DIGITAL INSIGHT CORP
Form 10-K
March 16, 2006
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2005

Commission File Number 0-27459

DIGITAL INSIGHT CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**77-0493142**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

26025 Mureau Road, Calabasas, California 91302

(Address of principal executive offices, including zip code)

(818) 871-0000

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, $0.001 par value per share

(Title of Class)

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

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

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

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

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 Act). YES ¨ NO x

Based on the closing sale price of $23.92 as reported by the Nasdaq National Market System on June 30, 2005, the last business day of the registrant s most recently completed second fiscal quarter, the aggregate market value of the registrant s common stock held by non-affiliates was $577.5 million. The shares of common stock held by each officer and director and by each person known to the registrant who owns 5% or more of the outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes. As of February 28, 2006, registrant had 34,827,596 shares of its common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s proxy statement for the 2006 annual meeting of stockholders are incorporated by reference into Part III of this Annual Report on Form 10-K to the extent stated herein. The proxy statement will be filed within 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

Table of Contents

INDEX

Table of Contents

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

In addition to historical information, this Annual Report on Form 10-K as well as other statements made or to be made by Digital Insight in periodic press releases and other public communications contain forward-looking statements that involve risks and uncertainties. These statements relate to future events or our future financial performance. In some cases, you can identify forward-looking statements by terminology such as may, will, should, expect, anticipate, intend, plan, believe, estimate, potential, continue, the negative o comparable terminology. These statements are only predictions. Actual events or results may differ materially from any forward-looking statement. In evaluating these statements, you should specifically consider various factors, including the risks outlined under Risk Factors in Item 1A of Part I.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of the forward-looking statements. We undertake no obligation to update publicly any forward-looking statements for any reason after the date of this Annual Report on Form 10-K.

INFORMATION ABOUT DIGITAL INSIGHT

We file annual, quarterly and current reports, proxy statements, and other documents with the Securities and Exchange Commission, or the SEC, under the Securities Exchange Act of 1934, or the Exchange Act. You may read and copy any materials that we file with the SEC at the SEC s Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Our reports, proxy statements, and other documents filed electronically with the SEC are available at the website maintained by the SEC at *http://www.sec.gov*.

We also make available free of charge on or through our Internet website at *http://www.digitalinsight.com* our annual, quarterly, and current reports, and, if applicable, amendments to those reports, filed or furnished pursuant to Section 13(a) of the Exchange Act as soon as reasonably practicable after we electronically file such reports with, or furnish them to, the SEC.

Table of Contents

PART I

ITEM 1. BUSINESS

Overview

We are a leading provider of outsourced online banking applications and services to banks, credit unions and savings and loan associations, serving more than 1,700 client financial institutions. We offer outsourced software products that are hosted in our data centers and delivered as an on-demand service offering to financial institutions, generally with under $20 billion in assets. Although we support our clients through a single version of software and common, multi-tenant data center infrastructure, our products are highly configurable to provide a look and feel that preserves the financial institution s unique brand identity. Our contracts with financial institutions are long-term in nature, generally ranging from three to five years. Our clients pay monthly fees that are generally variable with growth in active end users and the number of transactions. More than 90% of our revenues was derived from recurring service fees during 2005.

Our outsourcing operations include three main product lines: online banking for consumers, which also includes bill payment and bill presentment; online banking for businesses (also referred to as business banking); and online lending for consumer loans. We also offer online business banking products to large financial institutions that are available either as a licensed software implementation or hosted in our data centers. Our broad capabilities within online business banking allow us to serve all tiers of financial institutions and their business customers of all sizes. Our clients benefit from an extensive portfolio of complementary products and services that add value to our core offerings, including online check imaging, online statements, target marketing, online account opening, multi-language support, web portal technology, web site development and maintenance, and professional services.

In contrast to in-house software deployments that require significant development resources and lengthy installations, we provide comprehensive Internet applications that can be implemented rapidly and cost-effectively. By using our applications, financial institutions can keep pace with rapid advancements in Internet technology and large development expenditures by large banks without placing demands on in-house technical resources. We also help our clients generate a higher return on investment with our cooperative marketing and support programs, which promote end user adoption and cross-selling. Our comprehensive suite of products enables our clients to generate higher revenues from increased loan and account balances, to increase customer retention and to lower their costs to serve customers by promoting self-service functions available on the Internet.

Since our inception in 1995, we have established a growing range of strategic relationships with the industry s leading data processing vendors to ensure that financial institutions can leverage their investments in existing data processing systems by fully integrating them with our Internet applications. In recent years, we have also established a growing network of relationships with more than 100 developers of third party products that complement our core offerings with full interoperability and integration. Our scale and large client base typically allow us to negotiate more favorable pricing terms with these vendors and preferential support for new product releases relative to other online banking vendors that have less purchasing influence.

Our applications also offer high levels of security, up-time availability and system redundancy, and are designed to be readily expandable, or scalable, as the number of end users grows. We believe our data center facilities are large enough to support our expected growth for the next several years.

We have a large opportunity to grow our future revenues by increasing end user adoption among our current customers. As of December 31, 2005, 6.3 million consumer end users were actively using our Internet banking applications, representing 16.9% penetration of the 37.0 million potential end users among our live Internet banking clients. Of the 6.3 million active Internet banking end users, 1.4 million end users were signed up for our online bill payment service, representing 23.1% of active Internet banking users. As of December 31, 2005, 106,300 business end users were actively using our outsourced business banking solutions.

[Table of Contents](#)

We began operations in 1995. Our company was originally organized as a Minnesota limited liability company, which was then converted to a Delaware corporation in 1997.

Industry Background

Consumers, businesses and financial institutions increasingly recognize that the Internet is a powerful and efficient medium for the delivery of financial services, including Internet banking, bill payment and bill presentment, online lending, and a host of other services for retail and business customers of financial institutions. Consumers and businesses increasingly bank online because of the convenience of remote access to account information 24 hours a day, 7 days a week, the rapid growth of broadband technologies that encourage higher Internet use, and generally increasing product awareness and comfort with conducting financial transactions online. According to Jupiter Research, 55 million U.S. households will bank online by 2010, up from 38 million in 2005. Similarly, Forrester Research predicts that the number of households paying bills online at a bank web site will double from 15 million in 2005 to 30 million in 2010.

For financial institutions, the Internet offers a cost-effective service delivery channel from which to market a broad portfolio of products and services in an effort to strengthen and secure customer relationships and generate higher revenues. The Internet channel also enables financial institutions to expand their addressable markets and maintain service availability 24 hours a day, 7 days a week. In addition, a growing body of industry research and case studies, including recent analysis from Forrester Research, Celent, Bank of America and Citibank, has demonstrated that Internet banking and online bill payment end users are more profitable to serve because online users:

- generate significantly higher revenues than offline customers, primarily because online customers use more banking products and services, and maintain higher account balances than offline customers;

- cost less to serve because online users tend to utilize more self-service functions and therefore interact with the more costly retail branch and call center service channels less frequently than offline customers; and

- are retained by financial institutions at significantly higher rates than offline customers.

Research published by Bank of America demonstrated that end users of the bank s online bill payment service experienced attrition that was 80% lower than offline customers, and were 31% more profitable than offline customers within 31 months. Citibank also reported that its online customers are 40% more profitable than customers who do not bank online. Consequently, seven of the top 10 U.S. financial institutions have eliminated their monthly customer fees for online bill payment in recent years and launched aggressive marketing campaigns to promote adoption of the online channel. In response, a fast-growing segment of smaller financial institutions have initiated similar campaigns, increasing the adoption of bill payment throughout the industry, particularly among the two-thirds of U.S. consumers who will not pay for bill payment services, according to Forrester estimates.

The largest U.S. financial institutions generally develop and maintain an internally hosted solution for the delivery of online financial services such as Internet banking. By contrast, we believe that the majority of the approximately 18,000 credit unions, banks, and savings and loans in the U.S. with assets of less than $20 billion prefer to outsource the development and maintenance of their online banking initiatives to a technology services provider. These community and regional financial institutions increasingly seek to provide advanced Internet-based services to remain competitive, but frequently lack the capital, expertise, or information technology resources to offer such services in-house. Increased regulatory requirements, including new mandates for online security in 2006, have created additional complexity and provided financial institutions greater incentives to consider outsourcing their online banking channel.

Table of Contents

Our Business

We provide a comprehensive portfolio of outsourced online banking software products that are hosted in our data centers and delivered as an on-demand service offering to financial institutions with under $20 billion in assets. We generate recurring revenues that are generally variable with growth in active Internet banking end users and user transaction volume. Our contracts with financial institutions are long-term in nature, generally ranging between three to five years. More than 90% of our revenues were derived from recurring service fees in 2005.

Our three core product offerings are Internet banking, business banking and lending. Our Internet banking applications for consumers include: account management, account transfers and interfaces to personal financial management software, bill payment and bill presentment, check imaging, online statements, multi-language support, inter-institutional funds transfer, online account opening and other expanded services. Our business banking software products serve the online banking needs of our clients business customers and include features similar to those of our consumer product, as well as payroll direct deposits, wire and inter-account fund transfers, account reconciliation, foreign exchange trade, and other services. Our business banking software products can be deployed as a licensed software implementation or hosted in our data centers. A licensed implementation allows financial institutions to host our software using their own equipment and facilities. We have a versatile business banking product line that allows us to serve all tiers of financial institutions and their business customers of all sizes. Supporting products and services for consumer and business online banking include web portal technology, wireless capability, target marketing, professional services, and web site development and maintenance.

Our lending software products and related services are hosted in our data center and delivered as an on-demand service offering to client financial institutions. Our lending platforms streamline our clients lending operations for non-mortgage consumer loans across multiple customer service channels, including back office administrative functions such as document preparation. Lending products and services include a loan origination system for automating workflow throughout the loan approval process, an Internet-based, real-time loan decisioning product, multi-channel automated underwriting services, and call center services to support loan applicants and general customer support inquiries on behalf of our clients, 24 hours a day, 7 days a week.

We offer the following benefits to financial institutions:

Comprehensive and Customizable Solutions. We offer turnkey, subscription-based products and services with all critical applications hosted in our data centers. Our online banking applications can be configured to offer financial institutions and end users the industry s broadest portfolio of standard and optional features, including applications developed internally and in cooperation with our extensive network of product partners. Our web site design and implementation services also enable financial institutions to establish Internet banking services with a look and feel that preserves their unique brand identity.

Rapid and Affordable Implementation. Our applications can be rapidly implemented, and represent an affordable alternative to internally developed Internet banking applications for financial institutions. Average implementation times for our Internet banking applications range from four to six months, depending on the availability of an existing interface with a financial institution s data processing vendor and the financial institution s schedule.

Reliable, Secure, and Scalable Service. Our service is highly reliable. Our systems incorporate sophisticated data encryption techniques, a series of firewalls between the Internet and financial institutions, and several layers of security technology in order to guard against unauthorized access to our network. In addition, our data centers and systems have the capacity to scale rapidly to accommodate an increased number of end users and transactions.

Extensive Data Processing Vendor Relationships. We provide direct connections, or interfaces, to many vendors of core banking software and data processing services to financial institutions. As of

Table of Contents

December 31, 2005, we have developed interfaces to a majority of the major data processing vendors serving our addressable market of financial institutions. By working directly with these vendors, we can quickly and cost-effectively connect our systems allowing relatively more rapid implementation of new customers to the same core processing system. Our interfaces also allow for tight integration with other functions supported by the data processing vendor, such as loan origination, online statements and check imaging. We believe that the number of data processing vendor interfaces we have developed provides us with a unique and significant competitive advantage.

Uniquely Broad Set of Value-Added Products. We enable financial institutions to expand their Internet presence beyond their core banking functions by providing additional value-added products and services to their customers. We believe our product suite offers the broadest capabilities in the industry, including: online bill payment and bill presentment, online lending, online business banking, check imaging, account aggregation, inter-institutional payments, online statements, check reordering, target marketing software, multi-language support, online account opening, professional services, and training seminars. We maintain an extensive network of vendors that have cooperatively developed many of our value-added products and services.

Cooperative Marketing Programs. Our cooperative marketing programs encourage higher end user adoption of the online channel through a series of direct marketing and promotional tools including direct mail, in-branch displays, training programs, online banner advertisements, statement stuffers, and email campaigns.

Our Strategy

Our objective is to further enhance our position as a leading provider of online banking and related online solutions to financial institutions for their retail and business customers. We intend to provide these institutions with a competitive platform that will permit them to achieve additional revenue-producing opportunities, enhance long-term cost-efficiencies, and improve customer service and client retention. To achieve this objective, we intend to:

Increase End User Penetration. As of December 31, 2005, our financial institutions with live Internet banking sites had an average penetration of 16.9% for consumer online banking, and 23.1% of these online banking users were also registered for online bill payment. Although our penetration has grown rapidly, these averages are well below levels achieved by industry-leading financial institutions that have reported online banking penetration in excess of 50%. We believe our base of 37.0 million potential consumer end users among our live Internet banking clients provides a large opportunity to increase our revenues as end user adoption increases in the future. We help clients expand the number of active end users of our Internet banking and bill payment applications through marketing assistance programs and by sharing best practices. These cooperative marketing programs enable clients to increase their returns from the online channel through increased revenue opportunities, lower customer attrition, and reduced service costs.

Pursue Cross-Selling Opportunities Within Our Existing Customer Base. We currently enable financial institutions to offer Internet banking applications and automated lending capabilities to their retail and business customers. We believe that we have a significant opportunity to sell our comprehensive suite of products and services to existing customers as their needs evolve and their customer base expands. For example, at December 31, 2005, we had contracts with 214 financial institutions for our lending products and 644 financial institutions for our business banking products, demonstrating the cross-sale opportunity within our total customer base of 1,748 financial institutions.

Attract New Financial Institution Customers, Particularly Conversions From Competitive Platforms. We intend to further penetrate the substantial market for online banking applications. As of December 31, 2005, we had contracts with 1,748 financial institutions of the estimated 18,000 financial institutions in the U.S. under $20 billion in assets. Although we continue to contract with financial

Table of Contents

institutions that have yet to offer online banking, we primarily target institutions that currently offer online services and may demand a broader range of product functionality than offered by their current vendor, or those institutions evaluating a move to a fully outsourced online banking solution from an in-house system.

Retain Existing Customers. Approximately 20%-25% of our client base is subject to contract renewals each year. We intend to maximize client retention through a dedicated account management team, aggressive utilization of sales resources, a strategic approach to managing of key accounts, and other initiatives.

Increase Our Relationships with Core Data Processing Vendors. We intend to increase the number of our relationships with core data processing vendors to allow our applications to interface with more financial institutions and to expand our sales and distribution channel relationships. We currently interface with most of the major vendors that provide data processing services to the financial institutions in our addressable market. We intend to continually increase this coverage and to expand our existing relationships. We believe our uniquely broad portfolio of available products, financial strength, large client base and highly reliable data centers make us an attractive partner for core data processors.

Broaden Product and Service Offerings. We plan to continue to offer new and enhanced products and services to provide our customers with a comprehensive range of capabilities they need to compete effectively. In coming years, we intend to introduce several new products to enable our customers to better compete against larger financial institutions. Our product plans include internal development efforts and an increasing focus on introducing products in cooperation with other vendors. We believe our large client base allows us to negotiate the best available pricing terms with other vendors and receive preferential support for new product releases relative to smaller Internet banking providers with less purchasing influence. Our increasing focus on relationships with other vendors will allow us to introduce products more quickly and with reduced capital investment than if we relied solely on internal development efforts.

Pursue Strategic Merger and Acquisition Opportunities. We intend to continue to evaluate opportunities to acquire businesses that could expand our base of financial institution customers, add complementary technologies or services, or provide other benefits.

Products and Services

Consumer Internet Banking

We offer a broad range of outsourced Internet banking products and services for our financial institution clients retail customers that include the following features:

View online transaction history, account balances, check images, and statements.

Online bill payment capability to pay anyone through the financial institution s web site.

Online bill presentment capability to receive, view, pay and store electronic bills online.

Two-way data transfer with Microsoft Money® and Intuit Quicken® financial software.

Secure online applications to open new accounts, and apply for credit cards, insurance, loans or other products.

Inter-institutional and person-to-person payments outside the financial institution.

Wireless banking and alerts through mobile devices.

Promotion and marketing tools to allow financial institutions to market to online users.

E-commerce web portal for marketing third-party financial products.

Table of Contents

Web site design, development, maintenance, and implementation services.

Funds transfer between accounts, current or scheduled.

Re-ordering of checks online.

Online account opening and funding capabilities for new deposit accounts.

Business Banking

Our business banking products serve the business customers of our financial institution clients. We generally provide our business banking products on an outsourced basis; however, we also offer a licensed software option for large financial institutions. Primary features include:

Online administration platform to control access among business users.

View online transaction history and balance information.

Funds transfer between accounts, current or scheduled.

Stop payments for previously issued checks.

File export to business financial management software.

Bill payment and bill presentment.

Automated clearing house (ACH) services for payroll and other payments.

Wire transfers with other financial institutions or vendors.

Foreign exchange rates and trading.

Check reconciliation services.

Lockbox reporting and viewing of lockbox deposit detail.

Online payroll services.

Through December 31, 2003 we managed the business banking business within Internet banking. With the acquisition of Magnet Communications, Inc., or Magnet, on November 25, 2003, we expanded our business banking products and services and consequently we established business banking as a separate reportable business segment on January 1, 2004.

Consumer Lending

Our lending products provide, on a fully outsourced basis, loan origination capabilities and rules-based underwriting on behalf of our financial institution clients, applying client-specific and client-defined rules to reach a credit decision. We support a wide range of consumer loans including home equity, auto loans and personal loans. We do not support mortgage lending or bear any of the underwriting or financial risk for the loans we service. We charge our clients a predetermined fee per loan application regardless of whether the loan is approved and a fixed monthly maintenance fee for clients utilizing our loan origination system. Lending products are configured to support multiple service channels to match consumer preferences and include:

A loan origination system that manages workflow throughout the lending process, document preparation, and related back-office and administrative functions.

Real-time loan evaluation over the Internet for consumer loans, including the retrieval of an electronic credit report and a credit decision response to the applicant, generally in less than a minute.

Loan evaluation through a 24 hours a day, 7 days a week call center staffed with trained loan officers.

Table of Contents

Loan evaluation by the financial institution client s loan officer, using our Internet-based product for desktop decisioning within the retail branch.

Our lending underwriting products feature interfaces to our loan origination system as well as other major loan origination vendors, online credit bureau verification, and pre-qualification capabilities for home equity and consumer loans.

Data Centers

We currently provide our Internet banking services out of our main data center located in Westlake Village, California. Our disaster recovery data center in Norcross, Georgia allows for emergency backup and disaster recovery functions in the event of system interruption or shutdown involving the Westlake Village data center.

Both data centers maintain a controlled access environment with security measures ranging from alarms, video cameras, security guards, biometric access controls and a centrally monitored key card access system. Our data centers are also equipped with a self-contained power system that includes a high capacity battery backup system, providing continuous power to all production systems. In addition, diesel power generators provide backup power to each of our facilities in the event of an extended power outage. We maintain and test our Norcross disaster recovery data center to provide system redundancy, fail-over and emergency backup capabilities.

We believe our data center facilities are large enough to support our expected growth for the next several years.

Customers

As of December 31, 2005, we had contracts with 1,748 financial institutions, including 1,505 for Internet banking services, 644 for business banking services and 214 for lending services. We had approximately 6.3 million active Internet banking end users representing a 16.9% penetration of the 37.0 million potential end users among 1,400 live client sites at December 31, 2005.

For the year ended December 31, 2005, no individual financial institution accounted for over 10% of our total revenues.

Third Party Relationships

We have relationships and have developed interfaces with most of the major vendors of core data processing software and outsourced data processing services to financial institutions. These system interfaces enable us to access a financial institution s host system to provide end users access to their account data. In addition to developing new interfaces, we continue to significantly enhance our many existing interfaces in order to deliver more robust connectivity and increase operating efficiencies. We have developed interfaces to the majority of the core data processing systems that provide services to financial institutions, most of which are supported within joint marketing arrangements that we have in place with data processing vendors. More than 50% of our revenue is derived from these referral and reseller agreements with core processing vendors, including Fiserv, BISYS, Fidelity Information Services, Inc., Metavante (including Kirchman Corp., its affiliate), Computer Services Inc., Data Center Inc., re:Member Data (a division of Open Solutions, Inc.), Harland Financial Solutions, Bradford Scott, and BMA.

To deliver bill payment and bill presentment services, we maintain value-added reseller relationships with major providers such as Metavante Corporation and CheckFree Services Corporation, and have fully integrated these products into our offerings. We market bill payment and bill presentment services as an integral part of our product suite, enabling financial institutions to offer bill payment within their online banking site with the convenience of a single password. Our agreement with Metavante expires in June 2010. Our agreement with CheckFree is renewable for additional one-year terms following the expiration of the initial term in September 2007. Our agreements require us to pay variable fees based on factors such as the number of bill payment transactions, customers, and end users, and generally provide improved pricing terms as transaction volumes increase.

We entered into an outsourcing agreement with PSCU Financial Services, or PSCU, a credit union service organization, to provide outsourced call center services to Digital Insight clients through 2012. As of December 31, 2005, we were in the process of migrating clients served by our call center to call centers operated by PSCU. We also entered into a license and reseller agreement with PSCU through 2010, whereby PSCU has licensed our new lending platform and named Digital Insight as its preferred provider of Internet banking, business banking and lending products to PSCU clients. The license and reseller agreements include minimum payments to us beginning in 2006.

Sales and Marketing

We sell to our customers and potential customers primarily utilizing a direct sales model and, to a lesser extent, in cooperation with core processing partners. As of December 31, 2005, our sales, marketing and client relations staff consisted of 95 people, who are responsible for prospecting and acquiring new accounts, managing existing client relationships and renewals, and cross-selling additional products to those accounts. Our sales and account management team is primarily organized by financial institution asset size and location.

Our target market for outsourced online consumer Internet banking, business banking and consumer lending services is comprised of small to medium sized financial institutions seeking a comprehensive Internet solution to compete with the larger national banks in their market. The majority of our sales opportunities are with financial institutions evaluating a conversion from a competitive Internet banking platform, often in response to increased functionality demands among end users. To a lesser degree, we continue to market to newly-created banks and other financial institutions that have yet to offer online banking to their customers.

Our typical sales cycle is approximately six to eight months for new financial institution customers and approximately two months for add-on sales to existing financial institution customers. We have a dedicated account management and sales staff to manage the client renewal process, and a sales compensation plan that rewards client retention. Our account managers identify customers whose contracts are subject to renewal with sufficient lead-time to allow the customer, our sales staff, and executive sponsors to manage the renewal process and maximize client retention.

Our primary marketing efforts are focused on identifying potential customers and marketing our services to consumer end users in cooperation with our financial institution clients. Our marketing efforts include: press relations, advertising, direct mail, trade show meetings with Internet banking user groups, and client conferences hosted by us and our core processing partners. We also offer cooperative marketing programs for existing customers, under which financial institutions partner with us to promote higher adoption and retention of the online channel, and cross-selling of additional products to online end users. Sales compensation plans are aligned with our primary goal of increasing online adoption among our customer base.

In addition, we receive marketing benefits from endorsements and promotional arrangements. We are exclusively endorsed by the American Bankers Association, or ABA, for our Internet banking product. The ABA endorsement, issued by the Corporation for American Banking, or CAB, an ABA subsidiary, was granted to us after an extensive due diligence process which included an analysis of our management, financial soundness, solution functionality, marketing capabilities and customer service standards, as well as a review of other national providers of Internet banking solutions. Our endorsement agreement requires CAB to promote our Internet banking services to all ABA members in the United States and permits us to display the American Bankers Association-Sponsored logo in all of our marketing materials related to Internet banking services. We provide CAB with a small percentage share of the revenues received from ABA members who have become our customers since the effective date of the endorsement agreement, subject to annual minimum payments. In addition, we have promotional arrangements with several state banking associations that promote our products to their constituents in exchange for referral fees.

Product Development

As of December 31, 2005, our product development staff consisted of 254 software developers and engineers, as well as product and project managers. Their development efforts are focused on:

- *Enhancements to Existing Products.* We are continuously developing new features and functions for our consumer and business banking and lending products in order to provide a broader range of capabilities. Additional product enhancements will provide greater usability for our financial institution clients and their end users.

- *Introduction of New Product Lines Through Internal Development.* We are continuously seeking to expand our product offerings. For example, we recently introduced a loan origination system to complement our lending underwriting products, and to allow our customers to streamline workflow and administrative functions throughout the lending process.

- *Introduction of New Product Lines Provided by Technology Vendors.* We are increasingly committed to expanding our product portfolio by introducing new products through relationships with technology vendors. For example, we recently entered into an agreement with CashEdge to introduce a product that allows consumers to open and fund new deposit accounts online within a single Internet session. During 2006, we will also introduce a multi-factor authentication solution in conjunction with a technology vendor. Multi-factor authentication is a security feature that helps protect end users from online fraud by implementing enhanced user-verification during account login beyond username and password.

- *Interfaces with Data Processing Vendors and Other Third Parties.* We are continuing to enhance and expand our interfaces to financial institutions core data processing systems and other third-party systems, such as vendors of online check imaging systems.

Our research and development expenses were $23.9 million in 2005, $23.4 million in 2004, and $15.6 million in 2003. These expenses relate to product development and are charged to operations as incurred.

Competition

The market for Internet banking services is highly fragmented with many providers. In the area of retail Internet banking, we primarily compete with other companies that provide outsourced online banking services to financial institutions, including Online Resources, S1 Corporation and FundsXpress. Also, vendors such as Corillian and Financial Fusion (a subsidiary of Sybase) that primarily target the largest financial institutions occasionally compete with us in our market segment. In addition, Fiserv, Open Solutions, Jack Henry, Metavante and several other vendors of data processing services to financial institutions offer their own online banking products, although many of these firms also offer our products through a referral or reseller arrangement with us to clients demanding a broad set of online capabilities.

Our primary competitors in the business banking services segment are vendors of business banking systems for large corporations such as P&H Solutions, BankLink, Fundtech, and S1 Corporation. Our primary competitors for providing lending products to financial institutions are APPRO (a division of Equifax), IA Systems, and Lending Solutions, Inc.

Government Regulation

The financial services industry is subject to extensive and complex federal and state regulation. Our current and prospective customers, which consist of financial institutions such as commercial banks, savings and loans associations, credit unions and savings banks, operate in markets that are subject to rigorous regulatory oversight and supervision. The compliance of our products and services with these requirements depends on a variety of factors including the particular functionality, the interactive design, and the charter or license of the financial institution. Our financial services customers must independently assess and determine what is required of them under these regulations and are responsible for ensuring that our system and the design of their web sites conform to their regulatory obligations.

We are not licensed by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, the Federal Deposit Insurance Corporation, the National Credit Union Administration or other federal or state agencies that regulate or supervise depository institutions or other providers of financial services. We are examined by the Federal Financial Institution Examination Council under the Information Technology examination guidelines. Although we believe we are not subject to direct supervision by federal and state banking agencies relating to other regulations, we have from time to time agreed to examinations of our business and operations by these agencies. We are also subject to encryption and security export laws and regulations, which, depending on future developments, could render our business or operations more costly, less efficient or impossible.

Proprietary Rights

Our proprietary rights are important to our products and services, and we continually seek to expand the technology that we use in our business through internal development, licensing and acquisitions. We generally rely on copyright, trademark and trade secret laws, and contractual rights to establish and maintain our proprietary rights in our technology and products. In 2002, the Digital Insight mark was approved as a registered trademark by the U.S. Patent and Trademark Office. Due to the nature of the technology associated with our products and services, we believe that our ability to compete does not depend to any significant extent on whether or not our technology is patented, and none of our technology is currently patented. In order to protect our proprietary information we limit access to and distribution of our source code and other intellectual property, and we also enter into confidentiality agreements with our employees, consultants, resellers and customers.

Employees

As of December 31, 2005, we had approximately 800 employees, including 19 part-time employees. None of our work force is unionized. We have not experienced any work stoppages and consider our relations with our employees to be good. Following the completion of the call center outsourcing, we will reduce our staff count by approximately 90 employees in our lending division.

ITEM 1A. RISK FACTORS

You should carefully consider the following risk factors in your evaluation of us. Our business and results of operations could be seriously harmed by any of the following risks. The trading price of our common stock could decline due to any of these risks, and you may lose part or all of your investment.

Fluctuations of our operating results could cause our stock price to fluctuate.

Our operating results may fluctuate significantly in the future based upon a number of factors, many of which are not within our control. We base our operating expenses on anticipated revenue growth and many of our operating expenses are relatively fixed in the short-term. Our revenue model is based largely on recurring revenues, billed monthly, predominately derived from growth in end users and transaction volume within a monthly billing period. The number of total end users accessing our systems is affected by many factors, several of which are beyond our control, including the number of new user registrations, end user turnover, loss of customers, and general consumer trends. We may expend funds and management resources to increase end user

Table of Contents

penetration and still fail to achieve the targeted growth objectives. Accordingly, our results of operations for a particular period may be adversely affected if fluctuating growth in end users causes revenues and operating results to be lower than expectations of market analysts or investors. If this were to occur, the price of our common stock would likely decrease.

Our operating results may also fluctuate in the future due to a variety of other factors, including:

- the overall level of demand for Internet banking services by consumers and businesses and the demand for our products, product enhancements and services in particular;
- loss of significant customers due to non-renewals of the service contracts, acquisition of customers by non-customer financial institutions, customer insolvencies and other reasons;
- consolidation among core data processing vendors, which may affect our reseller and revenue-sharing agreements with certain core processor organizations or reduce the likelihood of extending our agreements at expiration;
- actions taken by our competitors, including the introduction of new products or changes in their pricing models;
- spending patterns and budgetary resources of financial institutions and their end user customers;
- the timing of upgrades to our computer hardware infrastructure;
- the timing of customer product implementations or our failure to timely complete scheduled product implementations;
- delays in the product development schedule of one or more of our new products or services;
- a negative outcome in any significant legal proceeding or prolonged litigation;
- the adoption of new accounting standards;
- governmental actions affecting Internet operations or content; and
- general economic trends and the impact of external factor or events, such as war or acts of terrorism.

If we are unable to implement appropriate systems, procedures and controls, we may not be able to successfully offer our services and grow our business.

Our ability to successfully offer our products and services and to grow our business requires an effective planning and management process. We updated our operations and financial systems, procedures and controls following our prior acquisitions. Our systems, however, will continue to require additional modifications and improvements to respond to current and future changes in our business. If we cannot grow our business, and manage that growth effectively, or if we fail to implement in a timely and cost-effective manner appropriate internal systems, procedures, controls and necessary modifications and improvements to these systems, our business will suffer. For example, our billing system must keep pace with our business and be able to interoperate with our contract database and production database.

Security breaches could damage our reputation and business.

Our products and networks may be vulnerable to unauthorized access, computer viruses and other disruptive problems. We transmit confidential financial information in providing our services. Users of Internet banking and other electronic commerce services are concerned about the security of transmissions over public networks. Therefore, it is critical that our facilities and infrastructure remain secure and be perceived by the marketplace as secure. A material security breach affecting us or one of our key vendors could damage our reputation, deter financial institutions from purchasing our products, deter their end user customers from using our products, or

Table of Contents

result in liability to us. Further, any material security breach affecting our competitors could affect the marketplace s perception of Internet banking in general and have the same adverse effects.

Concerns over security and the privacy of end users have intensified both within and outside of the U.S., and may inhibit the growth of the Internet and other online services generally, especially as a means of conducting commercial transactions. Any well-publicized compromise of security or a widespread epidemic involving identity theft could deter people from using the Internet or using it to conduct transactions that involve transmitting confidential information. We may need to expend significant capital or other resources to protect against the threat of security breaches or to alleviate problems caused by breaches. Although we intend to continue to implement state-of-the-art security measures and upgrade our products to address these issues, persons may be able to circumvent the measures that we implement in the future. Eliminating computer viruses and alleviating other security problems may result in interruptions, delays or cessation of service to users accessing web sites that deliver our services, any of which could harm our business.

Any failure in our disaster recovery or emergency fail-over procedures could cause interruption in our system and loss of customers.

Most of our communications and network equipment related to our Internet banking operation is currently located in our main data center in Westlake Village, California. We also maintain a backup data center in Norcross, Georgia for the Westlake Village data center. We maintain these two data centers in a manner that will continue to provide system redundancy, fail-over from the Westlake facility to the Norcross facility and emergency backup capabilities. While the architecture of the two systems is largely integrated, the process of failing over to a recovery site currently involves some manual intervention, and there is some attendant delay and loss of use of non-key features and functionality. In addition, we may experience problems during the recovery or fail-over process that could cause system failures and decreased levels of service. Although we perform testing on a periodic basis to ensure that recovery mechanisms perform as planned, unexpected failure of any of these mechanisms may prevent a successful recovery.

A natural disaster, such as a fire, an earthquake or a flood, at any of our data centers could result in failures or interruptions in providing our products and services to our customers. Although we maintain and regularly test an uninterruptible power supply system for our critical systems in all of our data centers, there is no assurance that this system, consisting of a backup battery and a diesel generator, will function properly, or at all, in case of a power loss. In addition to a potential loss of power, our systems are vulnerable to operational failures, telecommunications failures and similar events. We have contracted to provide a certain level of service to our customers and, consequently, an unexpected interruption of our system has in the past caused, and in the future could cause, us to refund fees to some of our customers to compensate for decreased levels of service. Even with our disaster recovery plan and the integration of our two main facilities, we could experience a failure or interruption in our systems that could lead to loss of data or the inability to provide services to our customers.

If we do not retain our customers or they do not successfully market our products, we will not be able to increase our revenues.

We also depend on our financial institution clients to market and promote our products to their end user customers. Neither we nor our financial institution customers may be successful in marketing our current or future Internet banking products and services.

Moreover, financial institutions generally agree to use our products and services pursuant to contracts with durations that range from three to five years. Upon expiration, these contracts may be discontinued and we may lose customers as a result. We lose customers every quarter for a variety of reasons, and continually seek to replace these and add new customers. Unless our Internet banking products and services are successfully deployed and marketed by a significant number of financial institutions and achieve widespread market acceptance by their end user customers for a significant period of time, we will not be able to achieve our business objectives and increase our revenues.

Table of Contents

We depend on the efficient operation of the Internet, other networks and systems of third parties; if they do not operate efficiently, we will not be able to effectively provide our products and services.

We depend on the efficient operation of network connections from our financial institution clients, their data processing vendors and other third-party vendors such as bill payment providers. Further, portions of our revenue are dependent on continued usage by end users of Internet banking services and their connections to the Internet. Each of these connections, in turn, depends on the secure and efficient operation of web browsers, Internet service providers and Internet backbone service providers, all of which have had periodic operational problems or have experienced outages. In addition, the majority of our services depend on real-time connections to the systems of financial institutions, data processing vendors and bill payment providers. Any operational problems or outages in these systems would cause us to be unable to provide a real-time connection to these systems and we would be unable to process transactions for end users, resulting in decreased revenues. In addition, any system delays, failures or loss of data, whatever the cause, could reduce customer and end user satisfaction with our products and services and harm our revenues.

If we are unable to rapidly integrate third-party software, we may not be able to deliver service to our clients on a timely basis, resulting in lost revenues and potential liability.

As part of our strategy to provide integrated services, we integrate software applications from a variety of third party vendors on to product platform and resell them. If we are unable to implement and integrate this software in a fully functional manner for our clients, we may experience difficulties that could delay or prevent the successful development, introduction or marketing of services. Software often contains errors or defects, particularly when first introduced or when new versions or enhancements are released. Despite internal testing and testing by current and potential vendors, our current and future solutions may contain serious defects due to third-party software or software we develop or customize for clients. Serious defects or errors could result in liability for damages, lost revenues or a delay in implementation of our solutions.

Our past and potential future acquisitions involve risks to our business and financial results.

We have acquired various businesses over the last several years and may acquire complementary technologies or businesses in the future. We closed our acquisitions of *n*Front Inc. on February 10, 2000; 1View Network Corporation, or 1View, on June 21, 2000; AnyTime Access, Inc., or ATA, on July 31, 2000; Virtual Financial Services, Inc., or ViFi, on January 28, 2002; and Magnet on November 25, 2003. Acquisitions may not perform as we expect and may involve large one-time write-offs, including goodwill impairment charges, and amortization expenses related to intangible assets. In this regard, any of these factors could adversely affect our operating results or stock price. Acquisitions involve numerous risks, including, but not limited to:

- difficulties in assimilating the operations, products, technology, information systems and personnel of the acquired company with our operations;
- diverting our management s attention from other business concerns;
- impairing relationships with our employees, affiliates, strategic marketing alliances and third-party vendors;
- the inability to maintain uniform standards, controls, procedures and policies;
- loss of acquired customers and strategic partners beyond projected thresholds;
- entering markets and adopting business models in which we have no direct prior experience; and
- losing key employees of the acquired company.

Some or all of these risks could result in a material adverse effect on our business, financial condition and operating results. In addition, we cannot assure you that we will be able to identify suitable acquisition candidates that are available for sale at reasonable prices. We may elect to finance future acquisitions with debt financing, which would create debt service requirements, or through the issuance of additional common or preferred stock, which could result in dilution to our stockholders. We cannot assure you that we will be able to arrange adequate financing, if required, for any acquisitions on acceptable terms.

We depend on cooperation from data processing vendors for financial institutions, including vendors that have resisted efforts in the past to allow the integration of our products and services with their systems.

Our products involve integration with products and systems developed by data processing vendors that serve financial institutions. If any of our products fail to be supported by financial institutions data processing vendors, we would have to redesign our products to suit these financial institutions. We cannot assure that any redesign could be accomplished in a cost-effective or timely manner. We rely on these vendors to jointly develop technology with us and to disclose source code specifications to enable our products to integrate effectively with their products and systems. In the past, some vendors have resisted integrating our products or have caused delays or other disruptions in the implementation process. Several of these data processing vendors offer or are planning to offer Internet banking products and services that are directly competitive with our products and services. In addition, financial institutions data processing vendors may develop new products and systems that are incompatible with our products. Our failure to integrate our products effectively with financial institutions data processing vendors could result in higher implementation costs or the loss of current and potential customers.

Competition could reduce or eliminate demand or result in lower prices for our products and services.

The market for Internet banking services is highly competitive and fragmented with many providers. We face competition from two main areas: other companies similar to us with outsourced Internet banking offerings, and vendors of data processing services to financial institutions. Also, vendors that primarily target the largest financial institutions occasionally compete in our target market. Some of our current and potential competitors have longer operating histories and may be in a better position to produce and market their services due to their greater financial, technical, marketing and other resources, as well as their significantly greater name recognition and larger installed bases of customers. In addition, many of our competitors have well-established relationships with our current and potential financial institution customers and data processing vendors and have extensive knowledge of our industry.

We may not be able to compete successfully against our current or future competitors and, accordingly, we cannot be certain that we will be able to expand the number of our customers and end users, retain our current customers or third-party service providers, or maintain our current pricing levels for our products and services. In particular, as we negotiate the renewal of long-term service contracts with current customers, we may be subject to competitive pressures and other factors that may require concessions on pricing and other material contract terms to induce the customer to remain with us.

We could be subject to potential liability claims related to use of our products and services.

Financial institutions use our products and services to provide Internet banking services to their customers. Any errors, defects or other performance problems in our products and services could result in financial or other damages to these financial institutions for which we may be liable. Moreover, we may be liable for transactions executed using Internet services based on our products and services even if the errors, defects or other problems are unrelated to our products and services. A claim brought against us, even if not successful, would likely be time consuming, result in costly litigation, and could seriously harm our business and reputation.

Our stock price is volatile, which could cause you to lose some or all of your investment.

The market price of our common stock has fluctuated significantly in the past and could fluctuate in the future in response to the following particular factors:

- actual or anticipated variations in operating results;
- announcements by us or our competitors of new products, significant contracts, acquisitions or relationships;
- additions or departures of key personnel;
- changes in estimates or ratings of securities analysts;
- future equity or debt offerings or acquisitions or our announcements of these transactions; and
- economic well-being of financial institutions.

Our stock price could also be impacted by shares purchased by us through our stock repurchase program or shares sold by our executive officers upon the exercise of vested options and restricted stock. In addition, in recent years, the stock market in general, and the Nasdaq National Market and the securities of technology companies in particular, have experienced extreme price and volume fluctuations. These fluctuations have often been unrelated or disproportionate to the operating performance of individual companies. These broad market fluctuations may materially adversely affect our stock price, regardless of our operating results.

The lengthy sales cycles of our business banking products may cause our business banking revenues and operating results to be unpredictable and to vary significantly from period to period.

The sale and implementation of our business banking products and services for large financial institutions are often subject to delays because of our customers internal budgets and procedures for approving large capital expenditures and deploying new technologies. The time elapsed between the date of initial contact with a potential customer and the execution of a contract typically ranges from six to twelve months. In addition, our prospective customers decision-making processes require us to provide a significant amount of information to them regarding the use and benefits of our business banking products. We may expend substantial management resources and fail to make the sale. These delays have adversely affected sales of our business banking products for large financial institutions. Any future delays in closing orders or implementation of products or services can cause our operating results to fall short of anticipated levels for any quarter.

If we estimate incorrectly the time required to complete our business banking projects, we will lose money on fixed-price contracts.

A majority of our professional services contracts for business banking are fixed-price contracts, rather than contracts in which the client pays us on a time and materials basis. We must estimate the number of hours and the materials required before entering into a fixed-price contract. Our future success will depend on our ability to continue to set rates and fees accurately and to maintain targeted rates of employee utilization and project quality. If we fail to accurately estimate the time and the resources required for a project, any required increase in the time and resources to complete the project could cause our profits to decline.

Our business banking and consumer lending business results could suffer if we lose key customers or fail to add additional customers.

Our business banking and consumer lending businesses derive a significant portion of their revenues from a limited number of customers in each period. Accordingly, for each business segment, if an existing contract expires or is cancelled and we fail to replace the contract with new business, revenues for the segment would be adversely affected. Our lending division has been adversely affected by customer losses in the past, which has led to a decrease in the number of loan applications processed and corresponding revenues. We expect that a limited number of customers will continue to account for a substantial portion of our business banking revenues and consumer lending revenues in each quarter for the foreseeable future.

Table of Contents

Our consumer lending operation could be adversely impacted by a downturn in the economy and by seasonal demand.

A softening of demand for our outsourced solutions caused by a weakening of the economy generally may result in decreased revenues or lower growth rates. Also, the lending industry is also generally subject to seasonal trends affecting loan demand.

Government regulation of our business could cause us to incur significant expenses, and failure to comply with certain regulations, if adopted, could make our business less efficient or impossible.

The financial services industry is subject to extensive and complex federal and state regulation. Financial institutions such as commercial banks, savings and loans associations, savings banks, and credit unions operate under high levels of government supervision. Our customers must ensure that our services and related products work within the extensive and evolving regulatory requirements applicable to them.

Neither federal depository institution regulators nor other federal regulators of financial services require us to obtain any licenses. We are examined by the Federal Financial Institution Examination Council under the Information Technology guidelines. Although we believe we are not subject to direct supervision by federal and state banking agencies relating to other regulations, we have from time to time agreed to examinations of our business and operations by these agencies. These regulators have broad supervisory authority to remedy any shortcomings identified in any such examination which could lead to changes in our business.

Federal, state or foreign authorities could also adopt laws, rules or regulations relating to the financial services industry that affect our business, such as requiring us or our customers to comply with data, record keeping and processing, and other requirements. It is possible that laws and regulations may be enacted or modified with respect to the Internet, covering issues such as end user privacy, pricing, content, characteristics, taxation and quality of services and products. If enacted or deemed applicable to us, these laws, rules or regulations could be imposed on our activities or our business, thereby rendering our business or operations more costly, burdensome, less efficient or impossible, and requiring us to modify our current or future products or services.

We may be found to infringe proprietary rights of others, which could harm our business.

We are subject to the risk of claims and litigation alleging infringement of the intellectual property rights of others. Third parties may assert infringement claims in the future with respect to our current or future products, or those of our key vendors. Any assertion of such claims, regardless of its merit, could require us to pay damages or settlement amounts and could require us to develop non-infringing technology, pay for a license for the technology that is the subject of the asserted infringement, or contract with a vendor that has non-infringing technology. For example, we have in the past received notices claiming infringement of intellectual property rights related to our Internet banking application. Any litigation or potential litigation could result in product delays, increased costs, or both. In addition, the cost of litigation and the resulting distraction of our management resources could adversely affect our operating results. We also cannot assure that any licenses for technology necessary for our business will be available or that, if available, these licenses can be obtained on commercially reasonable terms.

Consolidation of the banking and financial services industry could cause our revenues to fall.

Consolidation of the banking and financial services industry could result in a smaller market for our products and services. A variety of factors could cause our customers to reassess their purchase or potential purchase of our products and could result in termination of services by existing customers. Although our contracts typically provide for an early termination fee, the loss of customers may negatively impact our operating results in future periods. After consolidation, banks and other financial institutions may experience a

Table of Contents

realignment of management responsibilities and a reexamination of strategic and purchasing decisions. We may lose relationships with key constituencies within our customers organizations due to budget cuts, layoffs, or other disruptions following a consolidation. In addition, consolidation may result in a change in the technological infrastructure of the combined entity. Our products and services may not integrate with this new technological infrastructure. The acquiring institution may also have its own in-house system or outsource to competitors.

Our charter and bylaws and Delaware law contain provisions which could discourage a takeover.

Provisions of our charter and bylaws may make it more difficult for a third party to acquire, or may discourage a third party from attempting to acquire, control of us, even if doing so would be beneficial to our stockholders. These provisions could limit the price that investors might be willing to pay in the future for shares of our common stock. These provisions include:

- division of the board of directors into three separate classes;
- elimination of cumulative voting in the election of directors;
- prohibitions on our stockholders from acting by written consent and calling special meetings;
- procedures for advance notification of stockholder nominations and proposals; and
- the ability of the board of directors to alter key provisions of our bylaws without stockholder approval.

In addition, our board of directors has the authority to issue up to 5,000,000 shares of preferred stock and to determine the price, rights, preferences, privileges and restrictions, including voting rights, of those shares without any further vote or action by the stockholders. The issuance of preferred stock, while providing flexibility in connection with possible financings or acquisitions or other corporate purposes, could have the effect of making it more difficult for a third party to acquire a majority of our outstanding voting stock.

We are also subject to Section 203 of the Delaware General Corporation Law, which, subject to exceptions, prohibits a Delaware corporation from engaging in any business combination with any interested stockholder for a period of three years following the date that the stockholder became an interested stockholder. The preceding provisions of our charter and bylaws, as well as Section 203 of the Delaware General Corporation Law, could discourage potential acquisition proposals, delay or prevent a change of control and prevent changes in our management.

ITEM 1B. UNRESOLVED STAFF COMMENTS

There are no unresolved written comments that were received from the SEC staff 180 days or more before the end of our fiscal year relating to our periodic or current reports under the Securities Exchange Act of 1934.

ITEM 2. PROPERTIES

Our principal offices currently occupy approximately 46,000 square feet in Calabasas, California, pursuant to a lease that expires May 31, 2011. We also occupy an aggregate of approximately 167,000 square feet of office space in Westlake Village and Sacramento, California, and Athens, Atlanta and Norcross, Georgia pursuant to long-term leases with eighteen months to eight year terms. We believe that suitable additional or alternative space will be available in the future on commercially reasonable terms as needed.

ITEM 3. LEGAL PROCEEDINGS

In Re Digital Insight Corporation Initial Public Offering Securities Litigation

On December 6, 2001, Digital Insight and two of its former officers and one current director were named as defendants in a class-action lawsuit filed in the United States District Court for the Southern District of New

Table of Contents

York. The lawsuit is captioned In Re Digital Insight Corp. Initial Public Offering Securities Litigation, No. 01 CV 11231. The claims, which were also asserted against the managing underwriters in our previous public offerings, are based on allegations that the underwriter defendants solicited and received from certain investors, in exchange for allocating Digital Insight shares to the investors in connection with the previous public offerings, additional, excessive and undisclosed commissions and undisclosed commitments to purchase additional Digital Insight shares in the aftermarket. Other actions have been filed in New York making similar allegations regarding the IPOs of more than 300 other companies. Plaintiffs are seeking unspecified damages along with these companies and the individual defendants, but not the underwriter defendants, we have entered into a settlement agreement with the plaintiffs to settle the claims. As part of the settlement, once the settlement documents become effective, the plaintiffs will dismiss with prejudice the settling companies and individual defendants. On August 2005, the court issued an order preliminarily approving the proposed settlement and scheduling a settlement fairness hearing in April 2006. In the opinion of management, after consultation with legal counsel and based on currently available information, the ultimate disposition of these matters is not expected to have a material adverse effect on our business, financial condition or results of operations, and hence no amounts have been accrued for this lawsuit.

Magnet Claims

Currently, approximately $3.4 million of cash and 144,834 shares of our common stock issuable in connection with our acquisition of Magnet are held in escrow. We have notified the prior stockholders of Magnet that we have various claims against them in connection with the acquisition, and we are seeking recovery of damages, including the amounts in escrow. In response, the prior stockholders initiated arbitration proceedings in Los Angeles, California, seeking release of the escrowed amounts. Even a favorable resolution of our claims could result in distraction of our management and significant legal and other related costs. No amounts have been recorded in our financial statements for claims in connection with these matters at December 31, 2005 as we cannot determine the final outcome.

Other

In addition, we may be involved from time to time in litigation arising in the normal course of our business. Although we are currently not a party to such litigation that we believe would have a material adverse effect, individually or in the aggregate, on our business, financial condition or results of operations, it is possible that in the future we could become a party to such proceedings.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of 2005.

Table of Contents

PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market for Common Equity

Our common stock is traded on the Nasdaq National Market under the symbol DGIN. As of December 31, 2005, there were 180 holders of record of our common stock. The following table sets forth the range of high and low closing sale prices reported on the Nasdaq National Market for our common stock for the periods indicated.

	Common Stock Price	
	High	**Low**
2004		
First Quarter	$ 28.01	$ 18.59
Second Quarter	$ 22.72	$ 17.55
Third Quarter	$ 19.78	$ 13.21
Fourth Quarter	$ 18.75	$ 13.70
2005		
First Quarter	$ 18.01	$ 15.88
Second Quarter	$ 25.96	$ 16.56
Third Quarter	$ 27.72	$ 23.20
Fourth Quarter	$ 35.18	$ 25.63

We have never paid cash dividends on our common stock, and we anticipate that in the foreseeable future we will continue to retain any earnings for use in the operations of our business. [See Part III, Item 12 for information regarding securities authorized for issuance under our equity compensation plans.]

ITEM 6. SELECTED FINANCIAL DATA

The following table presents selected consolidated statement of operations data and selected consolidated balance sheet data. We derived this data from our audited consolidated financial statements for the years presented.

You should read this data together with our audited consolidated financial statements and related notes included elsewhere in this annual report.

Table of Contents

	Year Ended December 31,				
	2005	2004	2003[1]	2002[1][2]	2001[2]
	(in thousands, except per share data)				
Consolidated Statement of Operations Data					
Revenues	$ 213,971	$ 188,891	$ 154,362	$ 130,387	$ 94,635
Cost of revenues	89,828	84,276	72,569	67,453	53,124
Gross profit	124,143	104,615	81,793	62,934	41,511
Operating expenses	83,876	76,428	64,183	72,429	95,458
Income (loss) from operations	40,267	28,187	17,610	(9,495)	(53,947)
Interest and other income, net	3,113	838	556	600	1,999
Net income (loss) before cumulative effect of change in accounting method and income tax provision (benefit)	43,380	29,025	18,166	(8,895)	(51,948)
Income tax provision (benefit)	16,839	12,302	(28,428)		
Net income (loss) before cumulative effect of change in accounting method	26,541	16,723	46,594	(8,895)	(51,948)
Cumulative effect of change in accounting method				(29,036)	
Net income (loss)	$ 26,541	$ 16,723	$ 46,594	$ (37,931)	$ (51,948)
Basic net income (loss) per share before cumulative effect of change in accounting method	$ 0.76	$ 0.47	$ 1.41	$ (0.28)	$ (1.77)
Per share cumulative effect of change in accounting method				(0.91)	
Basic net income (loss) per share	$ 0.76	$ 0.47	$ 1.41	$ (1.19)	$ (1.77)
Diluted net income (loss) per share before cumulative effect of change in accounting method	$ 0.75	$ 0.47	$ 1.38	$ (0.28)	$ (1.77)
Per share adjustment for cumulative effect of change in accounting method				(0.91)	
Diluted net income (loss) per share	$ 0.75	$ 0.47	$ 1.38	$ (1.19)	$ (1.77)
Shares used to compute basic per share amounts	34,698	35,364	32,991	31,984	29,301
Shares used to compute diluted per share amounts	35,617	35,860	33,700	31,984	29,301

	As of December 31,				
	2005	2004	2003	2002	2001
	(in thousands)				
Consolidated Balance Sheet Data					
Cash, cash equivalents and short-term investments	$ 116,155	$ 99,469	$ 69,335	$ 74,379	$ 53,634
Long-term investments	8,802	17,785	1,007		13,334
Working capital	128,533	113,375	76,483	59,048	54,396
Total assets	385,402	377,256	348,812	259,063	236,628
Long-term portion of capital lease obligations and long-term debt	1,241				6,293
Total liabilities	54,333	44,175	42,341	49,400	39,737
Total stockholders equity	331,069	333,081	306,471	209,663	196,891

(1) The selected consolidated financial data includes the results of the purchase method acquisitions of ViFi and Magnet for periods subsequent to their acquisition dates in January 2002 and November 2003, respectively.

(2) In 2002, we adopted SFAS No. 142 which established an impairment approach to accounting for goodwill and discontinued amortization of goodwill prospectively for all acquisitions. We recorded an impairment charge of $29.0 million in the first quarter of 2002 from the adoption of SFAS No. 142.

Amortization of goodwill included in operating expenses was $25.5 million in 2001. The pro forma net loss and net loss per share excluding goodwill amortization in 2001 was as follows:

		2001 (in thousands, except per share data)
Pro forma net loss	$	(26,440)
Pro forma net loss per share	$	(0.90)

Table of Contents

ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The forward-looking statements included in this section involve risks and uncertainties, including anticipated financial performance, business prospects, anticipated capital expenditures and other similar matters, which reflect management s best judgment based on factors currently known. Actual results and experience could differ materially from the anticipated results or other expectations expressed in our forward-looking statements as a result of a number of factors, including but not limited to those discussed under the caption Risk Factors in Item 1A of Part I.

The following discussion should be read together with our financial statements and related notes.

Overview

Summarized results of operations for our reportable segments were as follows for the three years ended December 31, 2005, 2004 and 2003:

	Year Ended December 31,					
	2005		2004 (in thousands)		2003	
	Dollars	**%**	**Dollars**	**%**	**Dollars**	**%**
Revenues:						
Internet banking	$ 173,253	81	$ 151,873	80	$ 129,282	84
Business banking [1]	28,640	13	22,942	12	8,360	5
Lending	12,078	6	14,076	8	16,720	11
Total	$ 213,971	100	$ 188,891	100	$ 154,362	100
	Dollars	**Margin**	**Dollars**	**Margin**	**Dollars**	**Margin**
Gross profit:						
Internet banking	$ 103,322	60	$ 88,669	58	$ 70,745	55
Business banking [1]	17,482	61	11,708	51	4,119	49
Lending	3,339	28	4,238	30	6,929	41
Total	$ 124,143	58	$ 104,615	55	$ 81,793	53
	Dollars (3)	**%**	**Dollars (4)**	**%**	**Dollars (5)**	**%**
Operating expenses:						