

Edgar Filing: VERTRUE INC - Form 10-Q

VERTRUE INC
Form 10-Q
February 09, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

X Quarterly report pursuant to Section 13 or 15(d) of the Securities
----- Exchange Act of 1934 for the quarterly period ended December 31, 2005
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 No. 0-21527

VERTRUE INCORPORATED

(Exact name of registrant as specified in its charter)

DELAWARE

(State of Incorporation)

06-1276882

(IRS Employer
Identification No.)

680 Washington Boulevard
Stamford, Connecticut

(Address of principal executive offices)

06901

(Zip Code)

(203) 324-7635

(Registrant's telephone number,
including area code)

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

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

Large accelerated filer [] Accelerated filer [X] Non-accelerated filer []

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 9,671,000 shares of Common Stock, \$0.01 par value as of January 27, 2006.

Edgar Filing: VERTRUE INC - Form 10-Q

VERTRUE INCORPORATED INDEX TO FORM 10-Q

PART I.	FINANCIAL INFORMATION	PAGE
Item 1.	Condensed Financial Statements (Unaudited)	
	Consolidated Balance Sheets as of December 31, 2005 and June 30, 2005	1
	Consolidated Statements of Operations for the Three and Six Months Ended December 31, 2005 and 2004	2
	Consolidated Statements of Cash Flows for the Six Months Ended December 31, 2005 and 2004	3
	Notes to Condensed Consolidated Financial Statements	4
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	19
	Forward-Looking Statements	27
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	29
Item 4.	Controls and Procedures	29
PART II.	OTHER INFORMATION	
Item 1.	Legal Proceedings	31
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	31
Item 4.	Submission of Matters to a Vote of Security Holders	31
Item 6.	Exhibits	32
	Signatures	33

VERTRUE INCORPORATED ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)

CONSOLIDATED BALANCE SHEETS (in thousands, except per share amounts)

December 31,
2005

Assets

Current assets:

Edgar Filing: VERTRUE INC - Form 10-Q

Cash and cash equivalents	\$ 54,576
Restricted cash	3,857
Short-term investments	17,217
Accounts receivable	16,930
Prepaid membership materials	3,499
Prepaid expenses and other current assets	11,200
Deferred marketing costs	33,359

Total current assets	140,638
Fixed assets, net	37,603
Goodwill	212,859
Intangible assets, net	41,829
Other assets	13,496

Total assets	\$ 446,425
	=====
Liabilities and Shareholders' Deficit	
Current liabilities:	
Current maturities of long-term obligations	\$ 746
Accounts payable	37,705
Accrued liabilities	75,114
Deferred revenues	97,736
Deferred income taxes	11,527

Total current liabilities	222,828
Deferred income taxes	9,465
Other long-term liabilities	6,009
Long-term debt	237,897

Total liabilities	476,199

Commitments and contingencies	-
Shareholders' deficit:	
Preferred stock, \$0.01 par value -- 1,000 shares authorized; no shares issued	-
Common stock, \$0.01 par value -- 40,000 shares authorized; 19,834 shares issued (19,703 shares at June 30, 2005)	198
Capital in excess of par value	177,281
Retained earnings	51,985
Accumulated other comprehensive income (loss)	377
Treasury stock, 10,185 shares at cost (10,020 shares at June 30, 2005)	(259,615)

Total shareholders' deficit	(29,774)

Total liabilities and shareholders' deficit	\$ 446,425
	=====

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

Edgar Filing: VERTRUE INC - Form 10-Q

(in thousands, except per share amounts)

	Three months ended December 31,		Si
	2005	2004	
Revenues	\$ 160,130	\$ 136,479	\$ 317
Expenses:			
Marketing	76,270	68,689	150
Operating	35,258	25,952	70
General and administrative	29,527	26,302	57
Amortization of intangibles	2,197	1,753	4
Operating income	16,878	13,783	34
Interest expense, net	(4,387)	(4,611)	(8)
Other (expense) income, net	(120)	428	
Income before income taxes	12,371	9,600	25
Provision for income taxes	4,707	3,717	9
Net income	\$ 7,664	\$ 5,883	\$ 16
Earnings per share:			
Basic	\$ 0.79	\$ 0.58	\$
Diluted	\$ 0.66	\$ 0.51	\$
Weighted average common shares used in earnings per share calculations:			
Basic	9,695	10,128	9
Diluted	12,776	13,063	12

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

2

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

Six months ended December 31,	
2005	2004

Edgar Filing: VERTRUE INC - Form 10-Q

	-----	-----
Operating activities		
Net income	\$ 16,305	\$ 13,479
Adjustments to reconcile net income to net cash provided by operating activities:		
Change in deferred revenues	(10,611)	(19,369)
Change in deferred marketing costs	5,971	8,685
Depreciation and amortization	13,025	10,422
Stock-based compensation	2,250	-
Deferred income taxes	1,521	3,197
Excess tax benefit from stock-based compensation	(560)	939
Other	(243)	422
 Change in assets and liabilities:		
Restricted cash	(446)	283
Accounts receivable	(4,371)	(3,939)
Prepaid membership materials	(942)	(1,150)
Prepaid expenses	(1,138)	(2,247)
Other assets	(1,948)	(19)
Accounts payable	(4,372)	834
Accrued and other liabilities	375	3,089
 Net cash provided by operating activities	----- 14,816	----- 14,626
 Investing activities		
Acquisition of fixed assets	(6,518)	(4,339)
Purchases of short-term investments	(50,325)	(368,533)
Sales of short-term investments	49,830	425,912
Acquisitions of businesses, net of cash acquired	(14,942)	(16,097)
 Net cash (used in) provided by investing activities	----- (21,955)	----- 36,943
 Financing activities		
Net proceeds from issuance of stock	2,729	6,237
Excess tax benefit from stock-based compensation	560	-
Treasury stock purchases	(5,995)	(8,396)
Debt issuance costs	-	(750)
Payments of long-term obligations	(392)	(204)
 Net cash used in financing activities	----- (3,098)	----- (3,113)
 Effect of exchange rate changes on cash and cash equivalents	----- 457	----- 235
 Net (decrease) increase in cash and cash equivalents	(9,780)	48,691
Cash and cash equivalents at beginning of year	64,356	47,166
 Cash and cash equivalents at end of period	----- \$ 54,576	----- \$ 95,857
	=====	=====

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

Edgar Filing: VERTRUE INC - Form 10-Q

NOTE 1 - NATURE OF BUSINESS

Vertrue Incorporated ("Vertrue" or the "Company") is a leading internet marketing services company. The Company gives consumers access to both subscription and transaction based services focused on meeting consumer needs in large spending categories - healthcare, personal property, discounts, security and insurance and personals. The Company's service offerings provide consumers everyday savings, event-oriented discounts, benefits that provide the consumer with peace of mind and access to information and opportunities for self-enrichment.

NOTE 2 - BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and include the accounts of the Company, its wholly owned subsidiaries and variable interest entities required to be consolidated. All significant intercompany accounts and transactions have been eliminated. Such statements do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair statement have been included. The preparation of these consolidated financial statements in conformity with generally accepted accounting principles requires management of the Company to make estimates, judgments and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Operating results for the three and six months ended December 31, 2005 are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2006. For further information, refer to the financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2005.

The Company acquired Bargain Network, Inc. ("Bargain") on November 30, 2004 and My Choice Medical Holdings, Inc. ("MCM") on January 1, 2005. Therefore, their results of operations have been included in the consolidated results of operations since their acquisition dates. The results of Bargain have been included in the Marketing Services segment and the results of MCM have been included in the Management Services segment.

NOTE 3 - RECLASSIFICATIONS

Certain prior year amounts have been reclassified to conform to the current year's presentation to reclassify auction rate securities from cash and cash equivalents to short-term investments. Corresponding adjustments have been made in the consolidated statements of cash flows for prior periods to reflect gross purchases and sales of auction rate securities as investing activities rather than as a component of cash and cash equivalents. The Company reclassified \$112,330,000 and \$55,215,000 from cash and cash equivalents to short-term investments at June 30, 2004 and December 31, 2004, respectively. These reclassifications do not affect previously reported cash flows from operating or financing activities in the consolidated statements of cash flows. For the six months ended December 31, 2004, net cash provided by investing activities related to auction rate securities was \$57,115,000.

NOTE 4 - STOCK-BASED COMPENSATION

The Company adopted Financial Accounting Standards Board Statement ("SFAS") No. 123(R), "Share-Based Payment" ("SFAS 123R") on July 1, 2005. SFAS 123R establishes the accounting for share-based compensation and requires companies to measure and recognize compensation expense for all share-based payments at fair value. Accordingly, share-based compensation cost is measured at grant date based on the fair value of the award and is recognized as expense over the requisite service period. The Company adopted the modified prospective application method as permitted by SFAS 123R.

Edgar Filing: VERTRUE INC - Form 10-Q

VERTRUE INCORPORATED
 ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Prior to the adoption of SFAS 123R, the Company accounted for its share-based employee compensation plans under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and the related interpretations. If compensation cost for the Company's stock-based compensation plans had been determined based on the fair value method (estimated using the Black-Scholes option pricing model) at the grant dates in accordance with SFAS No. 123, "Accounting for Stock-Based Compensation," ("SFAS 123"), the Company's pro forma net income and earnings per share would have been as follows for the three and six months ended December 31, 2004 (in thousands, except per share data):

	Three months ended December 31, 2004	Six months ended December 31, 2004
Net income reported	\$ 5,883	\$
Add: Stock-based employee compensation expense under the intrinsic value method, net of related tax effects	-	
Deduct: Stock-based employee compensation expense under the fair value method, net of related tax effects (1)	961	
Pro forma net income	\$ 4,922	\$
Earnings per share:		
As reported		
Basic	\$ 0.58	\$
Diluted	\$ 0.51	\$
Pro forma		
Basic	\$ 0.49	\$
Diluted	\$ 0.43	\$

(1) Compensation expense was reduced for forfeitures as they occurred.

The Company evaluated its valuation method and assumptions in connection with SFAS 123R. The Company determined that the use of the Black-Scholes option-pricing model was appropriate and is consistent with the Company's pro forma disclosures under the fair value recognition provisions of SFAS 123. The Company believes it has used appropriate assumptions in accordance with SFAS 123R to estimate the fair value of its stock options and its employee stock purchase plan during the three and six months ended December 31, 2005. The following weighted average assumptions were used to estimate the fair value of options granted:

	Three months ended December 31,		Six months ended December 31,	
	2005 (4)	2004	2005	2004
Black-Scholes Option Valuation Assumptions				

Edgar Filing: VERTRUE INC - Form 10-Q

Dividend yield	NA	0.0%	0.0%	0.0%
Expected volatility (1)	NA	62%	65%	68%
Risk free interest rate (2)	NA	3.4%	3.8%	3.7%
Expected lives (in years) (3)	NA	5.0	5.6	5.0

- (1) Estimated based on historical experience.
 (2) Based on the U.S. Treasury constant maturity interest rate with a term consistent with the expected life of the options granted.
 (3) Estimated based on historical experience and expected future results.
 (4) No options were granted during the quarter ended December 31, 2005.

The weighted average fair value of options granted during the six months ended December 31, 2005 estimated on the grant date using the Black-Scholes option-pricing model with the assumptions listed above was \$21.13. The weighted average fair values of options granted during the three and six months ended December 31, 2004 estimated on the grant date using the Black-Scholes option-pricing model with the assumptions listed above were \$17.57 and \$17.59, respectively.

For the three and six months ended December 31, 2005, the Company recognized \$1,144,000 (\$709,000 net of tax) and \$2,250,000 (\$1,437,000 net of tax), respectively, in general and administrative expenses related to stock option compensation. As of December 31, 2005, unrecognized stock compensation expense related to unvested options was \$9,257,000, which is expected to be recognized over a weighted average period of 2.8 years.

5

VERTRUE INCORPORATED ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED) NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The total intrinsic value of options exercised during the three and six months ended December 31, 2005 was \$662,000 and \$2,119,000, respectively, and \$3,686,000 and \$4,547,000 during the three and six months ended December 31, 2004, respectively. The total cash received as a result of employee stock option exercises for the three and six months ended December 31, 2005 was \$1,109,000 and \$2,729,000, respectively, and \$5,318,000 and \$6,237,000 during the three and six months ended December 31, 2004, respectively. The tax benefits realized in connection with these exercises were \$209,000 and \$560,000 during the three and six months ended December 31, 2005, respectively, and \$810,000 and \$939,000 during the three and six months ended December 31, 2004, respectively.

As of December 31, 2005, the Company had the following stock-based compensation plans which are described below.

Under the 1996 Stock Option Plan, the Board of Directors can determine the date on which options vest and become exercisable as well as the term of the options granted. The 1996 Stock Option Plan is authorized to grant options to acquire 5,524,000 shares of Common Stock, of which, 1,924,000 must be issued using treasury stock.

Under the 1995 Executive Officers' Stock Option Plan and the 1995 Non-Employee Directors' Stock Option Plan, the Board is authorized to grant 360,000 and 180,000 options, respectively, to acquire shares of Common Stock at a price per share equal to or greater than fair market value at the grant date. Under the Executive Officers' Stock Option Plan, the Board can determine the date on which options vest and become exercisable.

Edgar Filing: VERTRUE INC - Form 10-Q

Under the stock option plans described above, options generally become exercisable over a four to five year period and expire at the earlier of termination of employment or ten years from the grant date.

In addition, the 2005 Equity Incentive Plan has 1,000,000 shares authorized, reserved and available for issuance. Awards granted may be in the form of stock options, restricted stock, restricted stock units, stock appreciation rights, performance stock and performance stock units. As of December 31, 2005, no awards have been made under this plan. The Board of Directors has the authority to determine the form, terms and conditions of awards at the time of grant, including vesting, exercisability, payment, and the effect, if any, that a participant's termination of service will have on an award.

As of December 31, 2005, 4,355,000 shares of common stock were reserved for issuance under these stock incentive plans, of which 1,482,000 shares were available for future grant.

Information with respect to options to purchase shares issued under the above plans is as follows (shares in thousands):

	Shares	Weighted Average Exercise Price
Outstanding at July 1, 2005	2,872	\$ 22.16
Granted	223	38.21
Exercised	(122)	20.22
Forfeited or expired	(100)	32.99
Outstanding at December 31, 2005	2,873	23.12

6

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following table summarizes the Company's stock options outstanding and exercisable as of December 31, 2005 (shares in thousands):

Exercise Price	Options Outstanding			Options Exercisable				
	Shares	Weighted Average Remaining Contractual Term (Yrs)	Weighted Average Exercise Price (\$)	Aggregate Intrinsic Value (\$)	Shares	Weighted Average Exercise Price (\$)	Aggregate Intrinsic Value (\$)	
\$4.167 - \$13.05	558	5.43	11.53	13,280	430	11.07	10,432	
\$14.00 - \$19.375	390	4.06	16.40	7,383	345	16.44	6,517	
\$20.31 - \$26.50	658	5.86	20.73	9,607	596	20.72	8,708	
\$29.00 - \$29.875	906	5.08	29.46	5,318	751	29.43	4,431	
\$31.249 - \$39.20	361	9.29	36.69	(491)	17	33.76	27	
	2,873	5.72	23.12	35,097	2,139	21.26	30,115	

Edgar Filing: VERTRUE INC - Form 10-Q

The weighted average remaining contractual term of stock options exercisable as of December 31, 2005 was 4.8 years.

NOTE 5 - GOODWILL AND OTHER INTANGIBLE ASSETS

The gross carrying value and accumulated amortization of goodwill and other intangibles are as follows (in thousands):

	December 31, 2005		Jun
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount
Amortizable intangible assets:			
Membership and client relationships	\$ 40,215	\$ 18,945	\$ 40,215
Trade names	21,859	2,388	21,859
Other	1,504	1,383	1,518
Total amortizable intangible assets	\$ 63,578	\$ 22,716	\$ 63,592
Amortizable intangible assets, net	\$ 40,862		\$ 45,509
Indefinite-lived intangible assets:			
Goodwill	\$ 212,859		\$ 201,499
Intangible asset related to minimum pension liability	\$ 967		\$ 967

Changes in the carrying amount of goodwill by segment were as follows (in thousands) during the six months ended:

	December 31, 2005			
	Marketing Services	Personals	Management Services	Total
Balance at beginning of period	\$ 95,917	\$ 82,215	\$ 23,367	\$ 201,499
Purchase adjustments and other	515	-	10,845	11,360
Balance at end of period	\$ 96,432	\$ 82,215	\$ 34,212	\$ 212,859

As required by SFAS 142, goodwill was tested for impairment during the quarters ended September 30, 2005 and 2004 using a July 1 measurement date. The Company concluded that none of its goodwill was impaired. Fair value was estimated using discounted cash flow methodologies. In addition, the Company reassessed the estimated useful lives of its definite lived intangible assets and determined that the lives were appropriate. The Company will continue to test the goodwill of each of its reporting units annually or more frequently if impairment indicators exist.

Edgar Filing: VERTRUE INC - Form 10-Q

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 - FOREIGN CURRENCY INSTRUMENTS

The Company uses purchase option contracts and forward contracts to minimize its exposure to changes in future cash flows caused by movements in foreign currency exchange rates between the U.S. dollar and the Canadian dollar. Derivatives are held only for the purpose of hedging such risks and are not used for speculative purposes. Derivatives used to hedge forecasted cash flows associated with Canadian dollar denominated forecasted transactions that meet the criteria for hedge accounting are designated as cash flow hedges. The effective portion of derivative gains and losses is deferred as a component of accumulated other comprehensive income and is recognized when the underlying hedged item is recognized in earnings.

The fair value of these contracts is included in prepaid and other current assets. As of December 31, 2005 and June 30, 2005, the fair value of these instruments was \$582,000 (asset) and \$559,000 (asset), respectively. Derivative gains recognized in earnings were recorded in operating expenses and general and administrative expenses and amounted to \$285,000 and \$413,000 for the three and six months ended December 31, 2005, respectively, and \$567,000 and \$611,000 for the three and six months ended December 31, 2004, respectively. All forecasted transactions currently being hedged are expected to occur over the remaining fiscal year.

NOTE 7 - ALLOWANCE FOR MEMBERSHIP CANCELLATIONS

Accrued liabilities reported in the accompanying unaudited condensed consolidated balance sheets as of December 31, 2005 and June 30, 2005 include an allowance for membership cancellations of \$12,256,000 and \$11,232,000, respectively.

NOTE 8 - COMMITMENTS AND CONTINGENCIES

The Company operates in leased facilities. Management expects that leases currently in effect will be renewed or replaced by other leases of a similar nature and term.

The Company has an amended and restated senior secured credit facility, which allows borrowings of up to \$45,000,000. Borrowings under the senior secured credit facility accrue interest at either the Eurodollar rate, or the higher of the Prime rate, or the Federal Funds rate plus an applicable margin. There were no borrowings outstanding under this bank credit facility as of December 31, 2005. The bank credit facility matures on March 23, 2006 and management expects it to be renewed or replaced during the third quarter of fiscal 2006.

Contingent payments related to the acquisition of MCM of up to \$56,000,000 may be paid if certain performance targets, including increasing levels of revenues and earnings, are achieved during the three calendar years ending December 31, 2007. As of December 31, 2005, the Company has recorded \$10,540,000 in accrued liabilities related to contingent payments expected to be paid during fiscal 2006.

As of December 31, 2005, the Company had outstanding purchase obligations of \$24,837,000 primarily related to marketing agreements and maintenance contracts on the Company's software, equipment and other assets. In addition, as of December 31, 2005, the Company had commitments of \$53,128,000 related to existing operating leases.

Legal proceedings

Edgar Filing: VERTRUE INC - Form 10-Q

Except as set forth below, in management's opinion, there are no significant legal proceedings to which the Company or any of its subsidiaries is a party or to which any of their properties is subject. The Company is involved in other lawsuits and claims generally incidental to its business, including, but not limited to, various suits, including previously disclosed suits, brought against the Company by individual consumers seeking monetary and/or injunctive relief relating to the marketing of the Company's programs. In addition, from time to time in the regular course of its business, the Company receives inquiries from various federal and/or state regulatory authorities.

On October 17, 2005, the U.S. Supreme Court declined to review the Connecticut Supreme Court's May 10, 2005 decision against the Company to uphold an arbitration panel's award of \$5,458,000 in punitive damages and costs to MedValUSA Health Programs, Inc. Accordingly, the Company paid the full amount of the award in the quarter ending December 31, 2005. The Company recorded a one-time \$5,458,000 charge in the quarter ended June 30, 2005 related to this award.

8

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 9 - INCOME TAX EXPENSE

Income tax expense as a percent of pre-tax income was 38.0% and 36.1% for the three and six months ended December 31, 2005, respectively, and 38.7% and 37.5% for the three and six months ended December 31, 2004, respectively. The effective tax rate was higher than the U.S. statutory rate for the three and six months ended December 31, 2005 primarily due to state taxes and other non-deductible items offset by the favorable impact of foreign operations. The effective tax rate was higher than the U.S. statutory rate for the three and six months ended December 31, 2004 primarily due to state taxes and other non-deductible items offset by the favorable impact of foreign operations.

The Company has open tax years in the U.S., Canada and other jurisdictions. The Company is currently under examination by the Internal Revenue Service for the fiscal year ended June 30, 2004. The audit is in the preliminary stages. The scope has not been determined nor have any assessments been issued.

In addition, there are certain tax years that are not currently under examination by the applicable tax authorities but may be subject to examination in the future. The results of audits are inherently uncertain. The Company periodically evaluates the adequacy of its related tax reserves, taking into account its open tax return positions and tax law changes. The Company believes that its tax reserves are appropriate. However, the final determination of tax audits could impact the Company's assessment of tax requirements.

NOTE 10 - EARNINGS PER SHARE

Basic and diluted earnings per share amounts are determined in accordance with the provisions of SFAS 128. The following table reconciles the numerators and denominators used in the computations of basic and diluted earnings per share (in thousands, except per share data):

Three months ended December 31,	

2005	2004

Edgar Filing: VERTRUE INC - Form 10-Q

Numerator:			
Income available to common shareholders used in basic earnings per share	\$ 7,664	\$ 5,883	
Add back interest expense on convertible securities, net of tax	767	761	
Income available to common shareholders after assumed conversion of dilutive securities	\$ 8,431	\$ 6,644	
Denominator:			
Weighted average number of common shares outstanding - basic	9,695	10,128	
Effect of dilutive securities:			
Convertible securities	2,230	2,230	
Stock options	851	705	
Weighted average number of common shares outstanding - diluted	12,776	13,063	
Basic earnings per share	\$ 0.79	\$ 0.58	
Diluted earnings per share	\$ 0.66	\$ 0.51	

The diluted earnings per common share calculations exclude the effect of potentially dilutive shares when their effect is antidilutive. Excluded from the diluted share calculation above for the three and six months ended December 31, 2005 are incremental weighted average stock options of approximately 581,000 and 581,000, respectively, and 44,000 and 917,000, respectively, for the three and six months ended December 31, 2004.

9

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11 - COMPREHENSIVE INCOME

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

	Three months ended December 31,		Six months ended December 31,	
	2005	2004	2005	2004
Net income	\$ 7,664	\$ 5,883	\$ 16,305	\$ 13,479
Unrealized (loss) gain on derivative assets	(404)	454	114	1,203
Foreign currency translation gain (loss)	171	(5)	411	93
Comprehensive income	\$ 7,431	\$ 6,332	\$ 16,830	\$ 14,775

NOTE 12 - SUPPLEMENTAL CASH FLOW INFORMATION

During the six months ended December 31, 2005, the Company incurred a capital lease obligation of \$231,000 to acquire equipment.

Edgar Filing: VERTRUE INC - Form 10-Q

NOTE 13 - BUSINESS SEGMENTS

The operating business segments reported below are the reportable business segments of the Company for which separate financial information is available and for which operating results are evaluated regularly by executive management in assessing performance and deciding how to allocate resources. The Company has three reportable business segments: Marketing Services, Personals and Management Services. The Marketing Services business segment primarily provides discounted products and services to consumers. The Personals business segment provides both web-based and phone-based personals services to its customers. During the quarter ended December 31, 2005, the Management Services business segment became reportable due to the increase in its assets. The Management Services business segment provides management services to healthcare professionals throughout the United States. The Corporate business unit includes unallocated general corporate expenses.

Management evaluates the operating results of each reportable business segment based on revenue and Adjusted EBITDA. The following is a summary of revenues, Adjusted EBITDA, capital expenditures, depreciation and amortization and assets by business segment (in thousands):

	Three months ended December 31,		Six months ended Dece	
	2005	2004	2005	
Revenues				
Marketing Services	\$ 134,479	\$ 118,714	\$ 266,327	\$
Personals	18,664	17,901	37,233	
Management Services	7,047	-	14,238	
Corporate	-	-	-	
Intersegment	(60)	(136)	(140)	
Total	\$ 160,130	\$ 136,479	\$ 317,658	\$
Adjusted EBITDA (1)				
Marketing Services	\$ 28,280	\$ 22,291	\$ 49,905	\$
Personals	1,692	976	3,922	
Management Services	395	-	983	
Corporate	(6,377)	(5,216)	(12,456)	
Total	\$ 23,990	\$ 18,051	\$ 42,354	\$
Capital Expenditures (2)				
Marketing Services	\$ 4,435	\$ 3,314	\$ 5,980	\$
Personals	229	306	482	
Management Services	38	-	56	
Corporate	-	-	-	
Total	\$ 4,702	\$ 3,620	\$ 6,518	\$

Edgar Filing: VERTRUE INC - Form 10-Q

ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED) NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Depreciation and Amortization	Three months ended December 31,		Six months ended Dec	
	2005	2004	2005	
Marketing Services	\$ 3,078	\$ 2,527	\$ 6,348	\$
Personals	2,396	2,337	4,751	
Management Services	406	-	805	
Corporate	282	101	556	
Total	\$ 6,162	\$ 4,965	\$ 12,460	\$

Assets	December 31,	June 30,
	2005	2005
Marketing Services	\$ 236,844	\$ 245,635
Personals	129,580	132,992
Management Services	51,784	41,053
Corporate (3)	28,217	27,482
Total	\$ 446,425	\$ 447,162

- (1) Defined as net income excluding interest and other expense, net, provision for income taxes, depreciation and amortization and the changes in deferred revenue and deferred marketing costs. See reconciliation below.
- (2) Management does not allocate certain capital expenditures to the Corporate business unit. However, the associated depreciation expense has been allocated for purposes of evaluating performance.
- (3) Includes unallocated non-operating assets including short-term investments, debt issuance costs and other.

The following tables reconcile Adjusted EBITDA to income before income taxes (in thousands):

	Three months ended December 31, 2005				
	Marketing Services	Personals	Management Services	Corporate	To
Income before income taxes					\$ 1
Interest and other expense, net (1)					
Operating income (expense)	\$ 24,071	\$ (684)	\$ 150	\$ (6,659)	\$ 1
Depreciation and amortization	3,078	2,396	406	282	
Change in deferred revenues	(850)	(20)	(161)	-	
Change in deferred marketing costs	1,981	-	-	-	
Adjusted EBITDA	\$ 28,280	\$ 1,692	\$ 395	\$ (6,377)	\$ 2

Edgar Filing: VERTRUE INC - Form 10-Q

	Three months ended December 31, 2004				
	Marketing Services	Personals	Management Services	Corporate	To
Income before income taxes					\$
Interest and other expense, net (1)					
Operating income (expense)	\$ 20,332	\$ (1,232)	\$ -	\$ (5,317)	\$ 1
Depreciation and amortization	2,527	2,337	-	101	
Change in deferred revenues	(2,905)	(129)	-	-	(
Change in deferred marketing costs	2,337	-	-	-	
Adjusted EBITDA	\$ 22,291	\$ 976	\$ -	\$ (5,216)	\$ 1

11

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	Six months ended December 31, 2005				
	Marketing Services	Personals	Management Services	Corporate	To
Income before income taxes					\$ 2
Interest and other expense, net (1)					
Operating income (expense)	\$ 47,770	\$ (744)	\$ 520	\$ (13,012)	\$ 3
Depreciation and amortization	6,348	4,751	805	556	1
Change in deferred revenues	(10,184)	(85)	(342)	-	(1
Change in deferred marketing costs	5,971	-	-	-	
Adjusted EBITDA	\$ 49,905	\$ 3,922	\$ 983	\$ (12,456)	\$ 4

	Six months ended December 31, 2004				
	Marketing Services	Personals	Management Services	Corporate	To
Income before income taxes					\$ 2
Interest and other expense, net (1)					
Operating income (expense)	\$ 42,310	\$ (1,284)	\$ -	\$ (10,511)	\$ 3
Depreciation and amortization	4,689	4,696	-	201	
Change in deferred revenues	(19,493)	124	-	-	(1
Change in deferred marketing costs	8,685	-	-	-	
Adjusted EBITDA	\$ 36,191	\$ 3,536	\$ -	\$ (10,310)	\$ 2

Edgar Filing: VERTRUE INC - Form 10-Q

- (1) Management does not allocate interest and other expense, net to the individual segments.

NOTE 14 - GUARANTOR AND NONGUARANTOR FINANCIAL INFORMATION

In April 2004, the Company issued \$150,000,000 aggregate principal amount of 9.25% Senior Notes due 2014. The Senior Notes are unsecured obligations and rank pari passu in right of payment to all of the Company's existing and future senior unsecured indebtedness and senior in right of payment to all of the Company's existing and future subordinated indebtedness that expressly provides for its subordination to the Senior Notes. The Senior Notes are fully and unconditionally guaranteed by all of the Company's existing and future domestic subsidiaries that guarantee the Company's Credit Facility (as defined in the Indenture governing the Senior Notes) and certain of the Company's existing and future foreign subsidiaries.

The following consolidating condensed financial information presents the consolidating balance sheets as of December 31, 2005 and June 30, 2005 and the related statements of operations for the three and six months ended December 31, 2005 and 2004 and the cash flows for the six months ended December 31, 2005 and 2004. The information includes the elimination entries necessary to consolidate the Company ("Parent") with the guarantor and nonguarantor entities.

Investments in subsidiaries are accounted for by the Parent using the equity method of accounting. The guarantor and nonguarantor subsidiaries are presented on a combined basis. The principal elimination entries eliminate investments in subsidiaries and intercompany balances and transactions.

12

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS
(In thousands)

	December 31, 2005		
	Parent	Guarantor Subsidiaries	Nonguarantor Subsidiaries
Assets			
Current assets	\$ 63,501	\$ 69,036	\$ 28,628
Fixed assets, net	18,656	11,636	7,311
Goodwill	-	117,750	95,109
Intangible assets, net	998	28,785	12,046
Other assets	10,600	289	2,607
Investment in subsidiaries	295,188	-	-
Total assets	\$ 388,943	\$ 227,496	\$ 145,701
Liabilities and Shareholders' (Deficit) Equity			
Current liabilities	\$ 174,440	\$ 45,350	\$ 23,565
Deferred income taxes	1,846	7,185	434
Other long-term liabilities	4,534	-	1,475

Edgar Filing: VERTRUE INC - Form 10-Q

Long-term debt	237,897	-	-
	-----	-----	-----
Total liabilities	418,717	52,535	25,474
	=====	=====	=====
Shareholders' (deficit) equity:			
Preferred stock	-	-	-
Common stock	198	6	3
Capital in excess of par value	177,281	165,285	113,432
Accumulated earnings (deficit)	51,985	9,416	6,682
Accumulated other comprehensive income (loss)	377	254	110
Treasury stock	(259,615)	-	-
	-----	-----	-----
Total shareholders' (deficit) equity	(29,774)	174,961	120,227
	-----	-----	-----
Total liabilities and shareholders' (deficit) equity	\$ 388,943	\$ 227,496	\$ 145,701
	=====	=====	=====

13

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS
(In thousands)

	June 30, 2005		
	Parent	Guarantor Subsidiaries	Nonguarantor Subsidiaries
	-----	-----	-----
Assets			
Current assets	\$ 80,036	\$ 60,684	\$ 23,509
Fixed assets, net	18,797	13,098	7,167
Goodwill	-	117,749	83,750
Intangible assets, net	1,097	31,789	13,590
Other assets	10,991	64	2,043
Investment in subsidiaries	275,213	-	-
	-----	-----	-----
Total assets	\$ 386,134	\$ 223,384	\$ 130,059
	=====	=====	=====
Liabilities and Shareholders' (Deficit) Equity			
Current liabilities	\$ 190,595	\$ 46,890	\$ 22,534
Deferred income taxes	2,588	7,265	(151)
Other long-term liabilities	3,565	-	1,692
Long-term debt	237,814	-	-
	-----	-----	-----
Total liabilities	434,562	54,155	24,075
	-----	-----	-----
Shareholders' (deficit) equity:			
Preferred stock	-	-	-

Edgar Filing: VERTRUE INC - Form 10-Q

Common stock	197	6	3
Capital in excess of par value	169,463	165,285	102,484
Accumulated earnings (deficit)	35,680	3,884	3,667
Accumulated other comprehensive (loss) income	(148)	54	(170)
Treasury stock	(253,620)	-	-
Total shareholders' (deficit) equity	(48,428)	169,229	105,984
Total liabilities and shareholders' (deficit) equity	\$ 386,134	\$ 223,384	\$ 130,059

14

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands)

	Three months ended Decem		
	Parent	Guarantor Subsidiaries	Nonguarantor Subsidiaries
Revenues	\$ 96,964	\$ 40,365	\$ 27,335
Expenses:			
Marketing	52,545	17,893	9,976
Operating	16,780	8,897	9,971
General and administrative	17,489	7,616	4,422
Amortization of intangibles	9	1,494	694
Operating income	10,141	4,465	2,272
Equity in income of subsidiaries	4,413	-	-
Interest (expense) income, net	(4,787)	202	198
Other (expense) income, net	(14)	(120)	14
Income before income taxes	9,753	4,547	2,484
Provision for income taxes	2,089	1,663	955
Net income	\$ 7,664	\$ 2,884	\$ 1,529

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands)

	Three months ended Decem		
	Parent	Guarantor Subsidiaries	Nonguarantor Subsidiaries

Edgar Filing: VERTRUE INC - Form 10-Q

Revenues	\$	92,351	\$	35,316	\$	10,026
Expenses:						
Marketing		49,373		16,839		2,984
Operating		15,616		7,291		3,752
General and administrative		15,664		8,588		2,050
Amortization of intangibles		76		1,527		150
Operating income		11,622		1,071		1,090
Equity in income of subsidiaries		1,767		-		-
Interest (expense) income, net		(4,649)		37		1
Other (expense) income, net		(5)		419		14
Income before income taxes		8,735		1,527		1,105
Provision for income taxes		2,852		321		544
Net income	\$	5,883	\$	1,206	\$	561

15

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands)

	Six months ended December					
	Parent	Guarantor Subsidiaries	Nonguarantor Subsidiaries			
Revenues	\$	193,773	\$	79,174	\$	54,425
Expenses:						
Marketing		103,781		34,835		20,631
Operating		34,055		17,715		19,207
General and administrative		34,283		15,025		8,673
Amortization of intangibles		85		3,003		1,545
Operating income		21,569		8,596		4,369
Equity in income of subsidiaries		8,547		-		-
Interest (expense) income, net		(9,506)		299		363
Other income (expense), net		13		(235)		61
Income before income taxes		20,623		8,660		4,793
Provision for income taxes		4,318		3,128		1,778
Net income	\$	16,305	\$	5,532	\$	3,015

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands)

Edgar Filing: VERTRUE INC - Form 10-Q

	Six months ended December		
	Parent	Guarantor Subsidiaries	Nonguarantor Subsidiaries
Revenues	\$ 188,636	\$ 69,822	\$ 15,346
Expenses:			
Marketing	99,872	33,404	4,452
Operating	30,748	14,480	6,129
General and administrative	31,178	16,769	2,960
Amortization of intangibles	76	3,071	150
Operating income	26,762	2,098	1,655
Equity in income of subsidiaries	2,587	-	-
Interest (expense) income, net	(9,349)	91	4
Other (expense) income, net	(98)	355	36
Income before income taxes	19,902	2,544	1,695
Provision for income taxes	6,423	842	810
Net income	\$ 13,479	\$ 1,702	\$ 885

16

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Six months ended December		
	Parent	Guarantor Subsidiaries	Nonguarantor Subsidiaries
Net cash provided by (used in) operating activities	\$ 15,537	\$ 6,939	\$ 887
Investing activities			
Acquisition of fixed assets	(3,538)	(885)	(2,095)
Purchases of short-term investments	(50,325)	-	-
Sales of short-term investments	49,452	378	-
Acquisitions of businesses, net of cash acquired	(14,717)	(224)	(1)
Investment in subsidiaries	(8,547)	-	-
Net cash (used in) provided by investing activities	(27,675)	(731)	(2,096)
Financing activities			
Net proceeds from issuance of stock	2,729	-	-
Excess tax benefit from stock-based compensation	560	-	-
Treasury stock purchases	(5,995)	-	-
Payments of long-term obligations	(195)	-	(197)

Edgar Filing: VERTRUE INC - Form 10-Q

Net cash used in financing activities	(2,901)	-	(197)
Effect of exchange rate changes on cash and cash equivalents	-	131	326
Net (decrease) increase in cash and cash equivalents	(15,039)	6,339	(1,080)
Cash and cash equivalents at beginning of year	24,366	29,821	10,169
Cash and cash equivalents at end of period	\$ 9,327	\$ 36,160	\$ 9,089

17

VERTRUE INCORPORATED
ITEM 1. CONDENSED FINANCIAL STATEMENTS (UNAUDITED)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Six months ended December		
	Parent	Guarantor Subsidiaries	Nonguarantor Subsidiaries
Net cash provided by (used in) operating activities	\$ 101,300	\$ (82,693)	\$ (1,394)
Investing activities			
Acquisition of fixed assets	(3,495)	(538)	(306)
Purchases of short-term investments	(368,533)	-	-
Sales of short-term investments	425,691	221	-
Acquisitions of businesses, net of cash acquired	(111,322)	93,937	1,288
Investment in subsidiaries	(2,587)	-	-
Net cash (used in) provided by investing activities	(60,246)	93,620	982
Financing activities			
Net proceeds from issuance of stock	6,237	-	-
Treasury stock purchases	(8,396)	-	-
Debt issuance costs	(750)	-	-
Payments of long-term obligations	(161)	(13)	(30)
Net cash used in financing activities	(3,070)	(13)	(30)
Effect of exchange rate changes on cash and cash equivalents	-	(291)	526
Net increase in cash and cash equivalents	37,984	10,623	84
Cash and cash equivalents at beginning of year	18,251	26,657	2,258
Cash and cash equivalents at end of period	\$ 56,235	\$ 37,280	\$ 2,342

NOTE 16 - NEW ACCOUNTING PRONOUNCEMENTS

Edgar Filing: VERTRUE INC - Form 10-Q

In May 2005, the FASB issued Statement No. 154, "Accounting Changes and Error Corrections - A replacement of APB Opinion No. 20 and FASB Statement No. 3" ("SFAS 154"). This statement requires retrospective application to prior periods' financial statements of changes in accounting principles unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. This statement applies to all voluntary changes in accounting principles and changes required by an accounting pronouncement that does not include specific transition provisions. SFAS 154 is effective beginning in the Company's first quarter of fiscal 2007. The Company does not expect the adoption of SFAS 154 to have a material effect on its consolidated financial position, results of operations or cash flows.

18

VERTRUE INCORPORATED ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

The following discussion should be read in conjunction with Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K for the year ended June 30, 2005, which describes, among other things, the Company's basic business model and critical accounting policies.

The Company has three reportable business segments: Marketing Services, Personals and Management Services. During the quarter ended December 31, 2005, the Management Services business segment became reportable due to the increase in its assets. The Management Services business segment provides management services to healthcare professionals throughout the United States. For additional information about these reportable business segments, see Note 13 to the condensed consolidated financial statements in this Quarterly Report on Form 10-Q.

The results of My Choice Medical Holdings, Inc. ("MCM") and Bargain Network, Inc. ("Bargain") (collectively the "Acquired Companies") have been included in the consolidated results since their acquisitions on January 1, 2005 and November 30, 2004, respectively.

Adjusted EBITDA and EBITDA are used by the Company's management to evaluate the performance of its business. A discussion of Adjusted EBITDA can be found in "Liquidity and Capital Resources" in this Quarterly Report on Form 10-Q. A description and reconciliation of net income to EBITDA and Adjusted EBITDA are disclosed in "Reconciliation of Non-GAAP Measures" in this Quarterly Report on Form 10-Q.

(Dollars in millions)	Three months ended December 31,		Percent Increase/ (Decrease)	Six months ended December 31,	
	2005	2004	'05 vs. '04	2005	2004
Revenues	\$ 160.1	\$ 136.5	17%	\$ 317.6	\$ 200.0
Marketing expenses	76.3	68.7	11%	150.2	111.5
Operating expenses	35.2	25.9	36%	70.3	51.8

Edgar Filing: VERTRUE INC - Form 10-Q

General and administrative expenses	29.5	26.3	12%	58.0
Amortization of intangibles	2.2	1.8	22%	4.6
<hr/>				
Operating income	16.9	13.8	22%	34.5
Interest expense, net	(4.4)	(4.6)	(4)%	(8.8)
Other (expense) income, net	(0.1)	0.4	(125)%	(0.2)
<hr/>				
Income before income taxes	12.4	9.6	29%	25.5
Provision for income taxes	4.7	3.7	27%	9.2
<hr/>				
Net income	\$ 7.7	\$ 5.9	31%	\$ 16.3
<hr/>				
EBITDA	\$ 23.0	\$ 18.7	23%	\$ 47.0
<hr/>				

19

VERTRUE INCORPORATED
ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following table sets forth revenue by payment plan and by segment (in millions):

	Three months ended December 31,		Percent Increase/ (Decrease)	Six months ended December 31,	
	2005	2004		2005	2004
Revenues					
Monthly payment plans	\$ 86.7	\$ 56.0	55%	\$ 169.8	\$ 103.8
Annual payment plans:					
Initial year	8.2	14.9	(45)%	17.8	32.7
Renewal year	29.7	40.0	(26)%	60.8	89.7
Other	9.9	7.8	27%	17.9	14.7
<hr/>					
Total Marketing Services	134.5	118.7	13%	266.3	236.2
Personals	18.6	17.8	4%	37.1	35.6
Management Services	7.0	-	NM	14.2	-
<hr/>					
Total	\$ 160.1	\$ 136.5	17%	\$ 317.6	\$ 272.7
<hr/>					

For the Three Months Ended December 31, 2005 and 2004

Revenues increased \$23.6 million, or 17%, in the 2006 fiscal second quarter primarily due to the inclusion of revenues from the Acquired Companies. Excluding revenues from the Acquired Companies, revenues would have increased 8% due to an increase in Marketing Services revenues, as discussed below. Net active members and customers increased 3% to 6.4 million at December 31, 2005

Edgar Filing: VERTRUE INC - Form 10-Q

from 6.2 million at December 31, 2004.

Marketing Services revenues increased \$15.8 million, or 13%, in the 2006 fiscal second quarter due to the inclusion of revenues from Bargain. Excluding revenues from Bargain, total marketing services revenues would have increased 9% due to a 47% increase in revenues from members enrolled in monthly payment plans partially offset by a 31% decrease in revenue from members enrolled in annual payment plans. The increase in revenues from monthly payment plans was due to a 31% increase in average monthly members billed and an 11% increase in the monthly member price point. Revenues from members enrolled in annual payment plans continue to decrease for both initial year members and renewal members due to the continued shift to enrolling new members in monthly payment programs as well as the attrition of the annual renewal base.

Personals revenues increased \$0.8 million, or 4%, in the 2006 fiscal second quarter primarily due to the incremental revenue generated from Lavalife's growing mobile service. Management Services revenues represent the revenues from MCM.

Marketing expenses increased \$7.6 million, or 11%, in the 2006 fiscal second quarter and as a percent of revenues, were 48% this year versus 50% last year. The increase in marketing expenses was due to the inclusion of costs incurred by the Acquired Companies as well as an increase in online marketing efforts which resulted in increased revenues, as discussed above. The decrease in marketing expenses as a percent of revenues was due to increased price points and synergies realized from our Acquired Companies.

Operating expenses increased \$9.3 million, or 36%, in the 2006 fiscal second quarter and as a percent of revenues, were 22% this year versus 19% last year. These increases were due to the inclusion of expenses incurred by the Acquired Companies in addition to increased costs of servicing the higher member and customer base. The Acquired Companies have a higher proportion of their cost structure included as operating expenses which resulted in an increase in the operating expense ratio.

General and administrative expenses increased \$3.2 million, or 12%, in the 2006 fiscal second quarter and included a \$1.1 million charge related to the adoption of Financial Accounting Standards Board Statement No. 123(R), "Share-Based Payment" ("SFAS 123R"). Excluding this expense, general and administrative expenses would have increased \$2.1 million, or 8%, and as a percent of revenues, would have been 18% this quarter versus 19% in the prior year quarter. The increase in general and administrative expenses was due to the inclusion of expenses incurred by the Acquired Companies. General and administrative expenses decreased as a percent of revenue due to leveraging expenses with the increased revenue.

Amortization of intangible assets increased \$0.4 million, or 22%, in the 2006 fiscal second quarter due to amortization expense related to the Acquired Companies.

20

VERTRUE INCORPORATED ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Operating income increased \$3.1 million, or 22%, in the 2006 fiscal second quarter and as a percent of revenues, was 11% this year and 10% last year, primarily due to the inclusion of the Acquired Companies' results of operations and a 2% improvement in marketing margin as a percent of revenue, as discussed

Edgar Filing: VERTRUE INC - Form 10-Q

above.

Interest expense, net decreased \$0.2 million, or 4%, in the 2006 fiscal second quarter and included \$3.6 million of interest expense related to the 9.25% Senior Notes and \$1.2 million of interest expense related to the 5.5% Convertible Notes.

The provision for income taxes increased \$1.0 million, or 27%, in the 2006 fiscal second quarter and was based on an effective tax rate of 38.0% this year versus 38.7% last year.

EBITDA increased 23% to \$23.0 million in the 2006 fiscal second quarter from \$18.7 million in the 2005 fiscal second quarter due to the improvement in the marketing margin discussed above and the inclusion of the Acquired Companies' results. As a percent of revenues, EBITDA was 14% this year and last year. The 2006 fiscal second quarter included a \$1.1 million charge related to the adoption of SFAS 123R. Excluding this charge, EBITDA would have been 15% of revenue this year versus 14% last year. Marketing Services EBITDA increased 19% to \$27.1 million in the 2006 fiscal second quarter from \$22.8 million in the 2005 fiscal second quarter due to increased price points and synergies realized from our Acquired Companies. Personals EBITDA increased 55% to \$1.7 million in the 2006 fiscal second quarter from \$1.1 million in the 2005 fiscal second quarter due to Lavalife's growing mobile service business and cost containment. Management Services EBITDA was \$0.6 million and represented the results of MCM. Corporate EBITDA decreased 23% to \$(6.4) million in the 2006 fiscal second quarter from \$(5.2) million in the 2005 fiscal second quarter due to the adoption of SFAS 123R.

For the Six Months Ended December 31, 2005 and 2004

Revenues increased \$45.5 million, or 17%, in the six months ended December 31, 2005 primarily due to the inclusion of revenues from the Acquired Companies. Excluding revenues from the Acquired Companies, revenues would have increased 6% due to an increase in Marketing Services' revenues, as discussed below. Net active members and customers increased 3% to 6.4 million at December 31, 2005 from 6.2 million at December 31, 2004.

Marketing Services revenues increased \$30.3 million, or 13%, in the six months ended December 31, 2005 due to the inclusion of revenues from Bargain. Excluding revenues from Bargain, total marketing services revenues would have increased 7% due to a 49% increase in revenues from members enrolled in monthly payment plans partially offset by a 32% decrease in revenues from members enrolled in annual payment plans. The increase in revenues from monthly payment plans was due to a 34% increase in average monthly members billed and a 10% increase in the monthly member price point. Revenues from members enrolled in annual payment plans continue to decrease for both initial year members and renewal members due to the continued shift to enrolling new members in monthly payment programs as well as the attrition of the annual renewal base.

Personals revenues increased \$1.0 million, or 3%, in the six months ended December 31, 2005 primarily due to the incremental revenue generated from Lavalife's growing mobile service. Management Services revenues represent the revenues from MCM.

Marketing expenses increased \$13.0 million, or 9%, in the six months ended December 31, 2005 and as a percent of revenues, were 47% this year versus 50% last year. The increase in marketing expenses was due to the inclusion of costs incurred by the Acquired Companies as well as an increase in online marketing efforts which resulted in increased revenues, as discussed above. The decrease in marketing expenses as a percent of revenues was primarily due to increased price points and synergies realized from our Acquired Companies.

Edgar Filing: VERTRUE INC - Form 10-Q

Operating expenses increased \$20.1 million, or 40%, in the six months ended December 31, 2005 and as a percent of revenues, were 22% this year versus 18% last year. The increased level of operating expenses was primarily due to the inclusion of expenses incurred by the Acquired Companies in addition to the increased costs of servicing the higher member and customer base. The increase as a percent of revenue was primarily due to the inclusion of the Acquired Companies which have a higher proportion of their cost structure included as operating expenses resulting in an increase in the operating expense ratio.

General and administrative expenses increased \$7.1 million, or 14%, in the six months ended December 31, 2005 and included a \$2.3 million charge related to the adoption of SFAS 123R. Excluding this expense, general and administrative

21

VERTRUE INCORPORATED ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

expenses would have increased \$4.8 million, or 9%, and as a percent of revenues, would have been 18% this year versus 19% in the prior year. This increase in general and administrative expenses was primarily due to the inclusion of expenses incurred by the Acquired Companies. General and administrative expenses decreased as a percent of revenue due to leveraging expenses with the increased revenue.

Amortization of intangible assets increased \$1.3 million, or 39%, in the six months ended December 31, 2005 due to amortization expense related to the Acquired Companies.

Operating income increased \$4.0 million, or 13%, in the six months ended December 31, 2005 primarily due to the 3% improvement in marketing margin as a percent of revenue discussed above and the inclusion of the Acquired Companies' results of operations. As a percent of revenues, operating income was 11% this year and last year.

Interest expense, net decreased \$0.4 million, or 4%, in the six months ended December 31, 2005 and included \$7.1 million interest expense related to the 9.25% Senior Notes and \$2.5 million of interest expense related to the 5.5% Convertible Notes.

The provision for income taxes increased \$1.1 million, or 14%, in the six months ended December 31, 2005 and was based on an effective tax rate of 36.1% this year versus 37.5% last year. The effective tax rate decreased from the prior year primarily due to the favorable impact of the foreign operations on our tax rate.

EBITDA increased 17% to \$47.0 million in the six months ended December 31, 2005 from \$40.1 million in the six months ended December 31, 2004 primarily due to the improvement in the marketing margin discussed above and inclusion of the Acquired Companies' results. As a percent of revenues, EBITDA was 15% this year and last year. The six months ended December 31, 2005 included a \$2.3 million charge related to the adoption of SFAS 123R. Excluding this charge, EBITDA would have been 16% of revenue this year versus 15% last year. Marketing Services EBITDA increased 15% to \$54.1 million in the six months ended December 31, 2005 from \$47.0 million in the six months ended December 31, 2004 due to increased price points and synergies realized from our Acquired Companies. Personal Services EBITDA increased 18% to \$4.0 million in the six months ended December 31, 2005 from \$3.4 million in the six months ended December 31, 2004 due to Lavalife's growing mobile service business and cost containment. Management Services EBITDA

Edgar Filing: VERTRUE INC - Form 10-Q

was \$1.3 million in the six months ended December 31, 2005. Corporate EBITDA decreased 20% to \$(12.4) million in the six months ended December 31, 2005 from \$(10.3) million in the six months ended December 31, 2004 due to the adoption of FAS 123R.

LIQUIDITY AND CAPITAL RESOURCES

Net cash flow provided by operating activities is an important measure used to understand the Company's liquidity. Net cash provided by operating activities increased to \$14.8 million in the six months ended December 31, 2005 from \$14.6 million in the six months ended December 31, 2004. Management believes it is useful to analyze the components of net cash provided by operating activities as follows: Revenue before deferral, marketing costs before deferral, operating expenses, general and administrative expenses, Adjusted EBITDA and changes in assets and liabilities. For definitions and reconciliations of revenue before deferral, marketing costs before deferral and Adjusted EBITDA, refer to the discussion in "Reconciliation of Non-GAAP Measures" in this Quarterly Report on Form 10-Q.

22

VERTRUE INCORPORATED ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The table below summarizes the components of revenues before deferral (in millions):

	Six months ended December 31,		Percent Increase/ (Decrease)
	2005	2004	'05 vs. '04
Revenues before deferral			
Monthly payment plans	\$ 172.0	\$ 108.2	59%
Annual payment plans:			
Initial year	14.1	20.3	(31)%
Renewal year	52.2	73.5	(29)%
Other	17.8	14.5	23%
Total Marketing Services	256.1	216.5	18%
Personals	37.0	36.2	2%
Management Services	13.9	-	NM
Total	\$ 307.0	\$ 252.7	21%

Revenues before deferral increased 21% to \$307.0 million in the six months ended December 31, 2005 due to a 10% growth in revenues before deferral in the existing business and the inclusion of revenues before deferral generated by the Acquired Companies. Revenues before deferral from monthly payment plans increased 59% due to a 39% increase in average monthly members billed to 2.1 million in the six months ended December 31, 2005 and a 14% increase in the monthly weighted average program price point which increased to \$13.69 for the six months ended December 31, 2005. The average monthly members billed increased due to the increase in the mix of new members enrolled in monthly payment plan programs, which was 88% during the six months ended December 31, 2005 and 83% during the six months ended December 31, 2004. Revenues before deferral from annual payment plans declined due to the continued shift to enrolling new members in monthly payment programs as well as the attrition of the annual

Edgar Filing: VERTRUE INC - Form 10-Q

renewal base. The new annual weighted average program price points were \$109 and \$106 for the six months ended December 31, 2005 and 2004, respectively. Personals revenues before deferral increased 2% from the prior year due to increased revenues before deferral related to mobile services. Management Services revenues before deferral represent the revenues from MCM in the six months ended December 31, 2005.

Marketing costs before deferral were \$144.2 million and \$128.5 million for the six months ended December 31, 2005 and 2004, respectively. As a percent of revenue before deferral, marketing costs before deferral were 47% and 51% in the fiscal 2006 and 2005 year to date periods, respectively. The improved ratio is due to increased price points, more efficient marketing spending and better retention in certain sectors of our business. Marketing costs before deferral increased 12% in the six months ended December 31, 2005 primarily due to the inclusion of marketing costs before deferral from the Acquired Companies.

Marketing margin before deferral was \$162.8 million and \$124.2 million for the six months ended December 31, 2005 and 2004, respectively. The effect of the increase in marketing margin before deferral in the fiscal 2006 year to date period on net cash provided by operating activities was partially offset by increased operating and general and administrative expenses and resulted in a \$13.0 million, or 44%, increase in Adjusted EBITDA to \$42.4 million for the six months ended December 31, 2005 from \$29.4 million for the six months ended December 31, 2004. The increase in Adjusted EBITDA was primarily driven by the Marketing Services segment. The table below presents Adjusted EBITDA by segment.

	Six months ended December 31,		Percent Increase/ (Decrease)
	2005	2004	'05 vs. '04
Adjusted EBITDA			
Marketing Services	\$ 49.9	\$ 36.2	38%
Personals	3.9	3.5	11%
Management Services	1.0	-	NM
Corporate	(12.4)	(10.3)	(20)%
Total	\$ 42.4	\$ 29.4	44%

23

VERTRUE INCORPORATED ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Changes in assets and liabilities used \$12.9 million of cash in the six months ended December 31, 2005 compared to \$3.2 million in the six months ended December 31, 2004. The use of cash in fiscal 2006 primarily related to the timing of trade and tax payments during the period and the \$5.5 million arbitration award payment made during the December 2005 quarter.

Capital expenditures were \$6.5 million and \$4.3 million in the 2006 and 2005 year to date periods, respectively. As a result, free cash flow, defined as operating cash flow less capital expenditures, was \$8.3 million for the six months ended December 31, 2005 compared to \$10.3 million for the prior year period.

Net cash (used in) provided by investing activities was \$(22.0) million and

Edgar Filing: VERTRUE INC - Form 10-Q

\$36.9 million in the six months ended December 31, 2005 and 2004, respectively. Net cash used in investing activities in the six months ended December 31, 2005 primarily reflected \$14.9 million used in connection with the Company's recent acquisitions. Net cash provided by investing activities in the six months ended December 31, 2004 primarily reflected \$57.4 million of net proceeds from sales of short-term investments and \$16.1 million related to business acquisitions.

Net cash used in financing activities was \$3.1 million in both fiscal 2006 and 2005 six-month periods. Net cash used in financing activities in 2006 principally reflected the use of \$6.0 million to repurchase the Company's stock, which was partially offset by \$2.7 million of proceeds from the exercise of stock options and \$0.6 million of excess tax benefit from stock-based compensation. Net cash used in financing activities in 2005 principally reflected the use of \$8.4 million to repurchase the Company's stock, which was partially offset by proceeds from the exercise of stock options of \$6.2 million.

Credit Facility

The Company has a senior secured credit facility, which allows borrowings of up to \$45.0 million. Borrowings under the senior secured credit facility accrue interest at either the Eurodollar rate, or the higher of the Prime rate or the Federal Funds rate plus an applicable margin. As of December 31, 2005, the effective interest rate for borrowings under the senior secured credit facility was 7.25%. The senior secured credit facility has certain financial covenants, including a maximum debt coverage ratio, potential restrictions on additional borrowings and potential restrictions on additional stock repurchases. As of December 31, 2005, the Company was in compliance with all such debt covenants. The bank credit facility matures on March 23, 2006 and management expects it to be renewed or replaced during the third quarter of fiscal 2006.

Stock Repurchase Program

The Company purchased 164,800 shares of its common stock for \$6.0 million at an average price of \$36.38 per share during 2006 compared to 314,500 shares for \$8.2 million at an average price of \$26.05 per share in 2005. The Company utilized cash from operations, stock issuances and the issuance of the Convertible Notes and Senior Notes to repurchase shares in fiscal 2006 and 2005.

As of December 31, 2005, the Company had 0.7 million shares available for repurchase under its stock repurchase program.

Other

As of December 31, 2005, the Company had cash, cash equivalents and short-term investments of \$75.7 million in addition to its senior secured credit facility. The Company believes that existing cash and short-term investment balances and funds available under its senior secured credit facility together with cash generated from operations will be sufficient to meet its funding requirements for the foreseeable future.

The Company expects to incur capital expenditures of \$15.0 million in fiscal 2006. In addition, contingent payments related to the acquisition of MCM of up to \$56.0 million may be paid if certain performance targets, including increasing levels of revenues and earnings, are achieved during the three calendar years ending December 31, 2007. As of December 31, 2005, the Company expects to pay \$10.5 million during fiscal 2006 related to these contingent payments. The Company intends to utilize cash on hand, short-term investments and cash generated from operations to fulfill payment obligations during 2006.

RECONCILIATION OF NON-GAAP MEASURES

Management believes that revenues before deferral and marketing costs before deferral are important measures of liquidity and are significant factors in understanding the Company's operating cash flow trends. These non-GAAP measures are used by management and the Company's investors to understand the liquidity

Edgar Filing: VERTRUE INC - Form 10-Q

trends of the Company's marketing margins related to current period operations which are reflected within the operating cash flow section of the cash flow statement. GAAP revenues and marketing expenses are important measures used to understand the marketing margins earned during the period in the income statement. However, in order to understand the Company's operating cash flow, it is important to understand the primary current period drivers of that cash flow.

24

VERTRUE INCORPORATED ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Two of the primary indicators of operating liquidity for the period are revenues before deferral and marketing costs before deferral. Revenues before deferral are revenues before the application of SAB 104 and represent the revenues billed during the current reporting period less an allowance for membership cancellations. That is, revenues before deferral for a reporting period include membership fees received in the current reporting period that will be recorded as GAAP revenues in future reporting periods and exclude membership fees received in prior reporting periods that are recorded as GAAP revenues in the current reporting period. Marketing costs before deferral are marketing costs before the application of SAB 104 and SOP 93-7 and represent marketing costs paid or accrued during the current reporting period. That is, marketing costs before deferral for a reporting period include costs paid or accrued in the current reporting period that will be recorded as GAAP marketing expenses in future reporting periods and exclude marketing expenses paid or accrued in prior reporting periods that are recorded as GAAP marketing expenses in the current reporting period. Neither revenues before deferral nor marketing costs before deferral exclude charges or liabilities that will require future cash settlement. Additionally, these measures are not a substitute for or superior to revenues and marketing expenses determined in accordance with generally accepted accounting principles.

Revenues before deferral are calculated as follows (in millions):

	Six months ended December 31,	
	2005	2004
Revenues	\$ 317.6	\$ 272.1
Change in deferred revenues	(10.6)	(19.4)
Revenues before deferral	\$ 307.0	\$ 252.7
	=====	=====

Marketing costs before deferral are calculated as follows (in millions):

	Six months ended December 31,	
	2005	2004
Marketing expenses	\$ 150.2	\$ 137.2
Change in deferred marketing costs	(6.0)	(8.7)
Marketing costs before deferral	\$ 144.2	\$ 128.5
	=====	=====

Edgar Filing: VERTRUE INC - Form 10-Q

Adjusted EBITDA and EBITDA are used by the Company's management to evaluate the year over year performance of its business and to measure that performance compared with internal budgets. Additionally, Adjusted EBITDA is used to determine compensation under the Company's management incentive plans.

Adjusted EBITDA is useful to management and investors because it eliminates the effects of interest and other expense, income taxes, non-cash depreciation of tangible assets and non-cash amortization of intangible assets and the amortization related to the recognition of GAAP revenues and GAAP marketing expenses and therefore includes only membership fees billed in the current reporting period less an allowance for cancellations and marketing costs paid or accrued in the current reporting period. Adjusted EBITDA is reconciled to net cash provided by operating activities because the Company believes that it is the most directly comparable liquidity measure. Adjusted EBITDA is also reconciled to net income because it is also used by the Company's management as a performance measure. EBITDA is useful to management and investors because it eliminates the effects of interest and other expense, income taxes, non-cash depreciation of tangible assets and non-cash amortization of intangible assets and is calculated using revenues and marketing expenses. EBITDA is reconciled to net income because the Company believes that it is the most directly comparable GAAP measure.

A limitation of Adjusted EBITDA and EBITDA is that they do not reflect the periodic amortization of certain capitalized tangible and intangible assets used in generating revenues in the Company's businesses nor do they reflect the effects of interest and taxes.

These non-GAAP measures should be considered in addition to, not as a substitute for or superior to, operating income, net income, operating cash flows or other measures of financial performance and liquidity determined in accordance with generally accepted accounting principles.

25

VERTRUE INCORPORATED ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following table reconciles net cash provided by operating activities to Adjusted EBITDA (in millions):

	Six months ended December 31,	
	2005	2004
Net cash provided by operating activities	\$ 14.8	\$ 14.6
Changes in assets and liabilities (use of cash)	12.9	3.2
Interest and other expense, net (to be paid in cash)	8.5	8.1
Taxes	8.3	3.9
Stock compensation expense	(2.3)	-
Other	0.2	(0.4)
Adjusted EBITDA	\$ 42.4	\$ 29.4
	=====	=====

The following tables reconcile net income to EBITDA and Adjusted EBITDA (in millions):

Edgar Filing: VERTRUE INC - Form 10-Q

Three months ended December 31, 2005

	Marketing Services	Personals	Management Services	Corporate	To
Net income					\$
Interest and other expense, net (1)					
Provision for income taxes (1)					
Operating income (expense)	\$ 24.1	\$ (0.7)	\$ 0.2	\$ (6.7)	\$
Depreciation and amortization	3.0	2.4	0.4	0.3	
EBITDA	\$ 27.1	\$ 1.7	\$ 0.6	\$ (6.4)	\$

Three months ended December 31, 2004

	Marketing Services	Personals	Management Services	Corporate	To
Net income					\$
Interest and other expense, net (1)					
Provision for income taxes (1)					
Operating income (expense)	\$ 20.3	\$ (1.2)	\$ -	\$ (5.3)	\$
Depreciation and amortization	2.5	2.3	-	0.1	
EBITDA	\$ 22.8	\$ 1.1	\$ -	\$ (5.2)	\$

Six months ended December 31, 2005

	Marketing Services	Personals	Management Services	Corporate	To
Net income					\$
Interest and other expense, net (1)					
Provision for income taxes (1)					
Operating income (expense)	\$ 47.8	\$ (0.8)	\$ 0.5	\$ (13.0)	\$
Depreciation and amortization	6.3	4.8	0.8	0.6	
EBITDA	54.1	4.0	1.3	(12.4)	
Change in deferred revenues	(10.2)	(0.1)	(0.3)	-	
Change in deferred marketing	6.0	-	-	-	
Adjusted EBITDA	\$ 49.9	\$ 3.9	\$ 1.0	\$ (12.4)	\$

Edgar Filing: VERTRUE INC - Form 10-Q

26

VERTRUE INCORPORATED
 ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS
 OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

	Six months ended December 31, 2004				
	Marketing Services	Personals	Management Services	Corporate	Total
Net income					\$
Interest and other expense, net (1)					
Provision for income taxes (1)					
Operating income (expense)	\$ 42.3	\$ (1.3)	\$ -	\$ (10.5)	\$
Depreciation and amortization	4.7	4.7	-	0.2	
EBITDA	47.0	3.4	-	(10.3)	
Change in deferred revenues	(19.5)	0.1	-	-	
Change in deferred marketing	8.7	-	-	-	
Adjusted EBITDA	\$ 36.2	\$ 3.5	\$ -	\$ (10.3)	\$

1) Management does not allocate interest and other expense, net nor does it allocate provision for income taxes to the individual segments.

Free cash flow represents net cash provided by operating activities less capital expenditures. Free cash flow is important because it represents the cash that is available to a company to pursue opportunities that enhance shareholder value, such as make acquisitions, reduce debt and develop new products. The following table reconciles operating cash flow to free cash flow (in millions):

	Six months ended December 31,	
	2005	2004
Net cash provided by operating activities	\$ 14.8	\$ 14.6
Capital expenditures	(6.5)	(4.3)
Free cash flow	\$ 8.3	\$ 10.3

COMMITMENTS

The Company is not aware of any factors that are reasonably likely to adversely affect liquidity trends, other than the risk factors presented in the Forward-Looking Statements in this Quarterly Report on Form 10-Q. The Company does not have off-balance sheet arrangements, non-exchange traded contracts or material related party transactions.

Future minimum payments of contractual obligations as of December 31, 2005 are as follows (in millions):

Edgar Filing: VERTRUE INC - Form 10-Q

	Payments Due by Period				
	Total	Less than 1 year	1 - 3 years	3 - 5 years	After 5 years
Operating leases	\$ 53.1	\$ 9.3	\$ 17.2	\$ 13.2	\$ 13.4
Capital leases	1.7	0.8	0.9	-	-
Long-term debt	240.0	-	-	90.0	150.0
Purchase obligations	24.8	22.3	2.5	-	-
Other (1)	157.8	29.4	37.7	38.0	52.7
Total payments due	\$ 477.4	\$ 61.8	\$ 58.3	\$ 141.2	\$ 216.1
	\$ 477.4	\$ 61.8	\$ 58.3	\$ 141.2	\$ 216.1

(1) Includes interest payments on long-term debt, pension obligations and expected contingent payments related to the MCM acquisition.

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements that are based on current expectations, estimates, forecasts and projections about the industry in which the Company operates and management's beliefs and assumptions. These forward-looking statements include statements that do not relate solely to historical or current facts and can be identified by the use of words such as

27

VERTRUE INCORPORATED ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

"believe," "expect," "estimate," "project," "continue" or "anticipate." These forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, are intended to qualify for the safe harbor provisions from liability provided by the Private Securities Litigation Reform Act of 1995.

Forward-looking statements are not guarantees of future performance and are based on many assumptions and estimates that are inherently subject to significant risks and uncertainties, many of which are beyond our control, cannot be foreseen and reflect future business decisions that may change. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. Among the many factors that could cause actual results to differ materially from the forward-looking statements are:

- o higher than expected membership cancellations or lower than expected membership renewal rates;
- o changes in the marketing techniques of credit card issuers;
- o increases in the level of commission rates and other compensation required by marketing partners to actively market with the Company;
- o potential reserve requirements by business partners, such as the Company's credit card processors;
- o unanticipated termination of marketing agreements;
- o the extent to which the Company can continue to successfully develop and market new products and services and introduce them in a timely

Edgar Filing: VERTRUE INC - Form 10-Q

- manner;
- o the Company's ability to integrate acquired businesses into the Company's management and operations and operate successfully;
- o unanticipated changes in or termination of the Company's ability to process revenues through third parties, including credit card processors and bank card associations;
- o the Company's ability to develop and implement operational and financial systems to manage growing operations;
- o the Company's ability to recover from a complete or partial system failure or impairment, other hardware or software related malfunctions or programming errors;
- o the degree to which the Company is leveraged;
- o the Company's ability to obtain financing on acceptable terms to finance the Company's growth strategy and to operate within the limitations imposed by financing arrangements;
- o the Company's ability to obtain new financing or re-finance existing debt;
- o further changes in the already competitive environment for the Company's products or competitors' responses to the Company's strategies;
- o changes in the growth rate of the overall U.S. economy or the international economy where the Company does business such that credit availability, interest rates, consumer spending, related consumer financing and related consumer debt are affected;
- o additional government regulations and changes to existing government regulations of the Company's industry;
- o the Company's ability to compete with other companies that have financial or other advantages;
- o adverse movements of foreign exchange rates;
- o the Company's ability to attract and retain active members and users;
- o adverse results of litigation or regulatory matters; and
- o new accounting pronouncements.

Many of these factors are beyond the Company's control and therefore its business, financial condition, results of operations and cash flows may be adversely affected by these factors.

The Company cautions that these factors are not exclusive. All forward-looking statements made in this Quarterly Report on Form 10-Q are qualified by these cautionary statements and readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this Quarterly Report on Form 10-Q. Except as otherwise required by federal securities law, the Company has no obligation and does not intend to publicly update or revise any forward-looking statements to reflect subsequent events or circumstances.

28

VERTRUE INCORPORATED

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate

The Company has a senior secured credit facility which allows borrowings of up to \$45.0 million. Borrowings under this senior secured credit facility accrue interest at either the Eurodollar rate or the higher of the Prime rate or the Federal Funds rate plus an applicable margin. There were no borrowings outstanding under this senior secured credit facility as of December 31, 2005. As of December 31, 2005, the effective interest rate for borrowings under the

Edgar Filing: VERTRU INC - Form 10-Q

senior secured credit facility was 7.25%. Management believes that an increase in the Eurodollar rate, the Prime rate or the Federal Funds rate would not be material to the Company's financial position or its results of operations. The bank credit facility matures on March 23, 2006 and management expects it to be renewed or replaced during the third quarter of fiscal 2006.

In addition, the Company has \$90.0 million aggregate principal amount of 5.5% Convertible Notes due 2010 and \$150.0 million aggregate principal amount of 9.25% Senior Notes due 2014. The Convertible Notes and the Senior Notes pay interest in cash semi-annually in arrears on April 1 and October 1. The fair value of the fixed interest instruments is affected by changes in interest rates and, with respect to the Convertible Notes, by changes in the Company's stock price and volatility. The Company does not currently hedge interest rates with respect to its outstanding debt. As of December 31, 2005, the carrying value of the Convertible Notes and the Senior Notes was \$90.0 million and \$147.9 million, respectively, and the fair value of the notes was \$95.9 million and \$155.2 million, respectively. Cash paid in connection with interest on the Convertible Notes and the Senior Notes in each of the next five years is expected to be \$18.8 million assuming none of the notes is converted into equity.

Foreign Currency

The Company conducts business in certain foreign markets, primarily Canada. The Company's primary exposure to foreign currency risk relates to investments in foreign subsidiaries that transact business in functional currencies other than the U.S. dollar, primarily the Canadian dollar. The Company's recent acquisitions, which are based in the United States, have reduced the proportion of its operations exposed to potentially volatile movements in currency exchange rates. The economic impact of currency exchange rate movements on the Company is often linked to variability in real growth, inflation, interest rates, governmental actions and other factors. These changes, if material, could cause the Company to adjust its financing and operating strategies. As currency exchange rates change, translation of the income statements of the Company's international businesses into U.S. dollars affects year-to-year comparisons of operating results.

The Company uses purchase option contracts and forward contracts to minimize its exposure to certain changes in future cash flows caused by movements in foreign currency exchange rates between the U.S. dollar and the Canadian dollar. However, there can be no assurance that the Company's foreign currency hedging activities will substantially offset the impact of all fluctuations in currency exchange rates on its results of operations, cash flows and financial position. The Company does not use derivatives for speculative purposes. Derivatives used to hedge forecasted transactions and specific cash flows associated with Canadian dollar denominated financial assets and liabilities that meet the criteria for hedge accounting are designated as cash flow hedges. The effective portion of gains and losses is deferred as a component of accumulated other comprehensive income and is recognized in earnings in the same line item as the underlying hedged item at the time the hedged item affects earnings.

Fair Value of Investments

The Company does not have material exposure to market risk with respect to investments since the Company's investments are short-term in nature (original maturities of less than one year).

Item 4. Controls and Procedures

Evaluation of disclosure controls and procedures

The Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined under Rules 13a-15(e) and 15d-15(e) of the Securities and Exchange Act of 1934) as of the end of the period covered by this report and

Edgar Filing: VERTRUE INC - Form 10-Q

have concluded that the Company's disclosure controls and procedures were effective at the reasonable assurance level. The Company's disclosure controls and procedures are designed to ensure that material information relating to the Company and its consolidated subsidiaries that is required to be disclosed in its reports under the Exchange Act is accumulated, communicated to the Chief Executive Officer and Chief Financial Officer and disclosed appropriately and timely in its reports under the Exchange Act.

Because a cost-effective control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met, misstatements due to error or fraud may occur and not be detected. In addition, projections of any evaluation of

29

VERTRUE INCORPORATED

effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

Changes in internal control over financial reporting
During the second quarter of 2006, there were no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

30

VERTRUE INCORPORATED PART II. OTHER INFORMATION

Item 1. Legal proceedings

Except as set forth below, in management's opinion, there are no significant legal proceedings to which the Company or any of its subsidiaries is a party or to which any of their properties is subject. The Company is involved in other lawsuits and claims generally incidental to its business including, but not limited to, various suits, including previously disclosed suits, brought against the Company by individual consumers seeking monetary and/or injunctive relief relating to the marketing of the Company's programs. In addition, from time to time in the regular course of its business, the Company receives inquiries from various federal and/or state regulatory authorities.

On October 17, 2005, the U.S. Supreme Court declined to review the Connecticut Supreme Court's May 10, 2005 decision against the Company to uphold an arbitration panel's award of \$5.5 million in punitive damages and costs to MedValUSA Health Programs, Inc. Accordingly, the Company paid the full amount of the award in the quarter ending December 31, 2005. The Company recorded a one-time \$5.5 million charge in the quarter ended June 30, 2005 related to this award. For additional information about the MedValUSA Health Programs, Inc. arbitration, refer to Item 3 - "Legal Proceedings" in the Company's Annual Report on Form 10-K for the year ended June 30, 2005.

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

Edgar Filing: VERTRUE INC - Form 10-Q

The following table summarizes the shares of the Company's equity securities purchased by or on behalf of the Company:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number Shares Purchased as Part of Public Announced Programs or Programs
-----	-----	-----	-----
October 1, 2005 to October 31, 2005	2,200	\$35.82	
November 1, 2005 to November 30, 2005	67,600	37.27	6
December 1, 2005 to December 31, 2005	45,100	36.58	4
	-----		-----
Total	114,900	36.97	11
	=====		=====

- (1) In October 2004, the Board of Directors authorized an additional 1,000,000 shares, no expiration date, to be purchased under the Company's stock repurchase program originally authorized during fiscal 1997.

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

The Company's 2005 Annual Meeting of Stockholders was held on November 17, 2005.

At the annual meeting, the following Directors were elected to the Board of Directors for a term of one year:

Name	For	Withheld
----	---	-----
Alec L. Ellison	8,745,784	279,372
Joseph E. Heid	8,542,519	482,637
Gary A. Johnson	8,826,661	198,495
Robert Kamerschen	8,501,452	523,704
Michael T. McClorey	8,807,707	217,449
Edward M. Stern	8,730,623	294,533
Marc S. Tesler	8,542,519	482,637

31

VERTRUE INCORPORATED PART II. OTHER INFORMATION

At the annual meeting, the following proposals were approved:

To approve an amendment to the 2004 Long-Term Incentive Plan:

For	6,699,578
Against	213,178
Abstain	13,445
Nonvotes	2,098,945

To approve the adoption of the 2005 Equity Incentive Plan:

For	3,972,914
Against	2,939,842

Edgar Filing: VERTRUE INC - Form 10-Q

Abstain	13,455
Nonvotes	2,098,945

To ratify PricewaterhouseCoopers LLP as the independent auditors:

For	8,925,645
Against	99,511
Abstain	0
Nonvotes	0

Item 6. Exhibits

Exhibits

- 31.1 Rule 13a-14(a) CEO Certification.
- 31.2 Rule 13a-14(a) CFO Certification.
- 32.1 CEO Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 CFO Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32

VERTRUE INCORPORATED
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.

VERTRUE INCORPORATED
(Registrant)

Date: February 9, 2006

By: /s/ Gary A. Johnson

Gary A. Johnson, President, Chief
Executive Officer and Director

February 9, 2006

By: /s/ James B. Duffy

James B. Duffy, Executive Vice President
and Chief Financial Officer (Principal
Financial and Accounting Officer)

33