IPASS INC
Form 10-Q
November 09, 2005

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2005

OR

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

For the transition period from __________to __________

000-50327
(Commission File Number)

iPass Inc.
(Exact name of Registrant as specified in its charter)

Delaware	**93-1214598**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

3800 Bridge Parkway
Redwood Shores, California 94065
(Address of principal executive offices, including zip code)
(650) 232-4100
(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 þ No o
Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act)
Yes þ No o
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes o No þ
The number of shares outstanding of the Registrant s Common Stock, $0.001 par value, as of October 31, 2005 was 63,869,512.

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iPASS INC. AND SUBSIDIARIES
FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2005

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

iPASS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited, in thousands)

	September 30, 2005	December 31, 2004
ASSETS		
Current assets:		
Cash and cash equivalents, including restricted cash of $250 and $0 at September 30, 2005 and December 31, 2004, respectively	$ 28,969	$ 34,395
Short-term investments	148,252	117,940
Accounts receivable, net of allowance for doubtful accounts of $2,082 and $2,071, respectively	23,651	23,884
Prepaid expenses and other current assets	3,203	3,161
Deferred income tax assets	4,108	8,642
Total current assets	208,183	188,022
Property and equipment, net	9,229	10,111
Other assets	1,172	1,224
Acquired intangibles, net	9,368	11,143
Goodwill	20,013	20,013
Total assets	$ 247,965	$ 230,513
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 10,183	$ 9,154
Accrued liabilities	14,641	14,137
Total current liabilities	24,824	23,291
Total liabilities	24,824	23,291
Stockholders equity:		
Common stock	64	63
Additional paid-in capital	243,941	240,629
Deferred stock-based compensation	(819)	(1,782)
Accumulated other comprehensive loss	(411)	(424)
Accumulated deficit	(19,634)	(31,264)
Total stockholders equity	223,141	207,222
Total liabilities and stockholders equity	$ 247,965	$ 230,513

See Accompanying Notes to the Condensed Consolidated Financial Statements

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iPASS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited, in thousands, except share and per share amounts)

	Three Months Ended September 30, 2005	Three Months Ended September 30, 2004	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004
Revenues	$ 41,881	$ 41,912	$ 129,078	$ 123,001
Operating expenses:				
Network access	10,568	9,443	31,423	27,690
Network operations	5,085	4,752	15,665	14,169
Research and development	4,237	3,337	13,084	9,697
Sales and marketing	12,227	11,416	37,975	34,227
General and administrative	4,252	4,513	13,064	13,023
Amortization of stock-based compensation (1)	237	480	912	1,890
Amortization of intangibles	592	21	1,775	21
Total operating expenses	37,198	33,962	113,898	100,717
Operating income	4,683	7,950	15,180	22,284
Other income, net	993	590	2,717	1,493
Income before income taxes	5,676	8,540	17,897	23,777
Provision for income taxes	1,466	3,334	6,267	9,385
Net income	$ 4,210	$ 5,206	$ 11,630	$ 14,392
Net income per share:				
Basic	$ 0.07	$ 0.08	$ 0.18	$ 0.24
Diluted	$ 0.06	$ 0.08	$ 0.18	$ 0.22
Number of shares used in per share calculations:				
Basic	63,461,175	61,352,058	62,918,027	60,400,040
Diluted	66,122,504	65,463,843	65,773,335	65,558,403
(1) Amortization of stock-based compensation consists of:				
Network operations	$ 32	$ 63	$ 132	$ 276
Research and development	34	67	143	289
Sales and marketing	57	121	213	446
General and administrative	114	229	424	879

Total amortization of stock-based compensation	$	237	$	480	$	912	$	1,890

See Accompanying Notes to the Condensed Consolidated Financial Statements

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iPASS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004
Cash flows from operating activities:		
Net income	$ 11,630	$ 14,392
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of stock-based compensation for employees	912	1,890
Amortization of acquired intangibles	1,775	21
Depreciation and amortization	3,657	3,165
Deferred income tax	4,534	8,096
Tax benefit from employee stock option plans	881	697
Interest on shareholder notes receivable		(56)
Provision for doubtful accounts	200	950
Realized loss on investments, net	31	95
Changes in operating assets and liabilities:		
Accounts receivable	33	(3,674)
Prepaid expenses and other current assets	(42)	(343)
Other assets	52	41
Accounts payable	1,029	716
Accrued liabilities	504	621
Net cash provided by operating activities	25,196	26,611
Cash flows from investing activities:		
Purchases of short-term investments	(126,313)	(136,292)
Maturities of short-term investments	95,983	100,522
Purchases of property and equipment	(2,775)	(4,921)
Acquisition of Safe3w, net of cash acquired		(8,481)
Net cash used in investing activities	(33,105)	(49,172)
Cash flows from financing activities:		
Proceeds from issuance of common stock	2,483	6,768
Proceeds from collection of stockholder notes receivable		2,887
Net cash provided by financing activities	2,483	9,655
Net decrease in cash and cash equivalents	(5,426)	(12,906)
Cash and cash equivalents at beginning of period	34,395	45,646
Cash and cash equivalents at end of period	$ 28,969	$ 32,740

See Accompanying Notes to the Condensed Consolidated Financial Statements

iPASS INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Description of Business

iPass, Inc. (the Company , iPass or we) provides software-enabled enterprise connectivity services for mobile workers. Its primary service offering, iPass Corporate Access, is designed to enable enterprises to provide their employees with secure access from approximately 160 countries to the enterprise s internal networks through an easy-to-use interface. As opposed to telecommunications companies that own and operate physical networks, iPass provides its services through a virtual network. iPass virtual network is enabled by its software, its scalable network architecture and its relationships with over 300 telecommunications carriers, internet service providers and other network service providers around the globe. In addition, we provide policy management services that extend our secure offering to enable better protection of user identities, the integrity of an enterprise s remote and mobile computer systems, or endpoints, as well as an enterprise s network. These services can be used in conjunction with iPass Corporate Access or over non-iPass network connections. The Company s software is designed to provide enterprises with a high level of security, the ability to affect and control policy management, and to receive centralized billing and detailed reporting. iPass was incorporated in California in July 1996 and reincorporated in Delaware in June 2000.

Note 2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying financial data, as of September 30, 2005 and for the three and nine months ended September 30, 2005 and 2004, has been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. The December 31, 2004 Condensed Consolidated Balance Sheet was derived from audited financial statements, but does not include all disclosures required by generally accepted accounting principles. However, the Company believes that the disclosures are adequate to make the information presented not misleading.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (which include normal recurring adjustments, except as disclosed herein) necessary to present fairly the Company s financial position, results of operations, and cash flows for the interim periods presented. The results of operations for the three and nine months ended September 30, 2005 are not necessarily indicative of the operating results for the full fiscal year or any future periods.

Use of Estimates

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

Principles of Consolidation

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

Foreign Currency Translation

Substantially all revenues and network access expenses are denominated in U.S. dollars. Therefore, the Company considers the functional currency of its foreign subsidiaries to be the U.S. dollar. Foreign currency transaction gains and losses are included in the accompanying Condensed Consolidated Statements of Income. Foreign currency transaction gains and losses were not significant for the three and nine months ended September 30, 2005 and 2004.

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Comprehensive Income

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

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Net income	$ 4,210	$ 5,206	$ 11,630	$ 14,392
Comprehensive income:				
Net change in accumulated unrealized gain (loss) on available-for- sale securities	52	170	13	(450)
Total comprehensive income	$ 4,262	$ 5,376	$ 11,643	$ 13,942

Cash Equivalents and Short-term Investments

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

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

Concentrations of Risk

Substantially all of the Company s cash and cash equivalents are held by two financial institutions.

The Company provides credit to its customers in the normal course of business, performs ongoing credit evaluations of its customers, and maintains an adequate allowance for doubtful accounts. As of September 30, 2005 and December 31, 2004, no individual customer represented 10% or more of accounts receivable.

Fair Value of Financial Instruments

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

Property and Equipment

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

Equipment (Three years)

Furniture and fixtures (Five years)

Computer software and equipment (Three years)

Leasehold improvements (Shorter of useful life or lease term)

Impairment of Long-Lived Assets

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

Income Taxes

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

Stock-Based Compensation

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

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

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

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
	2005	**2004**	**2005**	**2004**
Net income as reported	$ 4,210	$ 5,206	$ 11,630	$ 14,392
Add: Stock-based employee compensation expense included in the reported net income, net of related tax effects	140	288	538	1,134
Deduct: Stock-based employee compensation expense using the fair value method, net of related tax effects	(819)	(1,111)	(2,872)	(2,519)
Pro forma net income	$ 3,531	$ 4,383	$ 9,296	$ 13,007
Basic net income per common share:				
As reported	$ 0.07	$ 0.08	$ 0.18	$ 0.24
Pro forma	$ 0.06	$ 0.07	$ 0.15	$ 0.22
Diluted net income per common share:				
As reported	$ 0.06	$ 0.08	$ 0.18	$ 0.22
Pro forma	$ 0.05	$ 0.07	$ 0.14	$ 0.20

The weighted average fair value of options granted was $1.38 and $1.82 for the three months ended September 30, 2005 and 2004, respectively, and $1.53 and $2.05 for the nine months ended September 30, 2005 and 2004, respectively. For purposes of pro forma disclosure, the estimated fair value of the options was amortized to expense over the options vesting period, for employee stock options, and over six months, for stock purchases under the Company s 2003 Employee Stock Purchase Plan.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants for the three and nine months ended September 30, 2005 and 2004:

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	Employee Stock Options				Employee Stock Purchase Plan			
	Three Months Ended September 30,		Nine Months Ended September 30,		Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004	2005	2004	2005	2004
Risk-free rate	4.0%	3.1%	3.9%	3.1%	3.2%	1.2%	3.2%	1.2%
Expected dividend yield	0%	0%	0%	0%	0%	0%	0%	0%
Expected volatility	37%	47%	37-41%	41-47%	41%	32%	41%	32%
Expected life	3 Years	3 Years	3 Years	3 Years	.5 Years	.5 Years	.5 Years	.5 Years

Computation of Net Income per Share

Basic net income per share is computed by dividing net income by the weighted daily average number of shares of common stock outstanding during the period. Diluted net income per share is computed using the weighted daily average number of shares of common stock outstanding for the period plus dilutive potential common shares from the issuance of stock options using the treasury stock method.

Revenue Recognition

Services and Fees

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

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

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

License and Maintenance

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

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

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

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

Network Access

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

If the Company estimates that the revenues derived from the purchase commitment will be less than the purchase commitment, the Company recognizes a loss on that purchase commitment to the extent of that difference. No such loss has been recognized through September 30, 2005.

Advertising

Advertising and promotional costs are expensed as incurred. Advertising and promotional costs were approximately $184,000 and $290,000 for the three months ended September 30, 2005 and 2004, respectively, and $321,000 and $732,000 for the nine months ended September 30, 2005 and 2004, respectively.

Software Development Costs

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

The Company capitalizes the costs of computer software developed or obtained for internal use. Development costs are amortized over the estimated useful life of the software developed, which is generally three years. As of September 30, 2005, the Company had no capitalized internal use software development costs.

Recent Accounting Pronouncements

In December of 2004, the Financial Accounting Standards Board (FASB) issued a revised version of Statement No. 123 *Accounting for Stock-Based Compensation* (SFAS 123R), which supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees,* and its related implementation guidance. SFAS 123R requires recognition of the cost of employee services received in share-based payment transactions, thereby reflecting the economic consequences of those transactions in the financial statements. The accounting provisions for SFAS 123 are effective beginning with the first annual reporting period that begins after June 15, 2005, and we will be required to implement SFAS 123R beginning January 1, 2006. The pro forma disclosures previously permitted under SFAS 123 will no longer be an alternative to financial statement recognition. See *Stock-Based Compensation* above for the pro forma net income and net income per share amounts, for the three and nine months ended September 30, 2005 and 2004, as if we had used a fair-value-based method similar to the methods required under SFAS 123R to measure compensation expense for employee stock incentive awards. Although we have not yet determined whether the adoption of SFAS 123R will result in amounts that are similar to the current pro forma disclosures under SFAS 123, we are evaluating the requirements under SFAS 123R and expect the adoption of SFAS 123R to have a significant adverse impact on our Condensed Consolidated Statements of Income and net income per share.

In May 2005, the FASB issued Statement No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3 (FAS 154). FAS 154 provides guidance on the accounting for, and reporting of, a change in accounting principle, in the absence of explicit transition requirements specific to a newly adopted accounting principle. Previously, most voluntary changes in accounting principles were required to be recognized by way of a cumulative effect adjustment within net income during the period of the change. FAS 154 requires retrospective application to prior periods financial statements, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. FAS 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005. If required, the application of FAS 154 may have a material effect on our financial position on our results of operations.

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Note 3. Net Income Per Common Share

In accordance with SFAS 128, Earnings Per Share, basic net income per share is computed by dividing net income by the weighted daily average number of shares of common stock outstanding during the period. The weighted daily average number of shares of common stock excludes shares that have been exercised prior to vesting and are subject to repurchase by the company. As such, basic net income per share excludes 185,623 and 964,337 shares subject to repurchase for the three months ended September 30, 2005 and 2004, respectively, and 370,599 and 1,172,409 shares for the nine months ended September 30, 2005 and 2004, respectively. These shares have been included in diluted net income per share to the extent that the inclusion of such shares is dilutive. Diluted net income per share is based upon the weighted daily average number of shares of common stock outstanding for the period plus dilutive potential common shares from the issuance of stock options using the treasury-stock method.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Numerator:				
Net income	$ 4,210	$ 5,206	$ 11,630	$ 14,392
Denominator:				
Denominator for basic net income per common share Weighted average shares outstanding	63,461,175	61,352,058	62,918,027	60,400,040
Effect of dilutive securities:				
Stock options	2,661,329	4,111,785	2,855,308	5,158,363
Denominator for diluted net income per common share adjusted Weighted average shares	66,122,504	65,463,843	65,773,335	65,558,403
Basic net income per common share	$ 0.07	$ 0.08	$ 0.18	$ 0.24
Diluted net income per common share	$ 0.06	$ 0.08	$ 0.18	$ 0.22

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Options to purchase common stock	2,791,920	1,369,542	1,984,603	805,750

The weighted-average exercise price of options to purchase common stock excluded from the computation was $8.81 and $11.92 for the three months ended September 30, 2005 and 2004, respectively, and $10.06 and $14.55 for the nine months ended September 30, 2005 and 2004, respectively.

Note 4. Legal Contingencies

On January 14, 2005, a lawsuit entitled *Palumbo v. iPass, Inc., et al.,* Case No. C 05 228 MHP was filed in the United States District Court for the Northern District of California, purportedly on behalf of a class of investors who purchased iPass stock between April 22, 2004 and June 30, 2004, against iPass and certain of its officers and directors.

The complaint alleges that in April 2004 the defendants made misleading statements concerning the Company s projected revenues for the quarter ending June 30, 2004, and sets forth claims against the defendants under Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934 and seeks monetary damages to be proven at trial. Several similar lawsuits were subsequently filed in the same court, and all of the suits have since been consolidated into a single action. On April 22, 2005, the court appointed a lead plaintiff, and a consolidated amended complaint was filed by the lead plaintiff on July 5, 2005. All defendants filed a motion to dismiss on September 2, 2005. The motion is set for hearing in December 2005. This matter is at an early stage; no response to the complaint has been filed, no discovery has taken place and no trial date has been set. iPass and the individual defendants intend to take all appropriate actions to defend the suit. We cannot estimate any possible loss at this time.

On March 25, 2005, a stockholder purporting to act on our behalf filed a lawsuit entitled *Narendar Gupta, et al. v. Kenneth Denman, et al.*, Case No. CIV445765 in the California Superior Court for the County of San Mateo against our directors and certain officers. iPass was also named as a nominal defendant solely in a derivative capacity. On April 6, 2005, a similar lawsuit entitled *Eugene Danielson v. Kenneth D. Denman, et al.*, No. CIV446034 was filed in that same court. Both lawsuits were consolidated into a single action by stipulation and order dated April 26, 2005. The derivative action is based on the same factual allegations and circumstances

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as the purported securities class actions and alleges state law claims for insider trading, breach of fiduciary duty, abuse of control, gross mismanagement, waste of corporate assets, and unjust enrichment and seeks monetary damages on behalf of iPass to be proven at trial. This case is at an early stage; no consolidated complaint has been filed, no discovery has been taken and no trial date has been set. iPass and the individual defendants intend to take all appropriate action to defend these lawsuits. We cannot estimate any possible loss at this time.

Note 5. Segment Information

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

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

Forward-Looking Statements

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

Management Overview

We are a global provider of software-enabled enterprise connectivity services for mobile workers. Our primary service offering is designed to enable enterprises to provide their employees with secure access from approximately 160 countries to the enterprise s internal networks through an easy-to-use interface. Our total revenues remained relatively constant for the three months ended September 30, 2005 as compared to the three months ended September 30, 2004 and increased 5% for the nine months ended September 30, 2005 as compared to the same period in 2004. The increase in total revenues for the nine months ended September 30, 2005 was driven, in part, by an increase in revenue generated from services and other fees, in particular license and maintenance fees as a result of our acquisition of Mobile Automation, Inc. in October 2004. We also continued to add customers during the third quarter of 2005, including six from the Forbes Global 2000, bringing the total number of our Forbes Global 2000 customers to 276 as of September 30, 2005. International revenues, which are revenues generated from customers domiciled outside the United States, also increased as a percentage of our total revenues, in particular due to growth in our EMEA (Europe, Middle East and Africa) region.

We believe that there is an industry-wide trend away from dial-up toward wired and wireless broadband as the preferred method of connectivity for mobile workers. Distinct end users of our connectivity service decreased from 526,000 for the month of September

2004 to 510,000 for the month of September 2005. We also saw a decrease in user sessions for the quarter ended September 30, 2005 as compared to the same period in 2004.

Consistent with this trend, dial-up revenues decreased from $35.3 million for the three months ended June 30, 2005 to $33.7 million for the three months ended September 30, 2005 as compared to $37.7 million for the three months ended September 30, 2004. Conversely, we experienced a 15% increase in our broadband revenues from $2.1 million for the three months ended June 30, 2005 to $2.4 million for the three months ended September 30, 2005 as compared to $660,000 for the three months ended September 30, 2004.

Sources of Revenues

We derive our revenues primarily from providing enterprise connectivity services through our virtual network. We sell these services directly, as well as indirectly through our channel partners. We bill substantially all customers on a time basis for usage based on negotiated rates. We bill the remaining customers based on a fixed charge per active user per month with additional charges for excess time. Substantially all enterprise customers commit to a one to three year contract term. Most of our contracts with enterprise customers contain minimum usage levels. We bill customers for minimum commitments when actual usage is less than their monthly minimum commitment amount. We recognize the difference between the minimum commitment and actual usage as fee revenue once the cash for such fee has been collected. Our usage-based revenues represented 86% and 92% of our total revenues for the three months ended September 30, 2005 and 2004, respectively, and 87% and 92% of our total revenues for the nine months ended September 30, 2005 and 2004, respectively.

We have incurred expenses to expand our broadband coverage and are seeking to generate additional revenues from our broadband wired and wireless coverage. We generated approximately 6% and 5% of our total revenues from broadband usage for the three and nine months ended September 30, 2005, respectively.

We also provide customers with deployment services and technical support throughout the term of the contract. We typically charge fees for these services on a one-time or annual basis, depending on the service provided and the nature of the relationship. In addition, we also offer customers additional services for which we generally bill on a monthly basis. With the acquisition of Mobile Automation, Inc. in October of 2004, we also began generating license and maintenance revenue through software licensing agreements. Revenues generated from license and maintenance fees, together with revenues generated from fees, represented approximately 14% and 8% of our total revenues for the three months ended September 30, 2005 and 2004, respectively, and 13% and 8% of our total revenues for the nine months ended September 30, 2005 and 2004, respectively.

Critical Accounting Policies and Estimates

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

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

Revenue Recognition

Services and Fees

We have derived substantially all of our revenues to date from connectivity services. We recognize revenues when persuasive evidence of an arrangement exists, service has been provided to the customer, the price to the customer is fixed or determinable, and collectibility is probable.

We recognize revenues during the period the services are rendered to end users based on usage at negotiated rates. We typically require our customers to commit to minimum usage levels. Minimum usage levels can be based on an annual term, monthly term or over the term of the arrangement. If actual usage in a given period is less than the minimum commitment, we recognize the difference between the actual usage and the minimum commitment as revenue when cash is collected because we cannot reasonably estimate the

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amount of the difference that will be collected. We cannot reasonably estimate the amount of the difference to be collected because we have from time to time renegotiated minimum commitments in cases where customers have sought renegotiation of their contract for reasons such as a significant downturn in their business or where we have determined that it would be in our best interest to do so. Customers are not contractually entitled to use or otherwise receive benefit for unused service in subsequent periods.

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

License and Maintenance

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

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

We defer payments received in advance of services performed. We provide for allowances for estimated future returns and discounts upon recognition of revenue.

We generally perform credit reviews to evaluate the customers ability to pay. If we determine that collectibility is not probable, we recognize revenue as cash is collected.

Accounting for Income Taxes

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

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

Allowance for Doubtful Accounts

We base our allowance for doubtful accounts on a detailed assessment of accounts receivable for specific, as well as anticipated, uncollectible accounts receivable. We base our estimate in determining the allowance for doubtful accounts on credit profiles of our customers, current economic trends, contractual terms and conditions, and historical payment experience. We had an allowance for doubtful accounts of $2.1 million as of September 30, 2005 and

December 31, 2004, for estimated losses resulting from the inability of our customers to make their required payments to us. If the financial condition of our customers were to deteriorate, resulting in their inability to make payments, or if we underestimated the allowances required, additional allowances may be required, which would result in an increased general and administrative expense in the period such determination was made.

RESULTS OF OPERATIONS

Overview of the three and nine months ended September 30, 2005 and 2004

Revenue

	Three Months Ended September 30,		Change		Nine Months Ended September 30,		Change	
	2005	2004	$	%	2005	2004	$	%
	(In thousands, except percentages)							
Total revenue	$ 41,881	$ 41,912	$ (31)	(0.1)%	$ 129,078	$ 123,001	$ 6,077	4.9%

Total revenue remained relatively constant for the three months ended September 30, 2005, as compared to the same period in 2004. However, total revenue increased in the nine months ended September 30, 2005, as compared to the same period in 2004. The composition of our total revenues for the three month period ended September 30, 2005 has changed in comparison to the prior year period due primarily to a decrease in our dial-up revenues and an increase in revenues from broadband usage and fees. Broadband revenues were $2.4 million and $660,000 for the three months ended September 30, 2005 and 2004, respectively, and $5.9 million and $1.3 million for the nine months ended September 30, 2005 and 2004, respectively. Revenues from fees were $5.8 million and $3.5 million for the three months ended September 30, 2005 and 2004, respectively, and $16.7 million and $9.8 million for the nine months ended September 30, 2005 and 2004, respectively. No individual customer accounted for 10% or more of total revenues for the three and nine months ended September 30, 2005 and 2004. Revenues from minimum commitments, license and maintenance fees and additional services represented approximately 14% and 8% of our revenues for the three months ended September 30, 2005 and 2004, respectively, and 13% and 8% of revenues for the nine months ended September 30, 2005 and 2004, respectively.

International revenues accounted for approximately 46% and 41% of total revenues for the three months ended September 30, 2005 and 2004, respectively, and 44% and 41% of total revenues for the nine months ended September 30, 2005 and 2004, respectively. Substantially all of our international revenues are generated in the EMEA (Europe, Middle East and Africa) and Asia Pacific regions. Revenues in the EMEA region represented 29% and 24% of total revenues for the three months ended September 30, 2005 and 2004, respectively, and 28% and 24% of total revenues for the nine months ended September 30, 2005 and 2004, respectively. The increase in the EMEA region as a percentage of total revenues is due to the efforts of our expanded sales force in EMEA. Revenues in the Asia Pacific region represented 13% of total revenues for the three months ended September 30, 2005 and 2004, and 12% and 13% of total revenues for the nine months ended September 30, 2005 and 2004, respectively. The only individual foreign country to account for 10% or more of total revenues for the periods presented was the United Kingdom, which represented approximately 14% and 12% of total revenues for the three months ended September 30, 2005 and 2004, respectively, and 14% and 11% of total revenues for the nine months ended September 30, 2005 and 2004, respectively. Substantially all of our revenues to date have been denominated in U.S. dollars. In the future, some portion of revenues may be denominated in foreign currencies.

Operating Expenses

Network Access

Network access expenses consist of charges for access, principally by the minute or time-based, that we pay to our network service providers.

	Three Months Ended September 30,		Change		Nine Months Ended September 30,		Change	
	2005	2004	$	%	2005	2004	$	%

(In thousands, except percentages)

Network access expenses	$ 10,568	$ 9,443	$ 1,125	11.9%	$ 31,423	$ 27,690	$ 3,733	13.5%
As a percent of revenue	25.2%	22.5%			24.3%	22.5%		

The growth in network access expenses in the three months ended September 30, 2005 as compared to the same period in 2004 was due to the higher costs of broadband access as it continues to comprise an increased portion of our total network access usage. The increase in network access expenses for the nine months ended September 30, 2005 as compared to the same periods in 2004 was due to increased usage of our virtual network as well as the higher costs of broadband access. We expect network access expenses to increase slightly as a percentage of revenues.

Network Operations

Network operations expenses consist of compensation and benefits for our network engineering, customer support, network access quality and information technology personnel, outside consultants, transaction center fees, depreciation of our network equipment, and certain allocated overhead costs.

	Three Months Ended September 30,		Change		Nine Months Ended September 30,		Change	
	2005	2004	$	%	2005	2004	$	%
	(In thousands, except percentages)							
Network operations expenses	$ 5,085	$ 4,752	$ 333	7.0%	$ 15,665	$ 14,169	$ 1,496	10.6%
As a percent of revenue	12.1%	11.3%			12.1%	11.5%		

The growth in network operations expenses in the three months ended September 30, 2005 as compared to the three months ended September 30, 2004 was due primarily to $340,000 in additional compensation and benefits expense due to an increase in personnel and $70,000 of additional depreciation expense related to the purchase of equipment for new and existing data centers. The increase was offset in part by a $160,000 decrease in consulting expenses. As we expand our operations, we expect that our network operations expenses will continue to increase in absolute dollars and increase slightly as a percentage of revenues.

The growth in network operations expenses in the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004 was due primarily to $940,000 in additional compensation and benefits expense due to an increase in personnel and $560,000 of additional depreciation expense related to the purchase of equipment for new and existing data centers. The increase as a percentage of revenues from the first nine months of 2004 to the first nine months of 2005 was due primarily to the expansion and support of our virtual network in conjunction with lower than anticipated revenues.

Research and Development

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

	Three Months Ended September 30,		Change		Nine Months Ended September 30,		Change	
	2005	2004	$	%	2005	2004	$	%
	(In thousands, except percentages)							
Research and development expenses	$ 4,237	$ 3,337	$ 900	27.0%	$ 13,084	$ 9,697	$ 3,387	34.9%
As a percent of revenue	10.1%	8.0%			10.1%	7.9%		

The increase in research and development expenses for the three months ended September 30, 2005 as compared to the three months ended September 30, 2004 was due primarily to an additional $720,000 of compensation and benefits expenses related to an increase in headcount. The remaining portion of the increase was due to various individually insignificant items. The increase as a percentage of revenues as well as absolute dollars was due to the acceleration of our development of new products as well as the increase in research and development personnel as a result of the two acquisitions that occurred in 2004 as we integrated those technologies with our own products an services. We expect that our research and development expenses will continue to increase in absolute dollars as we increase the number of our personnel and consultants to develop and enhance new and existing service offerings. We also expect research and development expenses to remain relatively constant or increase slightly as a percentage of revenues.

The increase in research and development expenses for the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004 was due primarily to an additional $2.3 million of compensation and benefits expenses related to an increase in headcount, and approximately $450,000 in fees paid to consultants to further develop our services. The remaining portion of the increase was due to various individually insignificant items.

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Sales and Marketing

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

	Three Months Ended September 30,		Change		Nine Months Ended September 30,		Change	
	2005	2004	$	%	2005	2004	$	%
	(In thousands, except percentages)							
Sales and marketing expenses	$ 12,227	$ 11,416	$ 811	7.1%	$ 37,975	$ 34,227	$ 3,748	11.0%
As a percent of revenue	29.2%	27.2%			29.4%	27.8%		

Sales and marketing expenses increased in absolute dollars in the three months ended September 30, 2005 as compared to the three months ended September 30, 2004 primarily due to an additional $510,000 in compensation and benefits expenses from the addition of sales personnel from the Safe3w, Inc. and Mobile Automation, Inc. acquisitions in September and October of 2004, respectively. There was also a $210,000 increase in direct marketing and a $110,000 increase in compensation and benefits expenses for additional marketing personnel. We expect that sales and marketing expenses will increase in absolute dollars to the extent revenues increase and as we expand our sales force and increase marketing activities and increase slightly as a percentage of revenues.

Sales and marketing expenses increased in absolute dollars in the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004 primarily due to an additional $2.3 million in compensation and benefits expenses from the addition of sales personnel from the Safe3w, Inc. and Mobile Automation, Inc. acquisitions in September and October of 2004, respectively. There was also a $740,000 increase in direct marketing expenses, a $410,000 increase in compensation and benefits expenses for additional marketing personnel and a $150,000 increase in trade show expenses. The remainder of the increase was due to various individually insignificant items.

General and Administrative

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

	Three Months Ended September 30,		Change		Nine Months Ended September 30,		Change	
	2005	2004	$	%	2005	2004	$	%
	(In thousands, except percentages)							
General and administrative expenses	$ 4,252	$ 4,513	$ (261)	(5.8)%	$ 13,064	$ 13,023	$ 41	0.3%
As a percent of revenue	10.2%	10.8%			10.1%	10.6%		

General and administrative expenses decreased slightly in absolute dollars as well as a percent of revenue for the three months ended September 30, 2005 as compared to the three months ended September 30, 2004. The decrease was due to a decrease in bad debt expense, offset in part by increases in various individually insignificant items. We expect that our general and administrative expenses will increase slightly in absolute dollars as well as a percentage of revenues.

General and administrative expenses were relatively constant in absolute dollars for the nine months ended September 30, 2005 as compared to the nine months ended September 30, 2004. The decrease as a percent of revenue was due to the increase in revenues over the prior year period, combined with general and administrative expenses remaining relatively constant.

Amortization of Stock-Based Compensation

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

	Three Months Ended September 30, 2005	Three Months Ended September 30, 2004	Change $	Change %	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004	Change $	Change %
	(In thousands, except percentages)							
Amortization of stock-based compensation	$ 237	$ 480	$ (243)	(50.6)%	$ 912	$ 1,890	$ (978)	(51.7)%
As a percent of revenue	0.6%	1.1%			0.7%	1.5%		

We expect to incur amortization of stock-based compensation expense of at least $225,000 for the remainder of 2005 and $500,000 in 2006. The amount of amortization of stock-based compensation expense to be recognized in future periods could decrease if stock options for which accrued but unvested compensation expense has been recorded are forfeited.

Non-Operating Expenses

Other Income, Net

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

Interest and other income includes interest income on cash, cash equivalents, and short-term investment balances and foreign exchange gains or losses. Interest income and other was $993,000 and $590,000 for the three months ended September 30, 2005 and 2004, respectively, and $2.7 million and $1.5 million for the nine months ended September 30, 2005 and 2004, respectively. The increase in interest and other income in 2005 was due primarily to an increase in the rate of return on our investments as compared to the same periods in 2004.

Provision for Income Taxes

The provision for income taxes was $1.5 million and $3.3 million for the three months ended September 30, 2005 and 2004, respectively, and $6.3 million and $9.4 million for the nine months ended September 30, 2005 and 2004, respectively. The decrease is due to a decrease in income before income taxes for the three and nine months ended September 30, 2005 as compared to the same periods in 2004 as well as an adjustment of approximately $750,000 relating to differences in 2004 estimates and the actual 2004 tax return and the 2004 research and development tax credit study completed in the quarter. Both adjustments to the provision for income taxes occurred in the three months ended September 30, 2005.

The effective tax rate was 26% and 39% for the three months ended September 30, 2005 and 2004, respectively. The effective tax rate for the nine months ended September 30, 2005 and 2004 was 35% and 39%, respectively. The decrease in the effective tax rate for the three and nine months ended September 30, 2005 was due primarily to an adjustment to the expected realization of tax credits related to research and development expenses.

Liquidity and Capital Resources

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

Net cash provided by operating activities was $25.2 million for the nine months ended September 30, 2005, compared to $26.6 million for the nine months ended September 30, 2004. This is due primarily due to a decrease in net income for the nine months ended September 30, 2005 as compared to the same period in 2004.

Net cash used in investing activities for the nine months ended September 30, 2005 was $33.1 million, compared to $49.2 for the nine months ended September 30, 2004. Net cash used in investing activities for the nine months ended September 30, 2005 comprised of net purchases of short-term investments of $30.3 million and purchases of property and equipment of $2.8 million. Net cash used in investing activities for the nine months ended September 30, 2004 comprised of net purchases of short-term investments of $35.8 million, net cash used in the acquisition of Safe3w of

$8.5 million and purchases of property and equipment of $4.9 million.

Net cash provided by financing activities for the nine months ended September 30, 2005 was $2.5 million, compared to $9.7 million for the nine months ended September 30, 2004. Net cash provided by financing activities for the first nine months of 2005 was due primarily to proceeds from employee stock option exercises. Net cash provided by financing activities in the first nine months of 2004 was due primarily to stock option exercises as well as proceeds from payments on stockholder notes receivable.

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As of September 30, 2005, our principal source of liquidity was $177.2 million of cash, cash equivalents and short-term investments.

Commitments

At September 30, 2005, we had no material commitments for capital expenditures.

We have signed contracts with some network service providers under which we have minimum purchase commitments that expire on various dates through February 2006. Other than in the approximately 22 countries in which our sole dial-up network service provider is Equant, we have contracted with multiple network service providers to provide alternative access points in a given geographic area. In those geographic areas where we provide access through multiple providers, we are able to direct users to the network of particular service providers. Consequently, we believe we have the ability to fulfill our minimum purchase commitments in these geographic areas.

In May 2005, we consolidated several term license agreements that were set to expire into a single, longer-term operating lease with a vendor. Future minimum purchase commitments and operating lease payments under these agreements as of September 30, 2005 are as follows (in thousands):

Year ending December 31:	
2005	$ 1,004
2006	1,387
2007	1,066
2008	1,066
2009	266
	$ 4,789

We lease our facilities under non-cancelable operating leases that expire at various dates through February 2010. Future minimum lease payments under these operating leases as of September 30, 2005 are as follows (in thousands):

Year ending December 31:	
2005	$ 1,014
2006	4,145
2007	4,279
2008	4,374
2009 and thereafter	5,764
	$ 19,576

Liquidity and Capital Resource Requirements

Based on past performance and current expectations, we believe that our cash and cash equivalents, short-term investments, and cash generated from operations will satisfy our working capital needs, capital expenditures, investment requirements, commitments, and other liquidity requirements associated with our existing operations through at least the next 18 months. In addition to our historical working capital needs, we may utilize cash resources to fund acquisitions of complementary businesses, technologies or product lines.

FACTORS AFFECTING OPERATING RESULTS

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

Risks Relating to Our Business

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

We have generated substantially all of our usage revenues to date from the sale of enterprise connectivity services using narrowband technologies such as modem dial-up. In some countries, including the United States, the use of narrowband as a primary means of enterprise connectivity has declined and is expected to continue to decline over time as broadband access technologies, such as cable modem, DSL, Wi-Fi and other wireless technologies, including 3G, become more broadly used. Although we have not generated substantial revenues from broadband access, a substantial portion of the growth of our business may depend upon our ability to expand the broadband elements of our virtual network. Such an expansion may not result in additional revenues to us. Key challenges in expanding the broadband elements of our virtual network include:

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

There are approximately 22 countries in which we provide dial-up access only through Equant. The loss of Equant as a dial-up network service provider would substantially diminish our ability to deliver global network access.

In approximately 22 countries, our sole dial-up network service provider is Equant. Network usage from access within these countries accounted for less than 2% of our revenues for the years ended December 31, 2004 and 2003 and for the three and nine months ended September 30, 2005. If we lose access to Equant s network and are unable to replace this access in some or all of these countries, our revenues would decline. In addition, our ability to market our services as being global would be impaired, which could cause us to lose customers. Our agreement with Equant expires in February 2006, but Equant may terminate the agreement earlier if we materially breach the contract and fail to cure the breach, or if we become insolvent. In addition, Equant has no obligation to continue to provide us with access to its network after February 2006. If Equant were to cease operations or terminate its arrangements with us, we would be required to enter into arrangements with other dial-up network service providers, which may not be available. This process could be costly and time consuming, and we may not be able to enter into these arrangements on terms acceptable to us.

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

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

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

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

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

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

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

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

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

We generate a substantial portion of our revenues from business conducted internationally. Revenues from customers domiciled outside of the United States were 44% of our revenue for the nine months ended September 30, 2005, of which approximately 28% and 12% were generated in our EMEA (Europe, Middle East and Africa) and Asia Pacific regions, respectively. Revenues from customers domiciled outside of the United States were 41% of our revenues for fiscal year 2004, of which approximately 24% and 13% were generated in our EMEA and Asia Pacific regions, respectively. Although we currently bill for our services in U.S. dollars, our international operations subject our business to specific risks. These risks include:

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

Any of these factors could negatively impact our business.

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

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

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

We have experienced, and in the future may experience, rapid growth in operations which has placed and could continue to place, a significant strain on our network operations, development of services, internal controls and other managerial, operating, and financial resources. If we do not manage future expansion effectively, our business will be harmed. To effectively manage any future expansion, we will need to improve our operational and financial systems and managerial controls and procedures, which include the following:

- managing our research and development efforts for new and evolving technologies;
- expanding the capacity and performance of our network and software infrastructure;

developing our administrative, accounting and management information systems and controls; and

effectively maintaining coordination among our various departments, particularly as we expand internationally.

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

We are at risk of being subject to securities class action lawsuits if our stock price declines substantially. Securities class action litigation has often been brought against a company following a decline in the market price of its securities. For example, in June 2004, we announced that we would not meet market expectations regarding our financial performance in the second quarter, and our stock price declined. On January 14, 2005, a lawsuit entitled Palumbo v. iPass, Inc., et al., Case No. C 05 228 MHP was filed in the United States District Court for the Northern District of California, purportedly on behalf of a class of investors who purchased iPass stock between April 22, 2004 and June 30, 2004, against us and some of our officers and directors. The complaint alleges claims under Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934. Several similar lawsuits were subsequently filed in the same court. In addition, on March 25, 2005, a lawsuit entitled Narendar Gupta, et al. v. Kenneth Denman, et al., Case No. CIV445765 was filed in the California Superior Court for the County of San Mateo against our directors and certain officers. We were also named as nominal defendants solely in a derivative capacity. On April 6, 2005, a similar lawsuit entitled Eugene Danielson v. Kenneth D. Denman, et al., No. CIV446034 was filed in that same court. The derivative actions are based on the same factual allegations and circumstances as the purported securities class actions and allege state law claims for insider trading, breach of fiduciary duty, abuse of control, gross mismanagement, waste of corporate assets, and unjust enrichment. We cannot predict the outcome of the lawsuits. If our stock price declines substantially in the future, we may be the target of similar litigation. The current, and any future, securities litigation could result in substantial costs and divert management s attention and resources, and could seriously harm our business.

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

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

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

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

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

We cannot be certain that our products do not, or will not, infringe upon patents, trademarks, copyrights or other intellectual property rights held by third parties, or that other parties will not assert infringement claims against us. From time to time we have been, and we may continue to be, involved in disputes with these third parties. Any claim of infringement of proprietary rights of others, even if ultimately decided in our favor, could result in substantial costs and diversion of our resources. Successful claims against us may result in an injunction or substantial monetary liability, in either case which could significantly impact our results of operations or materially disrupt the conduct of our business. If we are enjoined from using a technology, we will need to obtain a license to use the technology, but licenses to third-party technology may not be available to us at a reasonable cost, or at all.

New and potential new accounting pronouncements may impact our future financial position and results of operations.

There may be potential new accounting pronouncements or regulatory rulings, which may have an impact on our future financial position and results of operations. In particular, in December of 2004, the Financial Accounting Standards Board (FASB) issued a revised version of Statement No. 123 Accounting for Stock-Based Compensation (SFAS 123R), which supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS 123R requires recognition of the cost of employee services received in share-based payment transactions, thereby reflecting the economic consequences of those transactions in the financial statements. The accounting provisions for SFAS 123 are effective beginning with the first annual reporting period that begins after June 15, 2005, and we will be required to implement SFAS 123R beginning on January 1, 2006. The pro forma disclosures previously permitted under SFAS 123 will no longer be an alternative to financial statement recognition. Although we have not yet determined whether the adoption of SFAS 123R will result in amounts that are similar to the current pro forma disclosures under SFAS 123, we are evaluating the requirements under SFAS 123R and expect the adoption of SFAS 123R to have a significant adverse impact on our consolidated statements of income and net income per share.

Risks Relating to Our Industry

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

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

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

Our revenues and profitability depend on the overall demand for enterprise connectivity services. The general weakening of the global economy from early 2001 to 2003 led to decreased trade and corporate spending on Internet infrastructure. In addition, in the past, terrorist attacks, including the attacks on the United States and internationally, have had a significant impact on global economic conditions and our operations. If there are further acts of terrorism, if hostilities involving the United States and other countries continue or escalate, or if other future financial, political, economic and other uncertainties or natural disasters arise, this could lead to a reduction in travel, including by business travelers who are substantial users of our services, and continue to contribute to a climate of economic and political uncertainty that could adversely affect our revenue growth and financial results.

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

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

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Foreign Currency

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

Interest Rate Sensitivity

As of September 30, 2005, we had cash, cash equivalents, and short-term investments totaling $177.2 million. Our investment portfolio consists of money market funds and securities, asset backed securities, corporate securities, and government securities, generally due within one to two years. All of our instruments are held other than for trading purposes. We place investments with high quality issuers and limit the amount of credit exposure to any one issuer. These securities are subject to interest rate risks. Based on our portfolio content and our ability to hold investments to maturity, we believe that a hypothetical 10% increase or decrease in current interest rates would not materially affect our interest income.

As of December 31, 2004, we had cash, cash equivalents and short-term investments totaling $152.3 million, which consisted of cash and highly liquid short-term investments with original maturities of three months or less at the date of purchase, which we held solely for non-trading purposes.

The following is a chart of the principal amounts of short-term investments by expected maturity as of September 30, 2005 (in thousands):

	Expected Maturity Date for Par Value Amounts For the Year Ended December 31,				Total Cost	As of September 30, 2005
	2005	**2006**	**2007**	**2008**	**Value**	**Total Fair Value**
Government agencies	$ 48,145	$ 57,500	$ 10,500	$ 12,490	$ 130,110	$ 129,533
Corporate notes		15,915			16,313	16,205
Auction rate and money market securities	1,500	1,000			2,500	2,514
Total	$ 49,645	$ 74,415	$ 10,500	$ 12,490	$ 148,923	$ 148,252

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

Item 4. Controls and Procedures

Disclosure Controls and Procedures

We carried out an evaluation, under the supervision and with the participation of our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Securities Exchange Act Rules 13a-15(e) and 15d-15(e)), as of the end of the period covered by this report. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures are effective to provide reasonable assurance that the information required to be disclosed by us in our periodic SEC reports are recorded, processed, summarized and reported within the time periods specified in the in the SEC s rules and the SEC reports.

Changes in Internal Control Over Financial Reporting

In addition, there have been no changes in our internal controls over financial reporting during the quarter ended September 30, 2005 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

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

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On January 14, 2005, a lawsuit entitled *Palumbo v. iPass, Inc., et al.,* Case No. C 05 228 MHP was filed in the United States District Court for the Northern District of California, purportedly on behalf of a class of investors who purchased iPass stock between April 22, 2004 and June 30, 2004, against iPass and certain of its officers and directors. The complaint alleges that in April 2004 the defendants made misleading statements concerning the Company s projected revenues for the quarter ending June 30, 2004, and sets forth claims against the defendants under Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934 and seeks monetary damages to be proven at trial. Several similar lawsuits were subsequently filed in the same court, and all of the suits have since been consolidated into a single action. On April 22, 2005, the court appointed a lead plaintiff, and a consolidated amended complaint was filed by the lead plaintiff on July 5, 2005. All defendants filed a motion to dismiss on September 2, 2005. The motion is set for hearing in December 2005. This matter is at an early stage; no response to the complaint has been filed, no discovery has taken place and no trial date has been set. iPass and the individual defendants intend to take all appropriate actions to defend the suit. We cannot estimate any possible loss at this time.

On March 25, 2005, a stockholder purporting to act on our behalf filed a lawsuit entitled *Narendar Gupta, et al. v. Kenneth Denman, et al*., Case No. CIV445765 in the California Superior Court for the County of San Mateo against our directors and certain officers. iPass was also named as a nominal defendant solely in a derivative capacity. On April 6, 2005, a similar lawsuit entitled *Eugene Danielson v. Kenneth D. Denman, et al*., No. CIV446034 was filed in that same court. Both lawsuits were consolidated into a single action by stipulation and order dated April 26, 2005. The derivative action is based on the same factual allegations and circumstances as the purported securities class actions and alleges state law claims for insider trading, breach of fiduciary duty, abuse of control, gross mismanagement, waste of corporate assets, and unjust enrichment and seeks monetary damages on behalf of iPass to be proven at trial. This case is at an early stage; no consolidated complaint has been filed, no discovery has been taken and no trial date has been set. iPass and the individual defendants intend to take all appropriate action to defend these lawsuits. We cannot estimate any possible loss at this time.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.

Item 3. Defaults upon Senior Securities

Not applicable.

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

Not applicable.

Item 5. Other Information

Not applicable.

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Item 6. Exhibits

Exhibit Number	Description
3.1	Amended and Restated Certificate of Incorporation (1)
3.2	Bylaws, as amended (2)
4.1	Reference is made to Exhibits 3.1 and 3.2
4.2	Specimen stock certificate (2)
10.1	Changes in Officer Compensation and Option Grants (3)
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(1) Filed as an exhibit to iPass Quarterly report on Form 10-Q for the quarter ended September 30, 2003 (Commission No. 000-50327), filed November 13, 2003, and incorporated herein by reference.

(2) Filed as an exhibit to iPass Registration Statement on Form S-1 (No. 333-102715) and incorporated herein by reference.

(3) Incorporated by reference to the disclosure in Item 1.01 of the Registrant s Current Report on Form 8-K filed with the SEC on July 29, 2005.

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SIGNATURE

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

		iPass Inc.
Date: November 9, 2005	By	/s/ Frank E. Verdecanna
		Frank E. Verdecanna Vice President and Interim Chief Financial Officer (duly authorized officer and principal financial officer)

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