CSG SYSTEMS INTERNATIONAL INC
Form 10-K
March 01, 2007
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2006

OR

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

For the transition period from to

Commission file number 0-27512

CSG SYSTEMS INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Delaware **(State or other jurisdiction of incorporation or organization)**	47-0783182 **(I.R.S. Employer Identification No.)**

9555 Maroon Circle

Englewood, Colorado 80112

(Address of principal executive offices, including zip code)

(303) 200-2000

(Registrant s telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:

Common Stock, Par Value $0.01 Per Share

Securities Registered Pursuant to Section 12(g) of the Act: None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ¨ No x

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, computed by reference to the last sales price of such stock, as of the close of trading on June 30, 2006 was $1,041,037,528.

Shares of common stock outstanding at February 26, 2007: 45,350,947

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s Proxy Statement for its 2007 Annual Meeting of Stockholders to be filed on or prior to April 30, 2007, are incorporated by reference into Part III of the Form 10-K.

Table of Contents

CSG SYSTEMS INTERNATIONAL, INC.

2006 FORM 10-K

TABLE OF CONTENTS

Table of Contents

Item 1. Business
Overview

CSG Systems International, Inc. (the Company , CSG , or forms of the pronoun we) was formed in October 1994 and acquired all of the outstanding stock of CSG Systems, Inc. (formerly Cable Services Group, Inc.) from First Data Corporation (FDC) in November 1994. CSG Systems, Inc. had been a subsidiary or division of FDC from 1982 until this acquisition.

We are a leading provider of outsourced billing, customer care and print and mail solutions and services supporting the North American cable and direct broadcast satellite (DBS) markets. Our solutions support some of the world s largest and most innovative providers of bundled multi-channel video, Internet, voice and IP-based services. Our unique combination of solutions, services and expertise ensure that cable and satellite operators can continue to rapidly launch new service offerings, improve operational efficiencies and deliver a high-quality customer experience in a competitive and ever-changing marketplace.

Our principal executive offices are located at 9555 Maroon Circle, Englewood, Colorado 80112, and the telephone number at that address is (303) 200-2000. Our common stock is listed on the Nasdaq Stock Market LLC under the symbol CSGS . We are a S&P Midcap 400 company.

General Development of Business

Comcast Business Relationship. In September 1997, we entered into a 15-year exclusive contract (the Master Subscriber Agreement) with Tele-Communications, Inc. (TCI) to consolidate all TCI customers onto our customer care and billing systems. At the same time, we acquired a non-operational billing system from TCI for $105 million. This transaction allowed our company to substantially increase the number of customers processed on our systems, and at the time, was one of the catalysts to the growth of our domestic broadband business.

In 1999 and 2000, respectively, AT&T completed its mergers with TCI and MediaOne Group, Inc. (MediaOne), and consolidated the merged operations into AT&T Broadband (AT&T), and we continued to service the merged operations under the terms of the Master Subscriber Agreement. On November 18, 2002, Comcast Corporation (Comcast) completed its merger with AT&T, and assumed the Master Subscriber Agreement. Comcast is our largest client, making up approximately 24% of our total revenues in 2006.

During 2002 and 2003, we were involved in various legal proceedings with Comcast, consisting principally of arbitration proceedings related to the Master Subscriber Agreement. In October 2003, we received an unfavorable ruling in the arbitration proceedings. The Comcast arbitration ruling included an award of $119.6 million to be paid by us to Comcast. The award was based on the arbitrator s determination that we had violated the most favored nations (MFN) clause of the Master Subscriber Agreement. We recorded the full impact from the arbitration ruling in the third quarter of 2003 as a charge to revenues. In addition, the arbitration ruling also required that we invoice Comcast for lower fees under the MFN clause of the Master Subscriber Agreement beginning in October 2003. This had the effect of reducing quarterly revenues from Comcast by approximately $13-14 million ($52-56 million annually), when compared to amounts prior to the arbitration ruling. In March 2004, we signed a new contract with Comcast (the Comcast Contract). The Comcast Contract superseded the former Master Subscriber Agreement that was set to expire at the end of 2012. Under the new agreement, we expect to continue to provide services to Comcast at least through December 31, 2008. The pricing inherent in the Comcast Contract was consistent with that of the arbitration ruling in October 2003. See Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) for additional discussion of our business relationship with Comcast.

Purchase and Sale of the GSS Business. In February 2002, we acquired the billing and customer care assets of Lucent Technologies (Lucent). Lucent s billing and customer care business consisted primarily of: (i) software products and related consulting services acquired by Lucent when it purchased Kenan Systems Corporation in February 1999; (ii) BILLDATS Data Manager mediation software; and (iii) elements of Lucent s client support, product support, and sales and marketing organizations (collectively, the Kenan Business). This acquisition allowed us to expand our customer care and billing product and service offerings into international markets. On December 9, 2005, we sold our Global Software Services (GSS)

Table of Contents

business (GSS Business), which consisted principally of the acquired Kenan Business, to Comverse, Inc., a division of Comverse Technology, Inc. (Comverse). As a result of our sale of the GSS Business, we no longer provide customer care and billing products or services outside of North America. The decision to sell the GSS Business is consistent with our decision to intensify our focus on our core competencies in the cable and DBS markets utilizing our Advanced Convergent Platform (ACP) product and related services. See Note 2 to our Consolidated Financial Statements and MD&A for additional discussion of the sale of the GSS Business.

Financial Information About Our Company and Business Segment

In addition to the sale of the GSS Business noted above, we also sold our plaNet Consulting business to a group of private investors led by the plaNet management team on December 30, 2005. As a result, the results of operations for the GSS and plaNet businesses have been reflected as discontinued operations for all periods presented in the accompanying Consolidated Statements of Income. The remainder of the Business section of this Form 10-K is focused on our continuing operations. See Notes 2 and 5 to our Consolidated Financial Statements and MD&A for additional discussion of our reporting of discontinued operations, and the impact these sales had on our reporting of segment and related information.

Industry Overview

Background. We provide customer care and billing services primarily to the North American converged broadband and DBS markets. Customer care and billing systems coordinate many aspects of the customer s interaction with a service provider, from the initial set-up and activation of customer accounts, to the support of various service activities, through the monitoring of customer invoicing and accounts receivable management, and the presentment of customer invoices. These systems enable service providers to manage the lifecycle of their customer interactions.

Market Conditions of Communications Industry. The North American communications industry has experienced significant consolidation and increased competition among communications providers, and there is the possibility of further consolidation. Market consolidation results in a fewer number of service providers who have massive scale and can deliver a total communications package. The significant plant upgrades and network rationalizations that have taken place have allowed service providers to focus their attention on new revenue and growth opportunities. In addition, new competitors, new technologies and unique partnerships are forcing service providers to be more creative in their approaches for rolling out new products and services and enhancing their customers experiences. These factors, in combination with the improving financial condition of service providers, are resulting in a more positive outlook for the demand for scalable, flexible and cost efficient customer care and billing solutions, which we believe will provide us with new revenue opportunities.

However, another facet of this market consolidation poses certain risks to our company. The consolidation of service providers decreases the potential number of buyers for our products and services, and carries the inherent risk that the consolidators may choose to move their purchased customers to a competitor s system. Should this consolidation result in a concentration of customer accounts being owned by companies with whom we do not have a relationship, or with whom competitors are entrenched, it could negatively affect our ability to maintain or expand our market share, thereby having a material adverse effect to our results of operations. In addition, service providers at times have chosen to use their size and scale to exert more pressure on pricing negotiations.

In addition, it is widely anticipated that communication service providers will continue their aggressive pursuit of providing convergent services. Traditional wireline and wireless telephone providers have recently entered the residential video market, a market dominated by our clients. Should these traditional telephone service providers be successful in their video strategy, it could threaten our clients market share, and thus our processing revenues, as generally speaking, these companies do not currently use our products and services.

Business Strategy

Our business strategy is designed to achieve revenue and profit growth. The key elements of our business strategy include:

Expand Core Processing Business. We will continue to leverage our investment and expertise in high-volume transaction processing to expand our processing business. Our processing business provides highly predictable, recurring revenues

4

Table of Contents

through multi-year contracts with a client base that includes leading communications service providers. We increased the number of customers processed on our systems from 18 million as of December 31, 1995 to 45.4 million as of December 31, 2006. We provide a full suite of customer care and billing products and services that combine the reliability and high volume transaction processing capabilities of a mainframe platform with the flexibility of client/server architecture.

Increase the Penetration of Ancillary Products/Services. We provide a complete suite of customer care and billing products and services that enable and automate various activities for service providers, ranging from the call center, to the field technicians, to the end consumer. As our clients businesses consolidate and become much more complex, we have seen an increase in the use of ancillary products and services.

Evolve Our Products and Services to Meet the Changing Needs of Our Clients. In 1995, we offered customer care and billing solutions to providers of analog cable video. Since then, our solution has evolved and expanded to satellite, digital, high-speed Internet (HSI) and digital voice. Our clients continue to look to add more services to their product bundle, including advanced IP and wireless services, as well as services to commercial customers. Our continued investment in our solution set is designed to enable our clients to grow their product offerings, and thereby, grow our revenues.

Enhance Growth Through Focused Acquisitions. We follow a disciplined approach in acquiring assets and businesses which provide the technology and technical personnel to expedite our product development efforts, provide complementary products and services, increase market share, and/or provide access to new markets and clients.

Continue Technology Leadership. We believe that our technology in customer care and billing solutions gives communications service providers a competitive advantage. Our continuing investment in research and development (R&D) is designed to position us to meet the growing and evolving needs of existing and potential clients. Over the last five years, we have invested approximately $175 million, or approximately 10% of our total revenues, into R&D.

Narrative Description of Business

General Description. Our operations consist of our processing operations and the provision of related software products. We generate a substantial percentage of our revenues by providing outsourced customer care and billing services to the North American cable television and satellite industries. Our full suite of processing, software, and professional services allows clients to automate their customer interaction management and billing functions. These functions include such things as set-up and activation of customer accounts, sales support, order processing, invoice calculation, production and mailing of invoices, management reporting, electronic presentment and payment of invoices, and deployment and management of the client s field technicians.

Clients. We work with the leading cable and satellite providers located in the U.S. and Canada. A partial list of those service providers as of December 31, 2006 is included below:

Charter Communications (Charter)	EchoStar Communications Corporation (EchoStar)
Comcast Corporation (Comcast)	Mediacom Communications
Cox Communications	Time Warner Inc. (Time Warner)

As discussed above, the North American communications industry has experienced significant consolidation over the last few years, resulting in a large percentage of the market being served by a limited number of service providers with greater size and scale. Consistent with this market concentration, a large percentage of our historical revenues have been generated from a limited number of clients, with approximately 70% of our revenues being generated from our four largest clients, which include Comcast, EchoStar, Time Warner, and Charter. Revenues from these clients represented the following percentages of our total revenues for 2006 and 2005:

	2006	2005
Comcast	24%	22%
EchoStar	19%	21%
Time Warner	12%	10%

Charter	11%	10%

Table of Contents

CCS Architectural Upgrade and Migration. During 2004, we completed a significant architectural upgrade to our primary product, CCS, and related services and software products. This enhancement to CCS, called ACP, has enhanced our ability to support convergent broadband services including cross-service bundling, convergent order entry and advanced service provisioning capabilities for video, HSI, and Voice over Internet Protocol (VoIP). This advanced convergent solution for broadband service providers will facilitate our clients offering of combinations of video, voice and data services (commonly referred to in the industry as the triple-play service offering). The ACP project was initiated in 2002 and is our next generation product offering. As of December 31, 2006, approximately 90% of the cable customer accounts processed on our systems have successfully migrated to our ACP solution, and we expect the remaining cable customer accounts to be migrated to ACP by the end of 2007.

Products and Services. Our primary product offerings include our core service bureau processing product, ACP, and related services and software products. A background in high-volume transaction processing, complemented with world-class applications software, allows us to offer one of the most comprehensive, pre-integrated products and services solutions to the communications market, serving video, data and voice providers and handling many aspects of the customer lifecycle. We believe this pre-integrated approach has allowed communications service providers to get to market quickly as well as reduce the total cost of ownership for their solution.

We license our software products (e.g., ACSR, Workforce Express, etc.) and provide our professional services principally to our existing base of processing clients to enhance the core functionality of our service bureau processing application, increase the efficiency and productivity of the clients operations, and allow clients to effectively roll out new products and services to new and existing markets, such as HSI and telephony to residential and commercial customers.

Historically, a substantial percentage of our total revenues have been generated from ACP processing services and related software products. These products and services are expected to provide a substantial percentage of our total revenues in the foreseeable future as well.

FDC Data Processing Facility. We outsource to FDC the data processing and related computer services required for the operation of our processing services. Our ACP proprietary software is run in FDC s facility to obtain the necessary mainframe computer capacity and other computer support services without us having to make the substantial capital and infrastructure investments that would be necessary for us to provide these services internally. Our clients are connected to the FDC facility through a combination of private and commercially-provided networks. Our service agreement with FDC expires June 30, 2010, and is cancelable only for cause, as defined in the agreement. We believe we could obtain mainframe data processing services from alternative sources, if necessary. We have a business continuity plan as part of our agreement with FDC should the FDC data processing center suffer an extended business interruption or outage. This plan is tested on an annual basis.

Client and Product Support. Our clients typically rely on us for ongoing support and training needs related to our products. We have a multi-level support environment for our clients. We have strategic business units (SBUs) to support the business, operational, and functional requirements of each client. These dedicated account management teams help clients resolve strategic and business issues and are supported by our Product Support Center (PSC), which operates 24 hours a day, seven days a week. Clients call an 800 number, and through an automated voice response unit, have their calls directed to the appropriate PSC personnel to answer their questions. We have a full-time training staff and conduct ongoing training sessions both in the field and at our training facilities.

Sales and Marketing. We organize our sales efforts to existing clients within our SBUs, with senior level account managers who are responsible for new revenues and renewal of existing contracts within a client account. The SBUs are supported by sales support personnel who are experienced in the various products and services that we provide. In addition, we have dedicated staff engaged in selling our products and services to prospective clients.

Competition. The market for customer care and billing products and services in the converging communications industry in North America is highly competitive. We compete with both independent outsourced providers and in-house developers of customer management systems. We believe that our most significant competitors are Amdocs Limited, Convergys Corporation, and in-house systems. Some of our actual and potential competitors have substantially greater financial, marketing and technological resources than us.

Table of Contents

We believe service providers in our industry use the following criteria when selecting a vendor to provide customer care and billing products and services: (i) functionality, scalability, flexibility and architecture of the billing system; (ii) the breadth and depth of pre-integrated product solutions: (iii) product quality, client service and support; (iv) quality of R&D efforts; and (v) price. We believe that our products and services allow us to compete effectively in these areas.

Proprietary Rights and Licenses

We rely on a combination of trade secret and copyright laws, nondisclosure agreements, and other contractual and technical measures to protect our proprietary rights in our products. While we hold a limited number of patents on some of our newer products, we do not rely upon patents as a primary means of protecting our rights in our intellectual property. There can be no assurance that these provisions will be adequate to protect our proprietary rights. Although we believe that our intellectual property rights do not infringe upon the proprietary rights of third parties, there can be no assurance that third parties will not assert infringement claims against us or our clients.

We continually assess whether there is any risk to our intellectual property rights. Should these risks be improperly assessed, or if for any reason should our right to develop, produce and distribute our products be successfully challenged or be significantly curtailed, it could have a material adverse impact on our financial condition and results of operations.

Research and Development

Our product development efforts are focused on developing new products and improving our existing products. We believe that the timely development of new applications and enhancements to existing applications is essential to maintaining our competitive position in the marketplace. Our most recent development efforts have been focused primarily on enhancements to ACP and related software products, to include the integration of the Telution COMX product with ACP (see Note 4 to our Consolidated Financial Statements for a discussion of our Telution acquisition), targeted to increase the functionalities and features of the products, including those necessary to service new and expanded product offerings provided by our clients (e.g., VoIP commercial services, etc.).

Our total R&D expenses were $46.2 million and $33.9 million, respectively, for 2006 and 2005, or approximately 12% and 9% of total revenues. Over the last five years, we have invested approximately 10% of our total revenues into R&D. We expect our future R&D efforts to continue to focus on enhancements to ACP and related products and services, and we expect that over time, our investment in R&D will approximate our historical investment rate of 10-12% of our total revenues. However, consistent with the fourth quarter of 2006 (which reflected R&D expense as a percentage of total revenues of approximately 14%), we expect this percentage to be at or above the top end of this range in the near term.

There are certain inherent risks associated with significant technological innovations. Some of these risks are described in this report in our Risk Factors section below.

Employees

As of December 31, 2006, we had a total of 1,685 employees, an increase of 145 from December 31, 2005. The increase in number of employees is due to an expected increase in our R&D and support function costs to address the opportunities we see within our clients   changing business needs, to include the personnel that came over in the Telution acquisition. Our success is dependent upon our ability to attract and retain qualified employees. None of our employees are subject to a collective bargaining agreement. We believe that our relations with our employees are good.

Available Information

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy materials, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act are available free of charge on our website at www.csgsystems.com. Additionally, these reports are available at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549 or on the SEC s website at www.sec.gov. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330.

7

Table of Contents

Code of Business Conduct and Ethics

A copy of our Code of Business Conduct and Ethics (the Code of Conduct) is maintained on our website. Any future amendment to the Code of Conduct, or any future waiver of a provision of our Code of Conduct, will be timely posted to our website upon their occurrence. Historically, we have had minimal changes to our Code of Conduct, and have had no waivers of a provision of our Code of Conduct.

Item 1A. Risk Factors

We or our representatives from time-to-time may make or may have made certain forward-looking statements, whether orally or in writing, including without limitation, any such statements made or to be made in MD&A contained in our various SEC filings or orally in conferences or teleconferences. We wish to ensure that such statements are accompanied by meaningful cautionary statements, so as to ensure, to the fullest extent possible, the protections of the safe harbor established in the Private Securities Litigation Reform Act of 1995.

Accordingly, the forward-looking statements are qualified in their entirety by reference to and are accompanied by the following meaningful cautionary statements identifying certain important risk factors that could cause actual results to differ materially from those in such forward-looking statements. This list of risk factors is likely not exhaustive. We operate in a rapidly changing and evolving market involving the North American communications industry (e.g., bundled multi-channel video, Internet, voice and IP-based services), and new risk factors will likely emerge. Management cannot predict all of the important risk factors, nor can it assess the impact, if any, of such risk factors on our business or the extent to which any risk factor, or combination of risk factors, may cause actual results to differ materially from those in any forward-looking statements. Accordingly, there can be no assurance that forward-looking statements will be accurate indicators of future actual results, and it is likely that actual results will differ from results projected in forward-looking statements and that such differences may be material.

We Derive a Significant Portion of Our Revenues From a Limited Number of Clients, and the Loss of the Business of a Significant Client Would Materially Adversely Affect Our Financial Condition and Results of Operations. The North American communications industry has experienced significant consolidation over the last few years, resulting in a large percentage of the market being served by a limited number of service providers with greater size and scale. Consistent with this market concentration, a large percentage of our revenues are generated from a limited number of clients, with approximately 70% of our revenues being generated from our four largest clients, which are (in order of size) Comcast, EchoStar, Time Warner, and Charter. See MD&A for a brief summary of our business relationship with each of these clients.

There are inherent risks whenever a large percentage of total revenues are concentrated with a limited number of clients. One such risk is that, should a significant client: (i) terminate or fail to renew their contracts with us, in whole or in part for any reason; (ii) significantly reduce the number of customer accounts processed on our systems, the price paid for our services, or the scope of services that we provide; or (iii) experience significant financial or operating difficulties, it could have a material adverse effect on our financial condition and results of operations (including possible impairment, or significant acceleration of the amortization of intangible assets).

Our industry is highly competitive, and the possibility that a major client may move all or a portion of its customers to a competitor has increased. While our clients may incur some costs in switching to our competitors, they may do so for a variety of reasons, including if we do not maintain favorable relationships, do not provide satisfactory services and products, or for reasons associated with price.

A Reduction in Demand for Our Key Customer Care and Billing Products and Services Could Have a Material Adverse Effect on Our Financial Condition and Results of Operations. Historically, a substantial percentage of our total revenues have been generated from our core outsourced processing product, ACP, and related services. These products and services are expected to continue to provide a large percentage of our total revenues in the foreseeable future. Any significant reduction in demand for ACP and related services could have a material adverse effect on our financial condition and results of operations, including possible impairment to intangible assets.

Table of Contents

We May Not Be Able to Respond to the Rapid Technological Changes in Our Industry. The market for customer care and billing systems is characterized by rapid changes in technology and is highly competitive with respect to the need for timely product innovations and new product introductions. As a result, we believe that our future success in sustaining and growing our revenues depends upon the continued market acceptance of our products, especially ACP, and our ability to continuously adapt, modify, maintain, and operate our products to address the increasingly complex and evolving needs of our clients, without sacrificing the reliability or quality of the products. In addition, the market is demanding that our products have greater architectural flexibility and are more easily integrated with other computer systems, and that we are able to meet the demands for technological advancements to our products and services at a greater pace. Attempts to meet these demands subjects our R&D efforts to greater risks.

As a result, substantial R&D will be required to maintain the competitiveness of our products and services in the market. Technical problems may arise in developing, maintaining and operating our products and services as the complexities are increased. Development projects can be lengthy and costly, and may be subject to changing requirements, programming difficulties, a shortage of qualified personnel, and/or unforeseen factors which can result in delays. In addition, we may be responsible for the implementation of new products and/or the migration of clients to new products, and depending upon the specific product, we may also be responsible for operations of the product.

There is an inherent risk in the successful development, implementation, migration, and operations of our products and services as the technological complexities, and the pace at which we must deliver these products and services to market, continues to increase. The risk of making an error that causes significant operational disruption to a client increases proportionately with the frequency and complexity of changes to our products and services. There can be no assurance:

- of continued market acceptance of our products and services;
- that we will be successful in the development of product enhancements or new products that respond to technological advances or changing client needs at the pace the market demands; or
- that we will be successful in supporting the implementation, migration and/or operations of product enhancements or new products.

Our Business is Dependent on the North American Communications Industry. We generate our revenues by providing products and services to the U.S. and Canadian communication industries. A decrease in the number of customers served by our clients, loss of business due to non-renewal of client contracts, industry and client consolidations, an adverse change in the economic condition of these industries, movement of customers from our systems to a competitor s system as a result of regionalization strategies by our clients, and/or changing consumer demand for services could have a material adverse effect on our results of operations. Additionally, our current clients distribution methods could be disrupted by new entrants into the communications industry. There can be no assurance that new entrants into the communications market will become our clients. Also, there can be no assurance that communication providers will be successful in expanding into other segments of the converging communications industry. Even if major forays into new markets are successful, we may be unable to meet the special billing and customer care needs of that market.

The Consolidation of the North American Communications Industry May Have a Material Adverse Effect on Our Results of Operations. The North American communications industry is undergoing significant ownership changes at an accelerated pace. One facet of these changes is that communications service providers are consolidating, decreasing the potential number of buyers for our products and services. Such client consolidations carry with them the inherent risk that the consolidators may choose to move their purchased customers to a competitor s system. Should this consolidation result in a concentration of customer accounts being owned by companies with whom we do not have a relationship, or with whom competitors are entrenched, it could negatively affect our ability to maintain or expand our market share, thereby having a material adverse effect on our results of operations. In addition, service providers may choose to use their size and scale to exercise more severe pressure on pricing negotiations.

In addition, it is widely anticipated that communication service providers will continue their aggressive pursuit of providing convergent services. Traditional wireline and wireless telephone providers have recently entered the residential

video market, a market dominated by our clients. Should these traditional telephone service providers be successful in their video strategy, it could threaten our clients market share, and thus our processing revenues, as generally speaking, these companies do not currently use our products and services.

We Face Significant Competition in Our Industry. The market for our products and services is highly competitive. We directly compete with both independent providers of products and services and in-house systems developed by existing and potential clients. In addition, some independent providers are entering into strategic alliances with other independent providers, resulting in either new competitors, or competitors with greater resources. Many of our current and potential competitors have significantly greater financial, marketing, technical, and other competitive resources than our company, many with significant and well-established domestic and international operations. There can be no assurance that we will be able to compete successfully with our existing competitors or with new competitors.

Client Bankruptcies Could Adversely Affect Our Business, and Any Accounting Reserves We Have Established May Not Be Sufficient. In the past, certain of our clients have filed for bankruptcy protection. Companies involved in bankruptcy proceedings pose greater financial risks to us, consisting principally of possible claims of preferential payments for certain amounts paid to us prior to the bankruptcy filing date, as well as increased collectibility risk for accounts receivable, particularly those accounts receivable that relate to periods prior to the bankruptcy filing date. We consider such risks in assessing our revenue recognition and the collectibility of accounts receivable related to our clients that have filed for bankruptcy protection, and for those clients that are seriously threatened with a possible bankruptcy filing. We establish accounting reserves for our estimated exposure on these items. However, there can be no assurance that our accounting reserves related to this exposure will be adequate. Should any of the factors considered in determining the adequacy of the overall reserves change adversely, an adjustment to the accounting reserves may be necessary. Because of the potential significance of this exposure, such an adjustment could be material.

We May Incur Additional Material Restructuring Charges in the Future. Since the third quarter of 2002, we have recorded restructuring charges related to involuntary employee terminations, various facility abandonments, and various other restructuring activities. The accounting for facility abandonments requires highly subjective judgments in determining the proper accounting treatment for such matters. We continually evaluate our assumptions, and adjust the related restructuring reserves based on the revised assumptions at that time. Moreover, we continually evaluate ways to reduce our operating expenses through new restructuring opportunities, including more effective utilization of our assets, workforce and operating facilities. As a result, there is a reasonable likelihood that we may incur additional material restructuring charges in the future.

Failure to Attract and Retain Our Key Management and Other Highly Skilled Personnel Could Have a Material Adverse Effect on Our Business. Our future success depends in large part on the continued service of our key management, sales, product development, and operational personnel. We believe that our future success also depends on our ability to attract and retain highly skilled technical, managerial, operational, and marketing personnel, including, in particular, personnel in the areas of R&D and technical support. Competition for qualified personnel at times can be intense, particularly in the areas of R&D, conversions, software implementations, and technical support, especially now that market conditions are improved and the demand for such talent has increased. For these reasons, we may not be successful in attracting and retaining the personnel we require, which could have a material adverse effect on our ability to meet our commitments and new product delivery objectives.

We May Not Be Successful in the Integration of Our Acquisitions. As part of our growth strategy, we seek to acquire assets, technology, and businesses which will provide the technology and technical personnel to expedite our product development efforts, provide complementary products or services, or provide access to new markets and clients.

Acquisitions involve a number of risks and difficulties, including: (i) expansion into new markets and business ventures; (ii) the requirement to understand local business practices; (iii) the diversion of management s attention to the assimilation of acquired operations and personnel; and (iv) potential adverse effects on a company s operating results for various reasons, including, but not limited to, the following items: (a) the inability to achieve revenue targets; (b) the inability to achieve certain operating synergies; (c) charges related to purchased in-process R&D projects; (d) costs incurred to exit current or acquired contracts or activities; (e) costs incurred to service any acquisition debt; and (f) the amortization or impairment of intangible assets.

Table of Contents

Due to the multiple risks and difficulties associated with any acquisition, there can be no assurance that we will be successful in achieving our expected strategic, operating, and financial goals for any such acquisition.

Failure to Protect Our Proprietary Intellectual Property Rights Could Have a Material Adverse Effect on Our Financial Condition and Results of Operations. We rely on a combination of trade secret and copyright laws, nondisclosure agreements, and other contractual and technical measures to protect our proprietary rights in our products. We also hold a limited number of patents on some of our newer products, but do not rely upon patents as a primary means of protecting our rights in our intellectual property. There can be no assurance that these provisions will be adequate to protect our proprietary rights. Although we believe that our intellectual property rights do not infringe upon the proprietary rights of third parties, there can be no assurance that third parties will not assert infringement claims against us or our clients.

We continually assess whether there are any risks to our intellectual property rights. Should these risks be improperly assessed or if for any reason should our right to develop, produce and distribute our products be successfully challenged or be significantly curtailed, it could have a material adverse effect on our financial condition and results of operations.

The Delivery of Our Products and Services is Dependent on a Variety of Computing Environments and Communications Networks, Which May Not Be Available or May Be Subject to Security Attacks. Our products and services are generally delivered through a variety of computing environments operated by us, which we will collectively refer to herein as Systems. We provide such computing environments through both out-sourced arrangements, such as our data processing arrangement with FDC, as well as internally operating numerous distributed servers in geographically dispersed environments. The end users are connected to our Systems through a variety of public and private communications networks, which we will collectively refer to herein as Networks. Our products and services are generally considered to be mission critical customer management systems by our clients. As a result, our clients are highly dependent upon the continuous availability and uncompromised security of our Networks and Systems to conduct their business operations.

Our Networks and Systems are subject to the risk of an extended interruption or outage due to many factors such as: (i) planned changes to our Systems and Networks for such things as scheduled maintenance and technology upgrades, or migrations to other technologies, service providers, or physical location of hardware; (ii) human and machine error; (iii) acts of nature; and (iv) intentional, unauthorized attacks from computer hackers. In addition, we continue to expand our use of the Internet with our product offerings thereby permitting, for example, our clients customers to use the Internet to review account balances, order services or execute similar account management functions. Allowing access to our Networks and Systems via the Internet increases their vulnerability to unauthorized access and corruption, as well as increasing the dependency of our Systems reliability on the availability and performance of the Internet s infrastructure.

As a means to mitigate certain risks in this area of our business, we have done the following: (i) established policies and procedures related to planned changes to our Systems and Networks; (ii) implemented a business continuity plan, and test certain aspects of this plan on a periodic basis; and (iii) implemented a security and data privacy program (utilizing ISO 17799 as a guideline) designed to mitigate the risk of an unauthorized access to the Networks and Systems primarily through the use of network firewalls, procedural controls, intrusion detection systems and antivirus applications. In addition, we undergo periodic security reviews of certain aspects of our Networks and Systems by independent parties.

The method, manner, cause and timing of an extended interruption or outage in our Networks or Systems are impossible to predict. As a result, there can be no assurances that our Networks and Systems will not fail, or that our business continuity plans will adequately mitigate all damages incurred as a consequence. Should our Networks or Systems: (i) experience an extended interruption or outage, (ii) have their security breached, or (iii) have their data lost, corrupted or otherwise compromised, it would impede our ability to meet product and service delivery obligations, and likely have an immediate impact to the business operations of our clients. This would most likely result in an immediate loss to us of revenue or increase in expense, as well as damaging our reputation. Any of these events could have both an immediate, negative impact upon our financial condition and our short-term revenue and profit expectations, as well as our long-term ability to attract and retain new clients.

Item 1B. Unresolved Staff Comments
None.

Item 2. Properties

As of December 31, 2006, we were operating from six leased sites in the U.S., representing approximately 493,000 square feet. This amount excludes approximately 68,000 square feet of leased space that we have abandoned.

We lease office facilities totaling approximately 100,000 square feet in Denver, Colorado and surrounding communities. We utilize these office facilities primarily for: (i) corporate headquarters; (ii) sales and marketing activities; (iii) product and operations support; and (iv) R&D activities. The leases for these office facilities expire in the years 2008 through 2015.

We lease office facilities totaling approximately 201,000 square feet in Omaha, Nebraska. We utilize these facilities primarily for (i) client services, training and product support; (ii) systems and programming activities; (iii) R&D activities; and (iv) general and administrative functions. The leases for these facilities expire in the years 2009 through 2012.

We lease an office facility totaling approximately 16,000 square feet in Chicago, Illinois. We utilize this facility primarily for: (i) R&D activities; (ii) client services; and (iii) professional services staff. The lease for this office facility expires in 2009.

We lease statement production and mailing facilities totaling approximately 176,000 square feet in Omaha, Nebraska and Wakulla County, Florida. The leases for these facilities expire in the years 2011 and 2013, respectively.

Item 3. Legal Proceedings

From time-to-time, we are involved in litigation relating to claims arising out of our operations in the normal course of business. In the opinion of our management, we are not presently a party to any material pending or threatened legal proceedings.

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

None.

Executive Officers of the Registrant

As of December 31, 2006, our executive officers were Edward C. Nafus (Chief Executive Officer and President), Randy R. Wiese (Executive Vice President and Chief Financial Officer), Peter E. Kalan (Executive Vice President of Business and Corporate Development), Robert M. (Mike) Scott (Executive Vice President and Chief Operating Officer) and Joseph T. Ruble (Executive Vice President, General Counsel and Corporate Secretary). We have employment agreements with each of the executive officers.

Edward C. Nafus

Chief Executive Officer and President

Mr. Nafus, 66, joined CSG in August 1998 as Executive Vice President and became the President of our Broadband Services Division in January 2002. In March 2005, he was added to our Board of Directors. Effective April 1, 2005, Mr. Nafus assumed the position of Chief Executive Officer and President of CSG. From 1978 to 1998, Mr. Nafus held numerous management positions within FDC. From 1992 to 1998, he served as Executive Vice President of FDC; from 1989 to 1992, he served as President of First Data International; and Executive Vice President of First Data Resources from 1984 to 1989. From 1971 to 1978, Mr. Nafus worked in sales management, training and sales for Xerox Corporation. From 1966 to 1971, Mr. Nafus was a pilot and division officer in the United States Navy. Mr. Nafus holds a BS degree from Jamestown College.

Peter E. Kalan

Executive Vice President of Business and Corporate Development

Mr. Kalan, 47, joined CSG in January 1997 and was named Chief Financial Officer in October 2000. In April 2006, he was named Executive Vice President of Business and Corporate Development. Prior to joining CSG, Mr. Kalan was Chief Financial

Table of Contents

Officer at Bank One, Chicago, and he also held various other financial management positions with Bank One in Texas and Illinois from 1985 through 1996. Mr. Kalan holds a BA degree in Business Administration from the University of Texas at Arlington.

Robert M. Scott

Executive Vice President and Chief Operating Officer

Mr. Scott, 56, joined CSG in September 1999 as Vice President of the Broadband Services Division and served as Senior Vice President of that division from 2001 to 2004. In December 2004, Mr. Scott was named Executive Vice President, and became the head of the Broadband Services Division in March 2005. In July 2006, he was named Chief Operating Officer. Prior to joining CSG, he served for 21 years in a variety of management positions, both domestically and internationally, with First Data Corporation. Mr. Scott holds a BA degree in Social Studies from Florida Atlantic University.

Randy R. Wiese

Executive Vice President and Chief Financial Officer

Mr. Wiese, 47, joined CSG in 1995 as Controller and later served as Chief Accounting Officer. He was named Executive Vice President and Chief Financial Officer in April 2006. Prior to joining CSG, he was manager of audit and business advisory services and held other accounting-related positions at Arthur Andersen & Co. Mr. Wiese is a member of the AICPA and the Nebraska Society of Certified Public Accountants. He holds a BS degree in Accounting from the University of Nebraska-Omaha.

Joseph T. Ruble

Executive Vice President, General Counsel & Corporate Secretary

Mr. Ruble, 46, joined CSG in 1997 as Vice President and General Counsel. In November 2000 he was appointed Senior Vice President of Corporate Development, General Counsel & Corporate Secretary. In February 2007, he was named Executive Vice President. Prior to joining CSG, Mr. Ruble served from 1991 to 1997 as Vice President, General Counsel & Corporate Secretary for Intersolv, Inc., and as counsel to Pansophic Systems, Inc. for its international operations from 1988 to 1991. Prior to that, he represented the software industry in Washington, D.C. on legislative matters. Mr. Ruble holds a JD from Catholic University of America and a BS degree from Ohio University.

Board of Directors of the Registrant

Effective November 16, 2006, our Board of Directors increased the number of directors of our company from seven to eight by adding a Class II director and elected Mr. Ronald Cooper to fill such additional director position.

Information related to our Board of Directors is provided below.

Bernard W. Reznicek

Consultant

The Premier Group

Mr. Reznicek, 70, was elected to the Board in January 1997 and presently serves as the Company s non-executive Chairman of the Board. He currently provides consulting services through Premier Enterprises. Mr. Reznicek previously was an Executive with Central States Indemnity Company of Omaha, a Berkshire Hathaway company, from 1997 to 2003. He has 40 years of experience in the electric utility industry, having served as Chairman, President and Chief Executive Officer of Boston Edison Company and President and Chief Executive Officer of Omaha Public Power District. Mr. Reznicek currently is a director of Pulte Homes, Inc. (NYSE) and infoUSA Inc. (NASDAQ).

Edward C. Nafus

Chief Executive Officer and President

CSG Systems International, Inc.

Mr. Nafus biographical information in included in Executive Officers of the Registrant section shown directly above.

Table of Contents

Ronald Cooper

Former President and Chief Operating Officer

Adelphia Communications

Mr. Cooper, 49, was elected to the Board in November 2006. He has spent nearly 25 years in the cable and telecommunications industry, most recently at Adelphia Communications where he served as President and Chief Operating Officer from 2003 to 2006. Prior to Adelphia, Mr. Cooper held a series of executive positions at AT&T Broadband, RELERA Data Centers & Solutions, and MediaOne and its predecessor Continental Cablevision, Inc. He has held various board and committee seats with the National Cable Television Association, California Cable & Telecommunications Association, Cable Television Association for Marketing and the New England Cable Television Association. In addition, Mr. Cooper is either a director or trustee at the Denver Art Museum, Colorado Public Radio and the Cable Center at the University of Denver.

Janice I. Obuchowski

President

Freedom Technologies, Inc.

Ms. Obuchowski, 55, was elected to the Board in November 1997. She has been President of Freedom Technologies, Inc., a public policy and corporate strategy consulting firm specializing in telecommunications, since 1992. In 2003, Ms. Obuchowski was appointed by President George W. Bush to serve as Ambassador and Head of the U.S. Delegation to the World Radio Communication Conference. She has served as Assistant Secretary for Communications and Information at the Department of Commerce and as Administrator for the National Telecommunications and Information Administration. Ms. Obuchowski currently is a director of Orbital Sciences Corporation and Stratos Global Corporation.

Donald B. Reed

Former Chief Executive Officer

Global Cable & Wireless

Mr. Reed, 62, was elected to the Board in May 2005. He currently is retired, having served as Chief Executive Officer of Cable & Wireless Global from May 2000 to January 2003. Cable & Wireless Global, Cable & Wireless plc s wholly owned operations in the United States, United Kingdom, Europe and Japan, is a provider of internet protocol (IP) and data services to business customers. From June 1998 until May 2000, Mr. Reed served Cable & Wireless in various other executive positions. Mr. Reed s career includes 30 years at NYNEX Corporation (now part of Verizon), a regional telephone operating company. From 1995 to 1997 Mr. Reed served NYNEX Corporation as President and Group Executive with responsibility for directing the company s regional, national and international government affairs, public policy initiatives, legislative and regulatory matters, and public relations. Mr. Reed currently is a director of Intervoice, Inc., St. Lawrence Cement (TSX), Idearc Media (formerly Verizon Yellow Pages) (NYSE) and Aggregate Industries in London, England, a wholly owned subsidiary of Holcim Group located in Switzerland.

Frank V. Sica

Managing Partner

Tailwind Capital

Mr. Sica, 56, has served as a director of the Company since its formation in 1994. He is currently a Managing Partner of Tailwind Capital. From 2004 to 2005, Mr. Sica was a Senior Advisor to Soros Private Funds Management. From 2000 until 2003, he was President of Soros Private Funds Management which oversaw the direct real estate and private equity investment activities of Soros. In 1998, he joined Soros Fund Management where he was a Managing Director responsible for Soros private equity investments. From 1988 to 1998, Mr. Sica was a Managing Director at Morgan Stanley and its private equity affiliate, Morgan Stanley Capital Partners. Prior to 1988, Mr. Sica was a Managing Director in Morgan Stanley s mergers and acquisitions department. From 1974 to 1977, Mr. Sica was an officer in the U.S. Air Force. Mr. Sica currently is a director of JetBlue Airways, Kohl s Corporation, NorthStar Realty Finance Corporation and Onvoy, Inc.

Table of Contents

Donald V. Smith

Senior Managing Director

Houlihan Lokey Howard & Zukin, Inc.

Mr. Smith, 64, was elected to the Board in January 2002. He presently serves as Senior Managing Director of Houlihan Lokey Howard & Zukin, Inc., an international investment banking firm with whom he has been associated since 1988. Mr. Smith currently is in charge of the firm s New York office and serves on the board of directors of the firm. From 1978 to 1988, he was employed by Morgan Stanley & Co. Incorporated, where he headed the valuation and reorganization services within that firm s corporate finance group. Mr. Smith is director of the Princeton (NJ) Health Care Foundation and of Business Executives for National Security.

James A. Unruh

Managing Principal

Alerion Capital Group

Mr. Unruh, 66, was elected to the Board in June 2005. He became a founding principal of Alerion Capital Group, LLC (a private equity investment company) in 1998 and currently holds such position. Mr. Unruh was an executive with Unisys Corporation from 1987 to 1997 and served as its Chairman and Chief Executive Officer from 1990 to 1997. From 1982 to 1987, Mr. Unruh held various executive positions, including Senior Vice President, Finance, with Burroughs Corporation, a predecessor of Unisys Corporation. Mr. Unruh currently is a director of Prudential Financial, Inc., Tenet Healthcare Corporation, and Qwest Communications International Inc.

Table of Contents

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities
Our common stock is listed on the Nasdaq Stock Market LLC (NASDAQ/NMS) under the symbol CSGS . The following table sets forth, for the fiscal quarters indicated, the high and low sale prices of our common stock as reported by NASDAQ/NMS.

	High	Low
2006		
First quarter	$ 23.29	$ 20.82
Second quarter	26.21	22.87
Third quarter	27.48	23.18
Fourth quarter	28.45	26.11

	High	Low
2005		
First quarter	$ 18.93	$ 15.88
Second quarter	19.75	15.74
Third quarter	21.82	16.15
Fourth quarter	24.76	21.06

On February 26, 2007, the last sale price of our common stock as reported by NASDAQ/NMS was $25.35 per share. On January 31, 2007, the number of holders of record of common stock was 242.

Dividends

We have not declared or paid cash dividends on our common stock since our incorporation. We did, however, complete a two-for-one stock split, effected in the form of a stock dividend, in March 1999. We intend to retain any earnings to finance the growth and development of our business, and at this time, we do not plan to pay cash dividends in the foreseeable future.

Our revolving credit facility contains certain restrictions on the payment of dividends. In addition, the payment of dividends has certain impacts to our Convertible Debt Securities. See Note 7 to our Consolidated Financial Statements for additional discussion of our revolving credit facility and Convertible Debt Securities, and the impact the payment of dividends may have on these items.

Table of Contents

Stock Price Performance

The following graph compares the cumulative total stockholder return on our common stock, the S&P 500 Index, and our Standard Industrial Classification (SIC) Code Index: Computer Processing and Data Preparation and Processing Services during the indicated five-year period. The graph assumes that $100 was invested on December 31, 2001, in our common stock and in each of the two indexes and that all dividends, if any, were reinvested.

	12/31/01	12/31/02	12/31/03	12/31/04	12/31/05	12/31/06
CSG Systems International Inc.	100.00	33.75	30.88	46.23	55.18	66.08
Data Preparation & Processing Services	100.00	76.63	91.21	100.18	100.68	112.54
S&P 500 Index	100.00	77.90	100.25	111.15	116.61	135.03

Equity Compensation Plan Information

The following table summarizes certain information about our equity compensation plans as of December 31, 2006:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights	Weighted-average exercise price of outstanding options, warrants, and rights	Number of securities remaining available for future issuance
Equity compensation plans approved by security holders	438,301	$ 29.51	12,224,515
Equity compensation plan not approved by security holders	121,455	20.09	58,790
Total	559,756	$ 27.47	12,283,305

Of the total number of securities remaining available for future issuance, 11,900,790 shares can be used for various types of stock-based awards, as specified in the individual plans, with the remaining 382,515 shares to be used for our employee stock purchase plan. See Note 13 to our Consolidated Financial Statements for additional discussion of our equity compensation plans.

17

Table of Contents

Issuer Repurchases of Equity Securities

The following table presents information with respect to purchases of company common stock made during the three months ended December 31, 2006 by CSG Systems International, Inc. or any affiliated purchaser of CSG Systems International, Inc., as defined in Rule 10b-18(a)(3) under the Exchange Act.

Period	Total Number of Shares Purchased[2]	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plan or Programs[1]
October 1 - October 31	150,000	$ 26.82	150,000	14,990,908
November 1 - November 30	343,370	27.40	343,370	14,647,538
December 1 - December 31	319,677	26.91	262,872	14,384,666
Total	813,047	$ 27.10	756,242	

[1] Effective July 12, 2006, our Board of Directors approved a 10 million share increase in the number of shares we are authorized to repurchase under the Stock Repurchase Program, bringing the total number of authorized shares to 30 million. The Stock Repurchase Program does not have an expiration date.

[2] The total number of shares purchased that are not part of the Stock Repurchase Program represents shares purchased and cancelled in connection with stock incentive plans.

Table of Contents

Item 6. Selected Financial Data

The following selected financial data have been derived from our audited financial statements. The selected financial data presented below should be read in conjunction with, and is qualified by reference to, our MD&A and our Consolidated Financial Statements. The information below is not necessarily indicative of the results of future operations.

	Year Ended December 31,				
	2006	**2005**	**2004**	**2003**	**2002**
	(in thousands, except per share amounts)				
Statement of Operations Data:					
Revenues:					
Processing and related services (2)	$ 351,764	$ 346,463	$ 326,556	$ 341,628	$ 372,426
Software, maintenance and services (2)	31,342	30,854	24,845	25,766	48,623
	383,106	377,317	351,401	367,394	421,049
Charge for arbitration ruling attributable to periods prior to July 1, 2003 (2)				(105,679)	
Total revenues, net	383,106	377,317	351,401	261,715	421,049
Cost of revenues (5):					
Processing and related services	173,536	170,344	146,837	140,475	138,452
Software, maintenance and services	20,975	19,720	25,047	30,359	26,696
Total cost of revenues	194,511	190,064	171,884	170,834	165,148
Gross margin (exclusive of depreciation)	188,595	187,253	179,517	90,881	255,901
Operating expenses (5):					
Research and development	46,191	33,932	31,887	30,398	32,764
Selling, general and administrative	43,127	52,492	39,453	50,041	40,864
Depreciation	10,438	9,862	10,412	12,701	14,751
Restructuring charges (4)	2,368	14,534	1,292	2,149	2,256
Total operating expenses	102,124	110,820	83,044	95,289	90,635
Operating income (loss)	86,471	76,433	96,473	(4,408)	165,266
Other income (expense):					
Interest expense	(7,465)	(7,537)	(10,261)	(14,296)	(13,817)
Write-off of deferred financing costs (6)			(6,569)		
Interest and investment income, net (1)	21,984	4,059	975	920	1,729
Other, net	(21)	6	(303)	(85)	833
Total other	14,498	(3,472)	(16,158)	(13,461)	(11,255)
Income (loss) from continuing operations before income taxes	100,969	72,961	80,315	(17,869)	154,011
Income tax (provision) benefit (2)	(38,408)	(26,219)	(29,317)	12,703	(55,960)
Income (loss) from continuing operations	62,561	46,742	50,998	(5,166)	98,051
Discontinued operations (1):					
Loss from discontinued operations (5)	(6,555)	(5,685)	(11,109)	(30,591)	(66,468)
Income tax benefit	3,764	12,172	7,295	9,480	13,035
Discontinued operations, net of tax	(2,791)	6,487	(3,814)	(21,111)	(53,433)

Net income (loss)	$ 59,770	$ 53,229	$ 47,184	$ (26,277)	$ 44,618
Diluted net income (loss) per common share:					
Income (loss) from continuing operations	$ 1.33	$ 0.96	$ 0.99	$ (0.10)	$ 1.87
Discontinued operations, net of tax	(0.06)	0.13	(0.07)	(0.41)	(1.02)
Net income (loss)	$ 1.27	$ 1.09	$ 0.92	$ (0.51)	$ 0.85
Weighted-average diluted shares outstanding (3)	47,102	48,571	51,223	51,432	52,525
Other Data (at Period End):					
Number of clients' customers processed (2)	45,354	45,228	43,472	44,148	45,816
Balance Sheet Data (at Period End):					
Cash, cash equivalents and short-term investments (1)(7)	$ 415,490	$ 392,224	$ 149,436	$ 105,397	$ 95,437
Working Capital (2)(7)	454,117	444,738	172,675	69,642	119,782
Total assets	653,496	638,376	710,407	724,775	731,317
Total debt (6)	230,000	230,000	230,000	228,925	270,000
Total treasury stock (3)	360,259	296,976	224,008	171,111	186,045
Stockholders' equity	317,734	298,330	308,070	290,785	282,105

Table of Contents

(1) We sold our GSS and plaNet businesses in 2005. As a result, the results of operations for the GSS and plaNet businesses have been reflected as discontinued operations for all periods presented in our Consolidated Statements of Income. We recorded a net pretax gain (loss) on the disposal of these businesses of $(6.0) million and $10.9 million, respectively, in 2006 and 2005. We received approximately $233 million in net cash proceeds from the sale of these businesses, which is the primary reason for the significant increase in cash, cash equivalents, and short-term investments between 2004 and 2005. See Note 2 to our Consolidated Financial Statements and MD&A for additional discussion.

(2) During 2003, we recorded a $119.6 million charge to revenue related to the Comcast arbitration ruling award. The award was segregated such that $105.7 million was attributable to periods prior to July 1, 2003, and $13.9 million was attributable to the third quarter of 2003. Of the $13.9 million attributable to the third quarter, we attributed $13.5 million to processing revenues, and the remaining $0.4 million to software maintenance revenues. The arbitration ruling also required us to begin invoicing Comcast lower monthly processing fees beginning in October 2003, which had the effect of reducing quarterly revenues from Comcast by approximately $13-$14 million ($52-$56 million annually), when compared to amounts prior to the arbitration ruling. As a result of the Comcast arbitration award, we were in a net operating loss position for the year, and recorded an income tax benefit of $12.7 million. During the fourth quarter of 2003, we paid Comcast $94.4 million of the arbitration award and in January 2004, we paid the remaining $25.2 million. Additionally, as a result of the arbitration ruling, Comcast customer accounts began being measured differently in October 2003, which resulted in a reduction in the total number of clients customers processed.

(3) In August 1999, our Board of Directors approved our Stock Repurchase Program which authorized us to purchase shares of our common stock from time-to-time as business conditions warrant. During 2006, 2005, 2004, 2003, and 2002, we repurchased 2.5 million, 3.8 million, 3.0 million, zero, and 1.6 million shares, respectively. As of December 31, 2006, 14.4 million shares of the 30.0 million shares authorized under the Stock Repurchase Program remain available for repurchase. See Note 12 to our Consolidated Financial Statements and MD&A for additional discussion of the Stock Repurchase Program.

(4) Beginning in the third quarter of 2002 and continuing through 2006, we made several changes to our business operations and implemented several cost reduction initiatives that resulted in restructuring charges of $2.4 million, $14.5 million, $1.3 million, $2.1 million, and $2.3 million, respectively, for 2006, 2005, 2004, 2003, and 2002. See Note 8 to our Consolidated Financial Statements and MD&A for additional discussion of the restructuring charges.

(5) In 2003, we adopted the fair value method of accounting for our stock-based awards. In addition, we completed our exchange of certain stock options for restricted stock (also referred to by us as our tender offer) in December 2003. As a result, our stock-based compensation expense is significantly higher in 2006, 2005, and 2004 when compared to previous years. Additionally, in 2005, certain equity awards held by key members of our management team included a change in control provision that was triggered upon the closing of the sale of the GSS Business. The change in control provision resulted in accelerated vesting as of December 9, 2005 for the equity awards impacted, and thus, stock-based compensation expense of $4.7 million related to the accelerated vesting of these equity awards was recorded as stock-based compensation expense in the fourth quarter of 2005, of which $0.9 million was included in discontinued operations, and $3.8 million was included in continuing operations as part of restructuring charges. Total stock-based compensation expense recognized during 2006, 2005, 2004, 2003, and 2002 was $12.2 million, $20.4 million, $14.9 million, $5.6 million, and $1.4 million, respectively. Of these amounts, $12.2 million, $17.0 million, $10.6 million, $5.0 million, and $1.3 million are reflected in continuing operations for 2006, 2005, 2004, 2003, and 2002, respectively, with the remaining amounts reflected in discontinued operations for the respective periods. See Notes 3 and 13 to our Consolidated Financial Statements for additional discussion of these matters.

(6) In February 2002, we entered into a $300 million term credit facility to finance the acquisition of the Kenan Business (which became part of our GSS Business). In June 2004, we completed an offering of $230 million of Convertible Debt Securities and used the proceeds, along with available cash, cash equivalents and short-term investments to: (i) repay the outstanding balance of the term credit facility; (ii) repurchase 2.1 million of shares of our common stock; and (iii) pay debt issuance costs of $7.2 million. As a result, we wrote off unamortized deferred financing costs attributable to the term credit facility of $6.6 million. See Note 7 to our Consolidated Financial Statements for additional discussion of our long-term debt.

(7) As a result of the sale of the GSS and plaNet businesses, our December 31, 2006 and 2005 Consolidated Balance Sheets no longer include any amounts related to these sold businesses. To provide for consistent comparisons, the December 31, 2004 Consolidated Balance Sheet was restated to reflect the components of the sold GSS and plaNet businesses as assets and liabilities related to discontinued operations. Thus, the 2006, 2005, and 2004 cash, cash equivalents and short-term investments and working capital amounts in the above table are presented on a different basis, as the 2003 and 2002 amounts have not been restated and still include amounts related to the GSS and plaNet businesses.

Table of Contents

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operation
Forward-Looking Statements

This report contains a number of forward-looking statements relative to our future plans and our expectations concerning the North American customer care and billing industry, as well as the converging communications industry it serves, and similar matters. These forward-looking statements are based on assumptions about a number of important factors, and involve risks and uncertainties that could cause actual results to differ materially from estimates contained in the forward-looking statements. Some of the risks that are foreseen by management are outlined above within Item 1A., Risk Factors . Item 1A. constitutes an integral part of this report, and readers are strongly encouraged to review this section closely in conjunction with MD&A.

Management Overview

Our Company. We are a leading provider of outsourced billing, customer care and print and mail solutions and services supporting the North American communications market. Our solutions support some of the world s largest and most innovative providers of bundled multi-channel video, Internet, and IP-based services. Our unique combination of solutions, services and expertise ensures that communication providers can continue to rapidly launch new service offerings, improve operational efficiencies and deliver a high-quality customer experience in a competitive and ever-changing marketplace.

As noted above, the North American communications industry has experienced significant consolidation over the last few years, resulting in a large percentage of the market being served by a fewer number of service providers with greater size and scale. Consistent with this market concentration, a large percentage of our revenues from continuing operations are generated from a limited number of clients, with approximately 70% of our revenues for 2006 being generated from our four largest clients, which are Comcast, EchoStar, Time Warner, and Charter.

Key Changes Made to Our Business During 2005. In 2005, we made several changes to our business operations in order to intensify our focus on our core competencies in the cable and DBS markets utilizing our ACP product and related services and improve our operating results. The most significant were the sale of our GSS Business to Comverse on December 9, 2005 and the sale of our plaNet Consulting business to a group of private investors led by the plaNet management team on December 30, 2005. These two businesses had been underperforming to our financial expectations and were no longer considered part of our core strategy, and thus were sold.

As a result, we have reflected the results of operations for the GSS Business and plaNet Business as discontinued operations in our results of operations for all periods presented. In addition, in conjunction with the closing of the sale of the GSS Business, during the fourth quarter of 2005, we incurred restructuring charges within our continuing operations of $7.1 million. These restructuring charges, and greater details of the sale of the GSS and plaNet businesses, are discussed below and in Notes 2 and 8 to our Consolidated Financial Statements.

Additionally, during 2005 we also made several changes to our Executive Management team and Board of Directors. Most notably was the retirement of Mr. Neal Hansen, our then current Chairman of the Board of Directors and Chief Executive Officer. In consideration for certain changes to his employment agreement and for post-termination consulting services to be provided as a result of his retirement, we agreed to pay Mr. Hansen $9.6 million. Of this amount, $7.6 million was paid in 2006 and $2.0 million was paid on January 2, 2007. We recorded expense related to Mr. Hansen s retirement package in 2006, 2005, and 2004 of $0.2 million, $8.9 million, and $0.5 million, respectively. The expense related to this matter is reflected within the Selling, General and Administrative caption in the accompanying Consolidated Statements of Income.

As a result of the retirement of Mr. Hansen, Mr. Edward Nafus, our then Executive Vice President and President of our Broadband Division, was added to our Board of Directors in March 2005, and assumed the position of Chief Executive Officer and President of our company effective April 1, 2005. In addition, effective July 1, 2005, Mr. Bernard Reznicek, a current Board member, was named non-executive Chairman of the Board to replace Mr. Hansen.

2006 Highlights. In 2006, we continued to execute on our decision to intensify our focus on our core competencies and evaluate ways in which we can achieve our objectives, align our organization to focus on our strengths, and maximize our opportunities within the communications industry. As part of this strategy, we made certain changes to our management team and Board of Directors during 2006, summarized as follows:

- In April 2006, we announced that Mr. Peter Kalan, our then Chief Financial Officer, was named Executive Vice President of Business and Corporate Development, and Mr. Randy Wiese, our Chief Accounting Officer, was named Executive Vice President and Chief Financial Officer. See our Form 8-K filed on April 25, 2006 for additional details of these matters.

- In July 2006, Mr. Robert M. Mike Scott was named our Chief Operating Officer.

- In November 2006, our Board of Directors named Mr. Joseph Ruble, Senior Vice President, General Counsel and Secretary, as an Executive Officer. See our Form 8-K filed on November 17, 2006 for additional details of these matters.

- In November 2006, Mr. Ronald Cooper, an individual with significant operational experience in the cable and telecommunications industry, joined our Board of Directors, bringing our total number of Board members to eight, of which, seven members are independent directors. See our Form 8-K filed on November 17, 2006 for additional details of these matters.

The market for customer care and billing systems is characterized by rapid changes in technology and is highly competitive with respect to the need for timely product innovations and new product introductions to enable communication providers to timely roll out new competitive product offerings while maintaining the highest standards of customer service. In response to the increased demand for such product enhancements, and the pace at which such changes are delivered, we substantially increased our internal investment in R&D during 2006 and acquired Telution on March 1, 2006.

Telution was a Chicago-based provider of operations support system (OSS) technologies that enabled communication companies to bring bundled, advanced services to market quickly and effectively. We acquired Telution and its COMX solution to expand our ability to support communication providers as they deliver advanced and IP-based services. As a result of this acquisition, we have begun to extend our ability to support our clients sales, ordering, partnering and service provisioning processes as well as deliver enhanced customer care capabilities through all customer touch points the Web, interactive television, field service, statement, the call center and more. See Note 4 to our Financial Statements for additional discussion of this transaction.

We are currently working on the natural evolution of the ACP platform to incorporate the COMX platform, accelerating the development of our product offerings to enable operators to more easily bundle and deploy new service offerings. The integrated solution will provide enhanced product configuration, offer management and order workflow functionality specifically targeted to support our clients ability to manage the complexities of both consumer and business services markets. In addition, the integrated solution will enable operators to better support customers of bundled services as they choose new services and seek support for existing services.

We believe that the investments we have made during 2006 have demonstrated our commitment to focus on our core competencies. Additionally, we continue to evaluate new opportunities and new ways to support our clients growth whether it be through R&D, acquisitions or partnerships.

Results of Operations. A summary of our results of operations for 2006 is as follows:

- Our consolidated revenues from continuing operations for 2006 were $383.1 million, up slightly when compared to $377.3 million for 2005. This is a result of certain downward revenue pressures we experienced during 2006 related to several specific client matters, which were more than offset by the continued growth we saw in the use of various ancillary products and services we offer to our existing client base.

Our operating expenses from continuing operations for 2006 decreased $4.3 million, or 1.4%, to $296.6 million, when compared to $300.9 million for 2005. The decrease in operating expenses from continuing operations between years is primarily due to the following:

Table of Contents

Restructuring charges were $2.4 million for 2006, compared to $14.5 million for 2005, a decrease of $12.1 million. Primarily all of the restructuring charges incurred during 2005 and 2006 related to the changes that we made to our business operations during the fourth quarter of 2005. Restructuring charges reduced 2006 and 2005 income from continuing operations by $0.03 and $0.19, respectively, per diluted share.

Expense related to the retirement of our former CEO was $0.2 million for 2006, as compared to $8.9 million for 2005, a decrease of $8.7 million. The $8.9 million of expense recorded for this item reduced 2005 net income from continuing operations by $0.12 per diluted share.

These decreases were offset to a certain degree by the impact of the acquisition of Telution in March 2006, in which we incurred approximately $10 million of expense related to Telution, and an increase in labor-related costs, primarily as a result of an increase in staff levels between periods related to the increase in our R&D efforts.

Income from continuing operations (net of tax) for 2006 was $62.6 million, or $1.33 per diluted share, an increase of 33.8% when compared to $46.7 million, or $0.96 per diluted share, for 2005. The restructuring charges and CEO retirement expense discussed above reduced 2005 income from continuing operations by $0.31 per diluted share.

Income from continuing operations for 2006 was positively impacted by a $17.9 million increase in interest and investment income over 2005. Interest and investment income was $22.0 million for 2006, as compared to $4.1 million for 2005, with the increase primarily attributed to the interest income earned on the cash proceeds received from the sale of the GSS Business in December 2005.

Continuing operations for 2006 and 2005 include non-cash charges related to depreciation, amortization, and stock-based compensation expense totaling $38.6 million (pretax impact), or $0.51 per diluted share, and $40.5 million (pretax impact), or $0.53 per diluted share, respectively.

We continue to generate strong cash flows as a result of our profitable operations and through our effective management of our working capital items. As of December 31, 2006, we had cash, cash equivalents and short-term investments of $415.5 million, compared to $392.2 million as of December 31, 2005. During 2006, we generated $118.2 million of cash flows from operating activities, as compared to $102.6 million for 2005, with the increase between years primarily related to changes in working capital items, as discussed in greater detail below.

Other key matters related to our continuing operations for 2006 were as follows:

Total customer accounts processed on our systems as of December 31, 2006 were 45.4 million, compared to 45.2 million as of December 31, 2005. The annualized revenue per processing unit (ARPU) for 2006 and 2005 was consistent between years at $7.81.

As of December 31, 2006, approximately 90% of the cable customer accounts processed on our systems have been successfully migrated to our ACP platform. We expect to migrate the remaining cable customer accounts to the ACP platform by the end of 2007.

We had no material client relationships scheduled for renewal in 2006, and do not have any material contracts up for renewal in 2007.

In August 2006, we announced our plans to repurchase up to $350 million of our common stock under our Stock Repurchase Program. In conjunction with this action, our Board of Directors approved a 10 million share increase in the number of shares authorized for repurchase under our Stock Repurchase Program, bringing the total number of authorized shares to 30 million. Subsequent to this announcement, and through December 31, 2006, we have repurchased approximately 1.6 million shares, for a total of approximately $42.4 million (a weighted average price of $26.90 per share) towards our planned $350 million stock repurchase amount. As of December 31, 2006, the remaining number of shares authorized for repurchase under our Stock Repurchase Program is 14.4 million shares.

Significant Client Relationships

Comcast. Comcast continues to be our largest client. For 2006 and 2005, revenues from Comcast represented approximately 24% and 22%, respectively, of our total revenues from continuing operations. Our processing agreement with

Table of Contents

Comcast runs through December 31, 2008. Under the terms of the Comcast processing agreement, Comcast could remove one or more regions from our systems, or significantly reduce the number of customers on our systems, without automatically incurring a financial penalty. The Comcast processing agreement and related amendments are included in the exhibits to our periodic filings with the SEC. The documents are available on the Internet and we encourage readers to review these documents for further details.

EchoStar. EchoStar is our second largest client. For 2006 and 2005, revenues from EchoStar represented approximately 19% and 21%, respectively, of our total revenues from continuing operations. During the fourth quarter of 2005, we signed a new processing agreement with EchoStar to continue providing customer care and billing support services. The EchoStar processing agreement was effective November 1, 2005, runs through December 31, 2008, and provides EchoStar with the option to extend the term of the agreement for either one or two years beyond the end of December 2008. The EchoStar processing agreement provides for certain pricing reductions when compared to the previous processing agreement, which explains the decrease between 2006 and 2005 in the percentage of our revenues generated from EchoStar. The EchoStar processing agreement includes certain annual financial commitments. The EchoStar processing agreement and related amendments are included in the exhibits to our periodic filings with the SEC. The documents are available on the Internet and we encourage readers to review these documents for further details.

Time Warner. Time Warner is our third largest client. For 2006 and 2005, revenues from Time Warner represented approximately 12% and 10%, respectively, of our total revenues from continuing operations. Our processing agreement with Time Warner runs through March 31, 2013. The Time Warner processing agreement contains provisions establishing annual minimum customer account levels that have to be processed on our systems, which we expect Time Warner to exceed based on the number of Time Warner customers currently on our systems. Under the terms of the Time Warner processing agreement, Time Warner could remove one or more regions from our systems, or significantly reduce the number of customers on our systems, without automatically incurring a financial penalty.

Charter. Charter is our fourth largest client. For 2006 and 2005, revenues from Charter represented approximately 11% and 10%, respectively, of our total revenues from continuing operations. Our contract with Charter runs though December 31, 2012. The Charter contract contains certain annual minimum customer account levels that have to be processed on our systems.

Adelphia. Adelphia has historically been our fifth largest client, with revenues from Adelphia for 2006 and 2005 representing approximately 5% and 9%, respectively, of our total revenues from continuing operations. Adelphia had been operating under bankruptcy protection since June 2002. On July 31, 2006, Adelphia completed the sale of its broadband assets to Comcast and Time Warner. Prior to the closing of this transaction, we processed approximately three million Adelphia domestic broadband customer accounts (the Acquired Customer Accounts) on our systems under a processing agreement that ran through March 31, 2009. Upon closing of this transaction, the Acquired Customer Accounts we processed remained on our systems and were transferred to the respective Comcast and Time Warner processing agreements. This transaction had the following impacts to our business:

In August 2006, we recognized $2.8 million of one-time, non-recurring revenues related to the Adelphia processing agreement when the Acquired Customer Accounts were transferred under our Comcast and Time Warner processing agreements. These revenues included items such as upfront payments for services that had previously been deferred and were being recognized ratably over the remaining term of the Adelphia processing agreement.

Our monthly processing revenues related to the Acquired Customer Accounts were approximately $4.5 million lower in 2006 when compared to 2005 due to the Comcast and Time Warner contracts having lower per unit pricing than the Adelphia contract (due to the relative size of Comcast and Time Warner when compared to Adelphia). The $4.5 million reflects five months of invoices at the lower per unit pricing for these Acquired Customer Accounts.

Although there was some movement of customer accounts between Comcast and Time Warner as the result of this transaction, it had minimal impact on the overall number of customer accounts processed on our systems as of the end of 2006.

24

Table of Contents

Stock Repurchase Program

We currently have a stock repurchase program, approved by our Board of Directors, authorizing us to repurchase up to 30 million shares of our common stock from time-to-time as market and business conditions warrant (the Stock Repurchase Program). To facilitate the repurchase of our common stock under the Stock Repurchase Program, we have from time-to-time established formal plans with financial institutions that comply with the provisions of Rule 10b5-1 under the Securities Exchange Act of 1934 (Rule 10b5-1 Plan). In effect, a Rule 10b5-1 Plan allows us to achieve our stock buyback objectives more readily by permitting the execution of trades during periods that would otherwise be prohibited by internal trading policies. A Rule 10b5-1 Plan supplements any stock repurchases we may decide to purchase under the existing terms of our Stock Repurchase Program.

In April 2005, we established a Rule 10b5-1 Plan to repurchase on the open market up to a maximum of 3 million shares of our common stock. In May 2006, we reached the 3 million share maximum established under the Rule 10b5-1 Plan, and therefore, the Rule 10b5-1 Plan expired.

In July 2006, our Board of Directors authorized the repurchase of $350 million of our outstanding common stock under our Stock Repurchase Program. In August 2006, we established a new Rule 10b5-1 Plan to facilitate the repurchase of the $350 million of common stock. As of December 31, 2006, we have repurchased approximately 1.6 million shares of our common stock for $42.4 million (a weighted-average price of $26.90 per share) toward our planned $350 million stock repurchase amount.

The number of shares repurchased under our new Rule 10b5-1 Plan is primarily based upon predetermined factors that were established when we implemented the plan in August 2006. These factors are evaluated on a periodic basis for possible adjustment. Over time, there will likely be some variability around the number of shares repurchases due to changing market conditions, as well as the trading volume of our stock. We remain committed to completing the repurchase of $350 million of our outstanding common stock, but the time period is now expected to extend beyond our original estimate of 12-15 months due to various market factors that have impacted the pace at which we have bought back our common stock.

As of December 31, 2006, a summary of the shares repurchased under the Stock Repurchase Program is as follows (in thousands, except per share amounts):

	2006	2005	2004	2003	1999-2002	Total
Shares repurchased	2,485	3,808	2,983		6,339	15,615
Total amount paid	$ 63,283	$ 72,968	$ 52,897		$ 199,710	$ 388,858
Weighted-average price per share	$ 25.46	$ 19.16	$ 17.73		$ 31.51	$ 24.90

As of December 31, 2006, the total remaining number of shares available for repurchase under the Stock Repurchase Program totaled 14.4 million shares.

Stock-Based Compensation Expense

Stock-based compensation expense is included in the following captions in the Consolidated Statements of Income (in thousands):

	2006	2005	2004
Continuing operations:			
Cost of processing and related services.	$ 4,371	$ 3,259	$ 2,622
Cost of software, maintenance and services	713	758	871
Research and development	1,530	1,137	1,193
Selling, general and administrative	5,600	7,688	5,934
Restructuring charges		4,205	
Total continuing operations	12,214	17,047	10,620

Discontinued operations		3,311	4,266
Total stock-based compensation expense (1)	$ 12,214	$ 20,358	$ 14,886

(1) The increase in stock-based compensation expense for continuing operations in 2005 is due primarily to certain equity awards held by key members of our management team having a change in control provision that was triggered upon the closing of the sale of the GSS Business in the fourth quarter of 2005, which resulted in accelerated vesting for the equity awards impacted. See Notes 3 and 13 to our Consolidated Financial Statements for additional discussion of our stock-based compensation expense.

Critical Accounting Policies

The preparation of our financial statements in conformity with accounting principles generally accepted in the U.S. requires us to select appropriate accounting policies, and to make judgments and estimates affecting the application of those accounting policies. In applying our accounting policies, different business conditions or the use of different assumptions may result in materially different amounts reported in our Consolidated Financial Statements.

We have identified the most critical accounting policies that affect our financial condition and the results of our business continuing operations. These critical accounting policies were determined by considering our accounting policies that involve the most complex or subjective decisions or assessments. The most critical accounting policies identified relate to: (i) revenue recognition; (ii) allowance for doubtful accounts receivable; (iii) impairment assessments of long-lived assets; (iv) loss contingencies; (v) income taxes; and (vi) capitalization of internal software development costs. These critical accounting policies, as well as our other significant accounting policies, are disclosed in the notes to our Consolidated Financial Statements.

Revenue Recognition. The revenue recognition policies that involve the most complex or subjective decisions or assessments that may have a material impact on our business continuing operations relate to: (i) the application of the guidelines of Emerging Issues Task Force (EITF) Issue No. 00-21, Accounting for Revenue Arrangements with Multiple Deliverables (EITF 00-21) when determining a revenue arrangement s separate units of accounting; and (ii) the accounting for software arrangements.

For those revenue arrangements within the scope of EITF No. 00-21, we are required to evaluate all deliverables in the arrangement to determine whether they represent separate units of accounting. If the deliverables qualify as separate units of accounting, the arrangement consideration is allocated among the separate units of accounting based upon their relative fair values, and applicable revenue recognition criteria are considered for the separate units of accounting. If the deliverables do not qualify as separate units of accounting, the consideration allocable to delivered items is combined with the consideration allocable to the undelivered items, and the appropriate recognition of revenue is then determined for those combined deliverables as a single unit of accounting. For the processing agreements that we have historically evaluated under EITF No. 00-21, we have generally concluded that the deliverables do not qualify as separate units of accounting, and thus have treated the deliverables as a single unit of accounting, with the revenue recognized ratably over the term of the processing agreement. The determination of separate units of accounting, and the determination of objective and reliable evidence of fair value of the undelivered items, if applicable, both require judgments to be made by us.

The accounting for software arrangements, especially when software is sold in a multiple-element arrangement, is complex and requires judgments in the following areas: (i) the identification of the separate elements of the software arrangement; (ii) the determination of whether any undelivered elements are essential to the functionality of the delivered elements; (iii) the assessment of whether our hosted service transactions meet the requirements of EITF Issue No. 00-03, Application of AICPA Statement of Position 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity s Hardware , to be treated as a separate element to the software arrangement; (iv) the determination of vendor-specific objective evidence of fair value for the various undelivered elements of the software arrangement; and (v) the period of time maintenance services are expected to be performed. The evaluation of these factors, and the ultimate revenue recognition decisions, require significant judgments to be made by us. The judgments made in this area could have a significant effect on revenues recognized in any period by changing the amount and/or the timing of the revenue recognized. In addition, because software licenses typically have little or no direct, incremental costs related to the recognition of the revenue, these judgments could also have a significant effect on our results of operations.

Table of Contents

Allowance for Doubtful Accounts Receivable. We maintain an allowance for doubtful accounts receivable based on client-specific allowances, as well as a general allowance. Specific allowances are maintained for clients which are determined to have a high degree of collectibility risk based on such factors, among others, as: (i) the aging of the accounts receivable balance; (ii) the client s past payment experience; (iii) the economic condition of the industry in which the client conducts the majority of its business; and (iv) a deterioration in a client s financial condition, evidenced by weak financial condition and/or continued poor operating results, reduced credit ratings, and/or a bankruptcy filing. In addition to the specific allowance, we maintain a general allowance for all our accounts receivable which are not covered by a specific allowance. The general allowance is established based on such factors, among others, as: (i) the total balance of the outstanding accounts receivable, including considerations of the aging categories of those accounts receivable; (ii) past history of uncollectible accounts receivable write-offs; and (iii) the overall creditworthiness of the client base. Our credit risk is heightened due to our concentration of clients within the North American cable television and satellite industries. A considerable amount of judgment is required in assessing the realizability of accounts receivable. Should any of the factors considered in determining the adequacy of the overall allowance change significantly, an adjustment to the allowance for doubtful accounts receivable may be necessary. Because of the overall significance of our gross billed accounts receivable balance ($111.2 million as of December 31, 2006), such an adjustment could be material.

Impairment Assessment of Long-Lived Assets. Long-lived assets, which for us relates primarily to property and equipment, software and client contracts, are required to be evaluated for possible impairment whenever events or changes in circumstances indicate that the carrying amount of these assets may not be recoverable. A long-lived asset is impaired if estimated future undiscounted cash flows associated with that asset, without consideration of interest, are insufficient to recover the carrying amount of the long-lived asset. Once deemed impaired, even if by $1, the long-lived asset is written down to its fair value which could be considerably less than the carrying amount or future undiscounted cash flows. The determination of estimated future cash flows and, if required, the determination of the fair value of a long-lived asset, are by their nature, highly subjective judgments. Changes to one of more of the assumptions utilized in such an analysis could materially affect our impairment conclusions for long-lived assets.

Loss Contingencies. In the ordinary course of business, we are subject to claims (and potential claims) related to various items including but not limited to: (i) legal and regulatory matters; (ii) client and vendor contracts; (iii) product and service delivery matters; and (iv) labor matters. We follow the guidelines of SFAS No. 5, Accounting for Contingencies in determining the appropriate accounting and disclosures for such matters, which requires us to assess the likelihood of any adverse judgments in or outcomes to these matters, as well as the potential ranges of probable losses. A determination of the amount of reserves for such contingencies, if any, for these contingencies is based on an analysis of the issues, often with the assistance of legal counsel. The evaluation of such issues, and our ultimate accounting and disclosure decisions, are by their nature, subject to various estimates and highly subjective judgments. Should any of the factors considered in determining the adequacy of any required reserves change significantly, an adjustment to the reserves may be necessary. Because of the potential significance of these issues, such an adjustment could be material.

Income Taxes. We are required to estimate our income tax liability in each jurisdiction in which we operate, which is primarily the U.S. (including both Federal and state income taxes). Various judgments are required in evaluating our income tax positions and determining our provisions for income taxes. During the ordinary course of our business, there are certain transactions and calculations for which the ultimate income tax determination may be uncertain. In addition, we may be subject to examination of our income tax returns by various tax authorities which could result in adverse outcomes. For these reasons, we establish reserves for tax-related uncertainties based on estimates of whether additional taxes and interest may be due. We adjust these reserves based upon changing facts and circumstances, such as the closing of a tax audit or the closing of a tax year upon the expiration of a statute of limitations. Should any of the factors considered in determining the adequacy of any required reserves change significantly, an adjustment to the reserves may be necessary. Because of the potential significance of these issues, such an adjustment could be material.

This income tax evaluation process requires us to estimate the actual current tax liability together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These temporary differences result in deferred income tax assets and liabilities in our Consolidated Financial Statements. We must then assess the likelihood that our net deferred income tax assets will be recovered, primarily from future taxable income. To the extent recovery is not likely, we must establish a valuation allowance. As of December 31, 2006, we had net deferred income tax assets of $28.5 million, which represented approximately 4% of our total assets. We believe that between (i) carryback opportunities to past periods with taxable income; and (ii) sufficient taxable income to be generated in the future, we will realize the benefit of our net deferred income tax assets. The assumption of future taxable income is, by its nature, subject to various estimates and highly subjective judgments.

Capitalization of Internal Software Development Costs. We expend substantial amounts on R&D for both new and existing (i.e., enhancements) software products and related services. Such costs are subject to capitalization under certain circumstances. The determination of whether internal software R&D costs are subject to capitalization is by its nature, highly subjective and involves significant judgments. This decision could significantly affect earnings during the development period by either: (i) capitalizing development costs; or (ii) expensing pre-technological feasibility and pre-application development stage research costs. Further, once capitalized, the software costs are generally amortized on a straight-line basis over the estimated economic life of the product. The determination of the expected useful life of a product is highly judgmental. Finally, capitalized software R&D costs are subject to the same judgments when evaluating for possible impairment as discussed above for other long-lived assets.

We did not capitalize any internal software R&D costs, as discussed above, during 2006, 2005, or 2004. In addition, we do not have any capitalized internal software R&D costs included in our December 31, 2006 and 2005 Consolidated Balance Sheets. We believe that during these periods no material internal software R&D costs were required to be capitalized. Our conclusion is primarily based upon the fact that the feature-rich, pre-integrated, and highly-scalable nature of our products requires that our development efforts include complex design, coding and testing methodologies, which include next generation software languages and development tools. Development projects of this nature carry a high-degree of development risk. Substantially all of our internal software R&D efforts are of this nature, and therefore, we believe the costs subject to capitalization during these periods were not material.

Detailed Discussion of Results of Operations

Total Revenues. Total revenues from continuing operations for: (i) 2006 increased $5.8 million, or 1.5%, to $383.1 million, from $377.3 million for 2005; and (ii) 2005 increased $25.9 million, or 7.4%, to $377.3 million, from $351.4 million for 2004. The increases in total revenues from continuing operations between years relates primarily to an increase in our processing revenues.

Processing Revenue. Processing revenues for: (i) 2006 increased $5.3 million, or 1.5%, to $351.8 million, from $346.5 million for 2005; and (ii) 2005 increased $19.9 million, or 6.1%, to $346.5 million, from $326.6 million for 2004.

Processing revenues for 2006 were up slightly when compared 2005. This is a result of certain downward revenue pressures we experienced during 2006 related to several specific client matters, which were more than offset by the continued growth we see in the use of various ancillary products and services we offer to our existing client base. The downward revenue pressures consisted primarily of the following items: (i) lower revenues in 2006 from EchoStar due to new contract pricing becoming effective November 1, 2005; (ii) client regionalization projects which resulted in the movement of approximately one million customer accounts from our systems to a competitor s system during the early part of 2006; (iii) lower revenues beginning in August 2006 related to the Adelphia Acquired Customer Accounts as a result of these accounts moving under our Comcast and Time Warner contracts, as discussed above; and (iv) $2.3 million related to one-time contract termination and bankruptcy settlements recorded in 2005, with no comparable amounts in 2006. These downward pressures were more than offset by the continued growth we see in the use of various ancillary products and services we offer, which consist of such things as our marketing services and various customer care solutions, which include self-care tools, professional services, system interfaces, and reporting tools.

The increase in processing revenues between 2005 and 2004 was primarily due to: (i) an increase in the number of customer accounts processed on our systems; and (ii) increased usage of ancillary products and services, similar to those discussed directly above.

Additional information related to processing revenues is as follows:

Amortization of the client contracts intangible asset (reflected as a reduction of processing revenues) for 2006, 2005, and 2004 was $13.4 million, $12.7 million, and $11.4 million, respectively.

Table of Contents

Total customer accounts processed on our systems as of December 31, 2006, 2005, and 2004 were 45.4 million, 45.2 million, and 43.5 million, respectively.

As noted above, as a result of certain client regionalization projects, approximately one million customer accounts processed on our systems moved to a competitor s system. However, this decrease was offset primarily by organic growth experienced by our clients. Additionally, as discussed above, the impact of the closing of the Adelphia transaction had minimal impact on the overall number of customer accounts processed on our systems as of the end of 2006.

The increase in customer accounts processed on our systems between 2005 and 2004 relates primarily to organic growth experienced by our clients.

ARPU for 2006, 2005, and 2004 was $7.81, $7.81, and $7.46, respectively. The consistency in ARPU between 2005 and 2006 relates to our relatively consistent processing revenues between years, without a significant change in customer accounts processed, as addressed above. The increase in 2005 ARPU when compared to 2004 was primarily attributed to higher revenues related to our clients discretionary and variable use of ancillary products and services, as noted above.

The ARPU for the fourth quarter of 2006 was $7.72 compared to $8.08 for the third quarter of 2006. The sequential decrease in ARPU between the third and fourth quarters of 2006 relates primarily to the Adelphia matters discussed above. Fourth quarter processing revenues related to the Adelphia Acquired Customer Accounts were $3.5 million lower when compared to that of the third quarter, which equates to a sequential decrease in ARPU of approximately $0.30 between the third and fourth quarters of 2006.

Software, Maintenance and Services Revenues. Software, maintenance and services revenues for: (i) 2006 were relatively flat between years at $31.3 million, compared to $30.9 million for 2005, which includes revenues from Telution, which was acquired on March 1, 2006; and (ii) 2005 increased $6.1 million, or 24.2%, to $30.9 million, from $24.8 million for 2004. The increase between 2005 and 2004 was due primarily to an increase in software license sales of our workforce automation and call center solutions during the first half of 2005.

Cost of Processing and Related Services. The cost of processing and related services revenues consists principally of the following: (i) data processing and communications costs; (ii) statement production costs (e.g., labor, paper, envelopes, equipment, equipment maintenance, etc.); (iii) client support organizations (e.g., our client support call center, account management, etc.); (iv) various product support organizations (e.g., product management and delivery, product maintenance, etc.); and (v) facilities and infrastructure costs related to the statement production and support organizations. The costs related to product development (including enhancements to existing products) are included in R&D expenses.

The cost of processing and related services for: (i) 2006 increased $3.2 million, or 1.9%, to $173.5 million, from $170.3 million; and (i) 2005 increased $23.5 million, or 16.0%, to $170.3 million, from $146.8 million for 2004.

The increase in cost of processing and related services between 2006 and 2005 was primarily due to an increase in labor-related costs, to include the impact of annual merit wage increases.

The increase in cost of processing and related services between 2005 and 2004 was primarily due to: (i) an increase in labor-related costs, primarily as a result of annual merit wage increases and the increase in staff levels to support the growth opportunities of our VoIP products and services and to accommodate the migration of clients to ACP; (ii) an increase in data processing costs, primarily due to growth in the number of customers processed on our systems, and greater processing requirements for ACP functionality; and (iii) an increase in variable costs related to the delivery of ancillary products and services (e.g., print costs, etc.), which directly correlate with the increase in revenues related to ancillary products and services.

Gross margin percentages related to our processing and related services revenues were 50.7%, 50.8%, and 55.0%, for 2006, 2005, and 2004, respectively.

The relatively flat gross margins between 2006 and 2005 are consistent with the relatively flat revenues and cost of related revenues, as noted above.

Table of Contents

The decrease in the gross margin percentages between 2005 and 2004 relates primarily to the increase in costs related to our ACP product initiatives without a commensurate increase in revenues associated with such initiatives. This is primarily the result of the investment we made in our ACP products and services, including the efforts to migrate our clients to the ACP platform, which began in 2004. We do not receive any additional revenue from our clients associated with their initial migration to the ACP platform. However, the ACP platform does facilitate the roll out of new products and services by our clients, which may result in additional revenue opportunities for us.

Cost of Software, Maintenance and Services. The cost of software, maintenance and services revenues consists principally of the following: (i) client support organizations (e.g., our client support call center, account management, etc.); (ii) various product support organizations (e.g., product management and delivery, product maintenance, etc.); (iii) professional services organizations; (iv) facilities and infrastructure costs related to these organizations; (v) third-party software costs and/or royalties related to certain software products; and (vi) amortization of acquired software and acquired client contracts. The costs related to product development (including enhancements to existing products) are included in R&D expenses.

The cost of software, maintenance and services for: (i) 2006 increased $1.3 million, or 6.4%, to $21.0 million, from $19.7 million; and (ii) 2005 decreased $5.3 million, or 21.3%, to $19.7 million, from $25.0 million for 2004.

The increase in cost of software, maintenance and services between 2006 and 2005 was due primarily to the amortization of the Telution intangible assets acquired in March 2006.

The decrease in cost of software, maintenance and services between 2005 and 2004 was related primarily to reductions in our personnel assigned to software maintenance projects.

Gross margin (loss) percentages related to our software, maintenance and services revenues were 33.1%, 36.1%, and (0.8%), respectively, for 2006, 2005, and 2004. The improvement in the gross margin percentages between 2005 and 2004 is primarily related to lower costs between periods, as noted above, and 2005 having the benefit of the impact of increased software license sales of our workforce automation and call center solutions during the first half of 2005.

Variability in quarterly revenues and operating results are inherent characteristics of companies that sell software licenses, and perform professional services. Our quarterly revenues for software licenses and professional services may fluctuate, depending on various factors, including the timing of executed contracts and revenue recognition, and the delivery of contracted services or products. However, the costs associated with software and professional services revenues are not subject to the same degree of variability (i.e., these costs are generally fixed in nature within a relatively short period of time), and thus, fluctuations in our software and maintenance, professional services, and overall gross margins, will likely occur between periods.

Overall Gross Margin (Exclusive of Depreciation). Our overall gross margin for 2006, 2005, and 2004 was $188.6 million, $187.3 million, and $179.5 million, respectively. The overall gross margin percentages for 2006, 2005, and 2004 were 49.2%, 49.6%, and 51.1%, respectively. The changes in the gross margin and gross margin percentage between 2006, 2005, and 2004 were due to the factors discussed above.

R&D Expense. R&D expense for: (i) 2006 increased $12.3 million, or 36.1%, to $46.2 million, from $33.9 million; and (ii) 2005 increased $2.0 million, or 6.4%, to $33.9 million, from $31.9 million for 2004.

The increase in R&D expense between 2006 and 2005 was primarily due to an increase in employees, to include the development personnel that came over in the acquisition of Telution, and is reflective of our increased focus on product development and enhancement efforts.

The increase in R&D expense between 2005 and 2004 was primarily due to increased employee-related costs, to include the impacts of the annual merit wage increases.

During 2006, 2005, and 2004, we focused our development and enhancement efforts on various R&D projects consisting principally of enhancements to ACP and related software products, which includes the integration of the Telution COMX product

Table of Contents

with ACP beginning in March 2006. These development efforts are targeted to increase the functionalities and features of our products, including those necessary to service new and expanded product offerings provided by our clients (e.g., VoIP, commercial services, etc.). We did not capitalize any internal software development costs during 2006, 2005, and 2004.

As a percentage of total revenues, R&D expense for 2006, 2005, and 2004 was 12.1%, 9.0%, and 9.1%, respectively. At this time, we expect our future R&D efforts to continue to focus on similar tasks as noted above, and we expect that over time our investment in R&D will approximate our historical investment rate of 10-12% of our total revenues. However, consistent with the fourth quarter of 2006 (which reflected R&D expense as a percentage of total revenues of approximately 14%), we expect this percentage to be at or above the top end of this range in the near term.

Selling, General and Administrative Expense (SG&A). SG&A expense for: (i) 2006 decreased $9.4 million, or 17.8%, to $43.1 million, from $52.5 million for 2005; and (ii) 2005 increased $13.0 million, or 33.0%, to $52.5 million, from $39.5 million for 2004. As a percentage of total revenues, SG&A expense for 2006, 2005, and 2004 was 11.3%, 13.9%, and 11.2%, respectively.

The decrease in SG&A expense between 2006 and 2005 relates primarily to the $8.7 million decrease in retirement benefits recorded for our former CEO between periods, as discussed above.

The increase in SG&A expense between 2005 and 2004 relates primarily to: (i) an increase of $8.4 million related to the retirement benefits recorded for our former CEO, as discussed above; and (ii) an increase of $4.5 million in various personnel-related costs, principally related to stock-based compensation expense as a result of new equity awards.

Depreciation Expense. Depreciation expense for all property and equipment is reflected separately in the aggregate and is not included in the cost of revenues or the other components of operating expenses. Depreciation expense for 2006, 2005, and 2004 was $10.4 million, $9.9 million, and $10.4 million, respectively. The decrease in depreciation expense for 2005 relates primarily to the limited amount of capital expenditures in 2004 and 2003, as a result of our focus on cost controls during that time frame.

Restructuring Charges. Our restructuring charges relate to various cost reduction initiatives implemented primarily as a result of the changes we made to our business operations in 2005. See Note 8 to our Consolidated Financial Statements for a more detailed discussion of our cost reduction initiatives and related restructuring charges, including the current activity in accrued liabilities related to the restructuring charges. Restructuring charges included in total operating expenses, and the impact (net of related estimated income tax expense) these restructuring charges had on net income from continuing operations and diluted earnings per share, for 2006, 2005, and 2004, are as follows (in thousands, except diluted earnings per share):

	2006	2005	2004
Activities related to the sale of the GSS Business:			
Stock-based compensation related to change in control provision	$	$ 3,783	$
Involuntary termination of executive officer		1,357	
Involuntary termination of certain corporate support staff	379	590	
Management incentive bonuses related to the GSS Business sale		1,409	
Subtotal restructuring charges related to the sale of the GSS Business	379	7,139	
Disposal of corporate aircraft	100	1,556	
Termination of the FairPoint contract	1,115	6,209	
Facility abandonments	748	(389)	1,045
All other restructuring charges	26	19	247
Total restructuring charges	$ 2,368	$ 14,534	$ 1,292
Impact of restructuring charges on results of continuing operations (i.e., have reduced operating results):			
Net income	$ 1,467	$ 9,311	$ 820

Diluted earnings per share	$ 0.03	$ 0.19	$ 0.02

31

Table of Contents

At this time, we do not expect to incur any material restructuring charges in 2007.

Operating Income. Operating income for: (i) 2006 was $86.5 million, or 22.6% of total revenues, compared to $76.4 million, or 20.3% of total revenues for 2005; and (ii) 2005 was $76.4 million, or 20.3% of total revenues, compared to $96.5 million, or 27.5% of total revenues for 2004.

The increases in operating income and the operating income margin between 2006 and 2005 were due primarily to the decreases in restructuring charges between years and the expense incurred in conjunction with the retirement of our former CEO, as discussed above. The $14.5 million of restructuring charges in 2005 and the $8.9 million of retirement benefits recorded in 2005 had the effect of reducing our operating margin by 6.2 percentage points for 2005. Ignoring the one-time impact of these items on 2005, the comparable, normalized operating margins between years decreased, with such decrease in 2006 related primarily to our 2006 increase in R&D expense, and the impact of our Telution acquisition in March 2006.

The decreases in operating income and the operating income margin between 2005 and 2004 were due primarily to the increase in restructuring charges between years, and the expense incurred in conjunction with the retirement of our former CEO, as discussed above. Ignoring the one-time 6.2 percentage point impact of these items on 2005, the comparable, normalized operating margins between years decreased, with such decrease in 2005 related primarily to our investment in our ACP product initiatives without a commensurate increase in revenues associated with such initiatives.

Our operating income margin for the fourth quarter of 2006 was approximately 21%, down from the third quarter of 2006 operating margin of approximately 23%. This downward trend is reflective of our increased R&D efforts (as discussed above), as well as new product support costs being incurred without a commensurate increase in revenues at this time.

Our operating results include non-cash charges related to depreciation, amortization (primarily shown as a reduction of processing revenues), and stock-based compensation expense. The total amount of these non-cash expenses, and their impact (net of related estimated income tax expense) on net income from continuing operations and diluted earnings per share, for 2006, 2005, and 2004 are as follows (in thousands, except diluted earnings per share):

	2006	2005	2004
Non-cash expenses related to:			
Depreciation	$ 10,438	$ 9,862	$ 10,412
Amortization	15,913	13,586	11,598
Stock-based employee compensation	12,214	17,047	10,620
Total	$ 38,565	$ 40,495	$ 32,630
Impact of non-cash expenses on results of continuing operations (i.e., have reduced operating results):			
Net income	$ 23,895	$ 25,941	$ 20,720
Diluted earnings per share	$ 0.51	$ 0.53	$ 0.40

Interest Expense. The following are the key points related to our interest expense between years:

Interest expense for: (i) 2006 and 2005 remained consistent between periods at $7.5 million; and (ii) 2005 decreased $2.8 million, or 26.5%, to $7.5 million, from $10.3 million for 2004.

The weighted-average balance of our long-term debt for 2006, 2005, and 2004 was $230.0 million, $230.0 million, and $224.2 million, respectively.

The weighted-average interest rate on our debt borrowings for 2006, 2005, and 2004, including the amortization of deferred financing costs and commitment fees on our revolving credit facility, was 3.2%, 3.2%, and 4.1%, respectively. The change in the weighted-average balance of our long-term debt and the weighted-average interest rate between 2005 and 2004 relates primarily to the issuance of our Convertible Debt Securities in June 2004 and the retirement of our

Table of Contents

2002 Credit Facility with the proceeds from such issuance. The Convertible Debt Securities have a stated coupon rate of 2.5%, which is substantially less than the interest rates paid on our previous bank debt. See Note 7 to our Consolidated Financial Statements for additional discussion of our Convertible Debt Securities.

Write-off of Deferred Financing Costs. As result of the repayment and termination of the 2002 Credit Facility with the proceeds from the issuance of our Convertible Debt Securities in June 2004, we wrote-off unamortized deferred financing costs attributable to the 2002 Credit Facility of $6.6 million (pretax impact) during the second quarter of 2004, which had the effect of reducing our 2004 net income per diluted share by $0.08.

Interest and Investment Income, net. Interest and investment income, net, for: (i) 2006 increased $17.9 million to $22.0 million, from $4.1 million for 2005; and (ii) 2005 increased $3.1 million to $4.1 million, from $1.0 million for 2004.

The large increase in interest and investment income between 2006 and 2005 was primarily a result of a significant increase in our cash, cash equivalents, and short-term investment balances between periods, primarily the result of the cash proceeds we received from the sale of the GSS Business in December 2005.

The increase in interest and investment income between 2005 and 2004 is primarily attributable to an increase in operating funds available for investment throughout the year and the interest earned during December 2005 on the cash proceeds received from the sale of the GSS Business.

Income Tax Provision. The following are the key changes related to our income tax provision from continuing operations between years:

For 2006, we recorded an income tax provision of $38.4 million, or an effective income tax rate of approximately 38%, compared to an income tax provision of $26.2 million, or an effective income tax rate of approximately 36% in 2005.

For 2005, we recorded an income tax provision of $26.2 million, or an effective income tax rate of approximately 36%, compared to an income tax provision of $29.3 million, or an effective income tax rate of approximately 37% for 2004.

For the fourth quarter of 2006, we recorded an effective income tax rate of approximately 42%. The higher effective income tax rate was primarily the result of a correction of minor income tax expense items from previous periods that were not considered material to the current or past periods, giving consideration to the SEC s Staff Accounting Bulletin No. 108, and thus were recorded in their entirety in the fourth quarter. The accounting correction of these items is considered one-time in nature, and is not expected to materially impact our estimated income tax rate going forward.

As of December 31, 2006, our net deferred income tax assets were $28.5 million and represented approximately 4% of total assets. We continue to believe that sufficient taxable income will be generated in the future to realize the benefit of these deferred income tax assets. Our assumptions of future profitable operations are supported by our strong operating performances over the last several years.

Discontinued Operations. As discussed above, as a result of the sale of the GSS and plaNet businesses in December 2005, the GSS and plaNet businesses have been reflected as discontinued operations in our results of operations for all periods presented. Gain (loss) from discontinued operations (net of tax) for 2006, 2005, and 2004 was $(2.8) million, $6.5 million, and $(3.8) million, respectively.

Discontinued operations activity for 2006 consisted of the following:

During the third quarter of 2006, we made a $6.0 million payment to Comverse related to the settlement of a dispute over a joint tax election associated with the sale of our GSS Business to Comverse in December 2005. This payment was considered a reduction in the purchase price previously paid by Comverse, and thus is reflected as part of discontinued operations. This settlement payment was not anticipated, and we do not expect any similar purchase price adjustments in future periods.

During the fourth quarter of 2006, we recorded an income tax benefit from the true-up of certain state income tax items related to the GSS Business. The previous accounting for these matters was appropriately based on various estimates. With the filing of the various state income tax returns during the fourth quarter, the determination of the actual benefits due is now certain.

As a result of this activity, 2006 net income per diluted share was reduced by $(0.06).

Discontinued operations activity for 2005 included a net pretax gain on the disposals of the GSS and plaNet businesses of $10.9 million.

Liquidity

Basis of Presentation. Cash flows have not been segregated between continuing operations and discontinued operations in the accompanying Consolidated Statements of Cash Flows. Therefore, unless indicated otherwise, all historical cash flow information presented below reflects the cash flow results from both continuing and discontinued operations.

Cash and Liquidity. As of December 31, 2006, our principal sources of liquidity included cash, cash equivalents, and short-term investments of $415.5 million, compared to $392.2 million as of December 31, 2005. We generally invest our excess cash balances in low-risk, short-term investments to limit our exposure to market risks. We have ready access to all of our cash, cash equivalents, and short-term investment balances.

In addition to the above sources of liquidity, we also have a $100 million senior secured revolving credit facility (the 2004 Revolving Credit Facility) with a syndicate of U.S. financial institutions that expires in September 2009. The 2004 Revolving Credit Facility has a $40 million sub-facility for standby and commercial letters of credit and a $10 million sub-facility for same day advances. As of the date of this filing, we have made no borrowings under the 2004 Revolving Credit Facility. Our ability to borrow under the 2004 Revolving Credit Facility is subject to a limitation of total indebtedness based upon the results of consolidated leverage and interest coverage ratio calculations, and a minimum liquidity requirement. As of December 31, 2006, we were in compliance with the financial ratios and other covenants of the 2004 Revolving Credit Facility, and had the entire $100 million available to us.

Cash Flows From Operating Activities. We calculate our cash flows from operating activities in accordance with generally accepted accounting principles, beginning with net income and then adding back the impact of non-cash items (e.g., depreciation, amortization, stock-based compensation, etc.), and then factoring in the impact of changes in working capital items.

Our primary source of cash is from our operating activities. Our current business model consists of a significant amount of recurring revenue sources related to our long-term processing arrangements (billed monthly), and software maintenance agreements (billed monthly, quarterly, or annually.) This recurring revenue base provides us with a reliable and predictable source of cash. In addition, software license fees and professional services revenues provide for material amounts of cash, but the payment streams for these items are not as predictable.

The primary use of our cash is to fund our operating activities. Approximately 50% of our total operating costs relate to labor costs (both employees and contracted labor) for: (i) compensation; (ii) related fringe benefits; and (iii) reimbursements for travel and entertainment expenses. The other primary cash requirements for our operating expenses consist of: (i) postage; (ii) paper and related supplies for our statement processing centers; (iii) data processing and related services and communication lines for our service bureau processing business; and (iv) rent and related facility costs. These items are purchased under a variety of both short-term and long-term contractual commitments. A summary of our material contractual obligations is provided below as well.

See Cash Flows From Investing Activities and Cash Flows From Financing Activities below for the other primary uses of our cash.

Table of Contents

Our 2005 and 2006 consolidated net cash flows from operating activities, broken out between operations and changes in working capital assets and liabilities, for the indicated periods are as follows (in thousands):

	Operations	Changes in Working Capital Assets and Liabilities	Net Cash Provided by Operating Activities Quarter Totals
Cash Flows from Operating Activities:			
2005:			
March 31(1)	$ 25,147	$ (6,282)	$ 18,865
June 30(1)	30,704	12,579	43,283
September 30	26,245	(1,533)	24,712
December 31(2)	29,576	(13,862)	15,714
Year-to-date total	$ 111,672	$ (9,098)	$ 102,574
2006:			
March 31	$ 25,872	$ (3,894)	$ 21,978
June 30(3)	29,358	9,393	38,751
September 30	31,489	(2,937)	28,552
December 31	29,549	(680)	28,869
Year-to-date total	$ 116,268	$ 1,882	$ 118,150

(1) Cash flows from operating activities for the first quarter of 2005 were negatively impacted by approximately $9 million due to a key client delaying payment of an invoice until after quarter-end. This amount was subsequently paid in April 2005, which resulted in the payment of four monthly invoices by this client in the second quarter of 2005. The payment of the delayed invoice, along with a contract termination settlement and client bankruptcy settlement contributed approximately $12 million to our cash flows from operating activities for the second quarter of 2005.

(2) Cash flows from operating activities for the fourth quarter of 2005 were negatively impacted by approximately $10 million due to a key client delaying payment of an invoice until after quarter-end. Cash flows for each quarter of 2006 reflect three monthly invoice payments from this client.

(3) Cash flows from operating activities for the second quarter of 2006 were positively impacted by favorable changes in working capital items during the quarter, primarily related to the reduction in the accounts receivable balance.

We believe the above table illustrates our ability to consistently generate strong quarterly and annual cash flows, and the importance of managing our working capital items, in particular, timely collections of our accounts receivable.

Management of our billed accounts receivable is one of the primary factors in maintaining strong quarterly cash flows from operating activities. Our billed trade accounts receivable balance includes billings for several non-revenue items (primarily postage, sales tax, and deferred revenue items). As a result, we evaluate our performance in collecting our accounts receivable through our calculation of days billings outstanding (DBO) rather than a typical days sales outstanding (DSO) calculation. DBO is calculated based on the billings for the period (including non-revenue items) divided by the average monthly net trade accounts receivable balance for the period. Our target range for our DBO is 55-65 days.

Table of Contents

Our gross and net billed trade accounts receivable and related allowance for doubtful accounts receivable (Allowance) related to our continuing operations as of the end of the indicated quarterly periods, and the related DBOs for the quarters then ended, are as follows (in thousands, except DBOs):

	Gross	Allowance	Net Billed