

TELETECH HOLDINGS INC

Form 10-Q

October 25, 2006

Table of Contents

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**Form 10-Q**

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

**For the quarterly period ended September 30, 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 001-11919**

**TeleTech Holdings, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**84-1291044**

(I.R.S. Employer  
Identification No.)

**9197 South Peoria Street**

**Englewood, Colorado 80112**

(Address of principal executive offices)

Registrant's telephone number, including area code: **(303) 397-8100**

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  NO

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. (Check one):

Large accelerated  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES  NO

As of October 19, 2006, there were 69,264,782 shares of the registrant's common stock outstanding.

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**SEPTEMBER 30, 2006 FORM 10-Q**  
**TABLE OF CONTENTS**

	<b>Page No.</b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
<u>Item 1. Condensed Consolidated Financial Statements (unaudited)</u>	1
<u>Condensed Consolidated Balance Sheets as of September 30, 2006 (unaudited) and December 31, 2005</u>	1
<u>Condensed Consolidated Statements of Operations and Comprehensive Income for the three months and nine months ended September 30, 2006 and 2005 (unaudited)</u>	2
<u>Condensed Consolidated Statements of Stockholders' Equity as of and for the nine months ended September 30, 2006 (unaudited)</u>	3
<u>Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2006 and 2005 (unaudited)</u>	4
<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	5
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	16
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	36
<u>Item 4. Controls and Procedures</u>	37
<b><u>PART II. OTHER INFORMATION</u></b>	37
<u>Item 1. Legal Proceedings</u>	37
<u>Item 1A. Risk Factors</u>	37
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	39
<u>Item 3. Defaults Upon Senior Securities</u>	39
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	39
<u>Item 5. Other Information</u>	39
<u>Item 6. Exhibits</u>	40
<b><u>SIGNATURES</u></b>	
<b><u>CERTIFICATIONS</u></b>	



**Table of Contents**

**Part I. FINANCIAL INFORMATION**  
**Item 1. Condensed Consolidated Financial Statements**  
**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Balance Sheets**  
(Amounts in thousands except per share amounts)

	(Unaudited) September 30, 2006	December 31, 2005
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 55,192	\$ 32,505
Accounts receivable, net	220,668	207,090
Prepaid and other assets	38,494	30,270
Deferred tax assets, net	11,960	12,990
Income tax receivable	16,146	16,298
Total current assets	342,460	299,153
<b>Long-term assets</b>		
Property and equipment, net	154,614	133,635
Goodwill	57,385	32,077
Contract acquisition costs, net	10,734	12,874
Deferred tax assets, net	38,563	30,621
Other assets	22,540	9,871
Total long-term assets	283,836	219,078
Total assets	\$ 626,296	\$ 518,231
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable	\$ 28,318	\$ 30,096
Accrued employee compensation and benefits	82,933	59,196
Other accrued expenses	36,632	40,422
Income tax payable	18,108	17,398
Deferred tax liabilities, net	1,542	2,556
Customer advances and deferred income	8,367	10,515
Total current liabilities	175,900	160,183
<b>Long-term liabilities</b>		
Capital lease obligations	680	976
Line of credit	77,750	26,700
Grant advances	7,163	6,476
Deferred tax liabilities	6,329	6,821
Other long-term liabilities	21,240	17,157

Total long-term liabilities	113,162	58,130
Total liabilities	289,062	218,313
<b>Commitments and contingent liabilities</b>		
<b>Minority interest</b>	6,731	6,544
<b>Stockholders equity</b>		
Common stock \$.01 par value; 150,000,000 shares authorized; 69,333,375 and 69,162,448 shares outstanding as of September 30, 2006 and December 31, 2005, respectively	693	694
Additional paid-in capital	150,617	146,367
Accumulated other comprehensive income	6,167	3,698
Retained earnings	173,026	142,615
Total stockholders equity	330,503	293,374
Total liabilities and stockholders equity	\$ 626,296	\$ 518,231

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

Table of Contents

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Operations and Comprehensive Income**  
(Amounts in thousands except per share amounts)  
(Unaudited)

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Revenue</b>	\$ 303,804	\$ 274,259	\$ 874,560	\$ 782,518
<b>Operating expenses</b>				
Cost of services	220,702	202,492	649,718	580,663
Selling, general and administrative	49,271	46,642	145,132	136,728
Depreciation and amortization	12,929	12,659	36,705	40,650
Restructuring charges, net	515	537	1,455	1,480
Impairment losses			478	2,537
Total operating expenses	283,417	262,330	833,488	762,058
<b>Income from operations</b>	20,387	11,929	41,072	20,460
<b>Other income (expense)</b>				
Interest income	662	882	1,350	2,448
Interest expense	(2,410)	(727)	(4,491)	(1,931)
Other, net	1,151	369	2,028	1,013
Total other income (expense)	(597)	524	(1,113)	1,530
<b>Income before income taxes and minority interest</b>	19,790	12,453	39,959	21,990
Provision for income taxes	6,428	432	7,889	3,204
<b>Income before minority interest</b>	13,362	12,021	32,070	18,786
Minority interest	(583)	(401)	(1,659)	(713)
<b>Net income</b>	\$ 12,779	\$ 11,620	\$ 30,411	\$ 18,073
<b>Other comprehensive income (loss)</b>				
Foreign currency translation adjustments	\$ 1,206	\$ 5,755	\$ 4,487	\$ 5,032
Derivatives valuation, net of tax	(86)	2,675	(2,018)	(1,397)
Total other comprehensive income (loss)	1,120	8,430	2,469	3,635

<b>Comprehensive income</b>	\$ 13,899	\$ 20,050	\$ 32,880	\$ 21,708
<b>Weighted average shares outstanding</b>				
Basic	69,085	71,650	68,979	72,946
Diluted	70,366	72,591	70,228	74,604
<b>Net income per share</b>				
Basic	\$ 0.18	\$ 0.16	\$ 0.44	\$ 0.25
Diluted	\$ 0.18	\$ 0.16	\$ 0.43	\$ 0.24

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

2

---



Table of Contents

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Stockholders Equity**  
(Amounts in thousands)  
(Unaudited)

	Common Stock		Additional	Accumulated Other	Retained	Total
	Shares	Amount	Paid-in Capital	Comprehensive Income	Earnings	Stockholders Equity
<b>Balance as of December 31, 2005</b>	69,162	\$694	\$146,367	\$ 3,698	\$142,615	\$293,374
Net income					30,411	30,411
Foreign currency translation adjustments				4,487		4,487
Derivatives valuation, net of tax				(2,018)		(2,018)
Exercise of stock options	1,335	11	10,821			10,832
Excess tax benefit from exercise of stock options			3,041			3,041
Compensation expense from stock options			5,024			5,024
Purchases of common stock	(1,164)	(12)	(14,636)			(14,648)
<b>Balance as of September 30, 2006</b>	69,333	\$693	\$150,617	\$ 6,167	\$173,026	\$330,503

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

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Cash Flows**  
(Amounts in thousands)  
(Unaudited)

	<b>Nine Months Ended</b>	
	<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>
<b>Cash flows from operating activities</b>		
Net income	\$ 30,411	\$ 18,073
Adjustment to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	36,705	40,650
Amortization of contract acquisition costs	2,327	2,942
Provision for doubtful accounts	1,714	378
Deferred income taxes	(5,810)	(17,763)
Minority interest	1,659	713
Impairment loss	478	2,537
Compensation expense from stock options	5,024	
Tax benefit from exercise of stock options		1,544
Loss on disposal of assets	241	74
Changes in assets and liabilities:		
Accounts receivable	(1,404)	(35,848)
Prepays and other assets	(12,578)	(3,760)
Accounts payable and accrued expenses	13,534	39,089
Customer advances and deferred income	311	4,103
Net cash provided by operating activities	72,612	52,732
<b>Cash flows from investing activities</b>		
Acquisition of a business, net of cash acquired of \$0.5 million	(46,412)	
Purchases of property and equipment	(51,219)	(26,763)
Purchases of intangible assets	(1,357)	(240)
Contract acquisition costs	(179)	(2,160)
Net cash used in investing activities	(99,167)	(29,163)
<b>Cash flows from financing activities</b>		
Proceeds from line of credit	380,700	243,100
Payments on line of credit	(329,650)	(243,100)
Debt refinancing fees	(811)	
Payments on long-term debt and capital lease obligations	(286)	(532)
Payments to minority shareholder	(1,498)	(2,700)
Proceeds from employee stock purchase plan		476
Excess tax benefit from exercise of stock options	3,041	
Proceeds from exercise of stock options	10,802	3,473
Purchases of treasury stock	(14,648)	(44,266)
Net cash provided by (used in) financing activities	47,650	(43,549)

Edgar Filing: TELETECH HOLDINGS INC - Form 10-Q

Effect of exchange rate changes on cash and cash equivalents	1,592	377
Increase (decrease) in cash and cash equivalents	22,687	(19,603)
Cash and cash equivalents, beginning of period	32,505	75,066
Cash and cash equivalents, end of period	\$ 55,192	\$ 55,463
<b>Supplemental disclosures</b>		
Cash paid for interest	\$ 2,862	\$ 788
Cash paid for income taxes	\$ 8,716	\$ 8,096

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

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

**(1) OVERVIEW AND BASIS OF PRESENTATION**

**Overview**

TeleTech Holdings, Inc. ( TeleTech or the Company ) serves its clients through two primary businesses: (i) Business Process Outsourcing ( BPO ), which provides outsourced business process, customer management, and marketing services for a variety of industries via operations in the United States ( U.S. ), Argentina, Australia, Brazil, Canada, China, Germany, India, Malaysia, Mexico, New Zealand, the Philippines, Singapore, Spain, the United Kingdom, and Venezuela; and (ii) Database Marketing and Consulting, which provides outsourced database management, direct marketing, and related customer acquisition and retention services for automotive dealerships and manufacturers in North America.

**Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared without audit pursuant to the rules and regulations of the Securities and Exchange Commission ( SEC ). The unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring entries) which, in the opinion of management, are necessary to present fairly the financial position of the Company as of September 30, 2006, and the results of operations and cash flows of the Company and its subsidiaries for the three months and nine months ended September 30, 2006 and 2005. Operating results for the three months and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ended December 31, 2006.

The unaudited condensed consolidated financial statements should be read in conjunction with the Company s audited consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005.

Certain amounts in 2005 have been reclassified in the condensed consolidated financial statements to conform to the 2006 presentation.

**Recently Issued Accounting Pronouncements**

In December 2004, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 123 (revised 2004) Share-Based Payment ( SFAS 123(R) ), which replaces SFAS No. 123 Accounting for Stock Issued to Employees ( SFAS 123 ). The Company adopted SFAS 123(R) on January 1, 2006. The impact of the adoption of SFAS 123(R) is discussed in Note 4.

In June 2006, the FASB issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109 ( FIN 48 ). FIN 48 is effective as of the beginning of the first annual period beginning after December 15, 2006. FIN 48 defines the threshold for recognizing the tax benefits of a tax return filing position in the financial statements as more-likely-than-not to be sustained by the taxing authority. This is different than the accounting practice currently followed by the Company, which is to recognize the best estimate of the impact of a tax position only when the position is probable of being sustained on audit based solely on the technical merits of the position. The term probable is consistent with the use of the term in SFAS No. 5 Accounting for Contingencies, to mean that the future event or events are likely to occur.

The Company is currently studying the impact FIN 48 will have on its consolidated financial statements when adopted. In the course of reevaluating the Company s tax return filing positions in light of the new more-likely-than-not standard, it is likely that the Company will reduce its liability for previously unrecognized tax benefits at the date of adoption. Consistent with the new accounting standard, any change to adjust the Company s consolidated financial statements arising from adoption of the new more-likely-than-not standard will be recognized in beginning retained earnings in the period of adoption as a change in accounting method.

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

**(2) ACQUISITION**

On June 30, 2006, the Company acquired 100 percent of the outstanding common shares of Direct Alliance Corporation ( DAC ) from Insight Enterprises, Inc. (NASDAQ: NSIT). DAC is a provider of outsourced direct marketing services to third parties in the U.S. and its acquisition is consistent with the Company s strategy to grow and to focus on providing outsourced marketing, sales, and BPO solutions to large multinational clients. DAC is included in the Company s North American BPO segment.

The preliminary total purchase price of \$46.4 million in cash was funded utilizing the Company s Credit Facility (see Note 7 to the Condensed Consolidated Financial Statements). The purchase agreement provides for the seller to (i) receive a future payment of up to \$11.0 million based upon the gross profit of DAC for 2006 exceeding specified amounts and (ii) pay the Company up to \$5.0 million in the event certain clients of DAC do not renew, on substantially similar terms, their service agreement with DAC as set forth in the purchase agreement.

The preliminary allocation of the purchase price to the assets acquired and liabilities assumed, based upon the Company s intention to make a 338 election for income tax reporting for the acquisition of DAC, is as follows (amounts in thousands):

Current assets	\$ 14,548
Property and equipment	4,410
Intangible assets	9,100
Goodwill	23,820
<b>Total assets acquired</b>	<b>\$ 51,878</b>
Current liabilities	(5,505)
<b>Total liabilities assumed</b>	<b>(5,505)</b>
Net assets acquired	\$ 46,373

The Company acquired identifiable intangible assets as a result of the acquisition of DAC. The intangible assets acquired, excluding costs in excess of net assets acquired, are preliminarily classified and valued as follows (amounts in thousands):

	<b>Value</b>	<b>Amortization Period</b>
Trade name	\$ 1,800	None; indefinite life
Customer relationships	7,300	10 years
<b>Total</b>	<b>\$ 9,100</b>	

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

The following table presents the pro-forma combined results of operations assuming (i) DAC's historical unaudited financial results, (ii) the DAC acquisition closed on January 1, 2005, (iii) pro-forma amortization expense of the intangible assets, and (iv) pro-forma interest expense assuming the Company utilized its Credit Facility to finance the acquisition (amounts in thousands):

	<b>Nine Months Ended</b>	
	<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>
Revenue	\$908,655	\$839,184
Income from operations	\$ 43,678	\$ 26,627
Net income	\$ 31,001	\$ 20,303
<b>Weighted average shares outstanding</b>		
Basic	68,979	72,946
Diluted	70,228	74,604
<b>Net income per share</b>		
Basic	\$ 0.45	\$ 0.28
Diluted	\$ 0.44	\$ 0.27

The pro-forma results above are not necessarily indicative of the operating results that would have actually occurred if the acquisition had been in effect on the date indicated, nor are they necessarily indicative of future results of the combined companies.

**(3) SEGMENT INFORMATION**

The Company serves its clients through two primary businesses, BPO Services and Database Marketing and Consulting. In previous filings the North American BPO segment was referred to as North American Customer Management and the International BPO segment was referred to as International Customer Management. BPO provides business process, customer management, and marketing services for a variety of industries via Customer Management Centers ( CMC or Center ) throughout the world. When the Company begins operations in a new country, it determines whether the country is intended to primarily serve U.S.-based clients, in which case the country is included in the North American BPO segment, or the country is intended to serve both domestic clients from that country and U.S.-based clients, in which case the country is included in the International BPO segment. This is consistent with the Company's management of the business, internal financial reporting structure, and operating focus. Operations for each segment of BPO Services are conducted in the following countries:

**North American BPO**

United States  
Canada  
India  
Philippines

**International BPO**

Argentina  
Australia  
Brazil  
China  
Germany  
Malaysia  
Mexico  
New Zealand  
Singapore  
Spain



**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

The Database Marketing and Consulting segment, which consists of one subsidiary company, provides outsourced database management, direct marketing, and related customer acquisitions and retention services for automobile dealerships and manufacturers operating in North America.

The Company allocates to each segment its estimated portion of corporate-level operating expenses. All intercompany transactions between the reported segments for the periods presented have been eliminated.

It is a significant Company strategy to garner additional business through the lower cost opportunities offered by certain foreign countries. Accordingly, the Company provides services to certain U.S. clients from CMCs in Argentina, Canada, India, Mexico, and the Philippines. Under this arrangement, while the U.S. subsidiary invoices and collects from the client, the U.S. subsidiary enters into a contract with the foreign subsidiary to reimburse the foreign subsidiary for its costs plus a reasonable profit. This reimbursement is reflected as revenue by the foreign subsidiary. As a result, a portion of the revenue from these client contracts is recorded by the U.S. subsidiary, while a portion is recorded by the foreign subsidiary. For U.S. clients served from Canada, India, and the Philippines, which represents the majority of these arrangements, all the revenue remains within the North American BPO segment. For U.S. clients served from Argentina and Mexico, a portion of the revenue is reflected in the International BPO segment. For the three months ended September 30, 2006 and 2005, approximately \$1.5 million and \$0.7 million, respectively, of income from operations in the International BPO segment were generated from these arrangements. For the nine months ended September 30, 2006 and 2005, approximately \$4.1 million and \$2.2 million, respectively, of income from operations in the International BPO segment were generated from these arrangements.

The following table presents Revenue and Income (Loss) from Operations by segment (amounts in thousands):

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Revenue</b>				
North American BPO	\$ 206,616	\$ 170,930	\$ 576,283	\$ 474,852
International BPO	90,336	82,596	264,277	244,157
Database Marketing and Consulting	6,852	20,733	34,000	63,509
Total	\$ 303,804	\$ 274,259	\$ 874,560	\$ 782,518
<b>Income (Loss) from Operations</b>				
North American BPO	\$ 25,194	\$ 15,654	\$ 55,995	\$ 40,752
International BPO	182	(1,871)	(3,731)	(12,188)
Database Marketing and Consulting	(4,989)	(1,854)	(11,192)	(8,104)
Total	\$ 20,387	\$ 11,929	\$ 41,072	\$ 20,460



**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

The following table presents Revenue based on the geographic location where the services are provided (amounts in thousands):

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Revenue</b>				
United States	\$ 108,421	\$ 119,158	\$ 318,448	\$ 330,898
Asia Pacific	65,071	46,413	172,099	135,488
Canada	48,311	49,689	157,001	146,511
Europe	35,699	30,866	105,274	92,171
Latin America	46,302	28,133	121,738	77,450
Total	\$ 303,804	\$ 274,259	\$ 874,560	\$ 782,518

**(4) EQUITY-BASED COMPENSATION**

The Company maintains several equity compensation plans (the Plans) for the benefit of certain of its directors, officers, and employees.

During the first quarter of fiscal 2006, the Company adopted SFAS 123(R), applying the modified prospective method. SFAS 123(R) requires all equity-based payments to employees, including grants of employee stock options, to be recognized in the Condensed Consolidated Statements of Operations and Comprehensive Income at the fair value of the award on the grant date. Under the modified prospective method, the Company is required to record equity-based compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards outstanding as of the date of adoption. The fair values of all stock options granted by the Company were determined using the Black-Scholes-Merton model (B-S-M Model).

The fair values of the options granted to the Company's employees were estimated on the date of grant using the B-S-M Model. The following table provides the range of assumptions used for stock options granted during the three months ended September 30, 2006 and 2005:

	<b>Three Months Ended</b>			
	<b>September 30,</b>			
	<b>2006</b>		<b>2005</b>	
Risk-free interest rate	4.73%	5.03%	3.75%	4.17%
Expected life in years	3.8	4.8		4.4
Expected volatility	54.81%		75.53%	
Dividend yield	0.00%		0.00%	
Weighted-average volatility	54.81%		75.53%	
Weighted-average fair value	\$	5.85	\$	5.09

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

A summary of option activity under the Plans as of September 30, 2006 and changes during the nine months then ended is presented below:

	<b>Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted- Average Remaining Contractual Term Years</b>	<b>Aggregate Intrinsic Value (in thousands)</b>
<b>Outstanding as of December 31, 2005</b>	8,486,681	\$ 10.26		
Grants	1,414,950	\$ 12.52		
Exercises	(1,386,186)	\$ 7.58		
Cancellations/expirations	(511,966)	\$ 12.91		
<b>Outstanding as of September 30, 2006</b>	8,003,479	\$ 10.95	6.9	\$ 43,396
<b>Vested and exercisable as of September 30, 2006</b>	3,690,697	\$ 11.76	4.7	\$ 20,803

A summary of the status of the Company's unvested shares as of September 30, 2006, and changes during the nine months ended September 30, 2006, is presented below:

	<b>Shares</b>	<b>Weighted- Average Grant- Date Fair Value</b>
<b>Unvested as of December 31, 2005</b>	4,129,995	\$ 5.62
Granted	1,414,950	\$ 5.85
Vested	(914,655)	\$ 5.33
Forfeited	(317,508)	\$ 5.57
<b>Unvested as of September 30, 2006</b>	4,312,782	\$ 5.76

As of September 30, 2006, there was approximately \$19.8 million of total unrecognized compensation cost (including the impact of expected forfeitures as required under SFAS 123(R)) related to unvested share-based compensation arrangements granted under the Plans that the Company had not recorded. That cost is expected to be recognized over the weighted-average period of four years (the Company recognizes compensation expense straight-line over the vesting term of the option grant). The total fair value of shares vested (excluding expected forfeitures) during the nine month period ended September 30, 2006 was \$4.9 million.

Cash received from option exercises under all share-based payment arrangements for the three months ended September 30, 2006 and 2005 was \$6.0 million and \$1.1 million, respectively.

Cash received from option exercises under all share-based payment arrangements for the nine months ended September 30, 2006 and 2005 was \$10.8 million and \$3.5 million, respectively.

As a result of adopting SFAS 123(R) on January 1, 2006, the Company's income before income taxes and net income for the three months ended September 30, 2006 are \$1.7 million and \$1.0 million lower, respectively, than if it had continued to account for share-based compensation under Accounting Principles Board Opinion ( APB ) No. 25

Accounting for Stock Issued to Employees ( APB 25 ). For the nine months ended September 30, 2006, the Company's income before income taxes and net income are \$5.0 million and \$3.0 million lower, respectively, than if it had continued to account for share-based compensation under APB 25. Basic and diluted earnings per share for the three months ended September 30, 2006 are \$0.02 and \$0.01 lower, respectively, than if the Company had continued to account for share-based compensation under APB 25. Additionally, basic and diluted earnings per share for the nine months ended September 30, 2006 are \$0.04 and \$0.04 lower, respectively. The compensation cost that has been charged against income for the Plans is included in Selling, General and Administrative Expenses in the Condensed Consolidated Statements of Operations and Comprehensive Income.

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

The following table illustrates the effect on net income and earnings per share for the three months and nine months ended September 30, 2005, if the Company had applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation (amounts in thousands except per share amounts):

	<b>September 30, 2005</b>	
	<b>Three Months Ended</b>	<b>Nine Months Ended</b>
<b>Net income as reported</b>	\$ 11,620	\$ 18,073
Add (deduct): Stock-based employee compensation expense included in reported net income, net of related tax effects	(1)	31
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(995)	(3,109)
<b>Pro forma net income</b>	<b>\$ 10,624</b>	<b>\$ 14,995</b>
 <b>Weighted average shares outstanding</b>		
Basic	71,650	72,946
Diluted	72,591	74,604
 <b>Net income per share</b>		
Basic as reported	\$ 0.16	\$ 0.25
Diluted as reported	\$ 0.16	\$ 0.24
Basic pro forma	\$ 0.15	\$ 0.21
Diluted pro forma	\$ 0.15	\$ 0.20

**(5) SIGNIFICANT CLIENTS**

The Company has one client (in the communications industry) that contributed in excess of 10% of the Company's revenue for the three months and nine months ended September 30, 2006 and two clients (both in the communications industry) that contributed in excess of 10% of the Company's revenue for the three months and nine months ended September 30, 2005. The revenue from these clients, as a percentage of total consolidated revenue, is as follows:

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Client A	15.9%	17.1%	17.1%	17.8%
Client B	6.1%	9.9%	7.8%	10.6%

As of September 30, 2006 and December 31, 2005, accounts receivable from clients A and B were as follows (amounts in thousands):

	<b>September 30, 2006</b>	<b>December 31, 2005</b>
Client A	\$ 31,200	\$ 34,600
Client B	\$ 12,200	\$ 18,500

The loss of one or more of its significant clients could have a material adverse effect on the Company's business, operating results, or financial condition. The Company does not require collateral from its clients. To limit the

Company's credit risk, management performs ongoing credit evaluations of its clients and maintains allowances for uncollectible accounts. Although the Company is impacted by economic conditions in certain industries including communications and media, automotive, financial services, healthcare, and government services, management does not believe significant credit risk exists as of September 30, 2006.

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

**(6) DERIVATIVES**

The Company conducts a significant portion of its business in currencies other than the U.S. dollar, the currency in which the condensed consolidated financial statements are reported. Correspondingly, the Company's operating results could be adversely affected by foreign currency exchange rate volatility relative to the U.S. dollar. The Company's subsidiaries in Argentina, Canada, and the Philippines use the local currency as their functional currency in addition to paying labor and other operating costs. Conversely, revenue for these foreign subsidiaries is derived principally from client contracts that are invoiced and collected in U.S. dollars. To hedge against the risk of a weaker U.S. dollar, the Company's U.S. entity has contracted on behalf of its foreign subsidiaries with several financial institutions to acquire (utilizing forward, non-deliverable forward, and option contracts) the functional currency of the foreign subsidiary at a fixed U.S. dollar exchange rate at specific dates in the future. The Company pays up-front premiums to obtain option hedge instruments.

While the Company has implemented certain strategies to mitigate risks related to the impact of fluctuations in currency exchange rates, it cannot ensure that it will not recognize gains or losses from international transactions, as this is part of transacting business in an international environment. Not every exposure is or can be hedged, and, where hedges are put in place based on expected foreign exchange exposure, they are based on forecasts which may vary or which may later prove to be inaccurate. Failure to successfully hedge or anticipate currency risks properly could adversely affect the Company's operating results.

As of September 30, 2006, the notional amount of these derivative instruments is summarized as follows (amounts in thousands):

	<b>Local Currency Amount</b>	<b>U.S. Dollar Amount</b>	<b>Dates Contracts are Through</b>
Canadian Dollar	178,068	\$ 159,471	June 2010
Argentine Peso	36,900	11,710	December 2007
Philippine Peso	2,120,000	40,837	December 2007
		\$212,018	

These derivatives, including option premiums, are classified as Prepaid and Other Assets of \$4.0 million and \$6.7 million; Other Assets of \$0.1 million and \$0.6 million; and Other Long-term Liabilities of \$1.4 million and \$0.0 million as of September 30, 2006 and December 31, 2005, respectively.

The Company recorded deferred tax liabilities of \$0.6 million and \$1.9 million related to these derivatives as of September 30, 2006 and December 31, 2005, respectively. A total of \$1.0 million and \$3.0 million of deferred gains, net of tax, on derivative instruments as of September 30, 2006 and December 31, 2005, respectively, were recorded in Accumulated Other Comprehensive Income.

During the three months ended September 30, 2006 and 2005, the Company recorded gains of \$1.4 million and \$1.1 million, respectively, for settled hedge contracts and the related premiums. During the nine months ended September 30, 2006 and 2005, the Company recorded gains of \$5.8 million and \$4.7 million, respectively, for settled hedge contracts and the related premiums. These are reflected in Revenue in the accompanying Condensed Consolidated Statements of Operations and Comprehensive Income.

The Company also entered into a foreign exchange forward contract to reduce the short-term effect of foreign currency fluctuations related to a \$19.2 million intercompany note payable from its Canadian subsidiary to a U.S. subsidiary. The gains and losses on this foreign exchange contract offset the transaction gains and losses on this foreign currency obligation. These gains and losses are recognized in earnings as the Company elected not to classify the hedge for hedge accounting treatment.



**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

**(7) INDEBTEDNESS**

During the third quarter 2006, the Company refinanced its credit facility ( Credit Facility ) with a syndication of banks. This Credit Facility permits the Company to borrow up to \$150 million, with an option to increase the borrowing limit to a maximum of \$225 million (subject to approval by the lenders) at any time up to 90 days prior to maturity of the Credit Facility. The Credit Facility matures on September 27, 2011. The Company may request a one year extension of the maturity date, subject to approval by the lenders. The Credit Facility is secured by the majority of the Company s domestic accounts receivable and a pledge of 65% of the capital stock of specified material foreign subsidiaries.

Subsequent to the end of the third quarter 2006, the Company exercised its option to increase the borrowing limit of the Credit Facility to \$180 million.

The Credit Facility, which includes customary financial covenants, may be used for general corporate purposes, including working capital, purchases of treasury stock, and acquisition financing. The Credit Facility accrues interest at a rate based on either (1) the Prime Rate, defined as the higher of the lender s prime rate or the Federal Funds Rate plus 0.50%, or (2) the London Interbank Offered Rate ( LIBOR ) plus an applicable credit spread, at the Company s option. The interest rate will vary based on the Company s leverage ratio as defined in the Credit Facility. As of September 30, 2006, interest accrued at the weighted-average rate of approximately 6%. As of September 30, 2006 and December 31, 2005, the Company had outstanding borrowings under the Credit Facility of \$77.8 million and \$26.7 million, respectively.

**(8) INCOME TAXES**

The Company accounts for income taxes in accordance with SFAS No. 109 Accounting for Income Taxes ( SFAS 109 ), which requires recognition of deferred tax assets and liabilities for the expected future income tax consequences of transactions that have been included in the Condensed Consolidated Financial Statements. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. When circumstances warrant, the Company assesses the likelihood that its net deferred tax assets will more likely than not be recovered from future projected taxable income. Management judgment has been used in forecasting future taxable income.

As required by SFAS 109, the Company continually reviews the likelihood that deferred tax assets will be realized in future tax periods under the more likely than not criteria. In making this judgment, SFAS 109 requires that all available evidence, both positive and negative, should be considered to determine whether, based on the weight of that evidence, a valuation allowance is required. As of September 30, 2006, the Company has \$50.5 million of deferred tax assets (after a \$3.7 million valuation allowance) and net deferred tax assets (after deferred tax liabilities) of \$42.7 million, related to the U.S. and international tax jurisdictions whose recoverability is dependent upon future profitability.

The effective tax rate, after minority interest, for the three months ended September 30, 2006 was 33.5%. The effective tax rate, after minority interest, for the nine months ended September 30, 2006 was 20.6%. Excluding the \$5.2 million change to the deferred tax valuation allowance accounted for in the second quarter of 2006, the Company s effective tax rate for the nine months ended September 30, 2006 was 34.2%.

**(9) RESTRUCTURING CHARGES AND IMPAIRMENT LOSSES**

**Restructuring Charges**

Restructuring Charges, Net for the three months ended September 30, 2006 of \$0.5 million relates to severance in the International BPO and Database Marketing and Consulting segments.

Restructuring Charges, Net for the nine months ended September 30, 2006 of \$1.5 million includes approximately (i) \$0.7 million for the fair value of the liability for lease payments for a portion of a CMC that the Company ceased to use in the International BPO segment, and (ii) \$1.0 million in severance costs, less (iii) a \$0.2 million reversal of unused prior-period balances.



Restructuring Charges, Net for the three months ended September 30, 2005 of \$0.5 million related to the Company's decision to exercise an early lease termination.

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

Restructuring Charges, Net for the nine months ended September 30, 2005 of \$1.5 million related to reductions in force across all three segments and the Company's decision to exercise an early lease termination.

A roll-forward of the activity in the restructuring reserve liability is as follows (amounts in thousands):

	<b>Closure of CMCs</b>	<b>Reduction in Force</b>	<b>Total</b>
<b>Balance as of December 31, 2004</b>	\$ 599	\$ 233	\$ 832
Expense	682	2,139	2,821
Payments	(193)	(1,145)	(1,338)
Reversal of unused balances		(148)	(148)
<b>Balance as of December 31, 2005</b>	1,088	1,079	2,167
Expense	724	935	1,659
Payments	(733)	(1,246)	(1,979)
Reversal of unused balances	(55)	(149)	(204)
<b>Balance as of September 30, 2006</b>	\$ 1,024	\$ 619	\$ 1,643

The restructuring reserve liability is included in Other Accrued Expenses in the accompanying Condensed Consolidated Balance Sheets.

**Impairment Losses**

Impairment Losses for the nine months ended September 30, 2006 of \$0.5 million includes approximately (i) \$0.3 million to reduce the net book value of long-lived assets in New Zealand and Malaysia to their then estimated fair value and (ii) \$0.2 million for the difference between assumed values to be received for assets in closed CMCs versus actual value received.

Impairment Losses for the nine months ended September 30, 2005 of \$2.5 million were to reduce the net book value of long-lived assets in the Glasgow, Scotland facility to its then estimated fair value.

**(10) CONTINGENCIES****Legal Proceedings**

From time-to-time, the Company may be involved in claims or lawsuits that arise in the ordinary course of business. Accruals for claims or lawsuits have been provided for to the extent that losses are deemed both probable and estimable. Although the ultimate outcome of these claims or lawsuits cannot presently be ascertained, on the basis of present information and advice received from counsel, it is management's opinion that the disposition or ultimate determination of such claims or lawsuits will not have a material adverse effect on the Company.

**Guarantees**

The Company's Credit Facility is guaranteed by the majority of the Company's domestic accounts receivable and a pledge of 65% of the capital stock of specified material foreign subsidiaries.

**Letters of Credit**

As of September 30, 2006, outstanding letters of credit and other performance guarantees totaled approximately \$13.8 million, which primarily guarantee workers' compensation, other insurance related obligations, and facility leases.

**Table of Contents**

**TELETECH HOLDINGS, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2006**

**(11) EARNINGS PER SHARE**

The following table sets forth the computation of basic and diluted earnings per share for the periods indicated (amounts in thousands):

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Shares used in basic per share calculation</b>	69,085	71,650	68,979	72,946
Effects of dilutive securities:				
Stock options	1,281	841	1,249	1,558
Restricted stock		100		100
Total effects of dilutive securities	1,281	941	1,249	1,658
<b>Shares used in diluted per share calculation</b>	<b>70,366</b>	<b>72,591</b>	<b>70,228</b>	<b>74,604</b>

For the three months ended September 30, 2006 and 2005, 0.5 million and 3.9 million, respectively, of options to purchase shares of common stock were outstanding but not included in the computation of diluted earnings per share because the effect would have been anti-dilutive. For the nine months ended September 30, 2006 and 2005, 1.3 million and 2.6 million, respectively, of options to purchase shares of common stock were outstanding but not included in the computation of diluted earnings per share because the effect would have been anti-dilutive. The Company has also excluded the impact of outstanding warrants, as the impact would be anti-dilutive for all periods presented.

**(12) OTHER FINANCIAL INFORMATION**

As of September 30, 2006, Accumulated Other Comprehensive Income included in the Company's Condensed Consolidated Balance Sheets consisted of \$5.1 million and \$1.0 million of foreign currency translation adjustments and derivatives valuation, net of tax, respectively. As of December 31, 2005, Accumulated Other Comprehensive Income consisted of \$0.7 million and \$3.0 million of foreign currency translation adjustments and derivatives valuation, net of tax, respectively.

**Table of Contents****Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Introduction**

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains certain forward-looking statements that involve risks and uncertainties. The projections and statements contained in these forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance, or achievements to be materially different from any future results, performance, or achievements expressed or implied by the forward-looking statements.

All statements not based on historical fact are forward-looking statements that involve substantial risks and uncertainties. In accordance with the Private Securities Litigation Reform Act of 1995, following are important factors that could cause our actual results to differ materially from those expressed or implied by such forward-looking statements, including but not limited to the following: our belief that we are continuing to see strong demand for our services and that sales cycles are shortening; risks associated with successfully integrating Direct Alliance Corporation ( DAC ) and achieving anticipated future revenue growth, profitability, and synergies; estimated revenue from new, renewed, and expanded client business as volumes may not materialize as forecasted or be sufficient to achieve our Business Outlook; achieving continued profit improvement in our International Business Process Outsourcing ( BPO ) operations; the ability to close and ramp new business opportunities that are currently being pursued or that are in the final stages with existing and/or potential clients in order to achieve our Business Outlook; our ability to execute our growth plans, including sales of new products (such as TeleTech On Demand™); our ability to achieve our year-end 2006 and 2007 financial goals, including those set forth in our Business Outlook; the possibility of our Database Marketing and Consulting segment not increasing revenue, lowering costs, or returning to profitability resulting in an impairment of its \$13.4 million of Goodwill; the possibility of lower revenue or price pressure from our clients experiencing a business downturn or merger in their business; greater than anticipated competition in the BPO and customer management market, causing adverse pricing and more stringent contractual terms; risks associated with losing or not renewing client relationships, particularly large client agreements, or early termination of a client agreement; the risk of losing clients due to consolidation in the industries we serve; consumers concerns or adverse publicity regarding our clients' products; our ability to find cost effective locations, obtain favorable lease terms, and build or retrofit facilities in a timely and economic manner; risks associated with business interruption due to weather, pandemic, or terrorist-related events; risks associated with attracting and retaining cost-effective labor at our customer management centers; the possibility of additional asset impairments and restructuring charges; risks associated with changes in foreign currency exchange rates; economic or political changes affecting the countries in which we operate; changes in accounting policies and practices promulgated by standard setting bodies; and new legislation or government regulation that impacts the BPO and customer management industry.

**Executive Overview**

We serve our clients through two primary businesses, BPO Services and Database Marketing and Consulting. BPO Services provides outsourced business process, customer management, and marketing services for a variety of industries via CMCs throughout the world. When we begin operations in a new country, we determine whether the country is intended to primarily serve U.S.-based clients, in which case we include the country in our North American BPO segment, or the country is intended to serve both domestic clients from that country and U.S.-based clients, in which case we include the country in our International BPO segment. This is consistent with our management of the business, internal financial reporting structure, and operating focus. Operations for each segment of BPO Services are conducted in the following countries:

**Table of Contents****North American BPO**

United States  
 Canada  
 India  
 Philippines

**International BPO**

Argentina  
 Australia  
 Brazil  
 China  
 Germany  
 Malaysia  
 Mexico  
 New Zealand  
 Singapore  
 Spain  
 United Kingdom  
 Venezuela

On June 30, 2006, we acquired 100 percent of the outstanding common shares of DAC. DAC is a provider of outsourced direct marketing services to third parties in the U.S. and its acquisition is consistent with our strategy to grow and to focus on providing outsourced marketing, sales, and BPO solutions to large multinational clients. DAC is included in our North American BPO segment. We project the acquisition of DAC will contribute approximately \$35 million of revenue during the last six months of 2006 since acquisition and will be slightly accretive to earnings during the first twelve months of combined operations.

Database Marketing and Consulting provides outsourced database management, direct marketing, and related customer acquisition and retention services for automobile dealerships and manufacturers.

Segment accounting policies are the same as those used in the Company's Condensed Consolidated Financial Statements. See Note 3 to the Condensed Consolidated Financial Statements for additional discussion regarding our preparation of segment information.

***BPO Services***

The BPO Services business generates revenue based primarily on the amount of time our representatives devote to a client's program. We primarily focus on large global corporations in the following industries; automotive, communications and media, financial services, healthcare, government, logistics, retail, technology, and travel. Revenue is recognized as services are provided. The majority of our revenue is, and we anticipate that the majority of our future revenue will continue to be, from multi-year contracts. However, we do provide certain client programs on a short-term basis. We have historically experienced annual attrition of existing client programs of approximately 7% to 15% of our revenue. Attrition of existing client programs during the first nine months of 2006 was 8% (approximately the same rate during the first nine months of 2005), excluding the short-term contract with the U.S. Government during the third quarter 2005. However, during all of 2005, we experienced net attrition of existing client programs of 3% (attrition of existing client programs was greater than the expansion of existing client programs) whereas during the first nine months of 2006, excluding the short-term contract with the U.S. Government during the third quarter 2005, we experienced net growth of existing client programs of 4% as expansion of existing client programs exceeded attrition of existing client programs. We believe this trend is attributable to our investment in an account management and operations team focused on client service. Our invoice terms with clients range from 30 to 60 days, with longer terms in Europe.

The BPO Services industry is highly competitive. Our ability to sell our existing services or gain acceptance for new products or services is challenged by the competitive nature of the industry. There can be no assurance that we will be able to sell services to new clients, renew relationships with existing clients, or gain client acceptance of our new products.

**Table of Contents**

We compete primarily with the in-house BPO operations of our current and potential clients. We also compete with certain companies that provide BPO services on an outsourced basis. In general, during the last several years, the global economy has negatively impacted the BPO market. More specifically, sales cycles lengthened, competition increased, and contract values were reduced. However, we believe that sales cycles have recently begun shortening. Nonetheless, pricing pressures continue within our industry due to the rapid growth of offshore labor capabilities. When renewing contracts, clients may request that all or a portion of the renewed work be located within offshore CMCs. These requests decrease our revenue as the billing rate we charge for offshore CMCs is lower than for our North American CMCs, and, in the short-term, increase our costs as we incur expenses related to relocating the work. For the three months and nine months ended September 30, 2006, we incurred contract relocation costs of approximately \$0.2 million and \$0.5 million, respectively. For the three months and nine months ended September 30, 2006, revenue was negatively impacted by \$0.0 million and \$2.6 million, respectively, as a result of relocating working from North American CMCs to International CMCs.

Quarterly, we review capacity utilization and projected demand for future capacity. In conjunction with these quarterly reviews, we may decide to consolidate or close under-performing CMCs, including those impacted by the loss of a major client program, in order to maintain or improve targeted utilization and margins.

Because clients may request that we serve their customers from International CMCs with lower prevailing labor rates, in the future we may decide to close one or more U.S.-based CMCs, even though it is generating positive cash flow, because we believe the future profits from conducting such work outside the U.S. may more than compensate for the one-time charges related to closing the facility.

The short-term focus of management is to increase revenue in both the North American and International BPO segments by:

Selling new business to existing clients;

Continuing to focus sales efforts on large, complex, multi-center opportunities;

Differentiating our products and services by developing and offering new solutions to clients; and

Exploring merger and acquisition possibilities.

It is possible that the contemplated benefits of any future acquisitions may not materialize within the expected time periods or to the extent anticipated. Critical to the success of our acquisition strategy in the future is the orderly, effective integration of acquired businesses into our organization. If this integration is unsuccessful, our business may be adversely impacted. There is also the risk that our valuation assumptions and models for an acquisition may be overly optimistic or incorrect.

Our ability to enter into new or renewed multi-year contracts, particularly large complex opportunities, is dependent upon the macroeconomic environment in general and the specific industry environments in which our clients operate. A weakening of the U.S. and/or the global economy could lengthen sales cycles or cause delays in closing new business opportunities.

As previously announced, we were recently awarded new business with new and existing clients. As a result, we are expanding our capacity in select International markets with the addition of an estimated 2,500 workstations in Argentina, Canada, Mexico, and the Philippines. We may have difficulties managing the timeliness of launching new or expanded client programs, and the associated internal allocation of personnel and resources. This could cause a decline or delay in recognition of revenues and an increase in costs, either of which could adversely affect our operating results. In the event we do not successfully expand our capacity or launch the new or expanded client programs, we may be unable to achieve the revenue and profitability targets set forth in the Business Outlook section below.

**Table of Contents**

Our profitability is significantly influenced by our ability to increase capacity utilization in our CMCs, the number of new or expanded programs during a period, and our success at managing personnel turnover and employee costs. Managing our costs is critical since we continue to see pricing pressure within our industry. These pricing pressures have been accentuated by the rapid growth in the availability of offshore labor.

We attempt to minimize the financial impact resulting from idle capacity when planning the development and opening of new CMCs or the expansion of existing CMCs. As such, management considers numerous factors that affect capacity utilization, including anticipated expirations, reductions, terminations, or expansions of existing programs, and the potential size and timing of new client contracts that we expect to obtain.

However, to respond more rapidly to changing market demands, to implement new programs, and to expand existing programs, we may be required to commit to additional capacity prior to the contracting of additional business, which may result in idle capacity. This is largely due to the significant time required to negotiate and execute a client contract as we concentrate our marketing efforts toward obtaining large, complex BPO programs.

We internally target capacity utilization in our Centers at 85% to 90% of our available workstations. As of September 30, 2006, the overall capacity utilization in our multi-client Centers was 75% (see Workstation Utilization below for further details).

As mentioned above, our profitability is influenced by the number of new or expanded client programs. We defer revenue for the initial training that occurs upon commencement of a new client contract ( Start-Up Training ) if that training is billed separately to the client. Accordingly, the corresponding training costs, consisting primarily of labor and related expenses, are also deferred. In these circumstances, both the training revenue and costs are amortized straight-line over the life of the client contract. In situations where Start-Up Training is not billed separately, but rather included in the hourly production rates paid by the client over the life of the contract, no deferral is necessary as the revenue is being recognized over the life of the contract, and the associated training expenses are expensed as incurred. For the three months and nine months ended September 30, 2006, we incurred \$0.8 million and \$2.3 million, respectively, of training expenses for client programs for which we did not separately bill Start-Up Training.

The following summarizes the impact of the deferred Start-Up Training on the three months and nine months ended September 30, 2006 (amounts in thousands):

	<b>Three Months Ended September 30, 2006</b>		<b>Nine Months Ended September 30, 2006</b>	
	<b>Income from</b>		<b>Income from</b>	
	<b>Revenue</b>	<b>Operations</b>	<b>Revenue</b>	<b>Operations</b>
Amounts deferred due to new business	\$ (3,538)	\$ (2,214)	\$ (9,072)	\$ (5,336)
Amortization of prior period deferrals	1,542	610	3,581	1,784
Net increase (decrease) for the period	\$ (1,996)	\$ (1,604)	\$ (5,491)	\$ (3,552)

As of September 30, 2006, we had \$8.2 million of net deferred Start-Up Training that will be amortized straight-line over the life of the corresponding client contracts (approximately 36 months).

Our potential clients typically obtain bids from multiple vendors and evaluate many factors in selecting a service provider including, among other factors, the scope of services offered, the service record of the vendor, and price. We generally price our bids with a long-term view of profitability and, accordingly, we consider all of our fixed and variable costs in developing our bids. We believe that our competitors, at times, may bid business based upon a short-term view, as opposed to our longer-term view, resulting in a lower price bid. While we believe our clients perceptions of the value we provide results in our being successful in certain competitive bid situations, there are often situations where a potential client may prefer a lower cost.

**Table of Contents**

Our industry is labor-intensive and the majority of our operating costs relate to wages, employee benefits, and employment taxes. An improvement in the local or global economies where our CMCs are located could lead to increased labor-related costs. In addition, our industry experiences high personnel turnover, and the length of training time required to implement new programs continues to increase due to increased complexities of our clients businesses. This may create challenges if we obtain several significant new clients or implement several new, large-scale programs, and need to recruit, hire, and train qualified personnel at an accelerated rate.

Our success in improving our profitability will depend on successful execution of a comprehensive business plan, including the following broad steps:

Increasing sales to absorb unused capacity in existing global CMCs;

Reducing costs and continued focus on cost controls; and

Managing the workforce in our CMCs in a cost-effective manner.

*Database Marketing and Consulting*

As of September 30, 2006, our Database Marketing and Consulting segment has relationships with more than 2,500 automobile dealers representing 27 different automotive brand names. These contracts generally have terms ranging from month-to-month to twenty-four months. For a few major automotive manufacturers, the automotive manufacturer collects from the individual automobile dealers on our behalf. Our average collection period is thirty to sixty days.

A majority of the revenue from this segment is generated utilizing a database and contact system to promote the service business of automobile dealership customers using targeted marketing solutions through the phone, mail, e-mail, and Web. A combination of factors contributed to this segment generating a loss from operations of approximately \$5.0 million and \$11.2 million, after corporate allocations, for the three months and nine months ended September 30, 2006. In our Quarterly Report on Form 10-Q for the three months ended June 30, 2006, we projected this segment would generate a loss from operations in the range of \$4.0 million to \$5.0 million. Excluding corporate allocations, this segment generated a loss from operations of \$4.5 million and \$9.3 million, respectively, for the three months and nine months ended September 30, 2006.

For 2006, we modified our agreement with Ford Motor Company ( Ford ; whose dealers represented approximately 32% of the revenue of our Database Marketing and Consulting segment for the third quarter of 2006), to provide services to Ford s automotive dealerships on a preferred basis, rather than on an exclusive basis as was the previous agreement, as Ford was to commence offering a competing product. The new agreement gives us flexibility to customize service offerings and the ability to contract directly with Ford s dealerships under our defined terms and conditions. Primarily due to Ford offering a competing product, our dealer attrition rate has exceeded our new account growth in 2006, resulting in a significant decrease in revenue from the prior year period. At the same time, we continue to focus on developing a field sales organization to approach dealers outside of the Ford family of automotive brands.

Due to the factors discussed above, we believe this segment will incur a loss from operations in the fourth quarter of 2006 in the range of \$3.5 million to \$4.5 million, as we work to implement the plans outlined below to return this segment to profitability.

We plan to continue our focus on the following during the fourth quarter 2006:

Diversifying our client base by establishing relations with new automotive manufacturers and dealer groups;

Reducing our client attrition rate by improving customer service and increasing customer contact;

Continuing to manage costs through operational effectiveness; and

Acquiring business platforms for similar and related services.



**Table of Contents**

The clients of our Database Marketing and Consulting segment, as well as our joint venture with Ford, come primarily from the automotive industry. The U.S. automotive industry is currently reporting declining earnings, which may result in client losses, lower volumes, or place additional pricing pressures on our operations.

*Overall*

As shown in the Financial Comparison below (see Net increase to income from BPO operations ), we believe that we have been successful in improving income from operations for our North American and International BPO segments. The increases are attributable to a variety of factors such as expansion of work on certain client programs, our multi-phased cost reduction plan, transitioning work on certain client programs to lower cost operating centers, and taking actions to improve individual client program profit margins and/or eliminate unprofitable client programs.

*Adoption of SFAS No. 123(R) and Equity-Based Compensation Expense*

During the first quarter of 2006, we adopted Statement of Financial Accounting Standards ( SFAS ) No. 123 (revised 2004) Share-Based Payment ( SFAS 123(R) ) applying the modified prospective method. SFAS 123(R) requires all equity-based payments to employees, including grants of employee stock options, to be recognized in the Condensed Consolidated Statement of Operations and Comprehensive Income based on the grant date fair value of the award. Prior to the adoption of SFAS 123(R), we accounted for equity-based awards under the intrinsic value method, which followed recognition and measurement principles of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations and equity-based compensation was included as pro-forma disclosure within the notes to the financial statements.

We did not modify the terms of any previously granted options in anticipation of the adoption of SFAS 123(R). Income from operations for the three months ended September 30, 2006 was adversely affected by the impact of equity-based compensation due to the implementation of SFAS 123(R). For the three months and nine months ended September 30, 2006 we recorded \$1.7 million and \$5.0 million, respectively, for equity-based compensation. We expect that equity-based compensation expense for fiscal 2006 will be approximately \$6.9 million based on current outstanding awards and assumptions applied. However, any significant awards granted during the remainder of fiscal 2006, required changes in the estimated forfeiture rates or significant changes in the market price of our common stock may impact this estimate. Based on current outstanding awards, compensation expense related to equity-based payments to employees is expected to be \$6.7 million and \$5.8 million during fiscal years 2007 and 2008, respectively. See Note 4 to the Condensed Consolidated Financial Statements for additional information.

**Critical Accounting Policies**

We have identified the policies below as critical to our business and results of operations. For further discussion on the application of these and other accounting policies, see Note 1 to our Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2005.

Our reported results are impacted by the application of the following accounting policies, certain of which require management to make subjective or complex judgments. These judgments involve making estimates about the effect of matters that are inherently uncertain and may significantly impact quarterly or annual results of operations. Specific risks associated with these critical accounting policies are described in the following paragraphs.

For all of these policies, management cautions that future events rarely develop exactly as expected, and the best estimates routinely require adjustment. Descriptions of these critical accounting policies follow.

**Table of Contents***Revenue Recognition*

For each client arrangement, we determine whether evidence of an arrangement exists, delivery of our service has occurred, the fee is fixed or determinable, and collection is probable. If all criteria are met, we recognize revenue at the time services are performed. If any of these criteria are not met, revenue recognition is deferred until such time as all of the criteria are met.

Our BPO segments recognize revenue under three models which are:

**Production Rate.** Revenue is recognized based on the billable time or transactions of each customer service representative ( CSR ), as defined in the client contract. The rate per billable time or transaction is based on a predetermined contractual rate. This contractual rate can fluctuate based on our performance against certain pre-determined criteria related to quality and performance.

**Performance-based.** Under performance-based arrangements, we are paid by our clients based on achievement of certain levels of sales or other client-determined criteria specified in the client contract. We recognize performance-based revenue by measuring our actual results against the performance criteria specified in the contracts. Amounts collected from clients prior to the performance of services are recorded as customer advances.

**Hybrid.** Under hybrid models we are paid a fixed fee or production element as well as a performance-based element.

Certain client programs provide for adjustments to monthly billings based upon whether we meet or exceed certain performance criteria as set forth in the contract. Increases or decreases to monthly billings arising from such contract terms are reflected in Revenue as earned or incurred.

Our Database Marketing and Consulting segment recognizes revenue when services are rendered. Most agreements require the billing of predetermined monthly rates. Where the contractual billing periods do not coincide with the periods over which services are provided, we recognize revenue straight-line over the life of the contract (typically six to twenty-four months).

From time-to-time, we make certain expenditures related to acquiring contracts (recorded as Contract Acquisition Costs in the accompanying Condensed Consolidated Balance Sheets). Those expenditures are capitalized and amortized in proportion to the initial expected future revenue from the contract, which in most cases results in straight-line amortization over the life of the contract. Amortization of these costs is recorded as a reduction of Revenue.

*Income Taxes*

We account for income taxes in accordance with SFAS No. 109 Accounting for Income Taxes ( SFAS 109 ), which requires recognition of deferred tax assets and liabilities for the expected future income tax consequences of transactions that have been included in the Condensed Consolidated Financial Statements. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. When circumstances warrant, we assess the likelihood that our net deferred tax assets will more likely than not be recovered from future projected taxable income.

As required by SFAS 109, the Company continually reviews the likelihood that deferred tax assets will be realized in future tax periods under the more likely than not criteria. In making this judgment SFAS 109 requires that all available evidence, both positive and negative, should be considered to determine whether, based on the weight of that evidence, a valuation allowance is required. As of September 30, 2006, the Company has \$50.5 million of deferred tax assets (after a \$3.7 million valuation allowance) and net deferred tax assets (after deferred tax liabilities) of \$42.7 million related to the U.S. and international tax jurisdictions whose recoverability is dependent upon future profitability.

**Table of Contents**

In the future, our effective tax rate could be adversely affected by several factors, many of which are outside of our control. Our effective tax rate is affected by the proportion of revenues and income before taxes in the various domestic and international jurisdictions in which we operate. Further, we are subject to changing tax laws, regulations, and interpretations in multiple jurisdictions in which we operate, as well as the requirements, pronouncements, and rulings of certain tax, regulatory, and accounting organizations. We estimate our annual effective tax rate each quarter based on a combination of actual and forecasted results of subsequent quarters. Consequently, significant changes in our actual quarterly or forecasted results may impact the effective tax rate for the current or future periods. The FASB recently issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes ( FIN 48 ), an interpretation of SFAS 109. FIN 48 will be effective for our 2007 fiscal year. See Note 1 to the Condensed Consolidated Financial Statements for a more complete description of the impact FIN 48 will have on our consolidated financial statements.

*Allowance for Doubtful Accounts*

We have established an allowance for doubtful accounts to reserve for uncollectible accounts receivable. Each quarter, management reviews the receivables on an account-by-account basis and assigns a probability of collection. Management's judgment is used in assessing the probability of collection. Factors considered in making this judgment include, among other things, the age of the identified receivable, client financial wherewithal, previous client history, and any recent communications with the client.

*Impairment of Long-Lived Assets*

We evaluate the carrying value of our individual CMCs in accordance with SFAS No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets ( SFAS 144 ). SFAS 144 requires that a long-lived asset group be reviewed for impairment only when events or changes in circumstances indicate that the carrying amount of the long-lived asset group may not be recoverable. When the operating results of a Center have deteriorated to the point it is likely that losses will continue for the foreseeable future, or we expect that a CMC will be closed or otherwise disposed of before the end of its estimated useful life, we select the CMC for further review.

For CMCs selected for further review, we estimate the probability-weighted future cash flows, using EBITDA (see Presentation of Non-GAAP (Generally Accepted Accounting Practices ( GAAP )) Measurements ) as a surrogate for cash flows, resulting from operating the CMC over its useful life. Significant judgment is involved in projecting future capacity utilization, pricing, labor costs, and the estimated useful life of the CMC. We do not subject to the same test CMCs that have been operated for less than two years or those CMCs that have been impaired within the past two years (the Two Year Rule ) because we believe sufficient time is necessary to establish a market presence and build a client base for such new or modified CMCs in order to adequately assess recoverability. However, such CMCs are nonetheless evaluated in case other factors would indicate an impairment had occurred. For impaired CMCs, we write the assets down to their estimated fair market value. If the assumptions used in performing the impairment test prove insufficient, the fair value estimate of the CMCs may be significantly lower, thereby causing the carrying value to exceed fair value and indicating an impairment had occurred.

**Table of Contents**

The following table presents a sensitivity analysis of the impairment evaluation assuming that the future results were 10% less than the two-year forecasted EBITDA for these CMC's (excluding Glasgow, which was impaired in 2005). As shown in the table below, the analysis indicates that an impairment of approximately \$3.0 million (a decrease of \$1.8 million from the second quarter of 2006) would arise. However, for the CMC's tested, the current probability-weighted projection scenarios indicated that impairment had not occurred as of September 30, 2006 (amounts in thousands, except number of CMCs):

	<b>Net Book Value</b>	<b>Number of CMCs</b>	<b>Additional Impairment Under Sensitivity Test</b>
<b>Tested based on Two Year Rule</b>			
Positive cash flow in period	\$ 58,978	53	\$ 419
Negative cash flow in period	2,036	4	739
Sub-total	61,014	57	1,158
<b>Not tested based on Two Year Rule</b>			
Positive cash flow in period	20,637	9	
Negative cash flow in period	6,865	5	1,806
Sub-total	27,502	14	1,806
<b>Total</b>			
Positive cash flow in period	79,615	62	419
Negative cash flow in period	8,901	9	2,545
Grand total	\$ 88,516	71	\$ 2,964

We also assess the realizable value of capitalized software on a quarterly basis based upon current estimates of future cash flows from services utilizing the software (principally utilized by our Database Marketing and Consulting segment). No impairment had occurred as of September 30, 2006.

*Goodwill*

Goodwill is tested for impairment at least annually at the segment level for the Database Marketing and Consulting segment (which consists of one subsidiary company) and for reporting units one level below the segment level for the other two segments in accordance with SFAS No. 142 Goodwill and Other Intangible Assets. Impairment occurs when the carrying amount of goodwill exceeds its estimated fair value. The impairment, if any, is measured based on the estimated fair value of the reporting unit. Fair value can be determined based on discounted cash flows, comparable sales, or valuations of other similar businesses. Our policy is to test goodwill for impairment in the fourth quarter of each year unless an indicator of impairment arises during an intervening period.

We have plans to improve the future profitability of our Database Marketing and Consulting segment. The goodwill for that segment is \$13.4 million as of September 30, 2006. As a result of this segment's financial performance in the third quarter of 2006, we updated our cash flow analyses (which assume annual revenue increases ranging from 10 percent to 13 percent per annum, calculated on a smaller revenue base than our historical revenue base and following our planned efforts to sell business to non-Ford dealers). Our analyses indicated that an impairment in goodwill had not occurred as of September 30, 2006. However, a sensitivity analysis of the forecast indicated that, without considering corresponding reductions in future operating expenses that we would implement in the event of a further revenue decline, it would not take a material change in the revenue forecast for an impairment to arise.

*Restructuring Reserve Liability*

We routinely assess the profitability and utilization of our CMCs. In some cases, we have chosen to close under-performing CMCs and complete reductions in workforce to enhance future profitability. We follow SFAS No. 146 Accounting for Costs Associated with Exit or Disposal Activities, which specifies that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred, rather than upon commitment to a plan.

A significant assumption used in determining the amount of the estimated liability for closing CMCs is the estimated liability for future lease payments on vacant centers, which we determine based on a third-party broker's assessment of our ability to successfully negotiate early termination agreements with landlords and/or our ability to sublease the facility. If our assumptions regarding early termination and the timing and amounts of sublease payments prove to be inaccurate, we may be required to record additional losses, or conversely, a future gain.

**Table of Contents**

*Contingencies*

We record a liability for pending litigation and claims where losses are both probable and reasonably estimable. Each quarter, management, with the advice of legal counsel, reviews these matters on a case-by-case basis and assigns probability of loss and range of loss based upon the assessments of in-house counsel and outside counsel, as appropriate.

**Explanation of Key Metrics and Other Items**

*Cost of Services*

Cost of Services principally include costs incurred in connection with our BPO operations and database marketing services, including direct labor, telecommunications, printing, postage, sales and use tax, and certain fixed costs associated with CMCs.

*Selling, General and Administrative*

Selling, General and Administrative expenses primarily include costs associated with administrative services such as sales, marketing, product development, regional legal settlements, legal, information systems (including core technology and telephony infrastructure), accounting, and finance. It also includes equity-based compensation expense, outside professional fees (i.e. legal and accounting services), building maintenance expense for non-CMC facilities, and other items associated with administration.

*Restructuring Charges, Net*

Restructuring Charges, Net primarily include costs incurred in conjunction with reductions in force or decisions to exit facilities, including termination benefits and lease liabilities, net of expected sublease rentals.

*Interest Expense*

Interest Expense includes interest expense and amortization of debt issuance costs associated with our grants, debt, and capitalized lease obligations.

*Other Expenses*

The main components of Other Expenses are expenditures not directly related to our operating activities, such as corporate legal settlements and foreign exchange transaction losses.

*Other Income*

The main components of Other Income are miscellaneous receipts not directly related to our operating activities, such as foreign exchange transaction gains and corporate legal settlements. In addition, Other Income includes income related to grants we may receive from time-to-time from local or state governments as an incentive to locate CMCs in their jurisdictions.

*Free Cash Flow*

We define Free Cash Flow as Net Cash Flows from Operating Activities less purchases of Property and Equipment, as shown in our Condensed Consolidated Statements of Cash Flows.

*Quarterly Average Daily Revenue*

We define Quarterly Average Daily Revenue as Revenue for the quarter divided by the calendar days during the quarter.

*Days Sales Outstanding*

We define days sales outstanding ( DSO ) as Accounts Receivable divided by Quarterly Average Daily Revenue.

**Table of Contents****Presentation of Non-GAAP Measurements***Free Cash Flow*

Free Cash Flow is a non-GAAP liquidity measurement. We believe that Free Cash Flow is useful to our investors because it measures, during a given period, the amount of cash generated that is available for debt obligations and investments other than purchases of Property and Equipment. Free Cash Flow is not a measure determined in accordance with GAAP and should not be considered a substitute for Income from operations, Net Income, Net cash provided by operating activities, or any other measure determined in accordance with GAAP. We believe this non-GAAP liquidity measure is useful, in addition to the most directly comparable GAAP measure of Net cash provided by operating activities, because Free Cash Flow includes investments in operational assets. Free Cash Flow does not represent residual cash available for discretionary expenditures, since it includes cash required for debt service. Free Cash Flow also excludes cash that may be necessary for acquisitions, investments, and other needs that may arise.

The following table reconciles Free Cash Flow to Net cash provided by operating activities for our consolidated results (amounts in thousands):

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Free cash flow	\$ 25,960	\$ 6,774	\$ 21,393	\$ 25,969
Add back:				
Purchases of Property and Equipment	22,753	10,645	51,219	26,763
Net cash provided by operating activities	\$ 48,713	\$ 17,419	\$ 72,612	\$ 52,732

We discuss factors affecting Free Cash Flow between periods in the Liquidity and Capital Resources section below. The following table reconciles Free Cash Flow to Net cash provided by operating activities for our Database Marketing and Consulting segment (amounts in thousands):

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Free cash flow	\$ (3,266)	\$ (332)	\$ (4,586)	\$ (571)
Add back:				
Purchases of Property and Equipment	474	630	1,074	2,544
Net cash provided by operating activities	\$ (2,792)	\$ 298	\$ (3,512)	\$ 1,973

*Earnings Before Interest, Taxes, Depreciation, and Amortization*

Earnings before interest, taxes, depreciation, and amortization ( EBITDA ) is a non-GAAP liquidity and profitability measurement. We use EBITDA to evaluate the profitability and cash flow of our CMCs when testing the impairment of long-lived assets. EBITDA is not a measure determined in accordance with GAAP and should not be considered a substitute for Income from operations, Net cash provided by operating activities, or any other measure determined in accordance with GAAP. As shown in the table below, EBITDA is calculated as earnings before interest, income taxes, depreciation, and amortization. Because not all companies calculate EBITDA identically, this presentation of EBITDA may not be comparable to similarly titled measures of other companies. EBITDA is not intended to be a measure of free cash flow for management's discretionary use, as it does not consider certain cash requirements such as interest expense, income taxes, or debt service payments.

**Table of Contents**

The following table reconciles Net Income to EBITDA for our consolidated results (amounts in thousands):

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Net Income	\$ 12,779	\$ 11,620	\$ 30,411	\$ 18,073
Add back:				
Provision for income taxes	6,428	432	7,889	3,204
Interest expense (income), net	1,748	(155)	3,141	(517)
Depreciation and amortization	12,929	12,659	36,705	40,650
EBITDA	\$ 33,884	\$ 24,556	\$ 78,146	\$ 61,410



**Table of Contents****Results of Operations***Operating Review*

The following tables are presented to facilitate Management's Discussion and Analysis of Financial Condition and Results of Operations (amounts in thousands):

	Three Months Ended September 30,		Three Months Ended September 30,		\$	% Change
	2006	% of Revenue	2005	% of Revenue		
<b>Revenue</b>						
North American BPO	\$ 206,616	68.0%	\$ 170,930	62.3%	\$ 35,686	20.9%
International BPO	90,336	29.7%	82,596	30.1%	7,740	9.4%
Database Marketing and Consulting	6,852	2.3%	20,733	7.6%	(13,881)	(67.0)%
	\$ 303,804	100.0%	\$ 274,259	100.0%	\$ 29,545	10.8%
<b>Cost of Services</b>						
North American BPO	\$ 146,537	70.9%	\$ 127,416	74.5%	\$ 19,121	15.0%
International BPO	69,671	77.1%	63,695	77.1%	5,976	9.4%
Database Marketing and Consulting	4,494	65.6%	11,381	54.9%	(6,887)	(60.5)%
	\$ 220,702	72.6%	\$ 202,492	73.8%	\$ 18,210	9.0%
<b>Selling, General and Administrative</b>						
North American BPO	\$ 27,716	13.4%	\$ 21,002	12.3%	\$ 6,714	32.0%
International BPO	16,070	17.8%	16,579	20.1%	(509)	(3.1)%
Database Marketing and Consulting	5,485	80.0%	9,061	43.7%	(3,576)	(39.5)%
	\$ 49,271	16.2%	\$ 46,642	17.0%	\$ 2,629	5.6%
<b>Depreciation and Amortization</b>						
North American BPO	\$ 7,169	3.5%	\$ 6,310	3.7%	\$ 859	13.6%
International BPO	4,005	4.4%	4,193	5.1%	(188)	(4.5)%
Database Marketing and Consulting	1,755	25.6%	2,156	10.4%	(401)	(18.6)%
	\$ 12,929	4.3%	\$ 12,659	4.6%	\$ 270	2.1%
<b>Restructuring Charges, Net</b>						
North American BPO	\$	0.0%	\$ 548	0.3%	\$ (548)	(100.0)%
International BPO	408	0.5%		0.0%	408	N/A
Database Marketing and Consulting	107	1.6%	(11)	(0.1)%	118	(1072.7)%

Edgar Filing: TELETECH HOLDINGS INC - Form 10-Q

	\$ 515	0.2%	\$ 537	0.2%	\$ (22)	(4.1)%
<b>Impairment Losses</b>						
North American BPO	\$	0.0%	\$	0.0%	\$	0.0%
International BPO		0.0%		0.0%		0.0%
Database Marketing and Consulting		0.0%		0.0%		0.0%
	\$	0.0%	\$	0.0%	\$	0.0%
<b>Income (Loss) from Operations</b>						
North American BPO	\$ 25,194	12.2%	\$ 15,654	9.2%	\$ 9,540	60.9%
International BPO	182	0.2%	(1,871)	(2.3)%	2,053	(109.7)%
Database Marketing and Consulting	(4,989)	(72.8)%	(1,854)	(8.9)%	(3,135)	169.1%
	\$ 20,387	6.7%	\$ 11,929	4.3%	\$ 8,458	70.9%
<b>Other Income (Expense)</b>	\$ (597)	(0.2)%	\$ 524	0.2%	\$ (1,121)	(213.9)%
<b>Provision for Income Taxes</b>	\$ 6,428	2.1%	\$ 432	0.2%	\$ 5,996	1388.0%

28

**Table of Contents**

	<b>Nine Months Ended September 30,</b>					
	<b>2006</b>	<b>% of Revenue</b>	<b>2005</b>	<b>% of Revenue</b>	<b>\$ Change</b>	<b>% Change</b>
<b>Revenue</b>						
North American BPO	\$ 576,283	65.9%	\$ 474,852	60.7%	\$ 101,431	21.4%
International BPO	264,277	30.2%	244,157	31.2%	20,120	8.2%
Database Marketing and Consulting	34,000	3.9%	63,509	8.1%	(29,509)	(46.5)%
	\$ 874,560	100.0%	\$ 782,518	100.0%	\$ 92,042	11.8%
<b>Cost of Services</b>						
North American BPO	\$ 423,097	73.4%	\$ 352,360	74.2%	\$ 70,737	20.1%
International BPO	207,418	78.5%	194,415	79.6%	13,003	6.7%
Database Marketing and Consulting	19,203	56.5%	33,888	53.4%	(14,685)	(43.3)%
	\$ 649,718	74.3%	\$ 580,663	74.2%	\$ 69,055	11.9%
<b>Selling, General and Administrative</b>						
North American BPO	\$ 77,788	13.5%	\$ 60,064	12.6%	\$ 17,724	29.5%
International BPO	47,352	17.9%	46,511	19.0%	841	1.8%
Database Marketing and Consulting	19,992	58.8%	30,153	47.5%	(10,161)	(33.7)%
	\$ 145,132	16.6%	\$ 136,728	17.5%	\$ 8,404	6.1%
<b>Depreciation and Amortization</b>						
North American BPO	\$ 19,277	3.3%	\$ 20,582	4.3%	\$ (1,305)	(6.3)%
International BPO	11,538	4.4%	12,797	5.2%	(1,259)	(9.8)%
Database Marketing and Consulting	5,890	17.3%	7,271	11.4%	(1,381)	(19.0)%
	\$ 36,705	4.2%	\$ 40,650	5.2%	\$ (3,945)	(9.7)%
<b>Restructuring Charges, Net</b>						
North American BPO	\$ 126	0.0%	\$ 1,094	0.2%	\$ (968)	(88.5)%
International BPO	1,222	0.5%	85	0.0%	1,137	1337.6%
Database Marketing and Consulting	107	0.3%	301	0.5%	(194)	(64.5)%
	\$ 1,455	0.2%	\$ 1,480	0.2%	\$ (25)	(1.7)%
<b>Impairment Losses</b>						
North American BPO	\$	0.0%	\$	0.0%	\$ 0	0.0%

Edgar Filing: TELETECH HOLDINGS INC - Form 10-Q

International BPO	478	0.2%	2,537	1.0%	(2,059)	(81.2)%
Database Marketing and Consulting		0.0%		0.0%		0.0%
	\$ 478	0.1%	\$ 2,537	0.3%	\$ (2,059)	(0.0)%
<b>Income (Loss) from Operations</b>						
North American BPO	\$ 55,995	9.7%	\$ 40,752	8.6%	\$ 15,243	37.4%
International BPO	(3,731)	(1.4)%	(12,188)	(5.0)%	8,457	(69.4)%
Database Marketing and Consulting	(11,192)	(32.9)%	(8,104)	(12.8)%	(3,088)	38.1%
	\$ 41,072	4.7%	\$ 20,460	2.6%	\$ 20,612	100.7%
<b>Other Income (Expense)</b>	\$ (1,113)	(0.1)%	\$ 1,530	0.2%	\$ (2,643)	(172.7)%
<b>Provision for Income Taxes</b>	\$ 7,889	0.9%	\$ 3,204	0.4%	\$ 4,685	146.2%

29

**Table of Contents****Financial Comparison**

The following table is a condensed presentation of the components of the change in Net Income between the three months and nine months ended September 30, 2006 and 2005 and is designed to facilitate the discussion of results of operations in this Form 10-Q (amounts in thousands):

	<b>Three Months Ended September 30,</b>	<b>Nine Months Ended September 30,</b>
Current period (2006) reported net income	\$ 12,779	\$ 30,411
Prior period (2005) reported net income	11,620	18,073
Difference	\$ 1,159	\$ 12,338
<b>Explanation</b>		
Net increase to income from BPO operations	\$ 11,593	\$ 23,700
Net increase to loss in Database Marketing and Consulting segment	(3,135)	(3,088)
Increase in interest expense	(1,683)	(2,560)
Decrease in interest income	(220)	(1,098)
Other	600	69
Increase in taxes	(5,996)	(4,685)
Total	\$ 1,159	\$ 12,338

**Workstation Utilization**

The table below presents workstation data for multi-client Centers as of September 30, 2006 and December 31, 2005. Workstations in Dedicated and Managed Centers of 11,219 and 11,081, respectively, for the same periods are excluded from the workstation data as unused seats in these facilities are not available for sale. Our utilization percentage is defined as the total number of utilized production workstations compared to the total number of available production workstations.

	<b>September 30, 2006</b>			<b>December 31, 2005</b>		
	<b>Total Production Workstations</b>	<b>In Use</b>	<b>% In Use</b>	<b>Total Production Workstations</b>	<b>In Use</b>	<b>% In Use</b>
North American BPO	9,806	7,360	75%	6,514	4,834	74%
International BPO	10,572	7,904	75%	9,447	6,695	71%
Total	20,378	15,264	75%	15,961	11,529	72%

As shown above, there was a significant increase in the total production workstations arising from our expansion plans (see discussion under BPO Services above), a corresponding increase in the number of production workstations in use, and an increase in the utilization percentage.

**Three Months Ended September 30, 2006 Compared to September 30, 2005***Revenue*

The increase in North American BPO between periods was due to new client programs, expansion of existing client programs, and the acquisition of DAC.

Revenue in the International BPO segment increased due to new client programs and expansion of existing client programs in Latin America and Europe.

Database Marketing and Consulting revenue decreased due to a net decrease in the customer base as discussed earlier.

**Table of Contents**

*Cost of Services*

Cost of Services as a percentage of revenue in North American BPO primarily decreased compared to the prior year due to the increase in revenue discussed above. In absolute dollars, the increase in Cost of Services corresponds to revenue growth from the implementation of new or expanded client programs and the acquisition of DAC.

Cost of Services, as a percentage of revenue, in International BPO remained constant as compared to the prior year. In absolute dollars, Cost of Services increased due to the implementation of new or expanded client programs.

Cost of Services for Database Marketing and Consulting decreased from the prior year primarily due to a decrease in revenue and our efforts to reduce costs.

*Selling, General and Administrative*

On a consolidated basis, Selling, General and Administrative increased by \$2.6 million, principally comprised of \$1.7 million of stock option expense required by the adoption of SFAS No. 123(R), additional incentive compensation related to increased earnings over the prior year period, and the acquisition of DAC.

Selling, General and Administrative expenses for North American BPO increased in both absolute dollars and as a percentage of revenue primarily due to increased salaries and related benefits resulting principally from the Company's expenditures to implement an eLearning strategy, compensation expense related to share-based payments (see Note 4 to the Condensed Consolidated Financial Statements), increased incentive compensation, and the acquisition of DAC. Selling, General and Administrative expenses for International BPO decreased in both absolute dollars and as a percentage of revenue due primarily to decreased salaries and benefits expense resulting from headcount reductions in our European and Asia Pacific operations.

The decrease in Selling, General and Administrative expenses for Database Consulting and Marketing was primarily due to our efforts to reduce costs and a lower allocation of corporate-level operating expenses as discussed above.

*Depreciation and Amortization*

In absolute dollars, Depreciation and Amortization in our North American BPO segment increased due to the addition of new CMCs and the expansion of existing CMCs. In absolute dollars and as a percentage of revenue, Depreciation and Amortization in our International BPO segment decreased between periods due primarily to the closure of certain facilities. Depreciation and Amortization in our Database Marketing and Consulting segment decreased compared to the prior year primarily due to assets reaching the end of their depreciable lives.

*Restructuring Charges, Net and Impairment Losses*

Restructuring Charges, Net for the three months ended September 30, 2006 of \$0.5 million relates to severance resulting from a reduction in force in the International BPO and Database Marketing and Consulting segments.

*Other Income (Expense)*

During the three months ended September 30, 2006, Interest Expense increased by \$1.7 million due to increased borrowings compared to the prior year due primarily to the acquisition of DAC and the Company's share repurchase program. Interest Income decreased by \$0.2 million due to lower cash investment balances during the quarter.

**Table of Contents***Income Taxes*

The effective tax rate, after minority interest, for the three months ended September 30, 2006 was 33.5%. The effective tax rate, after minority interest, for the three months ended September 30, 2005 was 3.6%. Excluding the \$9.9 million reversal of the U.S. deferred tax valuation allowance and \$3.9 million in taxes associated with our Dividend Repatriation Plan completed and accounted for in the third quarter of 2005, the effective tax rate would have been 53.3%. For succeeding quarters, our effective tax rate will be affected by many factors including (i) the amount and placement of new business into tax jurisdictions with valuation allowances and without valuation allowances, (ii) the recognition of tax benefits that may arise related to tax planning strategies not recorded in the financial statements as their benefit is currently uncertain, (iii) the impact of tax holidays in overseas tax jurisdictions, and (iv) adoption of the new accounting standard for tax uncertainties (see Note 1 to the Condensed Consolidated Financial Statements). We expect our effective tax rate for the year ending December 31, 2006 will be approximately 30% to 35%, excluding the \$5.2 million reversal of a portion of the deferred tax valuation allowance in the second quarter of 2006.

**Nine Months Ended September 30, 2006 Compared to September 30, 2005***Revenue*

The increase in North American BPO revenue between periods was due to new client programs, expansion of existing client programs, and the acquisition of DAC.

Revenue in the International BPO segment increased due to new client programs and expansion of existing client programs in Latin America and Europe.

Database Marketing and Consulting revenue decreased due to a net decrease in the customer base as discussed above.

*Cost of Services*

Cost of Services as a percentage of revenue in North American BPO remained relatively constant as compared to the prior year. In absolute dollars, Cost of Services increased due to the implementation of new client programs, the expansion of existing client programs, and the acquisition of DAC.

Cost of Services, as a percentage of revenue, in International BPO remained relatively constant as compared to the prior year. In absolute dollars, Cost of Services increased due to the implementation of new client programs and the expansion of existing client programs.

Cost of Services for Database Marketing and Consulting decreased from the prior year in absolute dollars primarily due to a decrease in revenue and our efforts to reduce costs.

*Selling, General and Administrative*

On a consolidated basis, the increase in Selling, General and Administrative expenses of \$8.4 million is related to stock option expense, increased incentive compensation related to the increase in earnings, and the acquisition of DAC.

Selling, General and Administrative expenses for North American BPO increased in absolute dollars due to increased salaries and related benefits resulting principally from the Company's expenditures in an eLearning strategy, compensation expense related to share-based payments (see Note 4 to the Condensed Consolidated Financial Statements), increased incentive compensation, and the acquisition of DAC.

Selling, General and Administrative expenses for International BPO increased in absolute dollars due primarily to increased technology-related expenses and the recording of compensation expense related to share-based payments (see Note 4 to the Condensed Consolidated Financial Statements).

The decrease in Selling, General and Administrative expenses for Database Consulting and Marketing was primarily due to our efforts to reduce costs and a lower allocation of corporate-level operating expenses as discussed above.



**Table of Contents***Depreciation and Amortization*

In absolute dollars, Depreciation and Amortization in our North American BPO and International BPO segments decreased between periods due primarily to the closure of certain facilities. Depreciation and Amortization in our Database Marketing and Consulting segment decreased compared to the prior year primarily due to assets reaching the end of their depreciable lives.

*Restructuring Charges, Net and Impairment Losses*

Restructuring Charges, Net for the nine months ended September 30, 2006 of \$1.5 million includes approximately (i) \$0.7 million for the fair value of the liability for lease payments for a portion of a CMC that the Company ceased to use in the International BPO segment, and (ii) \$1.0 million in severance costs, less (iii) a \$0.2 million reversal of unused prior-period balances.

Restructuring Charges, Net for the nine months ended September 30, 2005 of \$1.5 million related to termination benefits for administrative employees.

Impairment Losses for the nine months ended September 30, 2006 of \$0.5 million includes approximately (i) \$0.3 million to reduce the net book value of long-lived assets in New Zealand and Malaysia to their then estimated fair value and (ii) \$0.2 million for the difference between assumed values to be received for assets in closed CMCs versus actual value received.

Impairment Losses for the three months and nine months ended September 30, 2005 of \$2.5 million were to reduce the net book value of long-lived assets in our Glasgow, Scotland facility to their then estimated fair value.

*Other Income (Expense)*

During the nine months ended September 30, 2006, Interest Expense increased by \$2.6 million due to increased borrowings compared to the prior year and the acquisition of DAC. Interest Income decreased by \$1.1 million due to less cash investment balances during the quarter.

*Income Taxes*

The effective tax rate, after minority interest, for the nine months ended September 30, 2006 was 20.6%. Excluding the \$5.2 million change to the deferred tax valuation allowance accounted for in the second quarter of 2006, the Company's effective tax rate for the nine months ended September 30, 2006 was 34.2%. The effective tax rate, after minority interest, for the nine months ended September 30, 2005 was 15.1%. Excluding the \$9.9 million reversal of the U.S. deferred tax valuation allowance and \$3.9 million in taxes associated with our Dividend Repatriation Plan completed and accounted for in the third quarter of 2005, the effective tax rate would have been 43.3%. We expect our effective tax rate for the year ending December 31, 2006 will be approximately 30% to 35%, excluding the \$5.2 million reversal of a portion of the deferred tax valuation allowance in the second quarter of 2006.

**Liquidity and Capital Resources**

Our primary sources of liquidity during the nine months ended September 30, 2006 were existing cash balances, cash generated from operating activities, and borrowings under our revolving line of credit. We expect that our future working capital, capital expenditures, and debt service requirements will be satisfied primarily from existing cash balances and cash generated from operations. Our ability to generate positive future operating and net cash flows is dependent upon, among other things, our ability to (i) sell new business, (ii) expand existing client relationships, and (iii) efficiently manage our operating costs.

The amount of capital required in 2006 will also depend on our level of investment in infrastructure necessary to build new CMCs and maintain and upgrade existing CMCs. We currently expect that capital expenditures in 2006 will be higher than our 2005 capital expenditures resulting from our plans to expand our capacity in select markets with the addition of an estimated 2,500 workstations in Argentina, Canada, Mexico, and the Philippines.

The following discussion highlights our cash flow activities during the nine months ended September 30, 2006.

**Table of Contents***Cash and Cash Equivalents*

We consider all liquid investments purchased within 90 days of their maturity to be cash equivalents. Our Cash and Cash Equivalents totaled \$55.2 million as of September 30, 2006 compared to \$32.5 million as of December 31, 2005.

*Cash Flows From Operating Activities*

We reinvest the cash flows from operating activities in our business or in purchases of treasury stock. For the nine months ended September 30, 2006 and 2005, we reported net cash flows provided by operating activities of \$72.6 million and \$52.7 million, respectively. The increase for the nine months ended September 30, 2006 compared to the same period in 2005 is due primarily to higher net income and the recognition of a deferred tax benefit associated with changes in our deferred tax valuation allowance in the prior period.

*Cash Flows From Investing Activities*

We reinvest cash in our business primarily to grow our client base, expand our infrastructure, and complete select acquisitions. For the nine months ended September 30, 2006 and 2005, we reported net cash flows used in investing activities of \$99.2 million and \$29.2 million, respectively. The increase from 2005 to 2006 is due primarily to the expansion of CMCs in certain markets and the completion of the DAC acquisition in the second quarter of 2006.

*Cash Flows from Financing Activities*

For the nine months ended September 30, 2006 and 2005, we reported net cash flows provided by (used in) financing activities of \$47.7 million and \$(43.5) million, respectively. The change from 2005 to 2006 principally resulted from increased utilization of our Credit Facility, principally to finance the acquisition of DAC, offset by less repurchases of treasury stock compared to the prior year.

*Free Cash Flow and EBITDA*

Free Cash Flow (see Presentation of Non-GAAP Measurements for the definition of Free Cash Flow) was \$26.0 million and \$6.8 million for the three months ended September 30, 2006 and 2005, respectively, and \$21.4 million and \$26.0 million for the nine months ended September 30, 2006 and 2005, respectively. EBITDA (see Presentation of Non-GAAP Measurements for the definition of EBITDA), was \$33.9 million and \$24.6 million for the three months ended September 30, 2006 and 2005, respectively, and \$78.1 million and \$61.4 million for the nine months ended September 30, 2006 and 2005, respectively. The increase in EBITDA for the three months and nine months ended September 30, 2006, is primarily due to an increase in net income compared to the prior year periods.

**Obligations and Future Capital Requirements**

Future maturities of our outstanding debt and contractual obligations are summarized as follows (amounts in thousands):

	<b>Less than 1 year</b>	<b>2-3 years</b>	<b>4-5 years</b>	<b>More than 5 years</b>	<b>Total</b>
Line of credit <sup>1</sup>	\$	\$	\$ 77,750	\$	\$ 77,750
Capital lease obligations <sup>1</sup>	202	227	227	226	882
Grant advances <sup>1</sup>				7,163	7,163
Purchase obligations <sup>2</sup>	18,003	10,239	6,613	785	35,640
Operating lease commitments <sup>2</sup>	25,087	39,448	26,348	36,847	127,730
Total	\$ 43,292	\$ 49,914	\$ 110,938	\$ 45,021	\$ 249,165

<sup>1</sup> Reflected in the accompanying Condensed Consolidated Balance Sheets

<sup>2</sup> Not reflected in  
the  
accompanying  
Condensed  
Consolidated  
Balance Sheets

34

---

**Table of Contents**

*Purchase Obligations*

Occasionally, we contract with certain of our communication clients (which represent approximately one-third of our annual Revenue) to provide us with telecommunication services. We believe these contracts are negotiated on an arms-length basis and may be negotiated at different times and with different legal entities.

*Future Capital Requirements*

We expect total capital expenditures in 2006 to be approximately \$65 million, including capital expenditures for DAC. Expected capital expenditures in 2006 are related to the opening and/or expansion of CMCs as described above, which represents approximately 70% of expected capital expenditures, and maintenance capital for existing assets and internal technology projects, which represents the remaining 30%. The anticipated level of 2006 capital expenditures is primarily dependent upon new client contracts and the corresponding requirements for additional CMC capacity and enhancements to our technological infrastructure.

We may consider restructurings, dispositions, mergers, acquisitions, and other similar transactions. Such transactions could include the transfer, sale, or acquisition of significant assets, businesses, or interests, including joint ventures, or the incurrence, assumption, or refinancing of indebtedness, and could be material to our consolidated financial condition and consolidated results of operations.

**Debt Instruments and Related Covenants**

We discuss debt instruments and related covenants in Note 7 to the Condensed Consolidated Financial Statements.

**Client Concentration**

Our five largest clients accounted for 40% and 47% of our revenue for the three months ended September 30, 2006 and 2005, respectively. The five largest clients accounted for 43% and 49% of our revenue for the nine months ended September 30, 2006 and 2005, respectively. In addition, these five clients accounted for an even greater proportional share of our consolidated earnings. The profitability of services provided to these clients varies greatly based upon the specific contract terms with any particular client. In addition, clients may adjust business volumes served by us based on their business requirements. The relative contribution of any single client to consolidated earnings is not always proportional to the relative revenue contribution on a consolidated basis. We believe the risk of this concentration is mitigated, in part, by the long-term contracts we have with our largest clients. Although certain client contracts may be terminated for convenience by either party, this risk is mitigated, in part, by the service level disruptions that would arise for our clients.

The contracts with our five largest clients expire between 2007 and 2011. Additionally, a particular client can have multiple contracts with different expiration dates. We have historically renewed most of our contracts with our largest clients. However, there is no assurance that future contracts will be renewed, or if renewed, will be on terms as favorable as the existing contracts.

Based upon recent discussions, Client B (see Note 5 to the Condensed Consolidated Financial Statements) plans to utilize its internal offshore centers to perform a portion of the BPO work that we previously performed on their behalf from a North American CMC. The North American CMC that previously served Client B, and the corresponding Customer Service Representatives, have been assigned to new client engagements. This information was considered in developing our Business Outlook below.

**Recent Accounting Pronouncements**

We discuss the potential impact of recent accounting pronouncements in Note 1 to the Condensed Consolidated Financial Statements.

**Business Outlook**

For the full year 2006, we project revenue to grow approximately 11% to 12% over 2005. This projection includes a contribution of approximately \$35 million of revenue during the last six months of 2006 associated with the acquisition of DAC.

**Table of Contents**

We believe our fourth quarter 2006 EBITDA margin will approximate 11% to 12% and our operating margin will approximate 7% to 8% excluding unusual charges, if any.

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Market risk represents the risk of loss that may impact our consolidated financial position, consolidated results of operations, or consolidated cash flows due to adverse changes in financial and commodity market prices and rates. We are exposed to market risk in the areas of changes in U.S. interest rates, LIBOR, and foreign currency exchange rates as measured against the U.S. dollar. These exposures are directly related to our normal operating and funding activities. As of September 30, 2006, we had entered into financial hedge instruments with several financial institutions to manage and reduce the impact of changes, principally the U.S./Canadian dollar exchange rates.

**Interest Rate Risk**

The interest rate on our Credit Facility is variable based upon the Prime Rate and LIBOR and, therefore, is affected by changes in market interest rates. As of September 30, 2006, there was a \$77.8 million outstanding balance under the Credit Facility. If the Prime Rate increased 100 basis points, there would not be a material impact to the Company.

**Foreign Currency Risk**

We have operations in Argentina, Australia, Brazil, Canada, China, Germany, India, Malaysia, Mexico, New Zealand, the Philippines, Singapore, Spain, the United Kingdom, and Venezuela. The expenses from these operations, and in some cases the revenue, are denominated in local currency, thereby creating exposures to changes in exchange rates. As a result, we may experience substantial foreign currency translation gains or losses due to the volatility of other currencies compared to the U.S. dollar, which may positively or negatively affect our revenue and net income attributed to these subsidiaries. For the three months ended September 30, 2006 and 2005, revenue from non-U.S. countries represented 64% and 57% of consolidated revenue, respectively. For the nine months ended September 30, 2006 and 2005, revenue from non-U.S. countries represented 64% and 58% of consolidated revenue, respectively. A business strategy for our North American BPO segment is to serve certain U.S.-based clients from CMCs located in foreign countries, including Argentina, Canada, India, Mexico, and the Philippines, in order to leverage lower operating costs in these foreign countries. In order to mitigate the risk of these foreign currencies strengthening against the U.S. dollar, which thereby decreases the economic benefit of performing work in these countries, we may hedge a portion, but not 100%, of the foreign currency exposure related to client programs served from these foreign countries. While our hedging strategy can protect us from changes in the U.S./foreign currency exchange rates in the short-term, an overall strengthening of the foreign currencies would adversely impact margins in the North American BPO segment over the long-term.

The majority of this exposure is related to work performed from CMCs located in Canada. During the three months ended September 30, 2006 and 2005, the Canadian dollar weakened against the U.S. dollar by 0.3% and strengthened against the U.S. dollar by 5.3%, respectively. During the nine months ended September 30, 2006 and 2005, the Canadian dollar strengthened against the U.S. dollar by 4.3% and 3.7%, respectively. We have contracted with several financial institutions on behalf of our Canadian subsidiary to acquire a total of \$178.1 million Canadian dollars through June 2010 at a fixed price in U.S. dollars of \$159.5 million.

As of September 30, 2006, we had total derivative assets and liabilities associated with foreign exchange contracts of \$4.1 million and \$1.4 million, respectively, of which Canadian dollar derivative assets and liabilities represented \$2.7 million and \$1.4 million, respectively. 100% of the asset value and none of the liability balance settle within the next twelve months. If the U.S./Canadian dollar exchange rate were to increase or decrease 10% from period-end levels, we would incur a material gain or loss on the contracts. However, any gain or loss would be mitigated by corresponding gains or losses in the underlying exposures.

**Table of Contents**

Other than the transactions hedged as discussed above and in Note 6 to the Condensed Consolidated Financial Statements, the majority of the transactions of our U.S. and foreign operations are denominated in the respective local currency while some transactions are denominated in other currencies. For example, the intercompany transactions that are expected to be settled are denominated in the local currency of the billing company. Since the accounting records of our foreign operations are kept in the respective local currency, any transactions denominated in other currencies are accounted for in the respective local currency at the time of the transaction. Upon settlement of such a transaction, any foreign currency gain or loss results in an adjustment to income. We do not currently engage in hedging activities related to these types of foreign currency risks because we believe them to be insignificant as we endeavor to settle these accounts on a timely basis.

**Fair Value of Debt and Equity Securities**

We did not have any investments in debt or equity securities as of September 30, 2006.

**Item 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

We have established disclosure controls and procedures to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms. Our disclosure controls and procedures have also been designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to management, including the principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure. Based on their evaluation as of September 30, 2006, the principal executive officer and principal financial officer of the Company have concluded that the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) are effective.

**Changes in Internal Control Over Financial Reporting**

There has been no change in our internal control over financial reporting that occurred during the quarter ended September 30, 2006 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION**

**Item 1. LEGAL PROCEEDINGS**

From time-to-time, we may be involved in claims or lawsuits that arise in the ordinary course of business. Accruals for claims or lawsuits have been provided for to the extent that losses are deemed both probable and estimable. Although the ultimate outcome of these claims or lawsuits cannot be ascertained, it is our opinion, based on present information and advice received from counsel, that the disposition or ultimate determination of all such claims or lawsuits will not have a material adverse effect on the Company.

**Item 1A. RISK FACTORS**

The following is in addition to the risk factors titled *Our business may be affected by risks associated with international operations and expansion*, *Our financial results may be impacted by our ability to find new locations*, *Our financial results depend on our ability to manage capacity utilization*, *Our future success requires continued growth*, and *Our success depends on key personnel* in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

**Table of Contents**

*Our financial results may be adversely affected if we are unsuccessful in launching new client programs.* As previously announced, we were recently awarded new business with new and existing clients. As a result, we are expanding our capacity in select markets with the addition of an estimated 2,500 workstations in Argentina, Canada, Mexico, and the Philippines. We may have difficulties finding cost effective locations; obtaining favorable lease terms; building or retrofitting facilities in a timely and economic manner; launching new or expanded client programs; and successfully managing the associated internal allocation of personnel and resources. This could cause a decline in or delay in recognition of revenues and an increase in costs, either of which could adversely affect our operating results. In the event we do not successfully expand our capacity or launch the new or expanded client programs, we may be unable to achieve the revenue and profitability expectations outlined in the Business Outlook section.

The following restates the risk factor titled *Our success may be affected by our ability to complete and integrate acquisitions and joint ventures* in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

*Our success may be affected by our ability to complete and integrate acquisitions and joint ventures.* We may pursue strategic acquisitions of companies with services, technologies, industry specializations, or geographic coverage that extend or complement our existing business. We may face increased competition for acquisition opportunities, which may inhibit our ability to complete suitable acquisitions on favorable terms. We may pursue strategic alliances in the form of joint ventures and partnerships, which involve many of the same risks as acquisitions as well as additional risks associated with possible lack of control if we do not have a majority ownership position. There can be no assurance that we will be successful in integrating acquisitions or joint ventures into our existing businesses, or that any acquisition or joint venture will enhance our business, results of operations, or financial condition.

Further, it is possible that the contemplated benefits of acquisitions, including the acquisition of DAC in the second quarter of 2006, may not materialize within the expected time periods or to the extent anticipated. Critical to the success of our acquisition strategy in the future is the orderly, effective integration of acquired businesses into our organization. If this integration is unsuccessful, our business may be adversely impacted. There is also the risk that our valuation assumptions and models for an acquisition may be overly optimistic or incorrect. The acquisition model for DAC assumed revenue growth of \$18 million in 2007, including revenue growth within the existing client base. In the event we are not successful in growing DAC's revenue by \$18 million in 2007, or achieving revenue growth within the existing client base, we may not achieve the profitability expectations outlined in the DAC acquisition model, which could adversely affect our consolidated operating results.

The following restates the risk factor titled, *Our financial results may be adversely impacted by our Database Marketing and Consulting segment* in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

*Our financial results may be adversely impacted by our Database Marketing and Consulting segment.* Prior to 2005, our Database Marketing and Consulting segment historically experienced high levels of profitability. During 2005 and the nine months ended September 30, 2006, this segment reported an operating loss. We are taking steps to return this segment to profitability. There can be no assurance that we will be successful in executing our plans to return this segment to prior levels of profitability. In the event we are not successful in executing our plans, all or a portion of this segment's recorded goodwill of \$13.4 million would be impaired, with a corresponding adverse impact on our financial results in the period of impairment. Our current sensitivity testing of the fair value of this segment is such that it would not take a material change to the forecasted results used for estimating the fair value of this segment for an impairment to arise and, accordingly, our success at implementing our plans, as discussed above, during the remainder of 2006 will determine whether our assumptions used for evaluating the fair market value of this segment were sufficient. We plan to evaluate this matter again for the quarter ended December 31, 2006.

**Table of Contents****Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

In November 2001, the Board of Directors ( Board ) authorized a stock repurchase program to repurchase up to \$5 million of our common stock. That plan was subsequently amended by the Board resulting in the authorized repurchase amount increasing to \$165 million. During the three months ended September 30, 2006, we purchased 0.3 million shares for \$4.0 million. During the nine months ended September 30, 2006, we purchased 1.2 million shares for \$14.6 million. From inception of the program through September 30, 2006, we have purchased 13.1 million shares for \$113.7 million, leaving \$51.3 million remaining under the repurchase program as of September 30, 2006. The program does not have an expiration date.

**ISSUER PURCHASES OF EQUITY SECURITIES**

Period	Total Number of Shares Purchased (000 s)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (000 s)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (000 s)
July 1, 2006 - July 31, 2006	45,000	\$11.52	45,000	\$ 54,723
August 1, 2006 - August 31, 2006	52,000	\$13.04	52,000	\$ 54,045
Sept. 1, 2006 - Sept. 30, 2006	184,400	\$15.06	184,400	\$ 51,268
Total	281,400	\$14.12	281,400	

**Item 3. DEFAULTS UPON SENIOR SECURITIES**

None

**Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None

**Item 5. OTHER INFORMATION**

None



**Table of Contents**

**Item 6. EXHIBITS**

<b>Exhibit No.</b>	<b>Exhibit Description</b>
10.42	Amended and Restated Credit Agreement among TeleTech Holdings, Inc., as borrower, The Lenders named herein, as Lenders, and KeyBank National Association, as Lead Arranger, Sole Book Runner and Administrative Agent dated as of September 28, 2006.
10.43	First Amendment to the Amended and Restated Credit Agreement among TeleTech Holdings, Inc., as borrower, The Lenders named herein, as Lenders, and KeyBank National Association, as Lead Arranger, Sole Book Runner and Administrative Agent dated as of October 24, 2006.
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
31.2	Certification of Acting Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
32.2	Certification of Acting Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

TELETECH HOLDINGS, INC.  
(Registrant)

Date: October 25, 2006

By: /s/ KENNETH D. TUCHMAN  
Kenneth D. Tuchman  
Chairman and Chief Executive Officer

Date: October 25, 2006

By: /s/ JOHN R. TROKA  
John R. Troka  
Vice President and  
Acting Chief Financial Officer

---

**Table of Contents**

**EXHIBIT INDEX**

<b>Exhibit No.</b>	<b>Exhibit Description</b>
10.42	Amended and Restated Credit Agreement among TeleTech Holdings, Inc., as borrower, The Lenders named herein, as Lenders, and KeyBank National Association, as Lead Arranger, Sole Book Runner and Administrative Agent dated as of September 28, 2006.
10.43	First Amendment to the Amended and Restated Credit Agreement among TeleTech Holdings, Inc., as borrower, The Lenders named herein, as Lenders, and KeyBank National Association, as Lead Arranger, Sole Book Runner and Administrative Agent dated as of October 24, 2006.
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
31.2	Certification of Acting Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
32.2	Certification of Acting Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)