

GRADIENT'S 2003-2005 Research Reports Identified the Issues Central to SEC's Accounting Fraud Charges Against UTStarcom Executives

May 5, 2008 (Scottsdale, Arizona) – (Business Wire) Five years after Gradient Analytics first reported on UTStarcom (UTSI), the U.S. Securities and Exchange Commission has announced accounting fraud charges and a settlement fine against two UTSI executives for “false financial filings.”

Gradient Analytics initiated coverage of UTSI on Sept. 25, 2003, after finding that “insider selling activity ha[d] ballooned” at a time when the company was reporting “extremely high accruals... and anemic cash flows.” Gradient’s report also noted that, “despite a 77.4% increase in earnings, UTSI’s operating cash flow declined over 300% in the six months ended 06/30/03.”

According to the SEC’s press release, “UTStarcom publicly reported over \$400 million in sales between 2000 and 2005 that were subject to undisclosed side agreements or contract modifications rendering revenue recognition improper under applicable accounting principles.” The SEC also alleged that UTSI “failed to disclose and properly account for transactions between the company and an entity controlled by an executive of UTStarcom’s China subsidiary.”

As Gradient’s forensic accountants began to look more closely at the company’s financial reports, a number of significant concerns emerged. A January 23, 2004, Watch List entry cited concerns about “a highly material level of related-party transactions” and other balance-sheet concerns, such as potentially excessive inventory levels.

In March 2004, we reiterated our “F” rating for earnings quality based on concerns that “UTSI’s 10K [had been] delayed, disclosures over an additional related party, and internal-control weaknesses.” According to the SEC’s complaint, the company “failed to properly account for and disclose related-party transactions” and that “[d]espite being put on notice of potential accounting issues by, among other things, material weakness letters sent by the company’s outside auditors ... defendants falsely certified that UTSI’s quarterly and annual reports did not contain any material errors or omissions.”

UTSI was soon placed on Gradient’s first-ever edition of the Greatest Concerns List (July 30, 2004), where it remained for the next nine months. During this period, the company acknowledged that it had identified a variety of accounting irregularities involving revenue timing, related-party dealings, inventories, and a host of other account balances.

On April 1, 2005, Gradient warned clients that UTSI’s announcement of inventory losses related to related party MDC was likely “just the tip of the iceberg.” Indeed it was just the tip of the iceberg, as there would be many more restatements and disclosures of



ineffective internal controls to come. According to the SEC's complaint, "UTSI prematurely recognized over \$350 million from 78 sales transactions in China" between 2000 and 2005. The Commission also alleges that "[b]etween 2003 and 2005, (UTSI) prematurely recognized nearly \$50 million in net revenue from international sales...which were subject to side agreements."

According to UTSI's press release, the firm also is under investigation by the Department of Justice for "possible violations of the Foreign Corrupt Practices Act."

About Gradient Analytics

Gradient is one of the country's leading independent research firms providing objective, academically-rigorous research and quantitative stock ratings for institutional clients.

Media inquiries should be directed to:

Karen Hinton
Hinton Communications
703-798-3109
Karen@hintoncommunications.com