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

FORM 10-Q

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

For the quarterly period ended March 31, 2006

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

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 a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer x Accelerated filer o Non-accelerated filer o

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

As of April 30, 2006, there were 252,505,040 shares of $0.001 par value per share, common stock outstanding.

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PART I—FINANCIAL INFORMATION

Item 1: Financial Statements

SONUS NETWORKS, INC.

Condensed Consolidated Balance Sheets

(In thousands, except share data)

(unaudited)

	March 31, 2006	December 31, 2005
Assets		
Current assets:		
Cash and cash equivalents	$ 50,309	$ 155,679
Marketable debt securities	239,312	140,569
Accounts receivable, net	33,272	72,321
Inventory, net	37,169	37,831
Other current assets	15,197	15,833
Deferred income taxes	519	519
Total current assets	375,778	422,752
Property and equipment, net	15,315	15,181
Long-term investments	50,616	17,993
Other assets	1,878	631
	$ 443,587	$ 456,557
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 16,370	$ 20,408
Accrued expenses	19,384	23,204
Accrued restructuring expenses	198	195
Current portion of deferred revenue	73,209	88,199
Current portion of long-term liabilities	49	48
Convertible subordinated note	10,000	10,000
Total current liabilities	119,210	142,054
Long-term deferred revenue, net of current portion	28,990	33,853
Long-term liabilities, net of current portion	422	485
Total liabilities	148,622	176,392
Commitments and contingencies (Note 4)	—	—
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, 253,670,005 and 251,730,706 shares issued and 251,373,095 and 249,433,796 shares outstanding at March 31, 2006 and December 31, 2005	254	252
Capital in excess of par value	1,064,989	1,055,941
Accumulated deficit	(769,973)	(775,717)
Accumulated other comprehensive loss	(38)	(44)
Treasury stock, at cost; 2,296,910 common shares at March 31, 2006 and December 31, 2005	(267)	(267)
Total stockholders' equity	294,965	280,165
	$ 443,587	$ 456,557

See notes to the condensed consolidated financial statements.

SONUS NETWORKS, INC.

Condensed Consolidated Statements of Operations

(In thousands, except per share data)

(unaudited)

	Three months ended March 31, 2006	Three months ended March 31, 2005
Revenues:		
Product	$ 44,383	$ 22,458
Service	15,589	11,152
Total revenues	59,972	33,610
Cost of revenues:		
Product	15,853	6,843
Service	7,381	5,269
Total cost of revenues	23,234	12,112

Gross profit	36,738	21,498
Operating expenses:		
Research and development	12,891	11,017
Sales and marketing	13,898	9,027
General and administrative	6,719	6,800
Total operating expenses	33,508	26,844
Income (loss) from operations	3,230	(5,346)
Interest expense	(137)	(128)
Interest income	3,442	1,875
Income (loss) before income taxes	6,535	(3,599)
Provision for income taxes	791	96
Net income (loss)	$ 5,744	$ (3,695)
Net income (loss) per share:		
Basic and diluted	$ 0.02	$ (0.01)
Shares used in computing net income (loss) per share:		
Basic	250,064	247,877
Diluted	254,459	247,877

See notes to the condensed consolidated financial statements.

SONUS NETWORKS, INC.

Condensed Consolidated Statements of Cash Flows

(In thousands)

(unaudited)

	Three months ended March 31, 2006	2005
Cash flows from operating activities:		
Net income (loss)	$ 5,744	$ (3,695)
Adjustments to reconcile net income (loss) to cash flows provided by (used in) operating activities:.		
Depreciation	2,293	1,476
Stock-based compensation	1,903	—
Loss of disposal of property and equipment	6	—
Changes in operating assets and liabilities:		
Accounts receivable	39,071	4,855
Inventory	713	(2,910)
Other operating assets	(857)	(762)
Accounts payable	(4,072)	1,334
Accrued expenses and accrued restructuring expenses	(3,926)	(1,330)
Deferred revenue	(19,920)	948
Net cash provided by (used in) operating activities	20,955	(84)
Cash flows from investing activities:		
Purchases of property and equipment	(2,328)	(4,303)
Maturities of available-for-sale marketable debt securities	25,500	26,700
Purchases of available-for-sale marketable debt securities	(12,825)	(31,601)
Maturities of held-to-maturity marketable debt securities and long-term investments	22,950	8,921
Purchases of held-to-maturity marketable debt securities and long-term investments	(166,991)	(1,043)
Decrease in restricted cash	250	—
Other assets	85	(81)
Net cash used in investing activities	(133,359)	(1,407)
Cash flows from financing activities:		
Sale of common stock in connection with employee stock purchase plan	2,311	2,313
Proceeds from exercise of stock options	4,821	420
Payments of long-term liabilities	(12)	(58)
Net cash provided by financing activities	7,120	2,675
Effect of exchange rate changes on cash and cash equivalents	(86)	—
Net (decrease) increase in cash and cash equivalents	(105,370)	1,184
Cash and cash equivalents, beginning of period	155,679	121,931
Cash and cash equivalents, end of period	$ 50,309	$ 123,115
Supplemental disclosure of cash flow information:		
Interest paid	$ 12	$ 2
Income taxes paid	$ 905	$ 551
Non-cash purchases of property and equipment	$ 1,081	$ 1,582
Property and equipment acquired as part of a facility lease	$ 50	$ —
Property and equipment acquired under capital lease	$ —	$ 101

See notes to the condensed consolidated financial statements.

SONUS NETWORKS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

(1) Description of Business

Sonus Networks, Inc. (Sonus) was incorporated in August 1997 and is a leading provider of voice infrastructure solutions for wireline and wireless service providers. Sonus offers a new generation of carrier-class switching equipment and software that enable voice services to be delivered 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, 2005.

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

The presentation of transactions in marketable debt securities in the condensed consolidated statement of cash flows for the three months ended March 31, 2005 has been adjusted to conform to the presentation for the three months ended March 31, 2006.

(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, actual results may differ. 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, estimated commissions expense, assumptions for recorded stock-based compensation and recoverability of Sonus' net deferred tax assets and related valuation allowance. Although Sonus regularly assesses these estimates, actual results could differ

SONUS NETWORKS, INC.

Notes to Condensed Consolidated Financial Statements (Continued)

(unaudited)

(2) Summary of Significant Accounting Policies (Continued)

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 circumstances.

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

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

Cash equivalents and marketable debt securities consist of 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 the periods presented. The unrealized losses related to these securities at March 31, 2006 are not considered to be a permanent decline in the fair 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 as of the balance sheet date 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 include held-to-maturity investments with remaining maturities of one to five years as of the balance sheet date.

As of March 31, 2006 and December 31, 2005, marketable debt securities consisted of the following, in thousands:

	March 31, 2006			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Marketable debt securities				
Available-for-sale:				
State and municipal obligations	$ 85,200	$ —	$ —	$ 85,200
Held-to-maturity:				
U.S. government agency notes	65,670	—	(161)	65,509
Corporate debt securities	16,176	—	(54)	16,122
Commercial paper	70,368	—	(209)	70,159
Certificates of deposit	1,898	—	(4)	1,894
	$ 239,312	$ —	$ (428)	$ 238,884
Long-term investments				
Held-to-maturity:				
U.S. government agency notes	$ 41,035	$ —	$ (170)	$ 40,865
Corporate debt securities	9,581	—	(61)	9,520
	$ 50,616	$ —	$ (231)	$ 50,385

(2) Summary of Significant Accounting Policies (Continued)

	December 31, 2005			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Marketable debt securities				
Available-for-sale:				
State and municipal obligations	$ 97,875	$ —	$ —	$ 97,875
Held-to-maturity:				
U.S. government agency notes	16,643	—	(88)	16,555
Corporate debt securities	18,503	—	(79)	18,424
Commercial paper	5,950	—	(13)	5,937
Certificates of deposit	1,598		(4)	1,594
	$ 140,569	$ —	$ (184)	$ 140,385
Long-term investments				
Held-to-maturity:				
U.S. government agency notes	$ 17,993	$ —	$ (48)	$ 17,945

As of March 31, 2006, Sonus had $341,000 in restricted cash, which is used to collateralize standby letters of credit. Restricted cash is included in other current assets on the 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 debt securities, accounts receivable and long-term investments. Sonus' cash, cash equivalents and investment portfolio holdings were diversified among five financial institutions at March 31, 2006. Beginning in 2005, Sonus entered into foreign exchange contracts to hedge against currency fluctuations related to a particular account receivable and orders denominated in Japanese Yen. Sonus records changes in fair value of foreign exchange contracts to general and administrative expenses in the condensed consolidated statement of operations, which totaled a gain of $10,000 for the three months ended March 31, 2006.

The following customers contributed 10% or more of Sonus' revenues for the three months ended March 31, 2006 and 2005:

Customer	2006	2005
A	18%	15%
B	12	25
C	11	*

* Represents less than 10% of revenues.

As of March 31, 2006 and December 31, 2005, two customers each accounted for 10% or more of Sonus' accounts receivable balance, representing an aggregate of 25% and 43% of the accounts receivable balance, respectively. Sonus performs ongoing credit evaluations of its customers and generally does not require collateral on accounts receivable. Sonus maintains an allowance for potential doubtful accounts and such losses have been within management's expectations.

(2) Summary of Significant Accounting Policies (Continued)

The following table shows percentage of revenue by region for the three months ended March 31, 2006 and 2005:

	2006	2005
United States	77%	81%
Japan	11	9
Other Asia Pacific	9	4
Europe, Middle East and Africa	3	5
Other	—	1
	100%	100%

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:

	March 31, 2006	December 31, 2005
Earned accounts receivable	$ 20,562	$ 48,924
Unearned accounts receivable	13,307	23,823
Accounts receivable, gross	33,869	72,747
Allowance for doubtful accounts	(597)	(426)
Accounts receivable, net	$ 33,272	$ 72,321

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.

(2) Summary of Significant Accounting Policies (Continued)

(f) Inventory

Inventory consists of the following, in thousands:

	March 31, 2006	December 31, 2005
On-hand final assemblies and finished goods inventory	$ 21,032	$ 19,457
Deferred cost of sales	18,823	21,110
Evaluation inventory	4,693	4,615
Inventory, gross	44,548	45,182
Excess, obsolete and evaluation reserve	(7,379)	(7,351)
Inventory, net	$ 37,169	$ 37,831

Deferred cost of sales inventory represents deferred cost of revenues prior to satisfaction of Sonus' revenue recognition criteria.

Sonus values inventory at the lower of cost or net realizable 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 its customers as a charge to sales and marketing expense as it is probable that the inventory will not be realizable. If these evaluation shipments are later purchased by Sonus' customers, Sonus reclassifies amounts previously charged to sales and marketing expenses to cost of revenues in the period when all revenue recognition criteria are met.

(g) Property and Equipment

Property and equipment are stated at cost, net of accumulated depreciation. Expenditures for maintenance and repairs are charged to expense as incurred. Depreciation is computed using the straight-line method over the estimated useful life of the related assets, which range from two to five years. Leasehold improvements are amortized over the lesser of the lease term or five years. When an item is sold or retired, the cost and related accumulated depreciation or amortization is eliminated, and the resulting gain or loss, if any, is recognized in income (loss) from operations in the consolidated statement of operations.

(h) Deferred Revenue

Deferred revenue consists of the following, in thousands:

	March 31, 2006	December 31, 2005
Maintenance and support contracts	$ 59,927	$ 67,277
Customer deposits	28,965	30,952
Unearned revenue	13,307	23,823
Total deferred revenue	102,199	122,052
Less current portion	(73,209)	(88,199)
Long-term deferred revenue	$ 28,990	$ 33,853

(2) Summary of Significant Accounting Policies (Continued)

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 March 31, 2006 and December 31, 2005, deferred revenue and accounts receivable excluded $15.3 million and $5.3 million related to products shipped and billed to customers which are collectible under extended payment terms, for which revenue is recognized as cash is collected, or for which title had not passed to the customer as of the period end date.

(k) Revenue Recognition

Sonus' products are primarily marketed based on the software elements contained therein. In addition, hardware sold generally can not be used apart from the software. Therefore, the Company considers its principal products to be software related. 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 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. Earned maintenance revenues are typically deferred until the associated product revenue is accepted and all other revenue recognition are met. 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 completed.

(2) Summary of Significant Accounting Policies (Continued)

Sonus sells the majority of its products directly to its service provider customers. For products sold to resellers and distributors, Sonus generally recognizes revenue on a sell-through basis utilizing information provided to Sonus from its resellers and distributors. Through December 31, 2005, no revenues had been recognized on a sell-in basis due to the limited return history associated with shipments to resellers and distributors. During the three months ended March 31, 2006, Sonus began reporting revenue from its original equipment manufacturer (OEM) relationship with Motorola, Inc. on a sell-in basis where revenue is recognized upon the shipment of products to Motorola, assuming all other requirements for revenue recognition have been met. Sonus had previously recognized revenue for sales to Motorola when products had been sold through by Motorola to its customers. This change reflects the two years of history with Motorola during which Sonus has experienced no returns, no price concessions and an excellent payment history. As a result of this history, Sonus has determined that the risk of a potential price concession has been eliminated and therefore the price for products sold to Motorola is now fixed or determinable upon sale to Motorola. In the three months ended March 31, 2006, Sonus recognized revenue totaling approximately $3.0 million in connection with sales of products to Motorola through March 31, 2006 that had not yet sold through to Motorola's customers. This revenue would have been recognized in subsequent quarters if the Company had not changed to a sell-in basis for Motorola during the first quarter. This additional revenue from Motorola in the quarter negatively affected product gross margins during the first quarter as revenue from OEM relationships typically have lower margin profiles than revenue from direct sales to customers. This additional revenue resulted in approximately $1.0 million of additional net income in the quarter, but did not change reported basic and diluted earnings per share.

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 revenue includes customer deposits and amounts associated with maintenance contracts. Deferred revenue expected to be recognized as revenue more than one year subsequent to the balance sheet date is classified as long-term deferred revenue.

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.

(l) Stock-based Compensation

Sonus issues stock options and provides employees the right to purchase stock pursuant to the 1997 Stock Incentive Plan (Stock Plan) and the 2000 Employee Stock Purchase Plan (ESPP Plan). Effective January 1, 2006, Sonus adopted the provisions of SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS No. 123R). Prior to January 1, 2006, Sonus followed Accounting Principles Board Opinion 25, *Accounting for Stock Issued to Employees*, and related interpretations in accounting for its employee stock-based compensation.

Stock options are generally issued at the current market price on the date of grant with a four-year vesting period and contractual term of ten years. Under the provisions of SFAS No. 123R, Sonus recognizes the fair value of stock compensation in its consolidated financial statements over the requisite service period, which generally equals the vesting period, on a straight-line single option approach. Sonus includes as part of its inventory a portion of the fair value of stock compensation, which is expensed as inventory is relieved, generally over six months. All of Sonus' stock-based compensation is accounted for as

(2) Summary of Significant Accounting Policies (Continued)

an equity instrument and there have been no liability awards granted. The Company's policy is to issue new shares upon exercise of stock options.

Sonus has elected the modified prospective transition method for adopting SFAS No. 123R. Under this method, the provisions of SFAS No. 123R apply to all awards granted or modified after the date of adoption. The unrecognized expense of awards not yet vested at the date of adoption shall be recognized in net income in the periods after the date of adoption using the same valuation method, Black-Scholes, and assumptions determined under the original provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*. Sonus recorded $1.9 million of stock-based compensation in the condensed consolidated statement of operations for the three months ended March 31, 2006 in the following expense categories (in thousands):

Product cost of revenues	$ 3
Service cost of revenues	252
Research and development	610
Sales and marketing	405
General and administrative	633
	$ 1,903

In addition, Sonus included in inventory approximately $16,000 of stock-based compensation at March 31, 2006.

The recording of stock-based compensation expense for the three months ended March 31, 2006 in the condensed consolidated statement of operations resulted in a decrease in net income of $1.9 million and in basic and diluted earnings per share of $0.01, while in the condensed consolidated statement of cash flows for the three months ended March 31, 2006 cash flows from operating activities increased $1.9 million with no impact to cash flows from financing activities.

Sonus utilized the Black-Scholes valuation model for estimating the fair value on the date of grant of employee stock options granted after the adoption of SFAS No. 123R using the following assumptions for the three months ended March 31, 2006:

Risk-free interest rate	4.6%
Expectant dividend yield.	0.0%
Expected volatility	85%
Expected life (years)	4.5

The risk-free interest rate is the average U.S. Treasury Constant Maturities Rate for the expected term. The expectant dividend yield of zero is based on the fact that Sonus has never paid dividends and has no present intention to pay cash dividends. Expected volatility is based on a combination of the historical volatility of Sonus' common stock over the option's expected life and estimated volatility on option contracts traded in the open market. Prior to January 1, 2006, Sonus used historical volatility to estimate the grant-date fair value of stock options. Starting on January 1, 2006, Sonus changed its method to a combination of historical and implied volatility. Sonus believes that a combination of historical and

(2) Summary of Significant Accounting Policies (Continued)

implied volatility results in a more accurate estimate of the grant-date fair value of employee stock options because it more appropriately reflects the market's expectations of future volatility. Historical volatility during the period associated with the expected term of the Company's stock options over the past few years included a period of time during or subsequent to Sonus' initial public offering when its stock price experienced abnormally high volatility levels, which Sonus believes is unlikely to be indicative of future stock price behavior. However, Sonus has not placed sole reliance on implied volatility as options in its common stock that are actively traded on the open market currently have a term of less than one year - substantially shorter than its stock option's expected term. The expected life is based on a combination of exercise patterns of the option holder over the option's life and exercise patterns within similar industries. Sonus estimates forfeitures to occur at a rate of 5% per year.

The following table summarizes information relating to Stock Plan activity during the three months ended March 31, 2006:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at January 1, 2006	45,333,532	$ 4.74		
Granted	1,998,350	4.80		
Exercised	(1,359,769)	3.55		
Forfeited	(127,000)	4.00		
Expired	(205,817)	6.75		
Outstanding at March 31, 2006	45,639,296	$ 4.78	7.17	$ 47,919
Vested or expected to vest at March 31, 2006	45,314,098	$ 4.78	7.15	$ 47,582
Exercisable at March 31, 2006	41,241,100	$ 4.83	6.97	$ 42,625

The weighted average fair value of stock options granted during the three months ended March 31, 2006 was $3.31. The total intrinsic value of options exercised during the three months ended March 31, 2006 and 2005 was $2.1 million and $0.2 million, respectively. The total fair value of options vested during the three months ended March 31, 2006 and 2005 was $1.7 million and $8.0 million, respectively. As of March 31, 2006, there was $12.9 million of unrecognized compensation cost related to options, which is expected to be recognized over a weighted average period of 3.0 years.

For shares purchased under the ESPP Plan, Sonus utilized the Black-Scholes model, with a range for a majority of assumptions for the three months ended March 31, 2006. In valuing the ESPP Plan, Sonus used an assumed risk-free interest rate of 1.8%-4.8%, expected volatility of 56%-126%, an expected life of six months to two years and a zero expectant dividend yield.

(2) Summary of Significant Accounting Policies (Continued)

SFAS No. 123R requires the presentation of pro forma information for the comparative period prior to the adoption as if Sonus had accounted for stock-based compensation expense under the fair value method under SFAS No. 123. The following table shows Sonus' pro forma net loss and net loss per share as if accounted for under SFAS No. 123 for the three months ended March 31, 2005, in thousands except per share data:

Net loss as reported	$ (3,695)
Less: Employee stock-based compensation under fair value method	(10,391)
Pro forma net loss	$ (14,086)
Basic and diluted net loss per share—	
As reported	$ (0.01)
Pro forma	$ (0.06)

Sonus utilized the Black-Scholes valuation model for estimating the fair value of employee stock options granted for during the three months ended March 31, 2005 using the following assumptions:

Risk-free interest rate	3.9%
Expectant dividend yield.	0.0%
Expected volatility	122%
Expected life (years)	4.0

The weighted average fair value of stock options granted during the three months ended March 31, 2005 was $3.85.

For shares purchased under the ESPP Plan during the three months ended March 31, 2005, Sonus utilized the Black-Scholes model, with an assumed risk-free interest rate of 1.3%-2.1%, expected volatility of 72%-154%, an expected life of six months to two years and a zero expectant dividend yield.

(m) Comprehensive Net Income (Loss)

The following table shows Sonus' comprehensive net income (loss) for the three months ended March 31, 2006 and 2005 in thousands:

	2006	2005
Net income (loss).	$ 5,744	$ (3,695)
Foreign currency translation adjustments	6	—
Comprehensive income (loss)	$ 5,750	$ (3,695)

(n) Disclosures about Segments of an Enterprise

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

(2) Summary of Significant Accounting Policies (Continued)

regarding resource allocation and assessing performance. To date, the chief operating decision maker has made such decisions and assessed performance at the company level.

(o) Net Income (Loss) Per Share

Dilutive potential common shares consist of common stock issuable upon the exercise of stock options and conversion of a convertible subordinated note.

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

	Three months ended March 31,	
	2006	2005
Weighted average shares used in computing basic per share calculation	250,064	247,877
Add effect of dilutive potential common shares	4,395	—
Weighted average shares used in computing diluted per share calculation	254,459	247,877

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 20,399,453 shares as of March 31, 2006 as their effect would have been anti-dilutive.

(p) Warranty Reserve

Sonus' 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. 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 warranty obligations 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. As of March 31, 2006 and December 31, 2005, Sonus had $45,000 and $84,000 of warranty reserves recorded, respectively.

(2) Summary of Significant Accounting Policies (Continued)

(q) Income Taxes

Sonus provides for income taxes during interim periods based on the estimated effective tax rate for the full fiscal year. Sonus records cumulative adjustments to the tax provision in an interim period in which a change in the estimated annual effective rate is determined.

(3) Accrued Restructuring Expenses

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.

2002 Restructuring Accrual

The following table summarizes the activity during the three months ended March 31, 2006 relating to Sonus' accrual for fiscal 2002 restructuring actions, in thousands:

	December 31, 2005 Accrual Balance	Cash Payments	March 31, 2006 Accrual Balance	Current Portion	Long-term Portion
Consolidation of facilities	$ 613	$ (47)	$ 566	$ 198	$ 368

The remaining cash payments 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 our 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

(4) Contingencies (Continued)

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 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. On April 24, 2006, the court held a hearing on a motion to approve the final settlement and took the matter under advisement. As the settlement would not require any payment by Sonus, 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 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 opposed the motion. No hearing date has been scheduled.

On January 6, 2006, a purchaser of Sonus' common stock filed a complaint in the United States District Court for the District of Massachusetts that is essentially identical to the Consolidated Amended Complaint previously filed against the defendants. Three shareholders have filed motions seeking appointment as lead plaintiff. The court has not yet ruled on these motions. Following the appointment of a lead plaintiff, the defendants intend to file a motion to dismiss the complaint. There is no assurance Sonus will prevail in such a motion or defending this action. A judgment or a settlement of the claims

SONUS NETWORKS, INC.

Notes to Condensed Consolidated Financial Statements (Continued)

(unaudited)

(4) Contingencies (Continued)

against the defendants could have a material impact on Sonus' financial results. It is too early to determine the ultimate outcome or potential range of loss, if any.

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 our revenues, earnings, and financial position. 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. On December 10, 2005, the court held a hearing on the motions and took the matter under advisement. Sonus believes that it has substantial legal and factual defenses to the claims, which it intends to pursue vigorously. Sonus does not expect that this claim will have a material impact on its financial statements.

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 Sonus. 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 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, the case was dismissed 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. On December 10, 2005, the court held a hearing on the motions and took the matter under advisement. On March 31, 2006, the court entered an order granting the defendants' motions and dismissing the amended complaint. On April 26, 2006, the plaintiffs filed a notice of appeal of the dismissal order. Sonus does not expect that this claim will have a material impact on its financial statements.

SONUS NETWORKS, INC.

Notes to Condensed Consolidated Financial Statements (Continued)

(unaudited)

(4) Contingencies (Continued)

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 it dismissed the federal claims without prejudice and dismissed the state claims without prejudice. On November 23, 2005, the plaintiff filed a second amended complaint with essentially the same allegations as in the prior complaints. The defendants renewed their motions to dismiss with respect to the second amended complaint. On March 9, 2006, the court held a hearing on the defendants' motions during which the court entered an order dismissing the second amended complaint with prejudice. On April 17, 2006, the plaintiff filed a notice of appeal of the dismissal order. 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 "Risk Factors" in this 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, 2005, 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. Our voice solutions allow wireline and wireless operators to build converged voice over IP networks based on the same principles as the IP Multimedia Subsystem (IMS) architecture, which network operators globally are embracing as the common standard for constructing next generation networks.

Starting in 2004 and continuing into 2006, there has been increased interest and activity in the market for packet-based voice infrastructure products. This trend has been reflected in our order activity as we achieved record orders in the fourth quarter of fiscal 2004 and on an annual basis in fiscal 2005. Customer orders were less than revenue for the three months ended March 31, 2006 due to the seasonally slower period for customer order activity and the strong revenue for the quarter. 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. For the three months ended March 31, 2006, revenues were $60.0 million compared to $33.6 million in the same period in fiscal 2005, reflecting continuing improvements in the market for packet-based voice infrastructure products, as well as increased service revenues resulting from the growing installed base of our products.

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. We believe 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 tend to sporadically 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.

Since our inception through December 31, 2003, we have incurred significant losses. As of March 31, 2006, we had an accumulated deficit of $770.0 million. Although we achieved profitability in the first quarter of 2006 and on an annual basis in fiscal years 2005 and 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. 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 position and results of operations is based upon our condensed 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, royalty, litigation, and other loss contingency reserves,
- Stock-based compensation, and
- Accounting for income taxes.

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 service period, ranging from one to five years. Earned maintenance revenues are typically deferred until the associated product revenue is accepted and all other revenue recognition criteria are met. 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 completed.

We sell the majority of our products directly to our service provider customers. For products sold to resellers and distributors, we recognize revenue on a sell-through basis utilizing information provided to us from our resellers and distributors. Through December 31, 2005, no revenues had been recognized on a sell-in basis due to the limited return history associated with shipments to resellers and distributors. During the three months ended March 31, 2006, we began reporting revenue from our original equipment manufacturer (OEM) relationship with Motorola, Inc. on a sell-in basis where revenue is recognized upon the shipment of products to Motorola, assuming all other requirements for revenue recognition have been met. We had previously recognized revenue for sales to Motorola when products had been sold through by Motorola to its customers. This change reflects the two years of history with Motorola during which we have experienced no returns, no price concessions and an excellent payment history. As a result of this history, we have determined that the risk of a potential price concession has been eliminated and therefore the price for products sold to Motorola is now fixed or determinable upon sale to Motorola. In the three months ended March 31, 2006, we recognized revenue totaling approximately $3.0 million in connection with sales of products to Motorola through March 31, 2006 that had not yet sold through to Motorola's customers. This revenue would have been recognized in subsequent quarters if we had not changed to a sell-in basis for Motorola during the first quarter. This additional revenue from Motorola in the quarter negatively affected product gross margins during the first quarter as revenue from OEM relationships typically have lower margin profiles than revenue from direct sales to customers. This additional revenue resulted in approximately $1.0 million of additional net income in the quarter, but did not change reported basic and diluted earnings per share.

Deferred Revenue. 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 subsequent to 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.

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.

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 estimated 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.

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 warranty obligations 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.

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.

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.

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.

Stock-based Compensation. Effective January 1, 2006, we adopted the provisions of SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS No. 123R). Prior to January 1, 2006, we followed Accounting Principles Board Opinion 25, *Accounting for Stock Issued to Employees*, and related interpretations in accounting for our employee stock-based compensation.

Under the provisions of SFAS No. 123R, we recognize the fair value of stock-based compensation in our consolidated financial statements over the requisite service period, which generally equals the vesting period. We record into our inventory a portion of the fair value of stock-based compensation, which is expensed as inventory is relieved, generally over six months.

We have elected the modified prospective transition method for adopting SFAS No. 123R. Under this method, the provisions of SFAS No. 123R apply to all awards granted or modified after the date of

adoption. The unrecognized expense of awards not yet vested at the date of adoption shall be recognized in net income in the periods after the date of adoption using the same valuation method, Black-Scholes, and assumptions determined under the original provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*. We recorded $1.9 million of stock-based compensation in the condensed consolidated statement of operations for the three months ended March 31, 2006, included in the following expense categories (in thousands):

Product cost of revenues	$ 3
Service cost of revenues	252
Research and development	610
Sales and marketing	405
General and administrative	633
	$ 1,903

In addition, we included in inventory approximately $16,000 of stock-based compensation at March 31, 2006.

The recording of stock-based compensation expense for the three months ended March 31, 2006 resulted in a decrease in net income of $1.9 million and a decrease in basic and diluted earnings per share of $0.01. We expect stock-based compensation expense to reduce diluted net income per share by approximately $0.03 to $0.05 per share for fiscal 2006. As of March 31, 2006, there was $12.9 million of unrecognized compensation cost related to options, which is expected to be recognized over a weighted average period of 3.0 years.

However, our assessment of the estimated compensation charges is affected by our stock price as well as assumptions regarding a number of complex and subjective variables and the related tax impact. These variables include, but are not limited to, the volatility of our stock price and employee stock option exercise behaviors. We utilize the Black-Scholes valuation model for estimating the fair value on the date of grant of employee stock options. The Black-Scholes model requires us to make several assumptions, one of which is volatility. Prior to January 1, 2006, we used historical volatility to estimate the grant-date fair value of stock options. Starting on January 1, 2006, we changed our method to a combination of historical and implied volatility. We believe that a combination of historical and implied volatility results in a more accurate estimate of the grant-date fair value of employee stock options because it more appropriately reflects the market's expectations of future volatility. Historical volatility during the period associated with the expected term of our stock options over the past few years included a period of time during or subsequent to our initial public offering when our stock price experienced abnormally high volatility levels, which we believe is unlikely to be indicative of future stock price behavior. However, we have not placed sole reliance on implied volatility as options in our common stock that are actively traded on the open market currently have a term of less than one year - substantially shorter than our stock option's expected term.

On December 21, 2005, our Board of Directors approved accelerating the vesting of out-of-the-money, unvested stock options held by all current employees, subject to employee approval to the extent accelerating of vesting would create a change in classification of any grant from an incentive stock option to a non-qualified incentive stock option. Non-employee members of the Board of Directors were excluded from the acceleration. Unvested options having an exercise price of $4.00 per share or greater, representing the right to purchase a total of approximately 18.9 million shares, became exercisable as a result of the vesting acceleration. All other terms and conditions in the original grants remained unchanged. The acceleration of vesting did not result in the recognition of compensation expense in fiscal 2005 as the exercise price of the accelerated stock options exceeded the fair market value of the underlying common stock on the date of modification. The pro forma results reported for fiscal 2005 included approximately $63.8 million of pro forma compensation expense, net of tax, resulting from the vesting

acceleration. The decision to accelerate vesting of these stock options was made primarily to reduce compensation expense that would otherwise be recognized after the adoption of SFAS No. 123R.

Accounting for Income Taxes. We provide for deferred income taxes resulting from temporary differences between financial and taxable income. Such differences arise primarily from depreciation, accruals and reserves, deferred revenue, capitalized software costs, tax carryforwards, and allowances for accounts receivable. We record valuation allowances to reduce deferred income tax assets to the amount that is more likely than not to be realized. We have not provided for U.S. income taxes on the undistributed earnings of non-U.S. subsidiaries, as these earnings have been permanently reinvested or would be principally offset by foreign tax credits. Cumulative undistributed foreign earnings were approximately $497,000 at March 31, 2006.

Three Months Ended March 31, 2006 and 2005

Revenues. Revenues for the three months ended March 31, 2006 and 2005 were as follows, in thousands:

	2006	2005
Revenues:		
Product	$ 44,383	$ 22,458
Service	15,589	11,152
Total revenues	$ 59,972	$ 33,610

Product revenues comprise sales of our voice infrastructure products, including our GSX9000™ Open Services Switch, PSX, SGX, ASX, the Sonus Insight™ Management System and related product offerings. Product revenues for the three months ended March 31, 2006 increased 98% from the comparable period in fiscal 2005. The increase in product revenues was primarily the result of the conversion to revenue of orders received in the second half of fiscal 2005. In addition, during the three months ended March 31, 2006, we recorded $2.7 million of product revenue in connection with a change in reporting revenue with Motorola to a sell-in basis from a sell-through basis.

Service revenues primarily comprise hardware and software maintenance and support, network design, installation and other professional services. Service revenues for the three months ended March 31, 2006 increased 40% from the comparable period in fiscal 2005. The increase in service revenues was primarily a result of increases in maintenance revenues due to our growing installed customer base.

Global Crossing, Level 3 Communications and Motorola each contributed more than 10% of our revenues during one or more of the three months ended March 31, 2006 and 2005.

International revenues, primarily from Japan and the remainder of the Asia Pacific region, were 23% and 19% of revenues for the three months ended March 31, 2006 and 2005. International revenues increased due to uneven ordering patterns of our international customers and the achievement of revenue recognition criteria associated with each customer’s arrangement. We expect that international revenues will remain uneven as a percentage of revenue from quarter to quarter.

Our deferred product revenue was $42.3 million and $54.8 million as of March 31, 2006 and December 31, 2005. Our deferred service revenue was $59.9 million and $67.3 million as of March 31, 2006 and December 31, 2005. 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 March 31, 2006 and December 31, 2005, deferred revenue and accounts receivable excluded $15.3 million and $5.3 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, or for which title had not passed to the customer as of the period end date.

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 months ended March 31, 2006 and 2005 were as follows (in thousands, except percentages):

	2006	2005
Cost of revenues:		
Product	$ 15,853	$ 6,843
Service	7,381	5,269
Total cost of revenues	$ 23,234	$ 12,112
Gross profit margin (% of respective revenues):		
Product	64%	70%
Service	53	53
Total gross profit margin	61%	64%

The decrease in product gross profit as a percentage of revenues was primarily due to customer and product mix, including a greater percentage of revenue in fiscal 2006 from resellers with typically lower gross margins. Our product gross profit remained higher than our long-term financial model of 58-62%. We can provide no assurance that this favorable customer and product mix will continue, and we expect that over time our gross margins will return to levels consistent with our long-term financial model. The consistency in service gross profit as a percentage of service revenues was primarily due to increased investment in our service organization to support the expansion of our installed base and stock-based compensation recorded during the three months ended March 31, 2006, offset by an increase in service revenues. Our service cost of revenues is relatively fixed in advance of any particular quarter 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 expenses and prototype costs related to the design, development, testing and enhancement of our products. Research and development expenses were $12.9 million for the three months ended March 31, 2006, an increase of $1.9 million, or 17%, from $11.0 million for the same period in fiscal 2005. This increase primarily reflects an increase in salary and related expenses associated with increased headcount and stock-based compensation expense recorded during the three months ended March 31, 2006. 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 second quarter of fiscal 2006 will increase from the first quarter of fiscal 2006 primarily as a result of continued investment in new products, including the continued 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 inventory and other marketing and sales support expenses. Sales and marketing expenses were $13.9 million for the three months ended March 31, 2006, an increase of $4.9 million, or 54%, from $9.0 million for the same period in fiscal 2005. This increase primarily reflects an increase in salaries and travel expenses associated with increased headcount related to the expansion of our worldwide sales and support coverage, an increase in commissions associated with higher revenues, stock-based compensation

expense recorded during the three months ended March 31, 2006 and higher evaluation equipment expenses. We believe that our sales and marketing expenses for the second quarter of fiscal 2006 will increase from the first quarter of fiscal 2006 related to personnel costs and trade show expenses. The magnitude of the increase will be dependent upon our level of revenues in the second 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, allowance for doubtful accounts and professional fees. General and administrative expenses were $6.7 million for the three months ended March 31, 2006, a decrease of $0.1 million, or 1%, from $6.8 million for the same period in fiscal 2005. This decrease primarily reflects a decrease in directors and officers insurance premiums and a decrease in professional fees, offset by an increase in salary and related expenses associated with increased headcount and the recording of stock-based compensation expense during the three months ended March 31, 2006. We believe that our general and administrative expenses for the second quarter of fiscal 2006 will remain generally consistent with the first quarter of fiscal 2006 due to continued costs associated with improvements we are making in our internal control environment to address material weaknesses.

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 obligations. Interest income, net of interest expense, was $3.3 million for the three months ended March 31, 2006, as compared to $1.7 million for the same period in fiscal 2005. This increase reflects the benefit of an increase in the yield on our portfolio due to an increasing interest rate environment, shifting some of the marketable debt securities to longer-term investments with a higher yield during the three months ended March 31, 2006, and an overall increase in cash and investments compared to the prior year.

Income Taxes. Provisions for income taxes were $791,000 and $96,000 for the three months ended March 31, 2006 and 2005, which are primarily attributable to foreign income taxes and state and federal income taxes in the U.S. As of March 31, 2006, we had net operating loss carryforwards for federal and state income tax purposes of approximately $142 million and $86 million, respectively. The federal net operating loss carryforwards expire at various dates from 2019 through 2023. The state net operating loss carryforwards expire at various dates from 2006 through 2023. We have recorded a full valuation allowance for the related federal and state net deferred tax asset due to the uncertainty of realizing the benefit of this asset. We have recorded a foreign deferred income tax asset of $519,000 with no valuation allowance as of March 31, 2006 as it is more likely than not that it will be realized. We provide for income taxes during interim periods based on the estimated effective tax rate for the full fiscal year. We record cumulative adjustments to the tax provision in an interim period in which a change in the estimated annual effective rate is determined.

Off-balance Sheet Arrangements

We have no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Liquidity and Capital Resources

At March 31, 2006, our principal source of liquidity was our cash, cash equivalents, marketable debt securities and long-term investments that totaled $340.2 million.

Our cash from operating activities was $21.0 million for the three months ended March 31, 2006, as compared to cash used in operating activities of $84,000 for the same period in fiscal 2005. The increase in

cash flow from operating activities was primarily due to net income for the three months ended March 31, 2006 as compared to a net loss in the prior year and a decrease in accounts receivable, partially offset by decreases in deferred revenue, accounts payable and accrued expenses.

Net cash used in investing activities was $133.4 million for the three months ended March 31, 2006, as compared to net cash used in investing activities of $1.4 million for the same period in fiscal 2005. Net cash used in investing activities for the three months ended March 31, 2006 primarily reflects net purchases of marketable debt securities and long-term investments of $131.4 million and capital expenditures of $2.3 million. Net cash used in investing activities for the three months ended March 31, 2005 primarily reflects capital expenditures of $4.3 million, primarily offset by net maturities of marketable debt securities and long-term investments of $3.0 million. We expect to incur approximately $10-12 million in additional capital expenditures in the remaining three fiscal quarters of 2006.

Net cash provided by financing activities was $7.1 million for the three months ended March 31, 2006, as compared to $2.7 million for the same period in fiscal 2005 The net cash provided by financing activities for the three months ended March 31, 2006 and 2005 primarily resulted 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. In addition, we had a convertible subordinated note with a customer that matured on May 1, 2006 for which we made a payment of $10,000,000 plus accrued interest on that date. 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, to improve our internal control environment and for other general corporate activities, as well as to vigorously defend against existing and potential litigation relating to the restatement of our consolidated financial statements. See Note 4 to our condensed consolidated financial statements.

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 our investments and foreign currency fluctuations. We do not believe that a hypothetical 10% adverse movement in interest rates and foreign currency exchange rates would have a materially different impact than what was disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2005.

Item 4: Controls and Procedures

Our management, with the participation of our principal executive officer and principal 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 March 31, 2006, which included an evaluation of disclosure controls and procedures applicable to the period covered by the filing of this periodic report. The term “disclosure controls and procedures,” as defined in Rule 13a-15(e), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

In our *Management's Report on Internal Control over Financial Reporting* filed with our Annual Report on Form 10-K for the year ended December 31, 2005, we reported three (3) material weaknesses in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act). As a result of these material weaknesses, which were not remediated as of March 31, 2006, we have concluded that our disclosure controls and procedures were not effective as of March 31, 2006.

During the fiscal quarter ended March 31, 2006, we made changes that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. In particular, we implemented changes to the communication and monitoring of entity-level controls throughout the organization to provide reasonable assurance that appropriate information is disseminated to all employees in order for them to understand our corporate policies thoroughly, and to understand and accomplish their assigned duties, including their internal control responsibilities. These changes consist of the following:

· Established and posted a corporate governance web page on our intranet site; the web page sets forth our policies, procedures and best practices with respect to governing the Company;

· Established an anonymous employee hotline for employees to submit complaints regarding corporate governance, ethics and controls;

· Communicated to the entire organization the new corporate governance web page, the new anonymous employee hotline and our whistleblower policy through e-mail communication and in a company-wide employee meeting;

· Established and posted on our Internet site a process for third parties to submit complaints regarding corporate governance, ethics and controls;

· Established an on-line Incident Tracking and Reporting process to assist management in tracking complaints and potential violations of our code of business conduct, policies and controls; and

· Hired a Manager of Internal Controls to work with business process owners to design and implement more effective controls and procedures.

We expect these changes will contribute to the remediation of the material weakness relating to inadequate entity-level controls.

We have established a plan to implement procedures and controls during 2006 to remediate the remaining material weaknesses to our entity level, revenue recognition, and financial statement preparation and review procedures and controls. We will report each quarter on our progress and on changes made during the quarter that materially affect, or are reasonably likely to materially affect, our internal control over financial reporting.

We have implemented policies and procedures to ensure our financial reports are complete and accurate pending the remediation of the reported material weaknesses. These policies and procedures include:

· Implementation of code of ethics training and annual certification and whistleblower programs to mitigate risk of fraud;

· Enhanced review of journal entries and account reconciliations, including international entities, to provide reasonable assurance of complete and accurate transactions;

· Weekly revenue meetings, quarterly certifications and disclosure process and customer account reviews and revenue files to understand and document our customer arrangements;

· Manual documentation to adequately support the assignment of customer creditworthiness;

· Manual reconciliation of customer invoices to related purchase orders and shipping documentation;

· Manual reconciliation of cash payments applied to customer accounts with invoices and purchase orders; and

· Use of outside accounting and financial professionals to assist in the preparation, review and reconciliation of our accounts and financial statements.

In addition, we will continue to design and implement additional policies and procedures during the remediation of our reported material weaknesses.

Prior to the complete remediation of these material weaknesses, there remains risk that the processes and procedures 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. Moreover, because of the inherent limitations in all control systems, no evaluation of controls—even where we conclude the controls are operating effectively—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, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of 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 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 principal executive officer and principal financial officer required in accordance with Rule 13a-14(a) under the Exchange Act and Section 302 of the Sarbanes-Oxley Act of 2002 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 internal control over financial reporting, referred to in paragraph 4 of the 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 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. On April 24, 2006, the court held a hearing on a motion to approve the final settlement and took the matter under advisement. As the settlement would not require any payment by us, we do not expect that the settlement would have a material impact on our 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 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 opposed the motion. No hearing date has been scheduled.

On January 6, 2006, a purchaser of our common stock filed a complaint in the United States District Court for the District of Massachusetts that is essentially identical to the Consolidated Amended Complaint previously filed against the defendants. Three shareholders have filed motions seeking appointment as lead plaintiff. The court has not yet ruled on these motions. Following the appointment of a lead plaintiff, the defendants intend to file a motion to dismiss the complaint. There is no assurance we will prevail in such a motion or defending this action. A judgment or a settlement of the claims against the defendants could have a material impact on our financial results. It is too early to determine the ultimate outcome or potential range of loss, if any.

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. On December 10, 2005, the Court held a hearing on the motions and took the matter under advisement.

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 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, the case was dismissed 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. On December 10, 2005, the court held a hearing on the motions and took the matter under advisement. On March 31, 2006, the court entered an order granting the defendants' motions and dismissing the amended complaint. On April 26, 2006, the plaintiffs filed a notice of appeal of the dismissal order. We do not expect that this claim will have a material impact on our financial statements.

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 it dismissed the federal claims without prejudice and dismissed the state claims without prejudice. On November 23, 2005, the plaintiff filed a second amended complaint with essentially the same allegations as in the prior complaints. The defendants renewed their motions to dismiss with respect to the second amended complaint. On March 9, 2006, the court held a hearing on the defendants' motions during which the court entered an order dismissing the second amended complaint with prejudice. On April 17, 2006, the plaintiff filed a notice of appeal of the dismissal order.

We include standard intellectual property indemnification provisions in our product agreements in the ordinary course of business. Pursuant to our product agreements, we 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 our products. Other agreements with our customers provide indemnification for claims relating to property damage or personal injury resulting from the performance of services by us or our subcontractors. Historically, our 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 1A. Risk Factors

Investing in our common stock involves a high degree of risk. You should carefully consider the risks described below before buying our common stock. If any of the following risks actually occurs, the trading price of our common stock could decline and you may lose all or part of your investment. There have been no material changes to the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2005.

We have identified material weaknesses in 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.

We have taken and continue to take significant steps to improve our overall control over financial reporting. In 2005, we remediated seven of ten material weaknesses in our internal control over financial reporting that we had reported as of December 31, 2004. However, there is additional work and focus required to address remaining deficiencies in some of these areas. Management has concluded that our internal control over financial reporting continues to have certain material weaknesses as of March 31, 2006 and that our disclosure controls and procedures are ineffective. These weaknesses 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 remaining material weaknesses, there remains risk that the processes and procedures 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 have made 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.

In 2004, we were not current in our SEC filings and, as a result, our common stock was delisted from the NASDAQ National Market for a short period of time.

If we are unable to remain current in our SEC filings, we will not be able to have 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 and we will lose our status as a "well known seasoned issuer," including the registration advantages associated with such status. 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.

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. Three customers contributed more than 10% of our revenues for the first three months of fiscal 2006, which represented an aggregate of 41% of total revenues. One customer contributed more than 10% of our revenues for fiscal 2005, which represented an aggregate of 28% 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:

- acquisitions 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.

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, 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 of service providers. These conditions caused a substantial, unexpected reduction in demand for telecommunications equipment, including our products.

We expect some of 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.

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 in 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 adversely affect our financial position in the applicable 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 sales by 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 affected.

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 the remainder of the Asia Pacific region, were approximately $13.8 million for the first three months of fiscal 2006, and $47.8 million for fiscal 2005, 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 cycles;
- 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 sustain profitability.

We have incurred significant losses since inception and, as of March 31, 2006, had an accumulated deficit of $770.0 million. Although we achieved profitability in the first quarter of fiscal 2006 and on an annual basis in fiscal 2005 and 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 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 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 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 Alcatel, 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. Alcatel and Lucent have announced the merger of the two companies and other competitors may merge, intensifying competition. Additional competitors with significant financial resources also may enter our 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 and have the ability to offer lower prices to win business. 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;
- provide a cost-effective and space efficient solution for service providers; and
- meet price competition from low cost equipment 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 which could affect our business and operations.

We have made significant changes in our senior management team, including the hiring of new Vice Presidents of Engineering and Sales since January 1, 2006. 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 may 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 and certain tests 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. In 2006, we intend to consolidate our manufacturing to a single contract manufacturer. We also intend to move our contract manufacturing to a lower cost, offshore facility. If we do not manage this consolidation effectively, these consolidation activities could result in the disruption in the supply of our products and in delays in our fulfillment of customer orders.

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;
- reduce significantly our cash and investments;
- 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;
- potential loss of key employees, particularly those of the acquired organizations; and
- integration of internal controls and financial systems.

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 requires 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 require companies to record a charge to earnings for employee stock option grants and other equity incentives effective January 1, 2006, which we have adopted. 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.

In addition, in order to eliminate the compensation expense associated with unvested employee stock options with an exercise price of $4.00 or greater, in December 2005, we accelerated the vesting on the majority of these options. The acceleration of these unvested options may affect our ability to retain 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 where we operate, including the United States. 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 position.

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:

· 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. 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 6: Exhibits

Exhibit Number	Description
10.1(a)	Sublease agreement between Sonus Networks, Inc. and Teradyne, Inc. dated as of February 22, 2006.
10.2(b)	Summary of 2005 Executive Incentive Compensation Awards.
10.3(c)	Employment letter dated April 10, 2006, by and between the Registrant and James F. Collier.
31.1	Certification of Sonus Networks, Inc. Chief Executive Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
31.2	Certification of Sonus Networks, Inc. Chief Financial Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
32.1	Certification of Sonus Networks, Inc. Chief Executive Officer pursuant to Section 906 of the Sarbanes Oxley Act of 2002.
32.2	Certification of Sonus Networks, Inc. Chief Financial Officer pursuant to Section 906 of the Sarbanes Oxley Act of 2002.

(a) Incorporated by reference from an exhibit to the Registrant's Form 8-K (File No. 000-30229) filed March 9, 2006 with the SEC.

(b) Incorporated by reference from Item 1.01 to the Registrant's Form 8-K (File No. 000-30229) filed March 27, 2006 with the SEC.

(c) Incorporated by reference from an exhibit to the Registrant's Form 8-K (File No. 000-30229) filed April 24, 2006 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: May 8, 2006 SONUS NETWORKS, INC.

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

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

EXHIBIT INDEX

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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 March 31, 2006 ("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: May 8, 2006

/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 March 31, 2006 (“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: May 8, 2006

/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 March 31, 2006 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: May 8, 2006

/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 March 31, 2006 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: May 8, 2006

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