SOCKET COMMUNICATIONS INC
Form 10-K
March 07, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2007

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from _____ to _____

Commission file number 1-13810

SOCKET COMMUNICATIONS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-3155066**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

39700 Eureka Drive, Newark, CA 94560
(Address of principal executive offices including zip code)

(510) 933-3000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of Each Class	Name of Exchange on Which Registered
Common Stock, $0.001 Par Value per Share	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Exchange Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act YES [ ] NO [X]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES [ ] NO [X]

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [ ] Smaller reporting company [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES [ ] NO [X]

As of June 29, 2007, the aggregate market value of the registrant's common stock ($0.001 par value) held by non-affiliates of the registrant was $26,192,196 based on the closing sale price as reported on the National Association of Securities Dealers Automated Quotation Global Market System.

Number of shares of common stock ($0.001 par value) outstanding as of February 29, 2008: 32,015,975 shares

DOCUMENTS INCORPORATED BY REFERENCE

Items 10, 11, 12, 13, and 14 of Part III are incorporated by reference from the Registrant's Proxy Statement for the Annual Meeting of Stockholders to be held on April 23, 2008. Such Proxy Statement will be filed within 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

TABLE OF CONTENTS

PART I

This Annual Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements include statements forecasting future financial results and operating activities, market acceptance of our products, expectations for general market growth of handheld computers and other mobile computing devices, growth in demand for our products, expansion of the markets that we serve, expansion of the distribution channels for our products, adoption of our embedded products by third-party manufacturers of electronic devices, and the timing of the introduction and availability of new products, as well as other forecasts discussed under "Management's Discussion and Analysis of Financial Condition and Results of Operations." Words such as "may," "will," "predicts," "anticipates," "expects," "intends," "plans," "believes," "seeks," "estimates," variations of such words, and similar expressions are intended to identify such forward-looking statements. Such forward-looking statements are based on current expectations, estimates, and projections about our industry, management's beliefs, and assumptions made by management. These forward-looking statements are not guarantees of future performance and are subject to certain risks, uncertainties, and assumptions that are difficult to predict; therefore, actual results and outcomes may differ materially from what is expressed or forecasted in any such forward looking statements. Factors that could cause actual results and outcomes to differ materially include, but are not limited to: the risk of delays in the availability of our products due to technological, market or financial factors including the availability of necessary working capital; our ability to successfully develop, introduce and market future products; our ability to effectively manage and

contain our operating costs; the availability of announced third-party handheld computer hardware and software that our products are intended to work with; product delays associated with new model introductions and product changeovers by the makers of products that our products are intended to work with; continued growth in demand for handheld computers; market acceptance of emerging standards such as Bluetooth and Wireless LAN and of our related connection, data collection and mobile handheld computer products; the ability of our strategic relationships to benefit our business as expected; our ability to enter into additional distribution relationships; or other factors described in this Form 10-K including "Item 1A. Risk Factors" and recent Form 8-K and Form 10-Q reports filed with the Securities and Exchange Commission. We assume no obligation to update such forward-looking statements or to update the reasons why actual results could differ materially from those anticipated in such forward-looking statements.

You should read the following discussion in conjunction with the consolidated financial statements and notes included elsewhere in this report, and other information contained in other reports and documents filed from time to time with the Securities and Exchange Commission.

Item 1. Business

The Company

We are a producer of mobile systems serving the business market. Mobile systems solutions typically consist of a handheld computer, data collection and connectivity peripherals, and third-party vertical applications software. We have historically offered a wide range of data collection and connectivity peripheral products and embedded products for use with mobile computing devices offered by third-parties. Commencing in June 2007, we introduced our own mobile handheld computer and began offering mobile systems for use with third-party vertical applications software.

(Table of Contents)

See "Products" for a description of the products that we offer or plan to offer. We work with more than 100 software integration companies that are offering or developing vertical application software for use with handheld computers. Examples of these vertical applications include patient medication administration within the health care industry, retail merchandising such as managing inventory on retail store shelves, sales and field force automation involving the collection and processing of orders or service information from remote locations by sales and service personnel, asset management and inventory control for assets having bar codes or radio frequency identification tags, and mobile point of sale applications. These mobile solutions are designed to improve the productivity of business enterprises by automating manual tasks, improving the quality of information collected, and enhancing mobile productivity by processing and transferring information from remote locations and mobile devices to the business enterprise, and then if required, back to the remote locations and mobile devices.

We believe that growth in the mobile workforce, technical advances and cost reductions in mobile devices and networking technologies, and the pervasive use of the Internet are driving broader adoption of mobile data communications. Our products are designed to address the growing need for mobile workforce connectivity by enabling the use of handheld computers to extend data communications capabilities beyond location-dependent wired networks or telephone lines, thereby enabling handheld computer users to enhance their productivity, exploit time sensitive opportunities and improve customer satisfaction. Overall, our products enable the integration of hardware, software and applications into complete mobile data collection and connectivity solutions.

Total employee headcount on December 31, 2007 was 81 people. We subcontract the manufacturing of substantially all of our products to independent third-party contract manufacturers who are located in the U.S., China and Taiwan and who have the equipment, know-how and capacity to manufacture products to our specifications. We market our products through a worldwide network of distributors and resellers, as well as through original equipment manufacturers (OEMs), vertical industry partners, and value added resellers (VARs). See "Personnel," "Sales and Marketing," and "Manufacturing" for additional information about our personnel, sales and marketing and manufacturing operations.

We have financed our operations since inception primarily from the sale of equity capital and have no material long term debt. We also have a receivables-based working capital line of credit with a bank that we use for additional cash resources, and we typically draw on this line of credit at the end of each quarter. Our data collection, connectivity, serial, and mobile handheld computer products are offered as standard products through general distribution channels and can be supplied within a few weeks of being ordered, so we do not have a large order backlog. Our order backlog at December 31, 2007 was $1.4 million.

Socket Communications, Inc. was founded in March 1992 and reincorporated in Delaware in 1995. We began doing business as Socket Mobile, Inc. in January 2007 to better reflect our market focus on the mobile business market. Our Board of Directors is recommending to our stockholders a permanent name change to Socket Mobile, Inc. for approval at the Annual Meeting of Stockholders in April 2008. Our common stock trades on the NASDAQ Global Market under the symbol "SCKT". Our principal executive offices are located at 39700 Eureka Drive, Newark, CA 94560, and our phone number is (510) 933-3000. Our Internet home page is located at http://www.socketmobile.com; however, the information on, or that can be accessed through, our home page, is not part of this Annual Report. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to such reports are available free of charge on or through our Internet home page, as soon as reasonably practical after we electronically file such material with, or furnish it to, the Securities and Exchange Commission (SEC).

(Table of Contents)

Products

Our products may be classified into four broad product families:

- Mobile handheld computer products;
- Mobile peripheral products:
  - Data collection products,
  - Connectivity products;
- OEM embedded products; and
- Serial interface products.

Our *mobile handheld computer products* have been designed to address the business mobility market for a handheld computer that is neither a consumer-oriented handheld device nor a heavy duty industrial device. Our initial model, the SoMo 650 (SoMo is derived from Socket Mobile), introduced in June 2007, features the Microsoft Windows Mobile 5.0 Professional operating system to ensure a high level of mobile application compatibility and to give workers a familiar computing environment. Our mobile handheld computer is easy to customize and integrate with peripherals and information systems and has an expected product life cycle of three to five years which meets the needs of businesses for longer deployments than have been available with most consumer-oriented handheld devices. Our mobile handheld computer's features include Wireless LAN and Bluetooth, a fast processor, a large, bright screen display, large amounts of SDRAM and flash memory, extended battery life, programmable action buttons to activate

peripheral devices, reinforced CompactFlash and SDIO card slots, and a durable case. Additional models are in development that will run the Windows Mobile 6.0 operating system, add multiple language support, enable extended outdoor use, and offer specialized versions oriented to the needs of specific vertical markets. The SoMo 650 was specifically designed without an integrated mobile phone as most solutions involving our products use Bluetooth or Wireless LAN connections for data communications and do not require an integrated mobile phone. Mobile handheld computer products represented approximately 6 percent of our revenue for the year ended December 31, 2007.

Our mobile peripheral products consist of data collection products and connectivity products, which together represented approximately 60 percent, 58 percent, and 60 percent of our revenues for the years ended December 31, 2007, 2006, and 2005, respectively.

Our *data collection products* enable the electronic collection of data from bar codes, radio frequency identification tags, or magnetic stripes and consist of:

- bar code scanning products that plug into or connect wirelessly to handheld computers, tablet computers, notebook computers and smartphones that use Windows Mobile, Windows XP, Windows Tablet, J2ME, or Symbian 60 or Symbian 80 operating systems, and turn these devices into portable bar code scanners that can be used in various retail and industrial workplaces;
- radio frequency identification plug-in products that read radio frequency identification tags;
- a combination plug-in bar code scanner and radio frequency identification reader; and
- a plug-in magnetic stripe reader.

(Table of Contents)

We have developed extensive bar code scanning software called SocketScan that supports all of our data collection products, and have software developer kits that assist third-party developers in integrating our SocketScan software and our hardware products into their applications and solutions. Our bar code scanning products include CompactFlash and SDIO plug-in bar code scanners for linear and two-dimensional bar code scanning, along with a cordless handheld bar code scanner and a ring scanner worn on the index finger, both of which connect to computing systems using the Bluetooth standard for short-range wireless connectivity. Data collection products represented approximately 50 percent, 42 percent, and 39 percent of our revenue for the years ended December 31, 2007, 2006, and 2005, respectively.

Our *connectivity products* are connection devices that can be plugged into standard expansion slots in handheld computers, tablet computers, and notebook computers that use Windows Mobile, Windows XP, or Windows Tablet operating systems. These products allow users to connect their devices via Ethernet or telephone to communicate with other networks and devices such as desktop computers, other handheld, tablet and notebook computers, smartphones and printers. Our connectivity products include:

- modems for telephone connections that connect over a cable, and a cordless modem that utilizes Bluetooth wireless technology to connect a telephone to a Bluetooth-enabled computer or other device;
- ethernet cards for local area network connections that connect over a cable; and
- accessory products such as batteries and cables.

Connectivity products represented approximately 10 percent, 16 percent, and 22 percent of our revenue for the years ended December 31, 2007, 2006, and 2005, respectively.

Our *OEM embedded products* consist of Bluetooth and Wireless LAN modules and plug-in cards used primarily by OEMs of handheld computers and other devices to build wireless connection functions into their products using the Bluetooth and Wireless LAN standards for wireless connectivity. Our plug-in cards and modules using the Bluetooth standard for short-range wireless connectivity include extensive communications software enabling the use of these products. Our plug-in cards for connecting to local wireless networks using the Wireless LAN 802.11b/g (or Wi-Fi) standards include extensive communications software enabling the use of these products. We have recently added Cisco Compatible Extensions (CCX) 4.0 certification to our Wireless LAN software to enable our Wireless LAN products to be compatible with a Cisco wireless LAN infrastructure. Bluetooth and wireless LAN connection functions are being built into many third-party mobile devices, which may reduce the demand for our plug-in products through expansion slots but may increase the demand for our Bluetooth and Wireless LAN modules and embedded plug-in cards. OEM embedded products represented approximately 27 percent, 32 percent, and 27 percent of our revenue for the years ended December 31, 2007, 2006, and 2005, respectively.

(Table of Contents)

Our *serial interface products* enable the connection of a mobile computer to electronic devices either as a plug-in card (one, two or four ports) connecting over cables, or wirelessly over a Bluetooth network. We have recently introduced a USB to serial connector to enable a serial connection through a USB interface. Serial interface products represented approximately 7 percent, 10 percent, and 13 percent of our revenue for the years ended December 31, 2007, 2006, and 2005, respectively.

We target business customers and markets with our products. Most of our products, except our embedded products, are sold through distributors and resellers that service businesses. Our OEM embedded products are sold directly to the manufacturers of products in which our products are embedded. The geographic regions we serve include the Americas, Europe, the Middle East, Africa and Asia Pacific.

Market Dynamics

Handheld computers have evolved over the past several years from simple devices used mainly to hold personal information into small portable units with functionality similar to desktop PCs. Many handheld computers, such as the Pocket PC (including our SoMo line of mobile handheld computers) and Palm Treo, have built-in expansion capabilities in standard form factors, typically CompactFlash, Secure Digital Input/Output or Bluetooth, to allow for transfer of data in and out of the handheld computer over wireless or wired connections. Many handheld computers, such as the Palm Treo, Research-In-Motion's Blackberry and Windows Mobile handheld computer phone editions, often referred to as smartphones, also include an integrated phone to enable voice communications over mobile phone networks, and broadband radios for data communications. Notebooks and tablet computers also have expansion capabilities to enable their use in mobile environments, as well as broadband radios for data communications.

Advances in mobile network access and transfer speeds are enabling mobile computing device users to access the Internet, send and receive email including attachments, access corporate data files, and to transfer data directly to and from other mobile devices using Bluetooth wireless technology or cables for short distances, wireless local area networks, or broadband radios with increased speed and bandwidth. Our connectivity products and technologies (wireless LAN, Bluetooth and serial interface products) are designed to easily add these technologies to mobile devices. In addition, mobile devices with standard expansion capabilities are effective at collecting data. Our data collection products are designed to facilitate the collection of bar code, radio frequency identification, and magnetic stripe information on these devices by plugging into the standard expansion slots of these data collection devices or connecting wirelessly.

Handheld computers have traditionally been classified into consumer and industrial. Consumer devices such as those offered by Hewlett-Packard are designed for personal use and fit in a pocket or purse. Industrial devices such as those offered by Motorola are designed for rugged environments such as outdoors or warehouses and are much larger, heavier and more expensive. Businesses have had to choose from these two categories in designing mobile solutions, and we believe neither solution is an ideal fit for many business needs. Our first mobile handheld computer model introduced in June 2007 is a standard Windows Mobile OS based handheld device without telephony technology and is designed specifically to address essential business requirements to improve mobile worker productivity. Compared to consumer devices, it is similar in size and weight but is more durable, has programmable buttons to activate functions such as SocketScan, our data collection software, adds features such as seamless roaming to improve the worker experience in using wireless LAN, incorporates Socket's Connect!Agent to improve the user experience with short range cordless Bluetooth technology, has fast processors, large memory and extended battery life. Compared to industrial devices, it is smaller in size and weight, less rugged, and less expensive. We plan to introduce additional models to provide more choices to businesses that are deploying mobile computing solutions.

(Table of Contents)

Growth in the mobile workforce and increasing reliance on the Internet and on access to corporate databases and email are increasing the demand for mobile data communications. The capability of a mobile workforce to collect data in the field and to transfer it electronically generally improves the timeliness and accuracy of information such as order entry, process management or transaction reporting. Advances in connection technologies, local area networking and wide area networking are being commercialized to allow handheld computers to interact with nearby computers and with a wide array of electronic appliances, including mobile phones, printers, digital cameras, local area network access points, Global Positioning System receivers, automobile communications systems, bar code scanners, radio frequency identification tags, home entertainment and security systems, public kiosks, public Internet access locations and vending machines.

Current market dynamics driving the adoption of mobile data communications by enterprises include:

Functionality of today's mobile computing devices is extensive and improving. Unlike early models, most mobile computing devices now offer bright outdoor color screens and longer battery life, have software allowing their use as business messaging devices with capacity to store personal information, and have standard expansion capabilities or use Bluetooth or wireless local or wide area network connections to transfer data in and out of the device. Popular desktop programs such as Word and Excel are available for today's handheld, tablet and notebook computers, enabling users to send and receive emails with full attachments, run popular personal information management and business programs, run entertainment and education software for games, music or books, view and interact with the Internet with enhanced and feature-rich graphics, have direct access to corporate data files (subject to business security arrangements), and use instant messaging over mobile networks. Mobile devices also can become lightweight mobile bar code, radio frequency identification, and magnetic stripe scanning devices when used with our bar code scanning, radio frequency identification, or magnetic stripe reader products, enabling the capture and processing of bar code, radio frequency identification, or magnetic stripe information (such as credit or identification cards) in a mobile environment.

The mobile workforce is growing and is increasingly reliant on email and the Internet. The worldwide mobile workforce has been estimated at more than 20 percent of the global workforce. Before advancements in handheld computers and wireless networks over mobile phones and through wireless local area network access points, the mobile workforce had been unable to effectively stay connected with email, the Internet or corporate data except through telephone lines. With the growth in the use of the Internet and email for business and personal applications,

workers and consumers are increasingly dependent on access to the Internet and email for managing their business and personal lives. Recent improvements in wireless LAN and mobile phone connectivity for dial-up networking, and deployment of mobile computers by corporations to their mobile workforce are expected to be major factors driving growth in mobile data applications over the next several years.

(Table of Contents)

Third-party applications for enterprises are becoming available in increasing numbers. Third-party software applications are becoming increasingly available for the collection, processing and transfer of information by a mobile workforce. Mobile computing devices are being used for such diverse applications as checking patient medications when administering them in a hospital, capturing lot numbers of drug samples given to a doctor, managing the stocking of shelves in retail establishments, or entering sales orders from the field. Larger enterprise software companies such as Oracle Corporation have written applications for Windows Mobile devices that use our bar code scanning products. SAP has enabled our SDIO form factor scanning card in all mobile applications developed by SAP and by other vendors that interface with SAP solutions through SAP's NetWeaver Mobile program. We have supported the development and deployment of our products in third-party applications through our Vertical Industry Partners Program and more than 100 companies are participants in this program. Our Vertical Industry Partners Program is described more fully under "Sales and Marketing." The availability of productivity-enhancing application software is a major driver of enterprise deployment of mobile computing devices.

Marketing Strategy

Our marketing strategy has been to capitalize on our strategic relationships, expand and improve our product offerings including software to enable wireless and wired connections designed to provide an easy-to-use experience and adding a family of mobile handheld computers to our product lines, build a strong brand name, support the development of third-party software applications and integrator solutions, and encourage device manufacturers to build our technology directly into their products. With the introduction of our mobile handheld computer, we offer a complete hardware solution consisting of a mobile handheld computer and peripherals which allows VARs and integrators to offer a one-stop solution in combination with their own or third-party vertical software applications for the mobile workforce.

Capitalize on Strategic Relationships. We support and encourage direct endorsements and referrals for our products from our strategic relationships, including operating system providers, device manufacturers, third-party software developers, vertical industry partners, distributors, and end-user customers. We actively promote third-parties to integrate our products into their solutions through our Vertical Industry Partners Program. We have a team of employees that manages each strategic relationship, and we provide software developer kits, training and technical support to our software and hardware developers. We coordinate our product development efforts with Microsoft on an ongoing basis, with the goal of ensuring that our current and future products are compatible with new releases of Microsoft's operating systems. We spend extensive engineering time and resources to ensure that our data collection peripheral products are compatible with a wide variety of handheld computers including Pocket PCs, the Palm Treo, the Blackberry from Research-In-Motion, and smartphones using the Symbian 60 and 80 operating system. Dell is a direct reseller of our products including our SoMo family of mobile computers. We work closely with the sales teams of Dell and Hewlett-Packard to assist them in offering mobile device solutions that include our products.

(Table of Contents)

Expand and improve our product offerings. We offer a wide range of data collection and connectivity peripheral products that are used with our SoMo family of mobile computers and other mobile devices, and we encourage our distributors to carry the full range of our products. The goal is for customers to view Socket as a single source for their connection needs, instead of having to rely on individual product offerings from a number of different companies. During the past three years, we have introduced a number of hardware and software products, including a 56K plug-in modem in SDIO form factor, a radio frequency identification reader, a combination radio frequency identification reader and laser bar code scanner, a cordless ring bar code scanner designed to be worn on the index finger for use in package handling, an 802.11g upgrade to our CompactFlash 802.11b wireless LAN card, and a wireless LAN module to add embedded Wireless LAN to our OEM product offerings. We continue to add features to our Bluetooth software for Windows notebooks and tablets, our wireless local area network software and SocketScan, our bar code scanning and radio frequency identification software. During 2006, we upgraded our products to comply with the Reduction of Hazardous Substances (RoHS) rules being implemented in Europe and around the world by changing the solder used in our products to be lead-free. We also qualify our products with the agencies responsible for ensuring that electronic products meet worldwide standards for safety and performance.

Build a Stronger Brand Name. We are building a brand image of "Increasing Mobile Productivity." This image emphasizes quality and standards-based connectivity. Our products are "Mobility Friendly," which means products that are compact and designed to be mobile, low power to extend time between charges, and easy to use. Our focus is to work with our partners to develop productivity enhancing solutions for the mobile workforce. In January 2007, we began doing business as Socket Mobile, Inc. to emphasize our commitment to mobile computing solutions. Our overall company brand identity and positioning goal is to become "the leading provider of easy-to-deploy business mobility systems and peripherals."

Support the development of third-party software applications and integrator solutions. We have created software developer kits for many of our products including bar code scanning, radio frequency identification, Bluetooth, and Wireless LAN. In addition, we have employees dedicated to assisting developers and integrators with integrating our products into their solutions. Our Vertical Industry Partners Program includes over 100 companies that offer or are developing software solutions which incorporate Socket products. These solutions primarily involve data collection and address improving the productivity of the mobile workforce in a number of businesses including health care, field force automation, asset management, retail merchandising, and automotive/transportation.

Encourage device manufacturers to build our technology directly into their products. To capture the OEM embedded connection business, we have built relationships with certain mobile device manufacturers and work with them to integrate our Bluetooth and Wireless LAN modules and value-add software into their own product designs. The majority of these manufacturers are building vertical application devices for special purpose markets. We have an internal team of employees that manages our OEM products business. We also provide developer support to our mobile device manufacturer customers to assist them as needed to integrate our embedded products into their mobile devices.

(Table of Contents)

Competition and Competitive Risks

The overall market for data collection and connectivity products is both complex and competitive. Our products compete with similar products that are manufactured by companies in Asia and Europe. However, our longtime focus

on creating innovative data collection and connectivity solutions for the mobile workforce has resulted in good brand name recognition and reputation. We also believe that our brand name identifies our products as robust, dependable, small form factor, low power and easy to use, and the breadth of our product offerings, including the extensive features of our software, will continue to differentiate us relative to our competitors. The addition of a mobile handheld computer in 2007 enables us to better control the handheld computing environment for our peripheral products and allows us to offer one-stop shopping for the hardware portion of mobile business solutions. The competition in each of our product families is discussed in more detail below.

Handheld computers. Our first SoMo mobile handheld computer was introduced in June 2007 to address the price/performance market gap between consumer handheld computers and industrial handheld computers. Consumer-oriented handheld computers offer fewer features at a lower cost than industrial handheld computers. As described in Products - mobile handheld computer products, relative to a consumer-oriented handheld computer, our SoMo mobile handheld computer offers improved features beneficial in a business environment including increased durability, improved software features such as Wireless LAN roaming (staying connected between access points), and a combination of a fast processor, large memory, and multiple ways to access data including CompactFlash and Secure Digital plug-in slots and wireless LAN and Bluetooth technologies. The SoMo mobile handheld computer is less rugged than an industrial handheld computer but has many of the same features at a significantly reduced price point. We will continue to expand our family of SoMo mobile handheld computers to address the various needs of our enterprise customers. Consumer grade handheld computers are offered by Hewlett-Packard, Acer, Siemens and others. Industrial ruggedized grade of handheld computers are offered by Motorola, Intermec, and Honeywell. These companies have offered handheld computers for many years and have an established market presence. Their handheld computers are competitive alternatives to our mobile handheld computers, although we have differentiated our products for the markets that we have identified. In addition, in the past we have worked closely with handheld computer manufacturers to allow our peripheral products to work with their handheld computers, and we will continue to do so.

Data Collection Products. Our laser and CMOS imager bar code scanning products face competition from ruggedized integrated bar code scanning devices from Motorola, Intermec, Honeywell, Casio, Itronix and others. Many of these companies have been expanding their product lines to offer less expensive devices designed for enterprise use, which is narrowing the gap between the cost of consumer devices that use our peripheral data collection products and industrial devices. We purchase laser engines from Motorola and we have a license with Motorola to use these engines in our bar code scanning products. We also purchase imagers from Motorola and from other companies for use in our products. We face competition outside of the United States from a product similar to our plug-in bar code scanning card from BeInteractive, from products similar to our Cordless Hand Scanner from Baracoda, and from other competitive laser scanning products from Grabba (Australia) and Opticon (Japan). Motorola's patent position for laser bar code scanning tends to limit the sale of laser scanning bar code products by competitors in the United States, but a number of the Motorola patents will expire over the next several years, and we may face increasing competition from competitors both inside and outside the United States. We produce our laser bar code scanning products under a license from Motorola, which, to date, has not licensed these technologies to potential competitors. Motorola has historically been selective in licensing their technologies to third-parties. The continued availability of our licenses from Motorola and the continued absence of other licensees are dependent upon future licensing decisions by Motorola.

(Table of Contents)

In addition, companies such as Intermec have improved imager technology making such technology a viable alternative to laser scanning, and we expect both our laser and our imaging products to face more competition over

time from devices deploying imaging technology. Our laser scanning products are targeted to address specific market segments, such as patient medication administration within the health care industry, retail merchandising such as managing inventory on retail store shelves, sales and field force automation involving the collection and processing of orders or service information from remote locations by sales and service personnel, asset management and inventory control for assets having bar codes or radio frequency identification tags, and mobile point of sale applications.

Connectivity Products - Cable Connections. We are one of two principal manufacturers of low power Ethernet cards, the other being OvisLink. Our CompactFlash modem cards face competition from a number of manufacturers including Ambicom, Billionton Systems, Hawking, Zonet, OvisLink, Pharos, Trendware and Xircom. There are also a number of competitors that offer Bluetooth modems. These companies include Billionton Systems, ENR Technologies, Motorola, PSI, SiteCom, Sony, Typhoon, Trust, X Micro and Zoom.

OEM Embedded Products - Wireless Connections. We offer our wireless connection Bluetooth and Wireless LAN technologies in the form of modules for embedding in third party devices. We also offer CompactFlash plug-in cards and SDIO plug-in cards that may be plugged into the expansion slots of devices needing these technologies. We compete based on our brand name and customer support infrastructure, as well as software enhancements that provide ease-of-use, security features, and monitoring and troubleshooting tools.

Our Bluetooth and WLAN software works well with our hardware, providing us a complete solution for embedding Bluetooth and WLAN wireless connections into third-party devices. Manufacturers in Asia selling primarily hardware, such as Alps, Murata, and TaiyoYuden, along with integrators such as Bluesoft and Stonestreet One, are able to produce all or part of embedded solutions which may compete with our products and services. In addition, manufacturers of products that are sold in high volume may choose to build and support their own Bluetooth or WLAN connections.

Our Wireless LAN cards face competition in the market today principally from other manufacturers of low power Wireless LAN 802.11g cards, including Ambicom for CF cards, and AmbiCom, Spectec and Mobis for SDIO cards. The market for Bluetooth wireless communications technology is highly competitive. A number of companies offer competing CompactFlash Bluetooth cards including Ambicom, Brainboxes and Billionton.

Serial Interface Products. Our serial interface card products compete from time to time with similar products from small manufacturers including BeInteractive, Brainboxes, B&B Electronics, Elan Digital Systems, Quatech (now part of DPAC Technologies), and Ratoc Systems. We also offer a cordless serial adapter with Bluetooth wireless technology. Companies that offer competing Bluetooth serial products include AIRcable, Brainboxes, ConnectBlue, Digi International, Ezurio, Free 2 Move, Initium and Wavespeed.

(Table of Contents)

Proprietary Technology

We have developed a number of technological building blocks that enhance our ability to design new hardware and software products, to offer products which run on multiple software and hardware platforms, and to manufacture and package products efficiently.

One of our most important chip hardware building blocks is our proprietary mobility integrated circuit, which is a highly flexible interface for PC cards and CompactFlash cards that enables our products to work with all major handheld and notebook computers that have PC card or CompactFlash slots, regardless of their design. We have

incorporated our mobility integrated circuit into a broad range of our peripheral products to control signal transmission between these products and the handheld or notebook computer's PC card or CompactFlash slot.

Another area of intellectual property is our expertise in embedded radio-dependent firmware. Within our Bluetooth cordless products are software and firmware that include a wide variety of functions to enable efficient radio control and overall systems functionality. For cordless bar code scanning and radio frequency identification reading, this includes our patented Error Proof Protocol, which is designed to ensure that scanned data is correctly received by the mobile computing device and allow for real-time validation of data and error notification to the user.

We have developed a library of software drivers and control modules that allow our products to operate in handheld computers running the Windows Mobile operating systems and in notebooks running various Windows and third-party operating systems. We have been awarded ten U.S. Patents and seven design patents covering various inventions that relate to mobile products and to the designs of our products. In July 2004 we also acquired from Khyber Technologies a U.S. patent entitled Card Shaped Computer Peripheral Device. The patent is a basic patent covering the design and functioning of plug-in bar code scanners, bar code imagers, and radio frequency identification products. We have additional patents covering our proprietary technology pending with the U.S. Patent and Trademark Office.

We have developed a number of software programs that provide unique functions and features for our connection and data collection products. For example, our SocketScan software enables all of our bar code scanning products to scan a variety of bar codes and to route the scanned data to many different types of data files. Our Bluetooth software used in conjunction with our Bluetooth hardware provides a completely functional Bluetooth solution enabling connections and data transfers between Bluetooth-enabled devices. Our wireless local area network software that is integrated with our wireless local area network management software (which we call Wi-Fi Companion and have introduced a version with Cisco Compatible Extension protocols called Enhanced Wi-Fi Companion or e-WFC) and used in conjunction with our wireless local area network hardware, provides a completely functional wireless local area network solution, enabling connections and data transfers from mobile computing devices over wireless local area networks.

We have registered trademarks with the U.S. Patent and Trademark Office for "Socket" our logo, the term "Go-WiFi" associated with our Wireless LAN products and have a trademark registration pending for "SoMo" for our mobile handheld computer.

(Table of Contents)

We rely on a combination of patent, copyright, trademark and trade secret laws, and confidentiality procedures to protect our proprietary rights. As part of our confidentiality procedures, we generally enter into non-disclosure agreements with our employees, distributors and strategic partners, and limit access to our software, documentation and other proprietary information. Despite these precautions, it may be possible for a third-party to copy or otherwise obtain and use our products or technology without authorization, or to develop similar technology independently. In addition, we may not be able to effectively protect our intellectual property rights in certain foreign countries. From time to time we receive communications from third-parties asserting that our products infringe, or may infringe, their proprietary rights. In connection with any such claims, litigation could be brought against us that could result in significant additional expenses or compel us to discontinue or redesign some of our products.

Personnel

Our future success will depend in significant part upon the continued service of certain of our key technical and senior management personnel, and our continuing ability to attract, assimilate and retain highly qualified technical, managerial and sales and marketing personnel. Our total employee headcount as of December 31, 2007 was 81 people. Our employees are not represented by a union, and we consider our employee relationships to be good.

Sales and Marketing

During the year ended December 31, 2007, 65 percent of our sales were in North America, 27 percent in Europe, and 8 percent in Asia and Pacific Rim countries. During the year ended December 31, 2006, 68 percent of our sales were in North America, 24 percent in Europe and 8 percent in Asia and Pacific Rim countries. During the year ended December 31, 2005, 65 percent of our sales were in North America, 24 percent in Europe, and 11 percent in Asia and Pacific Rim countries. Export sales are subject to the complications of complying with laws of various countries and the risk of import/export restrictions and tariff regulations.

We market our products through a worldwide network of distributors and resellers, as well as through OEMs and VARs. In addition, we have more than 100 companies that are participants in our Vertical Industry Partners Program. Participants offer or intend to offer third-party software applications that utilize our products in their software solutions. Vertical market segments addressed by participants include health care, field force automation, retail merchandising, automotive/transportation, and asset management. Applications include checking patient medications when administering them in a hospital, capturing lot numbers of drug samples given to a doctor, managing the stocking of shelves in retail establishments, entering sales orders from the field, taking inventory of bar coded items, and entering and updating information in an enterprise data base. We support our distributors, resellers and integrators with software developer kits and by providing education, training and customer assistance through our sales, marketing, and technical support staff in the U.S., Europe and Asia-Pacific regions. As of December 31, 2007, we had 32 people in sales and marketing.

Our United States distributor Tech Data Corp. accounted for 23 percent of our revenue in 2007, 26 percent of our revenue in 2006 and 28 percent of our revenue in 2005. Our United States distributor Ingram Micro, Inc. accounted for 13 percent of our revenue in 2007 and 14 percent of our revenue in each of 2006 and 2005. We intend to increase our sales and marketing effort during 2008 by adding personnel and increasing promotional activities, particularly in support of our distributors and vertical industry partners.

(Table of Contents)

Consistent with industry practice, we provide our distributors with stock balancing and price protection rights which permit these distributors to return slow-moving products to us for credit, and to receive price adjustments for inventories of our products held by the distributors if we lower the price of those products. The immediate effect of returns and adjustments on our quarterly operating results is limited, since we recognize revenues on products shipped to distributors only at the time the merchandise is sold by the distributor. To date, we have not experienced any significant returns or price protection adjustments.

We rely significantly on our OEMs, distributors, and resellers for marketing and distribution of our products. Our agreements with OEMs, distributors, and resellers generally are nonexclusive and may be terminated on short notice by either party without cause. Furthermore, our OEMs, distributors and resellers are not within our control, are not obligated to purchase products from us, and may represent other lines of products, including those of our competitors. If any OEMs, distributors, or resellers reduce or discontinue efforts to sell our products, our revenues and operating results could be materially adversely affected.

Manufacturing

We subcontract the manufacturing of substantially all of our products to independent third-party contract manufacturers who are located in the U.S., China, and Taiwan and who have the equipment, know-how and capacity to manufacture products to our specifications. We perform final product testing and package our products at our Newark, California facility for most of our sales. As of December 31, 2007, we had 24 people employed in manufacturing operations, including planning, buying, manufacturing engineering, quality control, product assembly, shipping and receiving, MIS and product support. We augment this workforce with temporary employees on an as-needed basis.

Certain of our product components are available from only one vendor. These sole sourced components include the interface chip that controls the signal transmission between all of our plug-in CompactFlash products (except our Ethernet and Wireless LAN cards) and the card slot on the mobile computer, our Ethernet and Wireless LAN chips, our laser scanning engines, our SDIO plug-in cards, certain cable and connector components and, beginning in 2007, our mobile handheld computer. Although to date we have generally been able to obtain adequate supplies of these components, these components are generally purchased on a purchase order basis under standard commercial terms and conditions, and we do not have long-term supply contracts for these components. Accordingly, the manufacturers could stop providing these components to us at any time. Alternatively, although our suppliers are generally large, well-financed organizations, they could encounter financial difficulties that interfere with our product supplies. In such an event, we could experience a decline in revenues until we establish sufficient manufacturing supply through an alternative source. Locating and qualifying alternative suppliers, and commencing new manufacturing operations, could take a significant period of time, although we believe that we can relocate manufacturing or find alternative suppliers for sole sourced components should it become necessary. We generally stock higher inventory quantities of sole sourced components as safety stocks to mitigate the risk of supply disruption.

(Table of Contents)

Research and Development

Since our inception, we have made substantial investments in research and development. Research and development expenditures were $5.0 million in 2007, $5.1 million in 2006, and $3.5 million in 2005. The increased expenditures in 2007 and 2006 were in part due to an increase in the number of development projects including the removal of lead from our products as required by the Reduction in Hazardous Substances Act and new product development costs for our cordless ring scanner, our mobile handheld computer and our software programs including SocketScan, Wireless LAN and Bluetooth. We believe that our future performance will depend in large part on our ability to develop significant enhancements to our existing products, including technology upgrades and additional features, and to develop successful new products for emerging and existing markets.

As of December 31, 2007, we had 16 people on our product development staff, and we hire engineering consultants to perform additional engineering services as required. We anticipate that we will continue to commit substantial resources to research and development in the future.

General and Administration

As of December 31, 2007, we had 9 people responsible for our financial and administrative activities including accounting and finance, personnel, and administrative support.

(Table of Contents)

Item 1A. Risk Factors

We have a history of operating losses and may not achieve ongoing profitability.

We were unprofitable in each of the quarters in fiscal years 2007 and 2006. We were profitable in two quarters in 2005, but unprofitable for fiscal year 2005. Fiscal year 2004 was the first profitable year in our history, but only to the extent of $288,000. Prior to 2004, we incurred significant operating losses in each financial period since our inception. To achieve ongoing profitability, we must accomplish numerous objectives, including growth in our business and the development of successful new products. We cannot foresee with any certainty whether we will be able to achieve these objectives in the future. Accordingly, we may not generate sufficient net revenue to achieve ongoing profitability. If we cannot achieve ongoing profitability, we will not be able to support our operations from positive cash flows, and we would use our existing cash to support operating losses. If we are unable to secure the necessary capital to replace that cash, we may need to suspend some or all of our current operations.

We may require additional capital in the future, but that capital may not be available on reasonable terms, if at all, or on terms that would not cause substantial dilution to your stock holdings.

Although we do not anticipate the need to raise additional capital during the next twelve months to fund our operations, we may incur operating losses in future quarters and may need to raise capital to fund these losses. Our forecasts are highly dependent on factors beyond our control, including market acceptance of our products and sales of handheld computers. If capital requirements vary materially from those currently planned, we may require additional capital sooner than expected. There can be no assurance that such capital will be available in sufficient amounts or on terms acceptable to us, if at all. In addition, the availability of our bank line is dependent upon our meeting certain covenants, including maintaining minimum cash balances. Future operating losses could cause us to lose the availability of our bank line as a result of becoming non-compliant with these covenants.

Our Common Stock will become ineligible for listing on the NASDAQ Global Market or alternatively the NASDAQ Capital Market if it does not trade at or above $1.00, which would materially adversely affect the liquidity and price of our Common Stock.

We are listed on the NASDAQ Global Market. Our continued listing is contingent on meeting specific quantitative standards, including a minimum closing bid price of $1.00. Our Common Stock has traded below $1.00 for significant periods during the last twelve months. In particular, our stock failed to maintain a minimum closing bid price of at least $1.00 in the 30 consecutive business days prior to December 10, 2007. On December 10, 2007 we received a staff deficiency notice from the Listing Qualifications Department of the NASDAQ Stock Market which stated that our stock will have to achieve a minimum closing bid price of at least $1.00 for at least 10 consecutive business days within 180 calendar days, or by June 9, 2008, or else we may be delisted from the NASDAQ Global Market. As of March 6, 2008, our Common Stock has not achieved the minimum closing bid price of $1.00 on any single day since receipt of the deficiency notice. Should we be delisted from the NASDAQ Global Market, we may be eligible for listing on the NASDAQ Capital Market, subject to meeting specific quantitative standards, including maintaining a minimum closing bid price of $1.00, and would have to achieve that within the 180 calendar days of initial listing on the NASDAQ Capital Market.

(Table of Contents)

If our Common Stock becomes ineligible for listing on either the NASDAQ Global Market or the NASDAQ Capital Market, and is thereafter traded only on the over-the-counter market, our stockholders' abilities to purchase and sell our Common Stock could be less orderly and efficient and more costly. Furthermore, a delisting of our Common Stock could have a materially adverse impact on our business operations by damaging our general business reputation, impairing our ability to obtain additional capital, reducing the incentives that equity ownership is intended to provide to our employees, and causing a loss of confidence by investors, suppliers and employees. As a result of the negative impact on the liquidity of our Common Stock and on our business, a delisting would also likely decrease the market price of our Common Stock and increase the volatility of our stock price.

If third parties do not produce and sell innovative products with which our products are compatible, or if our line of mobile handheld computers is not successful, we may not achieve our sales projections.

Our success has been dependent upon the ability of third parties in the mobile personal computer industry to complete development of products that include or are compatible with our technology and then to sell these products into the marketplace. Even if we are successful in marketing and selling our new line of mobile handheld computers, our ability to generate increased revenue depends significantly on the commercial success of Windows-mobile handheld devices, particularly the Pocket PC and other devices such as the line of handhelds with expansion options offered by Palm, and the adoption of these handheld computers for business use. If manufacturers are unable or choose not to ship new products such as Pocket PC and other Windows-mobile devices or Palm devices, or experience difficulties with new product transitions that cause delays in the market as we experienced in fiscal years 2005, 2006 and 2007, or if these products, including our new line of mobile handheld computers of which we began shipping our first model in June of 2007, fail to achieve or maintain market acceptance, the number of our potential new customers would be reduced and we would not be able to meet our sales expectations.

If we fail to develop and introduce new products rapidly and successfully, we will not be able to compete effectively, and our ability to generate sufficient revenues will be negatively affected.

The market for our products is prone to rapidly changing technology, evolving industry standards and short product life cycles. If we are unsuccessful at developing and introducing new products and services on a timely basis that include the latest technologies conforming to the newest standards and that are appealing to end users, we will not be able to compete effectively, and our ability to generate significant revenues will be seriously harmed.

(Table of Contents)

The development of new products and services can be very difficult and requires high levels of innovation. The development process is also lengthy and costly. Short product life cycles expose our products to the risk of obsolescence and require frequent new product introductions. We will be unable to introduce new products and services into the market on a timely basis and compete successfully, if we fail to:

- identify emerging standards in the field of mobile computing products;
- enhance our products by adding additional features;
- invest significant resources in research and development, sales and marketing, and customer support;

- maintain superior or competitive performance in our products; and
- anticipate our end users' needs and technological trends accurately.

We cannot be sure that we will have sufficient resources to make adequate investments in research and development or that we will be able to identify trends or make the technological advances necessary to be competitive.

A significant portion of our revenue currently comes from two distributors, and any decrease in revenue from these distributors could harm our business.

A significant portion of our revenue comes from two distributors, Tech Data Corp. and Ingram Micro, Inc., which together represented approximately 36 percent, 40 percent, and 42 percent of our worldwide revenue in fiscal years 2007, 2006, and 2005, respectively. We expect that a significant portion of our revenue will continue to depend on sales to Tech Data Corp. and Ingram Micro, Inc. We do not have long-term commitments from Tech Data Corp. or Ingram Micro, Inc. to carry our products. Either could choose to stop selling some or all of our products at any time, and each of these companies also carries our competitors' products. If we lose our relationship with Tech Data Corp. or Ingram Micro, Inc., we would experience disruption and delays in marketing our products.

If the market for mobile computers experiences delays, or fails to grow, we will not achieve our sales projections.

Substantially all of our peripheral products are designed for use with mobile personal computers, including handhelds, notebook computers, tablets and smartphones. If the mobile personal computer industry does not grow, if its growth slows, or if product or operating system changeovers by mobile computer manufacturers and partners cause delays in the market, as we experienced in the past three years, or if the markets for our mobile handheld computers do not grow, we will not achieve our sales projections.

Our sales will be hurt if the new technologies used in our products do not become widely adopted, or are adopted slower than expected.

Many of our products use new technologies, such as 2D bar code scanning and radio frequency identification, which are not yet widely adopted in the market. If these technologies fail to become widespread, or are adopted slower than expected, our sales will suffer.

(Table of Contents)

We could face increased competition in the future, which would adversely affect our financial performance.

The market for handheld computers in which we operate is very competitive. Our future financial performance is contingent on a number of unpredictable factors, including that:

- some of our competitors have greater financial, marketing, and technical resources than we do;
- we periodically face intense price competition, particularly when our competitors have excess inventories and discount their prices to clear their inventories; and
- certain OEMs of personal computers, mobile phones and handheld computers offer built-in functions, such as Bluetooth wireless technology, Wi-Fi, or bar code scanning, that compete with our products.

Increased competition could result in price reductions, fewer customer orders, reduced margins, and loss of market share. Our failure to compete successfully against current or future competitors could harm our business, operating results and financial condition.

If we do not correctly anticipate demand for our products, our operating results will suffer.

The demand for our products depends on many factors and is difficult to forecast. We expect that it will become more difficult to forecast demand as we introduce and support more products and as competition in the market for our products intensifies. If demand increases beyond forecasted levels, we would have to rapidly increase production at our third party manufacturers. We depend on suppliers to provide additional volumes of components, and suppliers might not be able to increase production rapidly enough to meet unexpected demand. Even if we were able to procure enough components, our third party manufacturers might not be able to produce enough of our devices to meet our customer demand. In addition, rapid increases in production levels to meet unanticipated demand could result in higher costs for manufacturing and supply of components and other expenses. These higher costs could lower our profit margins. Further, if production is increased rapidly, manufacturing yields could decline, which may also lower operating results.

If demand is lower than forecasted levels, we could have excess production resulting in higher inventories of finished products and components, which could lead to write-downs or write-offs of some or all of the excess inventories, and reductions in our cash balances. Lower than forecasted demand could also result in excess manufacturing capacity at our third party manufacturers and in our failure to meet minimum purchase commitments, each of which may lower our operating results.

We rely primarily on distributors, resellers, and OEMs to sell our products, and our sales would suffer if any of these third parties stops selling our products effectively.

Because we sell our products primarily through distributors, resellers, and OEMs, we are subject to risks associated with channel distribution, such as risks related to their inventory levels and support for our products. Our distribution channels may build up inventories in anticipation of growth in their sales. If such growth in their sales does not occur as anticipated, the inventory build up could contribute to higher levels of product returns. The lack of sales by any one significant participant in our distribution channels could result in excess inventories and adversely affect our operating results.

(Table of Contents)

Our agreements with distributors, resellers, and OEMs are generally nonexclusive and may be terminated on short notice by them without cause. Our distributors, resellers, and OEMs are not within our control, are not obligated to purchase products from us, and may offer competitive lines of products simultaneously. Sales growth is contingent in part on our ability to enter into additional distribution relationships and expand our sales channels. We cannot predict whether we will be successful in establishing new distribution relationships, expanding our sales channels or maintaining our existing relationships. A failure to enter into new distribution relationships or to expand our sales channels could adversely impact our ability to grow our sales.

We allow our distribution channels to return a portion of their inventory to us for full credit against other purchases. In addition, in the event we reduce our prices, we credit our distributors for the difference between the purchase price of products remaining in their inventory and our reduced price for such products. Actual returns and price protection may adversely affect future operating results, particularly since we seek to continually introduce new and enhanced

products and are likely to face increasing price competition.

We depend on alliances and other business relationships with a small number of third parties, and a disruption in any one of these relationships would hinder our ability to develop and sell our products.

We depend on strategic alliances and business relationships with leading participants in various segments of the communications and mobile handheld computer markets to help us develop and market our products. Our strategic partners may revoke their commitment to our products or services at any time in the future or may develop their own competitive products or services. Accordingly, our strategic relationships may not result in sustained business alliances, successful product or service offerings, or the generation of significant revenues. Failure of one or more of such alliances could result in delay or termination of product development projects, failure to win new customers, or loss of confidence by current or potential customers.

We have devoted significant research and development resources to design activities for Windows-mobile products, Palm devices, smartphones using Windows Mobile and Symbian System 60 and 80 operating systems, and more recently, to develop our own family of mobile handheld computers. Such design activities have diverted financial and personnel resources from other development projects. These design activities are not undertaken pursuant to any agreement under which Microsoft, Palm, or Symbian is obligated to continue the collaboration or to support the products produced from the collaboration. Consequently, these organizations may terminate their collaborations with us for a variety of reasons, including our failure to meet agreed-upon standards or for reasons beyond our control, such as changing market conditions, increased competition, discontinued product lines, and product obsolescence.

Our intellectual property and proprietary rights may be insufficient to protect our competitive position.

Our business depends on our ability to protect our intellectual property. We rely primarily on patent, copyright, trademark, trade secret laws, and other restrictions on disclosure to protect our proprietary technologies. We cannot be sure that these measures will provide meaningful protection for our proprietary technologies and processes. We cannot be sure that any patent issued to us will be sufficient to protect our technology. The failure of any patents to provide protection to our technology would make it easier for our competitors to offer similar products. In connection with our participation in the development of various industry standards, we may be required to license certain of our patents to other parties, including our competitors, that develop products based upon the adopted standards.

(Table of Contents)

We also generally enter into confidentiality agreements with our employees, distributors, and strategic partners, and generally control access to our documentation and other proprietary information. Despite these precautions, it may be possible for a third party to copy or otherwise obtain and use our products, services, or technology without authorization, develop similar technology independently, or design around our patents.

Effective copyright, trademark, and trade secret protection may be unavailable or limited in certain foreign countries. Furthermore, certain of our customers have entered into agreements with us which provide that the customers have the right to use our proprietary technology in the event we default in our contractual obligations, including product supply obligations, and fail to cure the default within a specified period of time.

We may become subject to claims of intellectual property rights infringement, which could result in substantial liability.

In the course of operating our business, we may receive claims of intellectual property infringement or otherwise become aware of potentially relevant patents or other intellectual property rights held by other parties. Many of our competitors have large intellectual property portfolios, including patents that may cover technologies that are relevant to our business. In addition, many smaller companies, universities, and individuals have obtained or applied for patents in areas of technology that may relate to our business. The industry is moving towards aggressive assertion, licensing, and litigation of patents and other intellectual property rights. In June 2007, we received a letter from Wi-LAN Inc., accusing certain of our wireless LAN products of infringing two U.S. and one Canadian patent held by Wi-LAN Inc. In October 2007, Wi-LAN Inc. filed patent infringement lawsuits against a number of companies alleging that those companies infringe the two U.S. patents by manufacturing, using, or offering for sale products with wireless capability compliant with the IEEE 802.11 standards. Wi-LAN Inc. is asking for money damages and a court order barring the sale of products that use the patented technology. We have not been named in the lawsuit, and we do not plan to make any changes to our current business at this time. Nonetheless, we may be added to the lawsuit in the future, and even if we are not, the outcome of this lawsuit may result in future changes to our business, including potential increased costs for those of our products that make use of the related technology. In October 2007, we received a letter from WIAV Solutions, LLC, offering to license the wireless technology covered by two U.S. patents held by WIAV Solutions, LLC. To date we have not entered into discussions to license their technology.

If we are unable to obtain and maintain licenses on favorable terms for intellectual property rights required for the manufacture, sale, and use of our products, particularly those products which must comply with industry standard protocols and specifications to be commercially viable, our results of operations or financial condition could be adversely impacted.

(Table of Contents)

In addition to disputes relating to the validity or alleged infringement of other parties' rights, we may become involved in disputes relating to our assertion of our own intellectual property rights. Whether we are defending the assertion of intellectual property rights against us or asserting our intellectual property rights against others, intellectual property litigation can be complex, costly, protracted, and highly disruptive to business operations by diverting the attention and energies of management and key technical personnel. Plaintiffs in intellectual property cases often seek injunctive relief, and the measures of damages in intellectual property litigation are complex and often subjective or uncertain. Thus, any adverse determinations in this type of litigation could subject us to significant liabilities and costs.

New industry standards may require us to redesign our products, which could substantially increase our operating expenses.

Standards for the form and functionality of our products are established by standards committees. These independent committees establish standards, which evolve and change over time, for different categories of our products. We must continue to identify and ensure compliance with evolving industry standards so that our products are interoperable and we remain competitive. Unanticipated changes in industry standards could render our products incompatible with products developed by major hardware manufacturers and software developers. Should any major changes, even if anticipated, occur, we would be required to invest significant time and resources to redesign our products to ensure compliance with relevant standards. If our products are not in compliance with prevailing industry standards for a significant period of time, we would miss opportunities to sell our products for use with new hardware components from mobile computer manufacturers and OEMs, thus affecting our business.

Undetected flaws and defects in our products may disrupt product sales and result in expensive and time-consuming remedial action.

Our hardware and software products may contain undetected flaws, which may not be discovered until customers have used the products. From time to time, we may temporarily suspend or delay shipments or divert development resources from other projects to correct a particular product deficiency. Efforts to identify and correct errors and make design changes may be expensive and time consuming. Failure to discover product deficiencies in the future could delay product introductions or shipments, require us to recall previously shipped products to make design modifications, or cause unfavorable publicity, any of which could adversely affect our business and operating results.

(Table of Contents)

Our quarterly operating results may fluctuate in future periods, which could cause our stock price to decline.

We expect to experience quarterly fluctuations in operating results in the future. We generally ship orders as received, and as a result we may have little backlog. Quarterly revenues and operating results therefore depend on the volume and timing of orders received during the quarter, which are difficult to forecast. Historically, we have often recognized a substantial portion of our revenue in the last month of the quarter. This subjects us to the risk that even modest delays in orders may adversely affect our quarterly operating results. Our operating results may also fluctuate due to factors such as:

- the demand for our products;
- the size and timing of customer orders;
- unanticipated delays or problems in our introduction of new products and product enhancements;
- the introduction of new products and product enhancements by our competitors;
- the timing of the introduction of new products that work with our connection products;
- changes in the revenues attributable to royalties and engineering development services;
- product mix;
- timing of software enhancements;
- changes in the level of operating expenses;
- competitive conditions in the industry including competitive pressures resulting in lower average selling prices; and
- timing of distributors' shipments to their customers.

Because we base our staffing and other operating expenses on anticipated revenues, delays in the receipt of orders can cause significant variations in operating results from quarter to quarter. As a result of any of the foregoing factors, or a combination, our results of operations in any given quarter may be below the expectations of public market analysts or investors, in which case the market price of our common stock would be adversely affected.

The loss of one or more of our senior personnel could harm our existing business.

A number of our officers and senior managers have been employed for thirteen to sixteen years by us, including our President, Executive Vice President, Chief Financial Officer, and Chief Technical Officer. Our future success will depend upon the continued service of key officers and senior managers. Competition for officers and senior managers is intense, and there can be no assurance that we will be able to retain our existing senior personnel. The loss of one or more of our officers or key senior managers could adversely affect our ability to compete.

Beginning January 1, 2006 we began to expense options granted under our employee stock plans as compensation, and as a result our net income and earnings per share were negatively affected, we may continue to have net losses as a result of the requirement to expense options, and may find it necessary to change our

business practices to attract and retain employees.

Historically, we have used stock options as a key component of our employee compensation packages. We believe that stock options provide an incentive to our employees to maximize long-term stockholder value and, through the use of vesting, encourage valued employees to remain with us. The expensing of employee stock options adversely affected our net income and earnings per share in each of the quarters in fiscal years 2007 and 2006, will continue to adversely affect future quarters, and will make profitability harder to achieve or make our future profits or net losses worse. In addition, we may decide in response to the effects of expensing stock options on our operating results to reduce the number of stock options granted to employees or to grant options to fewer employees. This could adversely affect our ability to retain existing employees and attract qualified candidates, and also could increase the cash compensation we would have to pay to them.

(Table of Contents)

If we are unable to attract and retain highly skilled sales and marketing and product development personnel, our ability to develop and market new products and product enhancements will be adversely affected.

We believe our ability to achieve increased revenues and to develop successful new products and product enhancements will depend in part upon our ability to attract and retain highly skilled sales and marketing and product development personnel. Our products involve a number of new and evolving technologies, and we frequently need to apply these technologies to the unique requirements of mobile products. Our personnel must be familiar with both the technologies we support and the unique requirements of the products to which our products connect. Competition for such personnel is intense, and we may not be able to attract and retain such key personnel. In addition, our ability to hire and retain such key personnel will depend upon our ability to raise capital or achieve increased revenue levels to fund the costs associated with such key personnel. Failure to attract and retain such key personnel will adversely affect our ability to develop and market new products and product enhancements.

We may not be able to collect revenues from customers who experience financial difficulties.

Our accounts receivable are derived primarily from distributors and OEMs. We perform ongoing credit evaluations of our customers' financial conditions but generally require no collateral from our customers. Reserves are maintained for potential credit losses, and such losses have historically been within such reserves. However, many of our customers may be thinly capitalized and may be prone to failure in adverse market conditions. Although our collection history has been good, from time to time a customer may not pay us because of financial difficulty, bankruptcy or liquidation.

We may be unable to manufacture our products, because we are dependent on a limited number of qualified suppliers for our components.

Several of our component parts, including our serial interface chip, our Ethernet chip, our bar code scanning modules, and our new line of mobile handheld computers, are produced by one or a limited number of suppliers. Shortages could occur in these essential components due to an interruption of supply or increased demand in the industry. If we are unable to procure certain component parts, we could be required to reduce our operations while we seek alternative sources for these components, which could have a material adverse effect on our financial results. To the extent that we acquire extra inventory stocks to protect against possible shortages, we would be exposed to additional risks associated with holding inventory, such as obsolescence, excess quantities, or loss.

(Table of Contents)

Our operating results could be harmed by economic, political, regulatory and other risks associated with export sales.

Export sales (sales to customers outside the United States) accounted for approximately 35 percent, 32 percent, and 35 percent, of our revenues in fiscal years 2007, 2006, and 2005, respectively. Accordingly, our operating results are subject to the risks inherent in export sales, including:

- longer payment cycles;
- unexpected changes in regulatory requirements, import and export restrictions and tariffs;
- difficulties in managing foreign operations;
- the burdens of complying with a variety of foreign laws;
- greater difficulty or delay in accounts receivable collection;
- potentially adverse tax consequences; and
- political and economic instability.

Our export sales are primarily denominated in United States dollars and in Euros for our sales to European distributors. Accordingly, an increase in the value of the United States dollar relative to foreign currencies could make our products more expensive and therefore potentially less competitive in foreign markets. Declines in the value of the Euro relative to the United States dollar may result in foreign currency losses relating to collection of Euro denominated receivables if left unhedged.

Our operations are vulnerable to interruption by fire, earthquake, power loss, telecommunications failure, and other events beyond our control.

Our corporate headquarters is located near an earthquake fault. The potential impact of a major earthquake on our facilities, infrastructure, and overall business is unknown. Additionally, we may experience electrical power blackouts or natural disasters that could interrupt our business. Should a disaster be widespread, such as a major earthquake, or result in the loss of key personnel, we may not be able to implement our disaster recovery plan in a timely manner. Any losses or damages incurred by us as a result of these events could have a material adverse effect on our business.

Failure to maintain effective internal controls could have a material adverse effect on our business, operating results and stock price.

We have evaluated and will continue to evaluate our internal control procedures in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act, which requires an annual management assessment of the design and effectiveness of our internal controls over financial reporting. If we fail to maintain the adequacy of our internal controls, as such standards are modified, supplemented or amended from time to time, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal controls over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act. Moreover, effective internal controls, particularly those related to revenue recognition, are necessary for us to produce reliable financial reports and are important to helping prevent financial fraud. If we cannot provide reliable financial reports or prevent fraud, our business and operating results could be harmed, investors could lose confidence in our reported financial information, and the trading price of our stock could drop significantly.

The sale of a substantial number of shares of common stock could cause the market price of our common stock to decline.

Sales of a substantial number of shares of our common stock in the public market could adversely affect the market price for our common stock. The market price of our common stock could also decline if one or more of our significant stockholders decided for any reason to sell substantial amounts of our common stock in the public market.

As of February 29, 2008, we had 32,015,975 shares of common stock outstanding. Substantially all of these shares are freely tradable in the public market, either without restriction or subject, in some cases, only to S-3 prospectus delivery requirements and, in other cases, only to manner of sale, volume, and notice requirements of Rule 144 under the Securities Act.

(Table of Contents)

As of February 29, 2008, we had 10,947,309 shares subject to outstanding options under our stock option plans, and 1,149,737 shares were available for future issuance under the plans. We have registered the shares of common stock subject to outstanding options and reserved for issuance under our stock option plans. Accordingly, shares underlying vested options will be eligible for resale in the public market as soon as the options are exercised.

As of February 29, 2008, we had warrants outstanding to purchase a total of 918,810 shares of our common stock at exercise prices ranging from $0.722 to $2.73. All such warrants may be exercised at any time, and the shares issuable upon exercise may be resold, either without restrictions or subject, in some cases, only to S-3 prospectus delivery requirements, and, in some cases, only to manner of sale, volume, and notice requirements of Rule 144.

Volatility in the trading price of our common stock could negatively impact the price of our common stock.

During the period from January 1, 2006 through February 29, 2008, our common stock price fluctuated between a high of $1.75 and a low of $0.59. The trading price of our common stock could be subject to wide fluctuations in response to many factors, some of which are beyond our control, including general economic conditions and the outlook of securities analysts and investors on our industry. In addition, the stock markets in general, and the markets for high technology stocks in particular, have experienced high volatility that has often been unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the trading price of our common stock.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We lease a 37,100 square foot office facility in Newark, California under a lease expiring in June 2012. We have one option to extend the term of the lease for an additional five-year period with respect to the entire premises. This facility houses our headquarters and manufacturing operations. We believe that our current facilities are sufficient and adequate to meet our needs for the foreseeable future.

Item 3. Legal Proceedings

We are currently not a party to any material legal proceedings.

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

No matters were submitted for vote by security holders during the fourth quarter of 2007.

(Table of Contents)

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities

Common Stock

The Company's Common Stock is traded on the NASDAQ Global Market under the symbol "SCKT."

The quarterly high and low sales prices of our Common Stock, as reported on the NASDAQ Global Market through February 29, 2008, and for the last two fiscal years are as shown below:

	Common Stock			
Quarter Ended		**High**		**Low**
2006				
March 31, 2006	$	1.48	$	1.06
June 30, 2006	$	1.75	$	1.05
September 30, 2006	$	1.36	$	0.81
December 31, 2006	$	1.25	$	0.72
2007				
March 31, 2007	$	1.40	$	0.80
June 30, 2007	$	1.03	$	0.79
September 30, 2007	$	1.05	$	0.85
December 31, 2007	$	1.33	$	0.71
2008				
March 31, 2008 (through February 29, 2008)	$	0.89	$	0.59

On February 29, 2008, the closing sales price for our common stock as reported on the NASDAQ Global Market was $0.73. We had approximately 6,300 beneficial stockholders of record as of February 25, 2008. We have not paid dividends on our common stock, and we currrently intend to retain future earnings for use in our business and do not anticipate paying dividends in the foreseeable future.

The information required by this item regarding equity compensation plans is incorporated by reference to the information set forth in Item 12 of this Annual Report on Form 10-K.

(Table of Contents)

Performance Graph

The performance graph shown below shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liabilities under that section, and shall not be deemed to be incorporated by reference into any filing of Socket Communications, Inc. under the Securities Act of 1933, as amended, or the Exchange Act. The performance graph below shows a five-year comparison of cumulative total stockholder return, calculated on a dividend reinvestment basis and based on a $100 investment, from December 31, 2002 through December 31, 2007 comparing the return on the Company's common stock with the Russell 2000 Index and the NASDAQ Computer & Data Processing Index. No dividends have been declared or paid on the common stock during such period. Historical stock price performance is not necess