CSG SYSTEMS INTERNATIONAL INC
Form 10-Q/A
November 18, 2004
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

(Mark One)

x **AMENDMENT NO. 1 TO THE QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2004

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

7887 East Belleview, Suite 1000

Englewood, Colorado 80111

(Address of principal executive offices, including zip code)

(303) 796-2850

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). YES x NO ¨

Shares of common stock outstanding at August 4, 2004: 52,034,990.

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CSG SYSTEMS INTERNATIONAL, INC.

FORM 10-Q/A For the Quarter Ended June 30, 2004

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EXPLANATORY NOTE

CSG Systems International, Inc. (the Company or forms of the pronoun we) is filing this amendment to remove a reference to independent outside valuation firms and experts in Note 9 to our Condensed Consolidated Financial Statements, and this amendment does not result in the restatement of our previously reported financial position or results of operations for the periods covered in the report. This report continues to speak as of the date of the original filing, and the Company has not updated the disclosure in this report to speak as of a later date. All information contained in this report and the original filing is subject to updating and supplementing as provided in the Company s periodic reports filed with the Commission.

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CSG SYSTEMS INTERNATIONAL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

	June 30, 2004	December 31, 2003
	(unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 129,004	$ 105,397
Short-term investments	2,197	
Total cash, cash equivalents and short-term investments	131,201	105,397
Trade accounts receivable-		
Billed, net of allowance of $6,942 and $11,145	123,720	130,691
Unbilled and other	13,756	18,042
Deferred income taxes	5,971	9,134
Income taxes receivable	4,353	35,076
Other current assets	12,000	11,697
Total current assets	291,001	310,037
Property and equipment, net of depreciation of $94,134 and $89,529	33,827	38,218
Software, net of amortization of $70,069 and $62,957	31,414	37,780
Goodwill	217,778	219,199
Client contracts, net of amortization of $56,143 and $50,973	52,772	57,458
Deferred income taxes	49,485	53,327
Other assets	8,893	8,756
Total assets	$ 685,170	$ 724,775
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Current maturities of long-term debt	$	$ 45,137
Client deposits	19,317	17,175
Trade accounts payable	21,187	21,291
Accrued employee compensation	28,129	32,415
Deferred revenue	57,870	52,655
Income taxes payable	15,894	20,723
Arbitration charge payable		25,181
Other current liabilities	20,725	25,818
Total current liabilities	163,122	240,395
Non-current liabilities:		
Long-term debt, net of current maturities	230,000	183,788
Deferred revenue	4,381	3,270
Other non-current liabilities	5,306	6,537
Total non-current liabilities	239,687	193,595

Stockholders equity:		
Preferred stock, par value $.01 per share; 10,000,000 shares authorized; zero shares issued and outstanding		
Common stock, par value $.01 per share; 100,000,000 shares authorized; 17,526,955 and 8,911,634 shares reserved for employee stock purchase plan, stock incentive plans, and convertible debt securities; 52,029,424 and 53,788,062 shares outstanding	597	593
Additional paid-in capital	292,721	281,784
Deferred employee compensation	(2,646)	(4,458)
Accumulated other comprehensive income:		
Unrealized gain (loss) on short-term investments, net of tax	(2)	1
Cumulative translation adjustments	6,755	6,519
Treasury stock, at cost, 7,636,496 and 5,499,796 shares	(211,110)	(171,111)
Accumulated earnings	196,046	177,457
Total stockholders equity	282,361	290,785
Total liabilities and stockholders equity	$ 685,170	$ 724,775

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

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CSG SYSTEMS INTERNATIONAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share amounts)

	Three Months Ended		Six Months Ended	
	June 30, 2004	June 30, 2003	June 30, 2004	June 30, 2003
	(unaudited)		(unaudited)	
Revenues:				
Processing and related services	$ 80,895	$ 91,041	$ 162,027	$ 182,217
Software	8,109	12,148	15,746	22,312
Maintenance	23,653	22,828	48,704	45,231
Professional services	17,006	16,344	33,550	34,533
Total revenues	129,663	142,361	260,027	284,293
Cost of revenues:				
Cost of processing and related services	34,619	35,557	68,425	69,676
Cost of software and maintenance	17,162	17,395	33,436	35,705
Cost of professional services	15,616	14,673	29,766	33,228
Total cost of revenues	67,397	67,625	131,627	138,609
Gross margin (exclusive of depreciation)	62,266	74,736	128,400	145,684
Operating expenses:				
Research and development	14,382	16,922	30,222	32,420
Selling, general and administrative	22,242	32,184	45,465	62,020
Depreciation	3,517	4,334	7,153	8,933
Restructuring charges	145	993	2,296	4,152
Total operating expenses	40,286	54,433	85,136	107,525
Operating income	21,980	20,303	43,264	38,159
Other income (expense):				
Interest expense	(2,684)	(3,482)	(6,238)	(7,356)
Write-off of deferred financing costs	(6,569)		(6,569)	
Interest and investment income, net	273	443	556	731
Other, net	(537)	2,443	(1,050)	2,829
Total other	(9,517)	(596)	(13,301)	(3,796)
Income before income taxes	12,463	19,707	29,963	34,363
Income tax provision	(4,707)	(7,988)	(11,374)	(13,937)
Net income	$ 7,756	$ 11,719	$ 18,589	$ 20,426

Basic net income per common share:				
Net income available to common stockholders	$ 0.15	$ 0.23	$ 0.36	$ 0.40
Weighted average common shares	51,285	51,355	51,483	51,330
Diluted net income per common share:				
Net income available to common stockholders	$ 0.15	$ 0.23	$ 0.36	$ 0.40
Weighted average common shares	52,096	51,656	52,175	51,570

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

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CSG SYSTEMS INTERNATIONAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Six months ended	
	June 30, 2004	**June 30, 2003**
	(unaudited)	
Cash flows from operating activities:		
Net income	$ 18,589	$ 20,426
Adjustments to reconcile net income to net cash provided by operating activities-		
Depreciation	7,153	8,933
Amortization	13,572	12,366
Restructuring charge for abandonment of facilities	595	683
Loss on short-term investments	3	
Write-off of deferred financing costs	6,569	
Deferred income taxes	7,046	1,958
Tax benefit of stock options exercised	423	9
Stock-based employee compensation	7,945	2,709
Changes in operating assets and liabilities:		
Trade accounts and other receivables, net	11,654	(3,496)
Other current and noncurrent assets	(401)	(546)
Arbitration charge payable	(25,181)	
Income taxes payable/receivable	27,454	481
Accounts payable and accrued liabilities	(9,064)	(4,690)
Deferred revenue	5,794	20,530
Net cash provided by operating activities	72,151	59,363
Cash flows from investing activities:		
Purchases of property and equipment	(2,785)	(2,920)
Purchases of short-term investments	(6,813)	(11)
Proceeds from sale of short-term investments	4,610	
Acquisition of businesses and assets, net of cash acquired	(852)	(2,335)
Acquisition of and investments in client contracts	(1,185)	(1,030)
Net cash used in investing activities	(7,025)	(6,296)
Cash flows from financing activities:		
Proceeds from issuance of common stock	4,833	855
Repurchase of common stock	(40,448)	
Proceeds from long-term debt	230,000	
Payments on long-term debt	(228,925)	(21,075)
Payments of deferred financing costs	(7,158)	(87)
Net cash used in financing activities	(41,698)	(20,307)
Effect of exchange rate fluctuations on cash	179	227

Net increase in cash and cash equivalents	23,607	32,987
Cash and cash equivalents, beginning of period	105,397	94,424
Cash and cash equivalents, end of period	$ 129,004	$ 127,411
Supplemental disclosures of cash flow information:		
Cash paid (received) during the period for-		
Interest	$ 5,009	$ 5,774
Income taxes	(25,172)	9,625

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

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CSG SYSTEMS INTERNATIONAL, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL

The accompanying unaudited condensed consolidated financial statements as of June 30, 2004 and December 31, 2003, and for the three and six months ended June 30, 2004 and 2003, have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information, and pursuant to the instructions to Form 10-Q and the rules and regulations of the Securities and Exchange Commission (the SEC). Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation of the financial position and operating results have been included. The condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto, together with Management s Discussion and Analysis of Financial Condition and Results of Operations, contained in the Company s amended Annual Report on Form 10-K/A for the year ended December 31, 2003, filed with the SEC (the Company s 2003 10-K). The results of operations for the three and six months ended June 30, 2004, are not necessarily indicative of the expected results for the entire year ending December 31, 2004.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Postage. The Company passes through to its clients the cost of postage that is incurred on behalf of those clients, and typically requires an advance payment on expected postage costs. These advance payments are included in client deposits in the accompanying Condensed Consolidated Balance Sheets and are classified as current liabilities regardless of the contract period. The Company nets the cost of postage against the postage reimbursements, and includes the net amount in processing and related services revenues. The total cost of postage incurred on behalf of clients that has been netted against processing and related services revenues for the three months ended June 30, 2004 and 2003 was $44.0 million and $38.5 million, respectively, and for the six months ended June 30, 2004 and 2003 was $88.3 million and $76.4 million, respectively.

Stock-Based Compensation Expense. During the fourth quarter of 2003, the Company adopted the fair value method of accounting for stock-based awards in accordance with Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation (SFAS 123), using the prospective method of transition as outlined in SFAS No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure An Amendment of FASB Statement No. 123 (SFAS 148). The adoption of SFAS 123 was effective as of January 1, 2003. Under the prospective method of transition, all stock-based awards granted, modified, or settled on or after January 1, 2003, are accounted for in accordance with SFAS 123. Stock-based awards granted prior to January 1, 2003, continue to be accounted for in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees , and related Interpretations (APB 25), and follow the disclosure provisions of SFAS 123 and SFAS 148. As a result, the Company has restated its condensed consolidated financial statements for the three and six months ended June 30, 2003 to reflect the inclusion of additional stock-based compensation expense of $0.2 million and $0.3 million, respectively.

At June 30, 2004, the Company had five stock-based compensation plans. The Company recorded stock-based compensation expense of $3.8 million and $1.4 million, respectively, for the three months ended June 30, 2004 and 2003 and $7.9 million and $2.7 million, respectively, for the six months ended June 30, 2004 and 2003. Stock-based compensation expense is included in the following income statement captions in the accompanying Condensed Consolidated Statements of Income (in thousands):

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	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Cost of processing and related services	$ 643	$ 13	$ 1,264	$ 16
Cost of software and maintenance	251	4	469	5
Cost of professional services	299	5	574	8
Research and development	459	11	930	14
Selling, general and administrative	2,148	1,381	4,708	2,666
Total stock-based compensation expense	$ 3,800	$ 1,414	$ 7,945	$ 2,709

Awards under the Company s stock-based compensation plans generally vest over periods ranging from three to four years. Because the Company follows APB 25 for all stock-based awards granted prior to January 1, 2003, and the prospective method of transition under SFAS 148 for stock-based awards granted, modified, or settled on or after January 1, 2003, compensation expense recorded in the Company s accompanying Consolidated Statements of Income is less than what would have been recognized if the fair value based method under SFAS 123 had been applied to all awards for all periods. Had compensation expense for the Company s five stock-based compensation plans been based on the fair value at the grant dates for awards under those plans for all periods, consistent with the methodology of SFAS 123, the Company s net income and net income per share available to common stockholders for the three and six months ended June 30, 2004 and 2003, would approximate the pro forma amounts as follows (in thousands, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Net income, as reported	$ 7,756	$ 11,719	$ 18,589	$ 20,426
Add: Stock-based compensation expense included in reported net income, net of related tax effects	2,362	879	4,938	1,684
Deduct: Total stock-based compensation expense determined under the fair value-based method for all awards, net of related tax effects	(3,814)	(5,258)	(7,667)	(10,604)
Net income, pro forma	$ 6,304	$ 7,340	$ 15,860	$ 11,506
Net income per share:				
Basic as reported	$ 0.15	$ 0.23	$ 0.36	$ 0.40
Basic pro forma	0.12	0.14	0.31	0.22
Diluted as reported	0.15	0.23	0.36	0.40
Diluted pro forma	0.12	0.14	0.31	0.22

Reclassification and Restatement. Certain June 30, 2003 amounts have been reclassified to conform to the June 30, 2004 presentation. In addition, as discussed above, the Company restated 2003 amounts to reflect the adoption of SFAS 123 effective January 1, 2003.

3. DEBT

Convertible Debt Securities

On June 2, 2004, the Company completed an offering of $230.0 million of 2.5% senior subordinated convertible contingent debt securities due June 15, 2024 (the Convertible Debt Securities) to qualified buyers pursuant to Rule 144A under the Securities Act of 1933.

The Company used the proceeds from the Convertible Debt Securities, along with available cash, cash equivalents

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and short-tem investments, to: (i) repay the outstanding balance of $198.9 million and terminate its 2002 Credit Facility (including the revolving credit facility); (ii) repurchase 2.1 million shares of the Company s common stock for $40.0 million (market price of $18.72 per share) from the initial purchasers of the Convertible Debt Securities; and (iii) pay debt issuance costs of $6.9 million, of which $6.3 million consisted of underwriting commissions.

The Convertible Debt Securities are unsecured, subordinated to any of the Company s future senior debt, and senior to the Company s future junior subordinated debt. The Convertible Debt Securities, issued at a price of 100% of their principal amount, bear interest at a rate of 2.5% per annum, which is payable semiannually in arrears on June 15 and December 15 of each year, beginning on December 15, 2004. The $6.9 million of deferred financing costs related to the Convertible Debt Securities issuance are being amortized to interest expense over seven years. The Convertible Debt Securities are callable by the Company for cash, on or after June 20, 2011, at a redemption price equal to 100% of the principal amount of the Convertible Debt Securities, plus accrued interest. The Convertible Debt Securities can be put back to the Company by the holders for cash at June 15, 2011, 2016 and 2021, or upon a change of control, at a repurchase price equal to 100% of the principal amount of the Convertible Debt Securities, plus any accrued interest.

Commencing with the six-month period beginning June 15, 2011, the Company will pay contingent interest equal to 0.25% of the average trading price of the Convertible Debt Securities during any six-month period if the average trading price of the Convertible Debt Securities for the five consecutive trading days ending on the second trading day immediately preceding the first day of the six-month period equals 120% or more of the principal amount of the Convertible Debt Securities.

The Convertible Debt Securities are convertible into the Company s common stock, under the specified conditions below, at an initial conversion rate of 37.3552 shares per $1,000 principal amount of Convertible Debt Securities, which is equal to a conversion price of $26.77 per share and represents a maximum of 8.6 million shares of potentially issuable Company common stock. The conversion rate can be adjusted in the future for certain events, to include stock dividends, stock splits/reverse splits, the issuance of warrants to purchase Company stock at a price below the then-current market price, cash dividends, and certain purchases by the Company of its common stock pursuant to a tender offer or exchange offer.

Holders of the Convertible Debt Securities can convert their securities: (i) at any time the price of the Company s common stock trades over $34.80 per share (130% of the $26.77 conversion price) for a specified period of time; (ii) at any time the trading price of the Convertible Debt Securities fall below 98% of the average conversion value for the Convertible Debt Securities for a specified period of time; (iii) upon the Company exercising its right to redeem the Convertible Debt Securities at any time after June 20, 2011; and (iv) at any time upon the occurrence of specified corporate transactions, to include a change in control.

The Company has the right to settle the Convertible Debt Securities upon conversion by delivering Company common stock, cash or any combination of Company common stock and cash. At any time prior to maturity, the Company may irrevocably elect at its sole discretion to satisfy in cash 100% of the principal amount of the Convertible Debt Securities converted after the date of such election. After such election, the Company may still satisfy its conversion obligation, to the extent it exceeds the principal amount in cash or common stock, or a combination of cash and common stock.

As of June 30, 2004, the Convertible Debt Securities were not registered with the SEC. The Company has entered into a registration rights agreement with the initial purchasers, in which the Company has agreed to: (i) file a shelf registration statement with the SEC for the benefit of the holders of the Convertible Debt Securities within 90 days of the completion of the Convertible Debt Securities offering; (ii) use reasonable best efforts to cause such registration statement to become effective as promptly as possible, but in no event later than 180 days from the completion of the Convertible Debt Securities offering; and (iii) keep the registration statement effective for a specified period of time. If the Company defaults on the registration rights agreement, it will be required to pay additional interest at a rate of 0.25% per annum on the principal amount of the Convertible Debt Securities up to and including the 90th day following such default, and additional interest at a rate of 0.50% per annum on the principal amount of the Convertible Debt Securities from and after the 91st day following such default. On July 16, 2004, the Company filed, with the SEC, a shelf registration statement on Form S-3 for the Convertible Debt Securities.

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The fair value of the Convertible Debt Securities as of June 30, 2004, based upon quoted market prices, was approximately $237 million. The contingent interest feature of the Convertible Debt Securities discussed above is considered an embedded derivative that is required to be bifurcated and accounted for as a freestanding derivative financial instrument. The fair value of this derivative financial instrument, as of June 30, 2004, was not significant.

2002 Credit Facility

New Amendments. During the first quarter of 2004, the Company entered into two amendments to its 2002 Credit Facility. The Second Amendment was made to clarify the Company s ability to repurchase its common stock in certain situations pursuant to the Company s stock-based compensation plans. The Third Amendment was made in conjunction with the Company signing the Comcast Contract (see Note 7).

Mandatory Prepayment. In March 2004, the Company made a $30 million mandatory prepayment on its 2002 Credit Facility using the proceeds from income tax refunds received in the first quarter of 2004. This $30 million mandatory prepayment, required under the First Amendment to the 2002 Credit Facility, was to be paid on or before July 30, 2004.

Repayment and Termination. As discussed above, the Company used a portion of the proceeds from the Convertible Debt Securities to repay and terminate the 2002 Credit Facility. As a result, the Company wrote-off unamortized deferred financing costs attributable to the 2002 Credit Facility of $6.6 million during the second quarter of 2004.

4. STOCKHOLDERS EQUITY AND EQUITY COMPENSATION PLANS

Modifications to Stock-Based Compensation Awards. During the first quarter of 2004, the Company modified the terms of approximately 406,000 shares of unvested restricted stock, and 116,000 unvested stock options held by key members of management (members other than executive management) to include a provision which allows for full vesting of the stock-based awards upon a change in control of the Company. Unless such an event occurs, the stock-based awards will continue to vest as set forth in the original terms of the agreements. This modification did not have a significant impact on total stock-based compensation expense in the first quarter of 2004.

1996 Employee Stock Purchase Plan. During the second quarter of 2004, the Company s stockholders approved a 500,000 share increase in the authorized number of shares available under the 1996 Employee Stock Purchase Plan, bringing the total number of authorized shares to be sold under the plan to 958,043. As of June 30, 2004, 534,909 shares remain eligible for purchase under the plan.

Stock Repurchase Program. Effective June 2, 2004, the Company s Board of Directors approved a five million increase in the number of shares the Company is authorized to repurchase under its stock repurchase program, bringing the total number of authorized shares to 15.0 million. During the second quarter of 2004 (in conjunction with the issuance of the Convertible Debt Securities) the Company repurchased 2.1 million shares of its common stock for $40.0 million (market price of $18.72 per share). As of June 30, 2004, the total shares repurchased under the Company s stock repurchase program since its inception in August 1999 totaled 8.5 million shares, at a total repurchase price of approximately $240 million (weighted-average price of $28.28 per share). At June 30, 2004, the total remaining number of shares authorized for repurchase under the program totaled 6.5 million shares.

5. EARNINGS PER COMMON SHARE

Earnings per common share (EPS) has been computed in accordance with SFAS No. 128, Earnings Per Share . Basic EPS is computed by dividing income available to common stockholders (the numerator) by the weighted average number of common shares outstanding during the period (the denominator). Diluted EPS is consistent with the calculation of basic EPS while considering the effect of potentially dilutive common shares outstanding during the period. Unvested shares of restricted stock are not included in the basic EPS calculation. Basic and diluted EPS are presented on the face of the Company s Condensed Consolidated Statements of Income.

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No reconciliation of the basic and diluted EPS numerators is necessary for the three and six months ended June 30, 2004 and 2003, as net income is used as the numerator for each period. The reconciliation of the EPS denominators is included in the following table (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Basic common shares outstanding	51,285	51,355	51,483	51,330
Dilutive effect of stock options	403	112	341	102
Dilutive effect of unvested restricted stock	408	189	351	138
Dilutive effect of Convertible Debt Securities				
Diluted common shares outstanding	52,096	51,656	52,175	51,570

The following table sets forth the potential common shares that were excluded from the EPS computation as their effect was anti-dilutive (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Common stock options	799	5,817	993	6,420
Unvested restricted stock	529		816	
Total	1,328	5,817	1,809	6,420

The Convertible Debt Securities were excluded from the computation of diluted EPS since none of the contingent conversion features have been met as of June 30, 2004 (see Note 3). Under application of existing GAAP, the Convertible Debt Securities are not included within the computation of diluted EPS until one of the contingent conversion features has been met.

6. COMPREHENSIVE INCOME

The Company s components of comprehensive income were as follows (in thousands):

	Three Months Ended June 30,	Six Months Ended June 30,

	2004	2003	2004	2003
Net income	$ 7,756	$ 11,719	$ 18,589	$ 20,426
Other comprehensive income (loss), net of tax, if any:				
Foreign currency translation adjustments	(764)	4,947	237	2,903
Unrealized gain (loss) on short-term investments	(3)		(3)	7
Comprehensive income	$ 6,989	$ 16,666	$ 18,823	$ 23,336

7. SIGNIFICANT CLIENTS

Comcast Corporation

Arbitration Resolution. During 2002 and 2003, the Company was involved in various legal proceedings with its largest client, Comcast Corporation (Comcast), consisting principally of arbitration proceedings related to the Comcast Master Subscriber Agreement. In October 2003, the Company received the final ruling in the arbitration proceedings. The Comcast arbitration ruling included an award of $119.6 million to be paid by the Company to Comcast. The award was based on the arbitrator s determination that the Company had violated the most favored nations (MFN) clause of the Comcast Master Subscriber Agreement. The Company recorded the impact from the

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arbitration ruling in the third quarter of 2003 as a charge against its revenues. In the fourth quarter of 2003, the Company paid approximately $95 million of the arbitration award to Comcast, and in January 2004, the Company paid the remaining portion of the arbitration award of approximately $25 million. In addition to the arbitration award, the Company paid to Comcast interest of $1.1 million, of which $0.1 million was reflected as interest expense in the first quarter of 2004.

Signing of New Comcast Contract. In March 2004, the Company signed a new contract with Comcast (the Comcast Contract). The Comcast Contract superseded the former Comcast Master Subscriber Agreement that was set to expire at the end of 2012. The term of the new agreement runs through December 31, 2008. See Note 9 for discussion of the client contracts intangible asset related to the Comcast Contract.

Echostar Communications

Signing of New Contract Amendment. Echostar Communications (Echostar) is the Company s second largest client. In February 2004, the Company signed the Thirtieth Amendment to the Echostar Master Subscriber Agreement, extending the term of the Echostar Master Subscriber Agreement until March 1, 2006. The Echostar Master Subscriber Agreement was previously set to expire at the end of 2004.

8. SEGMENT INFORMATION

The Company serves its clients through its two operating segments: the Broadband Services Division (the Broadband Division) and the Global Software Services Division (the GSS Division). The Company s operating segment information and corporate overhead costs are presented below (in thousands, except percentages).

	Three Months Ended June 30, 2004			
	Broadband Division	GSS Division	Corporate	Total
Processing revenues	$ 80,278	$ 617	$	$ 80,895
Software revenues	935	7,174		