

case 11

Handspring, Inc., 2002

Lisa-Marie Mulkern and Alan N. Hoffman

My focus today, 100 percent, is making Handspring successful, making handheld computing successful. I still view the handheld computing industry as very embryonic; it's very early on. It's like 1982 of the PC world. And the big things haven't happened yet. As much success as Palm has had, and as much success as Handspring is currently having, it's just the beginning, and it takes a lot of concentrated effort to build a big business. And we think Handspring's going to be a very big business.¹

Jeff Hawkins, Handspring's Chairman and Chief Product Officer

Jeffrey Hawkins: The Journey from GRiD Systems to Treo

Handspring was founded in 1998 by three key executives from Palm Computing, Jeff Hawkins, currently Handspring's Chairman and Chief Product Officer; Donna Dubinsky, President and CEO; and Ed Colligan, the Chief Operating Officer (CEO). At Palm Computing, Hawkins had been the chief inventor, Dubinsky the President and CEO, and Colligan the Vice President (VP) of Marketing. The three veterans of handheld computing were credited with reviving the industry through their successful launch of the Palm Pilot in 1996.

The widespread success and ongoing technological improvements found in today's handheld computing devices are a direct result of Hawkins's design work at GRiD Systems back in the early 1980s. After graduating from Cornell University in 1979 with a bachelor of science degree in electronic engineering and a short tenure at Intel, Hawkins left to begin working at GRiD Systems in 1982. While at GRiD Systems, he developed a high-level programming language called GRiDTask that would later fuel further technological advancements in handheld computing, particularly in the area of text entry. Hawkins's work on GRiDTask also increased his own personal interest in the area of brain research.

In response to his related interest, Hawkins left his position at GRiD in 1986 in order to pursue a Ph.D at Berkeley. As Hawkins explained, he was in search of answers to questions such as "What does it mean for a brain, or for a system like a brain, to understand its environ-

This case was prepared by Lisa-Marie Mulkern, MBA student, and Professor Alan N. Hoffman of Bentley College. This case was edited for SMBP-9th Edition. Reprinted by permission of Dr. Alan N. Hoffman. The authors would like to thank Scott Barry, Wendy Dalwin, Lindsey Fuller, Bob Mammarella, and Diane Shaffer for their research and contributions to this case.

ment? What is a reductionist approach to understanding language, vision, and hearing? and What are the concepts underlying that?"² Although his Ph.D. thesis proposal was rejected on the basis that no other professors at Berkeley were pursuing similar research, a pattern classifier program that Hawkins had written was patented and used as a hand-printed-character recognizer. With his thesis proposal rejected and experiencing difficulties with being a graduate student after having had a successful career, Hawkins decided that he would return to the computer industry in lieu of pursuing his academic interests. Hawkins returned to GRiD Systems as Vice President of Research and began working on the first handheld computing device, the GRiDPad, which was released in 1989. Hawkins's personal goal at the time he rejoined GRiD Systems was "to become famous enough to and wealthy enough to really promote and sponsor significant research in neurobiology and theoretical neurobiology."³

The GRiDPad measured 9×12×1.4 inches and ran on a 10MHz 80C86 processor with a DOS platform. The handheld used GRiD's own software solutions that were written in GRiDTask. With a color graphics adapter (640×400) display, the GRiDTask cost \$2,370, exclusive of software, and used 256KB or 512KB battery-backed RAM cards. Using the character-recognition engine that Hawkins had developed, users were able to enter text by using either a pen or a keyboard. The GRiDPad was marketed primarily to data collection users in areas such as transportation and warehousing as well as to police, nurses, and census takers.

In Hawkins's mind, the GRiDPad was only a first step toward his revolutionary vision for handheld computing. Hawkins believed that the success of handheld computers depended on developing a product that was both small and lightweight enough for people to carry around with them all the time. Hawkins developed the specifications for a handheld computing device that was aptly named "Zoomer"—short for consumer, the device's intended market. However, the executives at GRiD were opposed to plans for entering the consumer market. Unable to find support from within, Hawkins left GRiD in 1992 with a software license for the GRiDPad and founded Palm Computing.

Corporate Governance

Exhibit 1-A shows the 7 members of the Board of Directors of Handspring, Inc., 5 of whom are external directors. Exhibit 1-B shows the 10 members of Handspring's executive team.

The Palm Pilot Era

On the heels of the GRiDPad's success, several high-tech companies, including IBM, NCR, NEC, and Samsung, joined in the rush to develop the next smaller computing device. Apple had been in the development phase of a handheld computing device since 1987. In 1992, John Sculley, then CEO of Apple, coined the term "personal digital assistant" (PDA).⁴

Following an initial commercial failure with the launch of the Zoomer, Palm went back to the drawing board and re-emerged in 1996 with its second product, the Palm Pilot. U.S. Robotics funded the development of the Palm Pilot through its acquisition of Palm Computing in 1995 for \$44 million in stock. It was at this time that Palm transformed itself from a strictly software company to one that would develop an entire product—both hardware and software. Hawkins created what he calls "a virtual company" by partnering with several hardware design and contract-manufacturing companies to bring the product to market. The Palm Pilot was a success, and as a result, Jeff Hawkins, along with his colleagues Donna Dubinsky and Ed Colligan, were credited with reviving the handheld computing industry. The Palm Pilot was the most successful product launch in computing history, selling faster than VCRs, color TVs, cell phones, and personal computers.

Exhibit 1

Board of Directors and Executive Team: Handspring, Inc.

A. Board of Directors

Donna L. Dubinsky
President, CEO and Acting
Chief Financial Officer
Handspring, Inc.

Kim B. Clark
Dean
Harvard Business School

Bruce W. Dunlevie
Managing Member
Benchmark Capital

Mitchell E. Kertzman
CEO and Chairman
Liberate Technologies

Jeffrey C. Hawkins
Chairman and Chief Product Officer
Handspring, Inc.

L. John Doerr
General Partner
Kleiner, Perkins, Caufield & Byers

William E. Kennard
Managing Director
The Carlyle Group

B. Executive Team

Jeffrey Hawkins
Founder, Chairman and Chief Product Officer



Jeff Hawkins co-founded Handspring with Donna Dubinsky in July of 1998 after 5 years together at Palm Computing. In 1994, Hawkins invented the original PalmPilot products and founded Palm Computing. He was often credited as the designer who reinvented the handheld market.

An industry veteran with nearly 20 years of technical expertise, Hawkins currently holds nine patents for various handheld devices and features. His vision for handheld computing dates back to the 1980s, when as Vice President of Research at GRiD Systems Corporation he served as principal architect and designer for the GRiDPad and GRiD Convertible. Prior to that, he held key technical positions with Intel Corporation. Hawkins earned a B.S. in electrical engineering from Cornell University.

He was also the Founder and Executive Director of the non-profit Redwood Neuroscience Institute, a scientific research institute working on theories and mathematical models of brain function (www.rni.org).

Donna Dubinsky
Founder and CEO



Donna Dubinsky co-founded Handspring with Jeff Hawkins in July 1998 to create a new breed of handheld computers for consumers. As President and CEO of Palm Computing, Dubinsky helped make the PalmPilot the best-selling handheld computer and the most rapidly adopted new computing product ever produced. When Dubinsky first joined Hawkins at Palm Computing in 1992, shortly after the company was founded, she brought with her more than 10 years of marketing and logistics experience from Apple and Claris. Dubinsky and Hawkins introduced the original PalmPilot in February 1996, a move that revitalized the handheld computing industry.

In addition to her position as CEO of Handspring, Dubinsky currently serves as a Director of Intuit Corporation and is a Trustee of the Computer History Museum. She earned a B.A. from Yale University and an M.B.A. from the Harvard Graduate School of Business Administration.

Exhibit 1

Board of Directors and Executive Team: Handspring, Inc. (continued)

Ed Colligan
Founder, President and COO



Ed Colligan joined Handspring to lead the development and marketing efforts for a new generation of handheld computers. As the Vice President of Marketing for Palm Computing, Ed Colligan worked with Jeff Hawkins and Donna Dubinsky to lead the product marketing and marketing communications efforts for Palm, including the successful positioning, launch, and marketing of the popular Palm product family.

Prior to Palm, Colligan was Vice President of Strategic and Product Marketing at Radius Corporation. During his eight years there, Colligan helped make Radius the brand leader in Macintosh graphics, graphic imaging, and hardware development.

Colligan's multiple successes had earned him several marketing industry accolades. Marketing Computers Magazine named him the 1997 Marketer of the Year, and *Advertising Age* named him one of the Top 100 Marketers of 1997, an award that spanned all product categories. He earned an B.A. from the University of Oregon.

Bill Slakey
Chief Financial Officer



Before joining Handspring in September, 2002 Bill Slakey was Chief Financial Officer at W J Communications, a leading RF semiconductor company. Prior to that, he was CFO at SnapTrack, a QUALCOMM company that pioneered the industry's most advanced GPS-based wireless tracking system for pinpointing wireless phones, PDAs, pagers and other wireless devices.

Slakey had over 16 years of experience in financial management, including a senior controller position at 3COM's Palm Computing Division and various financial roles spanning 10 years at Apple Computer.

Slakey earned a B.A. from the University of California and an M.B.A. from the Harvard Graduate School of Business Administration.

John Hartnett
Vice President, Worldwide Operations



John Hartnett joined Handspring from MetaCreations, where he served most recently as Senior Vice President of Marketing, Support & Operations for the United States. At MetaCreations, he was responsible for developing the marketing, branding and advertising strategies including online marketing and web site redesign.

Prior to MetaCreations, Hartnett served as Director of International Operations at Claris, where he developed and managed the operations business plan and was part of the lead team in the merger of the Applesoft and Claris business. Hartnett also spent time at AT&T GIS, Digital Equipment, and Wang.

Hartnett earned a Marketing Degree through the Marketing Institute of Ireland and a post grad diploma in Finance through the ACCA.

Exhibit 1Board of Directors and Executive Team: Handspring, Inc. (*continued*)**Patricia Tomlinson**
Vice President, Human Resources

With over 20 years of experience in the human resources field, Patricia Tomlinson came to Handspring from Edify Corporation where she was responsible for the worldwide human resources department. She also designed and implemented all HR-related programs and led the worldwide integration of all HR-functions for the merger of Edify with Security First Technologies.

Prior to Edify Corporation, Tomlinson's previous work experience was at Xerox Corporation, Synopsys, Inc., and Apple Computer, Inc. She earned a B.A. in Sociology from Pomona College in Claremont, California and completed the Program for Management Development from Harvard Business School.

Celeste Baranski
Vice President, Engineering

Celeste Baranski joined Handspring with over 18 years of engineering, design, and management experience in the mobile computing industry. Most recently, Baranski worked at Hewlett Packard Company as Research and Development Manager of its Mobile Computing Division, where she led R&D, manufacturing introduction, and quality assurance for the company's laptop computer product line.

Before Hewlett Packard, Baranski worked as a consultant and Director of R&D for Norand Corporation, where she was in charge of product design and engineering management for various companies including Plantronics, Kaldor, IDEO and Divicom. Prior to that she co-founded and served as Vice President of Hardware Engineering for EO Incorporated, and was also among the first employees at GO Corporation where she designed the first GO pen-based computer.

Baranski has also held technical staff positions at GRiD Systems and Rolm Corporation. She earned both a B.S. and a M.S. in Electrical Engineering from Stanford University.

David Pine
Vice President and General Counsel

David joined Handspring in May 2000 as Vice President and General Counsel. Prior to Handspring, he served as Senior Vice President and General Counsel for Excite@Home, a broadband online service provider. Before that he was Vice President, General Counsel of Radius Inc., a manufacturer of Macintosh computer peripherals. He started his career in private practice with Fenwick & West, LLP, a Silicon Valley law firm representing startup and high-growth technology companies. He also has been involved in government and politics and has served as a State Representative in the New Hampshire Legislature.

He earned a B.A. degree in government from Dartmouth College, where he was awarded a Harry S. Truman Scholarship, and a J.D. degree from the University of Michigan Law School.

Exhibit 1Board of Directors and Executive Team: Handspring, Inc. (*continued*)**Joe Sipher**
Vice President, Worldwide Marketing

Joe Sipher joined Handspring in May 2000. Sipher was a long time veteran of the handheld industry, having joined Palm, Inc. in 1993. His most recent role there was serving as Palm's first and only "Palm Fellow."

Before his fellowship, Joe managed Palm's wireless business, including the definition, development, and introduction of the Palm VII wireless Internet handheld. Joe was responsible for the hardware and software development of the breakthrough Palm VII product, and spearheaded the creation of Palm's wireless Internet service, Palm.Net. Before the Palm VII, Joe managed the PalmPilot product line and was a product manager on the original Pilot project.

Prior to Palm, Inc., Joe's work experience included positions at Microsoft and Apple. He held five patents pertaining to handheld and wireless technology. He earned a B.A. and an M.B.A. with high distinction from the University of Michigan.

Gregory Woock
Vice President, Worldwide Sales

Gregory Woock joined Handspring in 1999 with over 10 years of experience in sales and marketing within the high-tech industry. Prior to Handspring, Woock served as VP of Sales, at Creative Labs, Inc. As one of the original members of the pre-IPO team, Mr Woock helped build Creative from a small start-up into a dominant brand. Mr Woock was responsible for Sales, Channel marketing, Sales training and Sales operations in the United States, Canada and Latin America.

Woock earned his B.A. from Columbia College in Chicago

Source: Company document www.handspring.com/company/execteam.html. This section was edited.

The Exodus at Palm

By 1998, Hawkins, Dubinsky, and Colligan were already setting the stage for their departure from Palm and the formation of their own handheld computing company. Collectively, the three executives did not believe that Palm was a strategic match for 3Com (previously U.S. Robotics) and requested that Palm be spun off as a separate company. Eric Benhamou, 3Com's CEO, insisted that Palm would never be spun off because it was simply too important to the business. In addition to wanting a Palm spinoff, the trio also felt pressured to deliver products too quickly. As an example, Hawkins pointed to the fact that he felt pressured to deliver a wireless handheld in the form of the Palm VII. As Hawkins describes, "We were still at U.S. Robotics at the time, and the CEO, Casey Coswell, kept saying, 'I want you to do a wireless Palm.'" Hawkins objected on the basis that he would not have a great solution to deliver, but he ultimately yielded to the pressure by doing the best that he could with the development and subsequent release of the Palm VII wireless handheld in 1999.⁵

In response to these frustrations and armed with a license for the Palm operating system as well as the confidence that they could develop improved handheld computing devices, the three executives left Palm in July 1998 to form Handspring. September 14, 1999, one day after

3Com announced its plans to spin off Palm, Handspring unveiled its first handheld computing device, the Visor.

The Handspring Visor

The Visor featured the Springboard expansion slot, consisting of a series of modules for adding the capabilities of a digital camera, a wireless Web device, a cellular phone, or an MP3 music player. Many Palm enthusiasts followed Hawkins and his colleagues over to Handspring. The new company was overwhelmed with orders, and it took nearly four months before the supply was satisfying consumer demand for the new product. By the summer of 2000, Handspring's market share for Palm-based PDAs had reached 40%. Handspring went public in June 2000, with an initial public offering (IPO) price of \$20 per share. By October 2000, Handspring's stock price skyrocketed to \$95 per share. These successes attracted the attention of Palm and, throughout most of 2001, Palm and Handspring engaged in a price war with their competing handheld computing devices. Meanwhile, Microsoft was pressing ahead with its own version of a handheld computer, the Pocket PC, which had been introduced in early 1998.

In response to the increasing competition and pricing pressure in the handheld computing market, Handspring refocused its strategy with the introduction of the Treo line of communicators in fall 2001. Handspring's executives had decided that the market for strictly PDAs had become too crowded. The resulting price wars had eroded Handspring's margins and prevented the start-up from achieving its much-anticipated profitability.

THE TREO COMMUNICATOR

Handspring had learned a lot of valuable lessons through the development of its Visor product line. In particular, the two-year development process of the VisorPhone module taught the company several valuable lessons about phone and radio technology. In turn, Handspring's designers were able to utilize this experience in the development of the Treo product line, which began in summer 2000 and was completed within 14 months.

Under the code name "Manhattan," the Treo product development team consisted of both hardware and software developers. Each of the communicator's component parts also had New York-inspired names, such as "Shea Stadium" for the Graffiti handwriting system, "Central Park" for the screen, and "Metro" for the circuit board. In stark contrast to their rival Palm Computing, which had recently split its hardware and software businesses into two separate companies, Handspring's hardware and software developers worked together to design a communicator that addressed how and where people actually used their wireless devices. In addition, rather than employ traditional focus groups, Handspring employed an ethnographer who observed how people used both their cell phones and PDAs in everyday situations such as while driving or riding the subway.⁶ Such observations indicated that people preferred to use a cell phone with one hand to avoid the distractions of juggling. With Treo's thumb-touch QWERTY keyboard and the capability to look up addresses and telephone numbers by typing initials, Handspring's executives were confident that the Treo would set the company back on course toward near-term profitability.

In December 2001, Dubinsky announced that the Visor line would be phased out of production and that the company planned to achieve profitability by its fiscal year end on June 30, 2002. Handspring would eventually focus exclusively on the Treo platform of communicators, which in contrast to the hardware-based Visor products allowed users to increase functionality through additional software as opposed to bulky hardware expansions (see Exhibit 2).

Exhibit 2

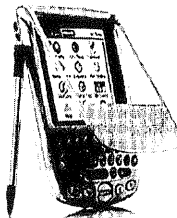
Handspring's Family of Organizers, Communicators, and Related Products

**Visor™ Expandable Handheld Computers**

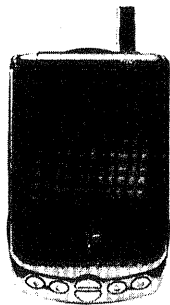
The Visor model line featured both B&W and color screens, used rechargeable or alkaline batteries, and ranged in list price from \$169 to \$229. This was Handspring's original product offering.

**Springboard™ modules transformed the Visor into a digital camera, wireless Web device, MP3 player, and more.**

Handspring offered more than 70 different modules. Some modules were included free with the purchase of a Visor handheld, whereas other modules had a list price in excess of \$400.

**Treo™ 90 Handheld Computer Organizer**

The Treo 90 featured a color screen, rechargeable battery, QWERTY keyboard, and SD/MMC expansion capabilities. It listed for \$299.

**Treo™ communicators were combination phone, messaging, data organizer, and Web access devices**

The original Treo 180 listed for \$399, and the improved Treo 270—offering global telephone coverage and released in 2002—listed for \$499. The Sprint PCS Treo 300—the result of a highly collaborative partnership and scheduled for release in late 2002—was to run on Sprint PCS's nationwide 3G data network. The Treo 300 was listed at \$449 after mail-in rebate.

Software and Accessories (Cases, Cables, Cradles, Keyboards, etc.) for Visor and Treo Products

A variety of accessories and additional software were available from Handspring and other third-party providers. Accessories for Handspring's family of products ranged in price from \$10.00 to \$50.00 and were model specific. The Treo e-mail annual subscription ranged in price from \$49.99 to \$99.99.

Handspring's Competitors

Because Handspring continued to serve the traditional PDA market while refocusing its strategy on becoming a leading provider of communicators, the company faced competition from a variety of providers. The competition between PDAs and smart phones continued to fuel the convergence of these two traditionally separate markets. Industry analysts expected PDA sales after 2004 to be strongly affected by smart phones.⁷ A Strand Consulting report stated that Palm and Handspring would have difficulty surviving in the smart phone market because they lacked experience in the mobile phone market and were faced with strong competition. Some analysts believed that Microsoft's 2.5G Smart Phone platform would succeed because of the company's strong customer base.⁸ Nokia, Sony, Ericsson, Siemens, and Motorola had more financial strength to compete in the market for smart phones and smart handheld devices.⁹ Traditional PDA providers such as Palm, Sharp, and Sony competed most directly with Handspring's Visor product line, while software and cell phone giants such as Microsoft and Nokia were concentrating their resources on combining the capabilities of wireless and handheld computing into their own versions of communicators that would compete for market share alongside Handspring's Treo products.

PALM i705

Palm was still the undisputed market share leader in the PDA market. However, the company had been under fire by competitors for several years and was clearly in the crosshairs of Microsoft and its Pocket PC operating system. Palm's current competitive advantage was its operating system, which was licensed to many PDA makers. The Palm i705 was the upgrade from the Palm VIIx. The i705 provided wireless e-mail and Internet access but lacked a long battery life and a color screen, and it had only 8MB of memory. Although the Palm i705 did not have cellular capability, it had "always-on" access to e-mail. This feature notified the user by a blink, beep, or vibration when there was new e-mail and had a very comprehensive support system that was second to none.

SHARP ZAURUS SL-500

Sharp was not a major player in the PDA market, but it was making some changes to its product in order to gain recognition and market share. The Zaurus SL-500 offered a hidden thumb keyboard as well as built-in handwriting-recognition software. Perhaps most noteworthy, the Sharp PDA was operating on a Linux operating system, which was getting some attention from software developers. The Zaurus also had a wide range of accessories, 64MB of RAM, and an Intel processor. Although Sharp had taken a big step forward, there were still some bugs that needed to be worked out to simplify software installation and Outlook access before it became a force in the current market.

SONY CLIE PEG-N760C

Sony had one of the best products in the PDA market. Its long-term commitment to R&D and innovation made it a market leader in almost every industry in which it competed. Although it was more expensive than other Palm OS devices, the CLIE offered a 65,334-color display screen along with MP3 audio capability, easy-to-use controls, remote control headphones, and picture/video viewing software. With some changes in its price and improvements in memory, Sony had the potential to utilize its deep pockets and strong product development capabilities to either enter into the cellular PDA market or work with a phone producer to enter into the market.

COMPAQ iPAQ 3835

The iPaq was one of the newest products in the PDA market. With a color screen, 64MB of RAM, the Pocket PC 2002 operating system, and improvements to iPaq's memory card and speakers, Compaq was positioned to increase its market share. Compaq's only setback at this time was the price of its PDA. At \$699, the iPaq was more expensive than its competitors' products. With the merger of HP and Compaq, the market for the iPaq had the potential to increase through the combined efforts of these two leaders in personal computing.

RIM/BLACKBERRY 957

With more solid financial backing, Blackberry should become a force in the market. The Blackberry 957 had PDA and phone capabilities, with a battery that lasted up to 80 hours. Blackberry was the first to develop the thumb keyboards and was widely preferred by its users. Compatible with applications such as Outlook and corporate networks, Blackberry had more than 13,000 companies using its product. Although the Blackberry 957 could not receive attachments via e-mail, the system was always ready to receive mail. Even with a price tag of \$499, Blackberry was struggling to improve its financial performance.

SAMSUNG SPH-M330

The Samsung PDA was positioned to compete directly with the Handspring Treo, Blackberry, and Kyocera models. The SPH-M330 had a color screen, support for an external camera, and cellular capability, and it ran on the Palm OS. The device also used gpsOne, a service that could display a map of the user's location and immediate vicinity on the LCD screen. Samsung was to launch the product through Sprint PCS but still lacked the brand recognition of Handspring and the other market-share leaders.

KYOCERA SMARTPHONE QCP 6035

Kyocera was Japan's version of the smart phone. The PDA portion of the device ran on the Palm OS and was compatible with most third-party applications. Kyocera was new to the U.S. market but would likely thrive in the Japanese market, which was usually protected by strict tariffs and import regulations.

NOKIA 9290 COMMUNICATOR

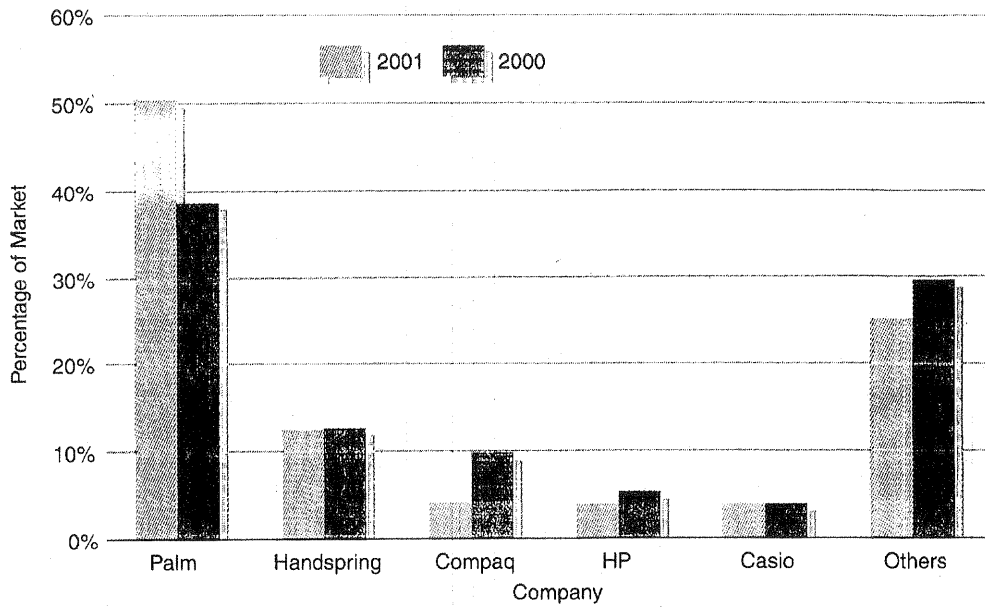
The Nokia 9290 Communicator was released into the U.S. market in 2002. It ran on the Symbian operating system and offered a full-color screen. The 9290 was capable of sending and receiving images, sound, and video clips. The handheld combined phone, fax, e-mail, calendar, and Internet capabilities as well as support for PC applications such as Microsoft Word, Excel, and PowerPoint. It was marketed as "the one device that does it all" and listed for \$599.

MICROSOFT POCKET PC PHONE EDITION

Microsoft was focused on the enterprise/corporate users who used products that were compatible with the operating systems and software controlled by Microsoft. It was more profitable to sell and support 5,000 Pocket PCs to one business than to 5,000 consumers. Microsoft's deep pockets and R&D capability posed the largest threat to reposition the PDA/phone market share. Although the product did not possess the capabilities of the Treo, Microsoft had just entered this market. The current device provided access to Outlook, e-mail

Exhibit 3

PDA Worldwide Market Share, 2001 and 2002

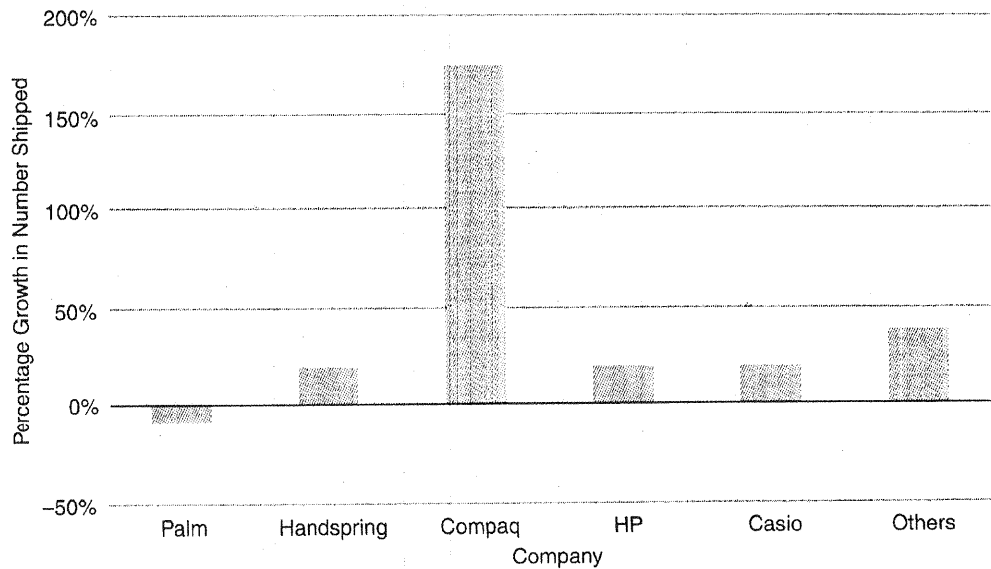


functions, and browsing. It was to be eventually tied into Microsoft's new Mobile Information Server software, which acted as a liaison between phones and exchange. The Microsoft Pocket PC 2002 Phone Edition combined a phone and an organizer into a device that contained versions of Microsoft Word and Excel with an Internet browser. The device listed for \$549.

Exhibit 3 shows the market shares for key companies in the PDA market. Exhibit 4 shows growth in the number of units shipped.

Exhibit 4

Percentage Growth in Number of Devices Shipped



Handspring's Strategy for the Treo Communicators

In the seemingly overcrowded market for traditional PDAs, Handspring was committed to setting itself apart from the competition with the introduction of the Treo line of communicators. In pursuit of this objective, Handspring was seeking to reach beyond the consumer market and become a force in the corporate wireless market. Corporate customers using the Treo would be able to access e-mail and more sophisticated corporate data through the Wireless Business Engine, or they could opt for the try-then-buy desktop software. Handspring was marketing this new product as "several digital products all in one tiny package".

Management viewed the Treo as: *Treo = Phone + Organizer + E-mail + Web*

The company had recently formed the Enterprise Alliance Partnership (EAP) Program to assist in its objective of bringing communications solutions and wireless handheld devices to corporations. Handspring planned to maximize its existing relationships with retailers, enterprise-focused resellers, corporate systems integrators, and wireless service providers to branch out toward a broader set of corporate clients. A primary example of the company's commitment to the EAP Program was its highly collaborative experience in developing the Sprint PCS Treo 300. The Treo 300, scheduled for release in fall 2002, was designed exclusively for Sprint's nationwide 3G data network. According to Handspring COO Colligan, "By working with the best integrators and back-end software providers in the industry, we can leverage each other's experience to give corporate customers exactly what they want."¹⁰

Handspring was also committed to increasing its marketing and distribution channels through similar partnership arrangements. On December 17, 2001, Handspring announced a strategic marketing and sales partnership with Neomar, a leading developer of wireless enterprise software solutions. The companies intended to work together on product evaluation, testing, and training. They would also combine sales and marketing efforts for Handspring's Visor and Treo product lines with Neomar's mobile infrastructure software for corporate customers.¹¹ Other strategic partnerships included Wireless Knowledge, Inc. (a subsidiary of QUALCOMM, Inc.), Visto Corporation, Aether Systems, AvantGo, Extended Systems, and Synchrologic.

HOW IMPORTANT IS THE MICROSOFT OS?

According to Neil Ward-Dutton of Ovum, most consumers of PDAs were business users who were reimbursed by their companies. The general consumer market was not yet developed. This gave Microsoft and companies using the Microsoft operating system an advantage over Handspring's use of the Palm operating system. Company IT departments preferred products that used the same operating system as the company computer systems.¹² The Microsoft Pocket PC ran versions of Word and Excel. Other people contended that compatibility with the desktop was more important than compatibility with back-end applications.¹³ In a 2001 interview with Business 2.0, Jeff Hawkins claimed that he did not believe the operating system was nearly as important to handhelds as it was to PCs. When asked if he had made a decision to use another operating system in lieu of continuing to license Palm's technology, Hawkins responded, "Long term, if Handspring grows as large as I think it will be . . . it is almost certain that we will have products that do not run on Palm. But that is not a product announcement."¹⁴

ENSURING PROFITABILITY PROJECTIONS ON THE BASIS OF TREO'S INITIAL SUCCESS

In the midst of Handspring's attempts to refocus its strategy on the communicator market, the young company was still struggling to achieve profitability. It had had a net loss every year since its inception.¹⁵ While its sales were increasing, net profit was decreasing. Worldwide, the market for PDAs was increasing. According to Gartner Dataquest, the number of PDAs shipped increased 18% from 2001 to 2002.¹⁶ Handspring's net profit, however, decreased as a result of downward pricing pressures from an increasing number of competitors. Gross margins fell from 31% to 9% during fiscal year 2001. Although Handspring received an additional \$57 million in funding in January 2002, Dubinsky knew that the shareholders were expecting profitability in the near future.

Dubinsky was reviewing her comments from the company's quarterly and fiscal year end conference call for June 30, 2002. During the conference call, Handspring announced that Hawkins had recently formed the nonprofit Redwood Neuroscience Institute to pursue his lifelong passion for brain research. He would be splitting his time between the institute and serving as Handspring's Chief Product Officer and Chairman of the Board of Directors. Now that Hawkins was no longer 100% focused on Handspring, Dubinsky wanted to assure shareholders that the company would continue to successfully execute on its plans for the Treo communicators in both the near and long terms.

When Handspring unveiled its plans to transition to a communicator-based company, Dubinsky also predicted profitability by mid-2002. However, consumers were still taking a wait-and-see approach and looking for a compelling technological breakthrough to convince them that an upgrade to a communicator was warranted. Consumer reluctance combined with an economic slowdown prevented the company from achieving its fiscal year end profitability as predicted.

Although profitability objectives were still unmet, Dubinsky reported that the Treo was being well received in the marketplace, with more than 93,000 units shipped to date. The Treo product line had significantly improved margins from 9.2% to 24.5% over the prior fiscal year end. Unlike the Visor product line, the Treo products were not experiencing any pricing pressure from competing products. Telecommunications service providers were reportedly very happy with the Treo line, and studies indicated that Treo users represented a 20% to 90% increase in average revenue per user over traditional cell phone users.

Handspring remained confident that its new line of Treo communicators would succeed in the marketplace and revised its outlook by stating that the company intended to achieve profitability by the second quarter, ending December 30, 2002. Dubinsky needed to decide how Handspring could best realize this goal and considered the following approaches to ensure that the company's profitability objectives were met:

1. Accelerate the company's plan to phase out of the Visor product line and concentrate all of Handspring's resources on the development and marketing of the Treo communicators through increased alliances with telecommunications service providers.
2. Dedicate resources to a costly marketing and advertising campaign to increase awareness of communicators rather than rely on the early adopters of the new Treo products to educate other consumers.
3. Focus resources on developing an operating system to compete with products offered by Palm, Microsoft, and Symbian.

Financial Performance

Exhibit 5 shows Handspring's consolidated statement of operations, and Exhibit 6 shows its consolidated balance sheet.

Exhibit 5

Consolidated Statements of Operations: Handspring, Inc.
(Dollar amounts in thousands, except per share amounts)

Year Ending	June 29, 2002	June 30, 2001	July 1, 2000
Revenue	\$240,651	\$ 370,943	\$101,937
Costs and operating expenses			
Cost of revenue	205,917	292,311	69,921
Research and development	24,739	23,603	10,281
Selling, general and administrative	85,612	145,132	42,424
In-process research and development	—	12,225	—
Amortization of deferred stock compensation and intangibles ¹	20,181	32,830	40,077
Total costs and operating expenses	<u>336,449</u>	<u>506,101</u>	<u>162,703</u>
Loss from operations	<u>(95,798)</u>	<u>(135,158)</u>	<u>(60,766)</u>
Interest and other income, net	5,259	12,195	675
Loss before taxes	<u>(90,539)</u>	<u>(122,963)</u>	<u>(60,091)</u>
Income tax provision	1,050	3,000	200
Net loss	<u>\$ (91,589)</u>	<u>\$ (125,963)</u>	<u>\$ (60,291)</u>
Basic and diluted net loss per share	<u>\$(0.71)</u>	<u>\$(1.21)</u>	<u>\$(1.77)</u>
Shares used in calculating basic and diluted net loss per share	<u>128,221</u>	<u>103,896</u>	<u>34,015</u>

Note: 1. Amortization of deferred stock compensation and intangibles:

Cost of revenue	\$ 2,586	\$ 4,521	\$ 5,904
Research and development	4,672	6,926	8,059
Selling, general and administrative	<u>12,923</u>	<u>21,383</u>	<u>26,114</u>
	\$ 20,181	\$ 32,830	\$ 40,077

Source: Handspring, Inc., SEC Form 10-K, June 29, 2002, p. 37.

Exhibit 6

Consolidated Balance Sheets: Handspring, Inc.

(Dollar amounts in thousands, except share and per share amounts)

Year Ending	June 29, 2002	June 30, 2001
Assets		
Current assets		
Cash and cash equivalents	\$ 85,554	\$ 87,580
Short-term investments	15,235	33,943
Accounts receivable, net of allowance for doubtful accounts of \$3,711 and \$2,239, as of June 29, 2002, and June 30, 2001, respectively	20,491	12,850
Prepaid expenses and other current assets	3,667	19,473
Inventories	<u>20,084</u>	<u>2,857</u>
Total current assets	145,031	156,703
Long-term investments	50,644	80,237
Property and equipment, net	19,092	15,041
Other assets	<u>1,408</u>	<u>1,254</u>
Total assets	<u>\$216,175</u>	<u>\$253,235</u>
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	\$ 44,490	\$ 37,881
Accrued liabilities	<u>48,779</u>	<u>70,152</u>
Total current liabilities	93,269	108,033
Commitments and contingencies		
Stockholders' equity		
Preferred stock, \$0.001 par value per share, 10,000,000 shares authorized; nil shares issued and outstanding at June 29, 2002, and June 30, 2001	—	—
Common stock, \$0.001 par value per share, 1,000,000,000 shares authorized; 143,126,516 and 129,949,768 shares issued and outstanding at June 29, 2002, and June 30, 2001, respectively	143	130
Additional paid-in capital	419,256	368,166
Deferred stock compensation	(9,468)	(29,445)
Accumulated other comprehensive income (loss)	(793)	994
Accumulated deficit	<u>(286,232)</u>	<u>(194,643)</u>
Total stockholders' equity	<u>122,906</u>	<u>145,202</u>
Total liabilities and stockholders' equity	<u>\$216,175</u>	<u>\$253,235</u>

Note: The notes were deleted.

Source: Handspring, Inc., SEC Form 10-K, June 29, 2002, p. 36.