

CSG SYSTEMS INTERNATIONAL INC  
Form 10-Q  
August 06, 2010  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2010

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 0-27512

**CSG SYSTEMS INTERNATIONAL, INC.**

(Exact name of registrant as specified in its charter)

Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**47-0783182**  
(I.R.S. Employer  
Identification No.)

**9555 Maroon Circle**  
**Englewood, Colorado 80112**

(Address of principal executive offices, including zip code)

**(303) 200-2000**

(Registrant's telephone number, including area code)

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 has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES  NO

Shares of common stock outstanding at August 3, 2010: 34,061,653

**Table of Contents**

**CSG SYSTEMS INTERNATIONAL, INC.**

**FORM 10-Q for the Quarter Ended June 30, 2010**

**INDEX**

	<b>Page No.</b>
<b>Part I - FINANCIAL INFORMATION</b>	
Item 1. <u>Condensed Consolidated Balance Sheets as of June 30, 2010 and December 31, 2009 (Unaudited)</u>	3
<u>Condensed Consolidated Statements of Income for the Quarter and Six Months Ended June 30, 2010 and 2009 (Unaudited)</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2010 and 2009 (Unaudited)</u>	5
<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	6
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	14
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	25
Item 4. <u>Controls and Procedures</u>	26
<b>Part II - OTHER INFORMATION</b>	
Item 1. <u>Legal Proceedings</u>	27
Item 1A. <u>Risk Factors</u>	27
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	33
Item 6. <u>Exhibits</u>	33
<u>Signatures</u>	34
<u>Index to Exhibits</u>	35

**Table of Contents****CSG SYSTEMS INTERNATIONAL, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS - UNAUDITED**

(in thousands, except share and per share amounts)

	June 30, 2010	December 31, 2009
<b><u>ASSETS</u></b>		
Current assets:		
Cash and cash equivalents	\$ 182,692	\$ 163,489
Short-term investments	46,974	34,888
<b>Total cash, cash equivalents and short-term investments</b>	<b>229,666</b>	<b>198,377</b>
Trade accounts receivable-		
Billed, net of allowance of \$2,130 and \$2,036	100,393	107,810
Unbilled and other	9,197	9,140
Deferred income taxes	2,519	16,826
Income taxes receivable	3,398	2,114
Other current assets	13,188	9,575
<b>Total current assets</b>	<b>358,361</b>	<b>343,842</b>
Property and equipment, net of depreciation of \$99,145 and \$88,195	50,417	56,799
Software, net of amortization of \$42,695 and \$40,266	11,456	12,157
Goodwill	108,022	107,052
Client contracts, net of amortization of \$128,396 and \$122,666	38,342	41,407
Other assets	8,317	4,920
<b>Total assets</b>	<b>\$ 574,915</b>	<b>\$ 566,177</b>
<b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>		
Current liabilities:		
Current maturities of long-term debt, net of unamortized original issue discount of \$2,549 and zero	\$ 47,855	\$ 29,906
Client deposits	30,617	29,906
Trade accounts payable	28,978	26,856
Accrued employee compensation	23,928	26,598
Deferred revenue	29,865	26,307
Other current liabilities	12,257	9,894
<b>Total current liabilities</b>	<b>173,500</b>	<b>119,561</b>
Non-current liabilities:		
Long-term debt, net of unamortized original issue discount of \$37,004 and \$12,853	112,996	157,447
Deferred revenue	19,584	20,498
Income taxes payable		5,889
Deferred income taxes	41,105	42,198
Other non-current liabilities	7,598	8,474
<b>Total non-current liabilities</b>	<b>181,283</b>	<b>234,506</b>
<b>Total liabilities</b>	<b>354,783</b>	<b>354,067</b>
Stockholders' equity:		

## Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

Preferred stock, par value \$.01 per share; 10,000,000 shares authorized; zero shares issued and outstanding		
Common stock, par value \$.01 per share; 100,000,000 shares authorized; 34,028,148 and 35,125,943 shares outstanding	640	636
Additional paid-in capital	433,537	408,722
Treasury stock, at cost, 29,956,808 and 28,456,808 shares	(704,963)	(675,623)
Accumulated other comprehensive income (loss):		
Unrealized gain on short-term investments, net of tax	1	10
Unrecognized pension plan losses and prior service costs, net of tax	(897)	(919)
Accumulated earnings	491,814	479,284
<b>Total stockholders' equity</b>	<b>220,132</b>	<b>212,110</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 574,915</b>	<b>\$ 566,177</b>

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

**Table of Contents****CSG SYSTEMS INTERNATIONAL, INC.****CONDENSED CONSOLIDATED STATEMENTS OF INCOME - UNAUDITED**

(in thousands, except share and per share amounts)

	Quarter Ended		Six Months Ended	
	June 30, 2010	June 30, 2009	June 30, 2010	June 30, 2009
<b>Revenues:</b>				
Processing and related services	\$ 121,363	\$ 114,859	\$ 243,409	\$ 229,587
Software, maintenance and services	9,983	9,977	18,200	18,795
<b>Total revenues</b>	<b>131,346</b>	<b>124,836</b>	<b>261,609</b>	<b>248,382</b>
<b>Cost of revenues (exclusive of depreciation, shown separately below):</b>				
Processing and related services	68,925	61,243	135,929	121,497
Software, maintenance and services	5,912	6,552	11,880	12,954
<b>Total cost of revenues</b>	<b>74,837</b>	<b>67,795</b>	<b>147,809</b>	<b>134,451</b>
<b>Other operating expenses:</b>				
Research and development	18,990	17,558	37,502	34,709
Selling, general and administrative	16,678	14,989	33,212	28,807
Depreciation	6,091	4,901	11,713	9,141
Restructuring charges	(7)	6	214	108
<b>Total operating expenses</b>	<b>116,589</b>	<b>105,249</b>	<b>230,450</b>	<b>207,216</b>
<b>Operating income</b>	<b>14,757</b>	<b>19,587</b>	<b>31,159</b>	<b>41,166</b>
<b>Other income (expense):</b>				
Interest expense	(1,629)	(1,394)	(3,177)	(2,967)
Amortization of original issue discount	(1,685)	(2,083)	(3,985)	(4,308)
Gain (loss) on repurchase of convertible debt securities			(10,952)	1,468
Interest and investment income, net	251	356	367	838
Other, net	6		4	
<b>Total other</b>	<b>(3,057)</b>	<b>(3,121)</b>	<b>(17,743)</b>	<b>(4,969)</b>
<b>Income before income taxes</b>	<b>11,700</b>	<b>16,466</b>	<b>13,416</b>	<b>36,197</b>
<b>Income tax provision</b>	<b>(234)</b>	<b>(5,763)</b>	<b>(886)</b>	<b>(12,669)</b>
<b>Net income</b>	<b>\$ 11,466</b>	<b>\$ 10,703</b>	<b>\$ 12,530</b>	<b>\$ 23,528</b>
<b>Weighted-average shares outstanding - Basic:</b>				
Common stock	32,303	33,201	32,677	33,136
Participating restricted stock	531	1,080	637	1,216
<b>Total</b>	<b>32,834</b>	<b>34,281</b>	<b>33,314</b>	<b>34,352</b>
<b>Weighted-average shares outstanding - Diluted:</b>				
Common stock	32,562	33,274	32,938	33,193
Participating restricted stock	531	1,080	637	1,216

Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

Total	33,093	34,354	33,575	34,409
Earnings per common share:				
Basic	\$ 0.35	\$ 0.31	\$ 0.38	\$ 0.68
Diluted	\$ 0.35	\$ 0.31	\$ 0.37	\$ 0.68

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

**Table of Contents****CSG SYSTEMS INTERNATIONAL, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - UNAUDITED**

(in thousands)

	Six Months Ended	
	June 30, 2010	June 30, 2009
<b>Cash flows from operating activities:</b>		
Net income	\$ 12,530	\$ 23,528
Adjustments to reconcile net income to net cash provided by operating activities-		
Depreciation	11,713	9,141
Amortization	8,285	7,125
Amortization of original issue discount	3,985	4,308
Gain on short-term investments and other	(79)	(443)
(Gain) loss on repurchase of convertible debt securities	10,952	(1,468)
Deferred income taxes	(44)	11,820
Excess tax benefit of stock-based compensation awards	(1,098)	(142)
Stock-based employee compensation	6,184	6,238
Changes in operating assets and liabilities:		
Trade accounts and other receivables, net	7,360	10,298
Other current and non-current assets	(3,911)	(2,815)
Income taxes payable/receivable	(6,423)	(6,961)
Trade accounts payable and accrued liabilities	3,637	(5,713)
Deferred revenue	2,644	4,650
<b>Net cash provided by operating activities</b>	<b>55,735</b>	<b>59,566</b>
<b>Cash flows from investing activities:</b>		
Purchases of property and equipment	(7,519)	(24,384)
Purchases of short-term investments	(46,922)	(22,215)
Proceeds from sale/maturity of short-term investments	34,900	44,200
Acquisition of businesses, net of cash acquired	(2,764)	(7,373)
Acquisition of and investments in client contracts	(2,623)	(3,748)
<b>Net cash used in investing activities</b>	<b>(24,928)</b>	<b>(13,520)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from issuance of common stock	772	645
Repurchase of common stock	(33,643)	(6,157)
Payments on acquired equipment financing	(571)	(463)
Proceeds from issuance of convertible debt securities	150,000	
Payments of deferred financing costs	(4,268)	
Repurchase of convertible debt securities	(124,992)	(26,714)
Excess tax benefit of stock-based compensation awards	1,098	142
<b>Net cash used in financing activities</b>	<b>(11,604)</b>	<b>(32,547)</b>
<b>Net increase in cash and cash equivalents</b>	<b>19,203</b>	<b>13,499</b>
Cash and cash equivalents, beginning of period	163,489	83,886
<b>Cash and cash equivalents, end of period</b>	<b>\$ 182,692</b>	<b>\$ 97,385</b>



## Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

Supplemental disclosures of cash flow information:

Net cash paid during the period for-

Interest	\$	1,499	\$	2,408
Income taxes		7,365		7,801

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

---

**Table of Contents**

**CSG SYSTEMS INTERNATIONAL, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(UNAUDITED)**

**1. GENERAL**

We have prepared the accompanying unaudited condensed consolidated financial statements as of June 30, 2010 and December 31, 2009, and for the second quarter and six months ended June 30, 2010 and 2009, in accordance with accounting principles generally accepted in the United States of America ( GAAP ) for interim financial information, and pursuant to the instructions to Form 10-Q and the rules and regulations of the Securities and Exchange Commission (the SEC ). Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of our management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation of our financial position and operating results have been included. The unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and notes thereto, together with Management's Discussion and Analysis of Financial Condition and Results of Operations, contained in our Annual Report on Form 10-K for the year ended December 31, 2009, filed with the SEC. The results of operations for the second quarter and six months ended June 30, 2010 are not necessarily indicative of the expected results for the entire year ending December 31, 2010.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Use of Estimates in Preparation of Condensed Consolidated Financial Statements.* The preparation of the accompanying Condensed Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

*Reclassification.* Certain prior year amounts have been reclassified to conform to the June 30, 2010 presentation.

*Accounting Pronouncements Issued But Not Yet Effective.* In October 2009, the FASB issued a new pronouncement related to revenue arrangements with multiple deliverables. This new guidance requires a vendor to allocate revenue to each unit of accounting in many arrangements involving multiple deliverables based upon the relative selling price of each deliverable. It also changes the level of evidence of stand-alone selling price required to separate deliverables by allowing a vendor to make its best estimate of the stand-alone selling price of deliverables when more objective evidence of selling price is not available. The pronouncement also prohibits the use of the residual method of allocating arrangement consideration to deliverables, but instead, requires the use of the relative selling price method where the vendor must determine a stand-alone selling price for all deliverables that meet the separation criteria. The pronouncement's scope is limited to multiple element arrangements, and does not apply to deliverables within the scope of the software revenue recognition rules or other authoritative literature that addresses both separation and allocation. The provisions of this new pronouncement are effective for fiscal years beginning on or after June 15, 2010, and can be adopted prospectively to new or materially modified revenue arrangements entered into or materially modified after the effective date or retrospectively for all periods presented. We are currently evaluating the impact that this new guidance will have on our consolidated results of operations and financial condition, which we expect to adopt on a prospective basis on January 1, 2011.

*Postage.* We pass through to our clients the cost of postage that is incurred on behalf of those clients, and typically require an advance payment on expected postage costs. These advance payments are included in client deposits in the accompanying Condensed Consolidated Balance Sheets and are classified as current liabilities regardless of the contract period. We net the cost of postage against the postage reimbursements, and include the net amount in processing and related services revenues. The cost of postage that has been shown net of the postage reimbursements from our clients for the second quarter of 2010 and 2009 was \$66.2 million and \$65.0 million, respectively, and for the six months ended June 30, 2010 and 2009 was \$135.2 million and \$132.3 million, respectively.

**Table of Contents****CSG SYSTEMS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(UNAUDITED)**

*Short-term Investments and Other Financial Instruments.* Our financial instruments as of June 30, 2010 and December 31, 2009, include cash and cash equivalents, short-term investments, accounts receivable, accounts payable, and debt. Because of their short maturities, the carrying amounts of cash equivalents, accounts receivable, and accounts payable approximate their fair value.

Our short-term investments and certain cash equivalents are considered available-for-sale and are reported at fair value in our accompanying Condensed Consolidated Balance Sheets, with unrealized gains and losses, net of the related income tax effect, excluded from earnings and reported in a separate component of stockholders' equity. Realized and unrealized gains and losses were not material in any period presented.

Our short-term investments at June 30, 2010, and December 31, 2009, consisted of the following (in thousands):

	<b>June 30, 2010</b>	<b>December 31, 2009</b>
Commercial paper	\$ 46,974	\$ 31,388
Certificates of deposit		3,500
<b>Total</b>	<b>\$ 46,974</b>	<b>\$ 34,888</b>

All short-term investments held by us as of June 30, 2010, have contractual maturities of less than one year from the time of acquisition. Proceeds from the sale/maturity of short-term investments for the six months ended June 30, 2010 and 2009 were \$34.9 million and \$44.2 million, respectively.

The following table represents the fair value hierarchy based upon three levels of inputs, of which Levels 1 and 2 are considered observable and Level 3 is unobservable, for our cash equivalents and short-term investments measured at fair value (in thousands):

	<b>June 30, 2010</b>			<b>December 31, 2009</b>		
	<b>Level 1</b>	<b>Level 2</b>	<b>Total</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Total</b>
Money market funds	\$ 121,897	\$	\$ 121,897	\$ 122,942	\$	\$ 122,942
Commercial paper		87,168	87,168		56,641	56,641
Certificates of deposit					3,500	3,500
<b>Total</b>	<b>\$ 121,897</b>	<b>\$ 87,168</b>	<b>\$ 209,065</b>	<b>\$ 122,942</b>	<b>\$ 60,141</b>	<b>\$ 183,083</b>

Valuation inputs used to measure the fair values of our money market funds were derived from quoted market prices. The fair values of all other instruments are based upon pricing provided by third-party pricing services. These prices were derived from observable market inputs.

As of June 30, 2010, our debt consists of our 2004 Convertible Debt Securities and our 2010 Convertible Notes (see Note 6). As of June 30, 2010 and December 31, 2009, the fair value of our 2004 Convertible Debt Securities, based upon quoted market prices or recent sales activity, was approximately \$51 million and \$169 million, respectively. As of June 30, 2010, the fair value of our 2010 Convertible Notes, based upon quoted market prices or recent sales activity, was approximately \$145 million.

**3. STOCKHOLDERS' EQUITY AND EQUITY COMPENSATION PLANS**

## Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

*Stock Repurchase Program.* We currently have a stock repurchase program, approved by our Board of Directors, authorizing us to repurchase our common stock from time-to-time as market and business conditions warrant (the "Stock Repurchase Program"). We did not repurchase any shares under our Stock Repurchase Program during the quarters ended June 30, 2010 and 2009. During the six months ended June 30, 2010 and 2009, we repurchased 1.5 million shares and 250,000 shares of our common stock under the Stock Repurchase Program for \$29.3 million (weighted-average price of \$19.56 per share) and \$3.8 million (weighted-average price of \$15.13 per share), respectively. As of June 30, 2010, the total remaining number of shares available for repurchase under the Stock Repurchase Program totaled 4.2 million shares.

**Table of Contents****CSG SYSTEMS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(UNAUDITED)**

*Stock Repurchases for Tax Withholdings.* In addition to the above mentioned stock repurchases, a summary of shares repurchased from our employees and then cancelled during the second quarter and six months ended June 30, 2010 and 2009, in connection with minimum tax withholding requirements resulting from the vesting of restricted common stock under our stock incentive plans, is as follows (in thousands):

	Quarter Ended		Six Months Ended	
	June 30, 2010	2009	June 30, 2010	2009
Shares repurchased	7	8	211	169
Total amount paid	\$ 140	\$ 110	\$ 4,305	\$ 2,376

*Stock-Based Awards.* A summary of our unvested restricted common stock activity during the second quarter and six months ended June 30, 2010, is as follows:

	Quarter Ended		Six Months Ended	
	June 30, 2010	June 30, 2010	June 30, 2010	June 30, 2010
	Shares	Weighted-Average Grant Date Fair Value	Shares	Weighted-Average Grant Date Fair Value
Unvested awards, beginning	1,770,792	\$ 17.13	1,751,717	\$ 16.12
Awards granted	5,500	19.18	616,330	20.13
Awards forfeited/cancelled	(49,678)	16.30	(53,053)	16.29
Awards vested	(19,975)	20.86	(608,355)	17.37
Unvested awards, ending	1,706,639	\$ 17.11	1,706,639	\$ 17.11

Included in the awards granted during the six months ended June 30, 2010, are performance-based awards for 83,500 restricted common stock shares issued to members of executive management, which vest in equal installments over three years upon meeting either pre-established financial performance objectives or pre-established stock price objectives. The performance-based awards become fully vested upon a change in control, as defined, and the subsequent involuntary termination of employment.

All other restricted common stock shares granted during the six months ended June 30, 2010, are time-based awards, which generally vest annually over four years with no restrictions other than the passage of time. Certain shares of the restricted common stock become fully vested upon a change in control, as defined, and the subsequent involuntary termination of employment.

We recorded stock-based compensation expense for the second quarter of 2010 and 2009 of \$3.2 million in both periods, and for the six months ended June 30, 2010 and 2009 of \$6.2 million in both periods.

**4. EARNINGS PER COMMON SHARE**

Basic and diluted earnings per common share ( EPS ) amounts are presented on the face of the accompanying Condensed Consolidated Statements of Income. The amounts attributed to both common stock and participating restricted common stock used as the numerators in both the basic and diluted EPS calculations are as follows (in thousands):

Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

	Quarter Ended		Six Months Ended	
	June 30,		June 30,	
	2010	2009	2010	2009
Net Income attributed to:				
Common stock	\$ 11,281	\$ 10,366	\$ 12,290	\$ 22,695
Participating restricted common stock	185	337	240	833
Total	\$ 11,466	\$ 10,703	\$ 12,530	\$ 23,528

**Table of Contents****CSG SYSTEMS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(UNAUDITED)**

The weighted-average shares outstanding used in the basic and diluted EPS denominators related to common stock and participating restricted common stock are as follows (in thousands):

	<b>Quarter Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
<b>Weighted-average shares outstanding Basic:</b>				
Common stock	32,303	33,201	32,677	33,136
Participating restricted common stock	531	1,080	637	1,216
<b>Total</b>	<b>32,834</b>	<b>34,281</b>	<b>33,314</b>	<b>34,352</b>
<b>Weighted-average shares outstanding Diluted:</b>				
Common stock	32,562	33,274	32,938	33,193
Participating restricted common stock	531	1,080	637	1,216
<b>Total</b>	<b>33,093</b>	<b>34,354</b>	<b>33,575</b>	<b>34,409</b>

The reconciliation of the basic and diluted EPS denominators related to the common shares is included in the following table (in thousands):

	<b>Quarter Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
Basic weighted-average common shares	32,303	33,201	32,677	33,136
Dilutive effect of common stock options	23	24	26	26
Dilutive effect of non-participating restricted common stock	236	49	235	31
Dilutive effect of 2010 Convertible Notes				
Dilutive effect of 2004 Convertible Debt Securities				
<b>Diluted weighted-average common shares</b>	<b>32,562</b>	<b>33,274</b>	<b>32,938</b>	<b>33,193</b>

Potentially dilutive common shares related to stock options and non-participating unvested shares of restricted common stock of 0.1 million and 0.2 million, respectively, for the second quarter of 2010 and 2009, and 0.2 million for the six months ended June 30, 2010 and 2009, respectively, were excluded from the computation of diluted EPS related to common shares as their effect was antidilutive.

The 2010 Convertible Notes have a dilutive effect only in those quarterly periods in which our average stock price exceeds the current effective conversion price of \$24.45 per share. The 2004 Convertible Debt Securities have a dilutive effect only in those quarterly periods in which our average stock price exceeds the current effective conversion price of \$26.77 per share. See Note 6 for additional discussion of our 2010 Convertible Notes and 2004 Convertible Debt Securities.

**5. COMPREHENSIVE INCOME**

## Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

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

	Quarter Ended		Six Months Ended	
	June 30,		June 30,	
	2010	2009	2010	2009
Net income	\$ 11,466	\$ 10,703	\$ 12,530	\$ 23,528
Other comprehensive income (loss), net of tax, if any:				
Change in unrecognized pension plan gains and prior service costs, net of tax			22	
Unrealized loss on short-term investments	(7)	(48)	(9)	(193)
<b>Comprehensive income</b>	<b>\$ 11,459</b>	<b>\$ 10,655</b>	<b>\$ 12,543</b>	<b>\$ 23,335</b>



Table of Contents

## CSG SYSTEMS INTERNATIONAL, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(UNAUDITED)

**6. DEBT**

As of June 30, 2010 and December 31, 2009, our long-term debt, net of unamortized original issue discount (OID), was as follows (in thousands):

	June 30, 2010	December 31, 2009
<b>Liability component:</b>		
2010 Convertible Notes – senior subordinated convertible notes; due March 1, 2017; cash interest at 3.0%; net of unamortized OID of \$37,004 and zero, respectively	\$ 112,996	\$
2004 Convertible Debt Securities – senior subordinated convertible contingent debt securities; due June 15, 2024; cash interest at 2.5%; net of unamortized OID of \$2,549 and \$12,853, respectively	47,855	157,447
	160,851	157,447
Current portion of long-term debt	(47,855)	
Total long-term debt	\$ 112,996	\$ 157,447
<b>Equity component (included within additional paid-in capital, net of tax):</b>		
2010 Convertible Notes	\$ 23,727	\$
2004 Convertible Debt Securities	38,270	39,752

The OID related to the 2010 Convertible Notes is being amortized to interest expense through March 1, 2017, the maturity date of the 2010 Convertible Notes. The OID related to the 2004 Convertible Debt Securities is being amortized to interest expense through June 15, 2011, which is the first date that the 2004 Convertible Debt Securities can be put back to us by the holders for cash. The effective interest rates of the liability components for the 2010 Convertible Notes and the 2004 Convertible Debt Securities are 7.75% and 8.00%, respectively.

*2010 Convertible Notes.* On March 1, 2010, we completed an offering of \$150 million of 3.0% senior subordinated convertible notes due March 1, 2017 (2010 Convertible Notes) to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended. The 2010 Convertible Notes are unsecured obligations, equal in right of payment to our 2004 Convertible Debt Securities, subordinated to any future senior indebtedness and senior to any future junior subordinated debt. The 2010 Convertible Notes were issued at a price of 100% of their par value and bear interest at a rate of 3.0% per annum, which is payable semiannually in arrears on March 1 and September 1 of each year, beginning on September 1, 2010.

The net proceeds from the sale of the 2010 Convertible Notes were approximately \$145 million, after debt issuance costs. We used the net proceeds, along with available cash, cash equivalents and short-term investments, to: (i) repurchase 1.5 million shares of our common stock for \$29.3 million (\$19.56 per share) under our existing Stock Repurchase Program; and (ii) repurchase \$119.9 million (par value) of our 2004 Convertible Debt Securities for a total purchase price of \$125.8 million, which included accrued interest of \$0.8 million.

The 2010 Convertible Notes are convertible into our common stock, under the specified conditions and settlement terms outlined below, at an initial conversion rate of 40.8998 shares of our common stock per \$1,000 par value of the 2010 Convertible Notes, which is equivalent to an initial conversion price of approximately \$24.45 per share. The Indenture related to the 2010 Convertible Notes (Notes Indenture) includes anti-dilution provisions for the holders such that the conversion rate (and thus the initial conversion price) can be adjusted in the future for certain events, to include stock dividends, the issuance of rights, options or warrants to purchase our common stock at a price below the then-current market price, and certain distributions of common stock, property or rights, options or warrants to acquire our common stock to all or substantially all holders of our common stock. Additionally, the conversion rate may be adjusted prior to the maturity date in connection with

the occurrence of specified corporate transactions for a make-whole premium as set forth in the Notes Indenture.

**Table of Contents**

**CSG SYSTEMS INTERNATIONAL, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(UNAUDITED)**

Prior to September 1, 2016, holders of the 2010 Convertible Notes can convert their securities: (i) at any time the price of our common stock trades over \$31.79 per share (130% of the \$24.45 initial conversion price) for a specified period of time; (ii) at any time the trading price of the 2010 Convertible Notes falls below 98% of the average conversion value for the 2010 Convertible Notes for a specified period of time; and (iii) at any time upon the occurrence of specified corporate transactions, to include a change of control (as defined in the Notes Indenture). On or after September 1, 2016, the holders of the 2010 Convertible Notes can elect to convert their securities at any time, with the settlement occurring on March 1, 2017. As of June 30, 2010, none of the contingent conversion features have been achieved, and thus, the 2010 Convertible Notes are not convertible by the holders.

Upon conversion of the 2010 Convertible Notes, we will settle our conversion obligation as follows: (i) we will pay cash for 100% of the par value of the 2010 Convertible Notes that are converted; and (ii) to the extent the value of our conversion obligation exceeds the par value, we will satisfy the remaining conversion obligation in our common stock, cash or any combination of our common stock and cash. As of June 30, 2010, the value of our conversion obligation did not exceed the par value of the 2010 Convertible Notes.

*2004 Convertible Debt Securities.* The 2004 Convertible Debt Securities are unsecured obligations, subordinated to any of our future senior indebtedness, and senior to any future junior subordinated debt. The 2004 Convertible Debt Securities were issued at a price of 100% of their par value and bear interest at a rate of 2.5% per annum, which is payable semiannually in arrears on June 15 and December 15 of each year. The 2004 Convertible Debt Securities are callable by us for cash, on or after June 20, 2011, at a redemption price equal to 100% of the par value of the 2004 Convertible Debt Securities, plus accrued interest. The 2004 Convertible Debt Securities can be put back to us by the holders for cash at June 15, 2011, 2016 and 2021, or upon a change of control, as defined in the 2004 Convertible Debt Securities bond indenture ( *Bonds Indenture* ), at a repurchase price equal to 100% of the par value of the 2004 Convertible Debt Securities, plus any accrued interest. Therefore, we have included the 2004 Convertible Debt Securities in current maturities of long-term debt on the Condensed Consolidated Balance Sheet as of June 30, 2010.

The 2004 Convertible Debt Securities are convertible into our common stock, under the specified conditions and settlement terms outlined below, at a conversion rate of 37.3552 shares per \$1,000 par value of the 2004 Convertible Debt Securities, which is equal to an initial conversion price of \$26.77 per share. The Bonds Indenture includes anti-dilution provisions for the holders such that the conversion rate (and thus the initial conversion price) can be adjusted in the future for certain events, to include stock dividends, stock splits/reverse splits, the issuance of warrants to purchase our stock at a price below the then-current market price, cash dividends, and certain purchases by us of our common stock pursuant to a self-tender offer or exchange offer.

Holders of the 2004 Convertible Debt Securities can convert their securities: (i) at any time the price of our common stock trades over \$34.80 per share (130% of the \$26.77 initial conversion price) for a specified period of time; (ii) at any time the trading price of the 2004 Convertible Debt Securities falls below 98% of the average conversion value for the 2004 Convertible Debt Securities for a specified period of time; (iii) upon us exercising our right to redeem the 2004 Convertible Debt Securities at any time after June 20, 2011; (iv) at any time upon the occurrence of specified corporate transactions, to include a change in control (as defined in the Bonds Indenture); and (v) if a certain level of dividends are declared, or a certain number of shares of our common stock are repurchased under a self-tender offer by us. As of June 30, 2010, none of the contingent conversion features have been achieved, and thus, the 2004 Convertible Debt Securities are not convertible by the holders.

Upon conversion of the 2004 Convertible Debt Securities, we will settle our conversion obligation as follows: (i) we will pay cash for 100% of the par value of the 2004 Convertible Debt Securities that are converted; and (ii) to the extent the value of our conversion obligation exceeds the par value, we will satisfy the remaining conversion obligation in our common stock, cash or any combination of our common stock and cash. As of June 30, 2010, the value of our conversion obligation did not exceed the par value of the 2004 Convertible Debt Securities.

In March 2010, we repurchased \$119.9 million (par value) of our 2004 Convertible Debt Securities for a total purchase price of \$125.0 million. In the first quarter of 2010, we recognized a non-cash loss on the repurchase of approximately \$11 million. In July 2010, we repurchased \$23.2 million (par value) of our 2004 Convertible Debt Securities for a total purchase price of \$23.9 million. As a result, in the third quarter of 2010, we expect to recognize a non-cash loss on the repurchase of approximately \$2 million. This debt has been considered extinguished for

accounting purposes.

**Table of Contents****CSG SYSTEMS INTERNATIONAL, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(UNAUDITED)**

As a result of the repurchases of our 2004 Convertible Debt Securities in 2009 and in 2010 through the date of this filing, beginning in 2014, we will have to pay cash of approximately \$30 million ratably over five years related to the deferred tax liabilities associated with the repurchased securities. In addition, if the remaining 2004 Convertible Debt Securities are put back to us on June 15, 2011, in 2011, we will have to settle in cash approximately \$7 million of deferred tax liabilities associated with the outstanding securities.

*Deferred Financing Costs.* As of June 30, 2010, net deferred financing costs related to the 2010 Convertible Notes were \$3.6 million, and are being amortized to interest expense through maturity (March 1, 2017). As of June 30, 2010, net deferred financing costs related to the 2004 Convertible Debt Securities were \$0.2 million, and are being amortized to interest expense through the first date the holders of the 2004 Convertible Debt Securities can be put back to us (June 15, 2011). The net deferred financing costs are reflected in Other Assets in the accompanying Condensed Consolidated Balance Sheets. Amortization of deferred financing costs included in interest expense for the second quarter of 2010 and 2009 was \$0.2 million in both periods, and for the six months ended June 30, 2010 and 2009 was \$0.3 million in both periods.

**7. LONG-LIVED ASSETS**

*Goodwill.* The changes in the carrying amount of goodwill for the six months ended June 30, 2010 were as follows (in thousands):

January 1, 2010, balance	\$ 107,052
Adjustments related to prior acquisitions	970
June 30, 2010, balance	\$ 108,022

The adjustments related to prior acquisitions are mainly due to the recording of contingent purchase price payments totaling \$1.0 million associated with the Quaero acquisition.

*Other Intangible Assets.* Our intangible assets subject to ongoing amortization consist primarily of client contracts and software. As of June 30, 2010 and December 31, 2009, the carrying values of these assets were as follows (in thousands):

	June 30, 2010			December 31, 2009		
	Gross		Net Amount	Gross		Net Amount
	Carrying Amount	Accumulated Amortization		Carrying Amount	Accumulated Amortization	
Client contracts	\$ 166,738	\$ (128,396)	\$ 38,342	\$ 164,073	\$ (122,666)	\$ 41,407
Software	54,151	(42,695)	11,456	52,423	(40,266)	12,157
Total	\$ 220,889	\$ (171,091)	\$ 49,798	\$ 216,496	\$ (162,932)	\$ 53,564

The total amortization expense related to intangible assets for the second quarter of 2010 and 2009 was \$4.0 million, and for the six months ended June 30, 2010 and 2009, was \$7.9 million and \$6.7 million, respectively. Based on the June 30, 2010 net carrying value of our intangible assets, the estimated total amortization expense for each of the five succeeding fiscal years ending December 31 are: 2010 \$16.1 million; 2011 \$15.5 million; 2012 \$13.0 million; 2013 \$4.9 million; and 2014 \$3.5 million.

**8. COMMITMENTS, GUARANTEES AND CONTINGENCIES**

*Warranties.* We generally warrant that our solutions and related offerings will conform to published specifications, or to specifications provided in an individual client arrangement, as applicable. The typical warranty period is 90 days from delivery of the solution or offering. For certain service offerings we provide a limited warranty for the duration of the services provided. We generally warrant that services will be performed in a professional and workmanlike manner. The typical remedy for breach of warranty is to correct or replace any defective deliverable, and if not possible or practical, we will accept the return of the defective deliverable and refund the amount paid under the client arrangement that is allocable to the defective deliverable. Our contracts also generally contain limitation of damages provisions in an effort to reduce our exposure to monetary damages arising from breach of warranty claims. Historically, we have incurred minimal warranty costs, and as a result, do not maintain a warranty reserve.

**Table of Contents**

**CSG SYSTEMS INTERNATIONAL, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(UNAUDITED)**

*Product and Services Indemnifications.* Our arrangements with our clients generally include an indemnification provision that will indemnify and defend a client in actions brought against the client that claim our products and/or services infringe upon a copyright, trade secret, or valid patent. Historically, we have not incurred any significant costs related to such indemnification claims, and as a result, do not maintain a reserve for such exposure.

*Claims for Company Non-performance.* Our arrangements with our clients typically cap our liability for breach to a specified amount of the direct damages incurred by the client resulting from the breach. From time-to-time, these arrangements may also include provisions for possible liquidated damages or other financial remedies for our non-performance, or in the case of certain of our outsourced customer care and billing solutions, provisions for damages related to service level performance requirements. The service level performance requirements typically relate to system availability and timeliness of service delivery. As of June 30, 2010, we believe we have adequate reserves, based on our historical experience, to cover any reasonably anticipated exposure as a result of our nonperformance for any past or current arrangements with our clients. The amount of the reserve maintained for this purpose is not material.

*Indemnifications Related to Sold Businesses.* In conjunction with the sale of the GSS business in December 2005, we provided certain indemnifications to the buyer of this business which are considered routine in nature (such as employee, tax, or litigation matters that occurred while these businesses were under our ownership). Under the provisions of this indemnification agreement, payment by us is conditioned on the other party making a claim pursuant to the procedures in the indemnification agreement, and we are typically allowed to challenge the other party's claims. In addition, certain of our obligations under this indemnification agreement are limited in terms of time and/or amounts, and in some cases, we may have recourse against a third party if we are required to make certain indemnification payments.

We estimated the fair value of these indemnifications at \$2.8 million as of the closing date for the sale of the GSS business. Since the sale of the GSS business, we have made an indemnification payment of \$0.1 million, and as of June 30, 2010, the indemnification liability was \$2.3 million and related principally to indemnifications related to income tax matters. It is not possible to predict the maximum potential amount of future payments we may be required to make under this indemnification agreement due to the conditional nature of our obligations and the unique facts and circumstances associated with each indemnification provision. We believe that if we were required to make payments in excess of the indemnification liability we have recorded, the resulting loss would not have a material effect on our financial condition or results of operations. If any amounts required to be paid by us would differ from the amounts initially recorded as indemnification liabilities as of the closing dates for the sale of the GSS business, the difference would be reflected in the discontinued operations section of our Consolidated Statements of Income.

*Indemnifications Related to Officers and the Board of Directors.* We have agreed to indemnify certain of our officers and members of our Board of Directors if they are named or threatened to be named as a party to any proceeding by reason of the fact that they acted in such capacity. We maintain directors' and officers' (D&O) insurance coverage to protect against such losses. We have not historically incurred any losses related to these types of indemnifications, and are not aware of any pending or threatened actions or claims against any officer or member of our Board of Directors. As a result, we have not recorded any liabilities related to such indemnifications as of June 30, 2010. In addition, as a result of the insurance policy coverage, we believe these indemnification agreements are not significant to our results of operations.

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

**9. INCOME TAXES**

In the second quarter of 2010, the Internal Revenue Service ( IRS ) completed an examination with respect to our 2006, 2007 and 2008 Federal income tax returns, which resulted in favorable adjustments to our liability for unrecognized income tax benefits of approximately \$4 million. Over the last several years, we have added to the balance of our liability for unrecognized income tax benefits due to uncertainty in the realization of certain tax credits and incentives we have claimed on our Federal income tax returns. The realization uncertainty was due to the complexity of the income tax regulations associated with the tax credits and incentives, and the judgments and estimates involved in calculating the tax credits and incentives claimed. The completion of the IRS examination resolved that uncertainty. As required by current accounting rules, the favorable adjustments have been reflected in total in the period the uncertainty was resolved. As a result, there is a significant variation

Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

in our effective income tax rate for the quarter and six months ended June 30, 2010.



## **Table of Contents**

### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The information contained in this Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) should be read in conjunction with the unaudited Condensed Consolidated Financial Statements and Notes thereto (our Financial Statements ) included in this Form 10-Q and the audited consolidated financial statements and notes thereto in our Annual Report on Form 10-K for the year ended December 31, 2009 (our 2009 10-K ).

#### ***Forward-Looking Statements***

This report contains a number of forward-looking statements relative to our future plans and our expectations concerning our business and the industries we serve. These forward-looking statements are based on assumptions about a number of important factors, and involve risks and uncertainties that could cause actual results to differ materially from estimates contained in the forward-looking statements. Some of the risks that are foreseen by management are outlined within Part II Item 1A., Risk Factors . Item 1A. constitutes an integral part of this report, and readers are strongly encouraged to review this section closely in conjunction with MD&A.

#### ***Company Overview***

*Our Company.* We are a leading provider of customer interaction management solutions to the North American market. We provide fully outsourced customer care and billing solutions to the cable and direct broadcast satellite ( DBS ) industry that combine the reliability and high-volume transaction processing capabilities of an enterprise server platform with the flexibility of client/server architecture. In addition to these critical business support services that we provide to our clients, our Intelligent Customer Communications solutions facilitate effective interactions between our clients and their end customers through various touch points, including electronic communication channels such as the Internet, interactive communications channels such as voice and text messaging, and through enhanced print communications.

Our broad suite of solutions help our clients improve their profitability by creating more compelling product offerings and an enhanced customer experience through more relevant and targeted interactions. Our solutions help our clients maximize the value and minimize the costs associated with their customer interactions by:

Targeting and acquiring the right customers through the most effective communications channels;

Analyzing customer purchasing and interaction patterns and other data to offer new products and services in relevant and meaningful packages;

Managing the critical back office processes required to offer, deploy, service, and bill customer orders and requests more efficiently;

Empowering our clients' workforce with the tools and the information required for them to improve customer satisfaction and retention through informed and efficient interactions;

Improving the communications between our clients and their end customers by providing meaningful, relevant, and targeted messages via the desired communication vehicle, whether that be electronic or print; and

Improving efficiencies by streamlining all operations through a customer-centric focus.

Recently, we have broadened and enhanced our Intelligent Customer Communication solutions to not only increase our capabilities to our existing clients, but to also expand these services into new industries, including utilities, healthcare, home security, financial services, and content distribution. These are industries where companies require solutions that foster relevant interactions with customers that result in increased customer satisfaction and revenues. This approach has helped us to diversify our revenue base. During the second quarter of 2010, 86% of our revenues came from the cable and DBS industry; whereas three years ago, nearly all of our revenues came from the cable and DBS industry. The shift in revenue mix has primarily been achieved through acquisitions, which has expanded the capabilities of our Intelligent

## Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

Customer Communications solutions, and has provided us new markets to penetrate.

Our solutions are delivered and supported by an experienced and dedicated workforce of more than 2,000 employees. We are a S&P SmallCap 600 company.

## Table of Contents

**Market Concentration.** The North American communications industry has experienced significant consolidation over the past decade, resulting in a large percentage of the market being served by a limited number of service providers with greater size and scale. Consistent with this market concentration, a large percentage of our revenues are generated from a limited number of clients, with approximately two-thirds of our revenues being generated from our four largest clients, which are Comcast Corporation ( Comcast ), DISH Network Corporation ( DISH ), Time Warner Cable Inc. ( Time Warner ), and Charter Communications ( Charter ).

**General Market Conditions.** Over the past few years, the U.S. has experienced a significant economic downturn and difficulties within all industry sectors, but in particular, the financial and credit markets. While these adverse economic conditions appear to be easing, our sales cycles continue to be extended and revenues related to our clients' discretionary spending for such things as special project work and marketing and advertising activities continue to be negatively impacted.

We believe that our recurring revenue and predictable cash flow business model, our sufficient sources of liquidity, and our stable capital structure lessen the risk of a significant negative impact to our business as a result of the current economic conditions. Also, our business model has certain economic advantages to our clients since it generally requires a lower initial capital investment, thus, allowing clients to utilize our advanced, integrated product offerings on a pay-as-you-grow basis. Additionally, we believe our key clients have business models that have historically performed well, as compared to other industries, in down economic conditions. However, there can be no assurances regarding the performance of our business, and the potential impact to our clients and key vendors, resulting from the current or future economic conditions.

### **Management Overview of Quarterly Results**

**Second Quarter Highlights.** A summary of our results of operations for the second quarter of 2010, when compared to the second quarter of 2009, is as follows (in thousands, except per share amounts and percentages):

	Quarter Ended June 30,	
	2010	2009
Revenues	\$ 131,346	\$ 124,836
Customer Accounts (end of period)	48,864	45,440
<b>Operating Results:</b>		
Operating Income	\$ 14,757	\$ 19,587
Operating Income Margin	11.2%	15.7%
Diluted EPS	\$ 0.35	\$ 0.31
<b>Supplemental Data:</b>		
Data center transition expenses	\$ 10,600	\$ 2,668
Stock-based compensation	3,175	3,223
Amortization of acquired intangible assets	1,163	2,293
Amortization of OID	1,685	2,083

**Revenues.** Our revenues for the second quarter of 2010 were \$131.3 million, up 5.2% when compared to \$124.8 million for the same period in 2009, with the increase entirely a result of organic growth factors.

**Operating Results.** Operating income for the second quarter of 2010 was \$14.8 million, or an 11.2% operating income margin percentage, compared to \$19.6 million, or a 15.7% operating income margin percentage, for the second quarter of 2009. These decreases in operating income and operating income margin percentage are related to the \$7.9 million increase in quarterly data center transition expenses between years, which resulted in a 6.0 percentage point reduction in our operating income margin percentage between periods. See the Data Center Transition Expenses section below for further discussion of these expenses.

**Effective Income Tax Rate.** For the second quarter of 2010, our effective income tax rate was 2%, compared to an effective income tax rate of 35% for the second quarter of 2009. The 2% effective income tax rate for the second quarter of 2010 is primarily the result of the completion during the quarter of an Internal Revenue

**Table of Contents**

Service ( IRS ) examination of our 2006, 2007, and 2008 Federal income tax returns, which resulted in favorable adjustments to our liability for unrecognized income tax benefits (i.e., income tax reserves) of approximately \$4 million. Absent the impact of these favorable adjustments, our effective income tax rate for the quarter and six months ended June 30, 2010, would have been approximately 38%, which is more in line with our historical rates. As a result, the diluted EPS impacts for specific items referred to in the following MD&A discussions for the quarter and six months ended June 30, 2010 have been calculated using an effective income tax rate of 38%, which is the implicit rate attributable to the related items. See the Income Tax Provision section below under the Results of Operations for further discussion.

**Diluted EPS.** Diluted EPS the second quarter of 2010 was \$0.35 per diluted share, which compares to \$0.31 per diluted share for the second quarter of 2009. Diluted EPS for the second quarter of 2010, when compared to diluted EPS for the second quarter of 2009, was significantly impacted by the following items:

the effective income tax rate of 2% for the second quarter of 2010, noted above, which provided a positive EPS impact of \$0.13 for the quarter; and

the \$7.9 million increase in the quarterly data center transition expenses between years, which provided a negative EPS impact of \$0.15.

**Balance Sheet and Cash Flows.** As of June 30, 2010, we had cash, cash equivalents, and short-term investments of \$229.7 million, as compared to \$210.7 million as of March 31, 2010, and \$198.4 million as of December 31, 2009. We continue to generate strong cash flows from operations. Cash flows from operating activities for the second quarter of 2010 were \$24.4 million, compared to \$43.6 million for the second quarter of 2009, and \$31.3 million for the first quarter of 2010, with the fluctuations between periods primarily attributed to changes in operating assets and liabilities, discussed in further detail below.

**Significant Client Relationships**

**Client Concentration.** Approximately two-thirds of our total revenues are generated from our four largest clients, which include Comcast, DISH, Time Warner, and Charter. Revenues from these clients represented the following percentages of our total revenues for the indicated periods:

	Quarter Ended		
	June 30, 2010	March 31, 2010	June 30, 2009
Comcast	25%	24%	24%
DISH	18%	18%	19%
Time Warner	12%	12%	13%
Charter	11%	10%	9%

The percentages of net billed accounts receivable balances attributable to our largest clients as of the indicated dates were as follows:

	As of		
	June 30, 2010	December 31, 2009	June 30, 2009
Comcast	21%	19%	29%
DISH	16%	26%	18%
Time Warner	16%	9%	12%
Charter	14%	13%	11%

See our 2009 10-K for additional discussion of our business relationships with the above mentioned significant clients.

**Risk of Client Concentration.** We expect to continue to generate a large percentage of our total revenues from our four largest clients mentioned above. There are inherent risks whenever a large percentage of total revenues are concentrated with a limited number of clients. One such risk is that, should a significant client: (i) terminate or fail to renew its contract with us, in whole or in part, for any reason; (ii) significantly reduce the

## Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

number of customer accounts processed on our solutions, the price paid for our services, or the scope of services that we provide; or (iii) experience significant financial or operating difficulties, it could have a material adverse effect on our financial condition and results of operations.

**Table of Contents****Data Center Transition**

In December 2008, we entered into an agreement with Infocrossing LLC ( Infocrossing ), a Wipro Limited company, to transition our outsourced data center services from First Data Corporation ( FDC ) to Infocrossing. The term of the Infocrossing agreement runs through May 2015 (five years from the date of conversion of our primary computing environment from FDC to Infocrossing). We are changing data center providers to partner with a global provider that focuses on data center operations in greater scale, and as their core business focus. This allows us to further improve the delivery of our solutions while benefiting from an improved cost structure.

We began our transition efforts to the new Infocrossing data center in the first quarter of 2009, and completed a significant portion of the migration to the Infocrossing data center during the second quarter of 2010. We are expecting the migration to be completed in the second half of 2010.

We are tracking the expenses attributable to our decision to change data center service providers separately, as these expenses are not considered reflective of our recurring core business operating results. See our 2009 10-K for a description of the items that are included in our data center transition expenses.

During the quarter and six months ended June 30, 2010 and 2009, we incurred the following expenses related to our data center transition efforts that are included in the following captions in the Condensed Consolidated Statements of Income (in thousands):

	Quarter Ended		Six Months Ended	
	June 30, 2010	June 30, 2009	June 30, 2010	June 30, 2009
Cost of processing and related services	\$ 9,908	\$ 2,668	\$ 16,303	\$ 4,057
Depreciation	692		2,014	
<b>Total data center transition expenses</b>	<b>\$ 10,600</b>	<b>\$ 2,668</b>	<b>\$ 18,317</b>	<b>\$ 4,057</b>
Estimated per diluted share impact (1)	\$ 0.20	\$ 0.05	\$ 0.34	\$ 0.08

(1) This represents the after-tax impact to net income on a per diluted share basis using an effective income tax rate of 38% for the quarter and six months ended June 30, 2010, and 35% for the quarter and six months ended June 30, 2009.

Additionally, during the second quarter of 2010 and 2009 we spent approximately \$1 million and \$11 million, and during six months ended June 30, 2010 and 2009 we spent approximately \$2 million and \$12 million, respectively, related to network and computer equipment needed to set-up and replicate the computing environment at the new Infocrossing data center location.

For the full year 2010, we estimate that the data center transition expenses will be approximately \$21 million (pretax impact), and are expected to have a negative impact of approximately \$12 million on our 2010 cash flows from operations. We do not expect any further significant capital expenditure requirements as the migration comes to a close over the coming months. These amounts are based on the best available estimates at this time and may fluctuate up or down as we continue to complete our transition plan.

The Infocrossing agreement, with confidential information redacted, is included in the exhibits to our periodic filings with the SEC.

**Table of Contents****Stock-Based Compensation Expense**

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

	Quarter Ended		Six Months Ended	
	June 30, 2010	June 30, 2009	June 30, 2010	June 30, 2009
Cost of processing and related services	\$ 787	\$ 908	\$ 1,549	\$ 1,830
Cost of software, maintenance and services	221	247	413	442
Research and development	446	408	856	827
Selling, general and administrative	1,721	1,660	3,366	3,139
<b>Total stock-based compensation expense</b>	<b>\$ 3,175</b>	<b>\$ 3,223</b>	<b>\$ 6,184</b>	<b>\$ 6,238</b>

**Critical Accounting Policies**

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

We have identified the most critical accounting policies that affect our financial condition and the results of our operations. Those critical accounting policies were determined by considering the accounting policies that involve the most complex or subjective decisions or assessments. The most critical accounting policies identified relate to: (i) revenue recognition; (ii) allowance for doubtful accounts receivable; (iii) impairment assessments of goodwill and other long-lived assets; (iv) income taxes; and (v) business combinations and asset purchases. These critical accounting policies, as well as our other significant accounting policies, are discussed in our 2009 10-K.

**Results of Operations**

**Total Revenues.** Total revenues for the: (i) second quarter of 2010 increased 5.2% to \$131.3 million, from \$124.8 million for the second quarter of 2009; and (ii) six months ended June 30, 2010 increased 5.3% to \$261.6 million, from \$248.4 million for the six months ended June 30, 2009. These increases are entirely a result of organic growth factors.

The components of total revenues are discussed in more detail below.

**Processing and related services revenues.** Processing and related services revenues for the: (i) second quarter of 2010 increased 5.7% to \$121.4 million, from \$114.9 million for the second quarter of 2009; and (ii) for the six months ended June 30, 2010 increased 6.0% to \$243.4 million from \$229.6 million for the six months ended June 30, 2009. These increases in processing and related services revenues can be entirely attributed to organic growth resulting from: (i) continued adoption and use of our advanced customer interaction management solutions; and (ii) conversions of customer accounts onto our solutions during the second half of 2009.

Additional information related to processing and related services revenues is as follows:

Amortization of our client contracts intangible assets (reflected as a reduction of processing and related services revenues) for the: (i) second quarter of 2010 and 2009 was \$1.6 million and \$1.0 million, respectively; and (ii) six months ended June 30, 2010 and 2009 was \$3.2 million and \$2.0 million, respectively.

## Edgar Filing: CSG SYSTEMS INTERNATIONAL INC - Form 10-Q

Total customer accounts processed on our solutions as of June 30, 2010, were 48.9 million, compared to 45.4 million as of June 30, 2009, and 49.0 million as of March 31, 2010. The year-over-year increase is attributed to the 3.1 million customer accounts we converted onto our solutions during the second half of 2009.



**Table of Contents**

*Software, Maintenance and Services Revenues.* Software, maintenance and services revenues for the: (i) second quarter of 2010 was \$10.0 million, consistent with the second quarter of 2009; and (ii) six months ended June 30, 2010 decreased 3.2% to \$18.2 million, from \$18.8 million for the six months ended June 30, 2009. The decrease in software, maintenance and services revenues is due to lower professional services revenue as a result of the completion of certain consulting projects in 2009.

*Total Expenses.* Our operating expenses for the: (i) second quarter of 2010 were \$116.6 million, up 10.8% when compared to \$105.2 million for the same period in 2009; and (ii) six months ended June 30, 2010 were \$230.5 million, up 11.2% when compared to \$207.2 million for the six months ended June 30, 2009. These year-over-year increases can be mainly attributed to the following items:

Approximately two-thirds of the increases can be attributed to the quarterly and year-to-date increases in our data center transition expenses. During the second quarter of 2010, we incurred \$10.6 million of costs related to our data center transition efforts, as compared to \$2.7 million of expense in the second quarter of 2009 (a \$7.9 million increase), and during the six months ended June 30, 2010, we incurred \$18.3 million of data center transition costs, as compared to \$4.1 million during the six months ended June 30, 2009 (a \$14.2 million increase). See the Data Center Transition Expenses section for a further discussion of these efforts.

Of the remaining quarterly and year-to-date expense increases, the majority can be attributed to various operational expenses, consistent with the growth in our business year-over-year.

The components of total expenses are discussed in more detail below.

*Cost of Revenues.* See our 2009 10-K for a description of the types of costs that are included in the individual line items for cost of revenues.

*Cost of Processing and Related Services.* The cost of processing and related services for the: (i) second quarter of 2010 increased 12.5% to \$68.9 million, from \$61.2 million for the second quarter of 2009; and (ii) six months ended June 30, 2010 increased 11.9% to \$135.9 million from \$121.5 million for the six months ended June 30, 2009. Total processing and related services cost as a percentage of our processing and related services revenues for the (i) second quarter of 2010 and 2009 was 56.8% and 53.3%, respectively; and (ii) six months ended June 30, 2010 and 2009 was 55.8% and 52.9%, respectively.

The increases in processing and related services cost and processing and related services cost as a percentage of our processing and related services revenues can be mainly attributed to the increased data center transition expenses, which had the following impact:

	Quarter Ended June 30, 2010		2009		Six Months Ended June 30, 2010		2009	
	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues
Cost of processing and related services revenues, all other	\$ 59,017	48.6%	\$ 58,575	51.0%	\$ 119,626	49.1%	\$ 117,440	51.1%
Data center transition expenses	9,908	8.2%	2,668	2.3%	16,303	6.7%	4,057	1.8%
Cost of processing and related services revenues	\$ 68,925	56.8%	\$ 61,243	53.3%	\$ 135,929	55.8%	\$ 121,497	52.9%

Absent the impact of the data center transition expenses, processing and related services cost of revenues as a percentage of our processing and related services revenues would have decreased between periods. This decrease is reflective of the scale benefits we have been able to achieve from the increased number of customer accounts on our systems and is also due to the operational and financial benefits that we began to experience during the second quarter of 2010, following our migration efforts to the new data center location.

*Cost of Software, Maintenance and Services.* The cost of software, maintenance and services for the: (i) second quarter of 2010 decreased 9.8% to \$5.9 million, from \$6.6 million for the second quarter of 2009; and (ii) six months ended June 30, 2010 decreased 8.3% to \$11.9 million, from \$13.0 million for the six months ended June 30, 2009. These decreases are a result of a reduction in personnel and related costs assigned internally to software maintenance and consulting projects.



---

**Table of Contents**

Total cost of software, maintenance and services as a percentage of our software, maintenance and services revenues for the: (i) second quarter of 2010 and 2009 was 59.2% and 65.7%, respectively; and (ii) six months ended June 30, 2010 and 2009 was 65.3% and 68.9%, respectively. Variability in quarterly revenues and operating results are inherent characteristics of companies that sell software licenses, and perform professional services. Our quarterly revenues for software licenses and professional services may fluctuate, depending on various factors, including the timing of executed contracts and revenue recognition, and the delivery of solutions. However, the costs associated with software and professional services revenues are not subject to the same degree of variability (e.g., these costs are generally fixed in nature within a relatively short period of time), and thus, fluctuations in our cost of software and maintenance, professional services as a percentage of our software, maintenance and services revenues will likely occur between periods.

*R&D Expense.* R&D expense for the (i) second quarter of 2010 increased 8.2% to \$19.0 million, from \$17.6 million for the second quarter of 2009; and (ii) six months ended June 30, 2010 increased 8.0% to \$37.5 million, from \$34.7 million for the six months ended June 30, 2009. The increase between periods is primarily due to an increase in personnel on R&D projects, reflective of focus on product development and enhancement efforts. As a percentage of total revenues, R&D expense was 14.5% for the second quarter of 2010, compared to 14.1% for the second quarter of 2009. We did not capitalize any internal software development costs during the six months ended June 30, 2010 and 2009.

Over the past few years, our R&D efforts have been focused on the continued evolution of our solutions, both functionally and architecturally, in response to market demands that our solutions have certain functional features and capabilities, as well as architectural flexibilities (such as service oriented architecture, or SOA). This evolution will result in the modularization of certain functionality that historically has been tightly integrated within our solution suite, which will allow us to respond more quickly to required changes to our solutions and provide greater interoperability with other computer systems. Additionally, our R&D efforts include creating an integrated suite of customer interaction management solutions that provide additional customer insight, communications channels, and an enhanced customer experience across all delivery vehicles, whether that be more traditional methods like print or more interactive means like electronic and digital communications. Our customer interaction management solutions are aimed at both of our core cable/DBS market as well as new verticals such as utilities, healthcare, home security, financial services, and content distribution.

We expect that the percentage of our total revenues invested in R&D to be relatively consistent with the most recent quarters, with the level of our R&D spend highly dependent upon the opportunities that we see in our markets.

*Selling, General and Administrative ( SG&A ) Expense.* SG&A expense for the (i) second quarter of 2010 increased 11.3% to \$16.7 million, from \$15.0 million for the second quarter of 2009; and (ii) six months ended June 30, 2010 increased 15.3% to \$33.2 million, from \$28.8 million for the six months ended June 30, 2009. These increases reflect our increased sales and marketing efforts to expand into other vertical markets. As a percentage of total revenues, SG&A expense was 12.7% for the second quarter of 2010, compared to 12.0% for the second quarter of 2009. SG&A expense for the first quarter of 2010 was 12.7%, consistent with the current quarter.

*Depreciation Expense.* Depreciation expense for the: (i) second quarter of 2010 increased 24.3% to \$6.1 million, from \$4.9 million for the second quarter of 2009; and (ii) six months ended June 30, 2010 increased 28.1% to \$11.7 million, from \$9.1 million for the six months ended June 30, 2009. The increase in depreciation expense is a result of the large amount of capital expenditures we have made over the last 18 months, related primarily to our data center transition. Included in the quarter and six months ended June 30, 2010 amounts are \$0.7 million and \$2.0 million of depreciation expense related to our data center transition efforts, discussed earlier, which accounts for the majority of the year-over-year increases.

**Table of Contents**

*Operating Income.* Operating income and operating income margin for the: (i) second quarter of 2010 was \$14.8 million, or 11.2% of total revenues, compared to \$19.6 million, or 15.7% of total revenues for the second quarter of 2009; and (ii) six months ended June 30, 2010 was \$31.2 million, or 11.9% of total revenues, compared to \$41.2 million, or 16.6% of total revenues for the six months ended June 30, 2009. The decreases in operating income and operating income margin between years can be mainly attributed to the data center transition expenses, which had the following impacts to our operating income and operating income margins:

	Quarter Ended June 30,				Six Months Ended June 30,			
	2010		2009		2010		2009	
	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues
Operating income, all other	\$ 25,357	19.3%	\$ 22,255	17.8%	\$ 49,476	18.9%	\$ 45,223	18.2%
Data center transition expenses	(10,600)	(8.1)%	(2,668)	(2.1)%	(18,317)	(7.0)%	(4,057)	(1.6)%
<b>Operating income</b>	<b>\$ 14,757</b>	<b>11.2%</b>	<b>\$ 19,587</b>	<b>15.7%</b>	<b>\$ 31,159</b>	<b>11.9%</b>	<b>\$ 41,166</b>	<b>16.6%</b>

Absent the impact of the data center transition expenses, our operating income and operating income margin would have improved between periods as a result of: (i) the scale benefits that we have been able to achieve from the increased number of customer accounts on our systems; (ii) the operational and financial benefits that we began to experience during the second quarter of 2010, following our migration efforts to the new data center location; and (iii) our continued expense management. With the substantial completion of our data center transition in the second quarter of 2010, we expect that our operating income margin for the second half of 2010 to improve over the first half of the year.

*Gain (loss) on Repurchase of Convertible Debt Securities.* During the six months ended June 30, 2010, we repurchased \$119.9 million (par value) of our 2004 Convertible Debt Securities for a total purchase price of \$125.0 million. As a result of this transaction, we recognized a non-cash loss on the repurchase of \$11.0 million (pretax impact), or \$0.20 per diluted share. During the six months ended June 30, 2009, we repurchased \$15.0 million (par value) of our 2004 Convertible Debt Securities for \$13.2 million, which resulted in a non-cash gain of \$1.5 million (pretax impact), or \$0.03 per diluted share.

*Income Tax Provision.* The effective income tax rates for the quarter and six months ended June 30, 2010 and 2009 were as follows:

	Quarter Ended		Six Months Ended	
	June 30,		June 30,	
	2010	2009	2010	2009
	2%	35%	7%	35%

The lower effective income tax rate for the quarter and six months ended June 30, 2010 is the result of the completion during the second quarter of 2010 of an IRS examination of our 2006, 2007, and 2008 Federal income tax returns. Under current accounting rules, we were required to establish a liability for unrecognized income tax benefits (i.e., income tax reserves) related to the uncertainty in the realization of certain tax credits and incentives over the last several years. The realization uncertainty was due to the complexity of the income tax regulations associated with the tax credits and incentives, and the judgments and estimates involved in calculating the tax credits and incentives claimed. The completion of the IRS examination essentially validated our calculation methodology and assumptions utilized in determining our credit and incentive amounts. Therefore, favorable adjustments to our income tax reserves of approximately \$4 million, or \$0.13 and \$0.12 per diluted share, respectively, for the quarter and six months ended June 30, 2010, were necessary in accordance with our accounting policies.

For the full year 2010, we expect our effective income tax rate to be approximately 28%. Absent the favorable impact of the \$4 million adjustment to our income tax reserves discussed above, our expected full year effective income tax rate would be approximately 35%. Both of these estimates assume that Congress will approve the proposed 2010 R&D tax credit legislation before the end of the year, as it has done so consistently in the past.

**Table of Contents****Liquidity***Cash and Liquidity*

As of June 30, 2010, our principal sources of liquidity included cash, cash equivalents, and short-term investments of \$229.7 million, compared to \$210.7 million as of March 31, 2010, and \$198.4 million as of December 31, 2009. We generally invest our excess cash balances in low-risk, short-term investments to limit our exposure to market risks. We have ready access to essentially all of our cash, cash equivalents, and short-term investment balances.

*Cash Flows From Operating Activities*

We calculate our cash flows from operating activities in accordance with GAAP, beginning with net income, adding back the impact of non-cash items (e.g., depreciation, amortization, amortization of OID, deferred income taxes, stock-based compensation, etc.), and then factoring in the impact of changes in operating assets and liabilities. See our 2009 10-K for a description of the primary uses and sources of our cash flows from operating activities.

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

	<b>Operations</b>	<b>Changes in Operating Assets and Liabilities</b>	<b>Net Cash Provided by Operating Activities Quarter Totals</b>
<b>Cash Flows from Operating Activities:</b>			
<b>2009:</b>			
March 31	\$ 30,449	\$ (14,436)	\$ 16,013
June 30	29,658	13,895	43,553
September 30	30,593	7,289	37,882
December 31	24,320	31,291	55,611
<b>2010:</b>			
March 31	27,376	3,948	31,324
June 30	25,052	(641)	24,411

Our cash flows from operating activities include a negative impact of approximately \$10 million for the six months ended June 30, 2010, and approximately \$8 million for the year ended December 31, 2009, related to the costs incurred for our data center transition efforts.

We believe the above table illustrates our ability to consistently generate strong quarterly and annual cash flows, and the importance of managing our working capital items. As the table above illustrates, the operations portion of our cash flows from operating activities remains relatively consistent between periods. The variations in our net cash provided by operating activities are related mostly to the changes in our operating assets and liabilities (related mostly to normal fluctuations in timing at quarter-end for such things as client payments and changes in accrued expenses), and generally over longer periods of time, do not significantly impact our cash flows from operations.

Significant fluctuations in the balances of key operating assets and liabilities between June 30, 2010, and December 31, 2009, that impacted our cash flows from operating activities, are as follows:

***Billed Trade Accounts Receivable***

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



**Table of Contents**

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

Quarter Ended	Gross	Allowance	Net Billed	DBOs
<b>2009:</b>				
March 31	\$ 133,041	\$ (2,831)	\$ 130,210	58
June 30	112,612	(2,148)	110,464	58
September 30 114	114,403	(2,079)	112,324	54
December 31	109,846	(2,036)	107,810	50
<b>2010:</b>				
March 31	109,456	(2,289)	107,167	51
June 30	102,523	(2,130)	100,393	51

The changes in our gross and net billed trade accounts receivable shown in the table above reflect the normal fluctuations in the timing of client payments made at quarter-end, evidenced by our consistent DBO metric over the past several quarters.

**Income Taxes Receivable/Payable**

As of June 30, 2010, CSG was in a net income taxes receivable position of \$3.4 million, as compared to December 31, 2009, where CSG was in a net income taxes payable position of \$3.8 million. This \$7.2 million change is primarily the result of: (i) the finalization of the IRS examination of our 2006, 2007, and 2008 Federal income tax returns, which resulted in favorable adjustments to our liability for unrecognized income tax benefits of approximately \$4 million (as discussed above); and (ii) normal timing differences related to our estimated Federal and state income tax payments.

**Cash Flows From Investing Activities**

Our typical investing activities consist of purchases/sales of short-term investments, purchases of property and equipment, and investments in client contracts, which are discussed below. During the first six months of 2010 and 2009, our cash flows from investing activities also included cash payments related to our prior year acquisition activities.

*Purchases/Sales of Short-term Investments.* During the six months ended June 30, 2010 and 2009, we purchased \$46.9 million and \$22.2 million, respectively, and sold (or had mature) \$34.9 million and \$44.2 million, respectively, of short-term investments. We continually evaluate the appropriate mix of our investment of excess cash balances between cash equivalents and short-term investments in order to maximize our investment returns and will likely purchase and sell additional short-term investments in the future.

*Property and Equipment/Client Contracts.* Our capital expenditures for the six months ended June 30, 2010 and 2009, for property and equipment, and investments in client contracts were as follows (in thousands):

	Six Months Ended June 30,	
	2010	2009
Property and equipment	\$ 7,519	\$ 24,384
Client contracts	2,623	3,748

Of the \$7.5 million spent on capital expenditures during the six months ended June 30, 2010, approximately \$2 million was related to our data center transition efforts. The remaining expenditures consisted principally of investments in: (i) computer hardware, software, and related equipment; and to a lesser degree, (ii) statement production equipment.

The investments in client contracts for the first six months of 2010 and 2009 relate to client incentive payments (\$1.2 million and \$0.9 million, respectively) and the deferral of costs related to conversion/set-up services provided under long-term processing contracts (\$1.4 million and \$2.8 million, respectively).

---

## **Table of Contents**

### *Cash Flows From Financing Activities*

Our financing activities typically consist of activities with our common stock and our convertible debt.

*Repurchase of Common Stock.* During the first six months of 2010 and 2009 we repurchased 1.5 million shares and 250,000 shares of our common stock under the guidelines of our Stock Repurchase Program for \$29.3 million and \$3.8 million, respectively. In addition, outside of our Stock Repurchase Program, during the first six months of 2010 and 2009, we repurchased from our employees and then cancelled approximately 211,000 shares and 169,000 shares of our common stock for \$4.3 million and \$2.4 million, respectively, in connection with minimum tax withholding requirements resulting from the vesting of restricted common stock under our stock incentive plans.

*Long-term debt.* In March 2010, we completed an offering of our 2010 Convertible Notes, as discussed in greater detail in Note 6 to our Financial Statements. We used a portion of the \$145 million net proceeds from the offering to repurchase \$119.9 million (par value) of our 2004 Convertible Debt Securities for \$125.0 million. In connection with the issuance of the convertible notes, we incurred debt issuance costs of \$4.3 million.

### *Capital Resources*

The following are the key items to consider in assessing our sources and uses of capital resources:

#### *Current Sources of Capital Resources.*

Cash, Cash Equivalents and Short-term Investments. As of June 30, 2010, we had cash, cash equivalents, and short-term investments of \$229.7 million.

Operating Cash Flows. As described in the Liquidity section above, we believe we have the ability to consistently generate strong cash flows to fund our operating activities.

*Uses of Capital Resources.* Below are the key items to consider in assessing our uses of capital resources:

Common Stock Repurchases. We have made significant repurchases of our common stock in the past. During the first quarter of 2010, and in conjunction with the issuance of our 2010 Convertible Notes, we repurchased 1.5 million shares of our common stock for \$29.3 million (\$19.56 per share). In the second quarter of 2010, we did not repurchase any of our common stock. As of June 30, 2010, we have 4.2 million shares authorized for repurchase remaining under our Stock Repurchase Program. We continue to evaluate the best use of our capital going forward, which from time-to-time, may include additional share repurchases as market and business conditions warrant.

Acquisitions. We have made five acquisitions in the last five years, which had a total aggregate cash purchase price of approximately \$150 million. Besides the cash paid at the date the acquisition closes, some acquisitions may include the payment of additional cash related to contingent purchase price payments. During the first six months of 2010, we made contingent purchase price payments of \$2.8 million, of which \$2.3 million we had accrued as of December 31, 2009. As of June 30, 2010, we have accrued \$0.5 million for contingent purchase price payments related to the achievement of product integration milestones in the second quarter of 2010, with payment to be made in the third quarter of 2010. In addition, in the future, we could potentially be paying up to \$1.0 million in contingent purchase price payments related to 2010 in connection with the Quaero acquisition.

Capital Expenditures. In the six months ended June 30, 2010, we spent \$7.5 million on capital expenditures, with \$2.0 million related to the data center transition to Infocrossing. At this time, we expect our total 2010 capital expenditures to be approximately \$16 million, with approximately \$2 million related to the data center transition to Infocrossing. The remainder of our expected capital expenditures will consist principally of hardware and software infrastructure to support our clients' expanding business needs, and



statement production equipment to continue to offer enhanced functionalities to our clients.

## **Table of Contents**

**Investments in Client Contracts.** In the past, we have provided incentives to new or existing clients to convert their customer accounts to, or retain their customer's accounts on, our customer care and billing solutions. During the six months ended June 30, 2010, we made client incentive payments of \$1.2 million. In addition, during the six months ended June 30, 2010, we capitalized costs related to the deferral of conversion/set-up services revenue of \$1.4 million. As of June 30, 2010, we have made commitments for investments in client contracts which are payable by us only upon the successful conversion of certain additional customer accounts to our processing solutions.

**Long-Term Debt.** As of June 30, 2010, our long-term debt consisted of our 2004 Convertible Debt Securities with a par value of \$50.4 million and our 2010 Convertible Notes with a par value of \$150.0 million.

During 2009 and the first six months of 2010, we voluntarily repurchased a total of \$149.9 million (par value) of our 2004 Convertible Debt Securities for \$151.5 million. In July 2010, we voluntarily repurchased a total of \$23.2 million (par value) of our 2004 Convertible Debt Securities for \$23.9 million. As a result of these repurchases, beginning in 2014, we will have to pay cash of approximately \$30 million ratably over five years related to the deferred tax liabilities associated with the repurchased securities.

Our 2004 Convertible Debt Securities are callable by us for cash on or after June 20, 2011, at a redemption price equal to 100% of par value, plus accrued interest. Our 2004 Convertible Debt Securities can be put back to us by the holders for cash at June 15, 2011, at a redemption price equal to 100% of par value, plus accrued interest. After taking into consideration our voluntary repurchase of our 2004 Convertible Debt Securities in July 2010, our debt service cash outlay related to the 2004 Convertible Debt Securities during the next twelve months could equal the remaining par value of \$27.2 million, plus interest payments of \$0.7 million. In addition, if the remaining 2004 Convertible Debt Securities are put back to us on June 15, 2011, we will have to pay in cash during 2011 approximately \$7 million of deferred tax liabilities associated with the outstanding securities.

We will continue to evaluate our 2004 Convertible Debt Securities for possible future buying opportunities.

Refer to Note 6 to our Financial Statements for details of the conversion triggers of our 2010 Convertible Notes. During the next twelve months, there are no scheduled conversion triggers. As a result, during the next twelve months and based upon the June 30, 2010 par value, we expect our required debt service cash outlay related to the 2010 Convertible Notes to be limited to interest payments of \$4.5 million.

In summary, we expect to continue to make material investments in client contracts, capital equipment, and R&D. We expect to continue to evaluate the possibility of 2004 Convertible Debt Securities and equity repurchases in the future. In addition, as part of our growth strategy, we are continually evaluating potential business and/or asset acquisitions, and investments in market share expansion with our existing and potential new clients. We believe that our current cash and short-term investments balance, together with cash expected to be generated from future operating activities, will be sufficient to meet our anticipated cash requirements for at least the next 12 months. We also believe we could obtain additional capital through other debt sources which may be available to us if deemed appropriate.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Market risk is the potential loss arising from adverse changes in market rates and prices. As of June 30, 2010, we are exposed to market risks related to fluctuations and changes in the market value of our cash equivalents and short-term investments. We have not historically entered into derivatives or other financial instruments for trading or speculative purposes.

**Table of Contents**

*Market Risk Related to Long-Term Debt.* The interest rate on our 2004 Convertible Debt Securities and 2010 Convertible Notes are fixed, and thus, as it relates to our long-term debt, we are not exposed to changes in interest rates.

*Market Risk Related to Cash Equivalents and Short-term Investments.* Our cash and cash equivalents as of June 30, 2010 and December 31, 2009 were \$182.7 million and \$163.5 million, respectively. Our cash balances are typically swept into overnight money market accounts on a daily basis, and at times, any excess funds are invested in low-risk, somewhat longer term, cash equivalent instruments and short-term investments. We have minimal market risk for our cash and cash equivalents due to the relatively short maturities of the instruments.

Our short-term investments as of June 30, 2010 and December 31, 2009 were \$47.0 million and \$34.9 million, respectively. The day-to-day management of our cash equivalents and short-term investments is performed by a large financial institution in the U.S., using strict and formal investment guidelines approved by our Board of Directors. Under these guidelines, short-term investments are limited to certain acceptable investments with: (i) a maximum maturity, (ii) a maximum concentration and diversification; and (iii) a minimum acceptable credit quality. At this time, we believe we have minimal market risk associated with the short-term investments included in our portfolio.

We do not utilize any derivative financial instruments for purposes of managing our market risks related to interest rate risk.

**Item 4. Controls and Procedures**

***(a) Disclosure Controls and Procedures***

As required by Rule 13a-15(b), our management, including the Chief Executive Officer ( CEO ) and Chief Financial Officer ( CFO ), conducted an evaluation as of the end of the period covered by this report of the effectiveness of our disclosure controls and procedures as defined in Rule 13a-15(e). Based on that evaluation, the CEO and CFO concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

***(b) Internal Control Over Financial Reporting***

As required by Rule 13a-15(d), our management, including the CEO and CFO, also conducted an evaluation of our internal control over financial reporting, as defined by Rule 13a-15(f), to determine whether any changes occurred during the quarter covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Based on that evaluation, the CEO and CFO concluded that there has been no such change during the quarter covered by this report.

---

**Table of Contents**

**CSG SYSTEMS INTERNATIONAL, INC.**

**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

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

**Item 1A. Risk Factors**

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

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

***We Derive a Significant Portion of Our Revenues From a Limited Number of Clients, and the Loss of the Business of a Significant Client Could Have a Material Adverse Effect on Our Financial Condition and Results of Operations.***

Over the past decade, the North American communications industry has experienced significant consolidation, resulting in a large percentage of the market being served by a limited number of service providers with greater size and scale. Consistent with this market concentration, approximately two-thirds of our revenues are generated from our four largest clients, which are (in order of size) Comcast, DISH, Time Warner, and Charter. See the Significant Client Relationships section of MD&A in our 2009 10-K for key renewal dates and a brief summary of our business relationship with these clients.

There are inherent risks whenever a large percentage of total revenues are concentrated with a limited number of clients. One such risk is that a significant client could: (i) undergo a formalized process to evaluate alternative providers for services we provide; (ii) terminate or fail to renew their contracts with us, in whole or in part for any reason; (iii) significantly reduce the number of customer accounts processed on our solutions, the price paid for our services, or the scope of services that we provide; or (iv) experience significant financial or operating difficulties. Any such development could have a material adverse effect on our financial condition and results of operations and/or trading price of our common stock.

Our industry is highly competitive, and while we recently have succeeded in gaining customers at the expense of competitors, there is no guarantee that this success will continue. It is possible that a competitor could increase its footprint and share of customers processed at our expense or a provider could develop their own internal solutions. While our clients may incur some costs in switching to our competitors or their own internally-developed solutions, they may do so for a variety of reasons, including: (i) price; (ii) if we do not provide satisfactory solutions; or (iii) if we do not maintain favorable relationships.

---

**Table of Contents**

***The Delivery of Our Solutions is Dependent on a Variety of Computing Environments and Communications Networks Which May Not Be Available or May Be Subject to Security Attacks.***

Our solutions are generally delivered through a variety of computing environments operated by us, which we will collectively refer to herein as Systems. We provide such computing environments through both outsourced arrangements, such as our current data processing arrangements with FDC and Infocrossing, as well as internally operating numerous distributed servers in geographically dispersed environments. The end users are connected to our Systems through a variety of public and private communications networks, which we will collectively refer to herein as Networks. Our solutions are generally considered to be mission critical customer management systems by our clients. As a result, our clients are highly dependent upon the high availability and uncompromised security of our Networks and Systems to conduct their business operations.

Our Networks and Systems are subject to the risk of an extended interruption or outage due to many factors such as: (i) planned changes to our Systems and Networks for such things as scheduled maintenance and technology upgrades, or migrations to other technologies, service providers, or physical location of hardware; (ii) human and machine error; (iii) acts of nature; and (iv) intentional, unauthorized attacks from computer hackers. As noted above, we began the transition of our data center services currently provided by FDC to Infocrossing during 2009, and expect to complete the transition of such services in the second half of 2010. Because of the magnitude of the Systems and Networks that will be impacted by this transition, the above risks of an extended interruption or outage will be significantly heightened during the transition period.

In addition, we continue to expand our use of the Internet with our product offerings thereby permitting, for example, our clients' customers to use the Internet to review account balances, order services or execute similar account management functions. Allowing access to our Networks and Systems via the Internet has the potential to increase their vulnerability to unauthorized access and corruption, as well as increasing the dependency of our Systems' reliability on the availability and performance of the Internet and end users' infrastructure they obtain through other third party providers.

The method, manner, cause and timing of an extended interruption or outage in our Networks or Systems are impossible to predict. As a result, there can be no assurances that our Networks and Systems will not fail, or that our business continuity plans will adequately mitigate the negative effects of a disruption to our Networks or Systems. Further, our property and business interruption insurance may not adequately compensate us for losses that we incur as a result of such interruptions. Should our Networks or Systems: (i) experience an extended interruption or outage, (ii) have their security breached, or (iii) have their data lost, corrupted or otherwise compromised, it would impede our ability to meet product and service delivery obligations, and likely have an immediate impact to the business operations of our clients. This would most likely result in an immediate loss to us of revenue or increase in expense, as well as damaging our reputation. An information breach in our Systems or Networks and loss of confidential information such as credit card numbers and related information could have a longer and more significant impact on our business operations than a hardware-related failure. The loss of confidential information could result in losing the customers' confidence, as well as imposition of fines and damages. Any of these events could have both an immediate, negative impact upon our financial condition and our short-term revenue and profit expectations, as well as our long-term ability to attract and retain new clients.

***The Occurrence or Perception of a Security Breach or Disclosure of Confidential Personally Identifiable Information Could Harm Our Business.***

In providing solutions to our customers, we process, transmit, and store confidential and personally identifiable information, including social security numbers and financial and health information. Our treatment of such information is subject to contractual restrictions and federal, state, and foreign data privacy laws and regulations. While we take measures to protect against unauthorized access to such information and comply with these laws and regulations, these measures may be inadequate, and any failure on our part to protect the privacy of personally identifiable information or comply with data privacy laws and regulations may subject us to contractual liability and damages, loss of business, damages from individual claimants, fines, penalties, criminal prosecution, and unfavorable publicity. Even the mere perception of a security breach or inadvertent disclosure of personally identifiable information could inhibit market acceptance of our solutions. In addition, third party vendors that we engage to perform services for us may unintentionally release personally identifiable information or otherwise fail to comply with applicable laws and regulations. The occurrence of any of these events could have an adverse effect on our business, financial condition, and results of operations.

## **Table of Contents**

### ***We May Not Be Able to Respond to Rapid Technological Changes.***

The market for customer interaction management solutions, such as customer care and billing solutions, is characterized by rapid changes in technology and is highly competitive with respect to the need for timely product innovations and new product introductions. As a result, we believe that our future success in sustaining and growing our revenues depends upon: (i) our ability to continuously adapt, modify, maintain, and operate our solutions to address the increasingly complex and evolving needs of our clients, without sacrificing the reliability or quality of the solutions; and (ii) the integration of our recently acquired technologies such as interactive messaging and customer intelligence with ACP, as well as creating an integrated suite of customer interaction management solutions that also include e-care and printing/ mailing capabilities, which are portable to new verticals such as utilities, healthcare, home security, financial services, and content distribution. In addition, the market is demanding that our solutions have greater architectural flexibility and interoperability, and that we are able to meet the demands for technological advancements to our solutions at a greater pace. Attempts to meet these demands subjects our R&D efforts to greater risks.

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

There is an inherent risk in the successful development, implementation, migration, and operations of our solutions as the technological complexities, and the pace at which we must deliver these solutions to market, continue to increase. The risk of making an error that causes significant operational disruption to a client, or results in incorrect customer or vendor billing calculations we perform on behalf of our clients, increases proportionately with the frequency and complexity of changes to our solutions. There can be no assurance: (i) of continued market acceptance of our solutions; (ii) that we will be successful in the development of enhancements or new solutions that respond to technological advances or changing client needs at the pace the market demands; or (iii) that we will be successful in supporting the implementation, migration and/or operations of enhancements or new solutions.

### ***Our Use of Open Source Software May Subject Us to Certain Intellectual Property-Related Claims or Require Us to Re-Engineer Our Software, Which Could Harm Our Business.***

We use open source software in connection with our solutions, processes, and technology. Companies that use or incorporate open source software into their products have, from time to time, faced claims challenging their use, ownership and/or licensing rights associated with that open source software. As a result, we could be subject to suits by parties claiming certain rights to what we believe to be open source software. Some open source software licenses require users who distribute open source software as part of their software to publicly disclose all or part of the source code in their software and make any derivative works of the open source code available on unfavorable terms or at no cost. In addition to risks related to license requirements, use of open source software can lead to greater risks than use of third party commercial software, as open source licensors generally do not provide warranties or controls with respect to origin of the software. While we take measures to protect our use of open source software in our solutions, open source license terms may be ambiguous, and many of the risks associated with usage of open source software cannot be eliminated. If we were found to have inappropriately used open source software, we may be required to release our proprietary source code, re-engineer our software, discontinue the sale of certain solutions in the event re-engineering cannot be accomplished on a timely basis, or take other remedial action that may divert resources away from our development efforts, any of which could adversely affect our business, financial condition, and results of operations.

## **Table of Contents**

### ***The Current Macroeconomic Environment Could Adversely Impact Our Business.***

Over the past few years, the U.S. has experienced a significant economic downturn and difficulties within the financial and credit markets. The timing, duration, and degree of an economic turnaround are uncertain and thus, these adverse economic conditions may continue into the foreseeable future. The possible adverse impacts to companies during these times include a reduction in revenues, decreasing profits and cash flows, distressed or default debt conditions, and/or difficulties in obtaining necessary operating capital. All companies are likely to be impacted by the current economic downturn to a certain degree, including CSG, our clients, and/or key vendors in our supply chain. There can be no assurances regarding the performance of our business, and the potential impact to our clients and key vendors, resulting from the current economic conditions.

### ***A Reduction in Demand for Our Key Customer Care and Billing Solutions Could Have a Material Adverse Effect on Our Financial Condition and Results of Operations.***

Historically, a substantial percentage of our total revenues have been generated from our core outsourced processing product, ACP, and related solutions. These solutions are expected to continue to provide a large percentage of our total revenues in the foreseeable future. Any significant reduction in demand for ACP and related solutions could have a material adverse effect on our financial condition and results of operations.

### ***We May Not Be Able to Efficiently and Effectively Implement New Solutions or Convert Clients onto Our Solutions.***

Our continued growth plans include the implementation of new solutions, as well as converting both new and existing clients to our solutions. Such implementations or conversions, whether they involve new solutions or new customers, have become increasingly more difficult because of the sophistication, complexity and interdependencies of the various computing and network environments impacted, combined with the increasing complexity of the underlying business processes. For these reasons, there is a risk that we may experience delays or unexpected costs associated with a particular implementation or conversion, and our inability to complete implementation or conversion projects in an efficient and effective manner could have a material adverse effect on our results of operations.

### ***Our Business is Highly Dependent on the North American Cable and DBS Industries.***

We have historically generated a significant portion of our revenues by providing solutions to clients in the North American cable and DBS industries. A decrease in the number of customers served by our clients, an adverse change in the economic condition of these industries, and/or changing consumer demand for services could have a material adverse effect on our results of operations. Additionally, a significant portion of our historical growth has come from our support of clients' expansion into new lines of business, such as HSD and VoIP. There can be no assurance that our current and potential clients will be successful in expanding into new segments of the converging North American communications industry. Even if major forays into new markets by our current or potential clients are successful, we may be unable to meet the special billing and customer interaction management needs of those markets.

Our clients operate in a highly competitive environment. Traditional wireline and wireless telephone service providers, and others, will continue their aggressive pursuit of providing convergent services, including residential video, a market historically dominated by our clients. In addition, content disintermediaries like Hulu, YouTube, and FloTV are trying to capture consumer attention by providing content on different devices over different networks. Should these alternative service providers be successful in their video strategies, it could threaten our clients' market share, and thus our source of revenues, as generally speaking these companies do not use our core solutions and there can be no assurance that new entrants will become our clients.

## **Table of Contents**

### ***Further Consolidation of the North American Cable and DBS Industries May Have a Material Adverse Effect on Our Results of Operations.***

The North American cable and DBS industries may continue to be subject to significant ownership changes. One facet of these changes is that consolidation by and among our core client base, the cable and DBS providers, as well as new entrants such as the traditional wireline and wireless carriers, will decrease the potential number of buyers for our solutions. Should these consolidations result in a concentration of customer accounts being owned by companies with whom we do not have a relationship, or with whom competitors are entrenched, we could be subject to the risk that subscribers will be moved off of our solutions and onto a competitor's system, thereby having a material adverse effect on our results of operations. Furthermore, movement of our clients' customers from our solutions to a competitor's system or an internally-developed solution as a result of regionalization strategies by our clients could have a material adverse effect on our operations. Finally, as the result of the consolidations, our current and potential clients may choose to use their size and scale to exercise more severe pressure on pricing negotiations.

### ***We Face Significant Competition in Our Industry.***

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

### ***Client Bankruptcies Could Adversely Affect Our Business.***

In the past, certain of our clients have filed for bankruptcy protection. As a result of the current economic conditions and the additional financial stress this may place on companies, the risk of client bankruptcies is significantly heightened. Companies involved in bankruptcy proceedings pose greater financial risks to us, consisting principally of the following: (i) a financial loss related to possible claims of preferential payments for certain amounts paid to us prior to the bankruptcy filing date, as well as increased collectibility risk for accounts receivable, particularly those accounts receivable that relate to periods prior to the bankruptcy filing date; and/or (ii) the possibility of a contract being unilaterally rejected as part of the bankruptcy proceedings, or a client in bankruptcy may attempt to renegotiate more favorable terms as a result of their deteriorated financial condition, thus, negatively impacting our rights to future revenues subsequent to the bankruptcy filing. We consider these risks in assessing our revenue recognition and the collectibility of accounts receivable related to our clients that have filed for bankruptcy protection, and for those clients that are seriously threatened with a possible bankruptcy filing. We establish accounting reserves for our estimated exposure on these items which can materially impact the results of our operations in the period such reserves are established. There can be no assurance that our accounting reserves related to this exposure will be adequate. Should any of the factors considered in determining the adequacy of the overall reserves change adversely, an adjustment to the accounting reserves may be necessary. Because of the potential significance of this exposure, such an adjustment could be material.

### ***We May Incur Material Restructuring Charges in the Future.***

In the past, we have recorded restructuring charges related to involuntary employee terminations, various facility abandonments, and various other restructuring activities. We continually evaluate ways to reduce our operating expenses through new restructuring opportunities, including more effective utilization of our assets, workforce and operating facilities. As a result, there is a risk, which is inherently greater during economic downturns, that we may incur material restructuring charges in the future.



## **Table of Contents**

### ***Failure to Attract and Retain Our Key Management and Other Highly Skilled Personnel Could Have a Material Adverse Effect on Our Business.***

Our future success depends in large part on the continued service of our key management, sales, product development, and operational personnel. We believe that our future success also depends on our ability to attract and retain highly skilled technical, managerial, operational, and marketing personnel, including, in particular, personnel in the areas of R&D and technical support. Competition for qualified personnel at times can be intense, particularly in the areas of R&D, conversions, software implementations, and technical support. For these reasons, we may not be successful in attracting and retaining the personnel we require, which could have a material adverse effect on our ability to meet our commitments and new product delivery objectives.

### ***We May Not Be Successful in the Integration of Our Acquisitions.***

As part of our growth strategy, we seek to acquire assets, technology, and businesses which will provide the technology and technical personnel to expedite our product development efforts, provide complementary solutions, or provide access to new markets and clients.

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

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

### ***Failure to Protect Our Intellectual Property Rights or Claims by Others That We Infringe Their Intellectual Property Rights Could Substantially Harm Our Business, Financial Condition and Results of Operations.***

We rely on a combination of trade secret, copyright, trademark, and patent laws in the United States and similar laws in other countries, and non-disclosure, confidentiality, and other types of contractual arrangements to establish, maintain, and enforce our intellectual property rights in our solutions. Despite these measures, any of our intellectual property rights could be challenged, invalidated, circumvented, or misappropriated. Further, our contractual arrangements may not effectively prevent disclosure of our confidential information or provide an adequate remedy in the event of unauthorized disclosure of our confidential information. Others may independently discover trade secrets and proprietary information, and in such cases we could not assert any trade secret rights against such parties. Costly and time consuming litigation could be necessary to enforce and determine the scope of our proprietary rights, and failure to obtain or maintain trade secret protection could adversely affect our competitive business position. In addition, the laws of certain countries do not protect proprietary rights to the same extent as the laws of the United States. Therefore, in certain jurisdictions, we may be unable to protect our proprietary technology adequately against unauthorized third party copying or use, which could adversely affect our competitive position.

Although we hold a limited number of patents and patent applications on some of our newer solutions, we do not rely upon patents as a primary means of protecting our rights in our intellectual property. In any event, there can be no assurance that our patent applications will be approved, that any issued patents will adequately protect our intellectual property, or that such patents will not be challenged by third parties. Also, much of our business and many of our solutions rely on key technologies developed or licensed by third parties, and we may not be able to obtain or continue to obtain licenses and technologies from these third parties at all or on reasonable terms.

Finally, third parties may claim that we, our customers, licensees or other parties indemnified by us are infringing upon their intellectual property rights. Even if we believe that such claims are without merit, they can be time consuming and costly to defend and distract management's and technical staff's attention and resources. Claims of intellectual property infringement also might require us to redesign affected solutions, enter into costly settlement or

**Table of Contents**

license agreements or pay costly damage awards, or face a temporary or permanent injunction prohibiting us from marketing or selling certain of our solutions. Even if we have an agreement to indemnify us against such costs, the indemnifying party may be unable to uphold its contractual obligations. If we cannot or do not license the infringed technology on reasonable pricing terms or at all, or substitute similar technology from another source, our business, financial condition, and results of operations could be adversely impacted.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table presents information with respect to purchases of company common stock made during the second quarter of 2010 by CSG Systems International, Inc. or any affiliated purchaser of CSG Systems International, Inc., as defined in Rule 10b-18(a)(3) under the Exchange Act.

Period		Total Number of Shares Purchased <sup>1</sup>	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plan or Programs
April 1	April 30	1,894	\$ 21.89		4,204,096
May 1	May 31	2,331	21.96		4,204,096
June 1	June 30	2,543	18.68		4,204,096
Total		6,768	\$ 20.71		

<sup>1</sup> The total number of shares purchased that are not part of the Stock Repurchase Program represents shares purchased and cancelled in connection with stock incentive plans.

**Item 3. Defaults Upon Senior Securities**

None

**Item 4. (Removed and Reserved)**

None

**Item 5. Other Information**

None

**Item 6. Exhibits**

The Exhibits filed or incorporated by reference herewith are as specified in the Exhibit Index.



**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.

Dated: August 6, 2010

CSG SYSTEMS INTERNATIONAL, INC.

/s/ PETER E. KALAN  
**Peter E. Kalan**  
**Chief Executive Officer and President**

**(Principal Executive Officer)**

/s/ RANDY R. WIESE  
**Randy R. Wiese**  
**Executive Vice President, Chief Financial Officer, and**

**Chief Accounting Officer**  
**(Principal Financial Officer and Principal Accounting Officer)**

**Table of Contents**

**CSG SYSTEMS INTERNATIONAL, INC.**

**INDEX TO EXHIBITS**

<b>Exhibit Description</b>	<b>Number</b>
10.52(1)	Employment Agreement with Michael J. Henderson, dated July 1, 2010
31.01	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.02	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.01	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(1) Incorporated by reference to the exhibit of the same number to the Registrant's Current Report on Form 8-K for the event dated July 13, 2010.