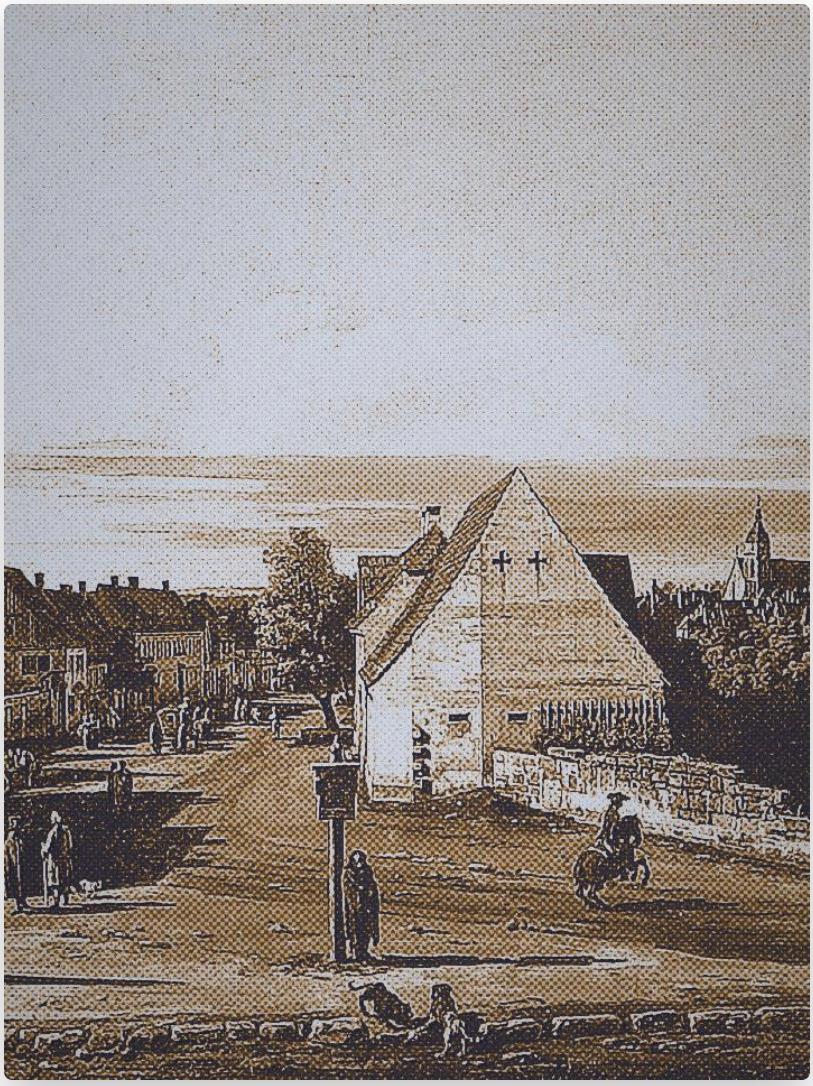
FORM S-1 · REGISTRATION STATEMENT

SonicWALL Inc

IPO priced 1999-11-10 · $14.00 a share · SNWL



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AS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ON FEBRUARY 23, 2000 REGISTRATION NO. 333- SECURITIES AND EXCHANGE COMMISSION WASHINGTON, DC 20549 FORM S-1 REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933 SONICWALL, INC. (EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER) CALIFORNIA 7372 77-0270079 (STATE OR OTHER (PRIMARY STANDARD INDUSTRIAL (I.R.S. EMPLOYER JURISDICTION CLASSIFICATION CODE NUMBER) IDENTIFICATION NO.) OF INCORPORATION) 1160 BORDEAUX DRIVE SUNNYVALE, CALIFORNIA 94089 (408) 745-9600 (ADDRESS, INCLUDING ZIP CODE, AND TELEPHONE NUMBER, INCLUDING AREA CODE, OF REGISTRANT'S PRINCIPAL EXECUTIVE OFFICES) SREEKANTH RAVI CHAIRMAN, PRESIDENT AND CHIEF EXECUTIVE OFFICER SONICWALL, INC. 1160 BORDEAUX DRIVE SUNNYVALE, CALIFORNIA 94089 (408) 745-9600 (NAME, ADDRESS, INCLUDING ZIP CODE, AND TELEPHONE NUMBER, INCLUDING AREA CODE, OF AGENT FOR SERVICE) COPIES TO:

Jerrold F. Petruzzelli William T. Quicksilver David M. Pike Manatt, Phelps & Phillips, LLP 3030 Hansen Way, Suite 100 Palo Alto, California 94304 Telephone: (650) 812-1300 Facsimile: (650) 213-0260	Gregory K. Miller Taitt Sato Andrew S. Williamson Latham & Watkins 505 Montgomery Street, Suite 1900 San Francisco, California 94111 Telephone: (415) 391-0600 Facsimile: (415) 395-8095

APPROXIMATE DATE OF COMMENCEMENT OF PROPOSED SALE TO THE PUBLIC: AS SOON AS PRACTICABLE AFTER THIS REGISTRATION STATEMENT BECOMES EFFECTIVE. IF ANY OF THE SECURITIES BEING REGISTERED ON THIS FORM ARE TO BE OFFERED ON A DELAYED OR CONTINUOUS BASIS PURSUANT TO RULE 415 UNDER THE SECURITIES ACT OF 1933, CHECK THE FOLLOWING BOX. [_] IF THIS FORM IS FILED TO REGISTER ADDITIONAL SECURITIES FOR AN OFFERING PURSUANT TO RULE 462(B) UNDER THE SECURITIES ACT OF 1933, CHECK THE FOLLOWING BOX AND LIST THE SECURITIES ACT REGISTRATION STATEMENT NUMBER OF THE EARLIER EFFECTIVE REGISTRATION STATEMENT FOR THE SAME OFFERING. [_] IF THIS FORM IS A POST-EFFECTIVE AMENDMENT FILED PURSUANT TO RULE 462(C) UNDER THE SECURITIES ACT OF 1933, CHECK THE FOLLOWING BOX AND LIST THE SECURITIES ACT REGISTRATION STATEMENT NUMBER OF THE EARLIER EFFECTIVE REGISTRATION STATEMENT FOR THE SAME OFFERING. [_] IF THIS FORM IS A POST-EFFECTIVE AMENDMENT FILED PURSUANT TO RULE 462(D) UNDER THE SECURITIES ACT OF 1933, CHECK THE FOLLOWING BOX AND LIST THE SECURITIES ACT REGISTRATION STATEMENT NUMBER OF THE EARLIER EFFECTIVE REGISTRATION STATEMENT FOR THE SAME OFFERING. [_] IF DELIVERY OF THIS PROSPECTUS IS EXPECTED TO BE MADE PURSUANT TO RULE 434, PLEASE CHECK THE FOLLOWING BOX. [_]

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount to be Registered(1)	Proposed Maximum Offering Price Per Share(2)	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
4,025,000 SHARES OF COMMON STOCK, NO PAR VALUE.....	4,025,000	$84.9375	$341,873,430	$90,255

(1) INCLUDES 525,000 SHARES WHICH THE UNDERWRITERS HAVE THE OPTION TO PURCHASE IN OVER-ALLOTMENT, IF ANY. (2) ESTIMATED SOLELY FOR THE PURPOSE OF COMPUTING THE AMOUNT OF THE REGISTRATION FEE PURSUANT TO RULE 457(O).

THE REGISTRANT HEREBY AMENDS THIS REGISTRATION STATEMENT ON SUCH DATES AS MAY BE NECESSARY TO DELAY ITS EFFECTIVE DATE UNTIL THE REGISTRANT FILES A FURTHER AMENDMENT WHICH SPECIFICALLY STATES THAT THIS REGISTRATION STATEMENT WILL THEREAFTER BECOME EFFECTIVE IN ACCORDANCE WITH SECTION 8(A) OF THE SECURITIES ACT OF 1933 OR UNTIL THIS REGISTRATION STATEMENT BECOMES EFFECTIVE ON SUCH DATE AS THE COMMISSION, ACTING PURSUANT TO SECTION 8(A), MAY DETERMINE.

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+The information in this prospectus is not complete and may be changed. We may +
+not sell these securities until the registration statement filed with the +
+Securities and Exchange Commission is effective. This prospectus is not an +
+offer to sell these securities and it is not soliciting an offer to buy these +

+securities in any state where the offer or sale is not permitted. +
++

PROSPECTUS 3,500,000 SHARES

LOGO

COMMON STOCK

WE ARE OFFERING 1,750,000 SHARES OF COMMON STOCK AND CERTAIN SHAREHOLDERS ARE OFFERING 1,750,000 SHARES OF OUR COMMON STOCK. WE WILL NOT RECEIVE ANY OF THE PROCEEDS FROM THE SALE OF SHARES BY THE SELLING SHAREHOLDERS.

ON FEBRUARY 22, 2000, THE LAST SALE PRICE OF OUR COMMON STOCK AS REPORTED ON THE NASDAQ NATIONAL MARKET WAS $86.75 PER SHARE.

INVESTING IN OUR COMMON STOCK INVOLVES A HIGH DEGREE OF RISK. SEE "RISK FACTORS" BEGINNING ON PAGE 7 TO READ ABOUT THE RISKS YOU SHOULD CONSIDER BEFORE BUYING SHARES OF OUR COMMON STOCK.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY OTHER REGULATORY BODY HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR DETERMINED IF THIS PROSPECTUS IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

PER SHARE TOTAL

PUBLIC OFFERING PRICE..... UNDERWRITING DISCOUNTS AND COMMISSIONS..... PROCEEDS, BEFORE EXPENSES TO US (1)..... PROCEEDS TO THE SELLING SHAREHOLDERS (1).....

(1) THE UNDERWRITERS MAY PURCHASE UP TO AN ADDITIONAL 250,000 SHARES OF COMMON STOCK FROM US AND 275,000 SHARES OF COMMON STOCK FROM CERTAIN SELLING SHAREHOLDERS, AT THE PUBLIC OFFERING PRICE LESS THE UNDERWRITING DISCOUNT, SOLELY TO COVER OVER-ALLOTMENTS.

THE UNDERWRITERS EXPECT TO DELIVER THE SHARES IN NEW YORK, NEW YORK ON OR ABOUT MARCH , 2000.

BEAR, STEARNS & CO. INC.

J.P. MORGAN & CO. CHASE H&Q THOMAS WEISEL PARTNERS LLC PACIFIC GROWTH EQUITIES, INC.

THE DATE OF THIS PROSPECTUS IS MARCH , 2000 TITLE: SONICWALL (LOGO)

[PICTURE OF SONICWALL PRODUCTS]

FIREWALL SECURITY BLOCKS ACCESS TO THE NETWORK BY UNAUTHORIZED PERSONS.

VIRTUAL PRIVATE NETWORKING ENABLES SECURE COMMUNICATIONS BETWEEN BRANCH OFFICES AND THEIR CORPORATE NETWORKS.

CONTENT FILTERING BLOCKS OBJECTIONABLE WEBSITES.

[SONICWALL, INC. LOGO]

GATEFOLD ARTWORK TEXT:

TITLE: SONICWALL (LOGO) INTERNET SECURITY APPLIANCES CORPORATE FIREWALL OUR PRODUCTS ARE COMPATIBLE WITH INTERNET SECURITY PRODUCTS FOR LARGE CORPORATE NETWORKS SUCH AS CHECK POINT SOFTWARE'S FIREWALL-1. WE HAVE NO AFFILIATION WITH THESE COMPANIES.

VIRTUAL PRIVATE NETWORKING WITH SONICWALL, MOBILE WORKERS CAN USE VPN TO CONNECT SECURELY TO THE OFFICE.

MOBILE WORKER CABLE MODEM OR DSL CONNECTION VIRTUAL PRIVATE NETWORKING (BRANCH OFFICE) A SONICWALL MAY BE DEPLOYED AT EACH BRANCH OFFICE FOR COMPLETE INTERNET SECURITY: FIREWALLING, VPN AND CONTENT FILTERING.

FIREWALL SECURITY WITH SONICWALL, SMALL TO MEDIUM SIZE BUSINESSES CAN DEPLOY INTERNET SECURITY. SONICWALL DMZ PROTECTS WEB AND E-COMMERCE SERVERS DEPLOYED BY THESE BUSINESSES.

CONTENT FILTERING WITH SONICWALL WITH CONTENT FILTERING SCHOOLS AND LIBRARIES CAN PROTECT CHILDREN FROM OBJECTIONABLE WEB SITES AS WELL AS SECURE THE NETWORK FROM INTERNET HACKERS.

FIREWALL SECURITY: BLOCKS ACCESS TO THE NETWORK BY UNAUTHORIZED PERSONS. .VIRTUAL PRIVATE NETWORKING (VPN): ENABLES SECURE COMMUNICATIONS BETWEEN BRANCH OFFICES AND THEIR CORPORATE NETWORKS. .CONTENT FILTERING: BLOCK OBJECTIONABLE WEBSITES.

GATEFOLD ARTWORK DESCRIPTION OF GRAPHICS: DIAGRAM SHOWING THE INTERNET AS AN OVAL SYMBOL AND LINES CONNECTING FROM THE INTERNET THROUGH DEPICTION OF SONICWALL PRODUCTS AS THEY RELATE TO VARIOUS USER GROUPS, SUCH AS BRANCH OFFICES, SMALL TO MEDIUM SIZE BUSINESSES, SCHOOLS, AND MOBILE WORKERS.

Prospectus Summary

You should read this summary together with the more detailed information regarding our company and the common stock being sold in this offering and our consolidated financial statements and related notes to financial statements appearing elsewhere in this prospectus. Because this is only a summary, you should read this entire prospectus carefully, especially the risks described under "Risk Factors."

SonicWALL, Inc.

SonicWALL, Inc. designs, develops, manufactures and sells Internet security infrastructure products designed to provide secure Internet access to our broadband customers. Broadband access, such as digital subscriber line, or DSL, and cable modems, allows users to connect to the Internet at speeds significantly greater than analog modems. We believe our security appliances provide high performance, robust, reliable, easy-to-use and affordable Internet security. We also sell content filtering services on an annual subscription basis. We sell our products to customers in the small to medium enterprise, branch office, telecommuter and education markets. Small to medium enterprises are generally considered to have less than 1,000 people. As of December 31, 1999, we had sold more than 35,000 of our Internet security appliances worldwide. An investment in our shares involves a high degree of risk. The risks associated with investing in our stock include the following. We may not be able to maintain profitability in the future. We compete in a highly competitive market and competition may intensify. After the offering, our officers and directors and their affiliates will own approximately 55.3% of our outstanding stock and, if acting together, would be able to significantly influence all matters requiring shareholder approval. We depend on two distributors for approximately 46% of our revenue. Due to any of these risks, the trading price of our common stock could decline and you could lose all or part of your investment.

From inception in 1991 through 1996, we derived substantially all of our revenue from the sale of networking products for Apple Computer Inc. Macintosh computers. These products enable Apple Macintosh computers to connect to computer networks using Ethernet communications standards. The Ethernet standard was developed in the 1970s by Xerox Corporation and is the most widely used technology to facilitate communication between computers on local area networks. The Ethernet standard is defined by the Institute of Electrical and Electronics Engineers and specifies the speed and other characteristics of a computer network. In 1998, we made a strategic business decision to concentrate our resources in the Internet security market due to our belief that this market had better

long-term growth prospects. As a result, we stopped shipments of our Ethernet product line during December 1999. In October 1997, we began shipments of our Internet security appliance products, and we now focus all of our development, sales and marketing efforts on the Internet security appliance market. In 1998, our Internet security products represented approximately 31% of our total revenue and in 1999, they represented 92% of our total revenue. In 1998, our Ethernet products represented approximately 69% of our total revenue and in 1999, Ethernet products represented approximately 8% of our total revenue. In the years ended December 31, 1997 and 1998 we incurred losses of $467,000 and $1,461,000, respectively. In 1999, our net income was $158,000 and we had an accumulated deficit of $850,000.

Although the need for Internet security solutions is widespread, security vendors generally have focused on providing solutions for large enterprises with highly complex needs and extensive information technology, or IT, support organizations. These solutions have typically involved expensive enterprise firewall software that runs on a dedicated server or personal computer, or PC, and requires extensive support, constant monitoring, and regular updates to maintain effectiveness. In addition, these solutions often require additional products to incorporate enhanced functionalities such as virtual private networking and content filtering. We believe the expense and complexity of these solutions make them impractical for the majority of small to medium enterprises, branch offices, telecommuters and education users. These users are increasingly demanding robust, reliable, easy-to-use and affordable Internet security products.

Our SonicWALL product line provides our customers with a comprehensive integrated security solution that includes a firewall, content filtering and virtual private networking. A firewall blocks access to the network by unauthorized persons. Content filtering blocks access to objectionable web sites. Virtual private networking enables secure communications between branch offices or telecommuters and their corporate networks. We believe the SonicWALL product line is easy to install and use and minimizes the purchase, installation and maintenance costs of Internet security. With suggested retail prices ranging from $495 to $2,995, our products are designed to enable customers to reduce purchase costs and avoid hiring costly IT personnel. Our SonicWALL products are designed to maximize reliability and uptime, can be used in networks ranging in size from 1 to 1,000 users, and are fully compatible with more expensive enterprise security products offered by, among others, Check Point Software Technologies, Ltd. and Cisco Systems, Inc.

We initially incorporated in California in 1991 as Sonic Systems. In August 1999 we changed our name to SonicWALL, Inc. References to "we," "our" and "us" in this prospectus refer to SonicWALL, Inc. Our executive offices are located at 1160 Bordeaux Drive, Sunnyvale, California 94089, and our telephone number is (408) 745-9600. Our Web site is located at http://www.sonicwall.com. Any information that is included on or linked to our Web site is not a part of this prospectus.

We own or have rights to various trademarks and trade names used in our business. These include the SonicWALL name and our logo. This prospectus also includes trademarks, service marks and trade names of other companies, which remain the property of their owners.

The Offering

Common stock offered by:

SonicWALL..... 1,750,000 shares Selling shareholders..... 1,750,000 shares Common stock to be outstanding after this offering..... 25,425,385 shares Use of proceeds..... General corporate purposes to support our growth, working capital, and potential acquisitions of complementary products and technologies. We will not receive any proceeds from shares sold by the selling shareholders. See "Use of Proceeds."

Nasdaq National Market SNWL symbol.....

The number of shares of common stock to be outstanding after this offering is based upon shares outstanding as of December 31, 1999, and this number excludes 849,261 shares of common stock reserved for issuance under our stock plans, 3,794,208 shares of common stock issuable upon exercise of outstanding stock options and 250,000 shares of common stock available for issuance under our employee stock purchase plan.

Except where stated otherwise, the information we present in this prospectus (1) gives effect to a 2 for 1 split of our common stock effected on August 25, 1999 and (2) assumes no exercise by the underwriters of their over-allotment option.

Summary Financial Data (In thousands, except per share data) Year Ended December 31, 1997 1998 1999

Statement of Operations Data:			
Revenue			
Internet security	$ 250	$ 2,349	$19,403
Ethernet	9,092	5,166	1,644
Total revenue	9,342	7,515	21,047
Cost of revenue	4,842	3,308	5,961
Gross margin	4,500	4,207	15,086
Operating expenses			
Research and development	1,983	2,051	3,634
Sales and marketing	2,468	2,870	5,342
General and administrative	644	753	1,761
Deferred stock compensation	--	42	2,895
Total operating expenses	5,095	5,716	13,632
Income (loss) from operations	(595)	(1,509)	1,454
Other income (expense), net	29	54	536
Income (loss) before income taxes	(566)	(1,455)	1,990
Benefit from (provision for) income taxes	99	(6)	(1,832)
Net income (loss)	$ (467)	$(1,461)	$ 158
Basic net income (loss) per share	$(0.06)	$ (0.13)	$ 0.01
Diluted net income (loss) per share	$(0.06)	$ (0.13)	$ 0.01
Shares used in computing basic net income (loss) per share	8,461	11,251	17,334
Shares used in computing diluted net income (loss) per share	8,461	11,251	21,196

December 31, 1999 Actual As Adjusted

Consolidated Balance Sheet Data:		
Cash and cash equivalents	$ 62,589	$206,789
Total assets	71,239	215,439
Total shareholders' equity	60,750	204,950

The preceding table summarizes . actual balance sheet data; and . as adjusted balance sheet data to give effect to the sale by SonicWALL, Inc. of 1,750,000 shares of common stock in this offering at an assumed price of $86.75 per share, after deducting underwriting discounts and commissions and estimated offering expenses.

See Note 1 of Notes to Consolidated Financial Statements for information concerning the calculation of basic and diluted net income (loss) per share.

Risk Factors

An investment in our shares involves a high degree of risk. In addition to the other information contained in this prospectus, you should consider carefully the following risks before purchasing our common stock. If any of these risks occurs, our business, financial condition or operating results could be adversely affected. In that case, the trading price of our common stock could decline and you could lose all or part of your investment.

Company Risks

We have just recently entered the emerging market for broadband Internet security appliances, and we do not know if we will be successful in marketing our products to our target customers.

From inception through 1996, we derived substantially all of our revenue from the sale of Ethernet products for Apple Macintosh computers. In October 1997, we introduced our SonicWALL line of products, and in 1998 we made a strategic decision to concentrate our resources in the Internet security market. As a result, we stopped shipment of Ethernet products during December 1999. In 1997, 1998 and 1999 our Ethernet revenue was $9,092,000, $5,166,000 and $1,644,000 and represented approximately 97%, 69% and 8% respectively, of our total revenue.

We believe that many potential customers in our target markets are not fully aware of the need for Internet security products and services. Historically, only enterprises having substantial resources developed or purchased Internet security solutions. Also, there is a perception that Internet security is costly and difficult to implement. Therefore, we will not succeed unless we can educate our target markets about the need for Internet security and convince potential customers of our ability to provide this security in a cost-effective and easy-to-use manner. Although we have spent, and will continue to spend, considerable resources educating potential customers about the need for Internet security and the benefits of our products and services, our efforts may be unsuccessful.

Even if we convince our target markets about the importance of and need for Internet security, we do not know if this will result in the sale of our products. We currently expect that almost all of our future revenue will be generated through sales of our SonicWALL products, including related services such as subscription and license fees. Our success depends on market acceptance of our products and services.

We may be unable to manage our growth, and if we cannot do so, it could have a material adverse effect on our business.

Our business has grown rapidly in the last year. At the end of 1998, we had 26 employees. As of December 31, 1999, we had 73 employees, an increase of approximately 181%. In addition, we have experienced expansion in our manufacturing and shipping requirements, our product lines, our customer base and our end user installed base. This rapid expansion has placed significant strain on our administrative, operational and financial resources and has resulted in ever-increasing responsibilities for our management personnel. These changes have increased the complexity of managing SonicWALL, Inc. If we continue to experience significant growth, our current systems, management and resources will be inadequate, and our organization will need to grow rapidly in order to meet the demands placed on our business. If we cannot manage our growth effectively, our business prospects will be materially adversely affected.

We do not know if we will be able to maintain profitability in the future.

We incurred losses of $467,000 in 1997 and $1,461,000 in 1998, which represented 5.0% and 19.5%, respectively, of total revenue. We made $158,000 in net income, or less than 1% of revenue, for the year ended December 31, 1999. As of December 31, 1999 we had an accumulated deficit of $850,000. We do not know if we will be able to maintain profitability in the future. If we are not able to maintain profitability, your investment in our common stock may decline in value.

Because we recently introduced our Internet security products, we cannot predict our future operating results or our future revenues from these products.

Because we recently changed our business focus from Ethernet products for Macintosh computers to Internet security products, our historical financial information is of limited value in projecting future operating results. We believe that comparing different periods of our operating results is not meaningful and you should not rely on the results for any period as an indication of our future performance.

Our limited experience with sales of Internet security products is one of many factors underlying our inability to predict our revenue for a given period. We base our spending levels for product development, sales and marketing, and other operating expenses largely on our expected future revenue. A large proportion of our expenses is fixed for a particular quarter or year, and therefore, we may be unable to decrease our spending in time to compensate for any unexpected quarterly or annual shortfall in revenue. As a result, any shortfall in revenue could adversely affect our operating results.

We depend on two major distributors for a significant amount of our revenue, and if they or others cancel or delay purchase orders, our revenue may decline and the price of our stock may fall.

In 1999, approximately 86% of our sales were to distributors. To date, sales to a limited number of distributors have accounted for a significant portion of our revenue. In 1999, Ingram Micro, Inc. and Tech Data Corp., both of which are global computer equipment and accessory distributors, accounted for approximately 34% and 12% of our revenue, respectively. In 1998, sales to Ingram Micro accounted for 34% of our revenue. We cannot assure you that either of these existing customers will continue to place orders with us, that orders by these existing customers will continue at the levels of previous periods or that we will be able to obtain large orders from new customers.

We anticipate that sales of our products to relatively few customers will continue to account for a significant portion of our revenue. If any of our major distributors stops or delays its purchase of our products, our revenue and profitability would be adversely affected. In addition, as of December 31, 1999, Ingram Micro and Tech Data represented $2.1 million and $0.6 million, respectively, of our accounts receivable, constituting 49% and 14%, respectively, of total receivables on such date. The failure of any of these distributors to pay us in a timely manner could adversely affect our payments to suppliers and our creditworthiness, which could make it more difficult to conduct business.

Although we have limited one year agreements with Ingram Micro and Tech Data, these contracts are subject to termination at any time, and we do not know if these customers will continue to place orders for our products.

If an OEM customer cancels, reduces, or delays purchases, our revenue may decline and our business could be adversely affected.

To date, we have formed OEM relationships with three OEMs, including, most recently, 3COM Corporation. If we fail to sell to such OEMs in the quantities expected, or if any OEM terminates our relationship, this could adversely affect our reputation, the perception of our products and technology in the marketplace, or the growth of our business, and your investment in our common stock may decline in value.

Our sales are usually done on a purchase order basis and we have no binding purchase commitments from our distributors or original equipment manufacturers, which could result in a lack of sales.

We sell our products to end users through distributors, resellers and original equipment manufacturers. Our success depends in large part on their performance. These customers:

. are not obligated to purchase or market our products and can stop doing so at any time; and . have no exclusive arrangements with us, and are not obligated to renew their agreements with us.

Average selling prices of our products may decrease, which may reduce our gross margins.

The average selling prices for our products may decline as a result of competitive pricing pressures, promotional programs and customers who negotiate price reductions in exchange for longer term purchase commitments. The pricing of products depends on the specific features and functions of the products, purchase volumes and the level of sales and service support. We expect competition to increase in the future. As we experience pricing pressure, we anticipate that the average selling prices and gross margins for our products will decrease over product life cycles. We cannot assure you that we will be successful in developing and introducing on a timely basis new products with enhanced features, or that these products, if introduced, will enable us to maintain our average selling prices and gross margins at current levels.

We offer retroactive price protection to our major distributors and if we fail to balance their inventory with end user demand for our products, our allowance for price protection may be inadequate. This could adversely affect our results of operations.

We provide our major distributors with price protection rights for inventories of our products held by them. If we reduce the list price of our products, our major distributors receive refunds or credits from us that reduce the price of such products held in their inventory based upon the new list price. As of December 31, 1999, we estimate that approximately $1.2 million of our products were in our distributors' inventory and therefore subject to price protection. This amount represented approximately 5.7% of our revenue for the year ending December 31, 1999. We have provided less than $100,000 of credits under our price protection policies in the past three fiscal years. Future credits for price protection will depend on the percentage of our price reductions for the products in inventory and our ability to manage the level of our major distributors' inventory. New product introductions or price reductions by us or our competitors could result in significant product price adjustments. If future price protection adjustments are higher than expected, our future results of operations could be materially adversely affected.

We are dependent on international sales for a substantial amount of our revenue. We face the risks of international business and associated currency fluctuations, which might adversely affect our operating results.

International revenue represented 32% of total revenue in 1998 and 34% of total revenue in 1999. For the year ended December 31, 1999, revenue from Japan represented 11% of our total revenue, and revenue from Europe, the Middle East and Africa collectively represented approximately 17% of our total revenue. We expect that international revenue will continue to represent a substantial portion of our total revenue in the foreseeable future. Our risks of doing business abroad include our ability to maintain distribution relationships on favorable terms. To the extent we are unable to favorably renew our distribution agreements or make alternative arrangements, revenue may decrease from our international operations. We also face risks associated with general economic conditions and regulatory uncertainties associated with our international sales. Because our sales are denominated in United States dollars, the weakness of a foreign country's currency against the dollar could increase the price of our products in such country and reduce our product unit sales by making our products more expensive in the local currency.

We are subject to the risks of conducting business internationally, including potential foreign government regulation of our technology, general geopolitical risks associated with political and economic instability, changes in diplomatic and trade relationships, and foreign countries' laws affecting the Internet generally.

Delays in deliveries from our component suppliers could cause our revenue to decline and adversely affect our results of operations.

We outsource all of our hardware manufacturing and assembly for our security appliances to a single manufacturer. Our SonicWALL products incorporate certain components or technologies which are only available from single or limited sources of supply. Specifically, our products rely upon microprocessors from Motorola, Inc. and Intel Corporation and incorporate software products from third-party vendors. In addition, our products utilize components that have in the past been subject to market shortages and price fluctuations.

We do not have long-term supply arrangements with any vendor, and this may adversely affect our ability to obtain necessary components or technology for our products. If we are unable to purchase such components or maintain licenses from these suppliers, this may delay or prevent product shipments and result in a loss of sales. This could cause a loss of revenue which would adversely affect our results of operations. We may not be able to replace any of these supply sources on economically advantageous terms. In addition, if we experience price increases in our product components, we will experience declines in our gross margins.

We may have to defend lawsuits or pay damages in connection with any alleged or actual failure of our products and services.

Because our products and services provide and monitor Internet security and may protect valuable information, we may face claims for product liability, tort or breach of warranty. Anyone who circumvents our security measures could misappropriate the confidential information or other property of end users using our products and services or interrupt their operations. If that happens, affected end users or others may sue us. In addition, we may face liability for breaches caused by faulty installation of our products by resellers or end users. Although we attempt to reduce the risk of losses from claims through contractual warranty disclaimers and liability limitations, these provisions may be unenforceable. Some courts, for example, have found contractual limitations of liability in standard computer and software contracts to be unenforceable in some circumstances. Defending a lawsuit, regardless of its merit, could be costly and could divert management attention. Although we currently maintain business liability insurance, this coverage may be inadequate or may be unavailable in the future on acceptable terms, if at all. Our business liability insurance has no specific provisions for potential liability for Internet security breaches.

A security breach of our internal systems or those of our customers could harm our business.

Because we provide Internet security, we may become a greater target for attacks by computer hackers. We will not succeed unless the marketplace is confident that we provide effective Internet security protection. Networks protected by our products may be vulnerable to electronic break-ins. Because the techniques used by computer hackers to access or sabotage networks change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques. Although we have not experienced any act of sabotage or unauthorized access by a third party of our internal network to date, if an actual or perceived breach of Internet security occurs in our internal systems or those of our end-user customers, regardless of whether we cause the breach, it could adversely affect the market perception of our products and services. This could cause us to lose current and potential customers, resellers, distributors or other business partners.

We rely primarily on one contract manufacturer for all of our product manufacturing and assembly, and if we cannot obtain its services, we may not be able to ship products.

We outsource all of our hardware manufacturing and assembly primarily to one third-party manufacturer and assembly house--Flash Electronics, Inc. We do not have a long-term manufacturing contract with this vendor. Flash Electronics has produced products with acceptable quality, quantity

and cost in the past, but it may be unable or unwilling to meet our future demands. Our operations could be disrupted if we have to switch to a replacement vendor or if our hardware supply is interrupted for an extended period. This could result in loss of customer orders and revenue.

We may have to reduce or cease operations if we are unable to obtain the funding necessary to meet our working capital requirements.

We believe that the net proceeds from this offering, together with our existing cash balances and our existing line of credit, will be sufficient to meet our capital requirements for at least the next twelve months. However, if our future revenue is insufficient to support the expenses of our operations and the expansion of our business, we may need additional equity or debt capital to finance our operations. If we are unable to generate sufficient cash flow from operations or obtain funds through additional financing, we may have to reduce some or all of our development and sales and marketing efforts or cease operations. Our funding requirements depend on several factors, including the rate of market acceptance of our products and services, our ability to expand our customer base and the growth of our sales and marketing capabilities. If our funding requirements vary from our current plans, we may require additional financing sooner than we anticipate. Additional financing may not be available when needed and, if such financing is available, it may not be available on terms favorable to us.

Acquisitions of products or technologies may result in disruptions to our business and management due to difficulties integrating personnel and operations.

Although we have no current plans, agreements or commitments with respect to any acquisitions, we may acquire or invest in other companies, products or technologies. If we make any acquisitions, we will be required to integrate the operations, products and personnel of the acquired businesses and train, retain and motivate key personnel from the acquired businesses. We may be unable to maintain uniform standards, controls, procedures and policies if we fail in these efforts. Similarly, acquisitions may cause disruptions in our operations and divert management's attention from day-to-day operations, which could impair our relationships with our current employees, customers and strategic partners.

We may have to incur debt or issue equity securities to pay for any future acquisitions. The issuance of equity securities for any acquisition could be substantially dilutive to our stockholders. In addition, our profitability may suffer because of acquisition-related costs or amortization costs for acquired goodwill and other intangible assets.

We may be unable to adequately protect our proprietary rights, which may limit our ability to compete effectively.

Unauthorized parties may misappropriate or infringe our trade secrets, copyrights, trademarks and similar proprietary rights. We have not received any patent protection for our technology or products. Even if we obtain such patents, that does not guarantee that our patent rights are valuable, create a competitive barrier, or will be free from infringement. We face additional risk when conducting

business in countries that have poorly developed or inadequately enforced intellectual property laws. In any event, competitors may independently develop similar or superior technologies or duplicate the technologies we have developed, which could substantially limit the value of our intellectual property.

Potential intellectual property claims and litigation could subject us to significant liability for damages and invalidation of our proprietary rights.

In the future, we may have to resort to litigation to protect our intellectual property rights or trade secrets or to determine the validity and scope of the proprietary rights of others. Any litigation, regardless of its success, would probably be costly and require significant time and attention of our key management and technical personnel. Litigation could also force us to:

. stop or delay selling, incorporating or using products that incorporate the challenged intellectual property;

. pay damages;

. enter into licensing or royalty agreements, which may be unavailable on acceptable terms; or . redesign products or services that incorporate infringing technology.

We may face infringement claims from third parties in the future. The computer industry has seen frequent litigation over intellectual property rights. We expect that infringement claims will be more frequent for Internet participants as the number of products, services and competitors grows and functionality of products and services overlaps.

Undetected product errors or defects could result in loss of revenue, delayed market acceptance and claims against us.

We offer a one-year warranty on all of our products, allowing the end user to receive a repaired or replacement product for any defective unit. Historically, refunds based on product warranty claims have been insignificant. Although we have discovered few errors or defects in our products, our products may contain undetected errors or defects. If there is a product failure, we may have to replace all affected products without being able to book revenue for such replacement units, or we may have to refund the purchase price for such units. Because of our recent introduction of Internet security products, we have little experience in gauging the risk of unexpected product failures or defects. Despite extensive testing, some errors are discovered only after a product has been installed and used by customers. Any errors discovered after commercial release could result in loss of revenue and claims against us. In the year ended December 31, 1999, refunds attributable to errors or defects in products amounted to less than 1% of total revenue for the period.

If we do not retain our key employees and attract new employees, our ability to execute our business strategy will be impaired.

We compete for employees in California's Silicon Valley, one of the most difficult employer environments in the United States. Our future success will depend largely on the efforts and abilities of our current senior management and our ability to attract and retain additional key development, technical, operations, information systems, customer support and sales and marketing personnel. We

do not have employment contracts with any of our key employees, who may leave us at any time. Specifically, the services of Sreekanth Ravi, President and Chief Executive Officer, and Sudhakar Ravi, Chief Technical Officer, would be difficult to replace. We do not maintain life insurance for any of our key personnel. See "Management" for detailed information on our key personnel.

Industry Risks

Our revenue growth is dependent on the continued growth of broadband access services, which are currently in early stages of development, and if such services are not widely adopted or we are unable to address the issues associated with the development of such services, our sales will be adversely affected.

Sales of our products depend on the increased use and widespread adoption of broadband access services, such as cable, DSL, Integrated Services Digital Network, or ISDN, Frame Relay and T-1. These broadband access services typically are more expensive in terms of required equipment and ongoing access charges than is the case with Internet dial-up access providers. Our business, prospects, results of operations and financial condition would be materially adversely affected if the use of broadband access services does not increase as anticipated or if our customers' access to broadband services is limited. Critical issues concerning use of broadband access services are unresolved and will likely affect the use of broadband access services. These issues include:

. security;

. reliability;

. bandwidth;

. congestion;

. cost;

. ease of access; and . quality of service.

Even if these issues are resolved, if the market for products that provide broadband access to the Internet fails to develop, or develops at a slower pace than we anticipate, our business, prospects, results of operations and financial condition would be materially adversely affected.

The broadband access services market is new and is characterized by rapid technological change, frequent enhancements to existing products and new product introductions, changes in customer requirements and evolving industry standards. We may be unable to respond quickly or effectively to these developments. The introduction of new products by competitors, market acceptance of products based on new or alternative technologies, or the emergence of new industry standards, could render our existing or future products obsolete, which would materially adversely affect our business, prospects, results of operations and financial condition.

The emergence of new industry standards might require us to redesign our products. If our products fail to comply with widely adopted industry standards, our customers and potential customers may not purchase our products. This would have a material adverse effect on our business, prospects, results of

operations and financial condition.

If we are unable to compete successfully in the highly competitive market for Internet security products and services, our business will fail.

The market for Internet security products is world-wide and highly competitive, and we expect competition to intensify in the future. There are few substantial barriers to entry, and additional competition from existing competitors and new market entrants will likely occur in the future. Current and potential competitors in our markets include, but are not limited to the following, all of whom sell world-wide or have a presence in most of the major markets for such products:

. enterprise firewall software vendors such as Check Point Software and Axent Technologies, Inc.;

. network equipment manufacturers such as Cisco Systems, Lucent Technologies, Inc., Nortel Networks Corp., 3COM Corporation and Nokia Corp.;

. computer or network component manufacturers such as Intel Corporation;

. operating system software vendors such as Microsoft Corporation, Novell, Inc. and Sun Microsystems, Inc.;

. security appliance suppliers such as WatchGuard Technologies, Inc.; and . low cost Internet router suppliers which may include limited Internet security functionality.

Most of our competitors to date have generally targeted large enterprises' security needs with firewall products that range in price from approximately $5,000 to more than $15,000. Recently, some of our competitors have introduced products priced at less than $1,000, which may increase competitive pressure on some of our products, resulting in both lower prices and gross margins. Many of our current or potential competitors have longer operating histories, greater name recognition, larger customer bases and significantly greater financial, technical, marketing and other resources than we do. Nothing prevents or hinders these actual or potential competitors from entering our target markets at any time. In addition, our competitors may bundle products competitive to ours with other products that they may sell to our current or potential customers. These customers may accept these bundled products rather than separately purchasing our products. If these companies were to use their greater financial, technical and marketing resources in our target markets, it could adversely affect our business.

Rapid changes in technology and industry standards could render our products and services unmarketable or obsolete, and we may be unable to successfully introduce new products and services.

To succeed, we must continually change and improve our products in response to rapid technological developments and changes in operating systems, broadband Internet access, application and networking software, computer and communications hardware, programming tools, computer language technology and other security threats. We may be unable to develop new products and services or achieve and maintain market acceptance of them once they have come to market. Product development for Internet security appliances requires substantial engineering time and testing. Releasing new products and services prematurely may result in quality problems, and delays may result in loss of

customer confidence and market share. In the past, we have on occasion experienced delays in the scheduled introduction of new and enhanced products and services, and we may experience delays in the future. When we do introduce new or enhanced products and services, we may be unable to manage the transition from the older products and services to minimize disruption in customer ordering patterns, avoid excessive inventories of older products and deliver enough new products and services to meet customer demand.

Governmental regulations affecting Internet security could affect our revenue.

Any additional governmental regulation of imports or exports or failure to obtain required export approval of our encryption technologies could adversely affect our international and domestic sales. The United States and various foreign governments have imposed controls, export license requirements and restrictions on the import or export of some technologies, especially encryption technology. In addition, from time to time governmental agencies have proposed additional regulation of encryption technology, such as requiring the escrow and governmental recovery of private encryption keys. Additional regulation of encryption technology could delay or prevent the acceptance and use of encryption products and public networks for secure communications. This, in turn, could decrease demand for our products and services.

In addition, some foreign competitors are subject to less stringent controls on exporting their encryption technologies. As a result, they may be able to compete more effectively than we can in the United States and international Internet security market.

Recently, political attention has resulted in legislative efforts to make the Internet safe for children at schools and other educational institutions receiving federal assistance by linking the receipt of federal funds to the existence of content filtering and security software for such institutions' Internet connections. Some have questioned the constitutionality or other legality of such efforts, but we believe that any government controls or attempts to regulate the Internet could have a material effect on our business. A government requirement of Internet security for schools receiving federal funds would encourage purchases of our SonicWALL products; a court ruling that prohibited such a requirement after the requirement was in place might reduce sales to these market segments.

Our failure or the failure of our key suppliers and customers to be year 2000 compliant could negatively impact our business.

We believe that we have successfully rendered our products, internal management and other administrative systems and external information systems year 2000 compliant. In addition, we have surveyed the vendors of the third- party technologies we incorporated into our products and services and applied updates or arrangements to correct potential year 2000 compliance problems. Since January 1, 2000, we have experienced no disruptions in our business operations as a result of year 2000 compliance problems or otherwise, and we have received no reports of any year 2000 compliance problems with our products and services. To date, the total cost of our efforts to address year 2000 compliance has not been material.

Nonetheless, some problems related to year 2000 risks may not appear until several months after January 1, 2000. Year 2000 issues could include problems with our own products and services or with third-party products or technology that we use or with which our products exchange data. Any problems that are not identified and corrected successfully and completely could adversely affect our business.

Investment Risks

Our management has broad discretion as to how to use the proceeds from this offering and the proceeds may not be used effectively.

We expect to use the net proceeds of this offering primarily for general corporate purposes to support our growth, working capital and potential acquisitions of complementary products and technologies. In particular, we intend to increase our spending on sales and marketing, research and development and administrative infrastructure. We have no specific plan as to how we will spend the majority of the proceeds of this offering. If our management uses poor judgment in spending the proceeds, our business will be adversely affected. We cannot assure you that investment of the proceeds will yield a favorable return or any return. See "Use of Proceeds."

Because they will own approximately 55.3% of our stock ownership after the offering, our officers, directors and their affiliates will be able to elect the board of directors and control all matters requiring shareholder approval.

Executive officers, directors, and entities affiliated with them, will, in the aggregate, beneficially own approximately 55.3% of our outstanding common stock following the completion of this offering. These shareholders, if acting together, would be able to significantly influence all matters requiring shareholder approval, including the election of directors, mergers or other forms of business combinations. See "Principal and Selling Shareholders."

The price of our common stock has been volatile and may continue to experience volatility.

The trading price of the shares being sold in this offering may fluctuate widely as a result of a number of factors, most of which are outside our control. Some of these factors include:

. quarter-to-quarter variations in our operating results;

. our announcements about the performance of our products and our competitors' announcements about performance of their products; and . changes in earnings estimates by, or failure to meet the expectations of, analysts.

In addition, the stock market has experienced extreme price and volume fluctuations, which have particularly affected the market prices of many technology and computer software companies and which have often been unrelated to the operating performance of these companies.

Charter and bylaw provisions limit the authority of our shareholders, and therefore minority shareholders may not be able to significantly influence SonicWALL, Inc.'s governance or affairs.

Our board of directors has the authority to issue shares of preferred stock and to determine the price, rights, preferences, privileges and restrictions, including voting rights, of those shares without any further vote or action by shareholders. The rights of the holders of common stock will be subject to, and may be adversely affected by, the rights of the holders of any preferred stock that may be issued in the future. The issuance of preferred stock, while providing flexibility in connection with possible acquisitions and other corporate purposes, could have the effect of making it more difficult for a third party to acquire a majority of our outstanding voting stock.

Our charter documents also provide for limitations on the ability of shareholders to call special meetings and act by written consent and prohibit cumulative voting for directors. As a result, minority shareholder representation on the board of directors may be difficult to establish. The charter documents also limit the persons who may call special meetings of the shareholders, prohibit shareholder actions by written consent and establish advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted on by shareholders at shareholder meetings.

Substantial future sales of our common stock in the public market could cause our stock price to fall.

If our shareholders sell substantial amounts of our common stock in the public market following this offering, including shares issued upon the exercise of outstanding options, the trading price of our common stock could fall. Such sales also might make it more difficult for us to raise capital in the future at a time and price that we deem appropriate. Upon completion of this offering, we will have outstanding 25,425,385 shares of common stock. Of these shares, the 4,600,000 shares sold in the initial public offering on November 11, 1999 and the 3,500,000 shares sold in this offering will be freely tradable, and the remaining 17,325,385 shares will become available for sale as follows:

Number of Date of Availability for Sale Shares May 9, 2000..... 3,268,711 90 days after completion of this offering..... 11,345,274 At various times after May 9, 2000 (as Rule 144 holding periods expire)..... 2,711,400 In addition, in connection with this offering, our selling shareholders and executive officers have agreed not to sell, transfer or exchange any shares of our common stock for a period of 90 days after the date of this prospectus without the written consent of Bear, Stearns & Co. Inc.

The holders of approximately 2,876,754 shares of common stock are entitled to require us to register their shares under the Securities Act of 1933, as amended, the Act, if more than 50% of the holders of registration rights demand registration of at least half of their shares having an expected aggregate offering price of $2,000,000 or more. These holders and holders of approximately 2,301,400 shares of common stock have the right to participate in any registration of shares we undertake on our own, except a registration of shares in connection with an employee benefit plan or merger. If these shareholders exercise their registration rights, a large number of our shares may be registered and sold in the public market. This could adversely affect the trading price for our shares. If we attempted to raise money through a registration and sale of our stock and these shareholders forced us to allow them to participate in the registration, our ability to raise the amount of money we need to execute our business plan could be adversely affected. See "Description of Capital Stock--Registration Rights."

Bear, Stearns & Co. Inc. may, in its sole discretion and at any time without notice, release all or any portion of the securities subject to lock-up agreements. See "Shares Eligible for Future Sale."

You will experience substantial dilution in the value of your shares immediately following this offering.

The price of the shares is substantially higher than the net tangible book value per share. If you buy any shares in the offering, you will incur immediate and substantial dilution in the net tangible book value of each share. If others exercise options to purchase our common stock, you will suffer further dilution. See "Dilution."

Cautionary Note on Forward-looking Statements

Some of the matters discussed under the captions "Prospectus Summary," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Business" and elsewhere in this prospectus include forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events, including, among other things:

. implementing our business strategy;

. developing and introducing new products;

. obtaining and expanding market acceptance of the products we offer;

. meeting our requirements with our customers; and . competition in the Internet security market.

In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "potential," "continue," "expects," "anticipates," "intends," "plans," "believes," "estimates" and similar expressions. These statements are based on our current beliefs, expectations and assumptions and are subject to a number of risks and uncertainties. A description of some risks that could cause our results to vary appears under the caption "Risk Factors" and elsewhere in this prospectus. In light of these assumptions, risks and uncertainties, the forward-looking events discussed in this prospectus might not occur.

Use of Proceeds

Our net proceeds from the sale and issuance of 1,750,000 shares of common stock will be approximately $144.2 million at an assumed sale price of $86.75 per share, after deducting underwriting discounts and commissions and the estimated offering expenses payable by us. We will use the net proceeds from this offering for general corporate purposes to support our growth, working capital, and potential acquisitions of complementary products and technologies. We do not have specific uses planned for much of the offering proceeds. We will not receive any proceeds from the shares sold by the selling shareholders.

We may use a portion of the net proceeds to acquire or invest in complementary businesses, products or technologies. From time to time, we evaluate these potential acquisitions and we anticipate continuing to make such evaluations. We have no current plans, agreements or commitments with respect to any such acquisitions. Pending any of these uses, we intend to invest the net proceeds of this offering in short-term, interest-bearing, investment grade securities.

Dividend Policy

We have never declared or paid any cash dividends on our capital stock and we do not anticipate paying any cash dividends on our capital stock in the foreseeable future. We currently intend to retain any future earnings for use in our business. Our line of credit arrangement prohibits us from paying dividends without the lender's prior consent.

Price Range of Common Stock

The following table sets forth the high and low closing prices for our common stock as reported on the Nasdaq National Market for the period from November 11, 1999 through:

High Low

Fourth Quarter ending December 31, 1999..... $43.50 $24.50 First Quarter through February 22, 2000 ..... $99.00 $35.00

Capitalization

The following table shows as of December 31, 1999:

. our actual capitalization; and . our capitalization as adjusted to reflect the sale by us of 1,750,000 shares of common stock at an assumed price of $86.75 per share in this offering, after deducting underwriting discounts and commissions and estimated expenses.

This table should be read in conjunction with the consolidated financial statements and notes appearing elsewhere in this prospectus.

December 31, 1999 Actual As Adjusted (In thousands, except share data)

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Shareholders' equity:
  Common stock: 200,000,000 shares authorized; 23,675,385
   shares issued and outstanding: actual 25,425,385
   shares issued and outstanding as adjusted..... $ 65,109   $209,309
  Deferred stock compensation.....                   (3,209)    (3,209)
  Note receivable from shareholder.....                (300)      (300)
  Accumulated deficit.....                             (850)      (850)
    Total shareholders' equity.....                  60,750    204,950
    Total capitalization..... $ 60,750   $204,950
```

The number of shares of common stock issued and outstanding as of December 31, 1999 excludes:

. 849,261 shares available for grant under our stock option plans;

. 3,794,208 shares of common stock issuable upon exercise of options outstanding under our stock option plans, at a weighted average exercise price of $4.51 per share, of which options to purchase 603,677 shares are currently exercisable; and . 250,000 shares of common stock available for issuance under our employee stock purchase plan.

Dilution

Our net tangible book value at December 31, 1999 was $59.4 million, or $2.51 per share of common stock. After giving effect to the sale of 1,750,000 shares of common stock by us in this offering at an assumed price of $86.75 per share, less underwriting discounts and commissions and estimated expenses we expect to pay, our net tangible book value at December 31, 1999 would have been $203.6 million, or $8.01 per share. Purchasers of common stock in this offering will experience substantial and immediate dilution in net tangible book value per share for financial accounting purposes. The following table illustrates this per-share dilution:

Public offering price per share..... $86.75 Less net tangible book value per share after this offering(1)..... 8.01 Immediate dilution in net tangible book value per share to new investors..... $78.04 (1) Determined by dividing the total number of common stock shares to be outstanding after this offering into our net tangible book value, after giving effect to the net proceeds of this offering.

SELECTED CONSOLIDATED FINANCIAL DATA (In thousands, except per share data) The following selected consolidated financial data should be read in conjunction with our consolidated financial statements and related notes thereto and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in this prospectus. The consolidated statements of operations data for each of the years in the three year period ended December 31, 1999 and the balance sheet data at December 31, 1998 and 1999 are derived from the audited consolidated financial statements included elsewhere in this prospectus. The consolidated statement of operations data for the years ended December 31, 1995 and 1996 and the balance sheet data at December 31, 1995, 1996 and 1997 are derived from audited financial statements which are not included in this prospectus. The historical results are not necessarily indicative of the operating results to be expected in the future.

Year Ended December 31, 1995 1996 1997 1998 1999

Statement of Operations Data:					
Revenue					
Internet security.....	$ --	$ --	$ 250	$ 2,349	$19,403
Ethernet.....	10,482	9,356	9,092	5,166	1,644
Total revenue.....	10,482	9,356	9,342	7,515	21,047
Cost of revenue.....	6,411	5,915	4,842	3,308	5,961
Gross margin.....	4,071	3,441	4,500	4,207	15,086
Operating expenses					
Research and development.....	1,241	1,048	1,983	2,051	3,634
Sales and marketing.....	1,856	1,665	2,468	2,870	5,342
General and administrative.....	529	432	644	753	1,761
Deferred stock compensation.....	--	--	--	42	2,895

Total operating expenses.....	3,626	3,145	5,095	5,716	13,632
Income (loss) from operations.....	445	296	(595)	(1,509)	1,454
Other income (expense), net.....	(30)	22	29	54	536
Income (loss) before income taxes.....	415	318	(566)	(1,455)	1,990
Benefit from (provision for) income taxes.....	(164)	(350)	99	(6)	(1,832)
Net income (loss).....	$ 251	$ (32)	$ (467)	$(1,461)	$ 158
Basic net income (loss) per share.....	$ 0.03	$ --	$ (0.06)	$ (0.13)	$ 0.01
Diluted net income (loss) per share.....	$ 0.02	$ --	$ (0.06)	$ (0.13)	$ 0.01
Shares used in calculation of basic net income (loss) per share.....	9,626	8,460	8,461	11,251	17,334
Shares used in calculation of diluted net income (loss) per share.....	11,224	8,460	8,461	11,251	21,196

December 31, 1995 1996 1997 1998 1999

Consolidated Balance Sheet Data:					
Cash and cash equivalents.....	$ 145	$1,036	$ 787	$ 1,051	$62,589
Total assets.....	2,810	3,448	2,374	4,751	71,239
Total shareholders' equity.....	$ 963	$ 932	$ 465	$ 1,488	$60,750

See Note 1 of Notes to Consolidated Financial Statements for information concerning the calculation of basic and diluted net income (loss) per share.

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following commentary should be read in conjunction with the financial statements and related notes contained elsewhere in this prospectus. The discussion contains forward-looking statements that involve risks and uncertainties. These statements relate to future events or our future financial performance. In many cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "potential," "intend" or "continue," or the negative of such terms and other comparable terminology. These statements are only predictions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of a variety of factors, including, but not limited to, those set forth under "Risk Factors" and elsewhere in this prospectus.

Overview

From inception through 1996, we derived substantially all of our revenue from the development and marketing of networking products for Apple Macintosh computers. These products enable Apple Macintosh computers to connect to computer networks using Ethernet communications standards. The Ethernet standard was developed in the 1970s by Xerox Corporation and is the most widely used technology to facilitate communication between computers on local area networks. The Ethernet standard is defined by the Institute of Electrical and Electronics Engineers and specifies the speed and other characteristics of a computer network. In 1998, we made a strategic business decision to

concentrate our resources in the Internet security market due to our belief that this market had better long-term growth prospects. As a result, we stopped shipments of our Ethernet product line during December 1999. In October 1997, we introduced our first Internet security appliance, the SonicWALL DMZ, and began volume shipments in 1998. In 1998 we began offering content filtering subscriptions to our SonicWALL customers. Customers can purchase subscriptions for one to four years, and they receive weekly updated lists of objectionable web site addresses to which they can block access. We now focus all our development, marketing and sales efforts on the Internet security appliance market. Our shift to selling Internet security products has not required any significant restructuring of our personnel, facilities, manufacturing or operations. We do not expect any significant charges related to our Ethernet product inventories or warranty obligations. In 1998, our Internet security products represented approximately 31% of our total revenue and in 1999 they represented 92% of our total revenue. In 1998, our Ethernet products represented 69% of our total revenue and in 1999, Ethernet products represented approximately 8% of our total revenue.

Our SonicWALL products are sold primarily through distributors who then resell our products to resellers and selected retail outlets. These resellers then sell our products to end-users. Two of our distributors, Ingram Micro, Inc. and Tech Data Corp., both of which are global computer equipment and accessory distributors, account for approximately 46% of our revenue. In 1998, sales to Ingram Micro accounted for 34% of our revenue. In 1999, sales to Ingram Micro and Tech Data accounted for 34% and 12% of our revenue, respectively.

Our revenue consists primarily of product sales and, to a lesser extent, subscription fees from content filtering services and extended warranty contract fees. Product sales comprised approximately 95% of total revenue for the year ended December 31, 1999. We generally recognize revenue when we ship products to our customers. Agreements with many of our distributors provide for stock rotation, price protection and co-op advertising rights. Stock rotation rights provide a distributor the right to exchange unsold inventory for alternative products. Ingram Micro's right to return or rotate its stock on- hand is unlimited, and therefore we recognize revenue for product sales to Ingram Micro when it has sold the product to its customers. Ingram Micro does not have the right to return non-defective products to us if a customer of Ingram Micro returns such a product to Ingram Micro. For all other distributors, the value of stock that can be rotated is generally limited to 15% of the prior quarter's purchases. Co-op advertising rights provide a distributor the right to be reimbursed up to 3% of the prior quarter's sales for costs it has incurred associated with advertising our products. For all of our distributors, we provide an allowance for sales returns, price protection rights and reserves for warranty and co-op advertising costs at the time of revenue recognition. Price reductions which may result in price protection require the approval of our president, chief financial officer, and vice president of sales. Subscription fees and extended warranty fees are deferred and amortized over the period of the related contracts. Subscription and extended warranty fees to date have not been material.

To date, a significant portion of our revenue has been dependent on large purchase orders from a limited number of distributors. These purchase orders typically have short lead times and are subject to delay or cancellation without penalty. We anticipate that our operating results for a given period will

continue to depend on a small number of customers. If we experience a decline in revenue from any of our significant distributors in a given quarter, our revenue for that quarter, or following quarters, will be adversely affected. This could adversely affect our business, prospects, results of operations and financial condition. Furthermore, if any of our significant customers experiences financial difficulties, our sales to these customers may be reduced, and we may have difficulty collecting accounts receivable from these customers. Any delay in large customer orders or customer financial difficulties could have a material adverse effect on our business, prospects, results of operations and financial condition.

We primarily use one contract manufacturer to manufacture our products. We also rely on single or limited source suppliers to provide key components of our products. A significant portion of our cost of revenue is related to these suppliers. These relationships are subject to a variety of risks.

In August 1998, we acquired all the partnership interest of AckFin Networks, a California general partnership, in exchange for an aggregate of 5,426,184 shares of all common stock with an estimated value of $0.90 per share, or $4,883,000, and the assumption of $150,000 in liabilities. The controlling partners of AckFin, Sreekanth Ravi and Sudhakar Ravi, two of our executive officers and principal shareholders, were also the majority shareholders of SonicWALL, Inc. and, therefore, were deemed to be a control group for purposes of determining the amount of purchase price to be "stepped-up." The value of the exchanged shares for AckFin was accounted for as a reorganization of entities under common control. Accordingly, net assets acquired were valued by applying carryover basis to the control group interest and a stepped-up basis to the minority interest. The step-up of the minority interest resulted in an intangible asset of $2,517,000. This intangible asset was attributed to acquired completed technology and will be amortized over a period of three years. Amortization expense was $350,000 and $839,000 for the years ended December 31, 1998 and 1999, respectively. The intangible assets acquired by us were rights to the completed core technology developed by AckFin that provides the foundation for our Internet products. Since this transaction occurred between entities that were under common control, the financial results of AckFin have been combined with our results for the period since the inception of AckFin, April 1997, through the date of exchange, August 1998. Expenses totaling $150,000 and $775,000 for the years ended December 31, 1997 and 1998, respectively, were included in the accompanying statements of operations. AckFin did not have any revenue transactions with unrelated third parties. Except for the expenses noted above, all other financial transactions for AckFin were eliminated upon combination with SonicWALL, Inc.

In 1998, we recorded total deferred stock compensation of approximately $48,000 in connection with stock and stock options granted during 1998 at prices subsequently deemed to be below fair market value on the date of grant. Options granted are typically subject to a four-year vesting period. Restricted stock acquired through the exercise of unvested stock options is subject to our right to repurchase the unvested stock at the price paid, which right lapses over a four-year period. We are amortizing the deferred stock compensation over the vesting periods of the applicable options and the repurchase periods for the restricted stock. In 1999, we recorded approximately $6.1 million in additional deferred stock compensation for stock options granted in the year ended December 31, 1999, at prices subsequently deemed to be below fair market value on the date of grant. We amortized approximately $2.9 million of deferred stock compensation for the year ended December 31, 1999.

Additionally, in 1999, we granted options to purchase common stock to certain consultants in exchange for services rendered. These options are subject to variable plan accounting with fair value re-measurements at the end of each quarterly reporting period.

Results of Operations The following table sets forth financial data for the years indicated as a percentage of total revenue:

Year Ended December 31, 1997 1998 1999

Revenue			
Internet Security	2.7%	31.3%	92.2%
Ethernet	97.3	68.7	7.8
Total revenue	100.0	100.0	100.0
Cost of revenue	51.8	44.0	28.3
Gross margin	48.2	56.0	71.7
Operating expenses			
Research and development	21.3	27.3	17.3
Sales and marketing	26.4	38.2	25.4
General and administrative	6.9	10.0	8.4
Deferred stock compensation	--	0.6	13.7
Total operating expenses	54.6	76.1	64.8
Income (loss) from operations	(6.4)	(20.1)	6.9
Other income (expense), net	0.3	0.7	2.6
Income (loss) before income taxes	(6.1)	(19.4)	9.5
Benefit from (provision for) income taxes	1.1	(0.1)	(8.7)
Net income (loss)	(5.0)%	(19.5)%	0.8 %

1999 compared to 1998 Internet security revenue. We shipped our first Internet security appliance product, the SonicWALL DMZ, near the end of 1997, and in 1998 we were in the early stages of our sales and marketing efforts for this product. Revenue from sales of our security appliance products increased to $19.4 million in the year ended December 31, 1999 from $2.3 million in the year ended December 31, 1998. This revenue growth was due primarily to the introduction of our SonicWALL PRO product, expansion of our distribution channel, and increasing demand in the security appliance market.

Ethernet revenue. Revenue from our Ethernet products declined to $1.6 million in the year ended December 31, 1999 from $5.2 million in the year ended December 31, 1998. This decrease was directly related to our 1997 decision to focus our development, sales and marketing efforts on our Internet security appliance products. We stopped shipment of Ethernet products during December 1999.

Cost of revenue; gross margin. Cost of revenue includes all costs associated with the production of our products, including cost of materials, manufacturing and assembly costs paid to contract manufacturers and related overhead costs associated with our manufacturing operations personnel. Additionally, all warranty costs and any inventory provisions or write-downs are expensed as cost of revenue. Cost of revenue increased to $6.0 million in the year ended December 31, 1999 from $3.3 million in the year ended December 31, 1998, primarily as a result of increased product sales. Gross margin increased to $15.1 million, or 72% of total revenue, in the year ended December 31, 1999 from $4.2 million, or 56% of total revenue, in the year ended December 31, 1998. The increase in gross margin relates primarily to the increase in sales of higher gross margin security appliance products, and a decrease in sales of lower gross margin Ethernet products. In addition, as the volume of units shipped has increased, our cost of revenue has declined as a percentage of revenue as a result of lower

component costs due to higher purchase volumes, and lower manufacturing and overhead costs per unit related to economies of scale. Our gross margins are affected by fluctuations in manufacturing volumes, component costs and the mix of products sold. In addition, an increase in total sales to original equipment manufacturers compared to total sales to our distribution partners will result in a decrease in gross margins. We must manage each of these factors effectively for our gross margins to remain at current levels.

Research and development. Research and development expenses primarily consist of personnel costs related to engineering and technical support, contract consultants, outside testing services, amortization of acquired technology from AckFin, and equipment and supplies associated with enhancing existing products and developing new products. Research and development expenses increased to $3.6 million in the year ended December 31, 1999 from $2.1 million in the year ended December 31, 1998. Research and development spending increased during 1999 by approximately $1.0 million related to the hiring of additional personnel, amortization of acquired technology of approximately $0.8 million and increased overhead and consulting costs.

Sales and marketing. Sales and marketing expenses primarily consist of personnel costs, including commissions, costs associated with the development of our business and corporate identification, and costs related to customer support, travel, trade shows, promotional and advertising costs. Sales and marketing expenses increased to $5.3 million in the year ended December 31, 1999 from $2.9 million in the year ended December 31, 1998. This increase primarily relates to increased hiring of sales and marketing personnel, increased travel and attendance at trade shows, increases in customer support personnel and expanded sales and marketing efforts in international markets. We intend to increase sales and marketing expenses as we add personnel to support our domestic and international sales and marketing efforts.

General and administrative. General and administrative expenses primarily consist of personnel costs for administrative officers and support personnel, legal, accounting and consulting fees, and facility expenses. Our general and administrative expenses increased to $1.8 million for the year ended December 31, 1999 from $0.8 million in the year ended December 31, 1998. This increase was primarily due to increases in staffing and related personnel costs to support our growth, as well as increased professional services costs.

Deferred stock compensation. Amortization of deferred stock compensation was $2.9 million in the year ended December 31, 1999. This amortization relates to deferred compensation of $6.1 million, related to stock options granted in the year ended December 31, 1999. We are amortizing this amount over the vesting periods of the applicable options. Amortization of deferred stock compensation in the year ended December 31, 1998 was $42,000.

Other income (expense), net. Other income (expense), net consists primarily of interest income on our cash and cash equivalents, and increased to $0.5 million for the year ended December 31, 1999 from $54,000 in the year ended December 31, 1998. This increase was related primarily to higher interest earnings on cash that increased in amount from $1.1 million to $62.6 million in the comparable period.

Provision for income taxes. The provision for income taxes in the year ended December 31, 1999 was $1.8 million. The provision for income taxes in the year ended December 31, 1998 was $6,000. In both periods, the provision for income taxes is based on an estimated effective rate for each of the respective calendar years. The effective tax rate in the year ended December 31, 1999 was 37.5% before the effect of amortization of deferred compensation, a permanent, non-deductible book/tax difference. This effective rate reflects statutory federal and state tax rates net of the estimated realization of deferred tax assets. In determining this effective rate, we concluded that it was more likely than not that we would realize the full value of this deferred tax asset based upon our estimate of profitability and our assessment of tax refunds available from net loss carrybacks in the event future profitability was less than our estimates.

1998 compared to 1997 Internet security revenue. Internet security revenue increased to $2.3 million in 1998 from $0.3 million in 1997 and related primarily to a full year of shipments of our expanded SonicWALL product offerings in 1998.

Ethernet revenue. Ethernet revenue declined to $5.2 million in 1998 from $9.1 million in 1997. This decline in Ethernet revenue related to our 1997 decision to focus development, sales and marketing efforts on our Internet security appliance products. Our development, marketing and sales efforts are now entirely focused on the Internet security appliance market.

Gross margin. In 1998, gross margin was $4.2 million, or 56% of revenue, compared to $4.5 million, or 48% of revenue, in 1997. The percentage increase in gross margin from 1997 to 1998 relates primarily to the increase in sales of higher margin Internet security appliance products.

Research and development. Research and development expenses increased to $2.1 million in 1998 from $2.0 million in 1997. This increase from 1997 to 1998 relates primarily to amortization of acquired technology offset in part by a reduction in compensation paid to a founder.

Sales and marketing. Sales and marketing expenses increased to $2.9 million in 1998 from $2.5 million in 1997. These increases were primarily due to the hiring of additional sales and marketing personnel, as well as increases in travel, trade shows, promotional and advertising costs.

General and administrative. General and administrative expenses increased to $0.8 million in 1998 from $0.6 million in 1997. These increases were due mainly to the addition of administrative personnel, professional services fees and facility expenses to support the growth of our operations.

Deferred stock compensation. During 1998, we recorded deferred compensation of $48,000 in connection with stock option grants of which $42,000 was amortized in the year ended December 31, 1998. We are amortizing this amount over the vesting periods of the applicable options.

Quarterly Results of Operations The following tables set forth our unaudited quarterly results of operations, in dollars and as a percentage of total revenue, for the eight quarters ended December 31, 1999. You should read the following tables in conjunction with the financial statements and related notes contained elsewhere in this prospectus. We have prepared this unaudited information on the same basis as our audited financial statements. These tables include all adjustments, consisting only of

normal recurring adjustments, that we consider necessary for a fair presentation of our financial position and operating results for the quarters presented. You should not draw any conclusions about our future results from the results of operations for any quarter.

Three Months Ended March 31, June 30, September 30, December 31, March 31, June 30, September 30, December 31, 1998 1998 1998 1998 1999 1999 1999 1999 (in thousands)

Revenue								
Internet security.....	$ 157	$ 248	$ 519	$ 1,425	$ 2,251	$ 3,223	$ 5,203	$ 8,726
Ethernet.....	1,546	1,355	1,555	710	813	403	258	170
Total revenue.....	1,703	1,603	2,074	2,135	3,064	3,626	5,461	8,896
Cost of revenue.....	833	819	833	823	943	1,055	1,464	2,499
Gross margin.....	870	784	1,241	1,312	2,121	2,571	3,997	6,397
Operating expenses								
Research and development....	385	437	595	634	658	723	817	1,436
Sales and marketing.....	661	739	682	788	811	1,043	1,554	1,934
General and administrative..	184	125	232	212	332	362	495	572
Deferred stock compensation..	--	--	--	42	15	768	518	1,594
Total operating expenses....	1,230	1,301	1,509	1,676	1,816	2,896	3,384	5,536
Income (loss) from operations.....	(360)	(517)	(268)	(364)	305	(325)	613	861
Other income (expense), net..	9	13	14	18	41	91	73	331
Income (loss) before income taxes.....	(351)	(504)	(254)	(346)	346	(234)	686	1,192
Provision for income taxes...	--	--	--	6	135	200	452	1,045
Net income (loss).....	$ (351)	$ (504)	$ (254)	$ (352)	$ 211	$ (434)	$ 234	$ 147

As a Percentage of Revenue March 31, June 30, September 30, December 31, March 31, June 30, September 30, December 31, 1998 1998 1998 1998 1999 1999 1999 1999

Revenue								
Internet security.....	9.2%	15.5%	25.0%	66.7%	73.5%	88.9%	95.3%	98.1%
Ethernet.....	90.8	84.5	75.0	33.3	26.5	11.1	4.7	1.9
Total revenue.....	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Cost of revenue.....	48.9	51.1	40.2	38.5	30.8	29.1	26.8	28.1
Gross margin.....	51.1	48.9	59.8	61.5	69.2	70.9	73.2	71.9
Operating expenses								
Research and development....	22.6	27.3	28.7	29.7	21.5	19.9	15.0	16.2
Sales and marketing.....	38.8	46.1	32.9	36.9	26.4	28.8	28.5	21.7

General and administrative..	10.8	7.8	11.2	9.9	10.8	10.0	9.0	6.4
Deferred stock compensation..	--	--	--	2.0	0.5	21.2	9.5	17.9
Total operating expenses....	72.2	81.2	72.8	78.5	59.2	79.9	62.0	62.2
Income (loss) from operations.....	(21.1)	(32.3)	(13.0)	(17.0)	10.0	(9.0)	11.2	9.7
Other income (expense), net..	0.5	0.8	0.7	0.8	1.3	2.5	1.3	3.7
Income (loss) before income taxes.....	(20.6)	(31.5)	(12.3)	(16.2)	11.3	(6.5)	12.5	13.4
Provision for income taxes...	--	--	--	0.3	4.4	5.5	8.3	11.7
Net income (loss).....	(20.6)%	(31.5)%	(12.3)%	(16.5)%	6.9%	(12.0)%	4.2%	1.7%

Internet security revenue. Internet security revenue has increased in each of the eight quarters ended December 31, 1999, due to increasing market acceptance of our security appliance products and the expansion of our product line to include the SonicWALL SOHO in August 1998 and SonicWALL PRO in May 1999.

Ethernet revenue. Ethernet revenue remained relatively flat through the first three quarters of 1998, and decreased significantly in the fourth quarter of 1998 and the four quarters of 1999. The overall decline in Ethernet revenue relates primarily to our decision to focus our development, sales and marketing resources exclusively on the security appliance product family. We stopped shipment of Ethernet products during December 1999.

Gross margin. Our gross margin has generally increased each quarter since the quarter ended March 31, 1998. These increases have been due to the introduction of our new security appliance products, which have higher average selling prices and higher gross margins, the reduction of production costs on a per unit basis as manufacturing volumes have increased, the reduction in materials costs due to increased purchase volumes, and improved absorption of manufacturing infrastructure costs. Gross margin decreased in the quarter ended December 31, 1999 due to the increased shipments of OEM products which have lower gross margins.

Operating expenses. Our operating expenses have increased in each of the eight quarters ended December 31, 1999 to $5.5 million in the quarter ended December 31, 1999 from $1.2 million in the quarter ended March 31, 1998. These increases related primarily to development of new products, increased marketing of new products, and increased investments in our internal infrastructure to support our growth.

Liquidity and Capital Resources Since our inception, we have financed our operations through cash flows from operations, private sales of securities and, to a lesser extent, bank borrowings. During the year ended December 31, 1999, we generated $5.8 million in cash from operating activities. This increase resulted from a significant increase in Internet security revenue, offset in part by a $3.4 million increase in accounts receivable and a $1.0 million increase in prepaids and other current assets. We expect that accounts receivable will continue to increase if our revenue continues to rise and that

we will continue to increase our investment in capital assets to expand our operations. During 1998, we generated $0.4 million in cash from operating activities, compared to a $0.4 million decrease from operating activities in 1997. Investing activities related to purchases of property and equipment used cash of $0.1 million in 1998 and $0.5 million in the year ended December 31, 1999. In 1997 purchases of property and equipment were immaterial.

In February 1999, we completed a private placement of approximately $5.0 million of redeemable Series A convertible preferred stock. We conducted no significant financing activities in 1997 or 1998. In November 1999, we completed our initial public offering of 4,000,000 primary shares of common stock at $14.00 per share which generated net proceeds to us of approximately $50.9 million. In connection with the initial public offering, all outstanding shares of preferred stock automatically converted into common stock.

Our principal source of liquidity as of December 31, 1999 consisted of $62.6 million in cash and cash equivalents. As of December 31, 1999 we have a credit facility with Comerica Bank of California that provides for borrowings up to the lesser of $1.0 million or 80% of eligible accounts receivable, as defined in the credit facility. Our line of credit bears interest at the bank's reference rate plus 1.75%, which equaled 10.25% at December 31, 1999 and borrowings are secured by accounts receivable, inventories, property and equipment. The credit facility may be terminated by the lender or us on thirty days prior notice. As of December 31, 1999, there were no borrowings outstanding under this credit facility.

We believe that the market risk arising from our holdings of financial instruments is not material.

We believe our existing cash balances and available line of credit will be sufficient to meet our cash requirements at least through the next twelve months. However, we may be required, or could elect, to seek additional funding prior to that time. Our future capital requirements will depend on many factors, including our rate of revenue growth, the timing and extent of spending to support product development efforts and expansion of sales and marketing, the timing of introductions of new products and enhancements to existing products, and market acceptance of our products. We cannot assure you that additional equity or debt financing will be available on acceptable terms or at all. As of the date of this offering, our sources of liquidity beyond twelve months, in management's opinion, will be our then current cash balances, funds from operations and whatever long-term credit facilities we can arrange. We have no other agreements or arrangements with third parties to provide us with sources of liquidity and capital resources beyond twelve months.

We do not have any other debt, long-term obligations or long-term capital commitments.

Year 2000 Readiness Disclosure We believe that we have successfully rendered our products, internal management and other administrative systems and external information systems year 2000 compliant. In addition, we have surveyed the vendors of the third- party technologies we incorporate into our products and services and applied updates or arrangements to correct potential year 2000 compliance problems. Since January 1, 2000, we have experienced no disruptions in our business operations as a

result of year 2000 compliance problems or otherwise, and we have received no reports of any year 2000 compliance problems with our products and services. To date, the total cost of our efforts to address year 2000 compliance has not been material.

Nonetheless, some problems related to the year 2000 risks may not appear until several months after January 1, 2000. Year 2000 issues could include problems with our own products and services or with third-party products or technology that we use or with which our products exchange data. Any problems that are not identified and corrected successfully and completely could adversely affect our business.

Disclosures About Market Risk Our exposure to market risk for changes in interest rates relates primarily to our cash and cash equivalents. We do not use derivative financial instruments in our investment portfolio. As stated in our investment policy, we are averse to principal loss and ensure the safety and preservation of our invested funds by limiting default and market risk. We mitigate default risk by investing in only investment-grade instruments.

We invoice all of our foreign customers from the United States in U.S. dollars and all revenue is collected in U.S. dollars. In addition, we do not have any cash balances denominated in foreign currencies. As a result, we do not have significant market risks associated with foreign currencies or related to sales and collections.

Business

Overview

SonicWALL, Inc. designs, develops, manufactures and sells Internet security infrastructure products designed to provide secure Internet access to our broadband customers. Broadband access, such as digital subscriber line, or DSL, and cable modems, allows users to connect to the Internet at speeds significantly greater than analog modems. We believe our security appliances provide high performance, robust, reliable, easy-to-use and affordable Internet security. We also sell content filtering services on an annual subscription basis. We sell our products to customers in the small to medium enterprise, branch office, telecommuter and education markets. As of December 31, 1999, we had sold more than 35,000 of our Internet security appliances worldwide.

Our SonicWALL product line provides our customers with a comprehensive integrated security solution that includes firewall, content filtering, and virtual private network functionality so users can enjoy affordable, secure Internet communications. SonicWALL products deliver a plug-and-play appliance solution that we believe is easy to install and use and minimizes the purchase, installation and maintenance costs of Internet security. With suggested retail prices ranging from $495 to $2,995, our products are designed to enable customers to reduce purchase costs and avoid hiring costly IT personnel for Internet security. By using an embedded single purpose operating system and a hardware design without moving parts, our SonicWALL products are designed to maximize reliability and

uptime. The SonicWALL product line can be used in networks ranging in size from 1 to 1,000 users and is fully compatible with more expensive enterprise security solutions offered by, among others, Check Point Software and Cisco Systems.

Recent Developments

On February 22, 2000, we announced a strategic partnership with myCIO.com, a Network Associates, Inc. business, to protect our customers worldwide against Internet transmitted computer viruses. SonicWALL products will ensure that users are protected against the threat of viruses by embedding anti-virus enforcement policies developed around myCIO.com's VirusScan ASaP anti-virus application service into our Internet security appliances. We intend to sell this integrated, managed anti-virus solution to our customers worldwide.

On December 21, 1999, we announced that Healtheon/WebMD Corporation had selected SonicWALL to provide Internet security within Healtheon/WebMD's services, which are being deployed to serve the healthcare industry. Healtheon/WebMD connects physicians and other healthcare providers to the Internet, allowing them to communicate with hospitals, payers, physician groups and consumers. Due to the highly confidential nature of patient information, healthcare providers need to ensure the security of patient data.

On December 7, 1999, Concentric Network Corporation announced its plans to resell our SonicWALL SOHO product. Concentric Network provides DSL access, Web hosting and electronic commerce services for small and medium sized enterprises.

Industry Background

Growth of Internet Usage By Small to Medium Enterprise, Branch Office, Telecommuter, and Education Markets Businesses and consumers are increasingly accessing the Internet for a wide variety of uses including communications, information gathering and commerce. Because it is an affordable means of achieving global reach and brand awareness, the Internet is a particularly attractive vehicle for small and medium size businesses as they endeavor to access and share information with a large number of geographically dispersed customers, employees and business partners. For example, of the 87.4 million devices estimated by International Data Corporation, or IDC, a market research organization, to have Internet access in 1998, approximately 60% were used by small businesses and home offices. IDC estimates that the proportion of small businesses, those with less than 100 people, accessing the Internet in the United States will increase from approximately 50% in 1998 to approximately 65% by 2001, to a total of 4.7 million businesses.

Today's large business enterprise is characterized by many branch offices, mobile workers, and telecommuters, all of whom connect electronically to the corporate office and each other. Because of the confidential nature of business data, these connections must be secure. Virtual private networks provide secure Internet connections between the business enterprise and dispersed employees and business partners. Communicating using virtual private networks offers significant cost savings over alternative solutions such as private leased line or frame relay networks. TeleChoice, a market researcher, estimates that virtual private networks can cut telecommunication costs by as much as 90%

over private leased line networks, and for this reason, their use is expected to grow rapidly. Infonetics Research projects worldwide expenditures on virtual private networks will grow by 100% per year through 2001, when they are expected to reach $11.9 billion.

The Internet also has become a vital tool of information access and communication for schools and libraries. According to the National Center for Education Statistics, there were over 96,000 K-12 public schools and libraries in the United States in 1998, of which 89% of schools and 35% of libraries were connected to the Internet. The growth in Internet connectivity in this market, combined with the proliferation of objectionable Web sites, has created a need for Internet security products that include content filtering capabilities.

Increasing Demand for Broadband Access Technologies Many small to medium enterprises and branch offices have addressed the need for Internet access by installing a single computer with a dial-up connection that is shared throughout the office, or by installing a dedicated network data connection at a significantly greater expense, such as a T-1 line. Recently, new high-speed technologies have emerged that can better satisfy the bandwidth requirements of small to medium enterprises at a fraction of the cost of traditional solutions. These technologies include DSL and cable modems, which provide access speeds of up to 100 times faster than traditional 28.8 kbps analog modems. In addition, new generations of Internet-based applications, such as business to business e-commerce, sales force automation and enterprise resource planning, or ERP, continue to emerge that require higher bandwidth than is available through dial-up solutions. As DSL and cable services have become more affordable and widely available, small to medium enterprises, branch offices, and telecommuters are increasingly deploying these technologies as their Internet access solution. IDC estimates that in the United States, the number of small businesses using high-speed access is expected to expand from 380,000 in 1998 to 3.3 million in 2003.

Importance of Internet Security Secure access to the Internet is a growing concern for most Internet users. Because broadband technologies, including DSL and cable, are always connected to the Internet, they present greater security issues than dial-up connections and increase the risk that proprietary data or other sensitive information might be compromised. These types of Internet connections present ongoing security issues for small to medium enterprises, branch offices, and telecommuters and increase the risk that computer hackers, disgruntled employees, contractors or competitors might successfully access proprietary data or other sensitive information. In addition, as more Web-enabled, mission critical business applications are developed and offered by vendors such as Oracle Corp., PeopleSoft Inc., Siebel Systems Inc., and SAP AG, the amount of sensitive data transmitted over the Internet has increased and led organizations to look for high performance, robust solutions to address these security needs.

Many Internet users also seek solutions that enable control over access to undesirable content, either to avoid potential legal liability or to eliminate distracting activity by employees or other users. In addition, public attention has recently focused on the advantages of using filtering software to screen offensive material for children accessing the Internet at libraries, schools, and other public institutions.

The market for Internet security products includes a variety of applications to address these issues, such as firewall, content filtering, Internet Protocol, address management and VPN. According to IDC, the market for Internet security products increased over 45% in 1998 to $3.2 billion and is expected to grow at a compounded annual growth rate of 21% to $8.3 billion by 2003. IDC also estimates that in the market for firewall appliances priced at less than $10,000, revenues will grow at an expected compounded annual growth rate of 88% over the same period.

Lack of a Cost Effective, High Performance Security Solution for the Broadband Access Market Although the need for Internet security products is widespread, security vendors generally have focused on providing solutions for large enterprises with highly complex needs and extensive information technology support organizations. These solutions have typically involved expensive enterprise firewall software that runs on a dedicated server or personal computer and requires extensive support, constant monitoring and regular updates by IT personnel to maintain its effectiveness. The expense and complexity of these solutions, which often require additional products to incorporate VPN capabilities, IP address management or content filtering, are impractical for the majority of small to medium enterprises due to their more limited resources. While there are suppliers of low cost Internet routers which may provide limited Internet security functionality, we believe these products are difficult to install and configure and provide relatively low performance.

The SonicWALL Solution SonicWALL, Inc. provides Internet security products designed for broadband access customers in the small to medium enterprise, branch office, telecommuter and education markets. We believe our security appliances provide high performance, robust, reliable, easy-to-use and affordable Internet security. SonicWALL products enable our customers to securely utilize Internet applications and services as an integral part of their business. As of December 31, 1999, we had sold more than 35,000 of our Internet security appliances worldwide. The SonicWALL product line provides our customers with the following key benefits:

. High Performance, Robust Security. The SonicWALL product family provides a comprehensive integrated security solution that includes firewall, content filtering and VPN functionality. Our firewall security protects private networks against Internet-based theft, destruction, or modification of data, and automatically notifies customers if their network is under attack. SonicWALL has been awarded the internationally recognized International Computer Security Association, or ICSA, Firewall Certification, the same certification awarded to significantly more expensive products sold by Check Point Software and Cisco Systems. Our VPN capabilities enable affordable, secure communications among remote offices, mobile employees and business partners over the Internet. Our content filtering enables businesses, schools and libraries to restrict access to objectionable or inappropriate Web sites.

. Ease of Installation and Use. The SonicWALL product family delivers a plug-and-play appliance designed for easy installation and use. Installation involves simply connecting SonicWALL between the private network and the broadband Internet access device. SonicWALL is easily configured and managed through a Web browser-based interface. No reconfiguration of any PC application is required. Our products are pre- configured to interface with all major Internet access technologies, including

cable, DSL, ISDN, Frame Relay, and T-1. In addition, SonicWALL's AutoUpdate capability automatically notifies all registered customers via e-mail when bug fixes or new features and products that have been purchased are available for download from our Web site.

. Low Total Cost of Ownership. The SonicWALL product design minimizes the purchase, installation and maintenance costs of Internet security. The suggested retail prices of our products range from $495 to $2,995, versus enterprise firewall products which range in price from approximately $5,000 to more than $15,000. Our affordable, easy-to-manage Internet security appliances also enable customers to avoid the expense of hiring costly information technology personnel who may otherwise be required to implement and maintain an effective Internet security solution.

. Reliability. The SonicWALL product design maximizes reliability and uptime. Our product uses an embedded single purpose operating system and a hardware design which contains no moving parts. Most competitors' products consist of software installed on general purpose host computers which use the Windows NT or UNIX operating systems. General purpose operating systems such as these are designed to run multiple applications, creating an environment in which random system crashes are commonplace. Moreover, since general purpose computers contain many moving parts, such as hard disk drives, floppy drives, fans and switching power supplies, they are more prone to hardware failures over time. These software and hardware failures can compromise Internet security.

. Scalability and Compatibility. SonicWALL products are designed to provide comprehensive Internet security for networks ranging in size from 1 to 1,000 users. Our products consist of three separate models designed to serve the specific security needs of our target markets. Our products vary with respect to the number of supported users, the number of ports and feature options such as VPN or content filtering. In addition to serving the security needs of the small to medium enterprise market, SonicWALL products are a fully compatible, perimeter security solution for large, distributed enterprises and their branch offices and telecommuters. Our products are designed to interoperate with enterprise security products offered by, among others, Check Point Software and Cisco Systems.

Strategy

Our goal is to extend our leadership position and become the industry standard Internet security solution for broadband access users in our target markets--the small to medium enterprise, branch office, telecommuter, and education markets. Key elements of our strategy include:

. Extend Our Leadership Position in Target Markets. We believe that we have established a market leadership position as a provider of Internet security products designed for our target markets by offering robust, reliable, easy-to-use products at attractive prices. We intend to continue to focus our product development efforts, distribution strategies, and marketing programs to satisfy the growing needs of these markets. We believe that the current Internet security offerings of most vendors are relatively expensive, technically complex, and generally unable to satisfy these target markets.

. Continue to Develop New Products and Reduce Manufacturing Costs. We intend to use our product design and development expertise to expand our product offerings and reduce our manufacturing costs. We believe that these new product offerings, other new products and associated cost reductions

will strengthen our market position and assist us in penetrating new markets. We are currently focusing our new product development efforts in the following areas:

- New services such as virus scanning, bandwidth management, e-mail spam filtering, public key infrastructure and intrusion detection.

- Management applications such as global console management and event monitoring to allow one network administrator or service provider to configure, manage and monitor hundreds of SonicWALL units simultaneously and remotely from one management console.

- New hardware products including new versions of SonicWALL appliances to meet the varying price and performance requirements of our customers and add-in modules to allow accelerated VPN performance for those customers who need to communicate securely with branch offices and telecommuters over the Internet.

- ASIC Design: we are working to achieve a higher level of Application Specific Integrated Circuit, or ASIC, design and integration to reduce product costs and increase product performance.

. Strengthen the SonicWALL Brand. We believe that strong brand recognition in our target markets is important to our long term success. We intend to continue to strengthen our SonicWALL brand name through industry trade shows, our Web site, advertising, direct mailings to both our resellers and our end users, and public relations. Our reputation as a reliable, high performance, easy-to-use and affordable Internet security vendor contributes to our resellers' sales efforts.

. Expand Our Indirect Channel. Our target markets are generally served by a two-tier distribution channel. We have successfully penetrated these markets with over 1,500 value added resellers, systems integrators, and distributors, who sell our products in over thirty countries, including large distributors such as Ingram Micro and Tech Data. In the fourth quarter of 1999 we established reseller relationships with Concentric Network, Healtheon/WebMD and Westcon. We intend to continue to build and expand our base of indirect channel relationships through additional marketing programs, hiring additional marketing staff, and increased advertising.

. Develop Strategic Original Equipment Manufacturer Relationships. By entering into original equipment manufacturer arrangements to sell our products, we intend to build upon the brand awareness and worldwide channels of major networking and telecommunications equipment suppliers to further penetrate our target markets. We presently have original equipment manufacturer agreements with the following three companies: Ramp Networks, a manufacturer of shared Internet access devices for small offices, Com21, a supplier of cable modems, and 3COM Corporation, a provider of diversified networking products. The terms of our agreements with these customers are variable but none of such purchasers is currently required to purchase a specified amount of our products or technology. Our 3COM agreement expires July 2002, with automatic renewal for successive one year periods subject to either party's election to terminate on six months prior notice. Our Com21 agreement terminates in January 2001, with automatic renewal for successive one year periods, subject to either party's cancellation upon not less than thirty days prior notice. Our agreement with Ramp Networks has been renewed through January 2001, and is automatically

renewable for successive one year terms unless either party elects to terminate upon thirty days prior notice. Com21 is licensed to incorporate our technology in its products. Ramp Networks sells our products under its own name, as does 3COM Corporation. We manufacture the products which Ramp Networks and 3COM Corporation purchase from us for resale through their own distribution channels. In the year ended December 31, 1999, revenue from Com21, Ramp Networks and 3COM constituted approximately 12% of total revenue. We are pursuing relationships with other broadband access equipment providers with the intent of further penetrating our target markets.

. Build Upon Our Installed Base. We continue to develop new subscription services and add on products to generate additional revenue from our installed base. For example, we recently announced a strategic partnership with myCIO.com, a Network Associates business, to sell an integrated managed anti-virus solution to our customers. We have dedicated marketing personnel and programs that focus on selling these products and services to our existing base of customers. We have actively sought registration of our customers and we have experienced a registration rate of nearly 65% to date. This has enabled us to pursue cost effective, targeted marketing campaigns to our installed base of registered users. Our AutoUpdate feature encourages our customers to register their product by offering periodic notifications via email of new security threats, bug fixes and marketing information on new features and products. Each SonicWALL model is configured to allow end users to easily and conveniently download new features and products that have been purchased, either through our resellers or our Web site. Such sales could include additional functionality such as virtual private networking or additional recurring revenue opportunities such as content filtering services.

Products and Services We believe the SonicWALL product line provides cost effective and high performance Internet security solutions for the small and medium size enterprise, branch office, telecommuter, and education markets. We design our products to address the specific needs of customers within each of these market segments. Our products vary with respect to the number of supported users, the number of ports, product features, processor speed and scalability. All of our products provide firewall security and are capable of delivering features such as content filtering and virtual private networking in a single, integrated security appliance that is managed through an intuitive and easy- to-use Web browser-based interface.

[DESCRIPTION OF GRAPHICS: Diagram showing WebServer, E-Commerce Server and three PC's connected to a SonicWALL DMZ or PRO security appliance on the left side, which is connected to a modem router in the middle of the graphic which is connected to an oval on the right side of the graphic with the words "THE INTERNET" in the center of the oval.]

SonicWALL SOHO. SonicWALL SOHO has two 10Base-T Ethernet ports and is designed to provide security for smaller networks using broadband connections to the Internet such as cable and DSL. SonicWALL SOHO provides protection against unauthorized access to the private network, filters out objectionable Web sites, and manages the complexity of IP addressing. It also has a virtual private networking option to give telecommuters and small remote offices affordable and secure connectivity to the main office. SonicWALL SOHO supports 10 or 50 user connections.

SonicWALL DMZ. SonicWALL DMZ has three 10Base-T Ethernet ports and is designed to meet the Internet security needs of small and medium size networks in business and education. SonicWALL security code operates between each port's connections to prevent unauthorized communication, regardless of its source. In addition to the features provided by SonicWALL, SonicWALL DMZ provides a third port, a DMZ, or De-Militarized Zone. With the additional DMZ port, public Web and e-commerce servers can both be accessed from the Internet without exposing the private network to Internet based attacks. SonicWALL DMZ protects the computers on the LAN port and the public servers on the DMZ port from Internet-based attacks. SonicWALL DMZ supports unlimited users.

SonicWALL PRO. SonicWALL PRO has three 10/100Base-T Fast Ethernet ports and is designed to meet the Internet security needs of medium and large size businesses and branch offices. SonicWALL PRO supports all of the features found in other SonicWALL models, and offers a more powerful and scalable platform for larger networks requiring faster connections, high performance virtual private networking and future expansion options. SonicWALL PRO supports unlimited users.

The following table provides a summary of SonicWALL models:

SonicWALL SOHO SonicWALL DMZ SonicWALL PRO

Target Markets	. Telecommuter . Small to medium size business	. Small to medium size business . Education	. Medium to large size business . Branch offices
Virtual Private Networking	Optional	Optional	Standard
Number of Users	10 or 50	Unlimited	Unlimited
LAN and WAN Ports	X	X	X
DMZ Port for Public Servers		X	X
Expandable Memory and PCI Expansion Slot			X
Type of Ports	10Base-T (Ethernet) Motorola	10Base-T (Ethernet) Motorola	10/100Base-T (Fast Ethernet) Intel
Microprocessor	33MHz MC 68360	33MHz MC 68360	233MHz StrongARM
List Price	$495-$995	$1,795	$2,995

End users may also purchase various product upgrades and subscriptions, such as updated content filter lists, virtual private networking, number of user upgrades, and extended warranties and premium support contracts.

Upgrade or Subscription Description List Price

Virtual Private Networking Upgrade	Activates optional virtual private networking feature for SonicWALL SOHO and SonicWALL DMZ models	$495-$695
Number of Users Upgrade	Adds support for additional users for user-limited models (SonicWALL SOHO/10 and SonicWALL SOHO/50)	$650-$1,300
Content Filter Subscription	Annual subscription to a continuously updated filter list of Internet sites that contain objectionable content	$175-$695 / year
Extended Warranty and	Annual extended warranty on SonicWALL	

Premium Support	hardware and premium technical support contract	$80-$675 / year

[DESCRIPTION OF GRAPHICS: Diagram showing the Internet as an oval symbol and lines connecting from the Internet through depiction of SonicWALL products to graphic for SME (office building), telecommuter (house), school or library (school), branch office (office building), corporate headquarters (office building), and mobile worker (laptop computer).]

The SonicWALL product line shares a common set of Internet security features that have been tailored to meet the needs of our target markets:

Firewall Security. Our firewall security protects private networks against Internet-based theft, destruction, or modification of data, and automatically notifies customers if their networks are under attack. SonicWALL has been awarded the internationally recognized ICSA Firewall Certification, the same certification awarded to significantly more expensive products sold by Check Point Software and Cisco Systems. In addition, SonicWALL is pre-configured to automatically detect and thwart Denial of Service attacks such as Ping of Death, SYN Flood, LAND Attack, and IP Spoofing.

Virtual Private Networking. Our virtual private networking capabilities enable affordable and secure communications over the Internet between branch offices, telecommuters, mobile workers and business partners. SonicWALL virtual private networking uses industry-standard data encryption algorithms and interoperates with other virtual private networking products such as Check Point Software's Firewall-1.

Content Filtering. Our content filtering feature enables businesses, families, schools and libraries to control access to objectionable or inappropriate Web sites. SonicWALL can filter Internet content by URL or keyword. We offer a content filter subscription service that provides a list of objectionable Web sites that is automatically updated on a weekly basis.

IP Address Management. SonicWALL includes Network Address Translation, or NAT, which allows a customer to connect multiple users on their private network to the Internet using a single public IP address. SonicWALL also includes Dynamic Host Configuration Protocol, or DHCP, Client and Server capabilities. DHCP Client allows SonicWALL to automatically acquire its IP address settings from the Internet Service Provider, or ISP. DHCP Server allows computers on the private network to automatically acquire IP address settings from SonicWALL, simplifying client PC configuration.

AutoUpdate. Our AutoUpdate feature automatically notifies all registered customers via e-mail when bug fixes or new products that have been purchased are available for download from our Web site. With AutoUpdate, we give our customers an easy-to-use method to address rapidly evolving Internet security issues.

Logging and Reporting. SonicWALL maintains an event log of potential security concerns which can be viewed with a Web browser or automatically sent to any e-mail address on a periodic basis. SonicWALL notifies the administrator of high-priority security issues, such as an attack on a server, by immediately

sending an alert message to a priority e-mail account such as an e-mail pager. SonicWALL also provides pre-defined reports that show different views of Internet usage, such as the most commonly accessed Web sites.

Web Browser-Based Management. SonicWALL is easily and securely configured and managed through a Web browser-based interface. The SonicWALL interface effectively insulates the user from the underlying complexity of Internet security, while providing enough flexibility to meet the diverse needs of our customers.

Case Studies

SonicWALL customers range from home users with Internet cable or DSL access to global companies with numerous branch offices and telecommuters. The following case studies illustrate how our customers are using our products and services.

Small to Medium Size Enterprise The Charlotte Hornets professional basketball franchise depends on the Internet for league communications, marketing and public relations. The Hornets' office uses an always-on broadband Internet connection that requires Internet security to protect confidential franchise and league information. A SonicWALL DMZ is used to provide firewall protection for all computers on the private network. Four Web sites and other servers are hosted on the DMZ port, where they are accessible from the Internet, but protected from Internet attacks.

Branch Office

Pixar, an Academy Award-winning computer animation studio with technical, creative and production capabilities, develops well-known computer-animated feature films. In addition to its headquarters in Richmond, California, Pixar has six branch offices with always-on broadband Internet connections that require firewall security to protect the computers on their private networks and virtual private networking connectivity to allow secure communications with headquarters. A SonicWALL unit at each branch office provides Pixar with firewall security. With the SonicWALL virtual private networking upgrade at each branch office and Check Point Software's Firewall-1 at headquarters, Pixar has created a secure distributed network that allows employees in different offices to collaborate on projects and to disseminate confidential information securely over the Internet throughout the enterprise.

Telecommuter

Mr. Marshall subscribes to Excite@Home's high speed Internet cable access service in Fremont, California. Recently, Mr. Marshall's employer installed a SonicWALL PRO at the office to allow telecommuters to use virtual private networking for secure access to sensitive resources on the company's private network, such as file servers and databases. Mr. Marshall installed a SonicWALL SOHO/10 with the virtual private networking upgrade at home to create a virtual private networking connection to his company's private network, allowing him to securely collaborate on projects and distribute private information with other employees over the Internet.

Education

The Santa Clara County California Library system offers free Internet access to all members of the community from any of its computer terminals located throughout nine community libraries. Responding to community concerns, the Library's governing body mandated the use of content filtering to restrict access to sexually explicit Internet sites in the children's rooms of all Library branches. Following a six-week study during which multiple security and filtering products were analyzed, the Library installed a SonicWALL DMZ with our content filtering subscription service to restrict access to objectionable Web sites. SonicWALL DMZ is configured to allow adult patrons to decide between filtered or unfiltered access while the computers in the children's rooms are always filtered. In addition to content filtering, SonicWALL DMZ provides firewall security for all of the Library's computers.

Sales and Marketing

Our sales and marketing efforts focus on successfully penetrating the small to medium enterprise, branch office, telecommuter, and education markets. Our marketing programs promote SonicWALL brand awareness and reputation as a reliable, high performance, easy-to-use, and affordable Internet security appliance. We try to strengthen our brand through a variety of marketing programs which include on-going public relations, our Web site, advertising, direct mail, industry and regional trade shows and seminars. We intend to rapidly expand our indirect channel relationships through additional marketing programs, additional marketing staff and increased advertising.

We believe that SonicWALL products are ideally suited for the indirect channel where it is not economically efficient for us to sell directly to the end users of our products. We primarily market and sell our products in this indirect channel through a two-tiered distribution structure consisting of distributors and resellers, both in the United States and over 30 countries. Distributors accounted for approximately 76% of our total revenue for the year ended December 31, 1999. Resellers, which include systems integrators, ISPs, dealers, mail order catalogs and online catalogs, generally purchase our products from our distributors and then sell our products to end-users in our target markets. Except for our Sonic Platinum level resellers described below, we do not have purchase agreements with or sell directly to our resellers. Our distributor and reseller agreements are non-exclusive.

We divide our sales organization regionally into three areas: the United States and Canada; the Pacific Rim and Latin America; and Europe, the Middle East and Africa. Regional sales representatives manage our relationships with our network of distributors, value added resellers and customers, help our value added reseller network sell and support key customer accounts, and act as a liaison between our value added reseller network and our marketing organization. The regional sales representative's primary responsibility is to help the indirect channel succeed and grow within the territory. We also have an internal sales staff that supports the indirect channel, and a dedicated business development organization whose primary responsibilities are identifying, promoting, and managing strategic relationships to sell our products with ISPs, industry leaders, and original equipment manufacturers as well as to obtain technology for incorporation in our product line.

Domestic Channel. In the United States, the primary distributors of our products to resellers are Ingram Micro and Tech Data. Ingram Micro accounted for 34% of our revenue in 1998 and 1999. Tech Data began distributing our Internet security products in February 1999, and in the year ended December 31, 1999, accounted for approximately 12% of total revenue.

Domestic resellers receive various benefits and product discounts depending on the level of purchases that the reseller commits to or achieves. The basic program is the Sonic Reseller level which offers access to privileged information and sales and marketing materials. Next we offer a Sonic Silver level, which extends those benefits by adding access to an expanded set of sales and marketing tools, as well as priority technical support. The top level is Sonic Gold, where additional benefits such as sales leads and market development funds are available. Sonic Reseller, Silver, and Gold resellers all source our products through a distributor. We also have a Sonic Platinum level program for selected resellers which includes sales leads, access to additional discounted demonstration units and market development funds. We sell directly to these Platinum level resellers.

International Channel. We believe there is a strong international market for our products. International sales represented 32% of our revenue in 1998 and approximately 34% of revenue in 1999. Sales to Japan accounted for 11% of total revenue in the year ended December 31, 1999.

We direct all of our international resellers to the appropriate distributor in each territory. We support our international distributors by offering customizable marketing materials, sales tools, leads, co-operative marketing funds, joint advertising, discounted demonstration units, and training. We also participate in regional press tours, trade shows, and seminars. Additional key international distributors include Access Networks in Switzerland, Tekdata Distribution in England, DataWorld in Hong Kong and Allasso in England.

Original Equipment Manufacturer Channel. We enter into select original equipment manufacturer relationships in order to take advantage of the channels of well established companies that sell into our target markets. We believe these channels expand our overall market while having a minor impact on our own indirect channel sales. We currently have agreements to sell our products or services through the following original equipment manufacturers: Com21, a supplier of cable modems, Ramp Networks, a provider of networking equipment to small businesses, and 3COM Corporation. The terms of our agreements with these customers are variable. Com21 is licensed to incorporate our technology in its cable modem products. Ramp Networks sells our products under its own name, as does 3COM Corporation. We manufacture the products which Ramp Networks and 3COM Corporation purchase from us for resale through their own distribution channels. In the year ended December 31, 1999, our original equipment manufacturer revenue accounted for approximately 12% of total revenue.

Customer Service and Technical Support We offer our customers a comprehensive range of support programs through a customer service and technical support organization which provides product maintenance and technical support services on a worldwide basis. Our technical support staff is located in Santa Clara, California. In addition to standard support, we offer premium support services which an end user customer located in the United States can purchase from us or our channel partners.

Standard Support. Included during the warranty period, standard support is a unique Web-based technical support mechanism whereby distributors, channel partners, and end users can use our extensive on-line technical support resource database. If the resource database does not answer a question, the user can immediately enter a query or "trouble ticket" on-line and our customer service organization will then generate a response via phone, fax, or e-mail.

Premium Support. Available for purchase only in the continental United States, our annual subscription-based Premium Support program offers extended benefits to the Standard Support offering. Premium Support benefits include:

.expedited response time;

.access to a dedicated toll-free support telephone number;

.overnight replacement of defective units; and .free shipping for units which we authorize for return.

Our products include a standard one-year warranty, which can be extended at additional cost. The warranty provides access to our standard technical support services along with repair or replacement guarantees for units with product defects.

Customers

We sell over 98% of our products through distributors and original equipment manufacturers. As of December 31, 1999, we had sold more than 35,000 Internet security appliances. The following lists our top five international and domestic distributors based on revenues in the year ended December 31, 1999, and all of our current original equipment manufacturers. The top five domestic distributors each represent between 1% and 34% of our total revenue. The top five international distributors each represent between 1% and 9% of our total revenue.

Top 5 Domestic Distributors	Top 5 International Distributors	Original Equipment Manufacturers
.Arcom	.Access Networks (Switzerland)	.3COM Corp.
.Ingram Micro	.Allasso (England)	.Com21
.Sound Business Systems	.Connect AS (Norway)	.Ramp Networks
.Tech Data	.Sumitomo Metal Systems (Japan)	
.Westcon	.Tekdata Ltd (England)	

End Users

Although we do not sell directly to end users, approximately 65% of the products we have sold to date have been registered for use with us by our end users in our target markets. The following is a representative list of end users in each of our target markets who have deployed one or more SonicWALL products. These include the small to medium enterprise, the branch offices of large corporations, telecommuter, and the education and public institution markets.

Small to Medium Branch Offices Telecommuter Education and Enterprises .American Express Public Institutions . Compaq Computer Corporation .BBDO Seidman .Bank of Nova Scotia . Lucent Technologies .Becks Beer .Centurion/Bank of. Microsoft Corporation .Albany County .Charlotte HornetsIreland . NEC School District .Fila Sports . Commercial Bank of .City of Santa San Francisco

Cruz . PricewaterhouseCoopers LLP .Pixar . Sun Microsystems .Wells Fargo . Comision Federal de Electricidad .Duke University .Johns Hopkins University . Santa Clara County California Library Technology We have designed our SonicWALL products using a unique combination of proprietary hardware and software that delivers comprehensive Internet security with what we believe are exceptional ease-of-use and industry-leading price/performance.

The SonicWALL product line currently has two base hardware configurations:

.SonicWALL SOHO and SonicWALL DMZ. These SonicWALL products use the 33MHz Motorola 68360 microprocessor. Both products have two 10 megabits per second (Mbps) Ethernet ports. A LAN port connects the SonicWALL to the user's internal, private network. A Wide Area Network, or WAN, port connects to the external, public network. The SonicWALL DMZ has a third 10 Mbps Ethernet port (DMZ) which connects to public servers that are separated from both the public and private networks but still protected from security breaches.

.SonicWALL PRO. The SonicWALL PRO product uses Intel's 233MHz StrongARM 110 microprocessor, and has three 10/100 Mbps Fast Ethernet ports. These three ports function just like the SonicWALL DMZ. For feature expansion, the SonicWALL PRO has an internal Peripheral Component Interconnect, or PCI, interface, upgradeable RAM, and flash memory.

The SonicWALL product line consists of the following core modules:

.Firewall. The core technology is the stateful packet inspection firewall software. Stateful packet inspection is generally accepted as the most advanced and secure method of implementing an Internet firewall. It examines all layers of the packet (from the physical layer up to application layer) and determines whether to accept or reject the requested communication based on state information derived from previous communications and the applications in use. Stateful packet inspection dynamically adjusts based on the changing state of the communication running across the firewall and is invisible to users on the protected network. It therefore requires no client PC configuration. Our SonicWALL firewall protects against a known set of security threats.

.Content Filter. The SonicWALL Internet content filter blocks objectionable content using a list of forbidden URLs and keywords. We license Microsystems Software's CyberNOT list of URLs and adapt it for our products. Each SonicWALL appliance can automatically download an updated URL list weekly to keep pace with the dynamic nature of Internet content.

.IP Address Management. We have developed tools to hide the complexity of IP addressing. NAT allows networks to share a small number of valid public IP addresses with an equal or larger number of client computers on the LAN. This is a common challenge in new broadband-connected networks. Our DHCP Server and Client tools allow both the firewall and the client computers behind it to obtain their respective IP addresses dynamically from a server and thereby eliminate the need for manual configuration.

.Virtual Private Networking. We developed virtual private networking support for the SonicWALL products to provide a means for our customers to use the Internet for secure communication between LANs, and from remote clients to LANs. SonicWALL virtual private networking complies with the

Internet Protocol Security (IPSec) standard and supports three data encryption methods: 56 bit Data Encryption Standard (DES); 168 bit Data Encryption Standard (Triple-DES); and 56 bit ARCFour (ARC4). By building our virtual private networking technology on industry standards--IPSec, DES and Triple-DES--we have been able to establish virtual private networking interoperability with other leading virtual private networking solutions such as Check Point Software's FW-1.

.Web Browser-Based Management Interface. We believe our products have an intuitive and easy-to-use Web-based management interface for rapid installation, configuration and maintenance, without the need for a dedicated information technology staff to install and maintain the solution. This interface can be easily accessed from any Web browser on the internal, private network. This interface can also be accessed remotely in a secure manner using the virtual private networking feature described above.

Research and Development We believe that our future success will depend in large part on our ability to develop new and enhanced Internet security solutions and our ability to meet the rapidly changing needs of our target customers who have broadband access to the Internet. We focus our research and development on evolving Internet security needs. In addition, we have made substantial investments in hardware and ASIC technologies which are critical to drive product cost reductions and higher performance solutions. Current activities include:

. Development of new security services including virus scanning, bandwidth management, e-mail spam filtering, public key infrastructure and intrusion detection.

. Development of a global console management and event monitoring system to allow one network administrator or service provider to configure, manage and monitor hundreds of SonicWALL units simultaneously and remotely from one management console.

. Development of new versions of the SonicWALL hardware to meet the varying price and performance requirements of our customers and add-in modules to increase VPN performance for those customers who need to communicate to branch offices and telecommuters over the Internet.

All of our research and development activities are conducted at our principal facility in Sunnyvale, California. In 1997, 1998 and 1999 we incurred expenses of $1,983,000, $2,051,000 and $3,634,000, respectively, for research and development.

Competition

The market for Internet security products is world-wide and highly competitive, and we expect competition to intensify in the future. There are few substantial barriers to entry, and additional competition from existing competitors and new market entrants will occur in the future. Current and potential competitors in our markets include, but are not limited to the following, all of whom sell world-wide or have a presence in most of the major markets for such products:

.enterprise firewall software vendors such as Check Point Software and Axent Technologies;

.network equipment manufacturers such as Cisco Systems, Lucent Technologies, Nortel Networks, 3COM and Nokia;

.computer or network component manufacturers such as Intel Corporation;

.operating system software vendors such as Microsoft Corporation, Novell and Sun Microsystems;

. security appliance suppliers such as WatchGuard Technologies, Inc., and .low cost Internet router suppliers which may include limited Internet security functionality.

Most of our competitors to date have generally targeted large enterprises' security needs with firewall products that are typically very complex and expensive, ranging in price from approximately $5,000 to more than $15,000. Recently, some of our competitors have introduced products priced at less than $1,000, which may increase competitive pressure on some of our products, resulting in both lower prices and gross margins. While there are suppliers of low cost Internet routers which may provide limited Internet security functionality, we believe these products are difficult to install and configure and provide relatively low performance. At any time, any of these competitors may adapt existing products for our target markets. Many of our current or potential competitors have longer operating histories, greater name recognition, larger customer bases and significantly greater financial, technical, marketing and other resources than we do. Nothing prevents or hinders these actual or potential competitors from entering our target markets at any time. In addition, our competitors may bundle products competitive to ours with other products that they may sell to our current or potential customers. These customers may accept these bundled products rather than separately purchasing our products. If these companies were to use their greater financial, technical and marketing resources in our target markets, it could adversely affect our business.

Proprietary Rights

We currently rely on a combination of copyright and trademark laws, trade secrets, confidentiality provisions and other contractual provisions to protect our proprietary rights. Despite our efforts to protect our proprietary rights, unauthorized parties may misappropriate or infringe on our trade secrets, copyrights, trademarks, service marks and similar proprietary rights. Although we are currently investigating patent protection for some of our proprietary technology, we have not yet received any patent protection for our technology or products. Even if we obtain such patents, that does not guarantee that our patent rights are valuable, create a competitive barrier, or will be free from infringement. We face additional risk when conducting business in countries that have poorly developed or inadequately enforced intellectual property laws. In any event, competitors may independently develop similar or superior technologies or duplicate the technologies we have developed, which could substantially limit the value of our intellectual property.

U.S. Government Export Regulation Compliance Our products are subject to federal export restrictions on encryption strength. Recent federal legislation, however, has increased exportable encryption strength and allows the export of any-strength encryption to designated business sectors overseas, including U.S. subsidiaries, banks, financial institutions, insurance companies and health and medical end users. In addition, we have obtained a federal export license that allows us to export encryption technology to commercial entities in approved countries. With these expanded export rights, we may

export strong encryption to a wide range of foreign end users, subject to limitations and record-keeping requirements. To comply with these constraints, we obtain from our distributors and resellers detailed information about each foreign end-user customer that will obtain strong encryption.

Manufacturing

We currently outsource our manufacturing to one contract manufacturer, Flash Electronics, under an agreement which may be cancelled upon 180 days prior notice by either party. Outsourcing our manufacturing enables us to reduce fixed overhead and personnel costs and to provide flexibility in meeting market demand.

We design and develop all the key components of our products, including printed circuit boards and software. In addition, we determine the components that are incorporated in our products and select the appropriate suppliers of these components. Product testing and burn-in is performed by our contract manufacturers using tests that we specify.

Employees

As of December 31, 1999, we had 73 employees. Of these, 38 were employed in sales and marketing, 8 in finance and administration, 19 in research and development and 8 in operations. We are not a party to any collective bargaining agreements with our employees and we have not experienced any work stoppages. We believe we have good relations with our employees.

Facilities

Our principal administrative, marketing, sales, development and operations facility is located in Sunnyvale, California. We occupy approximately 32,256 square feet in this facility, under a lease that expires in September 2004.

Legal Proceedings

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

Management

Executive Officers, Directors and Key Employees The following table lists the executive officers, directors and key employees of SonicWALL as of December 31, 1999.

Name Age Position

Sreekanth Ravi(1)..... 33 Chairman of the Board, President and Chief Executive Officer Sudhakar Ravi(1)..... 34 Chief Technical Officer, Director Michael J. Sheridan(1).. 35 Vice President, Finance, Chief Financial Officer and Secretary Steven R. Perricone..... 39 Vice President, Sales Richard Pearce..... 39 Vice President, Business Development Warren Smith..... 49 Vice President, Engineering Fara Zarrabi..... 58 Vice President, Operations Jerrold F. Petruzzelli(2)..... 46 Director David A. Shrigley(3).... 51 Director Robert M. Williams(2)(3)..... 44 Director (1) Executive officer (2) Member of audit committee (3) Member of compensation committee We have no employment

agreements with our executive officers or key employees. All are subject to termination at will. The board of directors is elected annually by shareholders, and members of the board serve until the next annual meeting of shareholders unless they resign before such meeting. The last annual shareholders meeting was held in September 1999.

Sreekanth Ravi has served as our Chairman of the Board, President and Chief Executive Officer since co-founding SonicWALL, Inc. in February 1991. Prior to SonicWALL, Inc., Mr. Ravi was the founder and Chief Executive Officer of Generation Systems, a manufacturer of high performance video products, which he later sold to a publicly held computer products company in 1990. Mr. Ravi received a bachelor of science degree in electrical engineering from the University of Illinois, Champaign-Urbana. Sreekanth Ravi and Sudhakar Ravi are brothers.

Sudhakar Ravi has served as our Chief Technical Officer since September 1999. Prior to that time Mr. Ravi served as our Vice President, Engineering. He has served as a director since co-founding SonicWALL, Inc. in February 1991. Prior to SonicWALL, Inc., Mr. Ravi was involved in semiconductor research at Stanford University. Mr. Ravi received a bachelor of science degree from the University of Illinois, Champaign-Urbana and a masters of science degree in computer science from Stanford University. Sudhakar Ravi and Sreekanth Ravi are brothers.

Michael J. Sheridan has served as our Chief Financial Officer since joining SonicWALL, Inc. in May 1999, and became Secretary in September 1999. Mr. Sheridan joined SonicWALL, Inc. from Genesys Telecommunications Laboratories, Inc., an enterprise software company in the call center automation industry, where he served as Vice President of Finance from January 1998 to May 1999, and served as Corporate Controller from November 1996 to December 1997. From August 1995 to November 1996, Mr. Sheridan was the Corporate Controller for Network Appliance, Inc., a network file server manufacturer. From 1986 to 1995, Mr. Sheridan was an audit professional with Arthur Andersen LLP, where he was involved primarily with technology clients. Mr. Sheridan received a bachelor degree in commerce from Santa Clara University and is a Certified Public Accountant.

Steven R. Perricone has served as our Vice President, Sales since joining SonicWALL, Inc. in April 1998. Mr. Perricone joined SonicWALL, Inc. from Structured Internetworks, an IP bandwidth management company, where he served as Vice President of Worldwide Sales and Support from July 1997 to April 1998. From July 1994 to June 1997, Mr. Perricone was Vice President of Worldwide Sales at Network TeleSystems, a provider of TCP/IP client and server technology for Internet access. Prior to Network TeleSystems, Mr. Perricone held various sales management positions at Emulex and Xylogics (now part of Nortel Networks Corp.). Mr. Perricone received a bachelor degree in business from California State University.

Richard Pearce, Ph.D. has served as our Vice President, Business Development since joining SonicWALL, Inc. in June 1999. Dr. Pearce joined SonicWALL, Inc. from WinNet MCS, Inc., a high-bandwidth wireless communications company where he served as Vice President of Marketing from November 1998 to June 1999. Prior to joining WinNet, Dr. Pearce was Director of Business Development for Bay Networks (a Nortel Networks Corp. company) from August 1996 to November 1998, responsible for defining and managing programs to add IP technology to Nortel's product lines.

He was also responsible for identifying and developing market opportunities enabled by the innovative mixing of Nortel products and technologies. Prior to Bay Networks' acquisition by Nortel, Dr. Pearce was responsible for developing emerging market opportunities for Bay Networks. From July 1994 to August 1996, Dr. Pearce was Senior Manager, Technology Alliances for Bay Networks. Dr. Pearce received a bachelor of science degree in applied physics & electronics and a Ph.D. in data networking from Durham University in the United Kingdom.

Warren Smith has served as our Vice President, Engineering since joining SonicWALL, Inc. in September 1999. Mr. Smith joined SonicWALL, Inc. from Concentric Network Corporation where he was Chief Information Officer and Vice President of Software Engineering from April 1996 to September 1999. Prior to Concentric Networks, Mr. Smith was the Director of Engineering for NetManage, Inc. which he joined in October 1992 and produced the Chameleon product line of PC networks applications. Prior to Netmanage, Mr. Smith held engineering positions at Sun Microsystems Inc., SEI information Technology and Sacramento Municipal Utility District. Mr. Smith received a bachelor degree in computer science from California State University, Sacramento.

Fara Zarrabi has served as our Vice President, Operations since joining SonicWALL, Inc. in July 1999. Mr. Zarrabi joined SonicWALL, Inc. from Genesys Telecommunications Laboratories, Inc., where he was Director of Operations from February 1997 to June 1999. Prior to Genesys Telecommunications, Mr. Zarrabi was the Director of Operations at Network Appliance, Inc., from February 1996 to February 1997. From May 1994 to February 1996, Mr. Zarrabi was Director of Manufacturing Operations at Radius, Inc., a manufacturer of computer graphics and video hardware. Mr. Zarrabi received a bachelor degree in electronic engineering from the University of California, Berkeley.

Jerrold F. Petruzzelli has served as a director since October 1993. From October 1993 through September 1999, Mr. Petruzzelli also was our Secretary. Mr. Petruzzelli has been a partner of Manatt, Phelps & Phillips, LLP, legal counsel to SonicWALL, Inc., since June 1999 and previously was a partner of Holtzmann Wise & Shepard, legal counsel to the Company, from January 1990 to July 1995, and a partner of Wise & Shepard LLP, legal counsel to the Company, from July 1995 to June 1999, at which time Wise & Shepard LLP merged with Manatt, Phelps & Phillips, LLP. Mr. Petruzzelli received a bachelor of arts degree from Yale University and a J.D. degree from the University of Chicago.

David A. Shrigley has been a director since July 1999. Since July 1999, Mr. Shrigley has been a venture partner of Sevin Rosen Funds, a venture capital firm. From November 1996 to April 1999, Mr. Shrigley was Executive Vice President, Sales and Services of Nortel Networks Corp., a network telecommunications company. From December 1978 to November 1996, Mr. Shrigley was an employee of Intel Corporation, a semiconductor manufacturing company, where he was last employed as Vice President, Corporate Marketing. Mr. Shrigley received a bachelor of science degree in business administration from Franklin University.

Robert M. Williams has been a director since May 1999. Since January 1998, Mr. Williams has been a general partner of Bay Partners, a venture capital firm, and an affiliate of Bay Partners SBIC II, L.P. and BaySonic Investors, LLC, shareholders of SonicWALL, Inc. From May 1993 to December 1997, Mr. Williams was Vice President, Marketing and Business Development of NetManage, Inc., a networking

software product development and sales company. Before then, Mr. Williams held various marketing positions at several companies, including Verity, Inc., an Internet text engine developer, and Ingres Corp., a developer of relational database management software. Mr. Williams received a bachelor of arts degree from Dartmouth College and a MBA from the Stanford Graduate School of Business.

Committees of the Board of Directors The compensation committee of our board of directors consists of Messrs. Shrigley and Williams. The compensation committee:

. reviews and approves the compensation and benefits for our executive officers and grants stock options under our stock option plan; and . makes recommendations to the board of directors regarding these matters.

The audit committee consists of Messrs. Petruzzelli and Williams. The audit committee:

. makes recommendations to the board of directors regarding the selection of independent auditors;

. reviews the results and scope of the audit and other services provided by our independent auditors; and . reviews and evaluates our audit and control functions.

We established these committees in August 1999.

Director Compensation We do not pay cash compensation to our directors for their services as directors or members of committees of the board of directors, but we do reimburse them for reasonable expenses they incur in attending meetings of the board of directors. Directors of SonicWALL, Inc. are eligible to participate in our stock option plans.

Director and Officer Indemnification and Liability Our articles of incorporation limit the liability of directors to the full extent permitted by California law. California law provides that a corporation's articles of incorporation may eliminate or limit the personal liability of directors for monetary damages for breach of their fiduciary duties as directors, except liability for:

. acts or omissions that involve intentional misconduct or a knowing and culpable violation of law;

. acts or omissions that a director believes to be contrary to the best interest of SonicWALL, Inc. or our shareholders or that involve the absence of good faith on the part of the director;

. any transaction from which a director derived an improper personal benefit;

. acts or omissions that show a reckless disregard for the director's duty to SonicWALL, Inc. or SonicWALL, Inc. shareholders in circumstances in which the director was aware, or should have been aware, in the ordinary course of performing a director's duties, of a risk of serious injury to SonicWALL, Inc. or our shareholders;

. acts or omissions that constitute an unexcused pattern of inattention that amounts to an abdication of the director's duty to SonicWALL, Inc. or our shareholders;

. unlawful payments of dividends or unlawful stock repurchases or redemptions, unlawful distribution of assets to shareholders or unlawful loans or guarantees to directors, officers and others; or . any transaction between a director and SonicWALL, Inc.

Our bylaws provide that we will indemnify our directors and officers to the fullest extent permitted by California law, including circumstances in which indemnification is otherwise discretionary under California law. We have entered into indemnification agreements with our directors and officers containing provisions that are in some respects broader than the specific indemnification provisions contained in the California Corporations Code. The indemnification agreements may require us:

. to indemnify our directors and officers against liabilities that may arise by reason of their status or service as directors or officers, other than liabilities arising from willful misconduct of a culpable nature;

. to advance their expenses incurred as a result of any proceeding against them as to which they could be indemnified; and . to obtain directors' and officers' insurance if available on reasonable terms.

At present, there is no pending litigation or proceeding involving any director, officer, employee or agent of ours in which indemnification would be required or permitted. We are not aware of any threatened litigation or proceeding that might result in a claim for indemnification. We believe that our charter provisions and indemnification agreements are necessary to attract and retain qualified persons as directors and officers.

The Securities and Exchange Commission has advised us that, in its opinion, any indemnification of our directors and officers for liabilities arising under the Act is against public policy as expressed in the Act and is therefore unenforceable.

Compensation Committee Interlocks and Insider Participation Our board of directors' compensation committee currently consists of Messrs. Shrigley and Williams. None of these individuals has at any time been an employee or officer of SonicWALL, Inc. Until the compensation committee was formed in August 1999, the full board of directors made all decisions regarding executive compensation. No member of our board of directors or of its compensation committee serves as a member of the board of directors or compensation committee of any entity that has one or more executive officers serving as members of its board of directors or its compensation committee.

Executive Compensation The following table provides information concerning the compensation received for services rendered to SonicWALL, Inc. in all capacities during the years ended December 31, 1999 and 1998, by our Chief Executive Officer and each of the other most highly compensated executive officers or key employees of SonicWALL, Inc. whose aggregate compensation exceeded $100,000 in fiscal 1999.

Summary Compensation Table Long-Term Compensation Awards Annual Compensation ---------- Securities Name and Principal Salary Bonus Other Annual Underlying All Other Position Year ($) ($) Compensation ($) Options (#) Compensation ($)

Sreekanth Ravi.....	1999	$240,000	$224,983	--	400,000	--
President and Chief Executive Officer	1998	$240,000	$732,345	--	--	$13,846(1)
Sudhakar Ravi.....	1999	$240,000	$232,214	--	400,000	--
Chief Technical Officer	1998	$240,000	$816,871	--	--	$13,846(1)
Steven R. Perricone.....	1999	$120,000	$246,089	--	--	--
Vice President, Sales	1998	$ 78,231	$ 23,389	--	600,000	$ 1,538(1)
Michael J. Sheridan						

(2).....	1999	$150,000	$100,000	--	300,000	--
Vice President, Finance, Chief Financial Officer and Secretary	1998	--	--	--	--	--

(1) Cash payment in lieu of vacation days (2) Hired in May 1999 Option Grants in Last Fiscal Year The following table provides information regarding stock options we granted in fiscal 1999 to named executive officers and key employees whose compensation exceeded $100,000 in fiscal 1999. The table includes the potential realizable value over the ten-year term of the options, based on assumed rates of stock appreciation of 5% and 10%, compounded annually. The assumed rates of appreciation are prescribed by the Securities and Exchange Commission for illustrative purposes only and are not intended to forecast or predict future stock prices. Any actual gains on option exercises will depend on the future performance of our stock. The year end value of realized and unexercised in- the-money options is calculated at December 31, 1999.

Option Grants in Last Fiscal Year

	Individual Grants					
					Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term	
Name	Number of Securities Underlying Options Granted (#)	Percent of Total Options Granted to Employees in Fiscal Year	Exercise Price ($/Sh)	Expiration Date	5% ($)	10% ($)
Sreekanth Ravi.....	400,000	12.3%	$8.25	8/24/04	$22,762,314	$38,199,879
Sudhakar Ravi.....	400,000	12.3%	$8.25	8/24/04	$22222,762,314	$38,199,879
Steven R. Perricone.....	--	--	--	--	--	--
Michael J. Sheridan(1)..	300,000	9.2%	$1.00	5/26/09	$19,246,735	$30,824,909

(1) Hired in May 1999 Options vest and become exercisable over four years, provided the employee remains employed at SonicWALL, Inc. In 1999, we granted options to purchase up to an aggregate of 3,259,500 shares to employees, directors and consultants. We granted all options under our stock option plans at exercise prices at the fair market value of our common stock on the date of grant, as determined in good faith by our board of directors.

The following table provides information regarding options exercised during 1999 and unexercised options held as of December 31, 1999 by our Chief Executive Officer and the other executive officers or key employees whose compensation exceeded $100,000 in fiscal 1999. The year-end value of realized and unexercised in-the-money options is calculated at December 31, 1999.

Aggregate Option Exercises Fiscal Year-End Option Values

			Number of Securities Underlying Unexercised Options at Fiscal Year-End (#)		Value of Unexercised In-the-Money Options at Fiscal Year-End ($)	
Name	Number of Shares Acquired on Exercise (#)	Value Realized ($)	Exercisable	Unexercisable	Exercisable	Unexercisable
Sreekanth Ravi.....	--	--	--	--	--	--
Sudhakar Ravi.....	--	--	--	--	--	--
Steven R. Perricone.....	20,000	$ 797,500	242,500	337,500	$9,669,688	$13,457,813
Michael J. Sheridan.....	300,000	$11,700,000	--	--	--	--

Employee Benefit Plans 1998 and 1994 Stock Option Plans The 1998 stock option plan provides for the grant of incentive stock options, as defined in Section 422 of the Internal Revenue Code, to employees and the grant of nonstatutory stock options to employees, non-employee directors and consultants. The purposes of the 1998 stock option plan are:

.to attract and retain the best available personnel;

.to provide additional incentives to our employees and consultants; and .to promote the success of our business.

The 1998 stock option plan was adopted by our board of directors in July 1998, approved by our stockholders in July 1998, and amended by the shareholders to increase the number of shares available for grant thereunder in February 1999. Unless terminated earlier by the board of directors, the 1998 stock option plan will terminate in July 2008. The 1998 stock option plan was amended by our board of directors in August 1999 to include some of the provisions provided below. These amendments were approved by our shareholders in August 1999. The number of shares reserved for issuance under the 1998 stock option plan will be subject to an automatic annual increase in the first day of 2000 through 2008 equal to the lesser of:

.2,000,000 shares;

.4% of our outstanding common stock on the last day of the immediately preceding fiscal year; or .a number of shares determined by the administrator.

The compensation committee currently administers the 1998 stock option plan. The administrator of the 1998 stock option plan determines numbers of shares subject to options, vesting schedules and exercise prices for options granted under the 1998 stock option plan.

The exercise price of incentive stock options must be at least equal to 100% of the fair market value of our common stock on the date of grant, and at least equal to 110% of the fair market value in the case of incentive stock options granted to an employee who holds, at the time the option is granted, more than 10% of the total voting power of all classes of our stock or any parent's or subsidiary's stock. Nonstatutory stock options will have an exercise price of at least 85% of the fair market value of our stock. Payment of the exercise price may be made in cash or other form of consideration approved by the administrator. The administrator determines the term of options, which may not exceed ten years, or five years in the case of an incentive stock option granted to an employee who holds, at the time the option is granted, more than 10% of the total voting power of all classes of our stock or any parent's or subsidiary's stock. No option may be transferred by the optionee other than by will or the laws of descent or distribution, provided, however, that the administrator may in its discretion provide for the transferability of nonstatutory stock options. The administrator determines when options become exercisable. Options granted under the 1998 stock option plan become exercisable at a rate not less than 20% per year. To the extent an optionee would have the right in any calendar year to exercise for the first time one or more incentive stock options for shares having an aggregate fair market value in excess of $100,000 as of the date the options were granted, the excess options will be treated as nonstatutory stock options.

Generally, in the event of a change of control of SonicWALL, Inc., outstanding options may be assumed or substituted by the successor corporation. If the successor corporation does not agree to this assumption or substitution, the options will terminate upon the closing of the transaction.

The board of directors may amend, modify or terminate the 1998 stock option plan if any amendments, modification or termination does not impair existing rights of plan participants. Additionally, shareholder approval is required for an amendment to the extent required by applicable law, regulations or rules.

Options outstanding under the 1994 stock option plan are subject to substantially the same terms as options under the 1998 stock option plan.

As of December 31, 1999:

.a total of 7,358,324 shares have been authorized for issuance under the 1994 and 1998 stock option plans;

.options to purchase an aggregate of 3,794,208 shares of common stock were outstanding under the 1994 stock option plan and 1998 stock option plan at a weighted average exercise price of $4.51;

. 2,714,855 shares had been issued upon exercise of outstanding options, net of repurchases, under the 1994 and 1998 stock option plans; and . 849,261 shares remained available for future grant under the 1994 and 1998 stock option plans.

1999 Employee Stock Purchase Plan Our 1999 employee stock purchase plan was adopted by the board of directors and shareholders in August 1999. The 1999 employee stock purchase plan became effective on the effective date of our initial public offering. A total of 250,000 shares of common stock has been reserved for issuance under the 1999 employee stock purchase plan.

The 1999 employee stock purchase plan, which is intended to qualify under Section 423 of the Internal Revenue Code, provides our employees with an opportunity to purchase our common stock through accumulated payroll deductions. The 1999 employee stock purchase plan is administered by the board of directors or by a committee appointed by the board of directors. The 1999 employee stock purchase plan permits an eligible employee to purchase common stock through payroll deductions of up to 15% of that employee's compensation. Employees, including officers and employee directors, of SonicWALL, Inc., or of any majority-owned subsidiary designated by the board of directors, are eligible to participate in the 1999 employee stock purchase plan if they are employed by SonicWALL, Inc. or any designated subsidiary for at least 20 hours per week and more than five months per year. Unless the board of directors or its committee determines otherwise, the 1999 employee stock purchase plan is implemented by a series of overlapping offering periods generally of 24 months' duration with new offering periods commencing on February 1 and August 1 of each year. Each offering period is divided into four consecutive purchase periods of approximately six months' duration. The first offering period commenced on the date of our initial public offering and will end on July 31, 2001; the initial purchase period ends six months after our initial public offering date. The price at which common stock will be purchased under the 1999 employee stock purchase plan is equal to 85% of the fair market value of the

common stock on the first day of the applicable offering period or the last day of the applicable purchase period, whichever is lower. Employees may end their participation in an offering period at any time, and participation automatically ends on termination of employment.

Under the 1999 employee stock purchase plan, no employee may be granted an option if immediately after the grant the employee would own stock and/or hold outstanding options to purchase stock equaling 5% or more of the total voting power or value of all classes of our stock or that of our subsidiaries. In addition, no employee may be granted an option under the 1999 employee stock purchase plan if the option would permit the employee to purchase stock under all of our employee stock purchase plans in an amount that exceeds $25,000 of fair market value for each calendar year in which the option is outstanding at any time. In addition, no employee may purchase more than 2,000 shares of common stock under the 1999 employee stock purchase plan in any one purchase period. If the fair market value of the common stock on a purchase date other than the final purchase date of an offering period is less than the fair market value at the beginning of the offering period, each participant in the 1999 employee stock purchase plan will automatically be withdrawn from the offering period as of the purchase date and re-enrolled in a new 24-month offering period on the first business day following the purchase date.

The 1999 employee stock purchase plan provides that, in the event of a change of control of SonicWALL, Inc. each right to purchase stock under the 1999 employee stock purchase plan will be assumed or an equivalent right substituted by the successor corporation. However, our board of directors will shorten any ongoing offering period so that employees' rights to purchase stock under the 1999 employee stock purchase plan are exercised prior to the transaction if the successor corporation refuses to assume each purchase right or to substitute an equivalent right.

The 1999 employee stock purchase plan will terminate in August 2009 unless terminated earlier in accordance with its provisions. The board of directors has the power to amend or terminate the 1999 employee stock purchase plan if its action does not adversely affect any outstanding rights to purchase stock thereunder. However, our board of directors may amend or terminate the 1999 employee stock purchase plan or an offering period even if it would adversely affect options in order to avoid our incurring adverse accounting charges.

401(k) Plan

We maintain a 401(k) plan that covers all our employees who satisfy the plan's eligibility requirements relating to minimum age, length of service and hours worked. We may make an annual contribution for the benefit of eligible employees in an amount determined by our board of directors. We have not made any contribution to date and have no current plans to do so. Eligible employees may make pretax elective contributions of up to 15% of their compensation, subject to maximum limits on contributions prescribed by law.

Certain Transactions and Business Relationships

Since January 1, 1996, SonicWALL, Inc. has not been a party to any transaction or series of similar transactions in which the amount involved exceeds $60,000 and in which any director, executive officer, or holder of more than 5% of our common stock had or will have a direct or indirect material interest other than . normal compensation arrangements which are described under "Management--Executive Compensation" above; and . the transactions described below.

Transactions with Executive Officers, Directors and Significant Shareholders (1) In August 1998, SonicWALL, Inc. acquired all the partnership interest of AckFin Networks ("AckFin"), a California general partnership, in exchange for an aggregate of 5,426,184 shares of common stock and the assumption of $150,000 in liabilities. The controlling partners of AckFin were Sreekanth Ravi and Sudhakar Ravi, executive officers and directors of SonicWALL, Inc. Additional partners were Ravi Anne and Bruce Wonnacott. The deemed fair market value of our common stock on the date of acquisition was $0.90 per share, resulting in an aggregate value of $4.9 million of common stock issued in this transaction. The intangible assets acquired by the Company were rights to the completed core technology developed by AckFin that provides the foundation for our Internet products.

(2) On December 23, 1998, we extended two loans in the aggregate amount of $96,069.60 to Sreekanth Ravi, Chairman of the Board, Chief Executive Officer, President and a director of SonicWALL, Inc. to pay the exercise price of options to purchase 1,067,440 shares of our common stock. Each loan had an interest rate of 8% per year, payable over four years and was secured by the shares of common stock purchased upon the exercise of Mr. Ravi's stock options. These loans were repaid in full in August 1999.

(3) On December 23, 1998, we extended two loans in the aggregate amount of $96,069.60 to Sudhakar Ravi, Chief Technical Officer and a director of SonicWALL, Inc. to pay the exercise price of options to purchase 1,067,440 shares of our common stock. Each loan had an interest rate of 8% per year, payable over four years and was secured by the shares of common stock purchased upon the exercise of Mr. Ravi's stock options. These loans were repaid in full in August 1999.

(4) On February 19, 1999, we issued an aggregate of 1,438,377 shares of our redeemable Series A convertible preferred stock at a purchase price of $3.48 per share to several investors, including 14,384 shares issued to Robert Williams, a director of the Company, 1,150,700 shares to Bay Partners SBIC II, L.P. Mr. Williams is a partner of Bay Management Company 1997, the general partner of Bay Partners SBIC II, L.P. The purchasers of redeemable Series A convertible preferred stock are entitled to registration rights in respect of the common stock issued or issuable upon conversion of the redeemable Series A convertible preferred stock.

(5) On May 26, 1999, we extended a loan in the amount of $300,000 to Michael Sheridan, Vice President Finance, Chief Financial Officer, and Secretary of SonicWALL, Inc. to pay the exercise price of options to purchase 300,000 shares of our common stock. Mr. Sheridan has purchased the optioned shares, and SonicWALL, Inc. has the right to repurchase the optioned shares for the purchase price paid, which right lapses over four years. The loan has an interest rate of 8% per year and is payable over

four years. The loan is payable in full if Mr. Sheridan is no longer an employee, officer, director or consultant of SonicWALL, Inc. As of December 31, 1999, aggregate principal and interest of approximately $314,000 were outstanding under the loan.

(6) On August 6, 1999, Sreekanth Ravi, Chairman of the Board, Chief Executive Officer and President, and Sudhakar Ravi, Chief Technical Officer and a director, sold an aggregate of 1,832,364 shares of common stock to Bay Sonic Investors, LLC at a purchase price of $6.52 per share. On August 11, , two shareholders also sold an aggregate of 400,000 shares of common stock to Bay Sonic Investors, LLC at a purchase price of $6.52 per share. Robert Williams, a director of the Company, is a managing member of Bay Sonic Investors, LLC. In addition, on August 6, 1999, Sreekanth Ravi sold 38,354 shares of common stock to David Shrigley, a director of the Company, at a purchase price of $6.52 per share and 30,682 shares of common stock to John McNulty at a purchase price of $6.52 per share. The purchasers of common stock in these transactions are entitled to registration rights in respect of the common stock purchased.

(7) Jerrold F. Petruzzelli, a director of SonicWALL, Inc. is a partner of Manatt, Phelps & Phillips, LLP, legal counsel to SonicWALL, Inc. In 1998, SonicWALL, Inc. paid Wise & Shepard LLP, a law firm of which Mr. Petruzzelli was then a partner, $88,772 in legal fees and expenses. In June 1999, Wise & Shepard LLP merged into Manatt, Phelps & Phillips, LLP and Mr. Petruzzelli became a partner of Manatt, Phelps & Phillips, LLP. For the year ended December 31, 1999, SonicWALL, Inc. had paid Wise & Shepard LLP and Manatt, Phelps & Phillips LLP an aggregate of $465,115 in legal fees and expenses.

Indemnification Agreements We have entered into indemnification agreements with our executive officers and directors. See "Management--Director and Officer Indemnification and Liability."

Registration Rights Agreements Some of our shareholders are entitled to have their shares registered by us for resale. See "Description of Capital Stock--Registration Rights."

Principal and Selling Shareholders

Principal Shareholders The following table provides information regarding the actual beneficial ownership of our outstanding common stock as of December 31, 1999, and as adjusted to reflect the sale of common stock offered by this prospectus, for:

. each person or group that we know beneficially owns more than 5% of our common stock;

. each of our directors;

. our chief executive officer;

. the other executive officers whose compensation exceeded $100,000 in fiscal 1999;

. all of our directors and executive officers as a group; and . selling shareholders.

Percentage of beneficial ownership is based on 23,675,385 shares of common stock outstanding as of December 31, 1999, together with options that are exercisable within 60 days of December 31, 1999 for each shareholder. Under the rules of the Securities and Exchange Commission, beneficial

ownership includes shares over which the indicated beneficial owner exercises voting and/or investment power. Shares of common stock subject to options that are currently exercisable or will become exercisable within 60 days are deemed outstanding for computing the percentage ownership of the person holding the option, but are not deemed outstanding for purposes of computing the percentage ownership of any other person. The percentages for beneficial ownership after offering assume that the underwriters do not exercise their over-allotment option. Unless otherwise indicated in the footnotes below, we believe that the persons and entities named in the table have sole voting and investment power with respect to all shares beneficially owned, subject to applicable community property laws. Unless otherwise indicated, the following beneficial owners can be reached at our principal offices.

Name and Address	Beneficially Ownership as of December 31, 1999		Number of Shares Being Offered	Beneficial Ownership After the Offering	
	Number	Percentage		Number	Percentage
Sreekanth Ravi(1).....	4,893,286	20.7%	500,000	4,393,286	17.3%
Sudhakar Ravi(2).....	4,893,286	20.7%	500,000	4,393,286	17.3%
Steven R. Perricone.....	287,500(3)	1.2%	60,000	227,500(4)	*%
Michael J. Sheridan.....	300,000	1.3%	--	300,000	1.2%
Bay Partners SBIC II, L.P.(5).....	2,301,400	9.8%	--	2,301,400	9.1%
Bay Sonic Investors, LLC(6).....	2,232,364	9.5%	--	2,232,364	8.8%
Ravi Anne.....	1,144,546	4.8%	100,000	1,044,546	4.1%
Bruce Wonnacott.....	1,111,546	4.7%	100,000	1,011,546	4.0%
Michael Barnick.....	917,592	3.9%	450,000	467,592	1.8%
Jerrold F. Petruzzelli(7).....	100,000	*%	--	100,000	*%
David Shrigley(8).....	84,354	*%	--	84,354	*%
Robert M. Williams(9)...	28,768	*%	--	28,768	*%
Niranjan Koduri(10).....	57,268	*%	10,000	47,268	*%
Lawrence Woodard(11)....	90,868	*%	10,000	80,868	*%
David Isherwood(12).....	29,120	*%	10,000	19,120	*%
Vinay Anne(13).....	64,944	*%	10,000	54,944	*%
All directors and executive officers as a group (7 persons)(14)(15).....	15,120,958	63.9%	1,060,000	14,060,958	55.3%

* Less than 1%. (1) Includes 600,000 shares transferred to a family trust. (2) Includes 600,000 shares transferred to a family trust.

(3) Includes 267,500 shares of common stock issuable upon exercise of immediately exercisable options. (4) Includes 207,500 shares of common stock issuable upon exercise of immediately exercisable options. (5) Represents 2,301,400 shares held by Bay Partners SBIC II, L.P. Robert Williams, a director of SonicWALL, Inc. is a partner of Bay Management Company 1997, the general partner of Bay Partners SBIC II, L.P. He shares voting and investing power with respect to the shares held by this entity, and disclaims beneficial ownership of shares in which he has no pecuniary interest. The address for Bay Partners SBIC II, L.P. is 10600 N. De Anza Boulevard, Suite 100, Cupertino, California 95014. (6) On August 6, 1999, Sreekanth Ravi and Sudhakar Ravi sold an aggregate of 1,832,364 shares of common stock to Bay Sonic Investors, LLC, and Ravi Anne and Bruce Wonnacott sold an aggregate of 400,000 shares of common stock to Bay Sonic Investors, LLC. See Note (6) in Certain Transactions and

Business Relationships above. Bay Sonic Investors, LLC is an affiliate of Robert Williams, a director of SonicWALL, Inc. Mr. Williams is a managing member of Bay Sonic Investors and as such may be deemed to have voting control of the shares held by Bay Sonic Investors, LLC. (7) Includes 5,000 shares held on behalf of a minor child in an irrevocable trust of which Mr. Petruzzelli is the sole trustee. The address for Mr. Petruzzelli is 3030 Hansen Way, Suite 100, Palo Alto, California 94304. (8) Includes 4,000 shares held by children residing in the same household as Mr. Shrigley. The address for Mr. Shrigley is 471 Santa Rosa Drive, Los Gatos, California 95032. (9) See note (4) above. The address for Mr. Williams is 10600 N. De Anza Boulevard, Suite 100, Cupertino, California 95014. (10) Includes 54,628 shares of common stock issuable upon exercise of immediately exercisable options. (11) Includes 90,868 shares of common stock issuable upon exercise of immediately exercisable options. (12) Includes 29,120 shares of common stock issuable upon exercise of immediately exercisable options. (13) Includes 64,944 shares of common stock issuable upon exercise of immediately exercisable options. (14) Includes 267,500 shares of common stock issuable upon exercise of immediately exercisable options. (15) Includes 207,500 shares of common stock issuable upon exercise of immediately exercisable options.

Selling Shareholders

If the underwriters exercise their over-allotment option in full, the following directors, officers and shareholders will sell the number of shares indicated below:

Name	Beneficial Ownership Prior to Over-allotment Exercise	Percentage of Shares of Common Stock Before Over-allotment Exercise	Number of Shares Being Offered	Beneficial Ownership After Over-allotment Exercise	Percentage of Shares of Common Stock Outstanding After Over-allotment Exercise
Sreekanth Ravi.....	4,393,286	17.3%	114,583	4,278,703	16.5%
Sudhakar Ravi.....	4,393,286	17.3%	114,583	4,278,703	16.5%
Ravi Anne.....	1,056,546	4.2%	22,917	1,033,629	4.0%
Bruce Wonnacott.....	1,011,564	4.0%	22,917	988,647	3.8%

Description of Capital Stock

We are authorized to issue up to two hundred million shares of common stock and ten million shares of preferred stock. You should carefully read our articles of incorporation, which are included as an exhibit to the registration statement of which this prospectus is a part.

Common Stock

As of December 31, 1999 there were 23,675,385 shares of common stock outstanding, held of record by approximately 65 holders of record. Following this offering, there will be 25,425,385 shares of common stock outstanding, assuming no exercise of the underwriters' over-allotment option and no exercise of outstanding options. The holders of common stock are entitled to one vote for each share held of record on all matters submitted to a vote of shareholders. Subject to preferences of any outstanding shares of preferred stock, the holders of common stock are entitled to receive ratably any

dividends the board of directors declares out of funds legally available for paying dividends. If SonicWALL, Inc. is liquidated, dissolved or wound up, the holders of common stock are entitled to share ratably in all assets remaining after paying liabilities and liquidation preferences of any outstanding shares of preferred stock. Holders of common stock have no preemptive rights or rights to convert their common stock into any other securities. There are no redemption or sinking fund provisions applicable to the common stock. All outstanding shares of common stock are fully paid and nonassessable, and the shares of common stock to be issued upon completion of this offering will be fully paid and nonassessable.

Preferred Stock

Under our articles of incorporation, the board of directors have the authority, without further action by the shareholders, to issue up to 8,561,623 shares of preferred stock in one or more series and to fix the price, rights, privileges, preferences and restrictions of that preferred stock, any or all of which may be greater than the rights of the common stock. The board of directors, without shareholder approval, can issue preferred stock with voting, conversion or other rights that could adversely affect the voting power and other rights of the holders of common stock. Preferred stock could thus be issued quickly with terms that could decrease the amount of earnings and assets available for distribution to common stock holders and could delay or prevent a change of control of SonicWALL, Inc. or make removal of management more difficult. Additionally, the issuance of preferred stock may decrease the market price of the common stock and may adversely affect the voting and other rights of the holders of common stock. The board of directors does not currently intend to seek shareholder approval prior to any issuance of preferred stock, unless required to do so by law. We have no current plans to issue any preferred stock.

Anti-takeover Provisions Some provisions of our charter documents may have the effect of delaying, deterring or preventing changes in control or management of SonicWALL, Inc., including changes a shareholder might consider to be favorable. This could have an adverse affect on the market price of our common stock. These provisions include:

. authorizing the board to issue additional preferred stock;

. prohibiting cumulative voting in the election of directors;

. limiting the persons who may call special meetings of shareholders;

. prohibiting shareholder actions by written consent; and . establishing advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted on by shareholders at shareholder meetings.

Preferred Stock

Our charter documents grant the board of directors broad power to establish the rights and preferences of the authorized but unissued preferred stock. Preferred stock could be issued with terms that delay, deter or prevent a change of control or management.

No Cumulative Voting for Directors Our charter documents prohibit cumulative voting for directors. This may limit or eliminate the power of minority shareholders to influence the composition of our board of directors.

No Shareholder Action by Written Consent Our charter documents provide that an action requiring or permitted to be taken at any annual or special meeting of shareholders may only be taken at a duly called annual or special meeting of our shareholders. This provision prevents shareholders from initiating or effecting any such action by written consent.

Notice Requirements

Our charter documents establish advance notice procedures with regard to all shareholder proposals to be brought before meetings of our shareholders, including relating to the nomination of candidates for election as directors, the removal of directors and amendments to our articles of incorporation or bylaws. These procedures provide that notice of these proposals must be given in writing, no later than 60 days prior to the meeting to our Secretary and must contain information specified in our charter documents.

Stock Option Plans

Our stock option plans and stock purchase plan generally provide for assumption of our benefit plans or substitution of equivalent options of a successor corporation or, alternatively, at the discretion of the board of directors, exercise of some or all of the options, including those for non- vested shares, or acceleration of vesting of shares issued pursuant to stock grants, upon a change of control or similar event.

These charter provisions and stock option plans may have the effect of delaying, deterring or preventing a change of control of SonicWALL, Inc.

Registration Rights

Under the terms of a registration rights agreement, subject to exceptions, if we propose to register any of our shares of common stock under the Act, either for our own account or the account of any shareholder, in any public offering, upon the completion of this offering, investors holding an aggregate of 5,178,154 shares of our common stock will be entitled to notice of such registration and will be entitled to include those registrable securities in a registration under the Act.

In addition, beginning May 9, 2000, investors holding an aggregate of 2,876,754 shares of our common stock will be entitled to additional rights under this registration rights agreement as follows: the holder or holders of an aggregate of at least 50% of the then outstanding registrable securities shall have the right to require us to file a registration statement on a form, other than Form S-3 under the Act, in order to register the registrable securities then held by such holder or holders, provided that:

. the anticipated aggregate offering price to the public is at least $2,000,000; and . we shall not be required to file more than two such registration statements.

Further, a holder or holders of at least 20% of the then outstanding registrable securities may require us to use our best efforts to file additional registration statements on Form S-3, provided that:

. the anticipated aggregate offering price to the public is at least $500,000; and . we shall not be required to file more than one such registration statement in any twelve-month period.

The right to include any of the above described registrable securities in any registration is subject to limitations and conditions, including the underwriters' right to limit the number of shares being registered by all holders. We are required to indemnify holders of registrable securities and the underwriters, if any, for these holders under described circumstances. In general, we are required to bear the expenses of registrations, except for the selling shareholders' pro rata portion of the underwriting discounts and commissions.

Transfer Agent and Registrar The transfer agent and registrar for the common stock is EquiServe Trust Company, N.A.

Nasdaq National Market Listing Our common stock symbol on the Nasdaq National Market is SNWL.

Shares Eligible for Future Sale

Future sales of substantial amounts of shares of our common stock in the public market could adversely affect prevailing market prices. Furthermore, since only a limited number of shares will be available for sale shortly after this offering because of contractual and legal restrictions on resale, as described below, sales of substantial amounts of common stock in the public market after the restrictions lapse could adversely affect the prevailing market price.

After this offering, 25,425,385 shares of common stock will be outstanding, assuming the issuance of an aggregate of 1,750,000 shares of common stock. The number of shares outstanding after this offering is based on the number of shares outstanding as of December 31, 1999, and assumes no exercise of outstanding options. The 4,600,000 shares sold in the initial public offering on November 11, 1999 and the 3,500,000 shares sold in this offering will be freely tradable without restriction under the Act. The remaining 17,325,385 shares of common stock outstanding upon completion of the offering are restricted securities in that they may be sold in the public market only if registered or if they qualify for an exemption from registration under the Act or Rules 144, 144(k) or 701 of the Act.

In connection with this offering, our selling shareholders and executive officers have agreed under lock-up agreements not to sell, transfer or exchange any shares of our common stock for a period of 90 days after the date of this prospectus without the prior written consent of Bear, Stearns & Co. Inc. Of the 17,325,385 shares of our common stock which are restricted securities, such shares will be available for sale after the date of this offering as follows:

Number of Date of Availability for Sale Shares May 9, 2000..... 3,268,711 90 days following completion of this offering..... 11,345,274 At various times after May 9, 2000 (as Rule 144 holding period expires)..... 2,711,400 Transfers may be made earlier:

. as a bona fide gift or gifts, provided the donee or donees agree in writing to be bound by this restriction;

. as a transfer to members of the transferor's immediate family or to trusts for the benefit of the transferor or members of the transferor's immediate family, provided that the transferees agree in writing to be bound by the terms of this restriction;

. as a distribution to limited partners or shareholders of the transferor, provided that the distributees agree in writing to be bound by the terms of this restriction;

. with respect to dispositions of common stock acquired on the open market; or . with the prior written consent of Bear, Stearns & Co. Inc.

Bear, Stearns & Co. Inc. may, in its sole discretion and at any time without notice, release all or any portion of the securities subject to lock-up agreements. When determining whether or not to release shares from the lock-up agreements, Bear, Stearns & Co. Inc. will consider, among other factors, the shareholder's reasons for requesting the release, the number of shares for which the release is being requested and market conditions at the time. Following the expiration of the 90 day lock-up period, additional shares of common stock will be available for sale in the public market subject to compliance with Rule 144 or Rule 701.

In general, under Rule 144 as currently in effect, an affiliate of SonicWALL, Inc. or a person, or persons whose shares are aggregated, who has beneficially owned restricted securities for at least one year, including the holding period of any prior owner except an affiliate, would be entitled to sell within any three-month period a number of shares that does not exceed the greater of 1% of the then outstanding shares of SonicWALL, Inc. common stock or the average weekly trading volume of SonicWALL, Inc. common stock on the Nasdaq National Market during the four calendar weeks preceding such sale. Sales under Rule 144 are also subject to manner of sale provisions, notice requirements and the availability of current public information about SonicWALL, Inc. Any person, or persons whose shares are aggregated, who is not deemed to have been an affiliate of SonicWALL, Inc. at any time during the 90 days preceding a sale, and who has beneficially owned shares for at least two years including any period of ownership of preceding non-affiliated holders, would be entitled to sell such shares under Rule 144(k) without regard to the volume limitations, manner of sale provisions, public information requirements or notice requirements.

In addition, the holders of an aggregate of 2,876,754 shares of outstanding common stock have rights to require us to register their shares for future sale. Subject to limited exceptions, these holders and holders of approximately 2,301,400 shares of common stock have the right to participate in any registration we undertake on our own (including an exception for a registration of shares in connection with an employee benefit plan or merger).

Underwriting

Subject to the terms and conditions of an underwriting agreement between us and the underwriters named below, who are represented by Bear, Stearns & Co. Inc., J.P. Morgan Securities Inc., Chase Securities Inc., Thomas Weisel Partners LLC and Pacific Growth Equities, Inc., the underwriters have severally agreed to purchase from us and the selling shareholders the following respective number of shares of common stock less the underwriting discounts and commissions set forth on the cover page of this prospectus.

Number of Underwriter Shares Bear, Stearns & Co. Inc..... J.P. Morgan Securities Inc..... Chase Securities Inc..... Thomas Weisel Partners LLC..... Pacific Growth Equities, Inc.....
Total.....

The underwriting agreement provides that the obligations of the several underwriters to purchase and accept delivery of the shares included in this offering are subject to approval of legal matters by their counsel and to customary conditions, including the effectiveness of the registration statement, the continuing correctness of our representations to them, the listing of the common stock to be sold on the Nasdaq National Market and no occurrence of an event that would have a material adverse effect on our business. The underwriters are obligated to purchase and accept delivery of all the shares, other than those covered by the over-allotment option described below, if they purchase any of the shares.

We and the selling shareholders have agreed to indemnify the underwriters against various liabilities, including liabilities under the Act, and, where such indemnification is unavailable, to contribute to payments that the underwriters may be required to make in respect of such liabilities.

The underwriters propose to offer the shares of common stock directly to the public initially at the public offering price set forth on the cover page of this prospectus and to selected dealers at such price less a concession not to exceed $ per share. The underwriters may allow, and such selected dealers may reallow, a concession not to exceed $ per share and that after the commencement of this offering, the public offering price and the concessions may be changed.

We have granted to the underwriters an option to purchase up to 250,000 additional shares and certain selling shareholders have granted to the underwriters an option to purchase in the aggregate up to 275,000 additional shares, to be sold in this offering at the public offering price less the underwriting discount set forth on the cover page of this prospectus. The underwriters may exercise this option solely to cover over-allotments, if any. The option may be exercised in whole or in part at any time within 30 days after the date of this prospectus. To the extent the option is exercised, the underwriters will be severally committed, subject to several conditions, including the approval of legal matters by their counsel, to purchase the additional shares of common stock in proportion to their respective purchase commitments as indicated in the preceding table.

The underwriting fee is equal to the public offering price per share of common stock less the amount paid by the underwriters to us per share of common stock. The following table shows the underwriters' discounts to be paid to the underwriters by us and the selling shareholders. Such amounts are shown

assuming both no exercise and full exercise of the underwriters' option to purchase additional shares.

	Per Share		Total	
	Without Over-Allotment	With Over-Allotment	Without Over-Allotment	With Over-Allotment
Underwriting discounts and commissions payable by us	$	$	$	$
Underwriting discounts and commissions payable by the selling shareholders	$	$	$	$

We estimate that the total expenses of the offering, excluding underwriting discounts and commissions, will be approximately $781,000 and will be paid by us. The offering of the shares is made for delivery, when, as and if accepted by the underwriters and subject to prior sale and to withdrawal, cancellation or modification of the offering without notice. The underwriters reserve the right to reject an order for the purchase of shares in whole or in part.

We and the selling shareholders have agreed not to, directly or indirectly, offer, sell, contract to sell, grant any option to purchase, pledge or otherwise dispose of (or announce any of the foregoing), or, in any manner, transfer all or a portion of the economic consequences associated with the ownership of any shares of common stock or any securities convertible into or exercisable or exchangeable for common stock beneficially owned during the 90- day period following the date of this prospectus, subject to limited exceptions, without the prior written consent of Bear, Stearns & Co. Inc.

In order to facilitate this offering, the underwriters may engage in transactions that stabilize, maintain or otherwise affect the price of the common stock during and after this offering. Specifically, the underwriters may over-allot or otherwise create a short position in the common stock for their own account by selling more shares of common stock than have been sold to them by us. The underwriters may elect to cover any such short position by purchasing shares of common stock in the open market or by exercising the over- allotment option granted to them. In addition, the underwriters may stabilize or maintain the price of the common stock by bidding for or purchasing shares of common stock in the open market and may impose penalty bids, under which selling concessions allowed to syndicate members or other broker-dealers participating in this offering are reclaimed if shares of common stock previously distributed in this offering are repurchased in connection with stabilization transactions or otherwise. The effect of these transactions may be to stabilize or maintain the market price of the common stock at a level above that which might otherwise prevail in the open market. The imposition of a penalty bid may also affect the price of the common stock to the extent that it discourages resales of the common stock. No representation is made as to the magnitude or effect of any such stabilization or other transactions. Such transactions may be effected on the Nasdaq National Market or otherwise and, if commenced, may be discontinued at any time.

Thomas Weisel Partners LLC, one of the representatives of the underwriters, was organized and registered as a broker-dealer in December 1998. Since December 1998, Thomas Weisel Partners has been named as a lead or co-manager on 126 filed public offerings of equity securities, of which 94 have been completed, and has acted as a syndicate member in an additional 59 public offerings of equity

securities. Thomas Weisel Partners does not have any material relationship with us or any of our officers, directors or other controlling persons, except with respect to its contractual relationship with us pursuant to the underwriting agreement entered into in connection with this offering.

Legal Matters

The validity of the common stock offered in this offering will be passed upon for us by Manatt, Phelps & Phillips, LLP of Palo Alto, California. Jerrold F. Petruzzelli, a partner of Manatt, Phelps & Phillips, LLP, is a director of SonicWALL, Inc. and owns or has voting control over 100,000 shares of SonicWALL, Inc. common stock and Manatt, Phelps & Phillips, LLP holds 2,000 shares of common stock. Legal matters in connection with the offering will be passed upon for the underwriters by Latham & Watkins, San Francisco, California.

Experts

The consolidated financial statements as of December 31, 1998 and 1999 and for each of the three years in the period ended December 31, 1999, included in this Prospectus and the financial statement schedule included in the Registration Statement have been so included in reliance on PricewaterhouseCoopers LLP, independent accountants, given on the authority of said firm as experts in auditing and accounting.

Sonicwall, Inc.

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Report of Independent Accountants

To the Board of Directors and Shareholders of SonicWALL, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of shareholders' equity and of cash flows present fairly, in all material respects, the financial position of SonicWALL, Inc. and its subsidiary at December 31, 1999 and 1998, and the results of their operations and their cash flows for each of the three years in the period ended

December 31, 1999, in conformity with accounting principles generally accepted in the United States. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

PricewaterhouseCoopers LLP San Jose, California January 13, 2000

Sonicwall, Inc.

CONSOLIDATED BALANCE SHEETS (In thousands, except share data) December 31, 1998 1999

ASSETS		
Current Assets:		
Cash and cash equivalents	$ 1,051	$62,589
Accounts receivable, net of allowance for doubtful accounts of $193 and $548	677	3,687
Inventories	331	558
Deferred income taxes	366	1,556
Prepaid expenses and other current assets	31	1,015
Total current assets	2,456	69,405
Property and equipment, net	107	435
Intangibles and other assets	2,188	1,399
Total assets	$ 4,751	$71,239
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$ 549	$ 2,692
Accrued payroll and related benefits	145	1,205
Other accrued liabilities	748	1,839
Deferred revenue	1,512	3,732
Income taxes payable	309	1,021
Total current liabilities	3,263	10,489
Commitments and contingencies (Note 9)		
Shareholders' Equity:		
Preferred stock, no par value; 10,000,000 shares authorized; none issued and outstanding	--	--
Common stock, no par value; 200,000,000 shares authorized; 16,272,164 and 23,675,385 shares issued and outstanding	2,732	65,109
Deferred stock compensation	(6)	(3,209)
Notes receivable from shareholders	(230)	(300)
Accumulated deficit	(1,008)	(850)
Total shareholders' equity	1,488	60,750
Total liabilities and shareholders' equity	$ 4,751	$71,239

The accompanying notes are an integral part of these consolidated financial statements.

Sonicwall, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS (In thousands, except per share data) Year Ended December 31, 1997 1998 1999

Revenue			
Internet security	$ 250	$ 2,349	$19,403
Ethernet	9,092	5,166	1,644
Total revenue	9,342	7,515	21,047
Cost of revenue			
Internet security	225	1,035	5,254
Ethernet	4,617	2,273	707
Total cost of revenue	4,842	3,308	5,961
Gross margin	4,500	4,207	15,086
Operating expenses			
Research and development	1,983	2,051	3,634
Sales and marketing	2,468	2,870	5,342
General and administrative	644	753	1,761
Deferred stock compensation	--	42	2,895
Total operating expenses	5,095	5,716	13,632
Income (loss) from operations	(595)	(1,509)	1,454
Other income (expense), net	29	54	536
Income (loss) before income taxes	(566)	(1,455)	1,990
Benefit from (provision for) income taxes	99	(6)	(1,832)
Net income (loss)	$ (467)	$ (1,461)	$ 158
Net income (loss) per share			
Basic	$ (0.06)	$ (0.13)	$ 0.01
Diluted	$ (0.06)	$ (0.13)	$ 0.01
Shares used in computing net income (loss) per share			
Basic	8,461	11,251	17,334
Diluted	8,461	11,251	21,196

The accompanying notes are an integral part of these consolidated financial statements.

Sonicwall, Inc.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (In thousands, except share data)

	Common Stock		Deferred Stock	Notes Receivable From	Retained Earnings (Accumulated	Total Shareholders'
	Shares	Amount	Compensation	Shareholders	Deficit)	Equity

Balance at December 31, 1996..... 8,461,100 $ 12 $ -- $ -- $ 920 $ 932 Net loss..... -- -- -- -- (467) (467) Balance at December 31, 1997..... 8,461,100 12 -- -- 453 465 Issuance of common stock upon exercise of stock options..... 2,384,880 230 -- (230) -- -- Issuance of common stock for acquisition..... 5,426,184 2,442 -- -- -- 2,442 Deferred stock compensation..... -- 48 (48) -- -- -- Amortization of deferred stock compensation..... -- -- 42 -- -- 42 Net loss..... -- -- -- -- (1,461) (1,461) Balance at December 31, 1998..... 16,272,164 2,732 (6) (230) (1,008) 1,488 Issuance of common stock upon exercise of stock options..... 526,467 467 -- (300) -- 167 Issuance of common stock in connection with the Company's initial public offering, net of issuance costs..... 4,000,000 50,841 -- -- -- 50,841 Conversion of preferred stock into common stock..... 2,876,754 4,971 -- -- -- 4,971 Payments of notes receivable from shareholders..... -- -- -- 230 -- 230

Deferred stock compensation..... -- 6,098 (6,098) -- -- -- Amortization of deferred stock compensation..... -- -- 2,895 -- -- 2,895 Net income..... -- -- -- -- 158 158 Balance at December 31, 1999..... 23,675,385 $65,109 $(3,209) $(300) $ (850) $60,750 The accompanying notes are an integral part of these consolidated financial statements.

Sonicwall, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS (In thousands) Year Ended December 31, 1997 1998 1999

Cash flows from operating activities:			
Net income (loss)	$ (467)	$(1,461)	$ 158
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	63	413	905
Loss on disposal of fixed assets	--	--	53
Liabilities acquired	--	(75)	--
Provision for allowance for doubtful accounts	52	122	366
Amortization of deferred stock compensation	--	42	2,895
Changes in operating assets and liabilities:			
Accounts receivable	(252)	(235)	(3,375)
Inventories	1,031	20	(228)
Prepaid expenses and other current assets	(235)	270	(984)
Deferred income taxes	38	(89)	(1,190)
Other assets	(19)	18	(50)
Accounts payable	(150)	(114)	2,143
Accrued payroll and related benefits	107	(12)	1,060
Other accrued liabilities	(43)	438	1,091
Deferred revenue	(362)	828	2,220
Income taxes payable	(158)	214	712
Net cash provided by (used in) operating activities	(395)	379	5,776
Cash flows from investing activities:			
Purchase of property and equipment	(11)	(115)	(447)
Cash flows from financing activities:			
Proceeds from exercise of stock options	--	--	167
Proceeds from issuance of redeemable Series A convertible preferred stock	--	--	4,971
Proceeds from issuance of common stock with initial public offering, net of issuance costs	--	--	50,841
Payments of notes receivable from shareholders	157	--	230
Net cash provided by financing activities	157	--	56,209
Net increase (decrease) in cash and cash equivalents	(249)	264	61,538
Cash and cash equivalents at beginning of year	1,036	787	1,051
Cash and cash equivalents at end of year	$ 787	$ 1,051	$62,589
Supplemental disclosure of cash flow information:			
Cash paid for income taxes	$ 151	$ 1	$ 2,310
Supplemental disclosure of noncash investing and financing activities:			
Issuance of notes receivable upon the exercise of stock options	$ --	$ 230	$ 300
Conversion of preferred stock into common stock	$ --	$ --	$ 4,971
Deferred stock compensation	$ --	$ 48	$ 6,098
Acquisition of minority interest in AckFin Networks	$ --	$ 2,517	$ --

The accompanying notes are an integral part of these consolidated financial statements.

Sonicwall, Inc.

Notes to Consolidated Financial Statements

Note 1--The Company and Summary of Significant Accounting Policies:

SonicWALL, Inc. (the "Company") was incorporated in California in February 1991. SonicWALL, Inc. is a leading provider of Internet security solutions designed for broadband access customers in the small to medium enterprise, or SME, branch office, telecommuter and education markets. The Company's SonicWALL solution is a high-performance, solid state appliance that provides robust, reliable, easy-to-use and affordable Internet security. The Company's products enable its customers to securely utilize Internet applications and services as an integral part of their business.

The following is a summary of the Company's significant accounting policies:

Consolidation

The consolidated financial statements include those of the Company and its wholly-owned subsidiary Sonic Systems International, Inc., a Delaware corporation. Sonic Systems International, Inc. is intended to be a sales office but to date has not had any significant transactions. All significant intercompany accounts and transactions are eliminated in consolidation.

In August 1998, the Company acquired all the partnership interest of AckFin Networks ("AckFin"), a California general partnership, in exchange for an aggregate of 5,426,184 shares of the Company's common stock (estimated value of $0.90 per share, or $4,883,000) and the assumption of $150,000 in liabilities. The controlling partners of AckFin, Sreekanth Ravi and Sudhakar Ravi, two of the Company's executive officers and majority shareholders, were deemed to be a control group for purposes of determining the amount of purchase price to be "stepped-up." The value of the exchanged shares for AckFin was accounted for as a reorganization of entities under common control. Accordingly, net assets acquired were valued by applying carryover basis to the control group interest and a stepped-up basis to the minority interest. The step-up of the minority interest resulted in an intangible asset of $2,517,000. This intangible asset was attributed to acquired completed technology and will be amortized over a period of three years. Amortization expense was $350,000 and $839,000 for the years ended 1998 and 1999, respectively. The intangible assets acquired by the Company were rights to the completed core technology developed by AckFin that provides the foundation for our Internet products. Since this transaction occurred between entities that were under common control, since the inception of AckFin, the financial results of AckFin have been combined with the results of the Company for the period since the inception of AckFin (April 1997) through the date of exchange (August 1998). Expenses totaling $150,000 and $775,000 for the years ended December 31, 1997 and 1998, respectively, were included in the accompanying statements of operations. AckFin did not have any revenue transactions with unrelated third parties. Except for the expenses noted above, all other financial transactions for AckFin were eliminated upon combination with the Company.

Use of estimates

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

Cash and cash equivalents The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) Fair value The carrying value of the Company's financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities approximate their fair values due to their relatively short maturities. The Company does not hold or issue financial instruments for trading purposes.

Concentration of credit risk, foreign operations and significant customers Financial instruments which potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents and accounts receivable. The Company places its temporary cash investments in corporate bonds, commercial paper and, money market accounts with high credit quality financial institutions. The Company's accounts receivable are derived from revenue earned from customers located in the U.S. and certain foreign countries and regions, including Europe, Canada, Japan and Australia. Sales to foreign customers for the year ended December 31, 1997, 1998 and 1999 all of which were denominated in U.S. dollars, accounted for 36%, 32% and 34% of total revenue, respectively. The Company performs ongoing credit evaluations of its customers' financial condition and requires no collateral from its customers. The Company maintains an allowance for doubtful accounts receivable based upon the expected collectibility of accounts receivable.

During the year ended December 31, 1998, one customer accounted for 34% of the Company's revenue and at December 31, 1998, this one customer accounted for 39% of total gross receivables. During the year ended December 31, 1999, two customers accounted for 46% of the Company's revenue and at December 31, 1999, and three customers accounted for 74% of total gross receivables.

The Company is dependent on a third party contract manufacturers and some of the key components in the Company's product come from single or limited sources of supply.

Inventories

Inventories are stated at the lower of cost or market with cost being determined on a first-in, first-out basis.

Property and equipment Property and equipment are stated at cost. Depreciation is computed using the straight-line method over their estimated useful lives, which range from three to five years. Depreciation expense for the years ended December 31, 1997, 1998 and 1999 was $63,000, $55,000 and $66,000, respectively.

Intangibles and other assets Acquired technology is amortized to expense on a straight-line basis over three years.

Long-lived assets

The Company periodically evaluates the recoverability of its long-lived assets based on expected undiscounted cash flows and recognizes impairment from the carrying value of long-lived assets, if any, based on the fair value of such assets. To date, the Company has not recorded any impairment charges against the value of its long-lived assets.

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) Stock-based compensation The Company accounts for stock-based employee compensation arrangements in accordance with the provisions of Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees," and complies with the disclosure provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation." Under APB No. 25, compensation costs is determined based on the difference, if any, on the grant date between the fair value of the Company's stock and the amount an employee must pay to acquire the stock. Compensation expense is recognized over the vesting period.

The Company accounts for equity instruments issued to non-employees in accordance with the provisions of SFAS No. 123 and Emerging Issues Task Force 96-18.

Revenue recognition

Revenue is generally recognized at the time of shipment if collectibility is probable and no significant obligations remain. Sales to distributors are subject to agreements allowing certain rights of return, cooperative advertising, stock balancing rights and price protection. The largest distributor has the right to return products that have not been sold to end users for full credit subject to a restocking fee. Revenue from sales to this distributor is deferred at the time of shipment and is recognized when the distributor has sold the product to its customers. Certain other distributors have limited rights of return which allow them to return a percentage of the prior quarter's purchases by these distributors. Accordingly, reserves for estimated returns and exchanges are provided at the time of shipment. These reserves are estimated and adjusted periodically based upon historical rates of returns and allowances, inventory levels at the distributors and other related factors. Reserves for credits for price protection are provided at the time list prices are reduced by the Company. In the years ended December 31, 1997, 1998 and 1999 the Company provided approximately $300,000, $400,000 and $1,046,000, respectively, of revenue reserves related to risks of product returns, stock rotation rights and price protection rights. As of December 31, 1998 and 1999, deferred revenues included approximately $0.8 million and $1.7 million, respectively, related to these reserves.

Revenue from extended warranty programs, premium technical assistance, and subscriptions to content filtering services is recognized ratably over the term of the contract or subscription.

The standard warranty provisions include technical assistance, insignificant bug fixes and feature updates and repair or replacement guarantees for units with product defects. The standard warranty period is one year. The estimated costs associated with the standard warranty provisions are accrued at the time of revenue recognition. In the years ended December 31, 1997, 1998 and 1999 , the Company provided approximately $25,000, $100,000 and $425,000 of warranty reserves, respectively. As of December 31 1998 and 1999, the accompanying balance sheets include a warranty accrual of approximately $130,000 and $555,000, respectively.

The Company has co-operative advertising agreements with certain of its distributors. These agreements allow the distributors to be reimbursed by the Company for approved promotional activities. The amounts available for reimbursement are related to a percentage of the distributor's eligible purchases from the Company. The Company accrues for co-operative advertising as the related revenue is recognized. In the years ended December 31, 1997, 1998 and 1999, the Company recorded provisions for co-op advertising costs of $664,000, $502,000 and $554,000, respectively. As of December 31, 1998 and 1999, the accompanying balance sheets include an accrual for co-op advertising costs of $125,000 and $410,000, respectively.

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) Income taxes The Company accounts for income taxes under the liability method, which requires, among other things, that deferred income taxes be provided for temporary differences between the tax bases of the Company's assets and liabilities and their financial statement reported amounts. In addition, deferred tax assets are recorded for the future benefit of utilizing net operating losses, research and development credit carryforwards and temporary differences. A valuation allowance is provided against deferred tax assets unless it is more likely than not that they will be realized.

Research and development and capitalized software development costs Software development costs incurred prior to the establishment of technological feasibility are charged to research and development expense as incurred. Technological feasibility is established upon completion of a working model, which is typically demonstrated by initial beta shipment. Software development costs incurred subsequent to the time a product's technological feasibility has been established, through the time the product is available for general release to customers, are capitalized if material. To date, software development costs incurred subsequent to the establishment of technological feasibility have been immaterial and accordingly have not been capitalized.

Advertising Costs

The Company expenses advertising costs as incurred. Advertising expense totaled $774,000, $515,000 and $1,036,000 for the years ended December 31, 1997, 1998 and 1999, respectively.

Comprehensive income

Effective January 1, 1998, the Company adopted the provisions of SFAS No. 130, "Reporting Comprehensive Income." SFAS No. 130 establishes standards for reporting comprehensive income and its components in financial statements. Comprehensive income, as defined, includes all changes in equity during a period from non-owner sources. To date, the Company has not had any transactions that are required to be reported in comprehensive income.

Computation of net income (loss) per share The Company computes net income (loss) per share in accordance with SFAS No. 128, "Earnings per Share" and SEC Staff Accounting Bulletin No. 98 ("SAB 98"). Under the provisions of SFAS No. 128 and SAB 98, basic net income (loss) per share is computed by dividing the net income (loss) for the period by the weighted average number of common shares outstanding during the period. Weighted average shares exclude shares subject to repurchase ("restricted shares"). Diluted net income (loss) per share is computed by dividing the net income (loss) for the period by the weighted average number of common and common equivalent shares outstanding during the period, if dilutive. Common equivalent shares are composed of unvested restricted shares and incremental common shares issuable upon the exercise of stock options.

Recent accounting pronouncements In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101 (SAB 101), "Revenue Recognition in Financial Statements." SAB 101 provides guidance for revenue recognition under certain circumstances. The Company does not believe it will have a material impact on the financial statements. The accounting and disclosures prescribed by SAB 101 will be effective for the Company's quarter ended March 31, 2000.

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) The following table sets forth the computation of basic and diluted net income (loss) per share for the periods indicated (in thousands, except per share data):

Year Ended December 31, 1997 1998 1999

Numerator:			
Net income (loss)	$ (467)	$(1,461)	$ 158
Denominator:			
Weighted average common shares outstanding	8,461	11,251	17,503
Weighted average unvested common shares subject to repurchase	--	--	169
Denominator for basic calculation	8,461	11,251	17,334
Common stock equivalents	--	--	3,862
Denominator for diluted calculation	8,461	11,251	21,196
Basic net income (loss) per share	$(0.06)	$ (0.13)	$ 0.01
Diluted net income (loss) per share	$(0.06)	$ (0.13)	$ 0.01

Outstanding options to purchase 2,494,880 and 1,163,676 shares of common stock at an average exercise price of $0.10 and $0.13 per share have not been considered in the computation of diluted net loss per share for the years ended December 31, 1997 and 1998, respectively, as their effect would have been anti- dilutive.

In May 1999, the Company issued 300,000 shares upon the exercise of certain stock options. At December 31, 1999, 256,250 common shares are subject to repurchase at the option of the Company for $1.00 per share. These shares vest ratably over a 48 month period.

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) Note 2--Balance Sheet Components:

December 31, 1998 1999 (in thousands)

Inventories:		
Raw materials	$ 49	$ 25
Work-in-process	13	--
Finished goods	269	533
	$ 331	$ 558
Property and equipment:		
Equipment	$ 161	$ 442
Leasehold improvements	5	103
Software	53	60
Transportation	94	24
	313	629
Less: accumulated depreciation	(206)	(194)
	$ 107	$ 435
Intangibles and other assets:		
Acquired technology	$ 2,517	$ 2,517
Other assets	21	71
	2,538	2,588
Less: amortization	(350)	(1,189)
	$ 2,188	$ 1,399

Note 3--Line of Credit:

At December 31, 1999, the Company had a line-of-credit agreement with a bank which allows the Company to borrow up to $1,000,000. Borrowings under the line of credit bear interest at the bank's reference rate plus 1.75% (which equaled 10.25% at December 31, 1999), and are secured primarily by accounts receivable, inventories, and property and equipment. The line of credit can be utilized at a percentage of eligible receivables, as defined in the loan agreement. The agreement contains certain covenants requiring the Company to maintain certain levels of profitability, minimum tangible net worth, working capital and other financial ratios and prohibits the payment of cash or stock dividends on common stock over the life of the agreement. This line of credit will be in force until terminated by either party by notice of not less than 30 days prior to the effective date of such termination. No amounts were outstanding under the line of credit at December 31, 1999.

Note 4--Redeemable Series A Convertible Preferred Stock:

In February 1999, the Company issued 1,438,377 shares of redeemable Series A convertible preferred stock ("Preferred Stock") at $3.48 per share for net proceeds of $4,971,000. Each share of Preferred Stock converts into two shares of Common Stock. In November 1999, the Company completed its

initial public offering of 4,000,000 shares of Common Stock at $14.00 per share. In connection with the initial public offering, all outstanding shares of Preferred Stock automatically converted into Common Stock.

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) Note 5--Shareholders' Equity:

Stock split

Share information for all periods presented has been retroactively adjusted to reflect a 2 for 1 stock split effected on August 25, 1999.

1999 Employee Stock Purchase Plan The 1999 Employee Stock Purchase Plan was adopted by the board of directors in August 1999. A total of 250,000 shares of common stock have been reserved for issuance under the plan.

The Company's Stock Option Plans (the "Plans"), as amended, authorize the Board of Directors to grant incentive stock options and nonstatutory stock options to employees, directors and consultants to purchase up to a total of 7,358,324 shares of the Company's common stock. Under the Plans, incentive stock options are granted at an exercise price that is not to be less than 100% of the fair market value of the Company's common stock on the date of grant, as determined by the Company's Board of Directors. Nonqualified stock options are granted at a price that is not to be less than 85% of the fair market value of the common stock on the date of grant, as determined by the Board of Directors.

Generally, options granted under the Plans are exercisable for a period of ten years after the date of grant, and vest over four years.

The following table summarizes option activity under the stock option plans:

		Options Outstanding		
	Available for Grant	Shares	Exercise Price	Weighted Average Exercise Price
Balance at December 31, 1996.....	549,612	2,396,880	$ 0.08-0.09	$0.09
Granted.....	(204,000)	204,000	$ 0.25	$0.25
Exercised.....	--	--	$ --	$ --
Canceled.....	106,000	(106,000)	$ 0.08	$0.08
Balance at December 31, 1997.....	451,612	2,494,880	$ 0.08-0.25	$0.10
Authorized.....	2,000,000	--	$ --	$ --
Granted.....	(1,015,000)	1,015,000	$ 0.13	$0.13
Exercised.....	--	(2,134,880)	$ 0.09	$0.09
Canceled.....	211,324	(211,324)	$ 0.08-0.25	$0.19
Balance at December 31, 1998.....	1,647,936	1,163,676	$ 0.08-0.25	$0.13
Authorized.....	2,358,324	--	$ --	$ --
Granted.....	(3,259,500)	3,259,500	$0.50-29.87	$5.58
Exercised.....	--	(526,467)	$ 0.08-1.50	$0.89
Canceled.....	102,501	(102,501)	$ 0.13-9.00	$7.25
Balance at December 31, 1999	849,261	3,794,208	$0.08-29.87	$4.51

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) The following table summarizes information regarding stock options outstanding at December 31, 1999:

	Options Outstanding			Options Exercisable	
Exercise Prices	Weighted Average Exercise Price	Shares	Weighted Average Remaining Contractual Life (Years)	Shares	Weighted Average Exercise Price
$ 0.08-$ 0.08.....	$ 0.08	82,000	5.6	79,472	$0.08
$ 0.13-$ 0.13.....	$ 0.13	912,271	8.6	345,891	$0.13
$ 0.25-$ 0.25.....	$ 0.25	60,844	7.1	54,140	$0.25
$ 0.50-$ 0.75.....	$ 0.73	246,128	9.3	43,418	$0.73
$ 1.00-$ 1.50.....	$ 1.30	393,966	9.5	51,098	$1.25
$ 2.50-$ 3.50.....	$ 3.12	419,000	9.6	--	--
$ 7.50-$11.00.....	$ 3.12	1,663,999	9.7	29,658	$8.30
$29.87-$29.87.....	$29.87	16,000	9.9	--	--
	$ 4.51	3,794,208	9.2	603,677	$0.68

For financial reporting purposes, the Company has determined that the deemed fair value on the date of grant of certain stock options granted in 1998 and 1999 was in excess of the exercise price of the options. The deemed fair value for options granted in the year ended December 31, 1999 was $19,127,000 which exceeded the aggregate exercise price of these options by $4,214,000. This difference is considered deferred stock compensation and is amortized over the vesting periods of the applicable options and the repurchase periods for the restricted stock.

Based upon the above assumptions, the weighted average fair value per share of options granted in 1998 and 1999 were $0.05 and $6.01, respectively.

During the year ended December 31, 1999, the Company granted approximately 52,500 options to purchase common stock to certain consultants in exchange for services rendered. The options vest over one year. These options are subject to variable plan accounting with fair value re-measurements at the end of each quarterly reporting period. During the year ended December 31, 1999, the Company recorded deferred stock-based compensation expense related to these grants of $1,884,000. Of this amount $1,066,000 was recognized as stock-based compensation expense in the year ended December 31, 1999.

Pro forma stock compensation The Company has adopted the disclosure-only provisions of SFAS No. 123. Accordingly, no compensation cost has been recognized for the Company's stock option plan in the accompanying statements of operations. Had compensation cost for the Company's stock option plan been determined based on the fair market value at the grant dates for stock options granted in 1998 and 1997 consistent with the provisions of SFAS No. 123, the Company's net income (loss) would have been changed to the pro forma amounts indicated below, in thousands:

Year Ended December 31, 1997 1998 1999 Net income (loss)--as reported..... $ (467) $ (1,461) $ 158 Net income (loss)--pro forma..... $ (471) $ (1,469) $ (109)

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) The pro forma amounts reflect compensation expense related to 1997, 1998 and 1999 stock option grants only. In future years, the annual compensation expense will increase relative to the fair value of the stock options granted in those future years. The weighted average fair value of the options granted in 1997, 1998 and 1999 of $0.13, $0.05 and $2.27, respectively.

The fair value of each grant is estimated on the date of grant using the minimum value method with the following assumptions:

1997 1998 1999

Expected volatility.....	0%	0%	80%
Risk-free interest rate.....	6.0%	4.5% to 5.64%	4.79% to 5.83%
Expected life.....	5 years	5 years	4 years
Dividend yield.....	0%	0%	0%

Note 6--Notes Receivable from Shareholders:

In December 1998, the Company issued notes receivable in connection with the exercise of 2,134,880 shares of incentive stock options held by two shareholders. The full recourse notes totaling $192,000, accrue interest at a rate of 8% per annum. Principal and accrued interest shall be paid one-fourth on the first anniversary date of the note, and one-fourth every year thereafter for a total of four years. The notes principal and interest were paid in full during 1999.

In May 1999, the Company issued a full recourse note for $300,000 in connection with the exercise of 300,000 shares of incentive stock options by one shareholder. The note accrues interest at a rate of 8% per annum. Principal and accrued interest shall be paid one-fourth on the first anniversary date of the note, and one-fourth every year thereafter for a total of four years.

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) Note 7--Income Taxes:

The (benefit from) provision for income taxes consist of the following (in thousands):

Year Ended December 31, 1997 1998 1999

Current tax expense (benefit):			
Federal.....	$ (138)	$ 94	$ 3,178
State.....	1	1	708
	(137)	95	3,886
Deferred tax expense (benefit):			
Federal.....	32	(89)	(1,598)
State.....	6	--	(456)
	38	(89)	(2,054)
	$ (99)	$ 6	$ 1,832

The following is a reconciliation of pre-tax income (loss) per the financial statements to taxable income (loss) (in thousands):

Year Ended December 31, 1997 1998 1999

Pre-tax income (loss) per books	$ (566)	$(1,455)	$ 1,990
Differences between book and tax:			
Distributor revenue deferral (net)	166	13	1,432
Changes in non-deductible reserves and accruals	(181)	672	2,270
Non-deductible deferred stock compensation	--	42	2,895
Other	59	(6)	53
Taxable income (loss)	$ (522)	$ (734)	$ 8,640

Deferred tax assets comprise the following (in thousands):

December 31, 1998 1999

Inventory reserves	$ 93	$ --
Deferred revenue	560	830
Other reserves & accruals	372	1,590
	1,025	2,420
Valuation allowance	(659)	--

$ 366 $ 2,420

In assessing the realizability of deferred tax assets, management has allocated, to the extent the Company does not have carryback rights, a valuation allowance at December 31, 1998. The ultimate realization of deferred tax assets at December 31, 1999 is dependent upon the generation of future taxable income during the periods in which temporary differences representing net future deductible amounts become deductible.

Sonicwall, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued) Note 8--Segment Reporting The Company adopted SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information." SFAS No.131 requires publicly held companies to report financial and other information about key revenue segments of the entity for which such information is available and is utilized by the chief operating decision maker. The Company conducts its business within one business segment.

Revenue by geographic region is presented as follows (in thousands):

Year Ended December 31, 1997 1998 1999 United States..... $5,986 $5,080 $13,859 Other..... 3,356 2,435 7,188 Total..... $9,342 $7,515 $21,047 Revenue to any one foreign country did not exceed 10% of total revenue in 1997 and 1998. Revenue attributed to Japan accounted for 11% of total revenue for the year ended December 31, 1999.

Note 9--Commitments and Contingencies:

In September 1999 the Company entered into a 5-year operating lease agreement for a new location for its facility which it began occupying in October 1999. Rent expense was approximately $118,000, $163,000 and $383,000, for the years ended December 31, 1997, 1998 and 1999, respectively.

Future minimum lease commitments at December 31, 1999 were as follows:

Year ending December 31,

2000	$ 527,000
2001	547,000
2002	566,000
2003	585,000
2004	450,000
	$ 2,675,000

The Company is involved in various threatened legal actions arising in the ordinary course of business. Management believes that the outcome of these actions will not have a material adverse effect on the Company's financial position, cash flows or results of operations.

Prospective investors may rely only on the information contained in this prospectus. Neither SonicWALL nor any underwriter has authorized anyone to provide prospective investors with different or additional information. This prospectus is not an offer to sell nor is it seeking offers to buy shares of common stock in any jurisdiction where offers and sales are not permitted. The information contained in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or of any sale of our common stock.

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Logo

Common Stock

Prospectus

Bear, Stearns & Co. Inc.

J.P. Morgan & Co.

Chase H&Q

Thomas Weisel Partners LLC Pacific Growth Equities, Inc.

March , 2000

Part Ii

Information Not Required in Prospectus

Item 13. Other Expenses of Issuance and Distribution The following table states the costs and expenses, other than the underwriting discounts and commissions, payable by the registrant in connection with the sale of the common stock being registered by this registration statement. All amounts shown are estimates, except the Securities and Exchange Commission registration fee, the NASD filing fee and the Nasdaq National Market listing fee.

Securities and Exchange Commission registration fee..... $ 90,255 NASD filing fee..... $ 30,500 Nasdaq National Market listing fee..... $ 17,500 Blue Sky fees and expenses..... $ 7,500 Printing and engraving expenses..... $232,500 Legal fees and expenses..... $150,000 Accounting fees and expenses..... $150,000 Transfer Agent and Registrar fees..... $ 10,000 Miscellaneous expenses..... $ 92,683 Total..... $780,938 Item 14. Indemnification of Directors and Officers Section 317 of the California General Corporation Law authorizes a court to award, or a corporation's Board of Directors to grant, indemnification to directors and officers in terms sufficiently broad to permit such indemnification under certain circumstances for liabilities (including reimbursement for expenses incurred) arising under the Act. Article V of the Registrant's Amended and Restated Articles of Incorporation (Exhibit 3.1 hereto) provides for indemnification of its directors and officers to the maximum extent permitted by the California General Corporation Law, and Article VI of the Registrant's Bylaws (Exhibit 3.2 hereto) provides for indemnification of its directors, officers, employees and other agents to the maximum extent permitted by the California General Corporation Law. In addition, the Registrant has entered into Indemnification Agreements (Exhibit 10.4 hereto) with its directors and officers containing provisions that are in some respects broader than the specific indemnification provisions contained in the California General Corporation Law. The indemnification agreements may require the Registrant, among other things, to indemnify its directors and officers against certain liabilities that may arise by reason of their status or service as directors of officers (other than liabilities arising from willful misconduct of a culpable nature), to advance their expenses incurred as a result of any proceeding against them as to which they could be indemnified, and to obtain directors' and officers' insurance if available on reasonable terms. Reference is also made to Section 7 of the Underwriting Agreement contained in Exhibit 1.1 hereto, which indemnifies officers and directors of the Registrant against certain liabilities.

Item 15. Recent Sales of Unregistered Securities Since August 1, 1996, SonicWALL, Inc. has issued and sold the following securities:

(1) SonicWALL, Inc. issued and sold 2,586,556 shares of its common stock to officers, directors, employees and consultants for an aggregate purchase price of approximately $630,630 pursuant to the exercise of options under its 1994 Stock Option Plan and 1998 Stock Option Plan.

(2) On August 10, 1998, SonicWALL, Inc. issued an aggregate of 5,426,184 shares of its common stock to Ravi Anne, Sreekanth Ravi, Sudhakar Ravi and Bruce Wonnacott, each a general partner of AckFin, a California general partnership, in consideration of the purchase of all of the general partner interests of AckFin and $150,000 cash.

(3) On December 29, 1998, SonicWALL, Inc. issued an aggregate of 250,000 shares of its common stock for an aggregate purchase price of $37,500 to Jerrold F. Petruzzelli, a director of SonicWALL, Inc., Pratibha and Mahi DeSilva and Ankineedu and Suseela Ravi, relatives of Sreekanth and Sudhakar Ravi.

(4) On February 19, 1999, SonicWALL, Inc. issued an aggregate of 1,438,377 shares of its redeemable Series A convertible preferred stock for an aggregate purchase price of $4,999,998.39 to Bay Partners SBIC II, L.P., Freidenrich Family Partnership, Dempsey Family Limited Partnership, Robert M. Williams and Margaret R. Caldwell, and Kathryn S. Wunsch, TTE Justin Yesil Wickett Trust and Troy Kevork Wickett Trust. Robert M. Williams is a director of the Company.

The issuances described in paragraph 1 were deemed exempt from registration under the Act in reliance upon Rule 701 promulgated under the Act. The issuances of the securities described in paragraphs 2 through 4 were deemed to be exempt from registration under the Act in reliance on Section 4(2) of the Act as transactions by an issuer not involving any public offering. In addition, the recipients of securities in each such transaction represented their intentions to acquire the securities for investment only and not with a view to or for sale in connection with any distribution thereof and appropriate legends were affixed to the share certificates issued in such transactions. All recipients had adequate access, through their relationships with SonicWALL, Inc., to information about SonicWALL, Inc.

No underwriters were used in connection with these sales and issuances.

Item 16. Exhibits and Financial Statement Schedules (a) Exhibits Number Description 1.1** Form of Underwriting Agreement. 3.1* Registrant's Amended and Restated Articles of Incorporation. 3.2* Registrant's Restated Bylaws. 4.1* Registrant's specimen common stock certificate. 4.2* Investor Rights Agreement dated February 19, 1999 by and between Registrant and the investors named therein. Legal opinion of Manatt, Phelps & Phillips, LLP, counsel for the 5.1 Registrant. 10.1* Registrant's 1994 Stock Option Plan. 10.2* Registrant's 1998 Stock Option Plan. 10.3* Registrant's 1999 Employee Stock Option Plan. 10.4* Form of Indemnity Agreement entered into by Registrant with each of its executive officers and directors. Loan and Security Agreement dated May 26, 1995 between Registrant and 10.5* Comerica Bank. OEM License Agreement dated January 27, 1999 between Registrant and 10.6++* Com21, Incorporated. OEM Purchase Agreement dated January 5, 1999 between Registrant and

10.7++* Ramp Networks. 10.8++* Distribution Agreement dated February 9, 1999 between Registrant and Tech Data Product Management, Inc. 10.9++* Distribution Agreement dated July 5, 1998 between Registrant and Sumitomo Metal Systems Development Co. Distribution Agreement dated November 11, 1992 between Registrant and 10.10++* Ingram Micro, Inc. Agreement of Sublease dated as of October 26, 1998 between Registrant 10.11* and AMP Incorporated.

Number Description

10.12++*	OEM Purchase and Development Agreement between 3COM Corporation and Registrant effective July 1, 1999. Purchase Agreement dated September 28, 1999 between Registrant and
10.13*	Flash Electronics, Inc.
10.14*	Lease dated September 27, 1999 by and between AMB Property, L.P. as Landlord and SonicWALL, Inc. as tenant.
23.1	Consent of Independent Accountants.
23.2	Consent of Manatt, Phelps & Phillips, LLP (see Exhibit 5.1).
24.1	Power of Attorney (contained on signature page).
27.1	Financial Data Schedule.

* Incorporated by reference to the Registrant's Registration Statement on Form S-1 (No. 333-85997), which became effective on November 9, 1999. ** To be filed by amendment. ++ Confidential treatment has been requested for portions of this exhibit. The omitted material has been separately filed with the Securities and Exchange Commission.

(b) Financial Statement Schedules Schedule I--Report of Independent Accountants Schedule II--Valuation and Qualifying Accounts and Reserves All financial statement schedules not listed are omitted because they are inapplicable or the requested information is shown in the financial statements of the registrant or in the related notes to the financial statements.

Item 17. Undertakings Insofar as indemnification for liabilities arising under the Act may be permitted to directors, officers and controlling persons of the registrant pursuant to the foregoing provisions, or otherwise, the registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Act, and is therefore unenforceable. If a claim for indemnification against such liabilities (other than the payment by the registrant of expenses incurred or paid by a director, officer or controlling person of the registrant in the successful defense of any action, suit or proceeding) is asserted against such director, officer or controlling person in connection with the securities being registered, the registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question of whether such indemnification by it is against public policy as expressed in the Act, and will be governed by the final adjudication of such issue.

The undersigned registrant hereby undertakes to provide to the underwriters at the closing specified in the Underwriting Agreement, certificates in such denominations and registered in such names as required by the underwriters to permit prompt delivery to each purchaser.

The undersigned registrant hereby undertakes that:

(1) for purposes of determining any liability under the Act, the information omitted from the form of prospectus filed as part of this registration statement in reliance upon Rule 430A and contained in a form of prospectus filed by the registrant pursuant to Rule 424(b)(1) or (4) or 497(h) under the Act shall be deemed to be part of this registration statement as of the time it was declared effective; and (2) for the purpose of determining any liability under the Act, each post-effective amendment that contains a form of prospectus shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

Signatures

Pursuant to the requirements of the Securities Act of 1933, as amended, the registrant has duly caused this Registration Statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Sunnyvale, State of California, on the 23rd day of February, 2000.

SonicWALL, Inc.

/s/ Sreekanth Ravi By: _____ Sreekanth Ravi, President and Chief Executive Officer KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Sreekanth Ravi and Michael J. Sheridan jointly and severally, his attorneys-in-fact, each with the power of substitution and each with power to act alone, for him in any and all capacities, to sign any amendments to this Registration Statement, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereto ratifying and confirming all that each of said attorneys-in-fact, or his substitute or substitutes, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Act of 1933, as amended, this Registration Statement has been signed by the following persons in the capacities and on the dates indicated below:

Signature Title Date

/s/ Sreekanth Ravi _____ Sreekanth Ravi	President, Chief Executive Officer and Director (Principal Executive Officer)	February 23, 2000

/s/ Sudhakar Ravi Chief Technical Officer February 23, 2000 _____ and Director Sudhakar Ravi /s/ Robert M. Williams Director February 23, 2000 Robert M. Williams /s/ David A. Shrigley Director February 23, 2000 David A. Shrigley /s/ Jerrold F. Petruzzelli Director February 23, 2000 Jerrold F. Petruzzelli /s/ Michael J. Sheridan Vice President, Finance February 23, 2000 _____ and Chief Financial Michael J. Sheridan Officer and Secretary (Principal Financial and Accounting Officer)

Schedule I

Report of Independent Accountants

In connection with our audits of the consolidated financial statements of SonicWall, Inc. as of December 31, 1998 and 1999 and for each of the three years in the period ended December 31, 1999, which financial statements are included in the Prospectus, we have also audited the financial statement schedule listed in Item 16 herein.

In our opinion, this financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respects, the information required to be included therein.

/s/ PricewaterhouseCoopers LLP San Jose, California January 13, 2000

Schedule Ii

SonicWALL, Inc. VALUATION AND QUALIFYING ACCOUNTS (in thousands)

	Balance at Beginning of Period	Charged to Cost and Expenses	Write-off of Accounts	Balance at End of Period
Year ended December 31, 1997				
Allowance for doubtful accounts...	$ 69	$ 52	$ --	$121
Year ended December 31, 1998				
Allowance for doubtful accounts...	121	122	50	193
Year ended December 31, 1999				
Allowance for doubtful accounts...	193	366	11	548

Index to Exhibits

Number Description

1.1**	Form of Underwriting Agreement.
3.1*	Registrant's Amended and Restated Articles of Incorporation.
3.2*	Registrant's Restated Bylaws.
4.1*	Registrant's specimen common stock certificate.
4.2*	Investor Rights Agreement dated February 19, 1999 by and between Registrant and the investors named therein.
5.1	Opinion of Manatt, Phelps & Phillips, LLP as to the legality of the shares.
10.1*	Registrant's 1994 Stock Option Plan.
10.2*	Registrant's 1998 Stock Option Plan.
10.3*	Registrant's 1999 Employee Stock Option Plan.
10.4*	Form of Indemnity Agreement entered into by Registrant with each of its executive officers and directors.
10.5*	Loan and Security Agreement dated May 26, 1995 between Registrant and Comerica Bank.
10.6++*	OEM License Agreement dated January 27, 1999 between Registrant and Com21, Incorporated.
10.7++*	OEM Purchase Agreement dated January 5, 1999 between Registrant and Ramp Networks.

10.8++*	Distribution Agreement dated February 9, 1999 between Registrant and Tech Data Product Management, Inc.
10.9++*	Distribution Agreement dated July 5, 1998 between Registrant and Sumitomo Metal Systems Development Co.
10.10++*	Distribution Agreement dated November 11, 1992 between Registrant and Ingram Micro, Inc.
10.11*	Agreement of Sublease dated as of October 26, 1998 between Registrant and AMP Incorporated.
10.12++*	OEM Purchase and Development Agreement between 3COM Corporation and Registrant effective July 1, 1999.
10.13*	Purchase Agreement dated September 28, 1999 between Registrant and Flash Electronics, Inc.
10.14*	Lease dated September 27, 1999 by and between AMB Property, L.P. as Landlord and SonicWALL, Inc. as Tenant.
23.1	Consent of Independent Accountants.
23.2	Consent of Manatt, Phelps & Phillips, LLP (see Exhibit 5.1).
24.1	Power of Attorney (contained on signature page).
27.1	Financial Data Schedule.

* Incorporated by reference to the Registrant's Registration Statement on Form S-1 (No. 333-85997), which became effect on November 9, 1999. ** To be filed by Amendment. ++ Confidential treatment has been requested for portions of this exhibit. The omitted material has been separately filed with the Securities and Exchange Commission. </TEXT>