Virgin Mobile USA, Inc.
Form 10-K
March 09, 2009
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 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, 2008

OR

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

For the transition period from to

Commission File Number: 001-33735

VIRGIN MOBILE USA, INC.

(Exact name of Registrant as specified in its charter)

Delaware	**20-8826316**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
10 Independence Boulevard	
Warren, NJ	**07059**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant s telephone number including area code: (908) 607-4000

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

Title of Class	Name of Exchange on Which Listed
Class A common stock, par value $0.01 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the 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 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. x

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 x Non-Accelerated Filer ¨ Smaller Reporting Company ¨

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 30, 2008, the aggregate market value of the voting and non-voting common equity of the Company held by non-affiliates was $81.7 million.

The number of shares of each of the registrant s classes of common stock outstanding as of February 28, 2009 was as follows:

Class A common stock, par value $0.01 per share	65,009,079
Class B common stock (privately held)	2
Class C common stock (privately held)	115,062

Documents Incorporated by Reference

Applicable portions of the Proxy Statement for the Annual Meeting of Stockholders of the Company to be held on May 20, 2009 are incorporated by reference into Part III of this Form 10-K.

Table of Contents

Introductory Note

In this annual report on Form 10-K (the annual report), unless we state otherwise or the context otherwise requires, the terms (1) the Company , we , us and our refer to Virgin Mobile USA, Inc., a Delaware corporation, and its consolidated subsidiaries; (2) Operating Partnership refers to Virgin Mobile USA, L.P., a Delaware limited partnership through which we conduct our business; (3) Helio refers to Helio LLC, a Delaware limited liability company; (4) SK Telecom refers to SK Telecom Co., Ltd., a company organized under the laws of the Republic of Korea, and its affiliated entities; (5) Sprint Nextel refers to Sprint Nextel Corporation, a corporation organized under the laws of the state of Kansas, and its affiliated entities; (6) the Virgin Group refers to Virgin Group Holdings Limited, a British Virgin Islands company, and its affiliated entities; and (7) EarthLink refers to EarthLink, Inc., a Delaware corporation.

Certain of the titles and logos of our products referenced in this annual report are our intellectual property or used by us under license. Each trade name, trademark or servicemark of any other company appearing in this annual report is the property of its holder.

This annual report includes industry data and forecasts that we have prepared based, in part, upon industry data and forecasts obtained from industry publications and surveys and internal company surveys. Third-party industry publications and surveys and forecasts generally state that the information contained therein has been obtained from sources believed to be reliable. The statements regarding our market position in this annual report are based on information derived from market studies and research reports cited in this annual report.

Although some of the companies that compete in our markets are publicly held as of the date of this report, some are not. Accordingly, only limited public information is available with respect to our relative market strength or competitive position. Unless we state otherwise, our statements about our relative market strength and competitive position in this annual report are based on our management s belief, internal studies and our management s knowledge of industry trends.

In this annual report, unless we state otherwise, (1) references to Nielsen Mobile refer to Nielsen Mobile s Quarterly Prepaid Report for the quarter ended December 31, 2008, (2) references to IDC refer to International Data Corporation s QView for the quarter ended September 30, 2008, (3) references to Current Analysis refer to Current Analysis, Inc. s report published in 2007, (4) references to the Yankee Group refer to the Yankee Group s Market Adoption Monitor and Forecast published in 2007, and (5) references to Market Tools refer to MarketTools ZoomPanel, an online panel of highly representive consumers.

The following annual report should be read in conjunction with our financial statements and related footnotes included in Item 8 of this document. Unless the context indicates otherwise, whenever we refer in this annual report to a particular fiscal year, we mean the fiscal year ending December 31 in that particular calendar year.

Forward-Looking Statements

This annual report contains certain forward-looking statements and information relating to us that are based on the beliefs of our management as well as assumptions made by, and information currently available to, us. These statements include, but are not limited to, statements about our strategies, plans, objectives, expectations, intentions, expenditures, and assumptions and other statements contained in this annual report that are not historical facts. When used in this document, words such as anticipate, believe, estimate, expect, intend, plan and project and simil expressions, as they relate to us are intended to identify forward-looking statements. These statements reflect our current views with respect to future events, are not guarantees of future performance and involve risks and uncertainties that are difficult to predict. Further, certain forward-looking statements are based upon assumptions as to future events that may not prove to be accurate.

Table of Contents

Many factors could cause our actual results, performance or achievements to be materially different from any future results, performance or achievements that may be expressed or implied by such forward-looking statements. These factors include, among other things:

- changes to our business resulting from increased competition;
- our ability to develop, introduce and market innovative products, services and applications;
- our customer turnover rate, or churn ;
- bulk handset purchase and trading schemes;
- changes in general economic, business, political and regulatory conditions;
- availability and cost of the nationwide Sprint PCS network and Sprint Nextel s costs associated with operating the network;
- potential liability resulting from pending or future litigation, or from changes in the laws, regulations or policies;
- the degree of legal protection afforded to our products;
- changes in interest rates;
- changes in the prices of mobile phones that we purchase from manufacturers;
- changes in the composition or restructuring of us or our subsidiaries and the successful completion of acquisitions, divestitures and joint venture activities; and
- the various other factors discussed in the Risk Factors section of this report.

Many of these factors are macroeconomic in nature and are beyond our control. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, our actual results, performance or achievements may vary materially from those described in this annual report as anticipated, believed, estimated, expected, intended, planned or projected. We neither intend nor assume any obligation to update these forward-looking statements, which speak only as of their dates.

Table of Contents

TABLE OF CONTENTS

Table of Contents

PART I

Item 1. Business.

Overview

We are a leading national provider of wireless communications services, offering prepaid services and, following the acquisition of Helio LLC, postpaid services targeted at the youth market. Our customers are attracted to our products and services because of our flexible terms, easy to understand and value-oriented pricing structures, stylish handsets offered at affordable prices and relevant mobile data and entertainment content. Our prepaid product and service offerings have no annual contract or credit check and we attract a wide range of customers, approximately half of whom are ages 35 and under. Our voice and data plans allow our customers to talk, use text messaging, picture messaging, email and instant messaging on a per usage basis or according to the terms of our monthly hybrid plans. Following the acquisition of Helio on August 22, 2008, we began to offer postpaid voice and data plans, some with two-year contracts, for both individuals and families.

We were founded as Virgin Mobile USA, LLC, a joint venture between Sprint Nextel and the Virgin Group, and launched our service nationally in July 2002. In October 2007, we completed our initial public offering (the IPO) and a related reorganization. Following this reorganization, Virgin Mobile USA, LLC converted into a Delaware limited partnership, changed its name to Virgin Mobile USA, L.P. (the Operating Partnership) and became the indirect, majority-owned subsidiary of Virgin Mobile USA, Inc., a holding company which holds partnership units in the Operating Partnership directly and indirectly through Bluebottle USA Investments L.P. (Bluebottle Investments) and Bluebottle USA Holdings L.P. (Bluebottle Holdings). Virgin Mobile USA, Inc. also holds the outstanding limited liability company interests of VMU GP, LLC, the general partner of Bluebottle Investments. As an indirect owner of VMU GP1, LLC, the sole general partner of the Operating Partnership, Virgin Mobile USA, Inc. operates and controls all of the business and affairs of the Operating Partnership. Sprint Nextel, EarthLink and Virgin Mobile USA, Inc. and its subsidiaries are the only partners of the Operating Partnership. Virgin Mobile USA, Inc. consolidates the financial results of the Operating Partnership, and the ownership interest of Sprint Nextel, EarthLink and SK Telecom in the Operating Partnership in the year ended December 31, 2008 is treated as a minority interest in our consolidated financial statements.

In August 2008 we acquired Helio, a provider of postpaid wireless products and services with a customer base of approximately 170 thousand. The Helio acquisition allowed us to offer high-value postpaid services and to acquire a unique and differentiated set of data applications that we expect to offer across our customer base. As of December 31, 2008, we served approximately 5.4 million customers (including Helio customers), an increase of 5.8% compared to the approximately 5.0 million customers we served as of December 31, 2007.

We market our products and services under the Virgin Mobile and the Helio by Virgin Mobile brands. We have exclusive rights to use the Virgin Mobile brand, which enjoys strong brand awareness, for mobile voice and data services through 2027 in the United States, Puerto Rico and the U.S. Virgin Islands through a trademark license agreement with the Virgin Group. We control our customers experience and all customer touch points including brand image, web site, retail merchandising, service and product pricing, mobile content, marketing, distribution and customer care but as a mobile virtual network operator, or MVNO, we do not own or operate a physical network, which frees us from related capital expenditures. This allows us to focus our resources and compete effectively against the major national wireless providers in our target market. We primarily focus on wireless consumers who use 200 to 1,000 minutes per month. According to Market Tools, 70% of wireless consumers use fewer than 1,000 minutes per month. According to Nielsen Mobile, prepaid subscribers average 425 minutes of calling per month.

We provide our services using the nationwide Sprint PCS network. We purchase wireless network services at fixed rates pursuant to our agreement with Sprint Nextel, under which Sprint Nextel provides the Company with access to its wireless voice and data services operating on the nationwide Sprint PCS network (the PCS Services Agreement). As a result, we are able to manage our network costs while dedicating our resources to acquiring and servicing customers rather than to acquiring spectrum or building and maintaining a wireless network.

Table of Contents

We operate in the highly competitive and regulated wireless communications industry. The primary bases of competition in our industry are the prices, types and quality of products and services offered. As the wireless communications industry continues to grow and consolidate, we continually reassess our business strategies and their impact on our operations. Our strategies have included pricing our handsets competitively to grow and maintain our customer base. We expect these strategies to continue in the future. We continually monitor the impact of handset prices on the profile of our new customers, the behavior of our existing customers and our financial performance. We make adjustments to our pricing strategy accordingly, including lowering or raising handset prices as necessary. Many factors, including risk factors described in the Risk Factors section of this annual report, could adversely affect our results, performance and achievements.

The following diagram depicts our current organizational structure:

Business Model

As a mobile virtual network operator, or MVNO, we dedicate the majority of our resources to acquiring and servicing customers rather than acquiring spectrum or building and maintaining a capital intensive wireless network. As a result, in the year ended December 31, 2008, we expended approximately 1.4% of our revenues on

6

Table of Contents

capital expenditures (mostly to support information technology and customer support infrastructure). Moreover, the simple, grab-and-go packaging of our handsets enables efficient distribution in third-party stores, saving us the expense of owning and operating our own retail stores.

Business Strategy

The following are core components of our business strategy:

Focus on Fast-growing Segments of U.S. Wireless Market. We believe there is substantial demand in the United States for our straightforward, value-oriented prepaid and postpaid wireless communication services. The Yankee Group projected that the number of users of wireless service in the under 35 year-old segment in the United States would increase by 16 million from 2006 to 2008, representing approximately 42% of the total growth in U.S. wireless customers over the same period. According to the Yankee Group, as of December 31, 2008, there were approximately 49.5 million prepaid wireless customers in the United States, with the U.S. prepaid and hybrid market representing 18.1% of total wireless customers. That number is expected to grow to approximately 62.1 million by the end 2011, or approximately 20.9% of all wireless customers in the United States. We plan to continue to focus upon the under 35 year-old segment and grow our market share by continuing to tailor our products, services and advertising message to this market, leveraging our brand through new and existing distribution channels and utilizing select youth-oriented media channels that specifically resonate with our target market.

Continue Product and Service Innovation. We continually innovate and strive to adapt to our customers needs. In February 2008, for example, we launched a suite of new service plans designed to broadly appeal to higher-usage, higher-revenue customers. Our monthly hybrid plans, which range from $20 each month to $79.99 each month, include anytime and night and weekend minutes without long-term contracts or commitments effectively expanding the prepaid market to include some customers who previously might have selected a postpaid service. We intend to continue our efforts to address our market s evolving needs and to offer innovative and popular products and services ahead of our competitors.

Enhance Our Brand Strength. We aim to maintain and strengthen a vibrant brand image that resonates with our customers and distinguishes us from other wireless communications providers. Our goal is to attract and retain customers through our youth-oriented marketing message and service offerings that are straightforward, flexible and a good value. For example, our marketing events in 2008 included the Virgin Mobile Festival, a two-day event that drew approximately 60 thousand fans to see major performing artists, increasing brand awareness for the brand and our products and services. We will continue to leverage our brand through innovative services, targeted marketing, advertising, product packaging, point-of-sale materials and our website.

Leverage Our Scale and Infrastructure to Drive Profitable Growth. As of December 31, 2008, our customer base was approximately 5.4 million. We have built our infrastructure to support future growth in customers and usage while leveraging the advantages of our predominantly variable cost structure. As we continue to scale the business, we expect our growing customer base to translate into improved cost economies without the need for substantial capital investment.

Customer Acquisition

Our customer acquisition approach is based on the acquisition cost and expected value of each customer. Our promotional offers are typically consumer driven, linking the purchase of our airtime with the purchase of our handsets and other products and services.

We have identified a number of customer acquisition principles that we believe are critical to our success, including:

- Marketplace segmentation that allows us to connect effectively with the best prospects through targeted use of media and an array of marketing vehicles;

- Compelling, focused marketing messages aimed at our best prospects;

Table of Contents

- Simple value proposition and service that is easy to articulate, understand, evaluate, buy and use;
- Good value and fair pricing;
- Innovative and exciting design in our products, packaging and point-of-sale presentation;
- Easy and efficient account activation and maintenance through our website and other self-service tools and customer service;
- Friendly and efficient customer care resulting in high customer satisfaction; and
- Extensive distribution network of approximately 150 thousand third-party retail stores that offer account replenishment, or Top-Up cards, including more than 40 thousand retail locations that also sell our handsets. Our retail partners include national chains such as Amazon.com, Best Buy, CVS, K-Mart, Meijer, RadioShack, Rite Aid, Sears, 7-11, Sprint Nextel Stores, Target Stores, Walgreens and Wal-Mart.

The prepaid wireless communications business in the United States is seasonal and is often disproportionately dependent on fourth quarter results. Our business has experienced a similar pattern and we expect this pattern to continue in the future. We rely heavily and concentrate our marketing efforts on key promotional periods, including Valentine s Day, Dads and Grads, Back to School, school graduation and the November/December holiday season.

Products and Services

We offer a range of products and services that are designed to meet the lifestyles of our target market.

Voice Services. We offer high-quality wireless services using the nationwide Sprint PCS network. In addition to voice services, our services include additional calling features such as voicemail and caller identification at no extra cost, as well as directory assistance and international calling.

Data Services. Our target customers use mobile data services at rates higher than those of the average wireless customer. In 2008, non-voice services represented 19.2% of our revenue, compared to 16.4% of our revenue in 2007.

We develop content and have entered into relationships with third parties to procure and offer customized content, graphics, messaging, music and other services, including:

- Messaging (text or short message services, or SMS); multimedia services, such as picture messaging, instant messaging, or IM and email). We have partnered with Yahoo and AOL to provide our customers with mobile email and instant messaging.
- Music (ringtones, text tones, alerts, artist profiles and communities).
- Web browsing and search.
- Downloadable games, customized wallpaper, screensavers and pictures.

Handsets. We offer stylish handsets at affordable prices. We currently offer fifteen handset models under the Virgin Mobile USA and Helio brands. Our handsets are affordably priced, with prices currently ranging from $9.99 to $149.99. We currently purchase our handsets from

Kyocera Wireless Corp., LG Electronics MobileComm U.S.A., Inc., Samsung Electronics America, Inc. and Personal Communications Devices LLC. We periodically negotiate to purchase handsets from other manufacturers. Although we attempt to maintain multiple vendors to the extent practicable, our handset inventory is currently acquired from only a few sources. We believe that our relationships with our suppliers are strong.

Each of our prepaid handsets is distributed in a simple package that can be picked up by a customer with no sales assistance. Each handset package includes everything a customer needs to get started, including the handset, battery, charger, initial credit for usage, promotional items and information that welcomes new customers to our service. Activation typically takes less than ten minutes on our website or through our customer service group, Virgin Mobile At Your Service. Our handsets are intended only for use with our wireless services.

Virgin Mobile Sugar Mama. Our Sugar Mama program is a service enhancement and mobile media platform that allows our customers to earn up to 75 minutes in airtime per month by viewing advertisements from several business partners. In the past, our Sugar Mama business partners have included companies, brands and institutions such as American Legacy Foundation, Levi Strauss, Showtime Networks, the U.S. Navy, Sony Pictures, Sony Music Entertainment, Unilever and Microsoft s Xbox. Internet access is required to establish and manage a Sugar Mama account. Customers generally must view an advertisement, rate it and answer a survey to receive airtime awards. As of December 31, 2008, our Sugar Mama program had approximately 900 thousand registered customers.

Content Related Quality Control. We have implemented policies to ensure the safety of our content and to safeguard against objectionable material. Our customers are prohibited from using our services for any illegal purpose. They are further prohibited from publishing, copying or reproducing (1) objectionable content or content that is offensive to third parties; (2) content that may infringe upon the patent, trademark or other intellectual property of others; (3) content used for purposes of solicitation of other customers or any other commercial purpose; or (4) content that could be harmful to other customers, such as content containing electronic viruses or worms. We reserve the right to remove any content that we, in our sole discretion, deem to be objectionable and to suspend or terminate the services of those we find to be in violation of our policies.

Pricing and Payment

Our wireless services are intended to be straightforward and easy to use. While our customers have the option of choosing fixed-term postpaid contracts, we do not require them to do so. We offer our products and services on a flat per-minute basis and on a monthly basis for specified quantities of minutes purchased in advance without requiring our customers to enter into long-term contracts or commitments in connection with fixed-term contracts.

Minute-based plans. We currently offer two plans under which our customers can pay by the minute. The first offers airtime costing $0.20 per minute, with the ability for customers to purchase optional add-on packages of minutes, or Minute Packs, costing $20, $30 and $50 per month for 30-day bundles of 200, 400 and 1,000 anytime minutes, respectively. If a customer purchases another Minute Pack within 30 days of the customer s last purchased Minute Pack, the customer may roll forward up to 5,000 unused Minute Pack minutes for an additional 30 days. The second offers airtime costing $0.10 per minute for a $6.99 monthly fee. Neither of our prepaid plans feature separate night and weekend rates.

Monthly plans. We currently offer several plans under which our customers can purchase airtime in advance on a monthly basis. These plans range from $24.99 per month for 200 anytime minutes and 500 separate night and weekend minutes to $79.99 per month for Totally Unlimited Calling.

Postpaid plans. We offer postpaid plans to customers under the Helio by Virgin Mobile brand name under which customers pay on a monthly basis for fixed terms up to two years. We currently offer three A La Carte postpaid plans ranging from $40 for 500 daytime minutes to $80 for unlimited minutes. We also offer three postpaid All-In plans ranging from $65 for 500 daytime minutes, unlimited night and weekend minutes and unlimited domestic text, picture, video and instant messaging, in addition to other features, to $99 for unlimited minutes and unlimited domestic text, picture, video and instant messaging, in addition to other features. We collect certain personal information from postpaid customers which we use for billing purposes, and require such customers to

Table of Contents

have and maintain satisfactory credit to receive and continue to receive our services. We reserve the right to suspend or terminate services to a customer if we determine at any time that payment for services may not be made when due.

Messaging. We currently offer several plans under which our prepaid customers can pay for domestic messaging services either on a monthly basis or per-message basis. Customers may choose from one of the following basic monthly pricing plans for domestic email, text, picture and instant messaging: (1) $5.00 per month for 200 messages; (2) $10.00 per month for 1,000 messages; and (3) $20.00 per month for an unlimited number of email, text, picture and instant messages. Customers using monthly plans which require a registered payment method may choose from one of the following basic monthly pricing plans for domestic email, text, picture and instant messaging: (1) $5.00 per month for 1,000 messages; and (2) $10.00 per month for an unlimited number of domestic email, text, picture and instant messages. Customers may also choose to pay by the message, at a rate of $0.15 per domestic email, text and instant message and $0.25 per picture message.

International. We provide international voice service that allows our customers to make and receive calls to and from approximately 220 countries worldwide. Customers making international calls are charged an international per-minute rate for each country in addition to the standard airtime rate of the respective customer s applicable plan. In addition, we offer international text messaging services priced on a per message basis. International text messages are $0.20 to send and $0.10 to receive. Standard domestic rates apply to calls to Puerto Rico and the United States Virgin Islands.

Feature Pricing. Additional features fall into three general categories: (1) ringtones and other mobile music content; and (2) downloads, including games and graphics; and (3) mobile web browsing. All additional features are priced individually or offered on a daily or monthly subscription basis.

Top-Up Cards and Payment Methods. Our prepaid customers may use Top-Up cards available in increments of $10, $20, $30, $50, and $90 to add money to their accounts. Our Top-Up cards are currently offered at approximately 150 thousand third-party retail locations throughout our coverage area. Customers may use Top-Up cards to add cash to their account balances for our prepaid minute based plans, recurring charges for certain of our monthly plans, text and picture messaging and mobile content. For those plans that do not require a registered payment method, customers may also elect to register a credit card, debit card or PayPal account to credit their accounts automatically on a monthly basis or when their accounts reach a specified minimum amount.

Legacy Pricing Offers. In addition to the pricing plans for our products and services described above, approximately 0.9 million of our customers use wireless services under our previous pricing plans, including our prepaid and monthly hybrid plans that predated new offers launched in February 2008, and our other Minute2Minute and Day2Day plans. Customers using our Minute2Minute plan are charged $0.25 per minute for each of the first 10 minutes of each day, and $0.10 for every minute thereafter. Customers electing our Day2Day plan are charged $0.35 per day and pay $0.10 for each minute of use. These pricing plans are not available to new customers.

Sales and Distribution

We use direct and third-party distribution channels to market our products.

Direct Distribution Channels. Our direct distribution channels consist of our website and Virgin Mobile At Your Service, our toll-free customer care center. Customers may purchase airtime directly from us by using a credit card, debit card or PayPal account or Top-Up card purchased at a third-party retail store, either using their handsets or through our website or customer care center. Customers may also register a credit, debit card or PayPal account with us, which allows them to elect to automatically add minutes to their account (1) once every month on a specified date, (2) once every 90 days, or (3) when their balance falls below $5 (or, for customers on certain minute-based plans that are no longer available, when their balance (i) falls below $5 or (ii) 90 days from their last Top-Up, whichever comes first).

Table of Contents

These channels fulfill the needs of a wide range of customers and prospects by providing means of purchasing products and services, replenishment, or Top-Up, as well as account services. As a source of sales, these channels represented approximately 2.42% of our 2008 total new customer additions (through both retail and direct channels). Periodically, we use direct promotions to increase sales in these channels. We advertise these promotions primarily through our online website, through Internet advertisements on third-party websites and through search engine advertising, as well as email and SMS communications to customers to stimulate referrals.

Our website also serves as an effective resource for potential customers to consider our products and services and an efficient channel for potential customers to buy products and activate their accounts as well as for existing customers to manage and service their accounts (adding airtime, changing their service plans, upgrading handsets, browsing and buying mobile content). Our website has low incremental operating costs and no third-party retailer subsidies. As a result, our website assists in reducing our customer acquisition, retention and service costs and is our most cost efficient advertising venue.

Third-Party Retail Distribution Channels. Our distribution network includes over 40 thousand stores selling handsets and approximately 150 thousand third-party retail stores selling Top-Up cards in the United States, Puerto Rico and the U.S. Virgin Islands. We intend to continue to expand our distribution network of retail partners.

We rely on four third-party retail distribution channels for product placement within their stores to promote the sale of our handsets to grow our customer base. As of December 31, 2008, we had direct or indirect arrangements with approximately 15 national retailers and a number of regional retailers, including Amazon.com, Best Buy, CVS, K-Mart, Meijer, RadioShack, Rite Aid, Sears, 7-11, Sprint Nextel Stores, Target Stores, Walgreens and Wal-Mart. In the first half of 2008, we entered into three agreements to expand our retail presence, entering new agreements with American Wireless and Sears and expanding our relationship with Wal-Mart. Collectively, these arrangements expanded our retail footprint by approximately two thousand doors in 2008. In addition, we have distribution arrangements with the Internet retailer Amazon.com and with certain other retailers, including Best Buy, RadioShack, Target and Wal-Mart, to offer our products on their websites.

As of December 31, 2008, sales through our third-party retail distribution channels represented approximately 95% of our total sales revenue (consisting of aggregated revenues from sales of our handsets and revenue realized upon use of our Top-Up cards) with Wal-Mart accounting for more than 10% of our total sales revenue. As of December 31, 2008, we also distributed our products through five other distribution agents for independent dealers which collectively represented approximately 11% of the total retail locations offering our products. Under our distribution agreements with these agents, we distribute our handsets and Top-Up cards to approximately 4,700 independent, regional wireless telecommunications dealers and stores.

To manage our relationship with third-party retail distribution channels, we have a dedicated internal sales force of approximately 32 representatives, and we have retained firms to provide regional support services. Our sales force is supplemented by a cross-functional team for each retail account consisting of members of our retail channel implementation, information technology, supply chain, brand, finance and legal teams. We provide our sales representatives with in-depth product and sales training to allow them to explain our products and services simply and clearly. We also have programs to train indirect representatives and retailers sales representatives.

Marketing

Our marketing and promotion activities distinguish and differentiate our brand through a focused and efficient use of communication vehicles based on measured impact. We also develop initiatives that enhance our brand position and differentiate us in the marketplace, such as the RE*Generation, our charitable campaign, and by sponsoring special events like the annual Virgin Mobile Festival and our sponsorship of the 2009 Britney Spears Circus Tour entitled Virgin Mobile Presents The Circus Starring Britney Spears. Our marketing campaigns, which extend across a variety of traditional, nontraditional and in-store media, promote key

Table of Contents

components of our value proposition and create an engaging dialogue with our prospects and customers. These campaigns are designed to increase consumer awareness, brand affinity, consideration and sales of our products and services. Support points of our overall value proposition include:

- Monthly Plans without Annual Contracts that include Totally Unlimited Minutes and Unlimited 7PM Nights and Weekends;
- Prepaid Plans without Annual Contracts that offer simple flat-rate minutes or Minute Packs that allow customers to buy minutes and roll forward unused minutes;
- Individual and family contract plans featuring a range of 3G handset options, including the Ocean and Ocean 2 handsets, which allow users easy and fast access to social networks and features like Google Maps, Garmin Mobile, MySpace and YouTube;
- Unlimited Text and Messaging for as little as $10 per month;
- Comprehensive coverage on the nationwide Sprint PCS network;
- No activation fees on prepaid plans;
- The ability to adjust or change plans at any time;
- Online account management and industry-leading customer service (according to Market Strategies, Inc., approximately 90% of our pre-paid customers are happy with their service and would recommend it to a friend); and
- Free minutes earned by our pre-paid customers for watching advertisements on Sugar Mama or through Studio V, our mobile content marketplace where users can create and sell their own mobile content.

As a central component of our marketing approach, we create year-round promotional plans and campaigns with our retail partners (Wal-Mart, Target, RadioShack, Best Buy and others) and assist them in the development of in-newspaper circulars, point-of-sale displays, in-store signage and customized offers that drive channel sales. Key promotional periods include Valentine s Day, Dads and Grads, Back to School and the November/December holiday season.

Our scale allows us to create our own major marketing and branding events, including the Virgin Mobile Festival, an annual music event featuring major performing artists that drew approximately 60 thousand fans in 2008. Our involvement and our presenting sponsorship include sweepstakes rewards, global streaming rights, the ability to sell sponsorships to other brands, on-site brand marketing and product demonstrations at an overall destination for our customers across the country, a distinctive VIP environment to entertain our many retail and trade constituents, and brand placement on all on-site and promotional media related to the event. In 2008, the Virgin Mobile Festival was nominated as U.S. festival of the year by Pollstar, a trade publication covering the worldwide concert industry.

Social Initiatives. Our RE*Generation charitable initiative is primarily dedicated to building awareness about and helping homeless youth. Our focus on this issue is based on extensive research and dialogue with our current and prospective customers regarding the causes about which they care most. The RE*Generation includes donations and service support to outstanding not-for-profit companies (including Stand Up For Kids and Children s Health Fund), as well as a range of outreach efforts designed to give our customers, prospects, and employees the ability to get involved and help homeless young people through direct donations and the use of our products and services. For example, customers can donate funds from their account or clothing provided by American Eagle Outfitters directly via SMS text messaging. We donate a portion of our net profits from mobile data service downloads to help young people in need, either through direct contributions to our charitable partners, additional outreach efforts or by funding the cost of programs that support and raise awareness for young people in need. We believe that it is important to support causes that matter to our customers and that customers who get involved with this initiative are more engaged with our services and brand. According to PR Week and Barkley Public Relations 2007 Cause Survey, more than 70% of consumers have purchased a product because the company brand supports a cause they believe in.

Table of Contents

Marketing Team. Our marketing team includes the following groups: (1) Consumer Insight and Marketing, which is responsible for our target audience identification, go-to-market and demand-creation strategies, all aspects of our customer-facing marketing efforts, and execution of our advertising campaigns; (2) Brand Development and Partnerships, which identifies and develops partnership programs and implements our events and sponsorships, including the Virgin Mobile Festival, Virgin Mobile Presents The Circus Starring Britney Spears, mobile ad sales (including Sugar Mama) and The RE*Generation; (3) Corporate Communications and Public Relations, which is responsible for developing public relations strategies and execution, press-generating events, and cultivation of relationships with traditional and social media; (4) Digital Marketing, Media Planning and Advocacy, which determines our most effective and efficient media mix and is responsible for our channel and media investments, website management, interactive marketing and online sales, and referral marketing; and (5) Brand and Operations, which is responsible for stewardship of the brand and includes an in-house creative services group.

Customer Care

Our customer care organization, known as Virgin Mobile At Your Service, is at the core of the Virgin Mobile brand. Our interactive voice response system, or IVR, operates in English, Spanish and Korean and handles about 180 thousand customer communications each day. The IVR is used by customers to perform many basic service transactions and get answers to frequently asked questions. After a customer s initial selection they can always reach a live advisor if they choose. Our live advisors handle on average 70 thousand telephone calls each day from customers through fully-outsourced call centers in Utah, South Korea, Jamaica, Nicaragua and the Philippines, as well as home-based agents located across the United States. We respond to approximately 1,200 emails each day from customers through our fully outsourced offshore care centers in India and the Philippines. During the seasonal new customer peak activation periods we activated numerous fully-outsourced call centers throughout the world to accommodate the additional volume. Virgin Mobile At Your Service operates 15 hours a day on weekdays and 14 hours a day on weekends, 365 days a year.

We believe we are able to operate our customer care more efficiently than traditional wireless providers because our straightforward and easy to use product and services are designed for low customer maintenance. Approximately 88% of Top-Up transactions in 2008 were completed without the assistance of a customer care representative. As a result, we believe we require significantly fewer customer service representatives per customer than our competitors.

We outsource our call centers under agreements with ICT Group, Inc., Sitel Operating Corp., West Telemarketing Corp., Results Global Services, Teleperformance, and email-based support under an agreement with Patni Computer Systems Inc.

The success of our efforts in customer service is supported by the recognition we have received from third parties and our customers:

- Pre-paid customer satisfaction ratings consistently exceed 90%, according to Market Strategies, Inc.

- Approximately 90% of our customers would recommend Virgin Mobile to a friend (75% have done so), according to Market Strategies, Inc.

- J.D. Power and Associates 2007 Award for Highest Wireless Prepaid Customer Satisfaction; recognized for exceeding industry standards in every surveyed customer service category (Aug. 23, 2007).

- Forrester Research s top ranking among National wireless carriers (November 2007 survey of nearly five thousand consumers) with the only excellent rating for ease of use. Virgin Mobile also was ranked highest by consumers for its usefulness and enjoyable customer experience.

- J.D. Power and Associates 2006 Award for Highest Wireless Prepaid Customer Satisfaction (Aug. 24, 2006).

Table of Contents

PC Magazine 2008, 2007 and 2006 Reader Choice for Satisfaction with Prepaid Service Providers.

J.D. Power Call Center Customer Satisfaction Excellence Award; recognized for providing an outstanding experience in our call centers nationwide (as compared to all communications providers) 2004.

Customer Base Management and Retention

We actively use customer lifecycle management initiatives to improve customer retention. Within 30 days of activation, all of our customers are scored for their propensity to churn using a statistical model measuring over fifty factors. Using this model, we are able to estimate the churn of our current customers and identify customers with the highest churn propensity. We can then focus lifecycle management spending on higher value, high-risk customers.

We have numerous systemic and outbound call systems in place to ensure that customers are constantly reminded of their balances, to Top-Up or of special offers for high-value customers. We also continuously deploy new lifecycle initiatives. We leverage all available channels to communicate and reinforce the value proposition of our highly competitive voice and data services offerings and deploy churn intervention programs at key lifecycle points utilizing direct marketing techniques. Our key churn reduction initiatives build upon proven successful programs and include: customer education, use of airtime incentives, discounts for replacement of lost, stolen and broken handsets, the recognition of high-value customers and win-back efforts focused on lapsed customers.

Our offerings and brand, combined with our high quality customer care and lifecycle management initiatives, allow us to maintain churn at levels below traditional prepaid levels. Our average monthly rate of customer turnover, or churn for the year ended December 31, 2008 was approximately 5.2%, compared to 4.9% in the year ended December 31, 2007.

Network

Through the nationwide Sprint PCS network, we offer digital wireless services in all 50 states, Puerto Rico and the U.S. Virgin Islands. The nationwide Sprint PCS network offers digital wireless services using wireless code division multiple access, or CDMA, technology. Sprint Nextel s third-party PCS affiliates provide additional PCS service provider network coverage in certain regional U.S. markets on CDMA wireless networks built and operated by such third-party PCS affiliates, in most instances using spectrum licensed to, and controlled by Sprint Nextel and its third-party PCS affiliates.

Information Technology

On July 3, 2008, we signed an outsourcing agreement with IBM, to which we refer in this annual report as the IBM Agreement. We believe that by outsourcing the development and maintenance of our information technology to IBM, we will enhance our technological capabilities and be able to improve our product portfolio for new and existing customers. Our agreement with IBM requires IBM to provide information technology services to us through May 15, 2013. We have the right, but not the obligation, to extend the agreement with IBM for one additional year, to May 15, 2014, if certain conditions are met. In certain circumstances, we may increase or decrease the level of baseline services provided by IBM, along with related payments.

As part of the IBM Agreement, we transitioned our information technology, infrastructure and applications development to IBM s service environment, and 46 of our employees transferred to IBM. We expect to complete the transition of our information technology, infrastructure and applications development to the IBM service environment in the first half of 2009. Prior to July 2008, we developed, procured, licensed, owned or maintained the IT systems required to operate our business.

Table of Contents

Either party can terminate the IBM Agreement early under certain circumstances, but if we terminate the IBM Agreement solely for our convenience, we would be required to pay certain termination fees and wind-down charges. The minimum termination fee that we would be obligated to pay at the beginning of 2009 is approximately $13.0 million, which decreases over the life of the IBM Agreement. Wind-down charges are defined as non-cancelable lease payments, lease termination fees, certain salaries, benefits, relocation costs, severance costs relating to IBM employees that were formerly our employees, and certain other costs. Wind-down costs cannot be reasonably estimated at this time but could be material to our financial position if we elect to terminate the IBM Agreement.

Our critical IT systems fall into the following categories:

Voice Processing and Rating Platform. Our prepaid service enables both our customers and us to manage in real-time customers accounts by automating the processes of activating new customer accounts, tracking customers service usage, maintaining credit balances and managing communication sessions.

Data Rating and Processing Platform. Our data rating and processing platform enables us to debit money from customers accounts continuously as services are being purchased and to direct customers to our customer service portal when a low balance threshold is triggered.

Middleware. Our customer information management solution automates the end-to-end provisioning, billing and customer care processes.

Customer Relationship Management System. As the interface for customer care and customer account management, our customer relationship management system (CRM) enables us to (1) manage our customer account features and lifecycle, (2) store customer and account data, (3) monitor the status of customer accounts, (4) generate messages alerting customers of their account status, and (5) add starter airtime to newly activated customer accounts.

Value-Added Service Platforms. We deliver our services through the following value-added service platforms: (1) text messaging, (2) website, (3) WAP portal, (4) content delivery systems, and (5) Interactive Voice Response, or IVR, system. These platforms combine our proprietary technology with technologies provided by IBM and other third-party suppliers.

Retail Channels. We manage our retail relationships and channels through the following integrated systems:

- *Point of Sale*. Integration between retailer point-of-sale and our systems provides us with the real time ability to unlock handsets and Top-Up cards, minimizing risk of theft and fraud.

- *Distribution.* Integration between our systems and distribution center systems allows real time inventory tracking, ordering, reporting and reconciliation to retailers.

- *Banking*. Integration between our systems and credit card processing systems enables replenishment, or Top-Up, and other purchase via credit or debit accounts and provides fraud controls and reporting.

Security and Controls. Together with IBM, we have implemented a comprehensive information security program utilizing technical, physical and administrative safeguards to protect against reasonably anticipated risks and to ensure compliance with any applicable statutory and regulatory obligations addressing information security protection. We utilize both internal and certified third-party resources to review and monitor adherence to industry and internally established security standards.

Supply and Logistics

Purchasing. We rely on outside vendors to produce handsets, accessories, user guides, Top-Up cards, point-of-sale material and product packaging. We provide all content and artwork for packaging and marketing materials. Our purchasing decisions rely on demand forecasts, which we base on communications with retailers, current and target inventory levels and anticipated marketing initiatives.

Table of Contents

Logistics and warehousing. We rely on Brightpoint, Inc. (Brightpoint), a third-party logistics provider, for warehousing and logistical inventory support. Handset and other inventory providers ship items to Brightpoint, which receives them as a bailee and performs quality assurance activities according to our guidelines. Brightpoint maintains a modern warehouse facility in Plainfield, Indiana and facilitates the distribution of our merchandise and materials to retailers based on our direction.

Distribution. Generally, we negotiate and place orders for all handsets, kit accessories, kitting material, Top-Up cards, and point of sale material. Accessories offered via the web and some other miscellaneous items are ordered directly by Brightpoint. Retailers submit their own electronic orders, which we release based on product availability, retail credit status and necessary lead times. Brightpoint packages all items according to our and our retailers requirements and arranges and monitors all shipments. Once Brightpoint ships orders, we invoice retailers either directly or through an electronic data interface maintained by Brightpoint. We handle all collection functions internally.

Reverse Logistics. Brightpoint assists us in processing product returns and customer repair requests. Brightpoint receives all returned products and assesses them according to criteria we provide for product condition and account credits. In some instances, Brightpoint may reprogram handsets or ship them to the handset vendor or to repair facilities.

Competition

The wireless communications industry is extremely competitive and, from a customer entry perspective, increasingly saturated. Wireless communications providers are increasingly competing to provide both voice and non-voice services to this saturated market. We believe that our primary competition in the U.S. wireless communications market comes from national and regional wireless communications providers, including AT&T, Verizon Wireless, T-Mobile, Sprint Nextel, Metro PCS and Cricket. We also face competition from resellers or MVNOs such as TracFone Wireless. The intensity of the competition in the wireless communications industry may affect our performance and results. Non-voice services, including data transmission, text messaging, e-mail and Internet access, are also now available from personal communications service providers and enhanced specialized mobile radio carriers. In many cases, non-voice services are offered in conjunction with or as adjuncts to voice services.

In the future, we may also face competition from entities providing similar services using different technologies, including Wi-Fi, Worldwide Interoperability for Microwave Access, or WiMax, and Voice over Internet Protocol, or VoIP. In addition, other potential competitors have announced plans (or suggested that they intend) to enter the mobile services marketplace. As wireless service becomes a viable alternative to traditional landline phone service, we increasingly compete directly with traditional landline telephone companies for customers and they have begun to advertise aggressively in the face of increasing competition from wireless communications providers, cable operators and other competitors. Cable operators are providing telecommunications services to the home, and some of these carriers are providing local and long distance voice services using VoIP. In particular circumstances, these carriers may be able to avoid payment of access charges to local exchange carriers for the use of their networks on long distance calls. Cost savings for these carriers could result in lower prices to customers and increased competition for wireless services. Some of our competitors offer these other services together with their wireless communications service, which may make their services more attractive to customers. In the future, we may also face competition from mobile satellite service, or MSS , providers, as well as from resellers of these services. The Federal Communications Commission (FCC) has granted to some MSS providers, and may grant others, the flexibility to deploy an ancillary terrestrial component to their satellite services. This added flexibility may enhance MSS providers ability to offer more competitive mobile services. We may also face competition from wireless companies offering femtocells, which are relatively small wireless communications stations potentially suitable for installation in private residences and small businesses to route calls made on a mobile phone over the Internet.

There has also been an increasing trend toward consolidation of wireless communications providers through joint ventures, reorganizations and acquisitions, such as our own acquisition of Helio. These consolidated carriers may have substantially larger service areas, more capacity and greater financial resources and bargaining power than we do. As consolidation creates even larger competitors, the advantages held by our competitors may increase.

The wireless communications industry is experiencing significant technological changes, as evidenced by the increasing pace of improvements in the capacity and quality of digital technology, shorter cycles for new products and enhancements and changes in consumer preferences and expectations. Accordingly, we expect competition in the wireless communications industry to be dynamic and intense as a result of the actions of competitors and the development of new technologies, products and services. We compete for customers based on numerous factors, including wireless system coverage and quality, service value proposition (minutes and features relative to price), local market presence, digital voice and features, customer service, distribution strength and brand name recognition. Some competitors also market other services, such as landline local exchange, Internet access services and femtocells, with their wireless service offerings. Competition has caused, and we anticipate will continue to cause, the decline of market prices for two-way wireless products and services. Wireless carriers have begun to offer calling plans with unlimited voice and data services for a flat monthly rate. The introduction of these plans will further pressure prices for mobile wireless services. Our ability to compete successfully will depend, in part, on our ability to distinguish our service from competitors through marketing and through our ability to anticipate and respond to other competitive factors affecting the industry, including new services that may be introduced, changes in consumer preferences, demographic trends, economic conditions, and competitors discount pricing and bundling strategies, all of which could adversely affect our operating margins, market penetration and customer retention. Many of the wireless communications providers in our markets have substantially greater financial resources than we do, and they may be able to offer prospective customers discounts or equipment subsidies that are substantially greater than those we are able to offer. While we believe that our various plans and our cost structure provide us with the means to react effectively to price competition, we cannot predict the effect that the market forces or the conduct of other operators in the industry will have on our business.

The following table summarizes our major competitors:

Category	**Service Provider**
Pure Prepaid	Boost Mobile (a product of Sprint Nextel), T-Mobile To Go, AT&T Go Phone, Verizon INpulse
Family plans of major providers	Verizon, AT&T, T-Mobile, Sprint Nextel
Hybrid offerings from major providers	AT&T GoPhone (Pick Your Plan), Verizon Easy Pay
Unlimited hybrid offerings	Cricket, Metro PCS
MVNOs	TracFone Wireless

The FCC is pursuing policies designed to increase the number of wireless licenses available. For example, the FCC has adopted rules that allow PCS and other wireless licenses to be partitioned, disaggregated and leased. The FCC also continues to allocate and auction additional spectrum that can be used for wireless services. It is possible that new companies, such as cable television, direct broadcast satellite operators, or Internet search engine providers will purchase or lease licenses and begin offering wireless services. In addition, because the FCC has recently permitted the offering of broadband services over power lines, it is possible that utility companies will begin competing against us.

While the U.S wireless communications market is very competitive, we believe that there are significant obstacles that keep most of the larger providers from directly competing with our service offering. In general, these carriers umbrella brands have failed to resonate with the youth market, and their strategies are focused on broad markets that include corporate and older customers and postpaid offerings. These providers may risk cannibalizing their existing customer base if they sought to compete more directly with us. In addition, the complexity of existing wireless offerings typically requires significant sales assistance that we believe is neither appealing to the youth market nor cost effective. We believe that there are also significant barriers to entry for companies attempting to enter the market with business models similar to ours due to the significant upfront investment to fund operating losses for several years prior to profitability.

We believe that we are strategically positioned to compete with other communications technologies that now exist. Continuing technological advances in telecommunications and FCC policies that encourage the development of new spectrum-based technologies make it difficult, however, to predict the extent of future competition.

Regulation

The FCC has statutory jurisdiction and regulatory authority over the licensing, operation, and offering of wireless services. As an MVNO, many of the FCC s regulations do not apply to us because we do not hold wireless radio licenses or operate network facilities. Our operations, however, are subject to certain FCC regulations since we are considered: (1) a telecommunications carrier, (2) a commercial mobile radio services (CMRS) provider, and (3) a common carrier under the FCC s regulations and the Communications Act of 1934, as amended. As noted below, we are also regulated, to varying degrees, by state and local governments. In addition to others, we are currently subject to the following regulatory programs:

Universal Service Fund (USF). The FCC and many state public utility commissions (PUCs) have established USF programs to ensure that affordable telecommunications services are widely available. Funds from these programs are used to reimburse communications carriers that provide subsidized communications to lower-income customers or individuals living in rural areas. All telecommunications carriers must contribute to these funds. The FCC has undertaken a rulemaking proceeding for the comprehensive reform of the manner in which it assesses carrier USF contributions, the methods by which carriers may recover their costs from customers and the system through which USF funds will be distributed among and between states, carriers and services. As part of this proceeding, the FCC has proposed to transition to a connections-based or numbers-based approach for USF contributions. Under such a system, we would be required to contribute a per-connection or per-number flat fee for each connect