **"Tenant's Share"** shall mean Tenant's ProRata Share adjusted as reasonably determined by Landlord to (aa) compensate for the first and final months of the Lease term and or (bb) reflect any disproportionate utility requirements of any occupant or tenant of the Building; provided, however, that in the event the Premises are ever separately metered, Tenant shall directly pay for Electricity Costs as so metered for the

Premises and shall have no further obligation to pay any other Electricity Costs, other than Tenant's Share of Electricity Costs attributable to the Common Area as reasonably determined by Landlord. Landlord shall use commercially reasonable efforts to cause any tenants of the Building whose equipment consumes a disproportionate amount of electricity (relative to other tenants in the Building) to pay their fair share of Electrical Costs.

DELINQUENT PAYMENT; HANDLING CHARGES

5. All payments required of Tenant hereunder shall bear interest from seven (7) days after the date due until paid at the lower of the Prime Rate (as defined in Section 18(a)) or the maximum lawful rate. Alternatively, Landlord may charge Tenant a fee equal to 5% of any delinquent payment (**"Late Fee"**) to reimburse Landlord for its cost and inconvenience incurred as a consequence of Tenant's delinquency if any payment is not made by Tenant within seven (7) days of the date due; provided however, such interest or Late Fee shall not be charged with respect to the first two (2) of such occasions hereunder during the Term, but not otherwise. In no event shall the charges permitted under this Section 5 or elsewhere in this Lease, to the extent the same are considered to be interest under applicable law, exceed the maximum lawful rate of interest.

SECURITY DEPOSIT

6. Within ten (10) business days of the Effective Date of this Lease, Tenant shall pay to Landlord, in immediately available funds, the Security Deposit, which shall be held by Landlord without liability for interest and as security for the performance by Tenant of its obligations under this Lease. The Security Deposit is not an advance payment of Rent or a measure or limit of Landlord's damages upon an Event of Default (defined below). Landlord may, from time to time and without prejudice to any other remedy, use all or a part of the Security Deposit to perform any obligation which Tenant was obligated, but failed, to perform hereunder. Following any such application of the Security Deposit, Tenant shall pay to Landlord on demand the amount so applied in order to restore the Security Deposit to its original amount. Within sixty (60) days after the Term ends, provided Tenant has performed all of its obligations hereunder, Landlord shall return to Tenant the balance of the Security Deposit not applied to satisfy Tenant's obligations. If Landlord transfers its interest in the Premises, then Landlord may assign the Security Deposit to the transferee and Landlord thereafter shall have no further liability for the return of the Security Deposit.

LANDLORD'S OBLIGATIONS

7.

(a) **Services**. Subject to the provisions of Section 4(b) (Tenant's Share of Electricity Costs) and the Rules and Regulations hereinafter referred to, and while Tenant is occupying the Premises, Landlord shall furnish to Tenant:

(i) water (hot and cold) at those points of supply provided for general use of tenants of the Building;

(ii) heated and refrigerated air conditioning in season during Building Hours (as set forth in Exhibit B hereto, the Rules and Regulations) throughout the year other than holidays, at such temperatures and in such amounts as are standard for comparable buildings in the vicinity of the Building; provided that Tenant acknowledges that such service and temperature may be subject to change by local, county, state or federal regulation; and whenever atypical business use, machines or equipment that generate abnormal heat are used in the Premises (excluding the server room on the first floor of the Premises) which affect the temperature otherwise maintained by the air conditioning system, Landlord shall have the right to install supplemental air conditioning in the Premises (excluding the server room on the first floor of the Premises), and the reasonable cost thereof, including the cost of installation, operation, use and maintenance, shall be paid by Tenant to Landlord as additional rental upon demand;

(iii) janitorial service and maintenance, as set forth in the attached Exhibit I (Janitorial Specifications) respecting the Building and Parking Facilities (as hereinafter defined) on weekdays other than holidays for Building-standard installations (Landlord reserves the right to bill Tenant separately for

extra janitorial service required for non-standard installations) and such window washing as may from time to time in

Landlord's judgment may be reasonably required (which shall not be less than two times per calendar year);

(iv) elevators for access to the Premises in common with other tenants, if applicable, provided that Landlord may reasonably limit the number of elevators to be in operation at times other than during customary business hours and on holidays,

(v) replacement of Building-standard light bulbs and fluorescent tubes; provided that Landlord's standard charge for such bulbs and tubes shall be paid by Tenant; and

(vi) electrical current to the Building during all hours for equipment that requires not more than 110 volts, and whose electrical energy consumption does not exceed normal office usage.

Landlord shall maintain the Common Area of the Building in reasonably good order and condition. If Tenant desires any of the services specified in this Section 7 (ii) at any time other than (A) between **7:00 a.m. and 7:00 p.m.** on weekdays and (B) between **8:00 a.m. and 1:00 p.m. on Saturday**, such services shall be supplied to Tenant upon the written request of Tenant delivered to Landlord before 3:00 p.m. on the business day preceding such extra usage, and Tenant shall pay to Landlord the lesser of (i) the cost of such services or (ii) $50.00 within 10 days after Landlord has delivered to Tenant an invoice therefor.

Landlord shall provide the services referred to in Section 7(a)(i) through 7{a) (v) and shall maintain the Common Area, the Building's HVAC, life-safety, plumbing, electrical and mechanical systems at a level substantially similar to the level of service and maintenance that is typical in other similar class office buildings located in the submarket in the city in which the Building is located.

Landlord shall, at its sole cost and expense, install a separate meter, or separate sub-meter, for electricity consumption attributable to the server room located at the first floor of the Premises and Tenant shall pay the electrical costs attributable to the server room directly to the utility provider, or to Landlord with the next due Monthly Basic Rental following receipt of a statement there for, as may be applicable.

(b) **Discontinuance**. **[INTENTIONALLY OMITTED]**.

(c) **Restoration of Services; Abatement**. Landlord shall use reasonable efforts to restore any service that becomes unavailable; provided however, such unavailability, irrespective of the cause thereof, shall not render Landlord liable for any damages caused thereby, be a constructive eviction of or disturbance of Tenant, constitute a breach of any implied warranty, or, except as provided in the next sentence, entitle Tenant to any abatement of Tenant's obligations hereunder. However, if Tenant is prevented from making reasonable use of the Premises for more than seven (7) consecutive days because of the unavailability of any such service, irrespective of the cause thereof, Tenant shall, as its exclusive remedy therefor, be entitled to a per diem abatement of Basic Rental for each consecutive day (after such 7-day period) that Tenant is so prevented from making reasonable use of the Premises, provided such unavailability is not caused in whole or in part by Tenant, in which case Tenant shall not be entitled to such abatement.

(d) **Landlord's Obligations**. Landlord shall commence making necessary repairs and cure of damage to the Building corridors, lobby, structural members of the Building and equipment used to provide the services referred to in sub-section 7(a) hereof within twenty (20) days of discovering such damage, and shall thereafter diligently prosecute such repairs at Landlord's cost (subject to reimbursement to Landlord by the Building's tenants, including Tenant, pursuant to a provision similar to Exhibit C hereto); unless any such damage is caused by the gross neglidence of Tenant, or Tenant's agents, employees or invitees, in which event Tenant shall bear the cost of such repairs. Tenant shall promptly give Landlord notice of any damage in the Premises requiring repair by Landlord, as aforesaid.

(e) **Access** Tenant will be provided access to the Premises 24 hours per day, seven days per

week. If such access is unavailable due to force majeure or any other reason beyond Landlord's control (including construction performed by parties other than Landlord which prohibits such access), Landlord shall not be in default under this Section 7(e). If reasonable access to the Premises is unavailable preventing Tenant from making reasonable use of any substantial portion of the Premises for its intended purpose for more than seven (7) consecutive days following written notice from Tenant to Landlord and such unavailability was not caused in whole or in part by Tenant, then Tenant shall, as its exclusive remedy therefor, be entitled to a reasonable abatement of Rent for each consecutive day (immediately following such 7-day period,) that Tenant is so prevented from making reasonable use of such portion of the Premises based on the area thereof.

(f) **Self-Help**. If at any time following the Commencement Date Landlord fails to deliver electrical service, elevator service, HVAC service, sewer service or water service to the Premises (the **"Critical Services"**) for ten (10) consecutive days after Tenant advises Landlord in writing that the Critical Services are not being provided to the Premises, and Landlord has not commenced to cure such cessation of Critical Services within five (5) days thereafter, has failed to prosecute such cure with reasonable diligence or has failed to cure same within one hundred fifty (150) days thereafter, Tenant shall be entitled to restore such service in a commercially reasonable manner. Landlord shall reimburse Tenant for its actual and reasonable, out-of-pocket costs therefor within 30 days after delivery to Landlord of a reasonably detailed invoice, failing which default interest shall accrue thereon from the date due until the date paid at the lesser of the Prime Rate or the maximum lawful rate. If the unavailability of such Critical Services is caused by a Taking (defined below) or a Casualty (defined below), then the provisions of

this Section shall not be applicable thereto; rather, the provisions of Section 14 and 15 (as the case may be) shall apply.

IMPROVEMENTS; ALTERATIONS; REPAIRS; MAINTENANCE

8. (a)(l) **Improvements; Alterations**. Improvements to the Premises (including any signage, antennas, or risers respecting the Building) may be installed at the expense of Tenant only in accordance with plans and specifications submitted to and approved in writing by Landlord, prior to the commencement of any improvements. No alterations or physical additions in or to the Premises may be made without Landlord's prior written consent, which shall not be unreasonably withheld, conditioned or delayed. Notwithstanding the foregoing, Tenant shall not be required to obtain Landlord's consent for repainting, recarpeting, or other cosmetic alterations, tenant improvements, alterations or physical additions to the Premises which are cosmetic in nature totaling less than $25,000 in any single instance or series of related cosmetic alterations performed within a six-month period (provided that Tenant shall not perform any such cosmetic improvements, alterations or additions to the Premises in stages as a means to subvert or circumvent this provision). Tenant may, subject to applicable law and Landlord's prior written approval, not to be unreasonably withheld, conditioned or delayed, and management, install signage at the Premises, only as provided herein. All alterations, additions, or improvements (whether temporary or permanent in character, and including without limitation all air-conditioning and all other equipment that is in any manner connected to the Building's plumbing system) made in or upon the Premises, either by Landlord or Tenant, shall be Landlord's property at the end of the Term and shall remain on the Premises without compensation to Tenant. Approval by Landlord of any of Tenant's drawings and plans and specifications prepared in connection with any improvements in the Premises shall not constitute a representation or warranty of Landlord as to the adequacy or sufficiency of such drawings, plans and specifications, or the improvements to which they relate, for any use, purpose, or condition, but such approval shall merely be the consent of Landlord as required hereunder.

(2) **HVAC**. Tenant shall be permitted to use the three existing HVAC units in the server room located on the first floor of the Premises and, at its sole election, shall be permitted to install additional HVAC units therein. If Tenant elects to use the existing HVAC units or to install additional units, Tenant shall, at its sole cost and expense, maintain the same and any other units installed by Tenant in the server room; provided, however, Tenant shall have no obligation to use such units or to replace any HVAC units in the Premises.

Other than as expressly provided in Exhibit D-l of this Lease, entitled Landlord's Remedial ADA Compliance Matters, which Landlord shall effectuate as provided in said Exhibit, Tenant shall be solely

responsible for the cost of all work required to comply with the retrofit requirements of the Americans with Disabilities Act of 1990 (**"ADA"**), and the Texas Elimination of Architectural Barriers Act or other applicable laws pertaining to accessibility of the Premises (but not including the Common Areas or the Parking Facilities for which Landlord shall be responsible) by disabled or handicapped persons, and all rules, regulations, and guidelines promulgated thereunder, as the same may be amended from time to time, **necessitated by any installations, additions, or alterations made in or to the Premises at the request of or by Tenant or by Tenant's use of the Premises** (other than retrofit work to the Building that is outside the Premises whose cost has been particularly identified as being payable by Landlord in an instrument signed by Landlord and Tenant), regardless of whether, such cost is incurred in connection with retrofit work required in the Premises.

(b) **Repairs; Maintenance**. Tenant shall maintain the Premises in a clean, safe, operable, attractive condition, and shall not permit or allow to remain any waste or damage to any portion of the Premises. Landlord shall, at its own expense, maintain the structure and foundation of the Building and Landlord shall, subject to reimbursement by Tenant as provided in Exhibit C, reasonably maintain the roof and structure of the Building and the electrical, mechanical, plumbing, elevators, and HVAC systems of the Building, unless such damage is caused in whole or in part by the gross negligence of Tenant, or Tenant's agents, employees or invitees, in which event Tenant shall bear the costs of such repairs. Tenant shall repair or replace, subject to Landlord's direction and supervision, any damage to the Building caused by Tenant or Tenant's agents, contractors, or invitees. If Tenant fails to commence to make any repairs or replacements required of Tenant hereunder within twenty (20) days after written demand therefor or thereafter fails to diligently pursue completion thereof, then Landlord may make the same at Tenant's cost. The reasonable cost of any repair or replacement work performed by Landlord under this Section 8 shall be paid by Tenant to Landlord within ten days after Landlord has delivered to Tenant an invoice therefor.

This Section 8(b) shall not apply in the case of damage or destruction by fire or other casualty which is covered by insurance maintained by Landlord on the Building (as to which Section 15 hereof shall apply), or damage resulting from an eminent domain taking (as to which Section 14 hereof shall apply).

(c) **Performance of Work**. All work described in this Section 8 shall he performed only by Tenant or by contractors and subcontractors approved in writing by Landlord, which approval shall not be unreasonably withheld or delayed. Tenant shall cause all contractors and subcontractors to procure and maintain insurance coverage against such risks, in such amounts, and with such companies as Landlord may reasonably require, and to procure payment and performance bonds reasonably satisfactory to Landlord covering the cost of the work. All such work shall be performed in accordance with all legal requirements and in a good and workmanlike manner so as not to damage the Premises, the primary structure or structural qualities of the Building, or plumbing, electrical lines, or other utility transmission facility. All such work which may affect the HVAC, electrical system, or plumbing must be approved by the Landlord's engineer, which shall not be unreasonably withheld, conditioned or delayed.

(d) **Mechanic's Liens**. Tenant shall not permit any mechanic's liens to be filed against the Premises, Building or any portion thereof for any work performed, materials furnished, or obligation incurred by or at the

request of Tenant. If such a lien is filed, then Tenant shall, within ten (10) days after Landlord has delivered notice of the filing to Tenant, either pay the amount of the lien or diligently contest such lien and deliver to Landlord a bond or other security reasonably satisfactory to Landlord. If Tenant fails to timely take either such action, then Landlord may pay the lien claim without inquiry as to the validity thereof, and any amounts so paid, including expenses and interest, shall be paid by Tenant to Landlord within ten (10) days after Landlord has delivered to Tenant an invoice therefor.

USE; SIGNAGE

9. Tenant shall continuously occupy and use the Premises only for the Permitted Use and shall comply with all laws, orders, rules, and regulations relating to the Permitted Use, condition, and occupancy of the Premises. The Premises shall not be used for any use which is disreputable or creates extraordinary fire hazards or results in an increased rate of insurance on the Building or its contents or the storage of any hazardous materials or substances. If, because of Tenant's acts, the rate of insurance on the

Building or its contents increases, then Tenant shall pay to Landlord the amount of such increase on demand, and acceptance of such payment shall not constitute a waiver of any of Landlord's other rights. Tenant shall conduct its business and control its agents, employees, and invitees in such a manner as not to create any nuisance or interfere with other tenants or Landlord in its management of the Building. Tenant, at Tenant's own expense, (a) shall not commit or permit waste in the Premises or the Building, and (b) shall not paint, erect or display any sign, advertisement, placard or lettering which is visible in the corridors or lobby of the Building or from the exterior of the Building without Landlord's prior written approval, which shall not be unreasonably withheld, conditioned or delayed.

ASSIGNMENT AND SUBLETTING

10. (a) **Transfers**. Except as provided in Section 10(h) (Permitted Transfers), Tenant shall not, without the prior written consent of Landlord, (1) assign, transfer, or encumber this Lease or any estate or interest herein, whether directly or by operation of law, (2) permit any other entity to become Tenant hereunder by merger, consolidation, or other reorganization, (3) if Tenant is an entity other than a corporation whose stock is publicly traded, permit the transfer of an ownership interest in Tenant so as to result in a change in the current control of Tenant, (4) sublet any portion of the Premises, (5) grant any license, concession, or other right of occupancy of any portion of the Premises, or (6) permit the use of the Premises by any parties other than Tenant (any of the events listed in Sections 10(a)(1) through 10(a)(6) being a **"Transfer"**), and any attempt to do any of the foregoing without the prior express written permission of Landlord shall be void and of no effect. In the event of any such attempted assignment or attempted sublease, or should Tenant, in any other nature of transaction, permit or attempt to permit anyone to occupy the Premises (or any portion thereof) without the prior express written permission of Landlord, and provided Tenant fails to affirmatively and effectively rescind or revoke such attempted assignment, sublease or other transfer *ab initio* within thirty (30) days of receipt of written notice from Landlord, then Landlord shall thereupon have the right and option to cancel and terminate this Lease effective upon ten (10) days(1) notice to Tenant given by Landlord at any time thereafter as to only the portion thereof which Tenant shall have attempted to assign or sublease or otherwise permitted some other party's occupancy without Landlord's prior express written permission, and if Landlord elects to cancel and terminate this Lease as to the aforesaid portion of the Premises, then the rental and other charges payable hereunder shall thereafter be proportionately reduced. Except as provided in Section 10(b) (Permitted Transfers), this prohibition against assignment or subletting shall be construed to include a prohibition against any assignment or subletting by operation of law.

(b) **Consent Standards**. Landlord shall not unreasonably withhold its consent to any assignment or subletting of the Premises, provided that the proposed transferee (1) is creditworthy, (2) will use the Premises for the Permitted Use and will not use the Premises in any manner that would conflict with any exclusive use agreement or other similar agreement entered into by Landlord with any other tenant of the Building, (3) will not use any portion of the Premises or the Building in a manner that would materially increase the pedestrian or vehicular traffic to the Premises or the Building, (4) is not a governmental entity, or subdivision or agency thereof, (5) is not another occupant of the Building, (6) is in compliance with the regulations of the Office of Foreign Asset Control (**"OFAC"**) of the Department of the Treasury (including those named on OFAC's Specially Designated and Blocked Persons List) and any statute; executive order (including the September 24, 2001, Executive Order Blocking Property and Prohibiting Transactions with Persons Who Commit, Threaten to Commit or Support Terrorism), or other governmental action relating thereto; and (7) is not a person or entity with whom Landlord is then, or has been within the six-month period prior to the time Tenant seeks to enter into such assignment or subletting, negotiating to lease space in the Building or any Affiliate of any such person or entity; otherwise, Landlord may withhold its consent in its sole discretion. Additionally, Landlord may withhold its consent in its sole discretion to any proposed Transfer if any Event of Default by Tenant then exists.

(c) **Request for Consent**. If Tenant requests Landlord's consent to a Transfer, then, at least fifteen (15) business days prior to the effective date of the proposed Transfer, Tenant shall provide Landlord with a written description of all material terms and conditions of the proposed Transfer, copies of the proposed transfer documentation, and the following information about the proposed transferee: name and address of the proposed transferee and any entities and persons who own, control or direct the proposed transferee; reasonably satisfactory information about its business and business history; its

proposed use of the Premises; banking, financial, and other credit information; and general references sufficient to enable Landlord to determine the proposed transferee's creditworthiness and character. Concurrently with Tenant's

notice of any request for consent to a Transfer, Tenant shall pay to Landlord a reasonable allocation of the expenses incurred by Landlord in reviewing such request (such allocation not exceed **$500.00**), and Tenant shall also reimburse Landlord immediately upon request for its reasonable attorneys' fees incurred in connection with considering any request for consent to a Transfer. No fees shall be payable with regard to a Permitted Transfer pursuant to Section 10(h).

If Landlord fails to notify Tenant that it approves or disapproves the requested Transfer within ten (10) business days after submission to Landlord of all of the items required under this Section 10, together with a Deemed Approval Notice (defined below), then Landlord shall be deemed to have **approved** such Transfer. A **"Deemed Approval Notice"** means a written notice from Tenant to Landlord that **conspicuously** states in bold, uppercase typeface that the requested transfer shall be deemed to be approved by Landlord unless Landlord expressly disapproves of such in a written instrument sent to Tenant within ten (10) business days of Landlord's receipt of the requested Transfer.

(d) **Conditions to Consent**. If Landlord consents to a proposed Transfer, then the proposed transferee shall deliver to Landlord a written agreement whereby it expressly assumes Tenant's obligations hereunder; however, any transferee of less than all of the space in the Premises shall be liable only for obligations under this Lease that are properly allocable to the space subject to the Transfer for the period of the Transfer. No Transfer shall release Tenant from its obligations under this Lease, but rather Tenant and its transferee shall be jointly and severally liable therefor. Landlord's consent to any Transfer shall not waive Landlord's rights as to any subsequent Transfers. If an Event of Default occurs while the Premises or any part thereof are subject to a Transfer, then Landlord, in addition to its other remedies, may collect directly from such transferee all rents becoming due to Tenant and apply such rents against Rent. Tenant authorizes its transferees to make payments of rent directly to Landlord upon receipt of notice from Landlord to do so during the continuance of an Event of Default hereunder. Tenant shall pay for the cost of any demising walls or other improvements necessitated by a proposed subletting or assignment.

(e) **Attornment by Subtenants**. Each sublease by Tenant hereunder shall be subject and subordinate to this Lease and to the matters to which this Lease is or shall be subordinate, and each subtenant by entering into a sublease is deemed to have agreed that in the event of termination, re-entry or dispossession by Landlord under this Lease, Landlord may, at its option, take over all of the right, title and interest of Tenant, as sublandlord, under such sublease, and such subtenant shall, at Landlord's option, attorn to Landlord pursuant to the then executory provisions of such sublease, except that Landlord shall not be (1) liable for any previous act or omission of Tenant under such sublease, (2) subject to any counterclaim, offset or defense that such subtenant might have against Tenant, (3) bound by any previous modification of such sublease not approved by Landlord in writing or by any rent or additional rent or advance rent which such subtenant might have paid for more than the current month to Tenant, and all such rent shall remain due and owing, notwithstanding such advance payment, (4) bound by any security or advance rental deposit made by such subtenant which is not delivered or paid over to Landlord and with respect to which such subtenant shall look solely to Tenant for refund or reimbursement, or (5) obligated to perform any work in the subleased space or to prepare it for occupancy, and in connection with such attornment, the subtenant shall execute and deliver to Landlord any instruments Landlord may reasonably request to evidence and confirm such attornment. Each subtenant or licensee of Tenant shall be deemed, automatically upon and as a condition of its occupying or using the Premises or any part thereof, to have agreed to be bound by the terms and conditions set forth in this Section 10(e). The provisions of this Section 10(e) shall be self-operative, and no further instrument shall be required to give effect to this provision.

(f) **Cancellation**. Landlord may, within twenty (20) days after submission of Tenant's written request for Landlord's consent to an assignment or subletting, cancel this Lease as to the portion of the Premises proposed to be sublet or assigned as of the date the proposed Transfer is to be effective. If Landlord cancels this Lease as to any portion of the Premises, then this Lease shall cease for such portion of the Premises and Tenant shall pay to Landlord all Rent accrued through the cancellation date relating to

the portion of the Premises covered by the proposed Transfer. Thereafter, Landlord may lease such portion of the Premises to the prospective transferee (or to any other person) without liability to Tenant.

Notwithstanding the foregoing, if Landlord provides written notification to Tenant of its election to cancel this Lease as to any portion of the Premises as provided above, Tenant may rescind its proposed assignment or subletting of all or any portion of the Premises by notifying Landlord in writing within ten (10) business days following Landlord's written cancellation notice.

(g) **Additional Compensation**. Tenant shall pay to Landlord, immediately upon receipt thereof, **fifty percent (50%)** of the excess of (1) all compensation received by Tenant for a Transfer less the actual out-of-pocket costs reasonably incurred by Tenant with unaffiliated third parties (i.e., brokerage commissions and tenant finish work) in connection with such Transfer (such costs shall be amortized on a straight-line basis over the term of the Transfer in question) over (2) the Rent allocable to the portion of the Premises covered thereby.

(h) **Permitted Transfers**. Notwithstanding Section 10(a), Tenant may Transfer all or part of its interest in this Lease or all or part of the Premises (a **"Permitted Transfer"**) to the following types of entities (a **"Permitted Transferee"**) without the written consent of Landlord:

(i) an Affiliate of Tenant;

(ii) any corporation, limited partnership, limited liability partnership, limited liability company or other business entity in which or with which Tenant, or its corporate successors or assigns, is merged or consolidated, in accordance with applicable statutory provisions governing merger and consolidation of business entities, so long as (A) Tenant's obligations hereunder are assumed by the entity surviving such merger or created by such consolidation; and (B) the Tangible Net Worth of the surviving or created entity is not less than the Tangible Net Worth of Tenant as of the date hereof; or

(iii) any corporation, limited partnership, limited liability partnership, limited liability company or other business entity acquiring all or substantially all of Tenant's assets if such entity's Tangible Net Worth after such acquisition is not less than the Tangible Net Worth of Tenant as of the date hereof.

Tenant shall promptly notify Landlord of any such Permitted Transfer. Tenant shall remain liable for the performance of all of the obligations of Tenant hereunder, or if Tenant no longer exists because of a merger, consolidation, or acquisition, the surviving or acquiring entity shall expressly assume in writing the obligations of Tenant hereunder. Additionally, the Permitted Transferee shall comply with all of the terms and conditions of this Lease, including the Permitted Use, and the use of the Premises by the Permitted Transferee may not violate any other agreements affecting the Premises, the Building, Landlord or other tenants of the Building. No later than forty-five (45) days after the effective date of any Permitted Transfer, Tenant agrees to furnish Landlord with (A) copies of the instrument effecting any of the foregoing Transfers, (B) documentation establishing Tenant's satisfaction of the requirements set forth above applicable to any such Transfer, (C) evidence of insurance as required under this Lease with respect to the Permitted Transferee, and (D) evidence of compliance with the regulations of OFAC and any statute, executive order (including the September 24, 2001, Executive Order Blocking Property and Prohibiting Transactions with Persons Who Commit, Threaten to Commit, or Support Terrorism), or other governmental action relating thereto, including the name and address of the Permitted Transferee and any entities and persons who own, control or direct the Permitted Transferee. The occurrence of a Permitted Transfer shall not waive Landlord's rights as to any subsequent Transfers. **"Tangible Net Worth"** means the excess of total assets over total liabilities, in each case as determined in accordance with generally accepted accounting principles consistently applied (**"GAAP"**) excluding, however, from the determination of total assets all assets which would be classified as intangible assets under GAAP including goodwill, licenses, patents, trademarks, trade names, copyrights, and franchises. Any subsequent Transfer by a Permitted Transferee shall be subject to the terms of this Section 10.

INSURANCE; WAIVERS; SUBROGATION; INDEMNITY

11. (a) **Insurance**. Effective as of the earlier of (1) the date Tenant enters or occupies the Premises, or (2) the Commencement Date, and continuing throughout the Term, Tenant shall maintain the following insurance policies: (i) commercial general liability insurance in amounts of $1,000,000 per occurrence, and $2,000,000 in the aggregate or, following the expiration of the initial Term, such other amounts as Landlord may from time to time reasonably require (and, if the use and occupancy of the Premises include any activity or matter that is or may be excluded from coverage under a commercial general liability policy [e.g., the sale, service or consumption of alcoholic beverages], Tenant shall obtain such endorsements to the commercial general liability policy or otherwise obtain insurance to insure all liability arising from such activity or matter [including liquor liability, if applicable] in such amounts as Landlord may reasonably require), insuring Tenant, Landlord, Landlord's property management company, Landlord's asset management company and, if requested in writing by Landlord, Landlord's Mortgagee, against all liability for injury to or death of a person or persons or damage to property arising from the use and occupancy of the Premises and (without implying any consent by Landlord to the installation thereof) the installation, operation, maintenance, repair or removal of Tenant's Off-Premises Equipment, (ii) insurance covering the full value of all alterations and improvements and betterments in the Premises, naming Landlord and Landlord's Mortgagee as additional loss payees as their interests may appear, (iii) insurance covering the full value of all furniture, trade fixtures and personal property (including property of Tenant or others) in the Premises or otherwise placed in the Building by or on behalf of Tenant (including Tenant's Off-Premises Equipment), (iv) contractual liability insurance sufficient to cover Tenant's indemnity obligations hereunder (but only if such contractual liability insurance is not already included in Tenant's commercial general liability insurance policy), and (v) worker's compensation insurance. Any insurance required to be maintained by Tenant may be taken out under a blanket insurance policy or policies covering other premises, property or insured in addition to the Premises and Tenant, provided such policy or policies otherwise comply with this Section 1l(a). Tenant's insurance shall provide primary coverage to Landlord when any policy issued to Landlord provides duplicate or similar coverage, and in such circumstance Landlord's policy will be excess over Tenant's policy. Tenant shall furnish to Landlord certificates of such insurance and, if requested by Landlord, copies of the actual insurance policies at least ten days prior to the earlier of the Commencement Date or the date Tenant enters or occupies the Premises, and at least 15 days prior to each renewal of said insurance, and Tenant shall obtain a written obligation on the part of each insurance company to notify Landlord at least 15 days before cancellation or a material change of any such insurance policies. All such insurance policies shall be in form, and issued by companies with a Best's rating of A+:VII or better, reasonably satisfactory to Landlord. If Tenant fails to comply with the foregoing insurance requirements or to deliver to Landlord the certificates or evidence of coverage required herein, Landlord, in addition to any other remedy available pursuant to this Lease or otherwise, may, but shall not be obligated to, obtain such insurance and Tenant shall pay to Landlord on demand the premium costs thereof, plus an administrative fee of 15% of such cost. As used hereunder, the term **"Tenant's Off-Premises Equipment"** means any of Tenant's equipment or other property that may be located on or about the Building (other than inside the Premises). As used hereunder, the term **"Tenant Party"** means any of the following persons: Tenant; any assignees claiming by, through, or under Tenant; any subtenants claiming by, through, or under Tenant; and any of their respective agents, contractors, employees and licensees.

(b) **Landlord's Insurance**. Throughout the Term of this Lease, Landlord shall maintain, as a minimum, the following insurance policies: (1) property insurance for the Building's replacement value (excluding property

required to be insured by Tenant), and (2) commercial general liability insurance in an amount of not less than $1,000,000 per occurrence, $2,000,000 in the aggregate.

(c) **Waiver of Negligence Claims; No Subrogation**. Landlord and Tenant each waives any claim it might have against the other for any damage to or theft, destruction, loss, or loss of use of any property, to the extent the same is insured against under any insurance policy of Landlord or Tenant that covers the Building, the Premises, Landlord's or Tenant's fixtures, personal property, leasehold improvements, or business, or is required to be insured against under the terms hereof, **REGARDLESS OF WHETHER THE NEGLIGENCE OF THE OTHER PARTY CAUSED SUCH LOSS (DEFINED BELOW)**. Additionally, Tenant waives any claim it may have against Landlord for any Loss to the extent such Loss is caused by a terrorist act. Each party shall cause its insurance carrier to endorse

all applicable policies waiving the carrier's rights of recovery under subrogation or otherwise against the other party. Notwithstanding any provision in this Lease to the contrary, Landlord, its agents, employees and contractors shall not be liable to Tenant or to any party claiming by, through or under Tenant for (and Tenant hereby releases Landlord and its servants, agents, contractors, employees and invitees from any claim or responsibility for) any damage to or destruction, loss, or loss of use, or theft of any property of any Tenant Party located in or about the Building, caused by casualty, theft, fire, third parties or any other matter or cause, **REGARDLESS OF WHETHER THE NEGLIGENCE OF ANY PARTY CAUSED SUCH LOSS IN WHOLE OR IN PART**. Tenant acknowledges that Landlord shall not carry insurance on, and shall not be responsible for damage to, any property of any Tenant Party located in or about the Building.

(d) **Indemnity**. Subject to Section 1l(c), Tenant shall defend, indemnify, and hold harmless Landlord and its representatives and agents from and against all claims, demands, liabilities, causes of action, suits, judgments, damages, and expenses (including reasonable attorneys' fees) arising from any injury to or death of any person or the damage to or theft, destruction, loss, or loss of use of, any property or inconvenience (a **"Loss"**) (1) occurring in or on the Building (other than within the Premises) to the extent caused by the negligence or willful misconduct of any Tenant Party, (2) occurring in the Premises, or (3) arising out of the installation, operation, maintenance, repair or removal of any property of any Tenant Party located in or about the Building, including Tenant's Off-Premises Equipment. **IT BEING AGREED THAT CLAUSES (2) AND (3) OF THIS INDEMNITY ARE INTENDED TO INDEMNIFY LANDLORD AND ITS AGENTS AGAINST THE CONSEQUENCES OF THEIR OWN NEGLIGENCE OR FAULT, EVEN WHEN LANDLORD OR ITS AGENTS ARE JOINTLY, COMPARATIVELY, CONTRIBUTIVELY, OR CONCURRENTLY NEGLIGENT WITH TENANT, AND EVEN THOUGH ANY SUCH CLAIM, CAUSE OF ACTION OR SUIT IS BASED UPON OR ALLEGED TO BE BASED UPON THE STRICT LIABILITY OF LANDLORD OR ITS AGENTS; HOWEVER, SUCH INDEMNITY SHALL NOT APPLY TO THE SOLE OR GROSS NEGLIGENCE OR WILLFUL MISCONDUCT OF LANDLORD AND ITS AGENTS.**

Subject to Section 11(c), Landlord shall defend, indemnify, and hold harmless Tenant and its agents from and against all claims, demands, liabilities, causes of action, suits, judgments, damages and expenses (including reasonable attorneys' fees) for any Loss arising from any occurrence in or on the Common Areas to the extent caused by the negligence or willful misconduct of Landlord or its agents.

The indemnities set forth in this Lease shall survive termination or expiration of this Lease and shall not terminate or be waived, diminished or affected in any manner by any abatement or apportionment of Rent under any provision of this Lease. If any proceeding is filed for which indemnity is required hereunder, the indemnifying party agrees, upon request therefor, to defend the indemnified party in such proceeding at its sole cost utilizing counsel satisfactory to the indemnified party.

SUBORDINATION ATTORNMENT; NOTICE TO LANDLORD'S MORTGAGEE

12. (a) **Subordination**. This Lease shall be, and is hereby made subordinate to, and Tenant accepts this Lease subject and subordinate to any deed of trust, mortgage, or other security instrument (a **"Mortgage"**), or any ground lease, master lease, or primary lease (a **"Primary Lease"**) that may presently or hereafter covers all or any part of the Premises (the mortgagee under any Mortgage or the lessor under any Primary Lease is referred to herein as **"Landlord's Mortgagee"**). The provisions of this Section 12(a) shall be self-operative without the necessity of any further instrument of subordination to be executed by Tenant, provided however, that Tenant covenants and agrees to execute and deliver to Landlord a subordination non-disturbance and attornment agreement (**"SNDA"**) substantially in the form of Exhibit G or such other form of SNDA as may be from time to time reasonably requested by a Landlord's Mortgagee within ten (10) days after requested. In the event that Tenant shall fail to execute any such instrument within ten (10) days after requested, then Tenant hereby irrevocably consents and agrees that Landlord may file of record in the Real Property Records of the county in which the Premises is situated an affidavit attaching true and correct copies of this Section 12(a), together with the signature pages hereto and a copy of Exhibit G hereto completed in favor of Landlord's Mortgagee.

(b) **Attornment**. Tenant shall attorn to any party succeeding to Landlord's interest in the

Premises, whether by purchase, foreclosure, deed in lieu of foreclosure, power of sale, termination of lease, or otherwise, upon such party's request, and shall execute such agreements confirming such attornment as such parry

may reasonably request. The current Landlord's Mortagee is Bank of Texas, N.A., whose address is set forth on Exhibit G hereto.

(c) **Notice to Landlord's Mortgagee**. Tenant shall not seek to enforce any remedy it may have for any default on the part of the Landlord without first giving written notice by certified mail, return receipt requested, specifying the default in reasonable detail, to any Landlord's Mortgagee whose address has been given to Tenant, and affording such Landlord's Mortgagee a reasonable opportunity to perform Landlord's obligations hereunder.

(d) **Subordination, Non-Disturbance and Attornment Agreement**. Landlord shall obtain a subordination, non-disturbance and attornment agreement from the current Landlord's Mortgagee in the form of Exhibit G hereto or as otherwise reasonably agreed to by Landlord's Mortgagee, and shall deliver same to Tenant contemporaneously with Landlord's execution of this Lease, and Landlord shall seek to obtain a similar subordination, non-disturbance and attornment agreement from any future Landlord's Mortgagee or other institutional lenders. The subordination of Tenant's rights hereunder to any future Landlord's Mortgagee under Section 12(a) shall be conditioned upon such future Landlord's Mortgagee's execution and delivery of a subordination, non-disturbance and attornment agreement in the form of Exhibit G hereto or another form reasonably acceptable to Tenant and such Landlord's Mortgagee or other institutional lenders.

RULES AND REGULATIONS

13. Tenant shall comply with the rules and regulations of the Building which are attached hereto as Exhibit B. Landlord may, from time to time, change such rules and regulations for the safety, care, or cleanliness of the Building and related facilities, provided that such changes are applicable to all tenants of the Building and will not unreasonably interfere with Tenant's use of the Premises. Tenant shall be responsible for the compliance with such rules and regulations by its employees, agents, and invitees.

CONDEMNATION

14. (a) **Taking - Termination**. If the entire Building or Premises are taken by right of eminent domain or conveyed in lieu thereof (a **"Taking"**), this Lease shall terminate as of the date of the Taking.

(b) **Partial Taking - Tenant's Rights**. If any part of the Premises or material portion of the Building becomes subject to a Taking and such Taking will prevent Tenant from conducting on a permanent basis its business in the Premises in a manner reasonably comparable to that conducted immediately before such Taking, then Tenant may terminate this Lease as of the date of such Taking by giving written notice to Landlord within thirty (30) days after the Taking, and Rent shall be apportioned as of the date of such Taking. If Tenant does not terminate this Lease, then Rent shall be abated on a reasonable basis as to that portion of the Premises that Tenant is prevented from conducting its business in a manner comparable to that conducted immediately before such taking.

(c) **Partial Taking - Landlord's Rights**. If any material portion, but less than all, of the Building becomes subject to a Taking, or if Landlord is required to pay any of the proceeds arising from a Taking to a Landlord's Mortgagee, then Landlord may terminate this Lease by delivering written notice thereof to Tenant within thirty (30) days after such Taking, and Rent shall be apportioned as of the date of such Taking. If Landlord does not so terminate this Lease, then this Lease will continue, but if any portion of the Premises has been taken, Rent shall abate as provided in the last sentence of Section 14(b).

(d) **Temporary Taking**. If all or any portion of the Premises becomes subject to a Taking for a limited period of time, this Lease shall remain in full force and effect and Tenant shall continue to perform all of the terms, conditions and covenants of this Lease, including the payment of Basic Rental and all other amounts required hereunder. If any such temporary Taking terminates prior to the expiration of the Term, Tenant shall restore the Premises as nearly as possible to the condition prior to such temporary Taking, at Tenant's sole cost and expense. Landlord shall be entitled to receive the entire award for any such temporary Taking, except that Tenant shall be entitled to receive the portion of such award which (1) compensates Tenant for its loss of use of the Premises within the Term and (2) reimburses Tenant for

the reasonable out-of-pocket costs actually incurred by Tenant to restore the Premises as required by this Section 14(d).

(e) **Award**. If any Taking occurs, then Landlord shall receive the entire award or other compensation for the Land, the Building, and other improvements taken; however, Tenant may separately pursue a claim (to the extent it will not reduce Landlord's award) against the condemnor for the value of Tenant's personal property which Tenant is entitled to remove under this Lease, moving costs, loss of business, and other claims it may have.

(f) **Restoration**. In the event of any Taking of less than the whole of the Premises which does not result in a termination of this Lease, (1) Landlord, at its expense, shall proceed with reasonable diligence to repair, alter and restore the remaining parts of the affected Building and the Premises therein to the extent practicable, and (2) if requested by either party, Landlord and Tenant shall promptly execute an amendment to this Lease confirming the deletion from the Premises of the space subject to the Taking.

FIRE OR OTHER CASUALTY

15. (a) **Repair Estimate**. If the Premises or the Building are damaged by fire or other casualty (a **"Casualty"**), Landlord shall, within sixty (60) days after such Casualty, deliver to Tenant a good faith estimate (the **"Damage Notice"**) of the time needed to repair the damage caused by such Casualty.

(b) **Tenant's Rights**: If a material portion of the Premises is damaged by Casualty such that Tenant is prevented from conducting its business in the Premises in a manner reasonably comparable to that conducted immediately before such Casualty and Landlord estimates that the damage caused thereby cannot be repaired within

two hundred ten (210) days after the commencement of repairs (the **"Repair Period"**), then Tenant may terminate this Lease by delivering written notice to Landlord of its election to terminate within thirty (30) days after the Damage Notice has been delivered to Tenant.

(c) **Landlord's Rights**. If a Casualty damages the Premises or a material portion of the Building and (1) Landlord estimates that the damage to the Premises cannot be repaired within the Repair Period, (2) the damage to the Premises exceeds 50% of the replacement cost thereof (excluding foundations and footings), as estimated by Landlord, and such damage occurs during the last two years of the Term, and Tenant does not exercise its next unexercised renewal option (if any) by written notice to Landlord within fifteen (15) days after the Damage Notice has been delivered to Tenant, (3) regardless of the extent of damage to the Premises, the damage is not fully covered by Landlord's insurance policies or Landlord makes a good faith determination that restoring the Building would be uneconomical, or (4) Landlord is required to pay any insurance proceeds arising out of the Casualty to a Landlord's Mortgagee, then Landlord may terminate this Lease (provided Landlord also terminates all leases for space in the Building that is similarly impacted by such Casualty) by giving written notice of its election to terminate within thirty (30) days after the Damage Notice has been delivered to Tenant.

(d) **Repair Obligation**. If neither party elects to terminate this Lease following a Casualty, then Landlord shall, within a reasonable time after such Casualty, begin to repair the Premises and shall proceed with reasonable diligence to restore the Premises to substantially the same condition as they existed immediately before such Casualty; however, Landlord shall not be required to repair or replace any alterations or betterments within the Premises (which shall be promptly and with due diligence repaired and restored by Tenant at Tenant's sole cost and expense) or any furniture, equipment, trade fixtures or personal property of Tenant or others in the Premises or the Building and Landlord's obligation to repair or restore the Premises shall be limited to the extent of the insurance proceeds actually received by Landlord for the Casualty in question or proceeds that would have been received had Landlord maintained the insurance required of Landlord under this Lease, and regardless of the cause of such Casualty, together with any deductible amounts. If this Lease is terminated under the provisions of this Section 15, Landlord shall be entitled to the full proceeds of the insurance policies providing coverage for all alterations, improvements and betterments in the Premises (and, if Tenant has failed to maintain insurance on such items as required by this Lease, Tenant shall pay Landlord an amount equal to the proceeds Landlord would have received had Tenant maintained insurance on such items as required by this Lease). If Landlord does not complete the restoration of the Premises within ninety (90) days after the time period

estimated by Landlord to repair the damage caused by such Casualty as specified in the Damage Notice, as the same may be extended by force majeure, Tenant may terminate this Lease by delivering written notice to Landlord and Landlord's Mortgagee within ten days following the expiration of such ninety (90)-day period (as the same may be extended as set forth above) and prior to the date upon which Landlord substantially completes such restoration. Such termination shall be effective as of the date specified in Tenant's termination notice (but not earlier than 30 days nor later than 90 days after the date of such notice) as if such date were the date fixed for the expiration of the Term.

(e) **Abatement of Rent**. If the Premises are damaged by Casualty, Rent for the portion of the Premises that Tenant is prevented from conducting its business in a manner comparable to that conducted immediately before such Casualty shall be abated on a reasonable basis from the date of damage until the completion of Landlord's repairs (or until the date of termination of this Lease by Landlord or Tenant as provided above, as the case may be).

TAXES

16. Tenant shall be liable for all taxes levied or assessed against personal property, furniture, or fixtures placed by Tenant in the Premises. If any taxes for which Tenant is liable are levied or assessed against Landlord or Landlord's property and Landlord elects to pay the same, or if the assessed value of Landlord's property is increased by inclusion of such personal property, furniture or fixtures and Landlord elects to pay the taxes based on such increase, then Tenant shall pay to Landlord, upon demand, that part of such taxes for which Tenant is primarily liable hereunder. Tenant has no right to protest the real estate tax rate assessed against the Building or Land and/or the appraised value of the Building or Land determined by any appraisal review board or other taxing entity with authority to determine tax rates and/or appraised values (each a "Taxing Authority"). Tenant hereby knowingly, voluntarily and intentionally waives and releases any right, whether created by law or otherwise, to (a) file or otherwise protest before any Taxing Authority any such rate or value determination even though Landlord may elect not to file any such protest; (b) receive, or otherwise require Landlord to deliver, a copy of any reappraisal notice received by Landlord from any Taxing Authority; and (c) appeal any order of a Taxing Authority which determines any such protest. The foregoing waiver and release covers and includes any and all rights, remedies and recourse of Tenant, now or at any time hereafter, under Section 41.413 and Section 42.015 of the Texas Tax Code (as currently enacted or hereafter modified) together with any other or further laws, rules or regulations covering the subject matter thereof. Tenant acknowledges and agrees that the foregoing waiver and release was bargained for by Landlord and Landlord would not have agreed to enter into this Lease in the absence of this waiver and release.

EVENTS OF DEFAULT

17. Each of the following occurrences shall constitute an **"Event of Default":**

(a) Tenant's failure to pay Rent when due and the continuance of such failure for a period of ten (10) days after Landlord has delivered written notice to Tenant that the same is past due;

(b) Tenant's failure to perform, comply with, or observe any other agreement or obligation of Tenant under this Lease and the continuance of such failure for a period of thirty (30) days after the date Landlord delivers to Tenant written notice thereof; however, if such failure cannot be cured with such 30-day period and Tenant commences to cure such failure within such 30-day period and thereafter diligently pursues such cure to completion,

then such failure shall not be an Event of Default, unless it is not fully cured within a reasonable time but in no event later than 150 days following receipt of written notice from Landlord of such failure;

(c) the filing of a petition by or against Tenant (the term "Tenant" shall include, for the purpose of this Section 17(c), any guarantor of the Tenant's obligations hereunder) (1) in any bankruptcy or other insolvency proceeding; (2) seeking any relief under any state or federal debtor relief law; or (3) for the appointment of a liquidator or receiver for all or substantially all of Tenant's property or for Tenant's interest in this Lease; and

(d) [Intentionally Omitted];

(e) the admission in writing by Tenant that it cannot meet its obligations as they become due or the making by Tenant of an assignment for the benefit of its creditors.

REMEDIES

18. Upon any Event of Default, Landlord may, in addition to all other rights and remedies afforded Landlord hereunder or by law or equity, take any of the following actions:

(a) Landlord may terminate this Lease by giving Tenant written notice thereof in which event, Tenant shall pay to Landlord the sum of (i) all Rent accrued hereunder through the date of termination, (ii) all amounts due under Section 19(a), and (iii) an amount equal to (A) the total Rent that Tenant would have been required to pay for the remainder of the Term discounted to present value at a per annum rate equal to the "Prime Rate" as published on the date this Lease is terminated by The Wall Street Journal, Southwest Edition, in its listing of "Money Rates" minus three percent, minus (B) the then present fair rental value of the Premises for such period, similarly discounted; or

(b) Landlord may terminate Tenant's right to possession of the Premises without terminating this Lease by giving written notice thereof to Tenant, in which event Tenant shall pay to Landlord (i) all Rent and other amounts accrued hereunder to the date of termination of possession, (ii) all amounts due from time to time under Section 19(a), and (iii) all Rent and other sums required hereunder to be paid by Tenant during the remainder of the Term, diminished by any net sums thereafter received by Landlord through reletting the Premises during such period. Landlord shall use reasonable efforts to relet the Premises on such terms and conditions as Landlord in its sole discretion may determine (including a term different from the Term, rental concessions, and alterations to, and improvement of, the Premises); however, Landlord shall not be obligated to relet the Premises before leasing other portions of the Building. Landlord shall not be liable for, nor shall Tenant's obligations hereunder be diminished because of, Landlord's failure to relet the Premises or to collect rent due for such reletting. Tenant shall not be entitled to the excess of any consideration obtained by reletting over the Rent due hereunder. Reentry by Landlord in the Premises shall not affect Tenant's obligations hereunder for the unexpired Term; rather, Landlord may, from time to time, bring action against Tenant to collect amounts due by Tenant, without the necessity of Landlord's waiting until the expiration of the Term. Unless Landlord delivers written notice to Tenant expressly stating that it has elected to terminate this Lease, all actions taken by Landlord to exclude or dispossess Tenant of the Premises shall be deemed to he taken under this Section 18(b). If Landlord elects to proceed under this Section 18(b), it may at any time elect to terminate this Lease under Section 18(a).

ADDITIONALLY, TO THE EXTENT PERMITTED BY APPLICABLE LAW, LANDLORD MAY ALTER LOCKS OR OTHER SECURITY DEVICES AT THE PREMISES TO DEPRIVE TENANT OF ACCESS THERETO; AND EXCEPT AS OTHERWISE PROVIDED BY APPLICABLE LAW, LANDLORD SHALL NOT BE REQUIRED TO PROVIDE A NEW KEY OR RIGHT OF ACCESS TO TENANT UNLESS AND UNTIL THE EVENT OF DEFAULT HAS BEEN CURED.

PAYMENT BY TENANT; NON-WAIVER

19. (a) **Payment by Tenant**. Upon any Event of Default, Tenant shall pay to Landlord all reasonable costs incurred by Landlord (including court costs and reasonable attorneys' fees and expenses) in (i) obtaining possession of the Premises, (ii) removing and storing Tenant's or any other occupant's property, (iii) repairing, restoring, altering, remodeling, or otherwise putting the Premises into the condition required by market conditions then prevailing so as to be reasonably acceptable to a new tenant, (iv) if Tenant is dispossessed of the Premises and this Lease is not terminated, reletting all or any part of the Premises (including brokerage commissions, cost of tenant finish work, and other costs incidental to such reletting), (v) performing Tenant's obligations which Tenant failed to perform, and (vi) enforcing, or advising Landlord of, its rights, remedies, and recourses arising out of the Event of Default. Tenant's obligations under this Section 19 shall survive the expiration of the Term or earlier termination of this Lease.

(b) **No Waiver**. Landlord's acceptance of Rent following an Event of Default shall not waive Landlord's rights regarding such Event of Default. No waiver by Landlord of any violation or breach of

any of the terms contained herein shall waive Landlord's rights regarding any future violation of such term or violation of any other term.

COMMON AREA

20. **"Common Area"** as used herein stall refer to that part of the Building and other improvements now or hereafter placed, constructed or erected on the Land designated by Landlord from time to time for the common use of all tenants, including among other facilities, sidewalks, service corridors, curbs, truckways, loading areas, private streets and alleys, lighting facilities, mechanical and electrical rooms, janitors' closets, halls, lobbies, delivery passages, elevators, drinking fountains, meeting rooms, public toilets, parking areas and garages, decks and other parking

facilities, landscaping and other common rooms and common facilities. The Common Area shall be subject to Landlord's sole management and control and shall be operated and maintained in a manner consistent with similar buildings in the market in which the Building is located. Landlord reserves the right to change from time to time the dimensions and location of the Common Area, to construct additional stories on the Building and to place, construct or erect new structures or other improvements on any part of the Land without the consent of Tenant. Tenant, and Tenant's employees and invitees shall have the nonexclusive right to use the Common Area as constituted from time to time, such use to be in common with Landlord, other tenants of the Building and other persons entitled to use the same, and subject to such reasonable rules and regulations governing use as Landlord may from time to time prescribe. Tenant shall not solicit business or display merchandise within the Common Area, or distribute handbills therein, or take any action which would interfere with the rights of other persons to use the Common Area. Landlord may temporarily close any part of the Common Area for such periods of time as may be reasonably necessary to prevent the public from obtaining prescriptive rights or to make repairs or alterations, provided Tenant retains reasonable access to the Premises.

SURRENDER OF PREMISES

21. No act by Landlord shall be deemed an acceptance of a surrender of the Premises, and no agreement to accept a surrender of the Premises shall be valid unless the same is made in writing and signed by Landlord. At the expiration or termination of this Lease, Tenant shall deliver to Landlord the Premises with all improvements located thereon in good repair and condition, reasonable wear and tear (and condemnation and fire or other casualty damage) excepted, and shall deliver to Landlord all keys to the Premises. Tenant may remove all unattached trade fixtures, furniture owned by it, equipment and personal property placed in the Premises by Tenant (but Tenant shall not remove any such item which was paid for, in whole or in part, by Landlord, as part of the Finish Work Allowance or otherwise).

Subject to Section 8(a)(2) of this Lease, all alterations, additions or improvements made in or upon the Premises shall, at Landlord's option, (to be exercised pursuant to following sentence), either be removed by Tenant prior to the end of the Term (and Tenant shall repair all damage caused thereby), or shall remain in the Premises at the end of the Term without compensation to Tenant. In connection with Landlord's review and approval of any of Tenant's proposed alterations, additions or improvements to the Premises, Landlord may notify Tenant in writing, contemporaneously with Landlord's notice of approval to Tenant with respect to the improvements in question, that Landlord will require Tenant to remove such alterations prior to the expiration of the Term; however, if Tenant submits plans and specifications to Landlord for proposed alterations, additions or improvements to the Premises and delivers a Removal Notice (defined below) to Landlord contemporaneously with such submission by Tenant, and Landlord fails to notify Tenant that Tenant will be required to remove such alterations, additions or improvements to the Premises at the expiration of the Term, Landlord may not request such removal at the expiration of the Term. A **"Removal Notice"** means a written notice from Tenant to Landlord that conspicuously states in bold, uppercase typeface that Tenant will not be required to remove the alterations, additions or improvements in question at the end of the Term unless, contemporaneously with Landlord's notice of approval to Tenant with respect to the improvements in question, Landlord notifies Tenant in writing that Landlord will require Tenant to remove such alterations prior to the expiration of the Term. Notwithstanding the foregoing, if Tenant does not obtain Landlord's prior written consent for any alterations, additions or improvements to the Premises (whether such approval is required hereunder or otherwise), Tenant shall, at Landlord's written request, remove all such alterations, additions, improvements, trade fixtures, equipment, wiring, and furniture as Landlord may request; however, Tenant shall not be required to remove any addition or improvement to the Premises if Landlord has specifically agreed in writing that the

improvement or addition in question need not be removed. Tenant shall repair all damage caused by such removal. All of the office furniture and equipment and all other items not so removed shall be deemed to have been abandoned by Tenant and may be appropriated, sold, stored, destroyed, or otherwise disposed of by Landlord without notice to Tenant and without any obligation to account for such items. Notwithstanding the foregoing, Landlord acknowledges that Landlord will not require the removal of the initial tenant improvement work performed by Tenant (as described in Section 3 of Exhibit D hereto) at the expiration of the Term. The provisions of this Section 21 shall survive the end of the Term or the earlier termination of this Lease.

HOLDING OVER

22. If Tenant fails to vacate me Premises at the end of the Term or upon the earlier termination of this Lease, then Tenant shall be a month-to-month tenant and Tenant shall pay, in addition to the other Rent, a daily Basic Rental equal to 150% of the daily Basic Rental payable during the last month of the Term. The provisions of this Section 22 shall survive the end of the Term or the earlier termination of this Lease.

CERTAIN RIGHTS RESERVED BY LANDLORD

23. Provided that the exercise of such rights does not unreasonably interfere with Tenant's permitted use and occupancy of the Premises, Landlord, its agents, employees, and contractors shall have the following rights:

(i) to decorate or to make inspections, repairs, alterations, additions, changes, or improvements, whether structural or otherwise, in and about the Building, or any part thereof as Landlord may deem necessary or desirable; for such purposes, to enter upon the Premises (after 24 hours' advance written notice to Tenant thereof) and, during the continuance of any such work, to temporarily close doors, entryways, public space, and corridors in the Building; to interrupt or temporarily suspend Building services and facilities; and to change the arrangement and location of entrances or passageways, doors, and doorways, corridors, elevators, stairs, restrooms, or other public parts of the Building;

(ii) to take such reasonable measures as Landlord deems advisable for the security of the Building and its occupants, including without limitation searching all persons entering or leaving the Building and requiring that persons entering or leaving the Building, whether or not during normal business hours, identify themselves to a

security officer by registration or otherwise and that such persons establish their right to enter or leave the Building; evacuating the Building for cause, suspected cause, or for drill purposes; temporarily denying access to the Building;

(iii) to change the name by which the Building is designated, provided that Landlord reimburses Tenant the actual costs of changing Tenant's stationery (including letterhead, business cards, envelopes and the like) on hand at the time of such name change; and

(iv) to enter the Premises (other than the raised floor area in the server room or the first floor of the Premises) at all reasonable hours, upon 24 hours advance written notice, to show the Premises to prospective purchasers or lenders, or, during the last 12 months of the Term, to prospective tenants; and

(v) to have access to and the right to enter upon any and all parts of the Premises with 24 hours advance written notice (except in cases of emergency, defined to be any situation in which Landlord perceives imminent danger of injury to person and/or damage to or loss of property, in which case Landlord may enter upon any and all parts of the Premises at any time) to examine the condition thereof, to clean, to make any repairs, alterations or additions required to be made by Landlord hereunder, and for any other purpose deemed reasonably by Landlord, and Tenant shall not be entitled to any abatement or reduction of rental by reason thereof.

LANDLORD'S LIEN

24. **Waiver of Landlord's Lien**. Landlord waives all contractual, statutory and constitutional liens held by Landlord on Tenant's personal property, goods, equipment, inventory, furnishings, chattels, accounts and assets to secure the obligations of Tenant under this Lease.

HAZARDOUS

25. (a) **Hazardous Substances**. The term **"Hazardous Substances,"** as used in this Lease, shall include, without limitation, flammables, explosives, radioactive materials, asbestos, polychlorinated

SUBSTANCES

biphenyls (**PCB's**), chemicals known to cause cancer or reproductive toxicity, pollutants, contaminants, hazardous wastes, toxic substances or related materials, petroleum and petroleum products, and substances declared to be hazardous or toxic under any law or regulation now or hereafter enacted or promulgated by any governmental authority. To the best of Landlord's knowledge, the Building does not contain any Hazardous Substances, other than as may have been previously disclosed to Tenant in writing.

(b) **Tenant's Restrictions**. Tenant shall not cause to occur (i) any violation of any federal, state, or local law, ordinance, or regulation now or hereafter enacted, without limitation, related to environmental conditions on, under, or about the Premises, or arising from Tenant's release of Hazardous Substances, including, but not limited to, soil and ground water conditions; or (ii) the use, generation, release, manufacture, refining, production, processing, storage, or disposal of any Hazardous Substance on, under, or about the Premises, or the transportation to or from the Premises of any Hazardous Substance, except for normal cleaning and office supplies in reasonable quantities.

(c) **Environmental Clean-up**. Tenant shall, at Tenant's own expense, comply with all laws regulating the use, generation, storage, transportation, or disposal of Hazardous Substances (the **"Laws"**) by Tenant and or its agents, employees or contractors within or respecting the Premises. Except as expressly provided in the immediately preceding sentence, Landlord shall make all submissions to, provide all information required by, and comply with, all requirements of all governmental authorities (the **"Authorities"**) under the Laws relating to the Premises. Should any authority or any third party demand that a clean-up plan be prepared and that a clean-up be undertaken because of any deposit, spill, discharge, or other release of Hazardous Substances by Tenant or its employees that occurs during the Term, at or from the Premises, then Tenant shall, at Tenant's own expense, prepare and submit the required plans and all related bonds and other financial assurances, and Tenant shall carry out such clean-up plan; otherwise, Landlord shall be responsible for any clean-up within the Building. Tenant shall promptly provide all information regarding the use, generation, storage, transportation, or disposal by Tenant of Hazardous Substances that is requested by Landlord. If Tenant fails to fulfill any duty imposed under this Section 25 within a reasonable time, Landlord may do so; and in such case, Tenant shall cooperate with Landlord in order to prepare all documents Landlord deems necessary or appropriate to determine the applicability of the Laws to the Premises and Tenant's use thereof, and for compliance therewith, and Tenant shall execute all documents upon Landlord's request. No such action by Landlord and no attempt made by Landlord to mitigate damages under any Law shall constitute a waiver of any of Tenant's obligations under this Section 25. The obligations and liabilities under this Section 25 shall survive the expiration of the Term or earlier termination of this Lease.

(d) **Tenant's Indemnity**. Tenant shall indemnify, defend, and save and hold harmless Landlord, the manager of the Building, and their respective officers, directors, beneficiaries, shareholders, partners, agents and employees from all fines, suits, procedures, claims, and actions of every kind, and all costs associated therewith (including attorneys' fees and expenses and consulting fees and expenses) arising out of or in any way connected with any deposit, spill, discharge, or other release of Hazardous Substances by Tenant or its employees or contractors that occurs during the Term, at or from the Premises, or which arises at any time during the Term from Tenant's use or occupancy of the Premises. Tenant's obligations and liabilities under this Section 25 shall survive the expiration of the Term or earlier termination of this Lease.

ESA. Landlord has previously delivered and Tenant hereby acknowledges receipt of the Property Site Assessment for the Building and the Land dated May 28, 2004 (File Number E2472) and prepared for Landlord by Pinnacle Environmental. Landlord represents and warrants, to its knowledge, there are no Hazardous Substances in, on or affecting the Building or the Premises, other than as may be reflected therein, if any. Landlord shall indemnify, defend, and save and hold harmless Tenant and its officers, directors, beneficiaries, shareholders, partners, agents and employees from all fines, suits, procedures, claims, and actions of every kind, and all costs associated therewith

(including attorneys' fees and expenses and consulting fees and expenses) arising out of or in any way connected with Landlord's breach of its representation set forth in the preceding sentence.

PARKING

26. Tenant shall have the right to use parking spaces as provided in Exhibit E.

MISCELLANEOUS

27. (a) **Landlord Transfer**. Landlord may transfer, in whole or in part, the Building and any of its rights under this Lease. If Landlord assigns its rights under this Lease, then, upon the transferee's written assumption of Landlord's obligations under this Lease, Landlord shall thereby be released from any further obligations hereunder.

(b) **Landlord's Liability**. The liability of Landlord (and its partners, shareholders or members) to Tenant (or any person or entity claiming by, through or under Tenant) for any default by Landlord under the terms of this Lease or any matter relating to or arising out of the occupancy or use of the Premises and/or other areas of the Building shall be limited to Tenant's actual direct, but not consequential, damages therefor and shall be recoverable only from the interest of Landlord in the Building, net proceeds derived from the sale thereof, and to the extent actually received by Landlord (thus excluding amounts paid to Landlord's Mortgagees) insurance proceeds and condemnation awards, and Landlord (and its partners, shareholders or members) shall not be personally liable for any deficiency. The provisions of this Section shall survive any expiration or termination of this Lease. Additionally, Tenant hereby waives its statutory lien under Section 91.004 of the Texas Property Code. Notwithstanding the foregoing, this section shall not be deemed to limit any remedies which Tenant may have in the event of default by Landlord of its indemnity obligations hereunder.

(c) **Tenant's Liability**. The liability of Tenant to Landlord for any monetary damages arising from any default by Tenant under the terms of this Lease shall be limited to Landlord's actual direct, but not consequential damages therefor. Nothing in this Section 27(c) shall affect or limit Landlord's rights to file legal actions to recover possession of the Premises; or for injunctive relief against Tenant, or any other non-monetary relief as provided in Sections 18 or 19 of this Lease.

(d) **Force Majeure**. Other than for Tenant's monetary obligations under this Lease and obligations which can be cured by the payment of money (e.g., maintaining insurance), whenever a period of time is herein prescribed for action to be taken by either party hereto, such party shall not be liable or responsible for, and there shall be excluded from the computation for any such period of time, any delays due to strikes, riots, acts of God, shortages of labor or materials, war, governmental laws, regulations, or restrictions, or any other causes of any kind whatsoever which are beyond the control of such party.

(e) **Brokerage**. Landlord and Tenant each warrant to the other that it has not dealt with any broker or agent in connection with the negotiation or execution of this Lease, other than Stream Realty Partners, L.P. and Cushman & Wakefield of Texas, Inc., (collectively **"Broker"**) whose commissions shall be paid by Landlord pursuant to separate written agreements. Tenant and Landlord shall each defend, indemnify, hold the other harmless against all costs, expenses, attorneys' fees, and other Liability for commissions or other compensation claimed by any broker or agent, other than Broker, claiming the same by, through, or under the indemnifying party.

(f) **Estoppel Certificates**. From time to time, either party shall furnish to any party designated by the non-requesting parry within ten (10) days after the requesting party has made a request therefor, a certificate signed by the non-requesting party confirming and containing such factual certifications and representations as to this Lease as the requesting party may reasonably request, including, but not necessarily limited to (i) that the Lease is unmodified and in full force and effect (or, if there have been modifications, that the same is in full force and effect as so modified), (ii) the dates to which rental and other charges payable under this Lease have been paid, and (iii) that the requesting party is not in default hereunder (or, if the requesting party is in default, specifying the nature of such default). Tenant further agrees that Tenant shall from time to time upon request by Landlord execute and deliver to Landlord an instrument in recordable form acknowledging Tenant's receipt of any notice of assignment of this Lease by Landlord

(g) **Notices**. All notices and other communications given pursuant to this Lease shall be in writing and shall be (i) mailed by first class, United States Mail, postage prepaid, certified, with return

receipt requested, and addressed to the parties hereto at the address specified in the Basic Lease Information, (ii) sent by a nationally recognized overnight courier service, or (iii) sent by facsimile transmission followed by a confirmatory letter sent in another method permitted hereunder. All notices shall be effective upon delivery to the address of the addressee. The parties hereto may change their addresses by giving notice thereof to the other in conformity with this provision.

(h) **Separability**. If any clause or provision of this Lease is illegal, invalid, or unenforceable under present or future laws, then the remainder of this Lease shall not be affected thereby and in lieu of such clause or provision, there shall be added as a part of this Lease a clause or provision as similar in terms to such illegal, invalid, or unenforceable clause or provision as may be possible and be legal, valid, and enforceable.

(i) **Amendments; and Binding Effect**. This Lease may not be amended except by instrument in writing signed by Landlord and Tenant. No provision of this Lease shall be deemed to have been waived by either party unless such waiver is in writing signed by such party, and no custom or practice which may evolve between the parties in the

administration of the terms hereof shall waive or diminish the right of either party to insist upon the performance by the other party in strict accordance with the terms hereof. The terms and conditions contained in this Lease shall inure to the benefit of and be binding upon the parties hereto, and upon their respective successors in interest and legal representatives, except as otherwise herein expressly provided. This Lease is for the sole benefit of Landlord and Tenant, and, other than Landlord's Mortgagee, no third party shall be deemed a third party beneficiary hereof.

(j) **Quiet Enjoyment**. Provided no Event of Default exists, Tenant shall peaceably and quietly hold and enjoy the Premises for the Term, without hindrance from Landlord or any party claiming by, through, or under Landlord, subject to the terms and conditions of this Lease.

(k) **Joint and Several Liability**. If there is more than one Tenant, then the obligations hereunder imposed upon Tenant shall be joint and several. If there is a guarantor of Tenant's obligations hereunder, then the obligations hereunder imposed upon Tenant shall be the joint and several obligations of Tenant and such guarantor, and Landlord need not first proceed against Tenant before proceeding against such guarantor nor shall any such guarantor be released from its guaranty for any reason whatsoever.

(l) **Captions**. The captions contained in this Lease are for convenience of reference only, and do not limit or enlarge the terms and conditions of this Lease.

(m) **No Merger**. There shall be no merger of the leasehold estate hereby created with the fee estate in the Premises or any part thereof if the same person acquires or holds, directly or indirectly, this Lease or any interest in this Lease and the fee estate in the leasehold Premises or any interest in such fee estate.

(n) **No Offer**. The submission of this Lease to Tenant shall not be construed as an offer, nor shall Tenant have any rights under this Lease unless and until Landlord executes a copy of this Lease and delivers it to Tenant.

(o) **Exhibits**. All exhibits and attachments attached hereto are incorporated herein by this reference.

Exhibit A-1	-	Legal Description of the Land
Exhibit A-2	-	General Depiction of the Premises – 1st Floor
Exhibit A-3	-	General Depiction of the Premises – 2nd Floor
Exhibit B	-	Building Rules and Regulations
Exhibit C	-	Operating Expense Escalator
Exhibit D	-	Special Provisions
Exhibit D-1	-	ADA Compliance Matters

Exhibit E	-	Parking
Exhibit F	-	Intentionally Deleted
Exhibit G	-	Subordination Non-Disturbance and Attornment Agreement
Exhibit H	-	Intentionally Deleted
Exhibit I	-	Janitorial Specifications

(p) **Entire Agreement**. This Lease constitutes the entire agreement between Landlord and Tenant regarding the subject matter hereof and supersedes all oral statements and prior writings relating thereto. Except for those set forth in this Lease, no representations, warranties, or agreements have been made by Landlord or Tenant to the other with respect to this Lease or the obligations of Landlord or Tenant in connection therewith.

ADDITIONAL PROVISIONS:

28. **DISCLAIMER. LANDLORD AND TENANT EXPRESSLY DISCLAIM ANY IMPLIED WARRANTY THAT THE PREMISES ARE SUITABLE FOR TENANT'S INTENDED COMMERCIAL PURPOSE. TENANT'S OBLIGATION TO PAY RENT HEREUNDER IS NOT DEPENDENT UPON THE CONDITION OF THE PREMISES OR THE PERFORMANCE BY LANDLORD OF ITS OBLIGATIONS HEREUNDER, AND, EXCEPT AS OTHERWISE EXPRESSLY PROVIDED HEREIN, TENANT SHALL CONTINUE TO PAY THE RENT, WITHOUT ABATEMENT, SETOFF OR DEDUCTION, NOTWITHSTANDING ANY BREACH BY LANDLORD OF ITS DUTIES OR OBLIGATIONS HEREUNDER, WHETHER EXPRESS OR IMPLIED. NOTHING IN THIS PARAGRAPH SHALL BE CONSTRUED TO DIMINISH THE OBLIGATIONS OF LANDLORD THAT ARE EXPRESSLY SET FORTH ELSEWHERE IN THIS LEASE.**

29. **Authority**. Tenant (if a corporation, partnership or other business entity) hereby represents and warrants to Landlord that Tenant is a duly formed and existing entity qualified to do business in the state in which the Premises are located, that Tenant has full right and authority to execute and deliver this Lease, and that each person signing on behalf of Tenant is authorized to do so. Landlord hereby represents and warrants to Tenant that Landlord is a duly formed and existing entity qualified to do business in the state in which the Premises are located, that Landlord has full right and authority to execute and deliver this Lease, and that each person signing on behalf of Landlord is authorized to do so.

30. **Telecommunications**. Tenant and its telecommunications companies, including local exchange telecommunications companies and alternative access vendor services companies, shall have no right of access to and within the Building, for the installation and operation of telecommunications systems, including voice, video, data, Internet, and any other services provided over wire, fiber optic, microwave, wireless, and any other transmission systems (**"Telecommunications Services"**), for part or all of Tenant's telecommunications within the Building and from the Building to any other location without Landlord's prior written consent, which shall not be unreasonably

withheld, conditioned or delayed. All providers of Telecommunications Services shall be required to comply with the rules and regulations of the Building, applicable Laws and Landlord's policies and practices for the Building. Tenant acknowledges that Landlord shall not be required to provide or arrange for any Telecommunications Services and that Landlord shall have no liability to any Tenant Party in connection with the installation, operation or maintenance of Telecommunications Services or any equipment or facilities relating thereto. Tenant, at its cost and for its own account, shall be solely responsible for obtaining all Telecommunications Services. However, nothing in this Section 29 shall prohibit Tenant's employees from accessing areas solely within the Premises that do not contain any equipment serving other tenants of the Building.

31. **Confidentiality**. Both Landlord and Tenant acknowledge that the terms and conditions of this Lease are to remain confidential for both parties' benefit, and may not be disclosed by either party to anyone, by any manner or means, directly or indirectly, without the other party's prior written consent; however, either party may disclose the terms and conditions of this Lease if required by Law or court order, to its attorneys, accountants, employees and existing or prospective financial partners provided same are advised by Landlord or Tenant (as the case may be) of the confidential nature of such terms and

conditions and agree to maintain the confidentiality thereof (in each case, prior to disclosure). The disclosing party shall be liable for any disclosures made in violation of this Section by the disclosing party or by any entity or individual to whom the terms and conditions of this Lease were disclosed or made available by the disclosing party. The consent by either party to any disclosures shall not be deemed to be a waiver on the part of such party of any prohibition against any future disclosure.

32. **Water Mold Notification.** To the extent Tenant or its agents or employees discover any water leakage, water damage or mold in or about the Premises or Building, Tenant shall promptly notify Landlord thereof in writing.

33. **No Recording**. Tenant shall **not** record this Lease or any memorandum of this Lease without the prior written consent of Landlord, which consent may be withheld or denied in the sole and absolute discretion of Landlord, and any recordation by Tenant stall be a material breach of this Lease. Tenant grants to Landlord a power of attorney to execute and record a release instrument releasing any such recorded instrument of record that was recorded without the prior written consent of Landlord.

34. WAIVER OF JURY TRIAL. TO THE MAXIMUM EXTENT PERMITTED BY LAW, LANDLORD AND TENANT WAIVE ANY RIGHT TO TRIAL BY JURY IN ANY LITIGATION OR TO HAVE A JURY PARTICIPATE IN RESOLVING ANY DISPUTE ARISING OUT OF OR WITH RESPECT TO THIS LEASE OR ANY OTHER INSTRUMENT, DOCUMENT OR AGREEMENT EXECUTED OR DELIVERED IN CONNECTION HEREWITH OR THE TRANSACTIONS RELATED HERETO.

35. **No Electronic Transactions**. The parties hereby acknowledge and agree this Agreement shall not be executed, entered into, altered, amended or modified by electronic means. Additionally, the parties hereby acknowledge and agree the transactions contemplated by this Agreement shall not be conducted by electronic means.

36. **Prohibited Persons and Transactions**. Landlord and Tenant each represent and warrant to the other, that it is currently in compliance with and shall at all times during the Term (including any extension thereof) remain in compliance with the regulations of the OFAC of the Department of the Treasury (including those named on OFAC's Specially Designated and Blocked Persons List) and any statute, executive order (including the September 24, 2001, Executive Order Blocking Property and Prohibiting Transactions with Persons Who Commit, Threaten to Commit or Support Terrorism), or other governmental action relating thereto.

37. **No Representations or Warranties**. Tenant acknowledges that except for any express warranties and representations contained in this Lease, Tenant is not relying on any written, oral, implied or other representations, statements or warranties by Landlord or any agent of Landlord or any real estate broker or salesman. All previous written, oral, implied or other statements, representations, warranties or agreements, if any, are merged in this Lease. Except as expressly set forth herein, Landlord shall have no liability to Tenant, and Tenant hereby **RELEASES** Landlord from any liability (including contractual and/or statutory actions for contribution or indemnity), for, concerning or regarding (1) the nature and condition of the Premises, including the suitability thereof for any activity or use; (2) any improvements or substances located thereon; or (3) the compliance of the Premises with any laws, rules, ordinances or regulations of any government or other body.

THE FOREGOING INCLUDES A RELEASE OF LANDLORD FROM CLAIMS BASED ON LANDLORD'S NEGLIGENCE IN WHOLE OR IN PART AND CLAIMS BASED ON STRICT LIABILITY. LANDLORD HAS NOT MADE, DOES NOT MAKE AND EXPRESSLY DISCLAIMS, ANY WARRANTIES, REPRESENTATIONS, COVENANTS OR GUARANTEES, EXPRESSED OR IMPLIED, OR ARISING BY OPERATION OF LAW, AS TO THE MERCHANTABILITY, HABITABILITY, QUANTITY, QUALITY OR ENVIRONMENTAL CONDITION OF THE PREMISES OR ITS SUITABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OR USE; OTHER THAN

AS EXPRESSLY PROVIDED IN THIS LEASE.

TENANT AFFIRMS THAT TENANT SHALL HAS (i) INVESTIGATED AND INSPECTED THE PREMISES TO ITS SATISFACTION AND BECOME FAMILIAR AND SATISFIED WITH THE CONDITION OF THE PREMISES, AND (ii) MADE ITS OWN DETERMINATION AS TO (a) THE MERCHANTABILITY, QUANTITY, QUALITY AND CONDITION OF THE PREMISES, INCLUDING THE POSSIBLE PRESENCE OF TOXIC OR HAZARDOUS SUBSTANCES, MATERIALS OR WASTES OR OTHER ACTUAL OR POTENTIAL ENVIRONMENTAL CONTAMINATES, AND (b) THE PREMISES' SUITABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OR USE. TENANT HEREBY ACCEPTS THE PREMISES IN ITS PRESENT CONDITION ON AN "AS IS", "WHERE IS" AND "WITH ALL FAULTS", INCLUDING ENVIRONMENTAL MATTERS AND ACKNOWLEDGES THAT WITHOUT THIS ACCEPTANCE, THIS LEASE WOULD NOT BE MADE.

38. **WAIVER OF CONSUMER RIGHTS**. THE UNDERSIGNED TENANT HEREBY ACKNOWLEDGES THAT IT IS NOT IN A SIGNIFICANTLY DISPARATE BARGAINING POSITION; AND HAS BEEN REPRESENTED BY COUNSEL IN SEEKING OR ACQUIRING THE LEASEHOLD THAT IS THE SUBJECT OF THIS LEASE. TENANT HEREBY WAIVES ANY AND ALL RIGHTS UNDER THE DECEPTIVE TRADE PRACTICES—CONSUMER PROTECTION ACT, SECTION 17.41 ET SEQ, BUSINESS & COMMERCE CODE, A LAW THAT GIVES CONSUMERS SPECIAL RIGHTS AND PROTECTIONS, AFTER CONSULTATION WITH AN ATTORNEY OF ITS OWN SELECTION. TENANT VOLUNTARILY CONSENTS TO THIS WAIVER.

39. Each party hereto may restrain or enjoin any breach of any covenant, duty or obligation of the other party herein contained without the necessity of proving the inadequacy of any legal remedy or irreparable harm. The remedies of either party hereunder shall be deemed cumulative, and no remedy of such party, whether exercised by such party or not, shall be deemed to be in exclusion of any other. Except as may be otherwise herein expressly provided, in all circumstances under this Lease where prior consent or permission of one (1) party ("**first party**") is required before the other party ("**second party**") is authorized to take any particular type of action, the matter of whether to grant such consent or permission shall be within the sole and exclusive judgment and discretion of the first party; and it shall not constitute any nature of breach by the first party hereunder or any defense to the performance of any covenant, duty or obligation of the second party hereunder that the first party delayed or withheld the granting of such consent or permission, whether or not the delay or withholding of such consent or permission was prudent or reasonable or based on good cause.

40. In all instances where either party is required to pay any sum or do any act at a particular indicated time or within an indicated period, it is understood that time is of the essence.

41. The obligation of Tenant to pay all rental and other sums hereunder provided to be paid by Tenant and the obligation of Tenant to perform Tenant's other covenants and duties hereunder constitute independent, unconditional obligations to be performed at all times provided for hereunder, save and except only when an abatement thereof or reduction therein is hereinabove expressly provided for and not otherwise. Tenant waives and relinquishes all rights which Tenant might have to claim any nature of lien against or withhold, or deduct from or offset against any rental and other sums provided hereunder to be paid Landlord by Tenant. Tenant waives and relinquishes any right to assert, either as a claim or as a defense, that Landlord is bound to perform or is liable for the nonperformance of any implied covenant or implied duty of Landlord not expressly herein set forth.

42. [Intentionally Omitted].

43. All monetary obligations of Landlord and Tenant (including, without limitation, any monetary obligation of Landlord or Tenant for damages for any breach of the respective covenants, duties or obligations of Landlord or Tenant hereunder) are performable exclusively in the county in which the

Building is located.

44. The laws of the State in which the Building is located shall govern the interpretation, validity, performance and enforcement of this Lease.

45. Words of any gender used in this Lease shall be held and construed to include any other gender, and words in the singular number shall be held to include the plural, unless the context otherwise requires.

46. Nothing herein contained shall be deemed or construed by the parties hereto, nor by any third party, as creating the relationship of principal and agent, or of partnership or of joint venture between the parties hereto, it being understood and agreed that neither the method of the computation of rental, nor any other provision contained herein, nor any acts of the parties hereto, shall be deemed to create any relationship between the parties hereto other than the relationship of landlord and tenant

47. Tenant further acknowledges that no rights, easements or licenses are acquired by Tenant by implication or otherwise, except as herein expressly set forth

48. Tenant warrants that Tenant is, and shall remain throughout the Term of this Lease, authorized to do business and in good standing in the State in which the Building is located. Tenant agrees, upon request by Landlord, to furnish Landlord satisfactory evidence of Tenant's authority for entering into this Lease.

49. [Intentionally Omitted.]

50. In the event Tenant requests from Landlord the written consent of Landlord to any proposed action for which this Lease requires such consent, Landlord may require (in addition to the payment of reasonable attorneys' fees) the payment by Tenant of a fee representing the administrative cost incurred by Landlord in processing such request, regardless of whether such consent is granted. Such fee shall be payable by Tenant at the time such request is made by Tenant. However, if Landlord reasonably believes that the out-of-pocket costs payable to third parties to be incurred by Landlord in reviewing the proposed action or consent will exceed $1,000, Landlord will first notify Tenant of such cost estimate before proceeding with such third-party expenses. The time period for Landlord's consent to the proposed action shall be tolled until such time as Tenant consents to such additional costs and expenses. If Tenant fails to consent to such additional costs and expenses within five business days after Landlord's written notification to Tenant thereof, Tenant shall be deemed to have rescinded its request for such action or consent.

51. Landlord shall have the right at any time to change the name or street address of the Building and to install and maintain a sign or signs on the interior or exterior of the Building.

52. The parties acknowledge that the parties and their counsel have reviewed and revised this Lease and that the normal rule of construction to the effect that any ambiguities are to be resolved against the drafting party shall not be employed in the interpretation of this Lease or any exhibits or amendments hereto.

RELOCATION

53. **[Intentionally Omitted].**

54. **Compliance with Laws**. Landlord represents and warrants to Tenant that, to the current, actual knowledge of Landlord, the Building is in compliance with all applicable laws (including any restrictive covenants affecting the Building) in existence as of the date of this Lease. If at any time during the Term, the Building fails to comply with any law (including any restrictive covenants affecting the Building) and (including any restrictive covenants affecting the Building), Landlord shall (subject to the reimbursement of such costs on the terms and subject to the limitations contained in this Lease) take such action in connection therewith as may be (and within the time frame) required by law (including any restrictive

covenants affecting the Building) and thereafter diligently pursue such action until completion.

55. **Internal Statute of Limitations**. Notwithstanding anything to the contrary in this Lease, any charges due to be paid by either Landlord or Tenant to the other party hereto, other than Basic Rental and any charges or other sums pertaining to the indemnity and insurance obligations of either party under this Lease, shall be deemed waived by the other party hereto unless invoiced to the party owing such amount prior to the expiration of twelve (12) months following the date such charges are due.

56. **Attorneys' Fees**. If there is any legal or arbitration action or proceeding between Landlord and Tenant to enforce any provision of this Lease or to protect or establish any right or remedy of either Landlord or Tenant hereunder, the unsuccessful party to such action or proceeding will pay to the prevailing party all reasonable, actual out-of-pocket costs and expenses paid or payable to third parties, including reasonable attorneys' fees incurred by such prevailing party in such action or proceeding and in any appeal in connection therewith, and if such prevailing party recovers a judgment in any such action, proceeding or appeal, such costs, expenses and attorneys' fees will be determined by the court or arbitration panel handling the proceeding and will be included in and as a part of such judgment.

57. **Landlord's Default**. Landlord shall be in default under this Lease only if Landlord fails to perform any of its obligations within the time period provided for under this Lease, and such failure continues for 30 days after Tenant delivers to Landlord written notice specifying such failure; provided however, Landlord shall use reasonable efforts to commence such cure as soon as reasonably practicable following Tenant's written notification and if such failure cannot reasonably be cured within such 30-day period, but Landlord commences to cure such failure within such 30-day period and thereafter diligently pursues the curing thereof to completion, then Landlord shall not be in default hereunder or liable for damages therefor; unless it is not fully cured within a reasonable time but in no event later than 150 days following receipt of written notice from Tenant of such failure Unless Landlord fails to so cure such default after such notice, Tenant shall not have any remedy or cause of action by reason thereof. If following the Commencement Date Landlord fails to perform its obligations within the time periods provided for in the previous sentences of this Section 57, then Tenant may reasonably and in a good and workmanlike manner perform such obligations and Landlord shall reimburse Tenant all reasonable and actual third-party, out-of-pocket costs reasonably and actually incurred by Tenant in connection with performing such obligations (other than those which would constitute a Basic Cost had Landlord performed such work, in which case, Landlord shall not be obligated to reimburse Tenant for the pro rata cost thereof) within 30 days after Tenant delivers to Landlord written demand therefor, accompanied by invoices substantiating Tenant's claim. Nothing herein contained shall give or allow Tenant any right of offset or credit to or towards its monetary obligations under this Lease.

THE REMAINDER OF THIS PAGE INTENTIONALLY LEFT BLANK.

Effective as of the date first written above.

LANDLORD:

Pearson Fund III, L.P.,
a Texas limited partnership

By: Pearson Group Capital Management III, Inc.
A Texas corporation
General Partner

By: /s/ Craig Nemec
Name: Craig Nemec
Title: President
Signed the 31st day of July, 2005

TENANT:

Sonas Networks, Inc.
a Delaware corporation

By: /s/ Ellen B. Richstone
Name: Ellen B. Richstone
Title: CFO
Signed the 29th day of July, 2005

EXHIBIT A-1

LEGAL DESCRIPTION OF LAND

BEING a 4.214 acre tract of land situated in the Baurch Cantrell Survey, Abstract No. 625, City of Richardson, Texas, Dallas County, Texas, and being all of LOT 2, BLOCK 1, of a Replat of Richardson Industrial Park East, according to the Map or Plat recorded in Volume 67089, Page 3521, Map Records of Dallas County, Texas.

EXHIBIT A-2 – 1st Floor

DEPICTION OF PREMISES AND FIRST FLOOR COMMON AREA

(Being attached for identification purposes only.
Such depictions are expressly made WITHOUT WARRANTY, EXPRESS OR IMPLIED, OF ANY KIND)

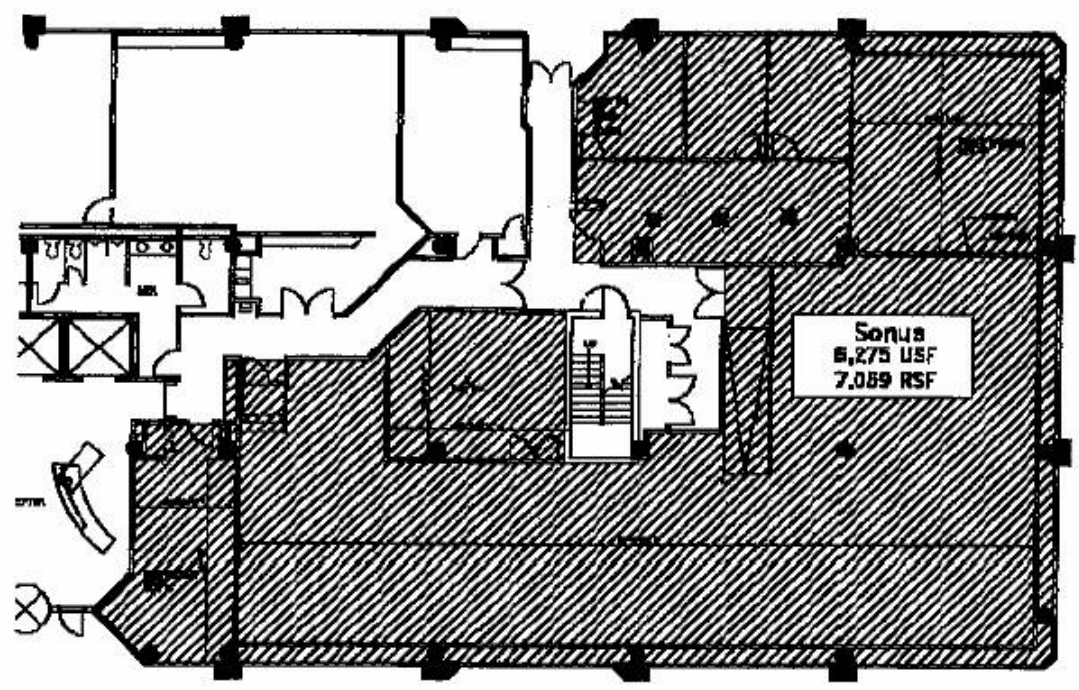

EXHIBIT A-3 – 2nd Floor

DEPICTION OF PREMISES

(Being attached for identification purposes only.
Such depictions are expressly made WITHOUT WARRANTY, EXPRESS OR IMPLIED, OF ANY KIND)

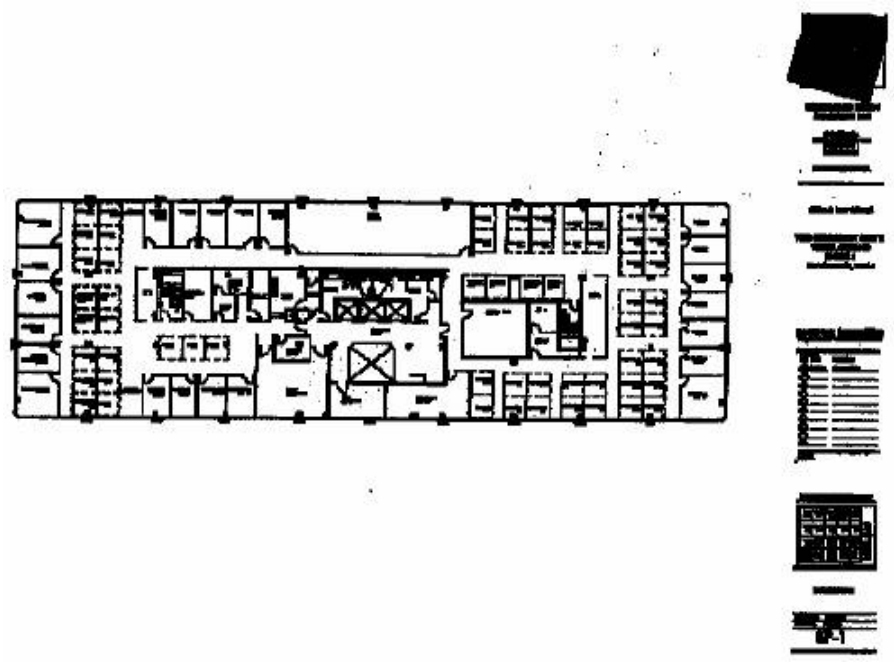

EXHIBIT B

BUILDING RULES AND REGULATIONS

The following rules and regulations shall apply to the Premises, the Building, the Parking Facilities associated therewith, the Land and the appurtenances thereto:

1. Sidewalks, doorways, vestibules, halls, stairways, and other similar areas shall not be obstructed by tenants or used by any tenant for any purpose other than ingress and egress to and from their respective leased premises and for going from one to another part of the Building.

2. Plumbing, fixtures and appliances shall be used only for the purposes far which designed, and no sweepings, rubbish, rags or other unsuitable material shall be thrown or deposited therein. Damage resulting to any such fixtures or appliances from misuse by a tenant or its agents, employees or invitees, shall be paid by such tenant.

3. No signs, advertisements or notices shall be painted or affixed on or to any windows or doors or other part of the Building without the prior written consent of Landlord. No curtains or other window treatments shall be placed between the glass and the Building standard window treatments.

4. Landlord shall provide and maintain an alphabetical directory for all tenants in the main lobby of the Building and Tenant shall be listed in the Building Directory on or before the Commencement Date.

5. Landlord shall provide all door locks in each tenant's leased premises, at Landlord's cost, and no tenant shall place any additional door locks in its leased premises without Landlord's prior written consent. Landlord shall furnish to each tenant a reasonable number of keys to such tenant's leased premises, at such tenant's cost, and no tenant shall make a duplicate thereof.

6. Movement in or out of the Building of furniture or office equipment, or dispatch or receipt by tenants of any bulky material, merchandise or materials which require use of elevators or stairways, or movement through the Building entrances or lobby shall be conducted under Landlord's supervision at such times and in such a manner as Landlord may reasonably require. Each tenant assumes all risks of and shall be liable for all damage to articles moved and injury to any property and or to any persons or public engaged or not engaged in such movement, including equipment, property and personnel of Landlord if damaged or injured as a result of acts in connection with carrying out this service for such tenant.

7. Landlord may prescribe weight limitations and determine the locations for safes and other heavy equipment or items, which shall in all cases be placed in the Building so as to distribute weight in a manner acceptable to Landlord, which may include the use of such supporting devices as Landlord may require. All damages to the Building caused by the installation or removal of any property of a tenant, or done by a tenant's property while in the Building, shall be repaired at the expense of such tenant.

8. Corridor doors, when not in use, shall be kept closed. Nothing shall be swept or thrown into the corridors, halls, elevator shafts or stairways. No birds or animals shall be brought into or kept in, on or about any tenant's leased premises other than those animals specially trained to assist the disabled. No portion of any tenant's leased premises shall at any time be used or occupied as sleeping or lodging quarters.

9. Tenant shall cooperate with Landlord's employees in keeping its leased premises neat and clean. Tenants shall not employ any person for the purpose of such cleaning other than the Building's cleaning and maintenance personnel.

---

10. To ensure orderly operation of the Building, notice, mineral or other water, towels, etc. shall be delivered to any leased area except by persons approved by Landlord, in its reasonable discretion.

11. Tenant shall not make or permit any improper, objectionable or unpleasant noises or odors in the Building or otherwise interfere in any way with other tenants or persons having business with them.

12. No machinery of any kind (other than normal office equipment, four Precision air-conditioning units, and Uninterrupted Power Supply equipment and other related equipment typical in large data centers) shall be operated by any tenant in its leased area without Landlord's prior written consent, nor shall any tenant use or keep in the Building any flammable or explosive fluid or substance.

13. Landlord will not be responsible for lost or stolen personal property, money or jewelry from tenant's leased premises or public or common areas regardless of whether such loss occurs when the area is locked against entry or not.

14. No vending or dispensing machines of any kind may be maintained in any leased premises without the prior written permission of Landlord.

15. All mail chutes located in the Building shall be available for use by Landlord and all tenants of the Building according to the rules of the United States Postal Service.

16. Building Hours: Shall be 7:00 a.m. to 6:00 p.m. Monday through Friday, and 8:00 a.m. to noon on Saturdays.

EXHIBIT C

OPERATING EXPENSE ESCALATOR

1. Tenant shall pay an amount (per each rentable square foot in the Premises) equal to the excess ("**Excess**") from time to time of the actual Basic Cost per rentable square foot in the Building over the actual Basic Cost per rentable square foot in the building for the Base Stop Year (the "**Expense Stop**"). Landlord may collect such amount in a lump sum, to be due within 30 days after Landlord furnishes to Tenant the annual cost statement, that is, a statement of Landlord's actual costs, to be furnished to Tenant by Landlord by April 1 of each calendar year or as soon thereafter as practicable ("**Annual Cost Statement**"). Alternatively, Landlord may make a good faith estimate of the Excess to be due by Tenant for any calendar year or part thereof during the Term, and, unless Landlord delivers to Tenant a revision of the estimated Excess, Tenant shall pay to Landlord, on the Commencement Date and on the first day of each calendar month thereafter, an amount equal to the estimated Excess for such calendar year or part thereof divided by the number of months in such calendar year during the Term. From time to time (but not more than twice in any calendar year), Landlord may estimate and re-estimate the Excess to be due by Tenant and deliver a copy of the estimate or re-estimate to Tenant. Thereafter, the monthly installments of Excess payable by Tenant shall be appropriately adjusted in accordance with the estimations so that, by the end of the calendar year in question, Tenant shall have paid all of the Excess as estimated by Landlord. Any amounts paid based on such an estimate shall be subject to adjustment pursuant to Section 3 of this Exhibit when actual Basic Cost is available for each calendar year.

2. For the purposes of this Exhibit, the term "**Basic Cost**" shall mean all expenses and disbursements of every kind (subject to the limitations set forth below) which Landlord incurs, pays or becomes obligated to pay in connection with the ownership, operation, and maintenance of the Building (including the associated Parking Facilities), determined in accordance with generally accepted or federal income tax basis accounting principles consistently applied, including but not limited to the following:

(a) Reasonable wages and salaries and management fees, in each case, at market rates of all employees engaged in the operation, repair, replacement, maintenance, and security of the Building, including taxes, insurance and benefits relating thereto (all of the foregoing not to exceed in the aggregate 5% of gross rents);

(b) All supplies and materials used in the operation, maintenance, repair, replacement, and security of the Building;

(c) Cost of all actual capital improvements made to the Building which although capital in nature can reasonably and demonstrably be expected to reduce the normal operating costs of the Building, to the extent of such reduction, as well as all capital improvements made in order to comply with any law hereafter promulgated by any governmental authority, as amortized over the period over which such improvements may be amortized for federal income tax purposes;

(d) Cost of all utilities, other than the cost of utilities actually reimbursed to Landlord by the Building's tenants;

(e) Cost of any insurance or insurance related expense applicable to the Building and Landlord's personal property used in connection therewith;

(f) All taxes and assessments and governmental charges whether federal, state, county or municipal, and whether they be by taxing or management districts or authorities presently taxing or by others, subsequently created or otherwise, and any other taxes and assessments attributable to the Building (or its operation), and the grounds, parking areas, driveways, and alleys around the Building, excluding, however, federal and state taxes on income (collectively, "**Taxes**"); if the present method of taxation changes so that in lieu of the whole or any part of any Taxes levied on the Land or Building, there is levied on Landlord a capital tax directly on the rents received

---

therefrom or a franchise tax, assessment, or charge based, in whole or in part, upon such rents for the Building, then all such taxes, assessments, or charges, or the part thereof so based, shall be deemed to be included within the term "Taxes" for the purposes hereof; and

(g) Cost of repairs, replacements, and general maintenance of the Building; and

(h) Cost of service or maintenance contracts with independent contractors for the operation, maintenance, repair, replacement, or security of the Building (including, without limitation, alarm service, window cleaning, and elevator maintenance).

(i) There are specifically excluded from the definition of the term "Basic Cost" costs and expenses.

(1) for capital improvements made to the Building, other than capital improvements described in Subsection 2(e) of this Exhibit and except for items which, though capital for accounting purposes, are properly considered maintenance and repair items, such as painting of common areas, replacement of carpet in elevator lobbies, and the like;

(2) for repair, replacements and general maintenance paid by proceeds of insurance or by Tenant or other third parties, and alterations attributable solely to tenants of the Building other than Tenant;

(3) for interest, amortization or other payments on loans to Landlord, as maker;

(4) for legal expenses, other than those incurred for the general benefit of the Building's tenants (e.g., tax disputes);

(5) for renovating or otherwise improving space for occupants of the Building or vacant space in the Building;

(6) for overtime or other expenses of Landlord in curing defaults or performing work expressly provided in this Lease to be home at Landlord's expense;

(7) for federal income taxes imposed on or measured by the income of Landlord from the operation of the Building;

(8) for repair or replacement or other work occasioned by exercise of the right of eminent domain (to the extent of the costs and expenses for which Landlord actually receives a cash award);

(9) for leasing commissions, advertising and other promotional costs and expenses, attorneys' fees, costs and disbursements and other expenses incurred in negotiating or executing leases or in resolving disputes with other tenants, other occupants, or other prospective tenants or occupants of the Building, collecting rents or otherwise enforcing leases of other tenants of the Building;

(10) for special services rendered to particular tenants of the Building or that exclusively benefit another tenant or tenants of the Building, including, without limitation, costs of tenant installations, decorating expenses, redecorating expenses, or constructing improvements or alterations to any tenant space, the costs of any janitorial cleaning service or security services provided to other tenants which exceed the standard of that provided to Tenant and costs in connection with services (including electricity), items or other benefits of a type which are not standard for the Building and which are not available to Tenant without specific charge therefor, but which are provided to another tenant or occupant of the Building, whether or not such other tenant or occupant is actually charged therefor by Landlord;

---

(11) for depreciation of the Building, the systems related thereto (e.g., HVAC, elevators, electrical, plumbing, etc.) or the equipment or tools used in connection therewith;

(12) incurred by Landlord for which Landlord is actually reimbursed by parties other than tenants of the Building, including, without limitation, insurance proceeds;

(13) for the initial construction of the Building, including the correction of any structural construction defects;

(14) except for the management fee, of any overhead or profit;

(15) of any amounts paid to any subsidiary or affiliate of Landlord for services on or to the Building, parking garage or related facilities and/or the Land on which the Building is situated, to the extent of any portion of the cost of such services exceeds the reasonable costs for such services rendered by persons or entities of similar skill, competence and experience other than a subsidiary or affiliate of Landlord;

(16) of rental under any ground or underlying lease or leases for the Land;

(17) except for the management fee, of Landlord's general overhead;

(18) of any compensation paid to clerks, attendants or other persons in commercial concessions operated by Landlord, other than with respect to the parking garage;

(19) for items and services for which Tenant directly reimburses Landlord or pays to third persons with Landlord's consent, to the extent of such reimbursement or payment;

(20) of fines, penalties, and legal fees incurred due to violations by Landlord, its employees, agents, contractors or assigns, or any other tenant or occupant of the Building, of building codes, any other governmental rule or requirement or the terms and conditions of any lease pertaining to the Building;

(21) of management fees to the extent of any portion of such fees which are unreasonable;

(22) of acquiring sculptures, paintings, wall hangings or other objects of art;

(23) of wages, salaries, or other compensation paid to any executive employees of Landlord above the level of property manager; provided, further, if any employee of Landlord works on several buildings within the area, including the Building, the costs and expenses connected with such employee shall be allocated among such buildings by Landlord in accordance with reasonable and consistent criteria;

(24) incurred in leasing air-conditioning systems, elevators, or other equipment ordinarily considered to be of a capital nature (other than on a temporary basis);

(25) associated with the removal or encapsulation of asbestos or other hazardous or toxic substances;

(26) for repairs or maintenance which are covered by warranties and service contracts, to the extent such maintenance and repairs are made at no cost to Landlord;

(27) representing any amount paid for services and materials to an affiliate of Landlord (i.e., persons or entities controlled by, under common control with, or which control, Landlord) to the extent such amount exceeds the amount that would reasonably be paid for such services or materials were they rendered by an unaffiliated person, firm or corporation;

---

(28) for amounts payable by Landlord by way of indemnity or for damages or which constitutes a fine or penalty, including interest or penalties for any late payment;

(29) for repairs necessitated by violations of law in effect as of the date of the Lease;

(30) for property taxes and assessments which are not properly allocable to the Building; without limiting the generality of the foregoing, property taxes and assessments which are properly allocable to undeveloped land shall be excluded from Basic Cost;

(31) of interest and penalties due to the late payment of taxes, utility bills or other such costs except any interest or penalties arising from late payments beyond Landlord's control; and

(32) bad debt expenses and charitable contributions and donations; and

(33) costs incurred as a result of the gross negligence of Landlord.

3. The Annual Cost Statement shall include a statement of Landlord's actual Basic Cost for the previous year adjusted as provided in Section 4 of this Exhibit. If the Annual Cost Statement reveals that Tenant paid more for Basic Cost than the actual Excess in the year for which such statement was prepared, then Landlord shall credit or reimburse Tenant for such excess within 30 days after delivery of the Annual Cost Statement; likewise, if Tenant paid less than the actual Excess, then Tenant shall pay Landlord such deficiency within 30 days after delivery of the Annual Cost Statement.

4. With respect to any calendar year or partial calendar year in which the Building is not occupied to the extent of 95% of the rentable area thereof, including calendar year 2006 (if applicable), the Basic Cost for such period shall, for the purposes hereof, be increased to the amount which would have been incurred had the Building been occupied to the extent of 95% of the rentable area thereof. The foregoing adjustment shall be applied only to those items of Basic Cost which vary with the level of occupancy of the Building, and in particular, shall not be applied to taxes described in Subsection 2(f) of this Exhibit C. In no event shall Landlord be entitled to recover more than one hundred percent (100%) of actual Basic Costs pursuant to this Section.

5. For purposes of calculating Excess under this Exhibit C, the Controllable Basic Costs (defined below) for each calendar year after **2006** shall not increase by more than 106% over the Controllable Operating Costs for the previous calendar year. "**Controllable Basic Costs**" shall mean all items of Basic Costs which are within the reasonable control of Landlord; thus, excluding taxes, insurance, utilities, snow removal costs, costs incurred to comply with governmental requirements, and other costs beyond the reasonable control of Landlord.

EXHIBIT D

SPECIAL PROVISIONS

The following Special Provisions are hereby made a part of the Lease Agreement, in all respects, and shall be read in context of the Standard Lease Provisions as set forth and contained therein. In the event of any express conflict between these Special Provisions and the Standard Lease Provisions, then these Special Provisions shall control:

1. Right of First Refusal. If during the term of this Lease, Landlord receives a bona fide offer from a third party (the "**Third Party Offer**") to execute a new lease for the lease of (a) the remaining portion of the first floor of the Building not included in the Premises or (b) any portion of the third floor of the Building (collectively, the "**Refusal Space**") and Landlord is willing to accept the terms of such Third Party Offer, Landlord shall, provided that (a) no Event of Default then exists, and (b) Tenant occupies the Premises, offer to lease to Tenant the Refusal Space on the same terms and conditions as the Third Party Offer; such offer shall be in writing, specify the rent to be paid for the Refusal Space, contain the basic terms and conditions of the Third Party Offer and the date on which the Refusal Space shall be included in the Premises (the "Offer Notice"). Tenant shall notify Landlord in writing whether Tenant elects to lease the entire portion of the Refusal Space subject to the Third Party Offer on the same terms and conditions as the Third Party Offer in the Offer Notice within seven (7) business days after Landlord delivers to Tenant the Offer Notice. If Tenant timely elects to lease the Refusal Space within such seven (7) - business day period by written notice to Landlord, then Landlord and Tenant shall execute

an amendment to this Lease effective as of the date the Refusal Space is to be included in the Premises, on the same terms as this Lease except (a) the Basic Rental shall be the amount specified in the Offer Notice (b) the term for the Refusal Space shall be that specified in the Offer Notice, (c) Tenant shall receive any tenant improvement allowance referenced in the Offer Notice with respect to the Refusal Space, and (d) other terms set forth in this Lease which are inconsistent with the terms of the Offer Notice shall be modified accordingly respecting the Refusal Space only. If Tenant fails to timely elect to Lease the Refusal Space or fails to execute the Amendment to the Lease consistent herewith within seven (7) business days of receipt of such from Landlord, then this right shall automatically terminate as to the portion of the Refusal Space covered by the applicable Third Party Offer only.

2. Monument Signage

So long as (i) no Event of Default then exists, and (ii) Tenant occupies at the Premises, effective as of the Commencement Date signage shall be made available for Tenant on both sides of the existing monument in front of the Building in a manner consistent with the signage currently in place. Any such signage shall be at Tenant's sole cost and subject to applicable governmental approvals and permits, and Landlord's prior written approval, which shall not be unreasonably withheld, conditioned or delayed. Notwithstanding the foregoing. Landlord shall have the right, at Landlord's sole cost and expense, from time to time during the Term, as the same may be extended, to relocate and/or replace said signage with similar signage of equal or greater size and of equivalent or better location and visibility. Tenant's sign panel or display shall be at least as large as any other panel or display of any other Tenant. In the event that the pertinent laws, rules, regulations or governmental authorities limit the number of designations that may be placed on the monument sign to one, then only the Building name shall be displayed thereon. In the event that the pertinent laws, rules, regulations and governmental authorities limit the

---

number of designations to be placed on the monument sign to two, then only the designation of the Building and the Tenant then occupying the greatest RSF in the Building shall be on the monument sign. Subject to the foregoing, Landlord shall use reasonable efforts to ensure that Tenant will have its name on the monument sign throughout the Lease Term.

3. Spandrel Signage

So long as (i) no Event of Default then exists, and (ii) Tenant occupies at the Premises, effective as of the Commencement Date, and subject to regulatory approvals and Landlord's prior written approval, which shall not be unreasonably conditioned, withheld or delayed, Tenant may install building signage above the 6th floor spandrel on the northwest side of the building facing Arapaho Road. Any such signage shall be at Tenant's sole cost.

4. Finish Work Allowance

The space will be provided in its "as-is" condition. Landlord shall provide Tenant with an allowance for the costs ("**Finish Work Allowance Costs**") of hereafter constructing any tenant improvements in the Premises (including, without limitation, third party architectural and engineering fees with respect thereto) in an amount not to exceed **$864,840.83** (i.e., the product of (x)**$32.59** per rentable square foot and (y) **26,537** rentable square feet of the Premises) (the "**Finish Work Allowance**"). All construction and design costs for the Premises in excess of the Finish Work Allowance shall be paid for entirely by Tenant, and Landlord shall not provide any reimbursement therefor. The Finish Work Allowance, less 10% retainage, shall be disbursed as requisitioned by Tenant, but not more frequently than monthly, within thirty (30) days after Tenant's submission of the requisition package. For each disbursement, Tenant shall submit a requisition package to Landlord with an itemization of the costs being requisitioned, a certificate by an officer of Tenant that all such costs are Finish Work Allowance Costs and have been incurred by Tenant, and appropriate back-up documentation including, without limitation, partial or full lien waivers (in a form reasonably approved by Landlord), invoices and bills (together with evidence of Tenant's payment of such amounts, if Tenant does not request such invoices to be paid by joint check pursuant to the next sentence), and, upon completion of the work, such certificates of completion, final lien waivers, certificates of occupancy, and as-built plans as Landlord may reasonably require in light of the nature and scope of the work Notwithstanding the foregoing, at Tenant's request, Landlord shall make disbursements of the Finish Work Allowance by check jointly payable to Tenant and Tenant's general contractor with respect to the portion of the work then completed; provided however, that Landlord shall have no responsibility or Liability to Tenant or such contractor with respect to such work, including without limitation, the quality or completeness of such work or any warranties associated therewith. If the reasonably estimated cost of the work exceeds the Finish Work Allowance, Landlord reserves the right to make pro-rata disbursements of the Finish Work Allowance in the proportion that the Finish Work Allowance bears to the estimated cost of the work, subject to a final reconciliation upon completion of the work. Subject to the foregoing, Landlord shall disburse the retainage amount upon receipt of a final back-up documentation, within forty-five (45) days of completion of all the work. Landlord shall have no obligation to pay the Finish Work Allowance at any time (a) when Tenant is in default under the Lease (as amended hereby) beyond the expiration of any applicable notice or cure period or (b) with respect to any requisition submitted after the last day of the Sixth (6th) Lease Month. After the final completion of the work and the reconciliation of the Finish Work Allowance and the Finish Work Allowance Costs, Tenant may use any excess Finish Work Allowance for the payment of Rent hereunder or towards the cost of Tenant's bona fide move-related expenses, furniture, and cabling costs respecting the Premises, and third party construction management services by

---

making written request for such final disbursement before the last day of the Sixth (6^{th}) Lease Month, together with all appropriate back up documentation, and Landlord shall reimburse Tenant for the cost of the same within thirty (30) days of Tenant's request therefor. Thereafter Landlord shall have no obligation for any unused portion of the Finish Work Allowance.

5. Early Termination:

Provided no monetary Event of Default by Tenant then exists at the time of the exercise of the option that is the subject of this special provision, Tenant shall have the irrevocable right to terminate the Lease effective on the last day of the 36^{th} Lease Month by delivering to Landlord written notice thereof ("**Termination Notice**") no later than the last day of the 28^{th} Lease Month accompanied by a Termination Fee (herein so called) in cash or its equivalent in an amount equal to the balance of as the effective date of such Termination of all unamortized Landlord's Finish Work Allowance, brokerage commissions and costs for the purchase and installation of the Generator associated with the Lease, such costs to be amortized at a rate of nine percent (9%) over the initial Term of this Lease. Failing the timely delivery of the Termination Notice and or the Termination Fee, then the right herein provided shall automatically cease and expire.

6. Single Renewal Option:

Tenant may renew this Lease for one additional period of five (5) years, provided there is not then an Event of Default by Tenant under the Lease, by delivering written notice of the exercise thereof to Landlord not later than six months before the expiration of the Term. The Basic Rental payable for each month during such extended Term shall be the prevailing rental rate (the "**Prevailing Rental Rate**"), at the commencement of such extended Term, for renewals of space in buildings comparable to the Building in the submarket in which the Premises are located of equivalent quality, size, utility and location, with the length of the extended Term and the credit standing of Tenant to be taken into account. Within 30 days after receipt of Tenant's notice to renew, Landlord shall deliver to Tenant written notice of the Prevailing Rental Rate and shall advise Tenant of the required adjustment to Basic Rental, if any, and the other terms and conditions offered. Tenant shall, within twenty (20) days after receipt of Landlord's notice, notify Landlord in writing whether Tenant accepts or rejects Landlord's determination of the Prevailing Rental Rate. If Tenant timely notifies Landlord that Tenant accepts Landlord's determination of the Prevailing Rental Rate, then, on or before the commencement date of the extended Term, Landlord and Tenant shall execute an amendment to this Lease extending the Term on the same terms provided in this Lease, except as follows:

(a) Basic Rental shall be adjusted to the Prevailing Rental Rate;

(b) Tenant shall have no further renewal option unless expressly granted by Landlord in writing;

(c) Landlord shall lease to Tenant the Premises in their then-current condition, and Landlord shall not provide to Tenant any allowances (e.g., moving allowance, construction allowance, and the like) or other tenant inducements; provided, if such allowances have been taken into account in determining the Prevailing Rental Rate, then Landlord shall provide such allowances to Tenant; and

(d) The Expense Stop shall be adjusted to be the calendar year in which the extended Term commences (provided such adjustment is taken into account in

---

determining the Prevailing Rental Rate).

If Tenant rejects Landlord's determination of the Prevailing Rental Rate and timely notifies Landlord thereof, Tenant may, in its notice to Landlord, require that the determination of the Prevailing Rental Rate be made by brokers. In such event, within 10 days thereafter, each party shall select a qualified commercial real estate broker with at least ten years experience in Leasing property and buildings in the city or submarket in which the Premises are located. The two brokers shall give their opinion of prevailing rental rates within 20 days after their retention. In the event the opinions of the two brokers differ and, after good faith efforts over the succeeding 20-day period, they cannot mutually agree, the brokers shall immediately and jointly appoint a third broker with the qualifications specified above. This third broker shall immediately (within five days) choose either the determination of Landlord's broker or Tenant's broker and such choice of this third broker shall be final and binding on Landlord and Tenant. Each party shall pay its own costs for its real estate broker. Following the determination of the Prevailing Rental Rate by the brokers, the parties shall equally share the costs of any third broker,

7. Satellite Dish/Riser:

Subject to the terms set forth below, Landlord hereby grants Tenant a license to use a portion of the roof of the Building for the installation of up to two (2) communications antennae or satellite dish or other communications equipment for Tenant's uses ancillary to the Permitted Use in the Premises (the "**Satellite Dish**"). The size, location, manner of placement, screening, installation specifications, and other particulars of the Satellite Dish shall be subject to the prior review and reasonable approval of Landlord. Tenant shall be responsible for obtaining all necessary permits, approvals, and operating licenses for such installation and shall pay all costs arising from the installation, maintenance, repair, and subsequent removal of the Satellite Dish, and repair and replacement of any disturbed roofing materials associated therewith. Similarly, subject to the terms set forth below, Landlord hereby grants Tenant a license to use a portion of the riser space situated at the Building for the installation of certain equipment for Tenant's uses ancillary to the Permitted Use in the Premises. The size, location,

manner of placement, screening, installation specifications, and other particulars of such equipment shall be subject to the prior review and reasonable approval of Landlord. Tenant shall be responsible for such installation and shall pay all costs arising from the installation, maintenance and repair of such equipment.

8. Generator

Landlord, at its sole cost and expense, shall purchase, install and maintain in good working order throughout the Term, an approximate 500 Kva generator with a 2-hour fuel "day tank", pursuant to written specifications as provided by Tenant, and subject to Landlord's review and approval, for use by Tenant during the Term; provided however that Landlord shall also have the right to use such for its benefit and the benefit of the Building for essential building systems. Such installation shall include the generator pad, screening and conduit to the Premises. Conduit shall be adequate in size to accommodate wiring from a second generator if installed by Tenant, at its sole cost and expense, with the prior written approval of Landlord, if any. The location of the generator shall be mutually acceptable to Landlord and Tenant.

Upon installation of the generator or contemporaneously therewith, Tenant may, at its sole cost and expense, perform the electrical testing of the generator and related systems, to its reasonable satisfaction. Landlord shall be responsible for, and shall timely perform, all other testing associated with the generator.

Landlord and Tenant shall use their best efforts in the installation and any testing of the generator, so that the generator will be installed and ready for use on or before November 1, 2005.

9. Furniture

In addition to the Finish Work Allowance, Landlord shall provide Tenant with an allowance for the costs ("**Furniture Allowance Costs**") of hereafter purchasing thirty (30) new Kimball "Reasons" cubicles and thirty (30) new "CUSP" task chairs, or, in each case, furniture of comparable quality, and otherwise furnishing up to three (3) conferences rooms with one (1) new or used conference table and up to twelve (12) new or used conference chairs for each of the three conference rooms within the Premises in an amount not to exceed **$100,000.00** (the "**Furniture Allowance**"). Prior to the acquisition of such furniture Tenant shall provide copies of the bids or other pricing for such furniture, and the type and cost of such shall be subject to Landlord's review and approval, which approval shall not be unreasonably withheld, conditioned or delayed; and in the event Landlord does not approve or disapprove of any such bids within five (5) business days of Tenant's submission thereof, then Landlord shall be deemed to have **approved** of such bid. Provided Landlord, has approved (or is deemed to have approved) the proposed furniture to be purchased, as provided in the foregoing, the Furniture Allowance shall be disbursed as requisitioned by Tenant, but not more frequently than monthly, within thirty (30) days after Tenant's submission of the requisition package. For each disbursement, Tenant shall submit a requisition package to Landlord with an itemization of the costs being requisitioned, a certificate by an officer of Tenant that all such costs are Furniture Allowance Costs and have been incurred by Tenant, and appropriate back-up documentation including, without limitation, invoices and bills (together with evidence of Tenant's payment of such amounts, if Tenant does not request such invoices to be paid by joint check pursuant to the next sentence). Notwithstanding the foregoing, at Tenant's request, Landlord shall make disbursements of the Furniture Allowance by check jointly payable to Tenant and the furniture supplier with respect to the portion of the furniture then acquired. Landlord shall have no obligation to pay the Furniture Allowance at any time (a) when Tenant is in default under the Lease (as amended hereby) beyond the expiration of any applicable notice or cure period or (b) with respect to any requisition submitted after the last day of the Sixth (6^{th}) Lease Month. Thereafter Landlord shall have no obligation for any unused portion of the Furniture Allowance. All furnishings purchased with the Furniture Allowance shall be and remain the property of Landlord, provided however, that during the Term, Tenant shall lease and have the right to use such furniture, in partial consideration of the Basic Rental provided for herein, and provided that Tenant during the Term of the Lease shall be responsible for any and all business personal property taxes assessed respecting such furniture.

10. Security System

Landlord will make its card-key access system available to Tenant so that Tenant may secure the Premises via the card-key access system and access the exterior security cameras (to the extent such cameras are operational).

11. Tenant Audit of Excess

Tenant, at its expense, shall have the right upon fifteen (15) business days advance written notice, to inspect Landlord's books and records relating to the Lease and the Building for any year in which Excess charges are due, any such inspection to be conducted at Landlord's building manager's office, during normal business hours; provided, however Landlord agrees to reimburse Tenant for the costs of any such inspection conducted by or for it in the event the inspection reflect that the Excess charged to Tenant by Landlord hereunder for the period of time covered by such

---

inspection shall have been overstated by seven (7%) or more. If such audit or inspection reveals that an error was made in the Excess previously charged to Tenant, Landlord shall refund to Tenant any overpayment of any such costs within 30 days of notification thereof. Any such inspection must cover a period within twenty-four (24) months prior to the then current calendar year, any objections to charges prior thereto being conclusively presumed to have been waived.

12. Permitted Equipment	Any provision of Section 12 of the Building Rules and Regulations to the contrary notwithstanding. Tenant may use and operate in the Premises four (4) Precision air-conditioning units, and Uninterrupted Power Supply equipment and other related equipment typical in large data centers, subject to the other terms and provisions as provided in this Lease.
13. Building Hours	Any provision of Section 16 of the Building Rules and Regulations to the contrary notwithstanding, the Building Hours, for purposes of this Lease shall be 7:00 a.m. to 7:30 p.m. Monday through Friday, and 8:00 a.m. to 1:00 p.m. on Saturdays.
14. Landlord's Remedial ADA Compliance	Landlord covenants and agrees to commence within 45 days of the Effective Date to commence and diligently pursue to completion the installation, remediation or repair of the ADA compliance matters set forth on Exhibit D-1 hereto.

Exhibit D-1
ADA Compliance Matters

Women's Restroom

1. Accessible signage on front door to be relocated to strike side of door at 60" a.f.f.
2. Entrance door to restroom is not accessible on the pull side.
3. ADA/TAS stall door to be 4" max. from side stall wall (it is currently at 7").
4. Coat book on women's ADA/TAS stall is mounted at 53" a.f.f. Needs to be mounted at 48" a.f.f.
5. Women's ADA/TAS water closet is not at an accessible height or distance from closest side wall. Relocate to 1'-6" from side wall and at 17" – 19" a.f.f. to top of rim.
6. Provide new women's rear grab bar (to be 36" minimum, is at 30" currently).
7. Lavatory apron is 26-1/2" a.f.f. and needs to be 29" a.f.f. minimum for required ADA/TAS knee clearance.
8. Kneespace under lavatory is not clear 8" deep X 27" high required ADA/TAS clearance because of existing angled panel.
9. Paper towel dispenser / trash receptacle is mounted too high. Relocate so that paper towel dispenser height is at 48" a.f.f.

Men's Restroom

1. Accessible signage on front door to be relocated to strike side of door at 60" a.f.f.
2. Entrance door is not accessible on the pull side.
3. Men's ADA/TAS water closet is not at an accessible distance from closest side wall. Relocate water closet to 1'-6" from side wall.
4. Existing urinal does not meet the 14" deep TAS requirement. Provide new urinal and mount per ADA/TAS requirements.
5. Cut privacy panel between urinals back to 24" deep maximum (or width will have to increase to 32" wide. Stall is currently at 30-1/2" wide).
6. Paper towel dispenser projects 4-1/4" from wall and is mounted 50" to paper towel dispenser. Provide new paper towel dispenser which projects 4" max. from wall and mount at 48" a.f.f. to paper towel dispenser.
7. Lavatory apron is 26-1/2" a.f.f. and needs to be at 29" a.f.f. minimum for required ADA/TAS knee clearance.
8. Kneespace under lavatory is not have 8" deep X 27" high required ADA/TAS clearance because of existing angled panel.

Breakroom millwork

1. Front vertical apron at accessible sink meets ADA/TAS knee clearance height, however, horizontal and sloped panel beyond is impeding on the 8" deep X 27" high required knee space.

EXHIBIT E

PARKING

Parking Spaces.

Landlord hereby grants to Tenant and persons designated by Tenant a license for the duration of the Term to use up to **one hundred and four (104) unreserved** surface parking spaces and **twenty (20) reserved** covered vehicle parking space (as Landlord shall determine) in that certain surface parking lot facility (the "**Parking Facilities**") owned by Landlord adjacent to the Building, for the initial Term of the Lease, subject to its early termination as provided in this Lease, and subject to such terms, conditions and regulations as are from time to time applicable to patrons of the Parking Facilities.

During such initial Term, there shall be a charge of $0.00 (plus tax) per month per unreserved parking space and a charge of $0.00 (plus tax) per month per reserved parking space, for the parking spaces designated above, whether or not Tenant utilizes such parking spaces. No deductions from the monthly charge will be made for days on which the Parking Facilities or any particular parking space is not used by Tenant.

After the initial Term, Tenant may continue such license, subject to the payment of the then prevailing fees generally charged by Landlord for such parking spaces, and subject to such terms, conditions and regulations as are from time to time applicable to patrons of the Parking Facilities.

Tenant may not assign its licenses without the prior written approval of Landlord, which shall not be unreasonably withheld, conditioned or delayed.

Control of Parking.

Tenant shall at all times comply with all applicable ordinances, rules, regulations, codes, laws, statutes and requirements of all federal, state, county and municipal governmental bodies or their subdivisions respecting the use of the Parking Facilities. Landlord reserves the right from time to time to adopt, modify and enforce reasonable rules governing the use of the Parking Facilities, including any key-card, sticker or other identification or entrance system, and hours of operation. Landlord may refuse to permit any person who violates such rules to park in the Parking Facilities, and any violation of the rules will subject the car to removal from same.

Liability.

The unreserved parking spaces hereunder will be provided on an unreserved "first-come, first-served" basis. Tenant acknowledges that Landlord has or may arrange for the Parking Facilities to be operated by an independent contractor, not affiliated with Landlord. Tenant agrees to look first to its insurance carrier and to require that Tenant's employees look first to their respective insurance carriers for payment of any losses sustained in connection with any use of the Parking Facilities. Tenant hereby waives on behalf of Tenants insurance carriers all rights of subrogation against Landlord or Landlord's agents. Landlord reserves the right to assign specific spaces, and to reserve spaces for visitors, small cars, handicapped persons and for other tenants, guests of tenants or other parties, and Tenant and persons designated by Tenant hereunder will not park in any such assigned or reserved spaces. Landlord also reserves the right to close all or any portion of the Parking Facilities on a temporary basis (as necessary) in order to make repairs or perform maintenance services, or to alter, modify, restripe or renovate the Parking Facilities, or if required by casualty, strike, condemnation, act of God, governmental law or requirement or other reason beyond Landlord's reasonable control. If, for any other reason, Tenant or persons properly designated by Tenant, are denied access to the Parking Facilities and Tenant or such persons will have complied with this Exhibit E. Landlord's liability will be limited to parking charges (excluding tickets for parking violations) incurred

---

by Tenant or such persons in utilizing alternative parking, which amount Landlord will pay upon presentation of documentation supporting Tenant's claims in connection therewith.

Landlord shall use reasonable efforts to monitor the use of reserved parking spaces by the licenses entitle to use of such, but shall have no liability whatsoever in this regard.

Default Remedies.

If Tenant defaults under this Exhibit E, Landlord will have the right to remove from the Parking Facilities any vehicles hereunder which are involved or are owned or driven by parties involved in causing such default, without liability there for whatsoever. In addition, if Tenant defaults under this Exhibit E, then, Landlord will have the right to cancel Tenant's reserved parking spaces after ten (10) days' written notice, provided Tenant does not cure such within that time period; such cancellation to continue in any event until such matter has been cured. If Tenant defaults with respect to the same term or condition under this Exhibit E, more than three (3) times during any twelve (12) month period, the next default of such term or condition, will, at Landlord's election, constitute a default of the parking arrangements and the person or persons causing such default shall no longer have access to any of the Parking Facilities.

EXHIBIT F

INTENTIONALLY DELETED

EXHIBIT G

SUBORDINATION, NON-DISTURBANCE AND ATTORNMENT AGREEMENT

THIS SUBORDINATION, NON-DISTURBANCE AND ATTORNMENT AGREEMENT (the "Agreement") is made as of the day of , 200 , by and between BANK OF TEXAS, N.A. having an address at 5956 Sherry Lane, Suite 1100, Dallas, Texas 75225 ("Lender") and SONUS NETWORKS, INC., a Delaware corporation, having an address at 1130 East Arapaho Road, Suite , Richardson, Texas 75081 ("Tenant").

RECITALS:

A. Tenant is the holder of a leasehold estate in a portion of the property described on Exhibit "A" (the "Property") under and pursuant to the provisions of a certain lease dated the day of , 2005 between PEARSON FUND III, L.P., a Texas limited partnership, as landlord, and Tenant, as tenant (the "Lease");

B. PEARSON FUND III, L.P., a Texas limited partnership ("Landlord") is the current holder of the "Landlord's" interest in the Lease;

C. The Property is or is to be encumbered by one or more mortgages, deeds of trust, deeds to secure debt or similar security agreements (collectively, the "Security Instrument") in favor of or to be assigned to Lender; and

D. Tenant has agreed to subordinate the Lease to the Security Instrument and to the lien thereof and Lender has agreed to grant non-disturbance to Tenant under the Lease on the terms and conditions hereinafter set forth.

AGREEMENT:

NOW, THEREFORE, the parties hereto mutually agree as follows:

1. Subordination. The Lease shall be subject and subordinate in all respects to the lien and terms of the Security Instrument, to any and all advances to be made there under and to all renewals, modifications, consolidations, replacements and extensions thereof.

2. Non-disturbance. So long as Tenant pays all rents and other charges as specified in the Lease and is not otherwise in default (beyond applicable notice and cure periods) of any of its obligations and covenants pursuant to the Lease, Lender agrees for itself and its successors in interest and for any purchaser of the Property upon a foreclosure of the Security Instrument, that Tenant's possession of the premises as described in the Lease will not be disturbed during the term of the Lease, as said term may be extended pursuant to the terms of the Lease or as said premises may be expanded as specified in the Lease, by reason of a foreclosure. For purposes of this agreement, a "foreclosure" shall include (but not be limited to) a sheriff's or trustee's sale under the power of sale contained in the Security Instrument, the termination of any superior lease of the Property and any other transfer of the Landlord's interest in the Property under peril of foreclosure, including, without limitation to the generality of the foregoing, an assignment or sale in lieu of foreclosure.

3. Attornment. Tenant agrees to attorn to, accept and recognize any person or entity which acquires the Property through a foreclosure (an "Acquiring Party") as the landlord under the Lease for the then remaining balance of the term of the Lease, and any extensions thereof as made pursuant to the Lease. The foregoing provision shall be self-operative and shall not require the execution of any further instrument or agreement by Tenant as a condition to its effectiveness. Tenant agrees, however, to execute and deliver, at any time and from time to time, upon the request of the Lender or any Acquiring Party any reasonable instrument which may be necessary or appropriate to evidence such attornment.

---

4. No Liability. Notwithstanding anything to the contrary contained herein or in the Lease, it is specifically understood and agreed that neither the Lender, any receiver or any Acquiring Party shall be:

(a) liable for any act, omission, negligence or default of any prior landlord (other than to cure defaults of a continuing nature with respect to the maintenance or repair of the demised premises or the Property); provided, however, that any Acquiring Party shall be liable and responsible for the performance of all covenants and obligations of landlord under the Lease accruing from and after the date that it takes title to the Property; or
(b) except as set forth in (a), above, liable for any failure of any prior landlord to construct any improvements;
(c) subject to any offsets, credits, claims or defenses which Tenant might have against any prior landlord; or
(d) bound by any rent or additional rent which is payable on a monthly basis and which Tenant might have paid for more than one (1) month in advance to any prior landlord;
(e) bound by any cancellation, surrender, amendment or modification of the Lease or release of liability thereunder not expressly consented to in writing by Lender or otherwise permitted by the Security Instrument in each instance, except, for those cancellations, surrenders, amendments or modifications contemplated in the Lease or permitted to be made without Lender's consent pursuant to the terms of the loan documents between Lender and Landlord, or
(f) be liable to Tenant hereunder or under the terms of the Lease beyond its interest in the Property.

Notwithstanding the foregoing, Tenant reserves its rights to any and all claims or causes of action against such prior landlord for prior losses or damages and against the successor landlord for all losses or damages arising from and after the date that such successor landlord takes title to the Property.

5. Rent. Tenant has notice that the Lease and the rents and all other sums due thereunder have been assigned in writing to Lender as security for the loan secured by the Security Instrument. In the event Lender notifies Tenant of the occurrence of a default under the Security Instrument and demands that Tenant pay its rents and all other sums due or to become due under the Lease directly to Lender, Tenant shall honor such demand and pay its rent and all other sums due under the Lease directly to Lender or as otherwise authorized in writing by Lender. Landlord hereby irrevocably authorizes Tenant to make the foregoing payments to Lender upon such notice and demand.

6. Lender to Receive Notices. Tenant shall notify Lender of any default by Landlord under the Lease which would entitle Tenant to cancel the Lease, and agrees that, notwithstanding any provisions of the Lease to the contrary, no notice of cancellation thereof shall be effective unless Lender shall have received notice of default giving rise to such cancellation and shall have failed within thirty (30) days after receipt of such notice to cure such default, or if such default cannot be cured within thirty (30) days, shall have failed within thirty (30) days after receipt of such notice to commence and thereafter diligently pursue any action necessary to cure such default.

7. NOTICES. All notices or other written communications hereunder shall be deemed to have been properly given (i) upon delivery, if delivered in person with receipt acknowledged by the recipient thereof, (ii) one (1) Business Day (hereinafter defined) after having been deposited for overnight delivery with any reputable overnight courier service, or (iii) three (3) Business Days after having been deposited in any post office or mail depository regularly maintained by the U.S. Postal Service and sent by registered or certified mail, postage prepaid, return receipt requested, addressed to the receiving party at its address set forth above, and:

if to Tenant:

Sonus Networks, Inc.
1130 East Arapaho Road, Suite 200
Richardson, Texas 75081
Attn:
Telephone:
Fax:

---

with a copy to:

Sonus Networks, Inc.
250 Apollo Drive
Chelmsford, MA 01824
Attn:
Telephone:
Fax:

if to Lender:

Bank of Texas, NA
5956 Sherry Lane, Suite 1100
Dallas, Texas 75225
Attn: Kimberly (Kim) W. Kittle, Vice President
kkittle@mail.bokf.com
Telephone: 214.987.8842 direct
Fax:

or addressed as such party may from time to time designate by written notice to the other parties. Either party by notice to the other may designate additional or different addresses for subsequent notices or communications. For purposes of this Section 7, the term "Business Day" shall mean any day other than Saturday, Sunday or any other day on which banks are required or authorized to close in Dallas County, Texas. Either party by notice to the other may designate additional or different addresses for subsequent notices or communications.

8. Successors. The obligations and rights of the parties pursuant to this Agreement shall bind and inure to the benefit of the successors, assigns, heirs and legal representatives of the respective parties.

9. Duplicate Originals; Counterparts. This Agreement may be executed in any number of duplicate originals and each duplicate original shall be deemed to be an original. This Agreement may be executed in several counterparts, each of which counterparts shall be deemed an original instrument and all of which together shall constitute a single agreement.

10. Transfer of Loan/Servicing. Lender may sell, transfer and deliver the Note and assign the Security Instrument, this Agreement and the other documents executed in connection therewith to one or more Investors (as defined in the Security Instrument) in the secondary mortgage market or otherwise. Lender may also retain or assign responsibility for servicing the loan evidenced by the Note, or may delegate some or all of such responsibility and/or obligations to a servicer including, but not limited to, any subservicer or master servicer, on behalf of the Investors. All references to Lender herein shall refer to and include any such servicer to the extent applicable. Lender may disclose the terms of this Agreement, the identity of Tenant or any principal of Tenant, or any financial information regarding Tenant or any principal of Tenant, to any Investor or potential Investor.

IN WITNESS WHEREOF, Lender, Landlord and Tenant have duly executed this Agreement as of the date first above written.

LENDER:

By: _____
Its: _____

STATE OF)
) ss.
COUNTY OF)

On the day of , in the year 200 , before me, the undersigned, a Notary Public in and for said State, personally appeared , personally known to me or proved to me on the basis of satisfactory evidence to be the individual whose name is subscribed to the within instrument and acknowledged to me that said person executed the same in said person's capacity as of , and that by said person's signature on the instrument, said corporation executed the instrument.

_____
Notary Public

TENANT:

By: _____

Its: _____

STATE OF TEXAS)
) ss.
COUNTY OF)

The foregoing instrument was acknowledged before me this day of , 2005, by the of , a , on behalf of the .

_____
Notary Public

My Commission Expires:

_____

The undersigned accepts and agrees to
the provisions of Section 5 hereof:

LANDLORD:

By: _____

Its: _____

STATE OF TEXAS)
) ss.
COUNTY OF)

This instrument was acknowledged before me this day of , 2005, by ..

My commission expires:

_____
Notary Public

_____

(Seal)

EXHIBIT A
to SNDA

LEGAL DESCRIPTION

EXHIBIT H

INTENTIONALLY DELETED

EXHIBIT I

JANITORIAL SPECIFICATIONS

CLEANING SPECIFICATIONS

Cleaning services are to be provided five (5) days a week unless otherwise specified. Cleaning hours are Sunday through Thursday between 6:00 p.m. and before 7:00 a.m. The cleaning specifications are as follows:

I. OFFICE AREAS

A. Daily

1. Dust and wipe clean all furniture, fixtures, shelving, and cabinets. Note: Desks with loose papers on the top will not be cleaned.
2. Spot clean all vertical desk surfaces.
3. Office wastepaper will be emptied. Liners will be replaced as required.
4. Vacuum carpet in offices as needed; moving light furniture other than desks, file cabinets, etc. Remove any spot on carpet, when possible.
5. Dust and spot mop all resilient tile floor areas. All floor edges will be damp mopped.
6. All telephones will be cleaned and sanitized, if possible.
7. Spot clean all surfaces and columns. All glass partitions will be spot cleaned.
8. Wipe metal door knobs, light switch plates, mirrors, kick plates, door saddles and directional signs.
9. Vacuum all traffic areas daily.

B. Weekly

1. Dust and clean all paneling, door frame, ornamental work, grilles, ventilating louvers, baseboards and entire doors.
2. Dust all mini-blinds

C. Monthly

1. Complete all high dusting.
2. Dust and wipe clean all air diffusers and ceiling ventilators.

3. Resilient tile floors will be buffed.

II. RESTROOMS

A. Daily

1. Restroom floors are to be swept and washed with disinfectant.
2. Basins, toilets bowls and urinals are to be washed and disinfected.
3. Clean and disinfect both sides of every toilet seat.
4. Mirrors, shelves, plumbing work, bright work, and enamel surfaces will be wiped down.
5. Remove spots, stains, splashes from all wall areas, doors, door frames, light switches, etc.
6. Waste receptacles will be emptied and cleaned. Soap, toilet, paper, toilet seat cover, towel, and sanitary napkin/tampon dispensers will he filled.
7. Tile walls and dividing partitions will be spot cleaned.
8. Dust top of all toilet partitions.

B. Weekly

1. Tile walls and dividing partitions will be washed and disinfected thoroughly.

---

2. Resilient tile floors will be buffed twice per month.

C. Monthly

1. Thoroughly scrub floors. Pay special attention to corners and edges, base of walls and grouting.

III. COMMON AREAS, KITCHEN AREA, BREAK AREA

A. Daily

1. All hard surface floors are to be swept and/or dust mopped with dust control treated mops or other effective tools, and left clean and free of dust (includes cove base and/or carpet caps).
2. Carpets are to be vacuumed and spot cleaned.
3. Main lobby floors are to be wiped and washed.
4. Spot clean all walls where possible, dust floor to ceiling as needed.
5. Clean entrance glass. Clean entrance doors. Polish thresh plates.
6. Clean directory board.
7. Waste receptacles are to be emptied.
8. All water fountains are to be sanitized and polished.
9. Lobby furniture is to be dusted and vacuumed.
10. Stairwell is to be swept and mopped.
11. All interior glass is to be spot cleaned.
12. All table tops, counters and sinks in kitchen and break area will be cleaned. Vending machines and ice makers will be wiped clean with a damp cloth.

B. Weekly

1. Dust and clean all paneling, ornamental work, grilles, ventilating louvers, baseboards and entire doors.
2. Resilient tile floors will be buffed twice per month.

C. Monthly

1. Complete all high dusting.
2. Dust and wipe clean all air diffusers and ceiling ventilators.

D. Quarterly

1. Scrub and refinish all resilient tile floor areas.

E. Semi-Annually

1. Strip and refinish all resilient floor areas.

EXHIBIT 31.1

CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Hassan M. Ahmed, Chief Executive Officer and Chairman of the Board of Directors, of Sonus Networks, Inc., certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the period ended September 30, 2005 ("Quarterly Report") of Sonus Networks, Inc. (the "Registrant");

2. Based on my knowledge, this Quarterly Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Quarterly Report;

3. Based on my knowledge, the financial statements, and other financial information included in this Quarterly Report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this Quarterly Report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Quarterly Report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this Quarterly Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Quarterly Report based on such evaluation; and

   (d) Disclosed in this Quarterly Report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors:

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: November 8, 2005

/s/ HASSAN M. AHMED
Hassan M. Ahmed
Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)

EXHIBIT 31.2

CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Ellen B. Richstone, Chief Financial Officer, of Sonus Networks, Inc., certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the period ended September 30, 2005 ("Quarterly Report") of Sonus Networks, Inc. (the "Registrant");

2. Based on my knowledge, this Quarterly Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Quarterly Report;

3. Based on my knowledge, the financial statements, and other financial information included in this Quarterly Report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this Quarterly Report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Quarterly Report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this Quarterly Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Quarterly Report based on such evaluation; and

   (d) Disclosed in this Quarterly Report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors:

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: November 8, 2005

/s/ ELLEN B. RICHSTONE
Ellen B. Richstone
Chief Financial Officer
(Principal Financial Officer)

EXHIBIT 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Sonus Networks, Inc. (the "Company") for the period ended September 30, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Hassan M. Ahmed, Chief Executive Officer and Chairman of the Board of Directors of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 8, 2005

/s/ HASSAN M. AHMED
Hassan M. Ahmed
Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)

EXHIBIT 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Sonus Networks, Inc. (the "Company") for the period ended September 30, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Ellen B. Richstone, Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 8, 2005

/s/ ELLEN B. RICHSTONE

Ellen B. Richstone
Chief Financial Officer
(Principal Financial Officer)