



leading thought

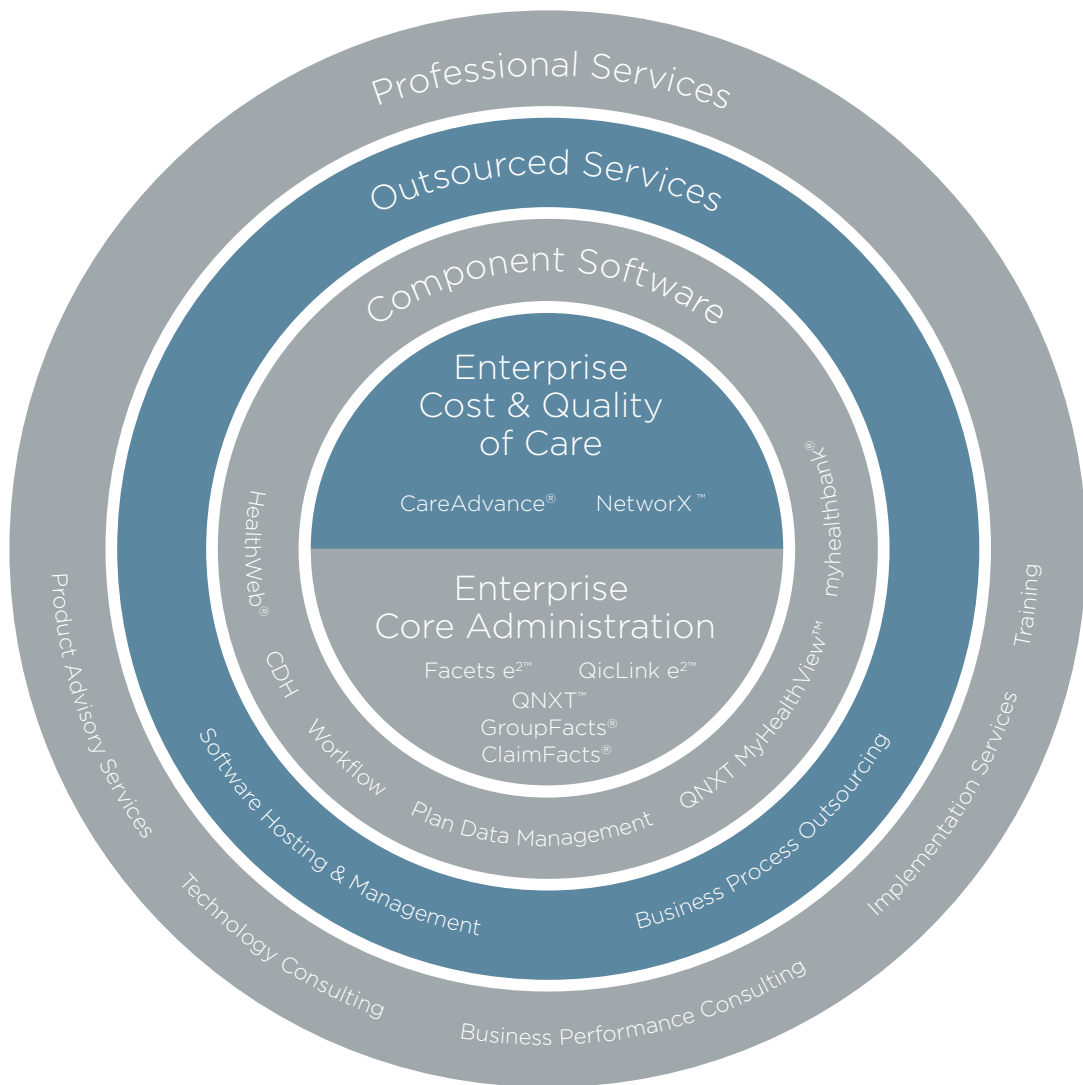
The patient's HRA account may reduce the patient's out-of-pocket costs.
The patient may wish to consider using HRA funds for out-of-pocket costs.

Explanation Codes

Is

Service Date	Charge	Allowed	Provided
01/22/2007	\$100.00	\$100.00	
01/22/2007	\$76.00	\$76.00	
01/22/2007	\$15.00	\$15.00	
01/22/2007	\$15.00	\$15.00	
Grand Total:	\$206.00	\$206.00	

leading technology



TriZetto Solutions

TriZetto offers a broad family of information technology products and services for the payer industry, which includes health plans and benefit administrators. In addition to the powerful individual functionality of these offerings, their unique integration delivers higher return on investment and greater competitive advantage to our customers.



TriZetto Reach

362

Payer Customers

145

Million Lives
Under Contract

117

Million Lives
in Production

To turn leading thought into leading technology for payers, TriZetto applies its unique vision, focus and reach.

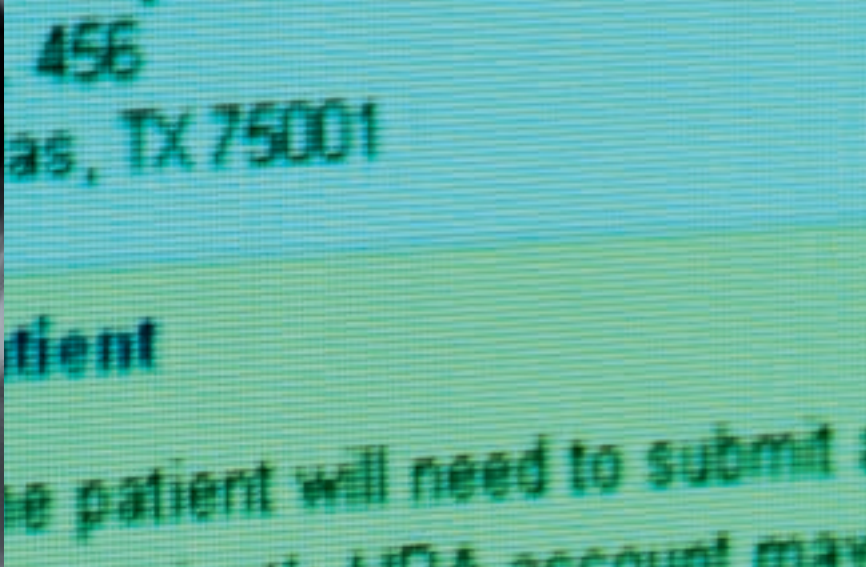


vision

Anticipating the future is challenging, but it is TriZetto's primary mission – and distinction – for payers and their constituents.



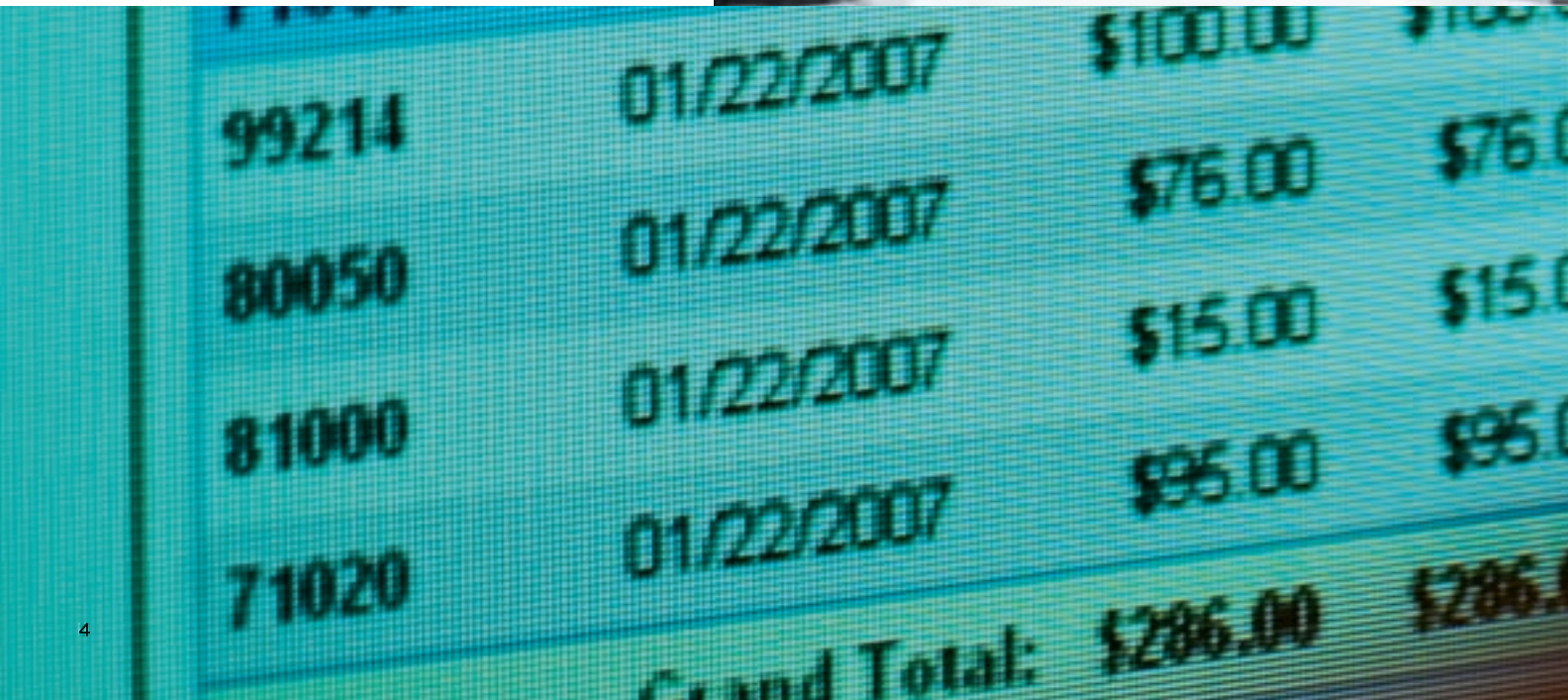
ALAN ROSS, SENIOR VICE PRESIDENT,
HUMAN CAPITAL MANAGEMENT



Looking ahead is always a challenge, but especially so in an industry undergoing as much change as healthcare. Founded by former CIOs and information technology experts from across the payer industry, TriZetto's unique core strength is its understanding of the complex forces affecting the integration, coordination and payment of healthcare.

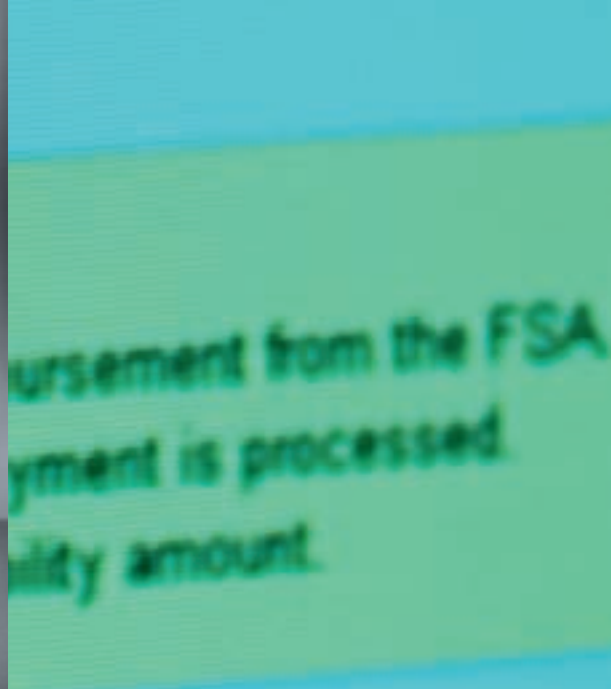


DAN SPIREK, SENIOR VICE PRESIDENT,
CHIEF SOLUTIONS OFFICER





JOE MANHEIM, SENIOR VICE PRESIDENT
BENEFITS ADMINISTRATION



Since its founding in 1997, TriZetto has proven its vision by delivering new software and services to make its payer customers' businesses more competitive and successful in the evolving market for healthcare insurance benefits and services. Recent examples of this include the company's advanced cost and quality of care solutions, which are generating strong market demand, and a unique patient liability and point-of-service claims adjudication system that helps payers improve their network physicians' cash flow.

Completing a two-year effort to further enhance the company's ability to anticipate the market, TriZetto is positioned to accelerate its pace of innovation. Over the next two years, TriZetto expects to lead the industry's delivery of new solutions for integrated incentive management (pay-for-performance), pending ICD-10 provider contracting and payment requirements, Medicare and Medicaid revenue enhancement, and business intelligence.

This screen: TriZetto Provider POS Direct™ is a real-time patient liability and point-of-service claims adjudication solution. Delivered through our payer customers, it enables physicians to provide patients with pre-service estimates of their out-of-pocket costs, and following treatment, to obtain immediate adjudication of the claim and collect fully before the patient leaves the office.



TONY BELLOMO, EXECUTIVE VICE PRESIDENT,
PRODUCT MANAGEMENT



focus

Health Record

Health Risk Assessment

Observations

Medication List

Condition List

Allergy List

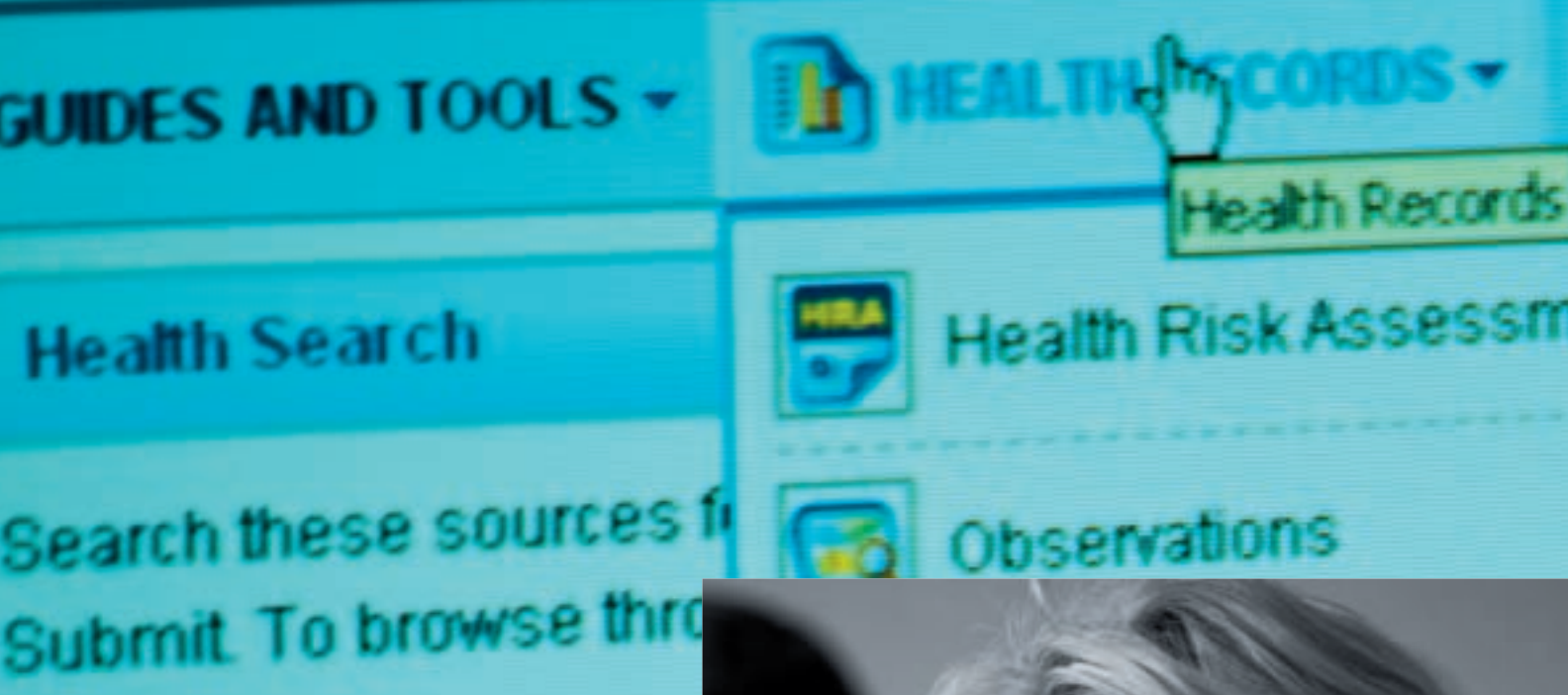
Vaccination List

Procedure List

PCP History

Handicap

TriZetto's unique ability to develop products for future needs stems from its single-minded focus on how the payer industry organizes systems of care.

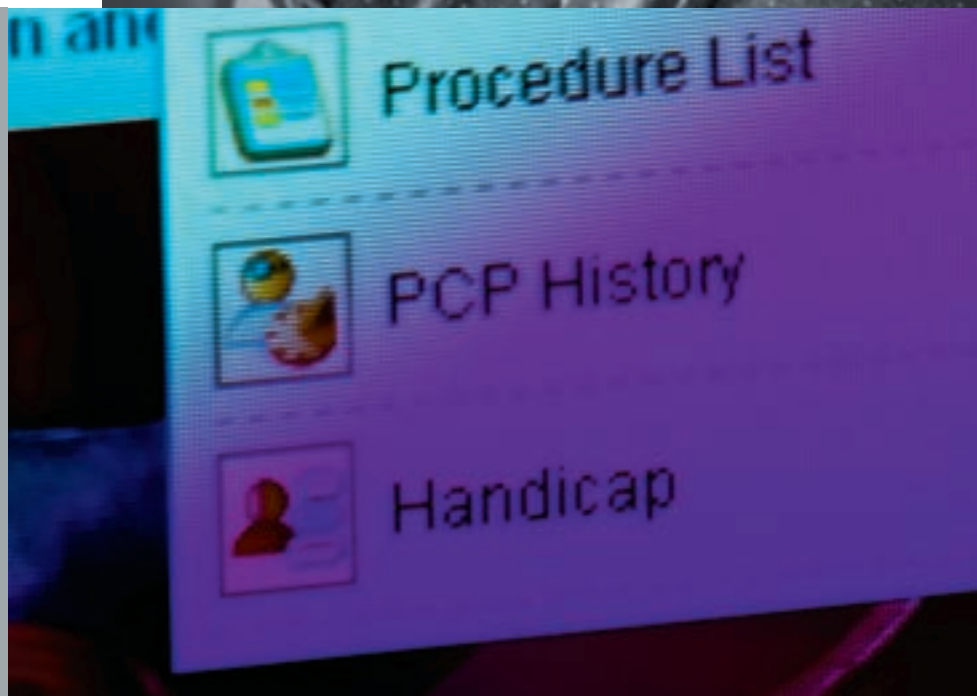


TriZetto supports payers in their position at the center of the healthcare supply chain. Our technology helps payers leverage their information systems to enhance revenue growth, drive administrative efficiency and improve the cost and quality of care for their members.



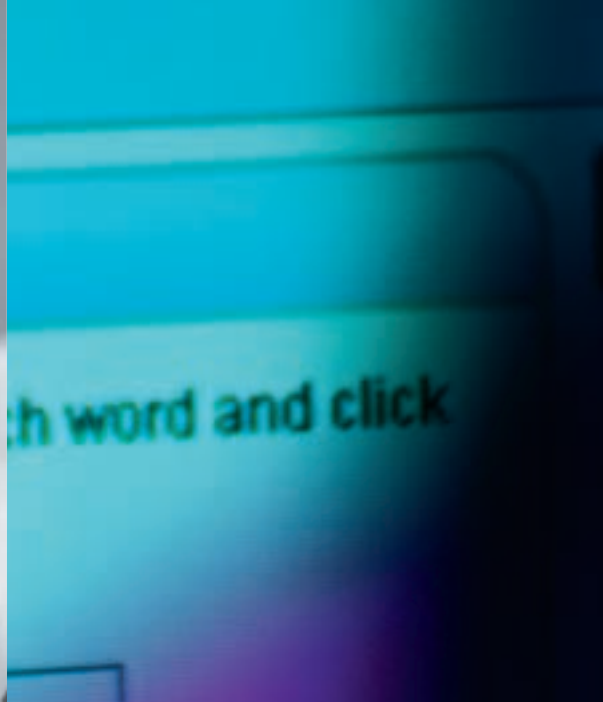
KATHLEEN EARLEY
PRESIDENT AND CHIEF OPERATING OFFICER

This screen: TriZetto Personal CareAdvance® supports payers' population management initiatives and helps shape members' care decisions by providing customized information and tools needed for effective self-management. Personal CareAdvance allows members to review information about their current health activity and share it with care managers, providers, family and others. The application also gives members access to extensive, up-to-date multimedia health libraries as well as personalized content.





JOHN JORDAN, SENIOR VICE PRESIDENT,
SALES AND ACCOUNT MANAGEMENT



Beginning with our peoples' heritage in the industry, TriZetto has always been uniquely focused on payers. Over the last five years, TriZetto has invested more than \$250 million towards developing new products for this market. That has resulted in the broadest integrated and scalable array of software and services available to payers from a single source.

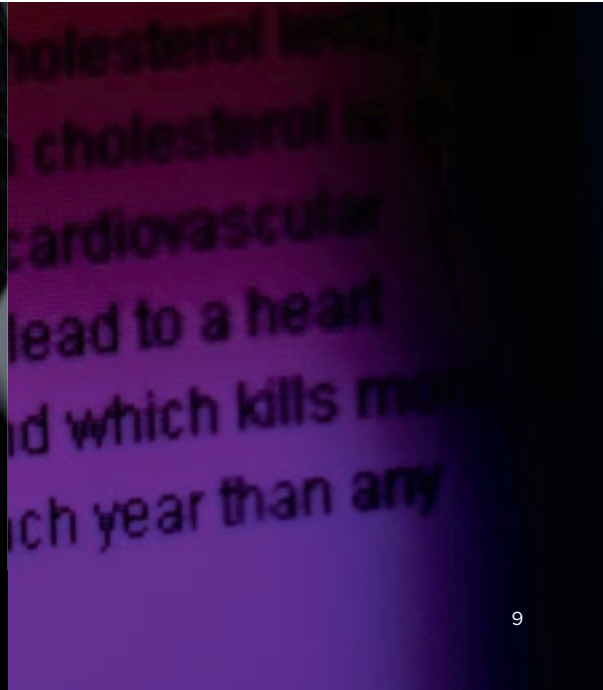
For example, in 2003, the company only offered payers solutions for administrative efficiency, which consumes about 11% of payers' spending. Today, TriZetto solutions

address a wide spectrum of payer needs, including cost and quality of care that comprises 85% of their budgets, as well as top-line revenue enhancement.

We continue to sharpen our focus on how payers need to transform for success. Ongoing expansion and improvement across many groups, including sales, product management and solutions architecture is helping TriZetto accelerate the development of new software and services that our customers will need in the future.



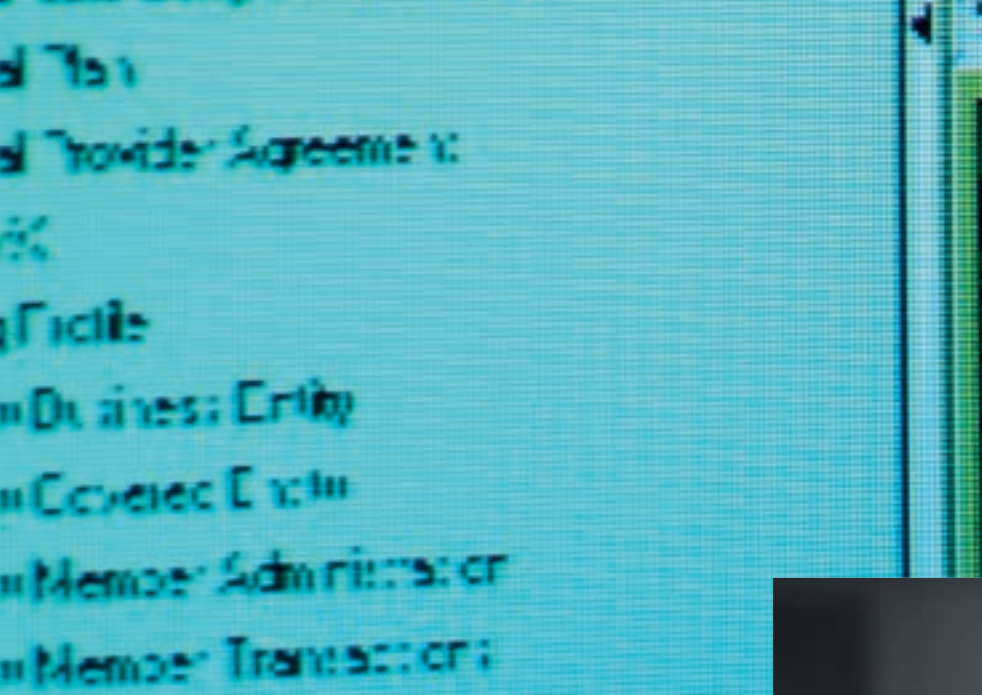
DIANE MARRA, SENIOR VICE PRESIDENT, INTEGRATED MARKETING
AND BUSINESS DEVELOPMENT





reach

Working together with more than 350 payer customers positions TriZetto to integrate many diverse needs and ideas into its software and services for payers.



This screen: Facets™ is an enterprise-wide core administration solution for all commercial, specialty, consumer-directed, Managed Medicaid and Medicare Advantage healthcare organizations. Architected to maximize automation, provide expanded business functionality and integration, this highly scalable, state-of-the-art technology platform can address all of a payer's business needs from e-business integration to care management and consumer-directed functionality. Facets e² is at the heart of the payer's healthcare enterprise and can be delivered on a hosted, installed or out-sourced basis, depending on business needs.

In just 10 years since its founding, TriZetto has built a leading footprint across the payer industry. Through more than 350 health plan and benefits administration customers, TriZetto technology touches about half the insured population of the U.S., including nearly 10 million lives hosted in the company's data center. The quick achievement of this scale is evidence of the value and return our customers realize.



PHIL TAMMINGA, EXECUTIVE VICE PRESIDENT, DEVELOPMENT AND PROFESSIONAL SERVICES





What makes TriZetto unique? It is useful to consider the fundamental traits that define our business and differentiate us in the marketplace as we think through strategies for driving future growth.

Our ability to turn leading thought into success-critical technology solutions for payers stems from our unique vision, focus and reach.

Our strategic progress and financial results in 2006 demonstrated expansion in all three of these key TriZetto attributes. As a result, we are well-positioned to increase the company's profitable growth and shareholder returns in 2007 and beyond.

Financial Highlights

(IN MILLIONS, EXCEPT PER SHARE AMOUNTS)

Years ended December 31

	2006	2005	2004
Total revenue	\$ 347.9	\$ 292.2	\$ 274.6
Services and other	\$ 272.9	\$ 243.5	\$ 223.3
Products	\$ 75.0	\$ 48.7	\$ 51.3
EPS: Net income per share (diluted)	\$ 0.33	\$ 0.48	\$ 0.18
Shares used in computing net income per share (diluted)	45.7	45.5	48.2
Net cash provided by operating activities	\$ 40.2	\$ 43.8	\$ 35.9
Research and development expenses, and capitalization of software development costs	\$ 51.4	\$ 40.3	\$ 39.0
Cash resources: Cash, restricted cash and short-term investments	\$ 108.0	\$ 108.5	\$ 73.1
Total assets	\$ 382.6	\$ 317.7	\$ 239.9
Total debt: (notes payable, capital lease obligations, line of credit and convertible debt)	\$ 115.6	\$ 103.2	\$ 57.6
Stockholders' equity	\$ 133.9	\$ 101.4	\$ 86.9

The State of the Market: Consumerization and Capitol Hill

Driven by many different forces, healthcare is undergoing rapid change. Because payers occupy the central coordination role in the healthcare supply chain, most of these trends converge in our market space. Today and for the foreseeable future, industry, technology and regulatory trends are expanding the breadth of TriZetto's market opportunities, as well as increasing overall demand for competitive success-enhancing information technology solutions throughout the healthcare supply chain.

It has been interesting to see the widening use of a term we coined several years ago to express a bigger concept about where the industry is headed: *Consumer Retail Healthcare*. Much attention has been focused on the number of people enrolled in high-deductible benefit plans with health savings accounts, which rose 43% in 2006 to 4.5 million people. While that group comprises less than 2% of the U.S. insured population, it represents just the visible tip of a very big iceberg. Most Americans have seen their deductible rise significantly over the last couple of years, or in many cases seen their \$10 co-payment transform into co-insurance responsibility of 10% or more. This greater financial burden placed on a majority of the population is driving new retail-shopping-like behaviors in healthcare, such as price shopping and quality comparisons.

This consumerization process requires that our payer customers change the way they do business – and TriZetto technology provides an efficient bridge for facilitating many of those changes.

Since the mid-term elections of 2006, I have been asked more about Capitol Hill risks and opportunities than I have been over the entirety of TriZetto's previous

history. Cutting through all the rhetoric, there are two key points to understand. First, the federal and state governments cannot legislate away the fundamental drivers of healthcare costs. Baby boomers are aging out to Medicare, and the number of government-insured Americans will not stop growing for a decade. In a global economy, U.S. employers continue to struggle with the costs of providing healthcare coverage and will continue to shift costs to their employees, even as they pay more. Driven by new drugs, devices and treatments, the cost of care keeps increasing faster than general inflation and erodes wage increases.

The second key point is that payers are more likely to gain than suffer from changing government programs. The Medicare Modernization Act was a historic piece of bipartisan legislation, which recognized that the private sector is an efficient mechanism for delivering benefits to consumers. Campaign rhetoric aside, it is much more likely that substantial portions of new government programs will be delivered through the private sector payer system. Again, payers will need to change their business practices to pursue these opportunities, and TriZetto provides the fast and cost-effective system upgrades and transition paths.

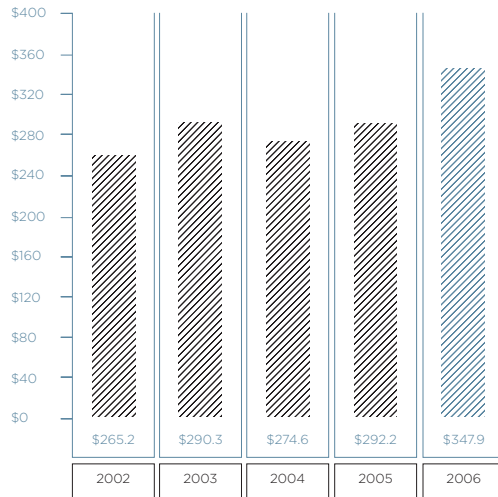
TriZetto's 2006 Strategic Progress: People, Operations and Strategy Processes

In 2006, we made significant progress in TriZetto's ability to leverage the expanding market opportunities. That progress included improvements in People Processes, Operations Processes and Strategy Processes.

Over the past four years we have focused our **people processes** on adding depth to our leadership bench at TriZetto, with executives possessing proven experience executing growth businesses. I call these people our *billion-dollar management team* that will enable

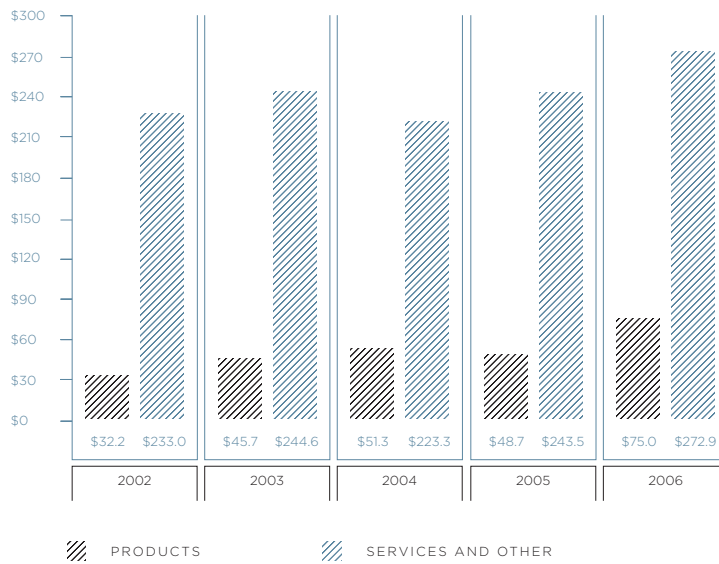
Revenue

(IN MILLIONS)



Revenue by Product

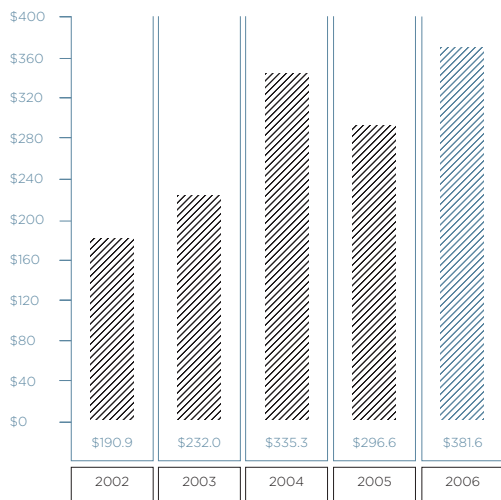
(IN MILLIONS)



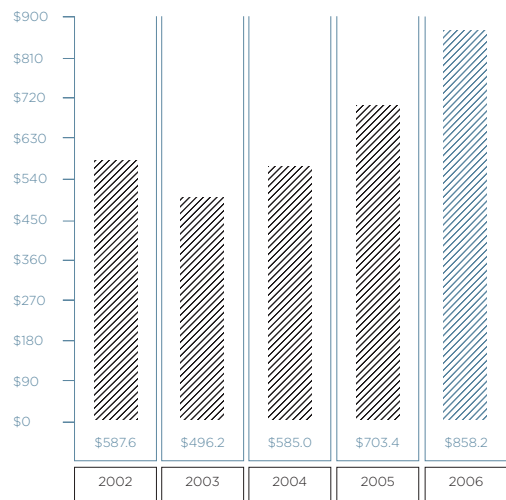
▨ PRODUCTS

▨ SERVICES AND OTHER

Bookings (IN MILLIONS)



Backlog (IN MILLIONS)



See page 65 for Definition and Reconciliation of Non-GAAP Financial Measures

TriZetto to grow its top line towards a billion dollars, and do so profitably to increase shareholder value. You have seen much of this team highlighted throughout the previous narrative section of this report.

Executive additions in 2006 that expanded our domain and functional expertise included human capital management, benefits administration, cost and quality of care, and hosting services. Acquisitions contributed valuable expertise as well. A skilled group in managed government programs and payer business intelligence joined us from Plan Data Management. TriZetto also benefits from the addition of the QCSI team with their supplemental expertise in enterprise administration systems.

We recognize and thank Lois Evans for the four years of strong support and expertise in healthcare and consulting she brought to our Board of Directors. Lois is not standing for re-election this year. Filling that seat is Nancy Handel, who brings growth-oriented financial management and reporting expertise as the retired Chief Financial Officer of Applied Materials.

Continuous improvement and strengthening of many **operations processes** in 2006 drove results and bolstered TriZetto's ability to succeed in 2007.

First, we completed a two-year turn of the company's structure to make all operations more market-focused and able to anticipate and respond to customer needs. This took the efforts of many business unit leaders and staff who stepped up to new responsibilities outside of their traditional comfort zones. This restructuring began in 2005, when we primarily focused on getting front-line, customer-facing teams better aligned with our client accounts. This included significant revamping of sales, sales support and account management.

In 2006, new disciplines were introduced to budgeting and product investment processes. On December 1, 2006, a new organizational structure was implemented to consolidate certain activities and functions across the company to increase coordination and eliminate silos and duplicate efforts. Perhaps most notable was the consolidation of all software development activities across the company under Phil Tamminga, as well as consolidation of all product management activities under Tony Bellomo. The CareKey and QCSI acquisitions were folded into these new structures as well.

As an innovative technology company, TriZetto is required to think several years ahead of what we are delivering in the market. In 2006, we made dramatic leaps ahead in our **strategy processes** to narrow the gap between our best thinking and our execution and delivery. We absolutely strengthened the company's operations around the three key tenets of our mission statement to help our customers enhance revenue, be administratively efficient, and improve the cost and quality of care for their members. The acquisitions of CareKey, Plan Data Management and QCSI furthered our ability to address those tenets. For the longer-term, those acquisitions give TriZetto a number of new game-changing opportunities in the payer market.

2007 Primary Strategic Thrusts

To provide further perspective on our outlook, I think it is worth sharing the company's primary strategic thrusts for 2007:

Help Customers Leverage Our Broadened Core Administration Footprint

With the addition of the QCSI customer base to our "technology community," TriZetto has built an unrivaled industry market position and, consequently, a strong

responsibility to its customers. TriZetto's standardized core administration technology footprint is bigger than even the largest managed care organization, and this provides great opportunities for industry efficiency and collaboration. Our ability to sell additional pre-integrated software technology and services into our broadened base is a straightforward business opportunity. The approaching change to ICD-10 diagnosis codes should be a driver for core system replacements, which could further increase TriZetto's footprint. Longer-term, our potential to create information value, both in the exchange and analysis of data across our constituency, represents a significant future opportunity. The larger footprint also means that the potential to influence standards and improve retail business practices at the point-of-care is an immense and largely untapped asset of the company.

Help Payers Capitalize on Medicare and Medicaid Changes

In 2006, TriZetto made good progress building expertise in the managed Medicare marketplace and we have specifically targeted offerings expected to roll-out in 2007. Through the acquisition of Plan Data Management, we have added revenue enhancement capability for Medicare plans. The converging forces of the Medicare Modernization Act and state-based initiatives for broader coverage (which are philosophically aligned with most healthcare thought leaders in the Democrat-controlled legislature) are a catalyst for Medicaid growth as well. The uptake of bringing uninsured and under-insured Americans into organized systems of care may well be a larger short-term growth driver for payers (in terms of number of members if not dollars) than will Medicare. TriZetto must accordingly continue to position itself for both membership-based licensing and per-member, per-month recurring services for the managed government programs market.

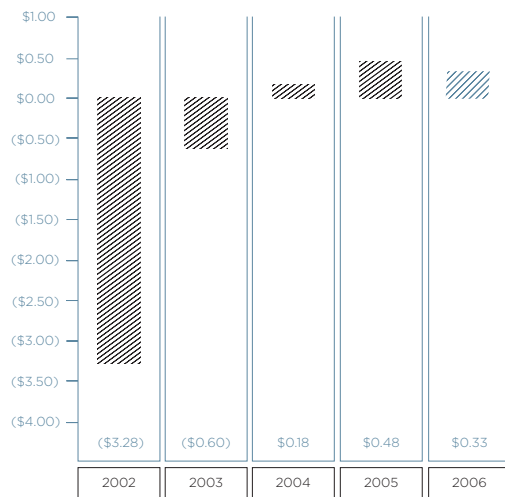
Build Additional Breadth in Component Solution Offerings

Since 2003, TriZetto's strategy has included the development of component solutions that are designed to expand the number of solutions we can offer to non-core administration customers, and to provide easily integrated additional value to our existing customers. As an example, approximately 35% of the commercially insured U.S. population is now licensed through payer customers utilizing either NetworX Modeler™ or NetworX Pricer™. Importantly, several of these customers are super-behemoth payers that do not utilize TriZetto's core administration solutions for the same membership base. We will continue to identify high-value opportunities to create new component offerings in a capital-efficient and agile manner while also evolving the delivery mechanism of our component solutions to align with the different purchasing methodologies of our customers. As an example, the term licensing model employed by QCSI provides the opportunity to develop corresponding offerings of our component products for these important customers. This would also add predictable recurring software license revenue.

Explore the Full Potential of Care Management Solutions and Offerings

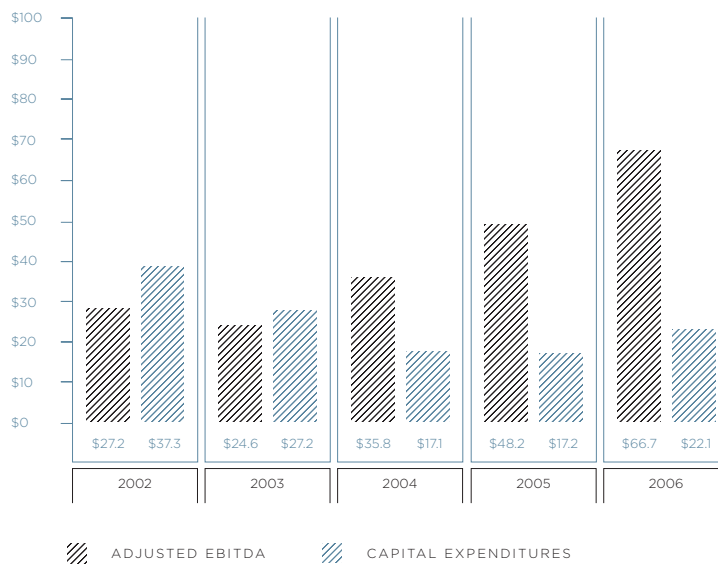
Clearly, the market opportunity around 85% of the payer's premium dollar spent on the cost of care eclipses even the exciting value of TriZetto's core administration solutions over time. Over the past several years, we have successfully repositioned TriZetto to be more than a core administration solutions company, and our acquisition of CareKey provided us with the most advanced software asset in the space to begin providing a consumer-centric linkage between health plans and their members. While we are still at the early stage in realizing our CareAdvance™ software

Diluted Earnings Per Share



Adjusted EBITDA vs. Capital Expenditures

(IN MILLIONS)

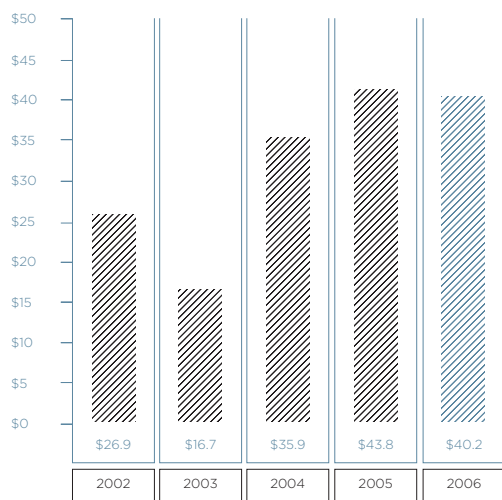


▨ ADJUSTED EBITDA ▨ CAPITAL EXPENDITURES

See page 65 for Definition and Reconciliation of Non-GAAP Financial Measures

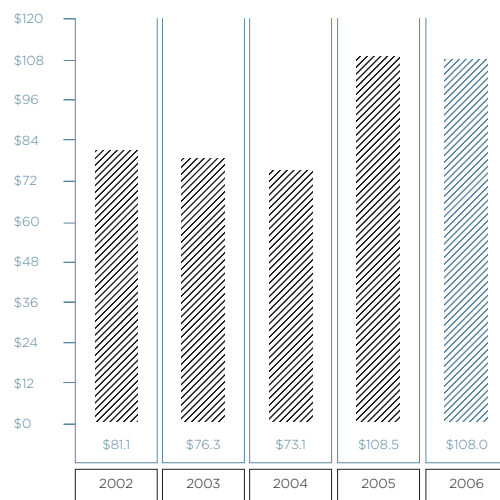
Net Cash Provided by Operations

(IN MILLIONS)



Cash and Equivalents

(IN MILLIONS)



opportunities, there are significant future opportunities to apply our core administration footprint to the care management arena. Looking toward the future, we see that no entity has yet “cracked the code” of fully integrating content with underlying administrative data and clinical methodologies for entire membership populations.

Drive Consumer Retail Healthcare Innovation

Continuing TriZetto’s strategy derived over the past several years, our focus in 2007 becomes the translation of our thought leadership into reasonably quick and measurable uptake in the market. There is no question in my mind that the ability to determine what the consumer owes at the point-of-service will become a commonplace expectation over the next five years. There is also little question that TriZetto is best positioned to deliver this “answer” across our immense core administration footprint. Variable and qualitative pay mechanisms for providers will require sophisticated claims payment capabilities like TriZetto’s, as pay-for-performance programs become more mainstream. The use of a pre-populated personal health record derived from accurate claims data will become a standard tool for both consumers and their caregivers, and Personal CareAdvance® has the opportunity to be a highly efficient and transportable standard among our customer base. Our leading research and development regarding new consumer-retail processes required among health plans and their broker, employer, provider and consumer constituents creates a new “greenfield” for both component and end-to-end integrated offerings.

Realizing the Value of Vision, Focus and Reach

In the 10 years since its founding in 1997, TriZetto’s unique vision, focus and reach have made the company a leading source for success-critical software and services for payers. We have achieved a position in the industry such that TriZetto technology is often the first choice.

The financial results for 2006 demonstrate the value of our three distinguishing attributes. The 54% increase in software product revenue – the biggest year-over-year increase in four years – says much about TriZetto’s expanded customer value. At the same time, the 38% increase in Adjusted EBITDA demonstrates the growing returns of TriZetto’s business operations.

As each year’s results evidence the continuous growth, improvement and refinement of TriZetto’s business model, I believe that our company is prepared for even greater success in the future.

Sincerely,



Jeffrey H. Margolis

Chairman of the Board and Chief Executive Officer
April 30, 2007

SELECTED FINANCIAL DATA

The following selected consolidated financial data, except as noted herein, has been taken or derived from our audited consolidated financial statements and should be read in conjunction with the full consolidated financial statements included herein.

	YEARS ENDED DECEMBER 31,				
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)	2006	2005	2004	2003	2002
CONSOLIDATED STATEMENT OF OPERATIONS DATA:					
Revenue:					
Services and other	\$272,943	\$243,483	\$223,257	\$244,641	\$ 233,019
Products	74,994	48,736	51,308	45,688	32,131
Total revenue	347,937	292,219	274,565	290,329	265,150
Operating costs and expenses:					
Cost of revenue—services and other ⁽¹⁾	165,229	144,318	157,573	217,552	174,073
Cost of revenue—products (excludes amortization of acquired technology)	14,175	14,210	12,025	6,455	3,747
Research and development	42,789	31,655	30,398	24,823	21,911
Selling, general and administrative	103,809	76,758	59,980	52,138	53,966
Restructuring and impairment charges ⁽²⁾	—	—	—	3,769	651
Impairment of goodwill ⁽³⁾	—	—	—	—	97,479
Impairment of acquired intangible assets ⁽³⁾	—	—	—	—	33,540
Amortization of acquired technology	4,120	660	440	7,120	18,335
Amortization of acquired other intangible assets	867	2,225	3,804	3,788	9,692
Total operating costs and expenses	330,989	269,826	264,220	315,645	413,394
Income (loss) from operations	16,948	22,393	10,345	(25,316)	(148,244)
Interest income	3,823	1,619	583	970	1,609
Interest expense	(3,342)	(1,579)	(1,369)	(2,005)	(1,479)
Other income	180	—	—	—	—
Income (loss) before provision for income taxes	17,609	22,433	9,559	(26,351)	(148,114)
Provision for income taxes	(2,494)	(412)	(1,101)	(1,124)	(250)
Net income (loss)	\$ 15,115	\$ 22,021	\$ 8,458	\$ (27,475)	\$ (148,364)
Net income (loss) per share:					
Basic	\$ 0.36	\$ 0.52	\$ 0.18	\$ (0.60)	\$ (3.28)
Diluted	\$ 0.33	\$ 0.48	\$ 0.18	\$ (0.60)	\$ (3.28)
Shares used in computing net income (loss) per share:					
Basic	42,389	41,948	46,794	46,170	45,256
Diluted	45,691	45,503	48,157	46,170	45,256

	DECEMBER 31,				
(IN THOUSANDS)	2006	2005	2004	2003	2002
CONSOLIDATED BALANCE SHEET DATA:					
Cash, cash equivalents, restricted cash, and short-term investments	\$107,978	\$108,483	\$ 73,147	\$ 76,347	\$ 81,117
Total assets	382,600	317,739	239,884	233,308	237,996
Total short-term debt and capital lease obligations	1,576	2,099	43,786	34,920	17,921
Total long-term debt and capital lease obligations	114,030	101,065	13,838	7,155	15,116
Total stockholders' equity	133,907	101,358	86,933	113,523	137,414

⁽¹⁾Included in cost of revenue are charges associated with loss on contracts. During the fourth quarter of 2003, we decided to wind-down our outsourcing services to physician group customers. As a result of this decision, we estimated that the existing customer agreements would generate a total loss of \$11.3 million until the terms of these agreements expired in 2008. We recorded a loss accrual in the fourth quarter of 2003. Through discussions and negotiations, we were able to accelerate the termination of our services agreements with certain physician group customers and implemented cost cutting measures that reduced the expected future costs to support our remaining customers. As a result of these actions, we were able to reverse approximately \$5.9 million of previously accrued loss on contracts charges in 2004. Early in the second quarter of 2005, we executed termination agreements with our two remaining physician group customers. We continued to provide outsourced business services through May 2005, when the transition services were completed. The completion of these services to the remaining customers allowed us to reverse the remaining balance in the loss on contracts accrual of \$2.9 million in the second quarter of 2005. The total amount of loss actually incurred related to the outsourcing services to physician group customers was \$2.1 million in 2004 and \$403,000 in the first six months of 2005.

In December 2003, we negotiated a settlement regarding out-of-scope work related to one of our large fixed fee implementation projects. As a result of this settlement, we estimated that this project would generate a total loss of \$3.7 million until its completion, which was expected to occur in mid-2004. We recorded a loss accrual in the fourth quarter of 2003. In 2004, we determined that the large fixed fee implementation project would require a greater effort to complete than previously estimated. As a result,

we accrued an additional \$5.0 million of loss on contracts charges in the first six months of 2004. In the fourth quarter of 2004, we negotiated a settlement of additional out-of-scope work, which decreased the total loss on the project and resulted in the reversal of approximately \$455,000 of previously accrued loss on contracts charges. This fixed fee implementation was completed by the end of the first quarter of 2005. The total amount of loss actually incurred on this project was \$7.7 million in 2004 and \$484,000 in the first quarter of 2005.

⁽²⁾In the fourth quarter of 2003, we made a decision to wind-down our outsourcing services to physician groups and to discontinue our outsourcing services to certain non-Facets® payer customers. We estimated that our future net cash flows from the assets used in these businesses would not recover their net book value. Accordingly, a total charge of \$4.0 million was taken as a restructuring and impairment charge in the fourth quarter of 2003, which represented the net book value of these assets. The assets were written off in the first quarter of 2004.

⁽³⁾After the end of the fourth quarter of 2002, our market capitalization decreased to a level that required us to perform additional analyses under FASB Statement No. 142 to quantify the amount of impairment to goodwill. This analysis resulted in an impairment charge to goodwill of \$97.5 million as of December 31, 2002. The decrease in market capitalization was also an indicator that our other intangible assets might also be impaired as of December 31, 2002, and they were also tested for impairment in accordance with FASB Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." The analysis resulted in an additional impairment charge of \$33.5 million.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

We offer a broad portfolio of proprietary information technology products and services targeted to the payer industry, which is comprised of health insurance plans and third party benefits administrators. We offer enterprise claims administration software, including Facets Extended Enterprise™ and QicLink Extended Enterprise™, and enterprise cost and quality of care software, including Clinical CareAdvance™, Personal CareAdvance™ and our NetworX™ suite for provider network management. We also provide a number of component software solutions and add-ons to the enterprise software solutions, including CDH Account Management, Workflow, HealthWeb® and Benefit Cost Modeler. To support these software products, we provide software hosting services and business process outsourcing services, giving customers variable cost alternatives to licensing software, as well as strategic, implementation and optimization consulting services. As of December 2006, we served 320 unique customers in the health plan and benefits administrator markets, which we refer to as payers. In 2006, these markets represented approximately 90% and 10% of our total revenue, respectively.

We measure financial performance by monitoring revenue, bookings and backlog, and net income. Total revenue for 2006 was \$347.9 million compared to \$292.2 million for 2005. Services and other revenue for 2006 was \$272.9 million compared to \$243.5 million for 2005. Products revenue for 2006 was \$75.0 million compared to \$48.7 million for 2005. Operating costs and expenses for 2006 were \$331.0 million compared to \$269.8 million for 2005. Bookings for 2006 were \$381.6 million compared to \$296.6 million for 2005. Backlog at December 31, 2006 was \$858.2 million compared to \$703.4 million at December 31, 2005. Net income in 2006 was \$15.1 million compared to \$22.0 million in 2005. These financial comparisons are further explained in the section below, "Results of Operations."

We generate services revenue from several sources, including the provision of outsourcing services, such as software hosting and business process outsourcing services, the sale of maintenance and support for our proprietary and certain of our non-proprietary software products, and from consulting fees for implementation, installation, configuration, business process engineering, data conversion, testing and training related to the use of our proprietary, and third-party licensed products. We generate products revenue from the licensing of our software. Cost of revenue includes costs related to the products and services we provide to our customers and costs associated with the operation and maintenance of our customer connectivity centers. These costs include salaries and related expenses for consulting personnel, customer connectivity centers' personnel, customer support personnel, application software license fees, amortization of capitalized software development costs, telecommunications costs, facility costs, and maintenance costs. Research and development ("R&D") expenses are salaries and related expenses associated with the development of software applications prior to establishing technological feasibility. Such expenses include compensation paid to software engineering personnel and other administrative, infrastructure and facility expenses and fees to outside contractors and consultants.

Selling, general and administrative expenses consist primarily of salaries and related expenses for sales, sales commissions, account management, marketing, administrative, finance, legal, human resources and executive personnel, and fees for certain professional services.

As part of our growth strategy, we intend to increase revenue per customer by continuing to introduce new complementary products and services, including new cost and quality of care products and services, to our established enterprise software and hosting and business process outsourcing services. Some of these service offerings, including hosting, business process outsourcing, and consulting have a higher cost of revenue, resulting in lower gross profit margins. Therefore, to the extent that our revenue increases through the sale of these lower margin product and service offerings, our total gross profit margin may decrease.

We are continuing to target larger health plan customers. This has given us the opportunity to sell additional services such as software hosting, business intelligence, and business process outsourcing services. As the technology requirements of our customers become more sophisticated, our service offerings have become more complex. This has lengthened our sales cycles and made it more difficult for us to predict the timing of our software and services sales.

In late 2003, a management decision was made to exit certain non-strategic and less profitable product offerings and business lines. This decision included winding down services related to our physician group customers, as well as the planned elimination of our hosting and business process outsourcing services for two competing third-party software platforms. Early in the second quarter of 2005, we executed termination agreements with the last two of our remaining physician group customers. We continued to provide outsourced business services through May 2005 when the transition services were completed.

On December 22, 2006, we acquired all of the issued and outstanding shares of Plan Data Management, Inc. The estimated purchase price as of December 31, 2006 was approximately \$19.6 million, which consisted of 491,488 shares of our common stock with a value of \$16.28 per share (which represents the average closing price of TriZetto's common stock for the 20 trading days ending October 27, 2006), cash payments of \$8.0 million, assumed liabilities of \$3.1 million and estimated acquisition-related costs of \$500,000. Due to the close of the acquisition late in the year, the issuance of the 491,488 shares of common stock and the cash payment of \$8.0 million to PDM stockholders and option holders were not completed prior to December 31, 2006. However, these amounts were accrued as of December 31, 2006. The computation of earnings per share for the year ended December 31, 2006 did not include the issuance of the 491,488 shares of common stock or the financial operating results of PDM since the impact of these amounts was not material.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities at the date of our financial statements. Those estimates are based on our experience, terms of existing contracts, observance of trends in the industry, information provided by our customers and information available from other outside sources, which are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

The following critical accounting policies affect the more significant judgments and estimates used in the preparation of our consolidated financial statements, and may potentially result in materially different results under different assumptions and conditions. We have identified the following as critical accounting policies to our company:

- Revenue recognition;
- Up-front payments to customers;
- Sales returns and allowance for doubtful accounts;
- Capitalization of software development costs;
- Goodwill and other intangible assets;
- Litigation accruals;
- Self-insurance;
- Bonus accrual;
- Income taxes; and
- Stock-based compensation.

This listing is not a comprehensive list of all of our accounting policies. For a detailed discussion on the application of these and other accounting policies, see Note 2 of Notes to Consolidated Financial Statements.

REVENUE RECOGNITION. We recognize revenue when persuasive evidence of an arrangement exists, the product or service has been delivered, fees are fixed or determinable, collection is reasonably assured and all other significant obligations have been fulfilled. Our revenue is classified into two categories: services and other, and products. For the year ended December 31, 2006, approximately 78% of our total revenue was generated from services and other revenue and 22% was from products revenue.

We follow the provisions of the Securities and Exchange Commission Staff Accounting Bulletin No. 104, "Revenue Recognition," AICPA Statement of Position ("SOP") 97-2, "Software Revenue Recognition," as amended, EITF Issue 00-3, "Application of AICPA Statement of Position 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware," and EITF Issue 00-21, "Revenue Arrangements with Multiple Deliverables."

We generate services revenue from several sources, including the provision of outsourcing services, such as software hosting and

other business services, and the sale of maintenance and support for our proprietary software products. We apply EITF 00-3 to hosting arrangements that include the licensing of software. A software element covered by SOP 97-2 is present in a hosting arrangement if the customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty and it is feasible for the customer to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software. Outsourcing services revenue is typically billed and recognized monthly over the contract term, generally three to seven years. Many of our outsourcing agreements require us to maintain a certain level of operating performance. We record revenue net of estimated penalties resulting from any failure to maintain the level of operating performance. These penalties have not been significant in the past. Software maintenance and support revenues are typically based on one-year renewable contracts and are recognized ratably over the contract period. Payment for software maintenance received in advance is recorded on the balance sheet as deferred revenue. Certain royalty costs paid to third-party software vendors associated with software maintenance are amortized over the software maintenance period.

We also generate services revenue from consulting fees for implementation, installation, configuration, business process engineering, data conversion, testing and training related to the use of our proprietary and third party licensed products. In certain instances, we also generate services revenue from customization services of our proprietary licensed products. We recognize revenue for these services as they are performed. When we cannot reasonably estimate the cost to complete, we recognize revenue using the completed contract method, upon completion of all contractual obligations. We also generate services revenue from set-up fees, which are services, hardware, and software associated with preparing our customer connectivity center or a customer's data center in order to ready a specific customer for software hosting services. The set-up fees are usually separate and distinct from the hosting fees, and performance of the set-up services represents the culmination of the earnings process. We recognize revenue for these services as they are performed. We generate other revenue from certain one-time charges, including certain contractual fees such as termination fees and change of control fees, and we recognize the revenue for these fees once the termination or change of control is guaranteed, there are no remaining substantive performance obligations and collection is reasonably assured. Other revenue is also generated from fees related to our product related conference.

For multiple element arrangements, such as software license, consulting services, outsourcing services and maintenance, and where vendor-specific objective evidence ("VSOE") of fair value exists for all undelivered elements, we account for the delivered elements in accordance with the "residual method." VSOE of fair value is determined for each undelivered element based on how it is sold separately, or in the case of maintenance, the renewal rate. For arrangements in which VSOE does not exist for each undelivered

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

element, including specified product and upgrade rights, revenue for the delivered element is deferred and not recognized until VSOE is available for the undelivered element or delivery of each element has occurred. In determining VSOE for the undelivered elements, no portion of the discount is allocated to specified or unspecified product or upgrade rights.

Under the residual method, the arrangement fee is recognized as follows: (1) the total fair value of the undelivered elements, as indicated by VSOE, is deferred and subsequently recognized in accordance with the relevant sections of SOP 97-2 and (2) the difference between the total arrangement fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements.

We generate products revenue from the licensing of our software. Under SOP 97-2, software license revenue is recognized upon the execution of a license agreement, upon delivery of the software, when fees are fixed or determinable, when collectibility is probable and when all other significant obligations have been fulfilled. For software license agreements in which customer acceptance is a significant condition of earning the license fees, revenue is not recognized until acceptance occurs. For software license agreements that require significant customization or modification of the software, revenue is recognized as the customization services are performed.

UP-FRONT PAYMENTS TO CUSTOMERS. We may pay certain up-front amounts to our customers in connection with the establishment of our hosting and outsourcing services contracts. Under EITF 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)," these payments are capitalized and amortized over the life of the contract as a reduction to revenue, provided that such amounts are recoverable from future revenue under the contract. If an up-front payment is not recoverable from future revenue, or it cannot be offset by contract cancellation penalties paid by the customer, the amount will be expensed in the period it is deemed unrecoverable. Unamortized up-front fees were \$6.2 million and \$7.7 million as of December 31, 2006 and 2005, respectively.

SALES RETURNS AND ALLOWANCE FOR DOUBTFUL ACCOUNTS. We maintain an allowance for sales returns and doubtful accounts to reserve for estimated discounts, pricing adjustments, and other sales allowances. The reserve is charged to revenue in amounts sufficient to maintain the allowance at a level we believe is adequate based on historical experience and current trends. We also maintain an allowance for doubtful accounts to reflect estimated losses resulting from the inability of customers to make required payments. We base this allowance on estimates after consideration of factors such as the composition of the accounts receivable aging and bad debt history and our evaluation of the financial condition of the customers. If the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional sales allowances and bad debt expense may be required. We typically do not require collateral. Historically, our estimates for sales returns and doubtful account reserves have been adequate to cover accounts

receivable exposures. We continually monitor these reserves and make adjustments to these provisions when we believe actual credits or other allowances may differ from established reserves.

For the twelve month period ended December 31, 2006, our allowance for sales returns and doubtful accounts increased by \$2.9 million. In December 2006, we entered into a settlement with one of our larger customers that had disputed payments due from a software implementation project. The amounts represented revenue recorded in the first two quarters of 2006 and were included in the allowance for sales returns and a reduction to revenue in the quarter ended September 30, 2006. The settlement fully resolved the issues and resulted in a payment that was less than the amount previously disputed. We do not believe the increase in the allowance for sales returns is a trend or representative of more significant issues in our business.

CAPITALIZATION OF SOFTWARE DEVELOPMENT COSTS. The capitalization of software costs includes developed technology acquired in acquisitions and costs incurred by us in developing our products that qualify for capitalization. We account for our software development costs, other than costs for internal-use software, in accordance with FASB Statement No. 86, "Accounting for Costs of Computer Software to be Sold, Leased or Otherwise Marketed." We capitalize costs associated with product development, coding and testing subsequent to establishing technological feasibility of the product. Technological feasibility is established after completion of a detailed program design or working model. Capitalization of computer software costs ceases upon a product's general availability release. Capitalized software development costs are amortized over the estimated useful life of the software product starting from the date of general availability.

On a quarterly basis, we monitor the expected net realizable value of the capitalized software for factors that would indicate impairment, such as a decline in the demand, the introduction of new technology, or the loss of a significant customer. As of December 31, 2006, our evaluation determined that the carrying amount of these assets was not impaired.

GOODWILL AND OTHER INTANGIBLE ASSETS. Acquisitions are accounted for using the purchase method of accounting. The purchase price is allocated to the tangible and intangible assets acquired and the liabilities assumed on the basis of their estimated fair market values on the acquisition date. The excess of the purchase price over the estimated fair market value of the assets purchased and liabilities assumed is allocated to goodwill and other intangible assets.

Under FASB Statement No. 142, "Goodwill and Other Intangible Assets," goodwill and intangible assets deemed to have indefinite lives are subject to annual (or more often if indicators of impairment exist) impairment tests using a two-step process. The first step looks for indicators of impairment. If indicators of impairment are revealed in the first step, then the second step is conducted to measure the amount of the impairment, if any. We performed our annual

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

impairment test on March 31, 2006, and this test did not reveal indications of impairment.

LITIGATION ACCRUALS. Pending unsettled lawsuits involve complex questions of fact and law and may require expenditure of significant funds. From time to time, we may enter into confidential discussions regarding the potential settlement of such lawsuits; however, there can be no assurance that any such discussions will occur or will result in a settlement. Moreover, the settlement of any pending litigation could require us to incur settlement payments and costs. In the period in which a new legal case arises, an expense will be accrued if our liability to the other party is probable and can be reasonably estimated. On a quarterly basis, we review and analyze the adequacy of our accruals for each individual case for all pending litigations. Adjustments are recorded as needed to ensure appropriate levels of reserve. Our attorney fees and other defense costs related to litigation are expensed as incurred.

SELF-INSURANCE. Effective January 1, 2006, we became self-insured for certain losses related to employee health and dental benefits. We record a liability based on an estimate of claims incurred but not recorded determined based on actuarial analysis of historical claims experience and historical industry data. We maintain individual and aggregate stop-loss coverages with a third party insurer to limit our total exposure for these programs. Our self-insurance liability contains uncertainties because the calculation requires management to make assumptions and apply judgment to estimate the ultimate cost to settle reported claims and claims incurred but not reported as of the balance sheet date. We do not believe that there is a reasonable likelihood that there will be a material change in the future assumptions or estimates we use to calculate our self-insurance liability. However, if actual results are not consistent with our assumptions and estimates, we may be exposed to losses or gains that could be material.

BONUS ACCRUAL. Our bonus model is designed to project the level of funding required under the bonus program as approved by the Compensation Committee of the Board of Directors. A significant portion of the bonus program is based on the Company meeting certain financial objectives, such as revenue, earnings per share, and the level of capital spending. The expense related to the bonus program is accrued in the year of performance and paid in the first quarter following the fiscal year end. The bonus model is analyzed and adjusted on a quarterly basis as necessary based on achievement of targets.

INCOME TAXES. We account for income taxes under FASB Statement No. 109, "Accounting for Income Taxes." This statement requires the recognition of deferred tax assets and liabilities for the future consequences of events that have been recognized in our financial statements or tax returns. The measurement of the deferred items is based on enacted tax laws. In the event the future consequences of differences between financial reporting bases and the tax bases of our assets and liabilities result in a deferred tax asset, FASB Statement No. 109 requires an evaluation of the probability of being able to realize the future benefits indicated by

such an asset. A valuation allowance related to a deferred tax asset is recorded when it is more likely than not that some portion or the entire deferred tax asset will not be realized. During 2006, our valuation allowance decreased by \$20.1 million, \$15.4 million as a result of purchase accounting and related deferred tax accounting adjustments associated with the acquisition of CareKey, Inc. ("CareKey") and \$4.7 million as a result of the utilization of net operating loss carryovers and true-ups. Of the remaining valuation allowance of \$2.1 million, approximately \$1.5 million will reverse through the income statement and approximately \$600,000 will reverse to goodwill.

STOCK-BASED COMPENSATION. Effective January 1, 2006, we adopted the fair value recognition provisions of FASB Statement No. 123R, "Share-Based Payment," using the modified prospective transition method, and therefore have not restated prior periods' results. Under this method, we recognize compensation expense for all share-based payments granted after January 1, 2006 and for all share-based payments granted prior to, but not yet vested as of, January 1, 2006. Under the fair value recognition provisions of FASB Statement No. 123R, stock-based compensation cost is estimated at the grant date based on the award's fair-value and is recognized as expense ratably over the requisite service period. We use the Black-Scholes option-pricing model to calculate fair value which requires the input of highly subjective assumptions. These assumptions include estimating the length of time employees will retain their vested stock options before exercising them ("expected term"), the estimated volatility of our common stock price over the expected term and the number of options that will ultimately not complete their vesting requirements ("forfeitures"). The assumptions used in calculating the fair value of share-based payment awards represent management's best estimates, but these estimates involve inherent uncertainties and the application of management judgment. As a result, if factors change and we use different assumptions, our stock-based compensation could be materially different in the future. In addition, if our actual forfeiture rate is materially different from our estimate, stock-based compensation expense could be significantly different from what we have recorded in the current period.

RECENT ACCOUNTING PRONOUNCEMENTS

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). FIN 48 applies to all tax positions accounted for under SFAS No. 109, "Accounting for Income Taxes," and defines the confidence level that a tax position must meet in order to be recognized in the financial statements. The interpretation requires that the tax effects of a position be recognized only if it is "more-likely-than-not" to be sustained by the taxing authority as of the reporting date. If a tax position is not considered "more-likely-than-not" to be sustained then no benefits of the position are to be recognized. FIN 48 requires additional disclosures and is effective as of the beginning of the first fiscal year beginning after December 15, 2006. We do not expect the adoption of FIN 48 to have a material impact on our consolidated results of operations and financial condition.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

REVENUE INFORMATION

Revenue by customer type and revenue mix for the years ended December 31, 2006, 2005, and 2004, is as follows (amounts in thousands):

YEARS ENDED DECEMBER 31,	2006		2005		2004	
REVENUE BY CUSTOMER TYPE:						
Health plans	\$312,567	90%	\$256,162	88%	\$224,806	82%
Benefits administration	35,370	10%	35,915	12%	45,080	16%
Provider	—	0%	142	0%	4,679	2%
Total revenue	\$347,937	100%	\$292,219	100%	\$274,565	100%
REVENUE MIX:						
Services and other revenue						
Outsourced business services	\$ 86,877	25%	\$ 79,418	27%	\$ 89,916	33%
Software maintenance	88,628	25%	80,719	28%	69,065	25%
Consulting services and other	97,438	28%	83,346	28%	64,276	23%
Services and other revenue total	272,943		243,483		223,257	
Products revenue						
Software license fees	74,994	22%	48,736	17%	51,308	19%
Total revenue	\$347,937	100%	\$292,219	100%	\$274,565	100%

Our total backlog is defined as the revenue we expect to generate in future periods from existing customer contracts. Our 12-month backlog is defined as the revenue we expect to generate from existing customer contracts over the next 12 months. Most of the revenue in our backlog is derived from multi-year service revenue contracts (including software hosting, business process outsourcing, IT outsourcing, and software maintenance with periods up to seven years) and consulting contracts. Consulting revenue is included in the backlog when the revenue from such consulting contract is expected to be recognized over a period exceeding 12 months.

Backlog can change due to a number of factors, including unforeseen changes in implementation schedules, contract cancellations (subject to penalties paid by the customer), or customer financial difficulties. In such event, unless we enter into new customer agreements that generate enough revenue to replace or exceed the revenue we expect to generate from our backlog in any given quarter, our backlog will decline. Our backlog at any date may not indicate demand for our products and services and may not reflect actual revenue for any period in the future. Our 12-month and total backlog data are as follows (in thousands):

	12/31/06	9/30/06	6/30/06	3/31/06	12/31/05	9/30/05	6/30/05	3/31/05	12/31/04
12-month backlog	\$213,300	\$191,600	\$186,100	\$187,300	\$185,100	\$194,500	\$174,800	\$172,000	\$173,100
Total backlog	\$858,200	\$747,800	\$717,500	\$704,700	\$703,400	\$663,100	\$638,900	\$604,800	\$585,000

Total quarterly bookings equal the estimated total dollar value of the contracts signed in the quarter. Bookings can vary substantially from quarter to quarter, based on a number of factors, including the number and type of prospects in our pipeline, the length of time it takes a prospect to reach a decision and sign the contract, and the effectiveness of our sales force. Included in quarterly bookings are up to seven years of maintenance revenue and hosting and other services revenue. Bookings for each of the quarters are as follows (in thousands):

	12/31/06	9/30/06	6/30/06	3/31/06	12/31/05	9/30/05	6/30/05	3/31/05	12/31/04
Quarterly bookings	\$139,700	\$75,900	\$78,600	\$87,400	\$83,100	\$75,100	\$85,300	\$53,100	\$58,800

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

YEAR ENDED DECEMBER 31, 2006
COMPARED TO THE YEAR ENDED DECEMBER 31, 2005.

REVENUE. Total revenue increased \$55.7 million, or 19%, to \$347.9 million in 2006 from \$292.2 million for 2005. Of this increase, \$29.4 million related to services and other revenue and \$26.3 million related to products revenue.

SERVICES AND OTHER REVENUE. Services and other revenue includes outsourced business services (primarily software hosting and business process outsourcing), maintenance fees related to our software license contracts, consulting services and other revenue. Services and other revenue increased \$29.4 million, or 12%, to \$272.9 million in 2006 from \$243.5 million in 2005. This increase was the result of a \$14.0 million increase in consulting services and other revenue, a \$7.9 million increase in software maintenance revenue, and an increase of \$7.5 million in outsourced business services. The increase in consulting services and other revenue was due primarily to new Facets®, QicLink™, NetworX™ and CareAdvance™ implementations. The increase in software maintenance revenue was attributable primarily to new agreements for certain Facets®, NetworX™, HealthWeb® and CareAdvance™ customers and annual rate increases from existing customers. The overall increase in outsourced business services revenue was primarily due to new Facets® and CareAdvance™ hosted customers and increased membership from existing Facets® hosted customers.

PRODUCTS REVENUE. Products revenue, which includes software license sales, increased \$26.3 million, or 54%, to \$75.0 million in 2006 from \$48.7 million in 2005 resulting from increased sales for new Facets®, NetworX™, HealthWeb® and CareAdvance™ license sales to our health plan customers.

COST OF REVENUE – SERVICES AND OTHER. Cost of revenue for services and other increased \$20.9 million, or 15%, to \$165.2 million in 2006 from \$144.3 million in 2005 to support the increase in our outsourced business services, software maintenance, and consulting services and other revenue.

Cost of revenue for our outsourced business services and software maintenance revenue increased \$6.1 million, primarily attributable to higher compensation costs of \$3.0 million, increased investment in infrastructure and technology of \$3.0 million, a \$2.9 million reversal of a loss on contracts accrual and a \$1.7 million increase in other costs, partially offset by a \$2.5 million decrease in depreciation expense and lower costs for outside consultants of \$1.8 million. Higher compensation costs were impacted by the annual merit increases in early 2006, the adoption of SFAS 123R and a reassignment of product and development leaders and other executives to more appropriately align their responsibilities with our market facing strategy. Higher infrastructure and technology costs were driven by customer and internal upgrades, new operating lease agreements for data center equipment and related maintenance. In 2005, we executed termination agreements with our two remaining physician group

customers, allowing us to reverse the remaining balance in our loss on contracts accrual. The overall increase in other costs was primarily related to bad debt expense, postage and freight, telecommunications, and travel. The reduction in depreciation expense related primarily to fully depreciated assets and a lower mix of equipment with longer estimated useful lives, offset in part by depreciation related to new additions in 2006. Reduced fees from our outside consultants were attributable to a higher utilization of internal resources for product support services.

Cost of revenue for our consulting services and other revenue increased \$14.8 million, primarily attributable to higher compensation costs of \$12.8 million, increased investment in infrastructure and technology of \$2.1 million, increased travel costs of \$1.1 million and a \$1.1 million increase in other costs, partly offset by a \$2.6 million reduction in utilization of outside consultants. Compensation costs were impacted by an increase in headcount, the adoption of SFAS 123R and a reassignment of product and development leaders and other executives to more appropriately align their responsibilities with our market facing strategy. Higher infrastructure and technology costs and travel costs were also impacted by increased headcount and the increased level of implementation projects. The overall increase in other costs was primarily related to facilities expense associated with a new facility acquired in the December 2005 acquisition of CareKey and expansion projects for certain of our existing facilities, as well as an increase in telecom usage. Reduced fees from outside consultants were attributable to a higher utilization of internal resources on implementation projects.

As a percentage of total revenue, cost of revenue for services and other approximated 48% in 2006 compared with 49% in 2005.

COST OF REVENUE – PRODUCTS. Cost of revenue for products, which excludes the amortization of acquired technology, remained flat year over year. Amortization of capitalized software development costs increased \$1.6 million, partly offset by a decrease in software customer pass-through costs of \$1.0 million and a \$700,000 decrease in royalty expense. The increase in amortization of capitalized software development costs resulted from new versions of certain of our proprietary software products which were released for sale in mid to late 2005 and in 2006. Software customer pass-through costs decreased due primarily to a decreased volume of customer pass-through agreements. The decrease in royalty expense was due primarily to the elimination of a pre-acquisition royalty relationship with CareKey in 2005. As a percentage of total revenue, cost of revenue for products approximated 4% in 2006 compared with 5% in 2005.

RESEARCH AND DEVELOPMENT (R&D) EXPENSES. R&D expenses increased \$11.1 million, or 35%, to \$42.8 million in 2006 from \$31.7 million in 2005. The overall increase in R&D expenses was due primarily to higher compensation costs which were impacted by our annual merit increases in early 2006, increased headcount related to the development of cost and quality of care solutions following the December 2005 acquisition of CareKey and the adoption

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

of SFAS 123R. As a percentage of total revenue, R&D expenses approximated 12% in 2006 compared with 11% in 2005. R&D expenses, as a percentage of total R&D expenditures (which includes capitalized R&D expenses of \$8.6 million in 2006 and 2005), was 83% in 2006 compared with 79% in 2005.

SELLING, GENERAL AND ADMINISTRATIVE (SG&A) EXPENSES. SG&A expenses increased \$27.0 million, or 35%, to \$103.8 million in 2006 from \$76.8 million in 2005. The overall increase resulted primarily from a \$15.0 million legal settlement that occurred in the third quarter of 2006, \$10.7 million in higher compensation and related costs, increased investment in infrastructure and technology of \$1.5 million, and an increase of approximately \$700,000 in legal costs. These increases were offset in part by a \$1.0 million reduction in utilization of outside consultants and a net decrease of \$400,000 related to facilities expense. In the third quarter of 2006, we entered into a settlement agreement with McKesson Information Solutions LLC ("McKesson") by which we agreed to pay McKesson a one-time royalty fee of \$15.0 million. Higher compensation and related costs were impacted by our annual merit increases in early 2006, increased headcount and recruiting fees related to new hires, and our adoption of SFAS 123R, offset in part by a reassignment of product and development leaders and other executives to more appropriately align their responsibilities with our market facing strategy. Investment in infrastructure and technology costs was driven primarily by support for internal growth and upgrades. The \$700,000 increase in legal fees was attributable to a \$1.1 million insurance reimbursement related to a legal settlement that occurred in 2005, partially offset by a \$400,000 decrease in litigation defense costs in 2006. The lower utilization of outside consultants related to strategic planning and process improvement projects in 2005. The net decrease in facilities expense is due to facility closures related to lease termination costs in 2005 of \$900,000, offset by a \$500,000 increase related primarily to incremental costs associated with the acquisition of CareKey in December 2005 and expansion projects for certain of our existing facilities. As a percentage of total revenue, selling, general and administrative expenses approximated 30% in 2006 compared with 26% in 2005.

AMORTIZATION OF INTANGIBLE ASSETS. Amortization of intangible assets is comprised of acquired technology and acquired other intangible assets. In total, amortization of intangible assets increased \$2.1 million, or 73%, to \$5.0 million in 2006 from \$2.9 million in 2005.

AMORTIZATION OF ACQUIRED TECHNOLOGY. The amortization of acquired technology is excluded from cost of revenue—products and consists primarily of amounts amortized with respect to core or completed technology and existing software. Amortization of acquired technology increased \$3.4 million, or 524%, to \$4.1 million in 2006 from \$660,000 in 2005. The increase was due to the amortization of core technology and existing software acquired through the CareKey acquisition.

AMORTIZATION OF ACQUIRED OTHER INTANGIBLE ASSETS. Amortization of acquired other intangible assets decreased \$1.3 million, or 61%, from \$2.2 million in 2005 to \$870,000 in 2006. The decrease was due primarily to certain intangible assets acquired in previous years, which were fully amortized in late 2005 and early 2006.

Future amortization expense related to existing intangible assets is estimated to be as follows (in thousands):

FOR THE YEARS ENDING DECEMBER 31,	ACQUIRED TECHNOLOGY	ACQUIRED OTHER INTANGIBLE ASSETS	TOTAL
2007	\$ 4,120	\$ 852	\$ 4,972
2008	4,120	852	4,972
2009	3,680	852	4,532
2010	3,460	852	4,312
2011 and thereafter	4,300	4,259	8,559
Total	\$19,680	\$7,667	\$27,347

Amortization expense related to existing intangible assets will vary from amounts identified above in the event we recognize impairment charges prior to the amortized useful life of any intangible assets. Additionally, amortization expense will vary from amounts identified above when the final accounting for the PDM and QCSI acquisitions are completed, and the allocation between goodwill and identifiable intangible assets is recorded.

INTEREST INCOME. Interest income increased \$2.2 million, or 136%, to \$3.8 million in 2006 from \$1.6 million in 2005. The increase is due primarily to higher cash balances in our operating and investment accounts, resulting primarily from the \$100.0 million convertible debt issued in 2005.

INTEREST EXPENSE. Interest expense increased \$1.7 million, or 112%, to \$3.3 million in 2006 from \$1.6 million in 2005. The increase relates primarily to a \$2.1 million increase in interest charges incurred on the \$100.0 million convertible debt issued in October 2005 and an increase of \$100,000 related to our line of credit borrowings. These increases were offset in part by a decrease of \$500,000 related primarily to certain capital leases ending in late 2005 and early 2006 and the IMS Health note payable, which was fully repaid in January 2005.

PROVISION FOR INCOME TAXES. Provision for income taxes was \$2.5 million in 2006 compared to \$412,000 in 2005. The provision increase is due mostly to an increase in state income taxes as a result of having previously utilized many of our state net operating loss carryovers, net of a release of a portion of our tax contingency reserve and state tax refunds received related to prior years for which income tax benefit was not previously recorded. The effective tax rate was 14.2% for 2006, which was lower than the Federal statutory rate primarily due to the decrease in (release of) valuation allowance, which occurred as a result of utilization of net operating loss carryovers, and the increase in state income taxes. The effective tax rate was 1.8% for 2005.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

YEAR ENDED DECEMBER 31, 2005
COMPARED TO THE YEAR ENDED DECEMBER 31, 2004.

REVENUE. Total revenue increased \$17.6 million, or 6%, to \$292.2 million in 2005 from \$274.6 million in 2004. Services and other revenue increased \$20.2 million and products revenue decreased \$2.6 million.

SERVICES AND OTHER REVENUE. Services and other revenue includes outsourced business services (primarily software hosting and business process outsourcing), maintenance fees related to our software license contracts, consulting services and other revenue. Services and other revenue increased \$20.2 million, or 9%, to \$243.5 million in 2005 from \$223.3 million in 2004. This increase was the result of \$19.1 million in consulting services and other revenue, \$11.6 million in software maintenance, and \$12.0 million in software hosting offsetting the loss of \$22.5 million of outsourced business services revenue from exited businesses and contracts. The \$19.1 million increase in consulting services and other revenue was due primarily to the higher utilization of consulting resources on more profitable implementation projects. The overall increase of \$11.6 million in software maintenance revenue primarily resulted from sales of our enterprise and component software in 2005, including Facets Extended Enterprise,[™] QicLink Extended Enterprise,[™] NetworX,[™] CareAdvance[™] and HealthWeb,[®] Workflow and HIPAA Gateway.[™] The overall decrease of \$10.5 million in outsourced business services revenue resulted primarily from (i) a \$9.3 million decline caused by the scheduled termination of our services for Altius, (ii) a \$5.8 million decline resulting from the wind-down of our services for PHN, (iii) a \$4.1 million reduction resulting from the planned wind-down of our services to physician group customers, and (iv) a \$3.3 million decrease from the planned elimination of our hosting and business process outsourcing services on certain competitive software platforms. The effect of this \$22.5 million decline in outsourced business services revenue was offset in part by a net increase of \$12.0 million of additional revenue primarily from new Facets[®] hosted customers and increased membership from existing Facets[®] hosted and benefits administrator customers.

PRODUCTS REVENUE. Products revenue, which includes software license sales, decreased \$2.6 million, or 5%, from \$51.3 million in 2004 to \$48.7 million in 2005 due to the timing of sales compared to 2004.

COST OF REVENUE — SERVICES AND OTHER. Cost of revenue for services and other decreased \$13.3 million, or 8%, from \$157.6 million in 2004 to \$144.3 million in 2005.

Cost of revenue for our outsourced business services and software maintenance revenue decreased \$9.1 million, primarily attributable to (i) reduced costs of \$7.2 million associated with the scheduled termination of our services for Altius, (ii) a \$4.6 million reduction resulting from the planned wind-down of our services to physician group customers, (iii) a decline of \$3.5 million related to the wind-down of our services for PHN, (iv) a \$3.0 million increase related to the loss on contracts from physician group customers, and (v) a \$3.2 million net increase in costs to support the additional outsourced business services revenue from new Facets[®] hosted customers and existing benefits administrator customers. We executed termination agreements with our two remaining physician group customers in the second quarter of 2005, allowing us to reverse the remaining balance in our loss on contracts accrual of \$2.9 million, which reduced our total cost of revenue by an equal amount. In 2004, we reversed \$5.9 million of previously accrued loss on contracts charges due to the accelerated termination of certain physician group contracts and the reduction of costs to support these remaining contracts. The net increase of \$3.2 million represented higher incentive and compensation costs, increased royalty expense related to license deals, new software and equipment maintenance agreements, and new operating leases, which were offset in part by reduced outsourced contractor expenses from the completion of certain internal and customer related data center projects and reduced costs related to cost containment efforts.

Cost of revenue for our consulting services and other revenue decreased \$4.2 million, primarily attributable to a \$4.5 million decrease related to the loss on contracts for a certain fixed fee implementation, partly offset by a \$400,000 increase in other costs. In 2004, we recorded a net \$4.5 million of loss on contracts charges, which primarily represented incremental hours required to complete a certain fixed fee implementation. This fixed fee implementation project was completed by the end of the first quarter of 2005. The overall increase in other costs was due primarily to higher incentive and compensation costs, partially offset by lower outsourced consulting costs related to the completion of a large fixed fee implementation project, lower facilities expense related to an office closure, and a decrease in overall travel expense.

As a percentage of total revenue, cost of revenue for services and other approximated 49% in 2005 compared with 57% in 2004.

COST OF REVENUE — PRODUCTS. Cost of revenue for products, which excludes the amortization of acquired technology, increased \$2.2 million, or 18%, to \$14.2 million in 2005 from \$12.0 million in 2004. This increase resulted primarily from an increase of \$4.3 million in the amortization of capitalized software development products related to the general release of additional products, partly offset by reduced royalty expense of \$1.0 million and a decrease of \$1.1 million in customer software pass-through costs. As a percentage of total revenue, cost of revenue for products approximated 5% in 2005 compared with 4% in 2004.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESEARCH AND DEVELOPMENT (R&D) EXPENSES. R&D expenses increased \$1.3 million, or 4%, to \$31.7 million in 2005 from \$30.4 million in 2004. This net increase was due primarily to increased spending related to the development of our proprietary software for the health plan and benefits administrator markets. Most of our R&D expense was used to continue our development of Facets Extended Enterprise,[™] which is a substantial upgrade of our flagship software for health plans, and for the development of certain new component software. Several enhancements were also made to QicLink,[™] a proprietary software product for benefits administrators and HealthWeb,[®] our web-enable platform, which allows health plans to exchange information on a secure basis over the Internet. As a percentage of total revenue, R&D expenses approximated 11% in 2005 and 2004. R&D expenses, as a percentage of total R&D expenditures (which includes capitalized R&D expenses of \$8.6 million in 2005 and 2004), was 79% in 2005 and 78% in 2004.

SELLING, GENERAL AND ADMINISTRATIVE (SG&A) EXPENSES. SG&A expenses increased \$16.8 million, or 28%, to \$76.8 million in 2005 from \$60.0 million in 2004. The overall increase resulted primarily from (i) \$8.8 million in higher personnel costs, including higher incentive and compensation costs associated with certain senior staff additions in late 2004 and higher commission expenses incurred related to the timing of new contracts signed, (ii) a \$3.0 million increase in outsourced services primarily for strategic planning and process improvements, in addition to support and enhancements related to our enterprise reporting system, (iii) a \$3.1 million increase related primarily to defense costs for McKesson in 2005 compared to lower costs in 2004, partially offset by a \$1.1 million insurance reimbursement received in 2005 related to the ATPA litigation settlement, and (iv) approximately \$1.9 million in other expenses such as audit and compliance, executive travel, sales and marketing, and other corporate support costs. SG&A expenses also increased \$1.1 million due to the collection of a fully reserved note receivable in the second quarter of 2004, which negatively affected the period comparison. As a percentage of total revenue, selling, general and administrative expenses approximated 26% in 2005 compared with 22% in 2004.

AMORTIZATION OF INTANGIBLE ASSETS. Amortization of intangible assets is comprised of acquired technology and acquired other intangible assets. Amortization of intangible assets decreased \$1.3 million, or 32%, from \$4.2 million in 2004 to \$2.9 million in 2005.

AMORTIZATION OF ACQUIRED TECHNOLOGY. The amortization of acquired technology is excluded from cost of revenue—products and consists primarily of amounts amortized with respect to core or completed technology and existing software. Amortization of acquired technology increased \$220,000, or 50%, to \$660,000 in 2005 from \$440,000 in 2004. The increase was related to the Diogenes acquisition in early 2004.

AMORTIZATION OF ACQUIRED OTHER INTANGIBLE ASSETS. Amortization of acquired other intangible assets decreased \$1.6 million, or 41%, from \$3.8 million in 2004 to \$2.2 million in 2005. The decrease was due primarily to certain intangible assets acquired in previous years, which were fully amortized in early 2005.

INTEREST INCOME. Interest income increased \$1.0 million, or 178%, to \$1.6 million in 2005 from \$583,000 in 2004. The increase is due primarily to higher cash balances attributed to the proceeds from the convertible debt deal, as well as higher interest earned in our investment accounts.

INTEREST EXPENSE. Interest expense increased \$210,000 or 15%, to \$1.6 million in 2005 from \$1.4 million in 2004. The increase relates primarily to interest incurred on the \$100.0 million convertible debt and borrowings on our revolving line of credit facility. The effect of this increase was offset in part by lower balances on our capital leases and notes payable.

PROVISION FOR INCOME TAXES. Provision for income taxes was \$412,000 in 2005 compared with \$1.1 million in 2004. The provision decrease is due to a decrease in state income taxes from benefits recorded for return to provision adjustments related to 2004 state taxes and refunds received related to prior years for which income tax benefit was not previously recorded, offset partially by an increase in Federal income taxes for alternative minimum tax. The effective tax rate was 1.8% for 2005, which was lower than the Federal statutory rate primarily due to the decrease in (release of) valuation allowance, which occurred as a result of utilization of net operating loss carryovers. The effective tax rate was 11.5% for 2004.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

SELECTED QUARTERLY RESULTS OF OPERATIONS

This data has been derived from unaudited consolidated financial statements that, in the opinion of our management, include all adjustments consisting only of normal recurring adjustments that we consider necessary for a fair presentation of the information when read in conjunction with our audited consolidated financial statements and the attached notes included herein. The operating results for any quarter are not necessarily indicative of the results for any future period. The following table sets forth certain unaudited consolidated statement of operations data for the eight quarters ended December 31, 2006 (in thousands, except per share data):

QUARTERS ENDED	12/31/06	9/30/06	6/30/06	3/31/06	12/31/05	9/30/05	6/30/05	3/31/05
Revenue: ⁽¹⁾								
Services and other	\$69,957	\$67,421	\$69,793	\$65,772	\$63,486	\$62,921	\$61,482	\$55,594
Products	18,515	19,016	17,917	19,546	11,354	10,132	11,026	16,224
Total revenue	88,472	86,437	87,710	85,318	74,840	73,053	72,508	71,818
Operating costs and expenses:								
Cost of revenue—services and other ⁽²⁾	41,064	41,838	41,980	40,347	37,011	36,546	34,901	35,860
Cost of revenue—products (excludes amortization of acquired technology)	3,231	3,238	3,232	4,474	3,068	3,188	4,205	3,749
Research and development	10,982	10,586	10,743	10,478	6,992	7,748	8,434	8,481
Selling, general and administrative	22,961	35,505	24,027	21,316	21,296	18,585	18,775	18,102
Amortization of acquired technology	1,030	935	940	1,215	165	165	165	165
Amortization of acquired other intangible assets	213	233	128	293	124	691	692	718
Total operating costs and expenses	79,481	92,335	81,050	78,123	68,656	66,923	67,172	67,075
Income (loss) from operations	8,991	(5,898)	6,660	7,195	6,184	6,130	5,336	4,743
Interest income	1,051	937	945	890	987	261	182	189
Interest expense	(850)	(825)	(835)	(832)	(836)	(206)	(178)	(359)
Other income	—	—	—	180	—	—	—	—
Income (loss) before (provision for) benefit from income taxes	9,192	(5,786)	6,770	7,433	6,335	6,185	5,340	4,573
(Provision for) benefit from income taxes	(1,646)	103	(356)	(595)	(71)	295	(361)	(275)
Net income (loss)	\$ 7,546	\$ (5,683)	\$ 6,414	\$ 6,838	\$ 6,264	\$ 6,480	\$ 4,979	\$ 4,298
Net income (loss) per share:								
Basic	\$ 0.18	\$ (0.13)	\$ 0.15	\$ 0.16	\$ 0.15	\$ 0.15	\$ 0.12	\$ 0.10
Diluted	\$ 0.16	\$ (0.13)	\$ 0.14	\$ 0.15	\$ 0.14	\$ 0.14	\$ 0.11	\$ 0.10
Shares used in computing net income (loss) per share:								
Basic	42,744	42,526	42,370	41,899	41,519	42,567	41,988	41,714
Diluted	46,273	42,526	45,394	45,666	45,518	46,921	44,816	43,934

⁽¹⁾ In December 2006, the Company entered into a settlement with one of its larger customers that had disputed payments due from a software implementation project. The amounts represented revenue recorded in the first two quarters of 2006 and were included in the allowance for sales returns and a reduction to revenue in the quarter ended September 30, 2006. The settlement fully resolved the issues and resulted in a payment that was less than the amount previously disputed.

⁽²⁾ Included in cost of revenue are charges associated with loss on contracts. During the fourth quarter of 2003, we decided to wind-down our outsourcing services to physician group customers. As a result of this decision, we estimated that the existing customer agreements would generate a total loss of \$11.3 million until the terms of these agreements expired in 2008. We recorded a loss accrual in the fourth quarter of

2003. Through discussions and negotiations, we were able to accelerate the termination of our services agreements with certain physician group customers and implemented cost cutting measures that reduced the expected future costs to support our remaining customers. As a result of these actions, we were able to reverse approximately \$5.9 million of previously accrued loss on contracts charges in 2004. Early in the second quarter of 2005, we executed termination agreements with our two remaining physician group customers. We continued to provide outsourced business services through May 2005, when the transition services were completed. The completion of these services to the remaining customers allowed us to reverse the remaining balance in the loss on contracts accrual of \$2.9 million in the second quarter of 2005. The total amount of loss actually incurred related to the outsourcing services to physician group customers was \$2.1 million in 2004 and \$403,000 in the first six months of 2005.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

LIQUIDITY AND CAPITAL RESOURCES

CAPITAL RESOURCES

Our principal sources of liquidity include cash from operations, borrowings under our debt facility, proceeds from the issuance of convertible debt, cash obtained from our acquisitions, employee exercises of stock options and private financings. As of December 31, 2006, we have the following sources of cash available to fund our ongoing operations:

- Cash and cash equivalents totaling \$108.0 million, including \$921,000 of restricted cash.
- In January 2007, we entered into an amendment to our Credit Agreement established December 21, 2004 to add a term loan of up to \$150.0 million and to extend the expiration date of the Credit Agreement, including our \$100.0 million revolving credit facility, to January 5, 2011. As of December 31, 2006, we had outstanding borrowings on the revolving line of credit of \$12.0 million and were in compliance with all applicable covenants and other restrictions under the Credit Agreement. In January 2007, we borrowed \$75.0 million under the term loan to help fund our acquisition of Quality Care Solutions, Inc. ("QCSI"). We can borrow up to an additional \$75.0 million under the term loan through June 30, 2007, at which time no additional funds can be borrowed under the term loan. All borrowings under our Credit Agreement bear interest at a per annum rate equal to either (i) the LIBOR rate plus an adjustable applicable margin of between 1.75% and 3.50% or (ii) Wells Fargo's prime rate plus an adjustable applicable margin of between 0.0% and 2.0%, at our election, subject to specified restrictions. The maximum amount that we may borrow under our revolving credit facility may be limited based upon multiples of EBITDA, as specified in the Credit Agreement. The Credit Agreement is also subject to other customary financial and negative covenants.
- In October 2005, we issued \$100.0 million aggregate principal amount of 2.75% Convertible Senior Notes due 2025 (the "Notes"). The Notes bear interest at a rate of 2.75%, which is payable in cash semi-annually. On or after October 5, 2010, we may from time to time at our option redeem the Notes, in whole or in part, for cash, at the applicable redemption date. Additionally, holders of the Notes may require us to purchase all or a portion of their Notes in cash on each October 1, 2010, October 1, 2015 and October 1, 2020.

The Notes are convertible into shares of our common stock at an initial conversion price of \$18.85 per share, or 53.0504 shares for each \$1,000 principal amount of Notes, subject to certain adjustments set forth in the Indenture. Upon conversion of the Notes, we will have the right to deliver shares of our common stock, cash or a combination of cash and shares of our common stock. The Notes are convertible (i) prior to October 1, 2020, during any fiscal quarter after the fiscal quarter ending December 31, 2005, if the closing sale price of our common stock for 20 or more trading days in a period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter exceeds 120% of the conversion price in effect on the last trading day of the immediately preceding fiscal quarter, (ii) prior to October 1, 2020, during the five business day period after any five consecutive trading day period (the "Note Measurement Period") in which the average trading price per \$1,000 principal amount of Notes was equal to or less than 97% of the average conversion value of the Notes during the Note Measurement Period, (iii) upon the occurrence of specified corporate transactions, as described in the Indenture, (iv) if we call the Notes for redemption, or (v) any time on or after October 1, 2020.

Based on our current operating plan, we believe that existing cash and cash equivalents balances, cash forecasted by management to be generated by operations and borrowings from existing credit facilities will be sufficient to meet our working capital and capital requirements for at least the next 12 months. However, if events or circumstances occur such that we do not meet our operating plan as expected, we may be required to seek additional capital and/or reduce certain discretionary spending, which could have a material adverse effect on our ability to achieve our business objectives. We may seek additional financing, which may include debt and/or equity financing or funding through third party agreements. There can be no assurance that any additional financing will be available on acceptable terms, if at all. Any equity financing may result in dilution to existing stockholders and any debt financing may include restrictive covenants.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

SUMMARY OF CASH ACTIVITIES

As of December 31, 2006, we had cash and cash equivalents totaling \$107.1 million and \$921,000 in restricted cash. Significant cash flow activities for the years ended December 31, 2006 and 2005 are as follows (in thousands):

YEAR ENDED DECEMBER 31,	2006	2005
Cash provided by operating activities	\$ 40,154	\$ 43,825
Purchase of property and equipment and software licenses	(10,575)	(7,171)
Capitalization of software development costs	(8,568)	(8,608)
Acquisitions, net of cash acquired	(40,581)	(26,799)
Proceeds from notes payable	—	100,000
Proceeds from revolving line of credit, debt financings and capital leases	37,992	79,650
Payments on notes payable	(997)	(40,991)
Payments on revolving line of credit and capital leases	(27,316)	(94,542)
Payments for repurchase of common stock	—	(19,798)
Employee exercise of common stock options and purchase of common stock	10,008	10,254

Cash and cash equivalents increased \$117,000 in 2006 from \$106.9 million at December 31, 2005 to \$107.1 million at December 31, 2006. The main contributors of this increase were \$40.2 million in cash provided by operating activities, \$38.0 million in proceeds from our revolving line of credit and other financing debt, and \$10.0 million in proceeds from employee option exercises and stock purchases. These cash inflows were partially offset by net cash payments of \$40.6 million which included \$42.4 million of payments related to the acquisition of CareKey and \$1.8 million of

cash acquired from PDM, payments on our debt (including revolving line of credit) of \$28.3 million and \$19.1 million for capital spending.

Although our acquisition of PDM was consummated on December 22, 2006, the initial closing consideration of \$8.0 million and 491,488 shares of common stock was paid and issued, respectively, in January 2007. In January 2007, we also consummated our acquisition of QCSI, pursuant to which we made an aggregate cash payment of \$130.0 million, net of cash received in the acquisition.

COMMITMENTS AND CONTINGENCIES

The following tables summarize our estimated contractual obligations and other commercial commitments (in thousands):

CONTRACTUAL OBLIGATIONS	TOTAL	PAYMENTS (INCLUDING INTEREST) DUE BY PERIOD			
		LESS THAN 1 YEAR	1-3 YEARS	3-5 YEARS	MORE THAN 5 YEARS
Short-term debt	\$ 115	\$ 115	\$ —	\$ —	\$ —
Capital lease obligations	3,806	1,618	1,625	563	—
Operating leases	63,363	13,603	19,944	12,703	17,113
Convertible debt	152,281	2,750	5,500	5,500	138,531
Total contractual obligations	\$219,565	\$18,086	\$27,069	\$18,766	\$155,644

OTHER COMMERCIAL COMMITMENTS	TOTAL AMOUNTS COMMITTED	LESS THAN 1 YEAR	1-3 YEARS	3-5 YEARS	MORE THAN 5 YEARS
Line of credit	\$ 12,000	\$ —	\$ —	\$12,000	\$ —
Standby letters of credit	921	—	500	308	113
Total other commercial commitments	\$ 12,921	\$ —	\$ 500	\$12,308	\$ 113

In the second quarter of 2006, we extended the term of our lease on our Colorado facility for a period of seven years from July 31, 2009 through July 31, 2016. At the same time, we leased an additional 50,862 square feet within this facility.

Convertible debt represents scheduled principal and interest payments for our October 2005 convertible debt offering, which includes \$100.0 million aggregate principal amount of our Convertible Senior Notes. The Notes bear interest at a rate of 2.75%, which is payable

in cash semi-annually in arrears on April 1 and October 1 of each year, commencing on April 1, 2006, to the holders of record on the preceding March 15 and September 15, respectively. The Notes mature on October 1, 2025. However, on or after October 5, 2010, we may from time to time at our option redeem the Notes, in whole or in part, for cash, at the applicable redemption date. Additionally, holders of the Notes may require us to purchase all or a portion of their Notes in cash on each of October 1, 2010, October 1, 2015 and October 1, 2020.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

As of December 31, 2006, we had outstanding four unused standby letters of credit in the aggregate amount of \$921,000 which serve as security deposits for certain operating leases. We are required to maintain a cash balance equal to the outstanding letters of credit, which is classified as restricted cash on our balance sheet.

Excluded from the tables above are certain potential payments to former CareKey stockholders and option holders as these payments are contingent upon the achievement of financial milestones. These amounts are payable in either cash or stock at our election. Former CareKey stockholders and option holders are entitled to receive three contingent consideration payments of \$8.3 million each (up to \$25.0 million), upon the achievement of certain revenue milestones during the period beginning upon acquisition and ending December 31, 2008. In addition, further consideration payable in cash or stock at our election, may be paid to former CareKey stockholders and option holders if, prior to December 31, 2008, the acquired CareKey products generate revenues in excess of certain revenue milestones and/or if a negotiated multiple of software maintenance revenues of acquired CareKey products during the fiscal year ended December 31, 2009 exceed total purchase consideration made to those former CareKey stockholders and option holders. Also excluded from the tables above are certain potential payments to former PDM and QCSI stockholders and option and warrant holders. In addition to the \$8.0 million and 491,488 shares of common stock paid and issued in January 2007, former PDM security holders may be entitled to receive contingent consideration as follows: aggregate payments of up to \$5.0 million on or before June 30, 2007, \$5.0 million on or before December 31, 2008, and \$8.0 million on or before December 31, 2009, each subject to reduction if certain revenue thresholds are not satisfied during the applicable measurement period. Additional contingent consideration may be paid on June 30, 2009 if certain revenue thresholds are satisfied, provided that in no event will the aggregate consideration of all payments exceed \$42.0 million. It is expected that 50% of each payment will be made in cash and 50% will be paid in shares of TriZetto's common stock.

In addition to the net cash payment of \$130.0 million paid in January 2007, former QCSI security holders are entitled to an aggregate cash payment of \$5.0 million on January 31, 2008, subject to reduction if the parties determine that QCSI had negative working capital under the acquisition agreement as of the date of closing or to the extent that we are entitled to claims for indemnification under the acquisition agreement. In addition, former QCSI security holders will be entitled to receive an aggregate cash payment of \$7.0 million on January 31, 2008 if license and software revenues arising from the sale of QCSI products reach specified thresholds during the fiscal year ending on December 31, 2007.

The tables further exclude the long-term debt obligations under our term loan used to help fund the purchase of QCSI in January 2007. As of January 31, 2007, there was \$75.0 million outstanding under our term loan. All borrowings under our term loan must be repaid in quarterly installments commencing on July 1, 2007 through

January 5, 2010 in amounts equal to the amount outstanding under the term loan on June 30, 2007, divided by 28.

OFF-BALANCE SHEET ARRANGEMENTS

We do not currently have any relationships with unconsolidated entities or financial partnerships, such as entities referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet or other contractually narrow or limited purposes.

QUANTITATIVE AND QUALITATIVE DISCLOSURES

ABOUT MARKET RISK

Market risk associated with adverse changes in financial and commodity market prices and rates could impact our financial position, operating results or cash flows. We are exposed to market risk due to changes in interest rates such as the prime rate and LIBOR. This exposure is directly related to our normal operating and funding activities. Historically, and as of December 31, 2006, we have not used derivative instruments or engaged in hedging activities.

The interest rate on our \$100.0 million revolving credit facility is a per annum rate equal to (i) the LIBOR rate plus an applicable margin of between 1.75% and 2.25% or (ii) the lending institution's prime rate plus an adjustable applicable margin of between 0.0% and 0.5%, at our election, subject to specified restrictions, and is payable monthly in arrears. The revolving credit facility expires in January 2010. As of December 31, 2006, we had outstanding borrowings on the revolving line of credit of \$12.0 million.

On September 30, 2005, we entered into a Purchase Agreement with UBS Securities, LLC, Banc of America Securities, LLC and William Blair & Company LLC (the "Initial Purchasers"), to sell \$100.0 million aggregate principal amount of our 2.75% Convertible Senior Notes due 2025 (the "Notes") in a private placement in reliance on Section 4(2) of the Securities Act of 1933, as amended (the "Securities Act"). The Notes have been resold by the Initial Purchasers to qualified institutional buyers pursuant to Rule 144A under the Securities Act. The sale of the Notes to the Initial Purchasers was consummated on October 5, 2005. The Notes were issued pursuant to an Indenture, dated October 5, 2005, by and between us and Wells Fargo Bank, National Association, as trustee. The Notes bear interest at a rate of 2.75%, which is payable in cash semi-annually in arrears on April 1 and October 1 of each year, commencing on April 1, 2006, to the holders of record on the preceding March 15 and September 15, respectively.

We manage interest rate risk by investing excess funds in cash equivalents and short-term investments bearing variable interest rates, which are tied to various market indices. We also manage interest rate risk by closely managing our borrowings on our credit facility based on our operating needs in order to minimize the interest expense incurred. As a result, we do not believe that near-term changes in interest rates will result in a material effect on our future earnings, fair values or cash flows.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS
OF THE TRIZETTO GROUP, INC.

We have audited the accompanying consolidated balance sheets of The TriZetto Group, Inc. as of December 31, 2006 and 2005, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2006. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The TriZetto Group, Inc. at December 31, 2006 and 2005, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2006, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment."

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of The TriZetto Group, Inc.'s internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 16, 2007 expressed an unqualified opinion thereon.

ERNST & YOUNG LLP

Orange County, California
February 16, 2007

CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS, EXCEPT PER SHARE DATA)

DECEMBER 31,	2006	2005
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 107,057	\$ 106,940
Restricted cash	921	1,543
Accounts receivable, less allowances of \$3,770 and \$855 at December 31, 2006 and 2005, respectively	64,386	41,745
Deferred tax assets	14,100	—
Prepaid expenses and other current assets	11,415	11,375
Total current assets	197,879	161,603
Property and equipment, net	26,777	25,730
Capitalized software development costs, net	27,913	28,724
Goodwill	90,337	87,170
Other intangible assets, net	27,347	3,335
Other assets	12,347	11,177
Total assets	\$ 382,600	\$ 317,739
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable	\$115	\$120
Current portion of capital lease obligations	1,461	1,979
Accounts payable	18,091	14,959
Accrued liabilities	61,595	56,957
Deferred revenue	30,508	35,625
Total current liabilities	111,770	109,640
Long-term convertible debt	100,000	100,000
Long-term revolving line of credit	12,000	—
Other long-term liabilities	2,340	1,752
Capital lease obligations	2,030	1,065
Deferred tax liabilities	14,100	—
Deferred revenue	6,453	3,924
Total liabilities	248,693	216,381
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock: \$0.001 par value; shares authorized: 4,000 (5,000 authorized net of 1,000 designated as Series A Junior Participating Preferred); shares issued and outstanding: zero in 2006 and 2005	—	—
Series A Junior Participating Preferred Stock: \$0.001 par value; shares authorized: 1,000; shares issued and outstanding: zero in 2006 and 2005	—	—
Common stock: \$0.001 par value; shares authorized: 95,000; shares issued and outstanding: 43,497 in 2006 and 42,104 in 2005	43	42
Additional paid-in capital	376,633	362,186
Deferred stock compensation	—	(2,986)
Accumulated deficit	(242,769)	(257,884)
Total stockholders' equity	133,907	101,358
Total liabilities and stockholders' equity	\$ 382,600	\$ 317,739

See accompanying notes.

CONSOLIDATED STATEMENTS OF OPERATIONS

(IN THOUSANDS, EXCEPT PER SHARE DATA)

YEARS ENDED DECEMBER 31,	2006	2005	2004
Revenue:			
Services and other	\$272,943	\$243,483	\$223,257
Products	74,994	48,736	51,308
Total revenue	347,937	292,219	274,565
Operating costs and expenses:			
Cost of revenue—services and other	165,229	144,318	157,573
Cost of revenue—products (excludes amortization of acquired technology)	14,175	14,210	12,025
Research and development	42,789	31,655	30,398
Selling, general and administrative	103,809	76,758	59,980
Amortization of acquired technology	4,120	660	440
Amortization of acquired other intangible assets	867	2,225	3,804
Total operating expenses	330,989	269,826	264,220
Income from operations	16,948	22,393	10,345
Interest income	3,823	1,619	583
Interest expense	(3,342)	(1,579)	(1,369)
Other income	180	—	—
Income before provision for income taxes	17,609	22,433	9,559
Provision for income taxes	(2,494)	(412)	(1,101)
Net income	\$ 15,115	\$ 22,021	\$ 8,458
Net income per share:			
Basic	\$ 0.36	\$ 0.52	\$ 0.18
Diluted	\$ 0.33	\$ 0.48	\$ 0.18
Shares used in computing net income per share:			
Basic	42,389	41,948	46,794
Diluted	45,691	45,503	48,157

Certain reclassifications have been made to prior year amounts to conform to current year presentation with respect to services and products revenue and cost of revenue, with no effect on net income.
See accompanying notes.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(IN THOUSANDS)

YEARS ENDED DECEMBER 31, 2006, 2005 AND 2004	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	DEFERRED STOCK COMPENSATION	ACCUMULATED DEFICIT	TOTAL STOCKHOLDERS' EQUITY
	SHARES	AMOUNT				
Balance, December 31, 2003	46,870	\$ 47	\$402,702	\$ (863)	\$(288,363)	\$113,523
Issuance of common stock to ValueAct Capital	6,600	7	44,543	—	—	44,550
Issuance of restricted stock grants	422	—	2,604	(2,604)	—	—
Stock-based compensation	—	—	—	594	—	594
Employee exercise of common stock options and purchase of common stock	452	—	1,772	—	—	1,772
Repurchase of common stock from IMS	(12,143)	(12)	(81,952)	—	—	(81,964)
Net income	—	—	—	—	8,458	8,458
Balance, December 31, 2004	42,201	42	369,669	(2,873)	(279,905)	86,933
Employee exercise of common stock options and purchase of common stock	1,370	2	10,252	—	—	10,254
Stock-based compensation	—	—	191	1,206	—	1,397
Issuance of restricted stock grants	100	—	1,319	(1,319)	—	—
Repurchase of common stock from ValueAct Capital	(600)	(1)	(5,297)	—	—	(5,298)
Repurchase of common stock related to convertible debt	(1,000)	(1)	(14,499)	—	—	(14,500)
Issuance of common stock for purchase of software patent	33	—	551	—	—	551
Net income	—	—	—	—	22,021	22,021
Balance, December 31, 2005	42,104	42	362,186	(2,986)	(257,884)	101,358
Employee exercise of common stock options and purchase of common stock	1,131	1	10,007	—	—	10,008
Elimination of deferred stock compensation in accordance with SFAS No. 123R	—	—	(2,986)	2,986	—	—
Stock-based compensation	—	—	7,426	—	—	7,426
Issuance of restricted stock grants	262	—	—	—	—	—
Net income	—	—	—	—	15,115	15,115
Balance, December 31, 2006	43,497	\$ 43	\$376,633	\$ —	\$(242,769)	\$133,907

See accompanying notes.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(IN THOUSANDS)

YEARS ENDED DECEMBER 31,	2006	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	\$ 15,115	\$ 22,021	\$ 8,458
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for (benefit from) doubtful accounts and sales allowance	3,214	(597)	(2,299)
Stock-based compensation	7,426	1,397	594
(Gain) loss on disposal of property and equipment	(158)	70	—
Depreciation and amortization	22,237	23,282	21,106
Amortization of other intangible assets	4,987	2,885	4,244
Recovery from contracts	—	(2,877)	(1,353)
Increase in cash surrender value of life insurance policies	(683)	(151)	—
Changes in assets and liabilities (net of acquisition):			
Restricted cash	622	(88)	23
Accounts receivable	(23,794)	12,825	(12,940)
Prepaid expenses and other current assets	(1,092)	(3,386)	(496)
Other assets	(486)	(8,384)	(914)
Accounts payable	4,911	2,417	1,488
Accrued liabilities	11,746	(2,620)	939
Deferred revenue	(3,891)	(2,969)	17,034
Net cash provided by operating activities	40,154	43,825	35,884
CASH FLOWS FROM INVESTING ACTIVITIES:			
Sale of short-term investments, net	—	1,203	17,640
Purchase of property and equipment and software licenses	(10,575)	(7,171)	(8,131)
Capitalization of software development costs	(8,568)	(8,608)	(8,610)
Purchase of intangible assets	—	(572)	(2,138)
Acquisitions, net of cash acquired	(40,581)	(26,799)	(89)
Net cash used in investing activities	(59,724)	(41,947)	(1,328)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from revolving line of credit	37,000	78,000	72,000
Proceeds from convertible note	—	100,000	—
Proceeds from debt financing	992	1,511	1,110
Proceeds from capital leases	—	139	1,150
Payments on revolving line of credit	(25,000)	(90,000)	(80,000)
Payments on notes payable	(997)	(40,991)	(1,429)
Payments on term note	—	—	(9,375)
Payments on capital leases	(2,316)	(4,542)	(5,321)
Proceeds from sale of common stock	—	—	44,550
Payment for repurchase of common stock	—	(19,798)	(44,550)
Employee exercises of stock options and purchase of common stock	10,008	10,254	1,772
Net cash provided by (used in) financing activities	19,687	34,573	(20,093)
Net increase in cash and cash equivalents	117	36,451	14,463
Cash and cash equivalents at beginning of year	106,940	70,489	56,026
Cash and cash equivalents at end of year	\$107,057	\$106,940	\$ 70,489

See Note 15 for supplemental disclosure of additional cash flow information, including certain non-cash investing and financing activities.

See accompanying notes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. FORMATION AND BUSINESS OF THE COMPANY

The TriZetto Group, Inc. (the "Company") was incorporated in the state of Delaware on May 27, 1997. The Company develops, licenses and supports proprietary and third-party software products for the healthcare industry. The Company also provides hosting, applications management, business process management, consulting and other services primarily to the healthcare industry. The Company provides access to its hosted solutions either through the Internet or through traditional networks and sells its software and services to customers primarily in the United States.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany transactions have been eliminated in consolidation.

LIQUIDITY AND CAPITAL RESOURCES

The Company has generated net income of \$15.1 million, \$22.0 million and \$8.5 million for the years ended December 31, 2006, 2005 and 2004, respectively, and has an accumulated deficit of \$242.8 million at December 31, 2006. The Company has generated cash from operating activities of \$40.2 million, \$43.8 million and \$35.9 million for the years ended December 31, 2006, 2005, and 2004, respectively. The Company has total cash, cash equivalents and restricted cash of \$108.0 million and net working capital of \$86.1 million at December 31, 2006. Based on the Company's current operating plan, management believes existing cash, cash equivalents and short-term investment balances, cash forecasted by management to be generated by operations and borrowings from existing credit facilities will be sufficient to meet the Company's working capital and capital requirements through at least December 31, 2007. However, if events or circumstances occur such that the Company does not meet its operating plan as expected, the Company may be required to seek additional capital and/or to reduce certain discretionary spending, which could have a material adverse effect on the Company's ability to achieve its intended business objectives. The Company may seek additional financing, which may include debt and/or equity financing or funding through third party agreements. There can be no assurance that any additional financing will be available on acceptable terms, or available at all. Any equity financing may result in dilution to existing stockholders and any debt financing may include restrictive covenants.

COMPANY OWNED LIFE INSURANCE

The Company has purchased life insurance policies to fund its obligations under certain deferred compensation plans for officers, key employees and directors. Cash surrender values of these policies are adjusted for fluctuations in the market value of underlying investments. The cash surrender value is adjusted each reporting period and any gain or loss is included with other income and expense in the Company's consolidated statements of operations.

USE OF ESTIMATES

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

CONCENTRATION OF CREDIT RISK

Financial instruments that potentially subject the Company to a concentration of credit risk consist of cash and cash equivalents, short-term investments and accounts receivable. Cash and cash equivalents are deposited in demand and money market accounts in three financial institutions. Deposits held with banks may exceed the amount of insurance provided on such deposits. The Company has not experienced any losses on its deposits of cash and cash equivalents. The Company's accounts receivable are derived from revenue earned from customers primarily located in the United States. The Company generally requires no collateral from its customers. The Company maintains an allowance for doubtful accounts receivable based upon the expected collectibility of individual accounts.

One customer, The Regence Group, accounted for more than 10% of the Company's consolidated revenue in 2006. No single customer accounted for more than 10% of the Company's accounts receivable in 2006. In 2005, one customer, The Regence Group, accounted for more than 10% of the Company's accounts receivable and two customers, The Regence Group and United Healthcare Services, Inc., each accounted for more than 10% of its consolidated revenue. No single customer accounted for more than 10% of the Company's accounts receivable and consolidated revenues in 2004.

FAIR VALUE OF FINANCIAL INSTRUMENTS

Carrying amounts of certain of the Company's financial instruments including cash and cash equivalents, short-term investments, accounts receivable and accounts payable approximate fair value due to their short maturities. Based on borrowing rates currently available to the Company for loans with similar terms, the carrying value of its debt obligations approximates fair value.

CASH AND CASH EQUIVALENTS

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Cash and cash equivalents include money market funds, commercial paper and various deposit accounts.

SHORT-TERM INVESTMENTS

Short-term investments include money market funds, commercial paper, and various deposit accounts.

RESTRICTED CASH

Restricted cash consists of \$921,000 in letters of credit issued for certain operating leases.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost and are depreciated on a straight-line basis over their estimated useful lives: computer equipment, other equipment and software are depreciated over three to twenty years, and furniture and fixtures are depreciated over seven years. Leasehold improvements are amortized over their estimated useful lives or the lease term, if shorter. Upon retirement or sale, the cost and related accumulated depreciation are removed from the balance sheet and the resulting gain or loss is reflected in operations. Maintenance and repairs are charged to operations as incurred.

GOODWILL

Under Financial Accounting Standards Board ("FASB") Statement Nos. 141 and 142, "Business Combinations" and "Goodwill and Other Intangible Assets," respectively, goodwill and intangible assets deemed to have indefinite lives are not amortized but, instead, are tested annually or on an interim basis if events or circumstances indicate that the fair value of the asset has decreased below its carrying value.

LONG-LIVED ASSETS, INCLUDING OTHER INTANGIBLE ASSETS

Other intangible assets arising from the Company's acquisitions consist of customer lists, core technology, consulting contracts, tradenames and intellectual property, which are being amortized on a straight-line basis over their estimated useful lives of five to ten years. Software technology rights are being amortized on a straight-line basis over the lesser of the contract term or five years. Long-lived assets and other intangible assets are reviewed for impairment when events or changes in circumstances indicate the carrying amount of an asset may not be recoverable in accordance with FASB Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." Recoverability is measured by comparison of the asset's carrying amount to future net undiscounted cash flows the assets are expected to generate. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the projected discounted future net cash flows arising from the assets. The discount rate applied to these cash flows is based on a discount rate commensurate with the risks involved.

REVENUE RECOGNITION

The Company recognizes revenue when persuasive evidence of an arrangement exists, the product or service has been delivered, fees are fixed or determinable, collection is reasonably assured and all other significant obligations have been fulfilled. The Company's revenue is classified into two categories: services and other, and products. For the year ended December 31, 2006, approximately 78% of the Company's total revenue was generated from services and other revenue and 22% was from products revenue.

The Company follows the provisions of the Securities and Exchange Commission Staff Accounting Bulletin No. 104, "Revenue Recognition," AICPA Statement of Position ("SOP") 97-2, "Software Revenue Recognition," as amended, EITF Issue 00-3, "Application of

AICPA Statement of Position 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware," and EITF Issue 00-21, "Revenue Arrangements with Multiple Deliverables."

The Company generates services revenue from several sources, including the provision of outsourcing services, such as software hosting and other business services, and the sale of maintenance and support for its proprietary software products. The Company applies EITF 00-3 to hosting arrangements that include the licensing of software. A software element covered by SOP 97-2 is present in a hosting arrangement if the customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty and it is feasible for the customer to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software. Software hosting and other business services revenue is typically billed and recognized monthly over the contract term, generally three to seven years. Many of the Company's outsourcing agreements require it to maintain a certain level of operating performance. The Company records revenue net of estimated penalties resulting from any failure to maintain the level of operating performance. These penalties have not been significant in the past. Software maintenance and support revenues are typically based on one-year renewable contracts and are recognized ratably over the contract period. Payment for software maintenance received in advance is recorded on the balance sheet as deferred revenue. Certain royalty costs paid to third-party software vendors associated with software maintenance are amortized over the software maintenance period.

The Company also generates services revenue from consulting fees for implementation, installation, configuration, business process engineering, data conversion, testing and training related to the use of its proprietary and third party licensed products. In certain instances, the Company also generates services revenue from customization services of its proprietary licensed products. The Company recognizes revenue for these services as they are performed. When the Company cannot reasonably estimate the cost to complete, it recognizes revenue using the completed contract method, upon completion of all contractual obligations. The Company also generates services revenue from set-up fees, which are services, hardware, and software associated with preparing its customer connectivity center or a customer's data center in order to ready a specific customer for software hosting services. The set-up fees are usually separate and distinct from the hosting fees, and performance of the set-up services represents the culmination of the earnings process. The Company recognizes revenue for these services as they are performed. The Company generates other revenue from certain one-time charges, including certain contractual fees such as termination fees and change of control fees, and it recognizes the revenue for these fees once the termination or change of control is guaranteed, there are no remaining substantive performance obligations and collection is reasonably assured. Other revenue is also generated from fees related to the Company's product related conference.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For multiple element arrangements, such as software license, consulting services, outsourcing services and maintenance, and where vendor-specific objective evidence ("VSOE") of fair value exists for all undelivered elements, the Company accounts for the delivered elements in accordance with the "residual method." VSOE of fair value is determined for each undelivered element based on how it is sold separately, or in the case of maintenance, the renewal rate. For arrangements in which VSOE does not exist for each undelivered element, including specified product and upgrade rights, revenue for the delivered element is deferred and not recognized until VSOE is available for the undelivered element or delivery of each element has occurred. In determining VSOE for the undelivered elements, no portion of the discount is allocated to specified or unspecified product or upgrade rights.

Under the residual method, the arrangement fee is recognized as follows: (1) the total fair value of the undelivered elements, as indicated by VSOE, is deferred and subsequently recognized in accordance with the relevant sections of SOP 97-2 and (2) the difference between the total arrangement fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements.

The Company generates products revenue from the licensing of its software. Under SOP 97-2, software license revenue is recognized upon the execution of a license agreement, upon delivery of the software, when fees are fixed or determinable, when collectibility is probable and when all other significant obligations have been fulfilled. For software license agreements in which customer acceptance is a significant condition of earning the license fees, revenue is not recognized until acceptance occurs. For software license agreements that require significant customizations or modifications of the software, revenue is recognized as the customization services are performed.

RESEARCH AND DEVELOPMENT EXPENSE AND CAPITALIZED SOFTWARE DEVELOPMENT COSTS

Research and development ("R&D") expenses are salaries and related expenses associated with the development of software applications prior to establishing technological feasibility. Such expenses include compensation paid to engineering personnel and fees to outside contractors and consultants. Costs incurred internally in the development of our software products are expensed as incurred as R&D expenses until technological feasibility has been established, after which production costs are capitalized as software development costs in accordance with FASB Statement No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed." Capitalization ceases and amortization of capitalized software development costs begins when the software product is available for general release to customers.

On a quarterly basis, the Company monitors the expected net realizable value of the capitalized software for factors that would indicate impairment, such as a decline in the demand, the introduction of new technology, or the loss of a significant customer. As of

December 31, 2006, the Company's evaluation determined that the carrying amount of these assets was not impaired.

Capitalized software development costs are amortized to cost of revenue on a straight-line basis over the estimated useful life of the related products, which is generally deemed to be five years. Software development costs of \$8.6 million have been capitalized for each of the years ended December 31, 2006, 2005 and 2004. Amortization expense for the years ended December 31, 2006, 2005, and 2004 was \$9.4 million, \$7.8 million, and \$6.2 million, respectively, and is included in cost of revenue—products.

Capitalized software development costs, net consist of the following (in thousands):

YEARS ENDED DECEMBER 31,	2006	2005
Capitalized software development costs	\$ 55,838	\$ 47,270
Less: accumulated amortization	(27,925)	(18,546)
	\$ 27,913	\$ 28,724

INTERNAL-USE SOFTWARE

The Company capitalizes direct costs of materials and services used in the development of internal-use software in accordance with Statement of Position ("SOP") 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." Amounts capitalized are amortized on a straight-line basis over a period of three to five years and are included in software within property, plant and equipment.

STOCK-BASED COMPENSATION

In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment." This statement requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. This statement establishes fair value as the measurement objective in accounting for share-based payment arrangements and requires all entities to apply a fair-value based measurement method in accounting for share-based payment transactions with employees except for equity instruments held by employee share ownership plans.

Prior to the January 1, 2006 adoption of SFAS No. 123R, the Company accounted for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25 ("APB 25"), "Accounting for Stock Issued to Employees," and related interpretations. The Company recognized compensation expense for stock options granted to employees, where the exercise price was lower than the fair market value of the Company's common stock on the date of grant, and recorded compensation expense accordingly. For stock options granted with an exercise price equal to the fair market value of the Company's common stock on the date of grant, no compensation expense had been recognized but was included as a pro forma disclosure in the notes to the consolidated

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

financial statements as permitted by SFAS No 123, "Accounting for Stock-Based Compensation."

Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123R, using the modified prospective method. Under this method, the provisions of SFAS No. 123R apply to all awards granted or modified after the date of adoption and all previously granted awards not yet vested as of the date of adoption. Prior periods have not been restated.

The following table is a summary of the amount of stock-based compensation expense recognized in the consolidated statements of operations (in thousands):

YEARS ENDED DECEMBER 31,	2006	2005	2004
Cost of revenue—			
services and other	\$1,675	\$ 36	\$ 4
Research and development	893	34	24
Selling, general and administrative	4,858	1,327	566
Total	\$7,426	\$1,397	\$594

The Company has the following stock-based compensation plans: (i) the 1998 Long-Term Incentive Plan, which is an amendment and restatement of the 1998 Stock Option Plan, permits the Company to grant other types of awards in addition to stock options, (ii) the RIMS Stock Option Plan, a plan the Company assumed through the acquisition of Resource Information Management Systems, Inc. in late 2000, and (iii) the Employee Stock Purchase Plan, which allows full-time employees to purchase shares of the Company's common stock at a discount to fair market value.

SFAS No. 123R requires disclosure of pro forma information for periods prior to the adoption. The following table illustrates the effect on net income and net income per share if the Company had applied the fair value recognition provisions of SFAS No. 123R to stock-based employee compensation (in thousands, except per share data):

YEAR ENDED DECEMBER 31,	2005	2004
Net income as reported	\$22,021	\$ 8,458
Add: stock-based employee compensation expense included in reported net income, net of related tax effects	—	—
Deduct: stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(5,782)	(4,889)
Pro forma net income	\$16,239	\$ 3,569
Net income per share		
Basic, as reported	\$ 0.52	\$ 0.18
Diluted, as reported	\$ 0.48	\$ 0.18
Basic, pro forma	\$ 0.39	\$ 0.08
Diluted, pro forma	\$ 0.36	\$ 0.07

The fair value of option grants was estimated using the Black-Scholes pricing model. The Company evaluates the assumptions used to value stock awards on a quarterly basis. The following weighted average assumptions were used for the periods presented:

YEARS ENDED DECEMBER 31,	2006	2005	2004
Expected volatility	45%	55%	50%
Risk-free interest rate	4.75%	3.70%	3.00%
Expected life	6.25 years	4 years	4 years
Forfeiture rate	6.0%	—	—
Expected dividends	—	—	—
Weighted average fair value	\$8.49	\$3.99	\$2.81

Expected volatility is based on implied volatility from traded options on the Company's stock and historical volatility of the Company's stock. The risk-free interest rate is the U.S. Treasury rate for the week of the grant having a term equal to the expected life of the option. The expected life of options granted represents the period of time that options granted are expected to be outstanding. The Company has determined that historical experience is not a good predictor of future exercise patterns and thus has applied the "simplified" method outlined in Staff Accounting Bulletin No. 107, "Share-Based Payment," to calculate expected life. The forfeiture rate is the estimated percentage of options granted that are expected to be forfeited or cancelled before becoming fully vested and is based on historical experience. The Company has not made any dividend payments nor does it have plans to pay dividends in the foreseeable future.

ADVERTISING COSTS

Advertising costs are expensed as incurred. Advertising expense for the years ended December 31, 2006, 2005, and 2004 was \$644,000, \$1.2 million, and \$937,000, respectively.

COMMON STOCK REPURCHASE PROGRAM

On January 26, 2006, the Board of Directors approved a repurchase program which allows for the repurchase of up to 1,000,000 shares of the Company's common stock at a price and time to be determined by the Company's Chief Executive Office or Chief Financial Officer. As of December 31, 2006, no shares had been repurchased under the plan. Unless extended by the Board of Directors, the current repurchase plan will expire on December 31, 2007. The Company had prior repurchase programs in place in 2004 and 2005, which have since expired, but no shares were repurchased under such plans.

INCOME TAXES

The Company accounts for income taxes under FASB Statement No. 109, "Accounting for Income Taxes." This statement requires the recognition of deferred tax assets and liabilities for the future consequences of events that have been recognized in the Company's financial statements or tax returns. The measurement of the deferred items is based on enacted tax laws. In the event the future consequences of differences between financial reporting bases and

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

the tax bases of the Company's assets and liabilities result in a deferred tax asset, FASB Statement No. 109 requires an evaluation of the probability of being able to realize the future benefits indicated by such asset. A valuation allowance related to a deferred tax asset is recorded when it is more likely than not that some portion of the deferred tax asset will not be realized. The Company reviews the need for a valuation allowance on a quarterly basis and believes sufficient uncertainty exists regarding the realizability of the deferred tax assets such that a valuation allowance has been recorded on net deferred tax assets.

COMPUTATION OF EARNINGS PER SHARE

The computation of basic earnings per share ("EPS") is based on the weighted average number of common shares outstanding during each period. The computation of diluted earnings per share is based on the weighted average number of common shares outstanding during the period plus, when their effect is dilutive, incremental shares consisting of shares subject to stock options, unvested restricted stock, and shares issued upon conversion of convertible debt.

Emerging Issues Task Force Issue No. 04-08, "The Effect of Contingently Convertible Instruments on Diluted Earnings per Share" ("EITF No. 04-08") requires companies to account for contingently convertible debt using the "if converted" method set forth in SFAS No. 128 "Earnings Per Share" for calculating diluted EPS. Under the "if converted" method, the after-tax effect of interest expense related to the convertible securities is added back to net income, and convertible debt is assumed to have been converted to equity at the beginning of the period and is added to outstanding common shares, unless the inclusion of such shares is anti-dilutive. For the years ended December 31, 2006 and 2005, the 5,305,040 shares from the assumed conversion of convertible debt are antidilutive.

The following is a reconciliation of the computations of basic and diluted EPS information for each of the three years ended December 31, 2006, 2005 and 2004 (in thousands, except per share data):

YEARS ENDED DECEMBER 31,	2006	2005	2004
Basic and diluted:			
Net income	\$15,115	\$22,021	\$ 8,458
Weighted average shares outstanding (basic)	42,389	41,948	46,794
Effect of dilutive securities:			
Unvested common shares outstanding	552	523	295
Unexercised stock options	2,750	3,032	1,068
Adjusted weighted average shares for diluted EPS	45,691	45,503	48,157
Basic earnings per share	\$ 0.36	\$ 0.52	\$ 0.18
Diluted earnings per share	\$ 0.33	\$ 0.48	\$ 0.18

On December 22, 2006, the Company acquired all of the issued and outstanding shares of Plan Data Management, Inc. The estimated purchase price as of December 31, 2006 was approximately \$19.6 million, which consisted of 491,488 shares of the Company's common stock with a value of \$16.28 per share (which represents the average closing price of TriZetto's common stock for the 20 trading days ending October 27, 2006), cash payments of \$8.0 million, assumed liabilities of \$3.1 million and estimated acquisition-related costs of \$500,000. Due to the close of the acquisition late in the year, the issuance of the 491,488 shares of common stock and the cash payment of \$8.0 million to PDM stockholders and option holders were not completed prior to December 31, 2006. However, these amounts were accrued as of December 31, 2006. The computation of earnings per share for the year ended December 31, 2006 did not include the issuance of the 491,488 shares of common stock or the financial operating results of PDM since the impact of these amounts was not material.

COMPREHENSIVE INCOME

The Company has adopted the provisions of FASB Statement No. 130, "Comprehensive Income" ("Statement 130"). Statement 130 establishes standards for reporting and display of comprehensive income and its components for general-purpose financial statements. Comprehensive income is defined as net income plus all revenues, expenses, gains and losses from non-owner sources that are excluded from net income in accordance with U.S. generally accepted accounting principles. Comprehensive income was equal to net income for 2006, 2005 and 2004.

RECLASSIFICATIONS

Certain reclassifications, none of which affected net income, have been made to prior year amounts to conform to current year presentation.

RECENT ACCOUNTING PRONOUNCEMENTS

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). FIN 48 applies to all tax positions accounted for under SFAS No. 109, "Accounting for Income Taxes" and defines the confidence level that a tax position must meet in order to be recognized in the financial statements. The interpretation requires that the tax effects of a position be recognized only if it is "more-likely-than-not" to be sustained by the taxing authority as of the reporting date. If a tax position is not considered "more-likely-than-not" to be sustained then no benefits of the position are to be recognized. FIN 48 requires additional disclosures and is effective as of the beginning of the first fiscal year beginning after December 15, 2006. The Company does not expect the adoption of FIN 48 to have a material impact on its consolidated results of operations and financial condition.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

3. PREPAID EXPENSES AND OTHER ASSETS

Prepaid expenses and other assets consist of the following (in thousands):

DECEMBER 31,	2006	2005
Prepaid expenses—other	\$ 1,450	\$ 1,369
Prepaid hardware & software license maintenance	5,484	3,473
Prepaid commission & royalty	145	1,919
Up-front fees	6,198	7,664
Accounts receivable—other	735	1,087
Prepaid insurance	576	551
Prepaid rent & operating leases	830	1,268
Prepaid deposits	5,045	4,293
Cash value of life insurance policies	572	151
Acquisition costs	1,471	—
Other	1,256	777
	23,762	22,552
Less: Current portion	(11,415)	(11,375)
	\$ 12,347	\$ 11,177

4. PROPERTY AND EQUIPMENT

Property and equipment, net, consist of the following (in thousands):

DECEMBER 31,	2006	2005
Computer equipment	\$ 37,104	\$ 32,831
Furniture and fixtures	6,647	5,292
Other equipment	4,878	4,261
Software	36,354	31,518
Leasehold improvements	6,702	3,974
	91,685	77,876
Less: Accumulated depreciation	(64,908)	(52,146)
	\$ 26,777	\$ 25,730

Depreciation expense for the years ended December 31, 2006, 2005 and 2004 was \$12.9 million, \$15.5 million and \$14.9 million, respectively. Included in property and equipment at December 31, 2006 and 2005 is equipment acquired under capital leases totaling approximately \$24.3 million and \$22.1 million, and related accumulated depreciation of \$20.9 million and \$18.7 million, respectively.

Under FASB Statement No. 144, the Company is required to perform an evaluation of its long-lived assets for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. The Company did not perform any evaluation in 2006 or 2005, as management did not believe that any such indicators existed.

5. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets, net, consist of the following (in thousands):

DECEMBER 31,	2006	2005
NON-AMORTIZABLE INTANGIBLE ASSETS		
Goodwill	\$ 90,337	\$ 87,170
AMORTIZABLE INTANGIBLE ASSETS		
Customer lists	\$ 9,700	\$ 2,300
Core technology and intellectual property	28,674	7,074
Tradenames	4,879	4,879
	43,253	14,253
Less: Accumulated amortization	(15,906)	(10,918)
	\$ 27,347	\$ 3,335

In December 2005, the Company recorded \$47.7 million in goodwill in connection with its acquisition of CareKey, Inc., which represented the excess of the purchase price over the estimated fair market value of the assets purchased and liabilities assumed. In the third quarter of 2006, the Company received the final valuation of assets and liabilities assumed. The final valuation of identifiable intangible assets was determined to be \$29.0 million. The \$29.0 million allocated to identifiable intangible assets includes customer relationships and maintenance agreements of \$7.4 million to be amortized over a ten-year life, existing software of \$13.0 million to be amortized over a five-year life, and core technology of \$8.6 million to be amortized over a ten-year life.

In December 2006, the Company recorded \$15.0 million in goodwill in connection with its acquisition of Plan Data Management, Inc. ("PDM") (Note 14), which represents the excess of the purchase price over the estimated fair market value of the assets purchased and liabilities assumed. Because the acquisition was completed on December 22, 2006, there was not sufficient time to finalize the fair market valuation of assets and liabilities acquired as of December 31, 2006. Goodwill also decreased by \$526,000 in December 2006 as a result of the initial recognition of tax benefits obtained in the Diogenes acquisition (Note 14).

The Company tested goodwill using the two-step process prescribed in FASB Statement No. 142. The first required step is a screen for potential impairment, while the second step measures the amount of the impairment, if any. The Company performed its annual impairment test on March 31, 2006, and this test did not reveal any indications of impairment.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The amount of amortization expense excluded from cost of revenue—products consists primarily of amounts amortized with respect to acquired technology, which includes core or completed technology and existing software. Amortization expense recorded for the years ended December 31, 2006, 2005, and 2004 related to acquired technology was \$4.1 million, \$660,000 and \$440,000, respectively. Amortization expense recorded for the years ended December 31, 2006, 2005, and 2004 related to acquired other intangible assets was \$867,000, \$2.2 million and \$3.8 million, respectively. The estimated aggregate amortization expense related to these intangible assets for the next five fiscal years and thereafter is as follows (in thousands):

FOR THE YEARS ENDING DECEMBER 31,	ACQUIRED TECHNOLOGY	ACQUIRED OTHER INTANGIBLE ASSETS	TOTAL
2007	\$ 4,120	\$ 852	\$ 4,972
2008	4,120	852	4,972
2009	3,680	852	4,532
2010	3,460	852	4,312
2011 and thereafter	4,300	4,259	8,559
Total	\$19,680	\$7,667	\$27,347

Amortization expense related to existing intangible assets will vary from amounts identified above in the event the Company recognizes impairment charges prior to the amortized useful life of any intangible assets. Additionally, amortization expense will vary from amounts identified above when the final accounting for the PDM and QCSI acquisitions are completed, and the allocation between goodwill and identifiable intangible assets is recorded.

6. ACCRUED LIABILITIES

Accrued liabilities consist of the following (in thousands):

DECEMBER 31,	2006	2005
Accrued payroll and benefits	\$29,475	\$20,767
Accrued professional and litigation fees and settlements	8,609	1,590
Accrued acquisition costs	16,500	25,611
Accrued outside services	370	959
Accrued employee relations	602	775
Accrued income and other taxes	2,125	1,253
Other	3,914	6,002
	\$61,595	\$56,957

Effective January 1, 2006, the Company became self-insured for certain losses related to employee health and dental benefits. The Company records a liability based on an estimate of claims incurred but not recorded determined by actuarial analysis of historical claims experience and historical industry data. The Company maintains individual and aggregate stop-loss coverages with a third party insurer to limit its total exposure for these programs.

7. DEBT

In December 2004, the Company and IMS Health Incorporated (“IMS Health”) entered into a Share Purchase Agreement pursuant to which the Company purchased all of the 12,142,857 shares of the Company’s common stock owned by IMS Health for an aggregate purchase price of \$82.0 million, or \$6.75 per share. The purchase price for the repurchase of shares was paid by delivery of \$44.6 million in cash and a Subordinated Promissory Note in the principal amount of \$37.4 million. The Subordinated Promissory Note bore interest at the rate of 5.75% and was due and paid in full on January 21, 2005 from the Company’s cash accounts. The cash portion of the purchase price was financed with the proceeds of the Company’s sale of 6,600,000 shares of its common stock to ValueAct Capital for \$6.75 per share totaling \$44.6 million in proceeds.

In January 2006, the Company entered into an amendment to its Credit Agreement established December 21, 2004. The amendment increased the amount of the revolving credit facility from \$50.0 million to \$100.0 million, subject to certain fixed percentages of its recurring revenues (which includes outsourced business services and software maintenance revenue—see Note 16), and extended the expiration date of the Credit Agreement to January 5, 2010. Principal outstanding under the facility bears interest at a per annum rate equal to either (i) the LIBOR rate plus an adjustable applicable margin of between 1.75% and 2.25% or (ii) the lending institution’s prime rate plus an adjustable applicable margin of between 0.0% and 0.5%, at the Company’s election, subject to specified restrictions. The unused portions of the facility are subject to unused facility fees. In the event the Company terminates the Credit Agreement prior to its expiration, the Company will be required to pay the lending institution a termination fee equal to 2% of the maximum credit amount if the termination is prior to the second anniversary of the Credit Agreement or 1% of the maximum credit amount if the Credit Agreement is terminated thereafter, up to 90 days prior to the expiration of the Credit Agreement, subject to specified exceptions. Management expects to use the proceeds for general working capital purposes and has granted the lending institution a security interest in all of the Company’s assets. The Credit Agreement contains customary affirmative and negative covenants for credit facilities of this type, including limitations with respect to indebtedness, liens, investments, distributions, mergers and acquisitions, dispositions of assets and transactions with the Company’s affiliates. The Credit Agreement also includes financial covenants including minimum EBITDA, determined on a quarterly basis ranging from \$33.4 million at March 31, 2006 and increasing over time to \$46.9 million at December 31, 2006. The Company also becomes subject to further restrictions, including minimum liquidity, minimum recurring revenue (which includes outsourced business services and software maintenance revenue—see Note 16) and maximum capital expenditures. As of December 31, 2006, the Company was in compliance with all applicable covenants and other restrictions under the Credit Agreement. As of December 31, 2006, the Company had outstanding borrowings on the revolving line of credit of \$12.0 million.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

On September 30, 2005, the Company entered into a Purchase Agreement with UBS Securities, LLC, Banc of America Securities, LLC and William Blair & Company LLC (the "Initial Purchasers"), to sell \$100 million aggregate principal amount of its 2.75% Convertible Senior Notes due 2025 (the "Notes") in a private placement in reliance on Section 4(2) of the Securities Act of 1933, as amended (the "Securities Act"). The Notes have been resold by the Initial Purchasers to qualified institutional buyers pursuant to Rule 144A under the Securities Act. The sale of the Notes to the Initial Purchasers was consummated on October 5, 2005.

The aggregate net proceeds received by the Company from the sale of the Notes were approximately \$82.0 million, after deducting the amount used to repurchase one million shares of its common stock at \$14.50 per share in connection with the private placement, the Initial Purchasers' discount and estimated offering expenses. The indebtedness under the Notes constitutes the Company's senior unsecured obligations and will rank equally with all of its existing and future unsecured indebtedness.

The Notes were issued pursuant to an Indenture, dated October 5, 2005, by and between the Company and Wells Fargo Bank, National Association, as trustee. The Notes bear interest at a rate of 2.75%, which is payable in cash semi-annually in arrears on April 1 and October 1 of each year, commencing on April 1, 2006, to the holders of record on the preceding March 15 and September 15, respectively.

The Notes are convertible into shares of the Company's common stock at an initial conversion price of \$18.85 per share, or 53.0504 shares for each \$1,000 principal amount of Notes, subject to certain adjustments set forth in the Indenture. Upon conversion of the Notes, the Company will have the right to deliver shares of its common stock, cash or a combination of cash and shares of its common stock. The Notes are convertible (i) prior to October 1, 2020, during any fiscal quarter after the fiscal quarter ending December 31, 2005, if the closing sale price of the Company's common stock for 20 or

more trading days in a period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter exceeds 120% of the conversion price in effect on the last trading day of the immediately preceding fiscal quarter, (ii) prior to October 1, 2020, during the five business day period after any five consecutive trading day period (the "Note Measurement Period") in which the average trading price per \$1,000 principal amount of Notes was equal to or less than 97% of the average conversion value of the Notes during the Note Measurement Period, (iii) upon the occurrence of specified corporate transactions, as described in the Indenture, (iv) if the Company calls the Notes for redemption, or (v) any time on or after October 1, 2020.

The Notes mature on October 1, 2025. However, on or after October 5, 2010, the Company may from time to time at its option redeem the Notes, in whole or in part, for cash, at a redemption price equal to 100% of the principal amount of the Notes the Company redeems, plus any accrued and unpaid interest to, but excluding, the redemption date. On each of October 1, 2010, October 1, 2015 and October 1, 2020, holders may require the Company to purchase all or a portion of their Notes at a purchase price in cash equal to 100% of the principal amount of the Notes to be purchased, plus any accrued and unpaid interest to, but excluding, the purchase date. In addition, holders may require the Company to repurchase all or a portion of their Notes upon a fundamental change, as described in the Indenture, at a repurchase price in cash equal to 100% of the principal amount of the Notes to be repurchased, plus any accrued and unpaid interest to, but excluding, the fundamental change repurchase date. Additionally, the Notes may become immediately due and payable upon an Event of Default, as defined in the Indenture. Pursuant to a Registration Rights Agreement dated October 5, 2005, the Company filed with the Securities and Exchange Commission, a registration statement under the Securities Act for the purpose of registering for resale, the Notes and all of the shares of its common stock issuable upon conversion of the Notes.

Notes payable and line of credit consist of the following at December 31 (in thousands):

	NOTES PAYABLE		LINE OF CREDIT	
	2006	2005	2006	2005
Long-term convertible debt, due 2025, interest at 2.75% fixed rate, payable semi-annually in arrears	\$100,000	\$100,000	\$ —	\$ —
Revolving credit facility of \$100.0 million, interest at the lending institution's prime rate (8.25% at December 31, 2006), payable monthly in arrears	—	—	12,000	—
Other	115	120	—	—
Total debt	\$100,115	\$100,120	\$12,000	—
Less: Current portion	(115)	(120)	—	—
	\$100,000	\$100,000	\$12,000	\$ —

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Future principal payments of notes payable and line of credit at December 31, 2006 are as follows (in thousands):

FOR THE PERIODS ENDING DECEMBER 31,	NOTES PAYABLE	LINE OF CREDIT
2007	\$ 115	\$ —
2008	—	—
2009	—	—
2010	—	12,000
2011	—	—
Thereafter	100,000	—

As of December 31, 2006, the Company had outstanding four unused standby letters of credit in the aggregate amount of \$921,000 which serve as security deposits for certain operating leases. The Company is required to maintain a cash balance equal to the outstanding letters of credit, which is classified as restricted cash on the balance sheet.

8. RELATED PARTY TRANSACTIONS

In December 2004, the Company entered into a Share Purchase Agreement with IMS Health (See Note 7).

9. COMMITMENTS AND CONTINGENCIES

The Company leases office space and equipment under non-cancelable operating and capital leases, respectively, with various expiration dates through 2016. Capital lease obligations are collateralized by the equipment subject to the leases. The Company is responsible for maintenance costs and property taxes on certain of the operating leases. Rent expense for the years ended December 31, 2006, 2005 and 2004 was \$7.8 million, \$6.8 million and \$7.5 million, respectively. These amounts are net of sublease income of \$331,000, \$668,000 and \$522,000, respectively.

The aggregate future minimum rentals to be received under non-cancelable subleases as of December 31, 2006 is approximately \$7,000. Future minimum lease payments under non-cancelable operating and capital leases at December 31, 2006 are as follows (in thousands):

FOR THE YEARS ENDING DECEMBER 31,	CAPITAL LEASES	OPERATING LEASES
2007	\$ 1,618	\$13,603
2008	1,119	11,424
2009	506	8,520
2010	404	6,739
2011	159	5,964
Thereafter	—	17,113
Total minimum lease payments	3,806	\$63,363
Less: interest	(315)	
Less: current portion	(1,461)	
	\$ 2,030	

As of December 31, 2006, the Company had three sale-leaseback transactions for certain computer hardware equipment. The leases, which are classified as operation, have lease terms of three years. The Company did not realize any gain or loss on the sale as the fair value approximated the carrying value of the equipment. The future lease payments under these sale-leaseback transactions for the years ending December 31, 2007, 2008 and 2009, are included in the above table totaling \$400,000, \$400,000 and \$140,000, respectively.

Pursuant to the terms of the Agreement and Plan of Merger in connection with the Company's acquisition of CareKey, CareKey stockholders and option holders are entitled to receive three contingent consideration payments of \$8.3 million each (up to \$25.0 million), upon the achievement of certain revenue milestones during the period beginning upon acquisition and ending December 31, 2008. In addition, further consideration payable in cash or stock at our election, may be paid to former CareKey stockholders and option holders if, prior to December 31, 2008, the acquired CareKey products generate revenues in excess of certain revenue milestones and/or if a negotiated multiple of software maintenance revenues of acquired CareKey products during the fiscal year ended December 31, 2009 exceed total purchase consideration made to those former CareKey stockholders and option holders.

Under the Agreement and Plan of Merger with PDM (Note 14), PDM stockholders and option holders may also be entitled to receive contingent consideration as follows: aggregate payments of up to \$5.0 million on or before June 30, 2007, \$5.0 million on or before December 31, 2008, and \$8.0 million on or before December 31, 2009, each subject to reduction if certain revenue thresholds are not satisfied during the applicable measurement period. Additional contingent consideration may be paid on June 30, 2009 if certain revenue thresholds are satisfied, provided that in no event will the aggregate consideration of all payments exceed \$42.0 million. The merger consideration is also subject to adjustment based upon minimum cash and working capital balances. It is expected that 50% of any such payment will be made in cash and 50% will be paid in shares of the Company's common stock.

10. LITIGATION

On October 26, 2004, a jury in California Superior Court, County of Alameda, delivered its verdict in the case of Associated Third Party Administrators v. The TriZetto Group, Inc., a dispute involving technology agreements between Associated Third Party Administrators ("ATPA"), a former QicLink™ customer, and the Company. In its verdict, the jury found that the Company made certain misrepresentations to ATPA in connection with the license of QicLink™ software in 2001 and awarded damages of approximately \$1.85 million, representing primarily the amount of the license fee paid by ATPA. In the first quarter of 2005, a judgment was entered by the court, which included, in addition to damages of \$1.85 million, approximately \$500,000 in pre-judgment interest and recoverable costs. The Company recorded an accrual for the additional \$500,000 of costs in

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

the first quarter of 2005 increasing the total accrual for the dispute to \$2.35 million. In June 2005, the Company entered into a settlement agreement with ATPA in which the Company agreed to pay ATPA \$2.2 million to fully resolve the dispute. The Company paid this amount to ATPA in July 2005. In June 2005, the Company's insurance carrier agreed to reimburse the Company a total of \$1.1 million of the settlement. The reimbursement was received in July 2005 and was recorded as a reduction to expense.

In September 2004, McKesson Information Solutions LLC ("McKesson") filed a lawsuit against the Company in the United States District Court for the District of Delaware. In its complaint, McKesson alleged that the Company made, used, offered for sale, and/or sold a clinical editing software system that infringed McKesson's United States Patent No. 5,253,164, entitled "System And Method For Detecting Fraudulent Medical Claims Via Examination Of Services Codes." McKesson sought injunctive relief and substantial monetary damages, including treble damages for willful infringement. On April 4, 2006, in response to the Company's motion for summary judgment, the court ruled, as a matter of law, that the Company's software products did not infringe 12 of the 15 claims of McKesson's patent that were involved in this dispute, leaving claims 1, 2 and 16. On April 17, 2006, a jury trial commenced on the first phase of this case to determine the issue of infringement of the remaining three claims. On April 26, 2006, the jury found that the Company's Facets[®], QicLink[™] and ClaimFacts[®] software products infringed claims 1 and 2, but not claim 16 of the patent. On May 4, 2006, the court scheduled the second phase of the trial to commence on October 3, 2006 on the issues of the Company's validity, estoppel and laches defenses and on the issue of McKesson's damages, if any.

On September 7, 2006, the Company entered into a Settlement Agreement with McKesson to settle the lawsuit. As part of the Settlement Agreement, the Company agreed to pay McKesson a one-time royalty fee of \$15.0 million for a license in the patent that covers past and future use of the Company's products and services by all existing customers. The \$15.0 million, payable in two equal installments on September 30, 2006 and September 30, 2007, was expensed in the third quarter of 2006. The Company's customers with maintenance agreements also will continue to receive software version upgrades that include clinical editing capabilities. Going forward, the Company may continue to include its clinical editing functionality in versions of Facets[®] sold to new health plan customers with 100,000 or fewer members and in versions of QicLink[™] sold to any new customers. The Company has agreed to pay McKesson a royalty fee of 5% of the net licensing revenue received from new sales of Facets[®] and QicLink[™] containing the Company's clinical editing functionality. However, pursuant to the terms of the Settlement Agreement, the Company will no longer include its clinical editing functionality in versions of Facets[®] sold to new customers with more than 100,000 members, beginning November 1, 2006. In these cases, new customers may choose their clinical editing solution from available third-party providers.

In addition to the matter described above, the Company is involved in litigation from time to time relating to claims arising out of its operations in the normal course of business. Except as discussed above, the Company was not a party to any other legal proceedings, the adverse outcome of which, in management's opinion, individually or in the aggregate, would have a material adverse effect on its results of operations, financial position and/or cash flows.

11. STOCKHOLDERS' EQUITY

COMMON STOCK

In December 2004, the Company and IMS Health entered into a Share Purchase Agreement pursuant to which, on the same date, the Company purchased all of the 12,142,857 shares ("IMS Shares") of the Company's common stock, owned by IMS Health for an aggregate purchase price of \$82.0 million, or \$6.75 per share. The purchase price was paid by delivery of \$44.6 million in cash and a Subordinated Promissory Note in the principal amount of \$37.4 million. The Subordinated Promissory Note bore interest at the rate of 5.75% and was due and paid in full on January 21, 2005 from the Company's cash accounts. Immediately following the purchase of the IMS Shares, the Company placed 6,600,000 of such shares with ValueAct Capital for an aggregate purchase price of \$44.6 million, or \$6.75 per share.

Pursuant to a letter dated December 5, 2004, the Company was given the right to repurchase up to 600,000 of the shares sold to ValueAct. On September 19, 2005, the Company exercised its repurchase right with respect to all 600,000 shares for an aggregate purchase price of \$5.3 million, or \$8.83 per share, that was paid for in cash.

On September 30, 2005, the Company entered into a Purchase Agreement with UBS Securities, LLC, Banc of America Securities, LLC and William Blair & Company LLC (the "Initial Purchasers"), to sell \$100 million aggregate principal amount of its 2.75% Convertible Senior Notes due 2025 (the "Notes") in a private placement in reliance on Section 4(2) of the Securities Act of 1933, as amended (the "Securities Act"). The Notes have been resold by the Initial Purchasers to qualified institutional buyers pursuant to Rule 144A under the Securities Act. The sale of the Notes to the Initial Purchasers was consummated on October 5, 2005.

The aggregate net proceeds received by the Company from the sale of the Notes were approximately \$82.0 million, after deducting the amount used to repurchase 1,000,000 shares of its common stock at \$14.50 per share in connection with the private placement, the Initial Purchasers' discount and estimated offering expenses. The indebtedness under the Notes constitutes the Company's senior unsecured obligations and will rank equally with all of its existing and future unsecured indebtedness.

Common stockholders are entitled to dividends as and when declared by the Board of Directors subject to the prior rights of preferred stockholders. The holders of each share of common stock are entitled to one vote.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

STOCK OPTION PLANS

In May 1998, the Company adopted the 1998 Stock Option Plan (the "1998 Stock Option Plan") under which the Board of Directors (the "Board") or the Compensation Committee (the "Committee") may issue incentive and non-qualified stock options to employees, directors and consultants. The Committee had the authority to determine to whom options will be granted, the number of shares and the term and exercise price. Options were to be granted at an exercise price not less than fair market value for incentive stock options or 85% of fair market value for non-qualified stock options. For individuals holding more than 10% of the voting rights of all classes of stock, the exercise price of incentive stock options will not be less than 110% of fair market value. The options generally vest and become exercisable annually at a rate of 25% of the option grant over a four-year period. The term of the options would be no longer than five years for incentive stock options for which the grantee owns greater than 10% of the voting power of all classes of stock and no longer than ten years for all other options.

On November 30, 2000, in connection with the Resource Information Management Systems, Inc. ("RIMS") acquisition, the Company adopted the RIMS Stock Option Plan based primarily upon RIMS' existing non-statutory stock option plan. Unless previously terminated by the stockholders, the Plan shall terminate at the close of business on January 1, 2009, and no options shall be granted under it thereafter. Such termination shall not affect any option previously granted. Upon a business combination by the Company with any corporation or other entity, the Company may provide written notice to optionees that options shall terminate on a date not less than 14 days after the date of such notice unless theretofore exercised. In connection with such notice, the Company may, in its discretion, accelerate or waive any deferred exercise period.

In March 2004, the Board of Directors of the Company amended and restated the 1998 Stock Option Plan, renaming it the 1998 Long-Term Incentive Plan (the "Plan"). As amended, the Plan permits the granting of the following types of awards: options, share appreciation rights, restricted and unrestricted share awards, deferred share units, and performance awards. The principal changes made to the 1998 Stock Option Plan pursuant to this amendment and restatement are as follows: (i) renaming it "The TriZetto Group, Inc. 1998 Long-term Incentive Plan," (ii) increasing the numbers of shares available for issuance by 2,000,000 (from 11,000,000 to 13,000,000 shares), (iii) adding provisions that permit awards other than options, and (iv) modifying the Committee's discretion to administer the Plan and past or future awards. The terms and conditions of all options outstanding under the 1998 Stock Option Plan immediately before the effective date of this amendment and restatement shall continue to be governed by the terms and conditions of the 1998 Stock Option Plan (and the respective instruments evidencing each such option) as in effect on the date each such option was granted; provided, however, that any one or more provisions of the amended and restated Plan, may, in the Committee's discretion, be extended to one or more of such options (subject to the participant's written consent of any adverse changes).

In April 2006, the Board of Directors of the Company adopted, subject to stockholder approval, amendments to the Plan to (i) increase by 1,500,000 the total number of shares of the Company's common stock available for issuance under the Plan from 13,000,000 to 14,500,000 and (ii) increase by 500,000 the share limitation on awards other than options and stock appreciation rights from 700,000 to 1,200,000.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Activity under the plans related only to stock options was as follows (in thousands, except per share data):

	OUTSTANDING OPTIONS			
	SHARES AVAILABLE FOR GRANT	NUMBER OF SHARES	EXERCISE PRICE	WEIGHTED AVERAGE EXERCISE PRICE
Balances, December 31, 2003	2,761	6,815	\$ 0.25–\$63.25	\$10.26
Additional options reserved	2,000	—		
Granted	(2,442)	2,442	5.86– 7.07	6.64
Exercised	—	(255)	0.25– 6.50	2.59
Cancelled	1,314	(1,314)	1.00– 63.25	10.41
Balances, December 31, 2004	3,633	7,688	0.25– 63.25	9.33
Granted	(2,214)	2,214	8.35– 16.07	8.67
Exercised	—	(1,290)	0.25– 15.13	7.51
Cancelled	365	(365)	3.34– 15.25	8.71
Balances, December 31, 2005	1,784	8,247	0.25– 63.25	9.44
Additional options reserved	1,500	—		
Granted	(737)	737	12.75– 18.36	16.68
Exercised	—	(1,086)	0.25– 15.13	8.54
Cancelled	178	(178)	3.49– 20.25	9.88
	2,725	7,720	\$ 0.25–\$63.25	\$10.25
Less: Restricted stock awards granted	(722)			
Balances, December 31, 2006	2,003			

At December 31, 2006, the Company had reserved approximately 9,722,983 shares of common stock for issuance upon exercise of stock options and shares issuable under its stock option plans.

The options outstanding and currently exercisable by exercise price at December 31, 2006 are as follows (in thousands, except per share data):

RANGE OF EXERCISE PRICE	OPTIONS OUTSTANDING AT DECEMBER 31, 2005			OPTIONS EXERCISABLE AT DECEMBER 31, 2005	
	NUMBER OF SHARES	REMAINING CONTRACTUAL LIFE (YEARS)	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER OF SHARES	WEIGHTED AVERAGE EXERCISE PRICE
\$ 0.25–\$ 3.49	807	4.79	\$2.60	662	\$2.41
\$ 4.11–\$ 6.53	302	5.98	5.78	200	5.84
\$ 6.66–\$ 6.66	1,309	7.13	6.66	509	6.66
\$ 7.00–\$ 7.77	295	6.81	7.11	210	7.13
\$ 8.35–\$ 8.35	1,288	8.12	8.35	202	8.35
\$ 8.48–\$ 9.25	790	6.56	8.85	270	8.98
\$11.14–\$12.50	845	4.83	12.29	675	12.30
\$12.69–\$14.50	242	6.34	13.52	132	13.46
\$15.13–\$15.13	915	3.75	15.13	915	15.13
\$15.25–\$57.50	927	7.50	20.73	235	26.79
	<u>7,720</u>	6.30	10.25	<u>4,010</u>	10.47

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

At December 31, 2006, 2005, and 2004, options exercisable under the plans were 4,010,132, 3,765,394, and 3,825,989, respectively. The total intrinsic value of options outstanding and options exercisable at December 31, 2006 was \$66.0 million and \$33.9 million, respectively. The remaining contractual life of options exercisable at December 31, 2006 was 5.02 years.

The total intrinsic value of options exercised during the year ended December 31, 2006 was \$9.3 million. As of December 31, 2006, \$10.1 million of total unrecognized compensation cost related to stock options is expected to be recognized over a weighted average period of 1.92 years.

EMPLOYEE STOCK PURCHASE PLAN

In August 1999, the Board of Directors of the Company adopted the Employee Stock Purchase Plan (the "Stock Purchase Plan"), which is intended to qualify under Section 423 of the Internal Revenue Code. A total of 600,000 shares of common stock were reserved for issuance under the original Stock Purchase Plan. The Stock Purchase Plan was amended and restated on May 14, 2003 and again on May 11, 2005, ultimately increasing the number of common stock reserved for issuance to 1,500,000 shares, of which 385,052 remain available for issuance at December 31, 2006. Each employee of the Company who customarily works more than 20 hours per week for more than five months per calendar year is eligible to participate in offerings under the Stock Purchase Plan if on the offering date, such employee has been employed by the Company for at least 90 days. Employees who own more than 5% of the Company's outstanding stock may not participate. The Stock Purchase Plan permits eligible employees to purchase common stock through payroll deductions, which may not exceed the lesser of 15% of an employee's compensation or \$25,000.

The two semi-annual offerings under the Stock Purchase Plan begin on January 1 and July 1 and continue until the end of the six-month period ending on June 30 and December 31 (the "Offering Period"). The first Offering Period commenced on January 1, 2000. Effective July 1, 2005, the purchase price of the common stock under the Stock Purchase Plan will be equal to 95% of the fair market value per share of common stock on the last date of the offering period (or purchase date). The Stock Purchase Plan will terminate in 2009, unless terminated sooner by the Board of Directors. Shares issued under the Stock Purchase Plan in 2006, 2005, and 2004 were 70,866, 89,869, and 196,806, at a weighted average purchase price of \$15.82, \$8.02, and \$5.65 per share, respectively. Shares issued in 2005 represent only one offering period since the purchase date of the second offering period took place in early January 2006.

SHAREHOLDER RIGHTS PLAN

In September 2000, the Board of Directors of the Company adopted a shareholder rights plan. The plan provides for a dividend distribution of one preferred stock purchase right (a "Right") for each outstanding share of common stock, distributed to stockholders of record on or after October 19, 2000. The Rights will be exercisable only if a person

or group acquires 15% or more of the Company's common stock (an "Acquiring Person") or announces a tender offer for 15% or more of the common stock. Each Right will entitle stockholders to buy one one-hundredth of a share of newly created Series A Junior Participating Preferred Stock, par value \$0.001 per share, of the Company at an initial exercise price of \$75 per Right, subject to adjustment from time to time. However, if any person becomes an Acquiring Person, each Right will then entitle its holder (other than the Acquiring Person) to purchase at the exercise price, common stock of the Company having a market value at that time of twice the Right's exercise price. If the Company is later acquired in a merger or similar transaction, all holders of Rights (other than the Acquiring Person) may, for \$75.00, purchase shares of the acquiring corporation with a market value of \$150.00. Rights held by the Acquiring Person will become void. The Rights Plan excludes from its operation ValueAct Capital with respect to the shares of the Company's common stock acquired by it on December 21, 2004. As a result, their holdings will not cause the Rights to become exercisable or non-redeemable or trigger the other features of the Rights. The Rights will expire on October 2, 2010, unless earlier redeemed by the Board at \$0.001 per Right.

The holders of Series A Junior Participating Preferred Stock in preference to the holders of common stock, shall be entitled to receive, when, as and if declared by the Board of Directors, quarterly dividends payable in cash in an amount per share equal to 100 times the aggregate per share amount of all cash dividends or non-cash dividends other than a dividend payable in share of common stock.

Each share of Series A Junior Participating Preferred Stock shall entitle its holder to 100 votes.

DEFERRED STOCK COMPENSATION AND RESTRICTED STOCK

Prior to the January 1, 2006 adoption of SFAS No. 123R, the Company recorded deferred stock compensation related to stock options granted to employees, where the exercise price is lower than the fair market value of the Company's common stock on the date of the grant. Additionally, the Company recorded deferred stock compensation for the issuance of restricted stock to certain employees related to acquisitions and to certain employees to encourage continued service with the Company.

The Company recorded a total of \$1.4 million and \$3.0 million of deferred stock compensation in 2005 and 2004, respectively, for the issuance of restricted stock. The deferred stock compensation charge was then amortized to compensation expense over the vesting period of the underlying stock option or restricted stock awarded. Amortization of deferred stock compensation expense was \$1.4 million and \$594,000 in 2005 and 2004, respectively. The valuation of restricted stock is calculated based on the fair market value on the date of grant. Pursuant to the restricted stock agreements, the Company shall cancel any unvested shares of common stock upon termination of services. There were approximately 1,086,000 shares of restricted stock outstanding at December 31, 2005, of which 479,400 shares were unvested.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

With the adoption of SFAS No. 123R on January 1, 2006, the Company reclassified \$3.0 million of unearned deferred stock compensation to additional paid-in capital. There were approximately 1,348,000 shares of restricted stock outstanding at December 31, 2006, of which 545,536 shares were unvested.

The following table summarizes nonvested restricted stock awards as of December 31, 2006 and changes during the year ended December 31, 2006 (in thousands, except per share data):

	NUMBER OF SHARES	WEIGHTED- AVERAGE GRANT-DATE FAIR VALUE
Nonvested at December 31, 2005	479	\$ 7.64
Granted	270	16.56
Vested	(195)	7.30
Forfeited	(8)	16.81
Nonvested at December 31, 2006	546	12.04

As of December 31, 2006, there was \$5.2 million of total unrecognized compensation cost related to nonvested restricted stock awards, which will be amortized over the weighted-average remaining service period of 2.18 years.

12. INCOME TAXES

The components of the provision for income taxes are as follows (in thousands):

YEARS ENDED DECEMBER 31,	2006	2005	2004
Current:			
Federal	\$1,272	\$429	\$ —
State	1,222	(17)	1,101
	2,494	412	1,101
Deferred:			
Federal	—	—	—
State	—	—	—
	—	—	—
Provision for income taxes	\$2,494	\$412	\$1,101

Deferred income taxes reflect the net tax effects of temporary differences between carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax liabilities and assets as of December 31, 2006 and 2005, are as follows (in thousands):

	DECEMBER 31, 2006		DECEMBER 31, 2005	
	CURRENT	LONG TERM	CURRENT	LONG-TERM
Deferred tax assets:				
Reserves and accruals	\$ 8,143	\$ —	\$ 2,349	\$ —
Deferred compensation	—	2,886	—	130
Other	—	376	6	34
State taxes	729	—	12	—
Deferred revenue	—	—	533	—
Acquired intangible assets	—	—	—	1,137
Depreciation	—	245	—	—
Start-up costs	554	2,440	813	2,440
Net operating losses and capital losses	8,787	—	8,000	19,233
Tax credits	—	2,674	—	1,964
Total deferred tax assets	18,213	8,621	11,713	24,938
Deferred tax liabilities:				
Deferred revenue	(1,984)	—	—	—
Depreciation	—	—	—	(1,272)
State taxes	—	(40)	—	(1,204)
Acquired intangible assets	—	(13,234)	—	—
Capitalized software	—	(9,447)	—	(11,949)
Total deferred tax liabilities	(1,984)	(22,721)	—	(14,425)
Net deferred tax assets before valuation allowance	16,229	(14,100)	11,713	10,513
Valuation allowance	(2,129)	—	(11,713)	(10,513)
Net deferred taxes	\$14,100	\$(14,100)	\$ —	\$ —

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The valuation allowance on the deferred tax assets was \$2.1 million and \$22.2 million as of December 31, 2006 and 2005, respectively. The valuation allowance decreased by \$20.1 million during 2006 as a result of current year operating profits which allowed for the utilization of net operating loss carryovers, and also as a result of \$15.4 million of net deferred liabilities recorded in connection with the acquisition of CareKey.

At December 31, 2006 and 2005, deferred tax assets do not include \$9.5 million and \$5.8 million, respectively, of excess tax benefits from employee stock option exercises that are a component of the Company's net operating loss carryovers. Deferred taxes and the valuation allowance as of December 31, 2005 have been restated in order to conform to the 2006 presentation. Equity will be increased by \$9.5 million when such excess tax benefits are realized.

If and when the Company decreases the valuation allowance on its deferred tax asset, approximately \$1.5 million will be allocated to income tax benefit and \$600,000 will be recorded as an adjustment to goodwill. During 2006, goodwill decreased by \$526,000 as a result of the initial recognition of tax benefits obtained in the Diogenes acquisition.

The Company's effective tax rate differs from the statutory rate as shown in the following schedule (in thousands):

YEARS ENDED DECEMBER 31,	2006	2005	2004
Tax expense at federal statutory rate	\$ 6,163	\$ 7,851	\$ 3,250
State income taxes	1,970	(17)	1,101
Change in valuation allowance	(5,926)	(7,658)	(3,498)
Initial recognition of tax benefits allocated to goodwill	526	—	—
Refund of prior year state taxes	(354)	—	65
Reduction in reserve for uncertain tax positions	(350)	—	—
Nondeductible items	465	236	183
	\$ 2,494	\$ 412	\$ 1,101

Federal and state tax loss carryforwards at December 31, 2006 are \$44.1 million and 42.0 million, respectively. The federal tax loss carryforwards will start to expire beginning in 2010. The state tax loss carryforwards will start to expire beginning in 2007. Approximately \$12.0 million of the remaining federal and state tax loss carryforwards are related to net operating losses obtained in connection with the Diogenes and CareKey acquisitions. Such net operating losses are subject to limitations in accordance with IRC Section 382.

13. EMPLOYEE BENEFIT PLANS

In January 1998, the Company adopted a defined contribution plan (the "401(k) Plan") which qualifies under Section 401(k) of the Internal Revenue Code of 1986. Employees are eligible to participate the first day of the month following 30 days of employment. Eligible employees may make voluntary contributions to the 401(k) Plan of up to 25% of their annual compensation, not to exceed the statutory limit.

Effective January 1, 2001, the Company provides a discretionary matching contribution to the 401(k) Plan in the amount of \$0.50 for each \$1.00 contributed to the Plan, up to 6% of pay. Employees must be employed on the last day of the Plan Year (December 31) to receive the match. The match has a three-year vesting period after which the employee will be 100% vested. The Company's cash contributions to the 401(k) plan in 2006, 2005, and 2004 were approximately \$2.3 million, \$1.9 million, and \$2.1 million, respectively.

On December 21, 2005, the Company's Compensation Committee of the Board of Directors formally adopted the Executive Deferred Compensation Plan (the "Plan"). The Plan is an unfunded deferred compensation plan established and maintained for the purpose of providing key management employees with the opportunity to defer the receipt of compensation and to accumulate earnings on such deferrals on a tax-deferred basis. The Company's Compensation Committee of the Board of Directors determines which key management employees will be eligible to participate in the Plan. Currently, all of the executive officers of the Company are eligible to participate. The Plan is administered by the Company and became effective as of June 30, 2005.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Under the Plan, each participant may elect to defer, for any calendar year, up to 75% of his or her base salary and/or 100% of any commissions and/or bonuses earned during such calendar year. Amounts deferred for each participant are recorded in a bookkeeping account for such participant. Each participant is allowed to make a hypothetical allocation of the amounts credited to his or her account among investment options/indices that the Company makes available from time to time. Each account is credited at least annually with notational earnings equal to the aggregate/weighted average return on the investment options/indices selected by the participant, less expenses. The Company also may credit each participant's account with a discretionary company contribution. Company contributions vest after three years of service with the Company. The Company's cash contribution to the Plan in 2006 was approximately \$52,000.

Upon termination of employment, a participant is entitled to a benefit from the Company equal to the amount of vested contributions credited to his or her account, subject to certain restrictions. Alternatively, a participant may elect to have all or a portion the contributions in his or her account paid in one or more installments, subject to certain waiting period and other restrictions set forth in the Plan.

The Company has purchased life insurance policies with the funds in which the executive officers elected to defer in the Plan. The majority of the non-qualified retirement plan assets are held in a company-owned life insurance policy, whose investment assets are a separately-managed portfolio administered by an insurance company. The assets held under this insurance policy are recorded at estimated fair value with changes in estimated value recorded in net earnings. At the end of fiscal year 2006, the Company was the beneficiary of various insurance contracts on some of the participants in the Plans. At December 31, 2006, these life insurance contracts had cash surrender values of approximately \$600,000.

14. ACQUISITIONS

DIOGENES, INC.

On April 26, 2004, the Company completed its acquisition of Diogenes, Inc. ("Diogenes"). Diogenes developed and marketed transaction-messaging software, which provides EDI-class transaction processing across the Internet. The Company determined that Diogenes' software as adapted to handle healthcare claims and other business transactions would broaden and augment its current offerings and strengthen the infrastructure of its current offerings.

The final purchase price as of April 26, 2005 was approximately \$5.2 million, which consisted of cash payments of \$2.2 million, deferred payments of \$2.5 million, and acquisition-related costs of \$459,000. The former shareholders of Diogenes received a total payment of \$2.5 million on April 26, 2005, which was paid in cash. The acquisition of Diogenes was not significant to the Company's results of operations and therefore is not required to present pro forma information for the periods prior to acquisition.

The acquisition was accounted for using the purchase method of accounting and, accordingly, the purchase price was allocated to the tangible and intangible assets acquired and liabilities assumed on the basis of their estimated fair market values on the acquisition date. The excess of the purchase price over the estimated fair market value of the assets purchased and liabilities assumed was \$5.2 million and was allocated to goodwill and other intangible assets. Goodwill, representing the excess of the purchase price over the fair value of tangible and identifiable intangible assets acquired in the acquisition, will not be amortized and is not deductible for tax purposes. In 2006, goodwill decreased by \$526,000 as a result of the initial recognition of tax benefits obtained in the Diogenes acquisition. Other intangibles are being amortized over a period of 60 months from the date of acquisition.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CAREKEY, INC.

On December 22, 2005, the Company acquired all of the issued and outstanding shares of CareKey, Inc. ("CareKey") for cash. The acquisition was accounted for using the purchase method of accounting. As of December 31, 2005, the excess of the purchase price over the preliminary fair market value of the assets purchased and liabilities assumed was \$47.7 million and was allocated to goodwill.

In August 2006, the Company received the final valuation of assets and liabilities assumed. The final valuation of identifiable intangible assets was determined to be \$29.0 million. The \$29.0 million allocated to identifiable intangible assets includes customer relationships and maintenance agreements of \$7.4 million to be amortized over a ten-year life, existing software of \$13.0 million to be amortized over a five-year life, and core technology of \$8.6 million to be amortized over a ten-year life. CareKey stockholders and option holders are entitled to receive three contingent consideration payments of \$8.3 million each (up to \$25.0 million), upon the achievement of certain revenue milestones during the period beginning upon acquisition and ending December 31, 2008. In addition, further consideration payable in cash or stock at the Company's election, may be paid to former CareKey stockholders and option holders if, prior to December 31, 2008, the acquired CareKey products generate revenues in excess of certain revenue milestones and/or if a negotiated multiple of software maintenance revenues of acquired CareKey products during the fiscal year ended December 31, 2009 exceeds total purchase consideration made to those former CareKey stockholders and option holders.

The following unaudited pro forma summary combines the consolidated results of operations of the Company and CareKey for the years ended December 31, 2005 and 2004 as if the acquisition had occurred at the beginning of 2004, after giving effect to certain pro forma adjustments. This pro forma financial information is provided for informational purposes only and may not be indicative of the results of operations as they would have been had the transaction been effected on the assumed date, nor is it indicative of the results of operations which may occur in the future (in thousands, except per share amounts).

YEARS ENDED DECEMBER 31, (UNAUDITED)	2005	2004
Total revenue	\$298,462	\$274,636
Net income	\$ 16,709	\$ 1,951
Net income per share (diluted)	\$ 0.37	\$ 0.04

PLAN DATA MANAGEMENT, INC.

On December 22, 2006, the Company acquired all of the issued and outstanding shares of Plan Data Management, Inc. ("PDM"). PDM is a business solutions company focused on providing software and services to the healthcare industry primarily for payers that service members in Medicare Advantage, Medicare Part D and Medicaid plans.

Because the acquisition was completed on December 22, 2006, there was not sufficient time to finalize the fair market valuation of assets and liabilities acquired as of December 31, 2006. Once the Company receives a final valuation, the estimated purchase price will be adjusted and the allocation between goodwill and identifiable intangible assets will be recorded. Portions related to goodwill, representing the excess of the purchase price over the fair value of tangible and identifiable intangible assets acquired in the acquisition will not be amortized and is not deductible for tax purposes. Any amounts attributable to identifiable intangible assets will be amortized over their useful life and deductible over varying tax periods. The estimated purchase price as of December 31, 2006 was approximately \$19.6 million, which consisted of 491,488 shares of the Company's common stock with a value of \$16.28 per share (which represents the average closing price of TriZetto's common stock for the 20 trading days ending October 27, 2006), cash payments of \$8.0 million, assumed liabilities of \$3.1 million and estimated acquisition-related costs of \$500,000. Due to the close of the acquisition late in the year, the issuance of the 491,488 shares of common stock and the cash payment of \$8.0 million to PDM stockholders and option holders were not completed prior to December 31, 2006. However, these amounts were accrued as of December 31, 2006. The computation of earnings per share for the year ended December 31, 2006 did not include the issuance of the 491,488 shares of common stock or the financial operating results of PDM since the impact of these amounts was not material.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

PDM stockholders and option holders will also be entitled to receive contingent consideration under each of the following circumstances: aggregate payments of up to \$5.0 million on or before June 30, 2007, \$5.0 million on or before December 31, 2008, and \$8.0 million on or before December 31, 2009, each subject to reduction if certain revenue thresholds are not satisfied during the applicable measurement period. Additional contingent consideration may be paid on June 30, 2009 if certain revenue thresholds are satisfied, provided that in no event will the aggregate consideration of all payments exceed \$42.0 million. The merger consideration is also subject to adjustment based upon minimum cash and working capital balances. It is expected that 50% of each payment will be made in cash and 50% will be paid in shares of the Company's common stock.

The acquisition was accounted for using the purchase method of accounting. The excess of the purchase price over the preliminary fair market value of the assets purchased and liabilities assumed was \$15.0 million and was allocated to goodwill. Once the Company completes its final determination of the fair market value of the assets and liabilities assumed, the estimated purchase price will be adjusted and the allocation between goodwill and identifiable intangible assets will be recorded. The acquisition of PDM was not significant to the Company's results of operations and therefore no pro forma information for the periods prior to acquisition have been presented.

The purchase price allocations for the acquisitions described above were based on the estimated fair value of the assets and liabilities, on the date of purchase as follows (in thousands):

	DIOGENES	CAREKEY	PDM (1)
Total current assets	\$ 155	\$13,935	\$ 3,758
Property, plant, equipment and other non-current assets	834	1,562	861
Goodwill	1,350	36,390	15,018
Other intangible assets	3,300	29,000	—
Total assets acquired	5,639	80,887	19,637
less: liabilities assumed	(433)	(3,537)	(3,137)
Total purchase price of net assets acquired	\$5,206	\$77,350	\$16,500

(1) Allocation is preliminary pending final determination in 2007.

15. SUPPLEMENTAL CASH FLOW DISCLOSURES (IN THOUSANDS)

FOR THE YEARS ENDED DECEMBER 31,	2006	2005	2004
SUPPLEMENTAL DISCLOSURES			
FOR CASH FLOW INFORMATION			
Cash paid for interest	\$3,280	\$941	\$1,486
Cash paid for income taxes	2,467	1,090	1,189
NON-CASH INVESTING AND FINANCING ACTIVITIES			
Assets acquired through capital lease	2,487	1,424	1,151
Deferred stock compensation (net of cancellations)	—	1,319	2,604
Common stock issued for purchase of intangible assets	—	551	—
Note payable in exchange for repurchase of shares	—	—	37,414

16. SEGMENT INFORMATION

The Company has adopted FASB Statement No. 131, "Disclosures about Segments of an Enterprise and Related Information" ("Statement 131"). Statement 131 requires enterprises to report information about operating segments in annual financial statements and selected information about reportable segments in interim financial reports issued to stockholders. It also establishes standards for related disclosures about products and services, geographic areas and major customers. The Company has only one reportable segment.

The Company classifies its revenue in the following categories: services and other, and products as follows (in thousands):

FOR THE YEARS ENDED DECEMBER 31,	2006	2005	2004
Outsourced business services	\$ 86,877	\$ 79,418	\$ 89,916
Software maintenance	88,628	80,719	69,065
Consulting services and other	97,438	83,346	64,276
Services and other revenue	272,943	243,483	223,257
Software license fees	74,994	48,736	51,308
Products revenue	74,994	48,736	51,308
Total revenue	\$347,937	\$292,219	\$274,565

The Company's assets are all located in the United States and the Company's sales were primarily to customers located in the United States.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

17. QUARTERLY FINANCIAL DATA

(UNAUDITED AND IN THOUSANDS, EXCEPT PER SHARE DATA)

	NET REVENUE	GROSS PROFIT	NET INCOME (LOSS)	NET INCOME (LOSS) PER SHARE, BASIC	NET INCOME (LOSS) PER SHARE, DILUTED
FISCAL YEAR 2006 ⁽¹⁾					
First quarter	\$85,318	\$78,123	\$ 6,838	\$ 0.16	\$ 0.15
Second quarter	87,710	81,050	6,414	0.15	0.14
Third quarter	86,437	92,335	(5,683)	(0.13)	(0.13)
Fourth quarter	88,472	79,481	7,546	0.18	0.16
FISCAL YEAR 2005					
First quarter	71,818	67,075	4,298	0.10	0.10
Second quarter ⁽²⁾	72,508	67,172	4,979	0.12	0.11
Third quarter	73,053	66,923	6,480	0.15	0.14
Fourth quarter	74,840	68,656	6,264	0.15	0.14

⁽¹⁾In December 2006, the Company entered into a settlement with one of its larger customers that had disputed payments due from a software implementation project. The amounts represented revenue recorded in the first two quarters of 2006 and were included in the allowance for sales returns and a reduction to revenue in the quarter ended September 30, 2006.

⁽²⁾Included in cost of revenue are charges associated with loss on contracts. During the fourth quarter of 2003, the Company decided to wind-down its outsourcing services to physician group customers. As a result of this decision, the Company estimated that the existing customer agreements would generate a total loss of \$11.3 million until the terms of these agreements expired in 2008. The Company recorded a loss accrual in the fourth quarter of 2003. Through discussions and negotiations, the Company was

able to accelerate the termination of its services agreements with certain physician group customers and implemented cost cutting measures that reduced the expected future costs to support its remaining customers. As a result of these actions, the Company was able to reverse approximately \$5.9 million of previously accrued loss on contracts charges in 2004. Early in the second quarter of 2005, the Company executed termination agreements with its two remaining physician group customers. The Company continued to provide outsourced business services through May 2005, when the transition services were completed. The completion of these services to the remaining customers allowed the Company to reverse the remaining balance in the loss on contracts accrual of \$2.9 million in the second quarter of 2005. The total amount of loss actually incurred related to the outsourcing services to physician group customers was \$2.1 million in 2004 and \$403,000 in the first six months of 2005.

18. SUBSEQUENT EVENTS

QUALITY CARE SOLUTIONS, INC.

On January 10, 2007, the Company announced that it had completed the acquisition of privately held Quality Care Solutions, Inc. ("QCSI"). As previously announced, the definitive agreement for the acquisition was executed on September 13, 2006 and the Company received regulatory clearance for the transaction on December 29, 2006. QCSI is a provider of healthcare claims administration platforms and consumer-directed health solutions for payers. Enterprise applications include the QNXT product family, the QMACS product family and the web-based MyHealthBank suite of products.

Under the merger agreement, the Company paid to QCSI stockholders, warrant holders and option holders approximately \$130.0 million, net of cash received in the merger. QCSI security holders are entitled to an aggregate cash payment of \$5.0 million on January 31, 2008, subject to reduction if the parties determine that QCSI had negative working capital under the acquisition agreement as of the date of closing or to the extent that the Company is entitled to claims for indemnification under the acquisition agreement. In addition, former QCSI security holders will be entitled to receive an aggregate cash payment of \$7.0 million on January 31, 2008 if license and software revenues arising from the sale of QCSI products reach specified thresholds during the fiscal year ending on December 31, 2007. The Company also assumed approximately \$1.0 million of QCSI's debt.

In connection with the QCSI acquisition, the Company adopted the Quality Care Solutions, Inc. Stock Option Plan based primarily upon QCSI's existing stock option plan. Unless previously terminated by the stockholders, the Plan shall terminate at the close of business on December 31, 2007, and no options shall be granted under it thereafter.

WELLS FARGO LINE OF CREDIT

On January 10, 2007, the Company and each of its subsidiaries (the "Borrowers") entered into an Amended and Restated Credit Agreement (the "Credit Agreement") with Wells Fargo Foothill, Inc., as the administrative agent and lender (the "Lender").

The Credit Agreement amends and restates the Borrowers' current \$100.0 million credit facility with the Lender and provides that the Lender shall make available to the Borrowers up to \$150.0 million of term debt (the "Term Loan"). The Credit Agreement will expire by its terms on January 5, 2011. All borrowings under the Credit Agreement will bear interest at a per annum rate equal to either (i) the LIBOR rate plus an adjustable applicable margin of between 1.75% and 3.50% or (ii) Wells Fargo's prime rate plus an adjustable applicable margin of between 0.0% and 2.0%, at the election of the Borrowers, subject to specified restrictions. All borrowings under the Term Loan must be repaid in quarterly installments commencing on April 1, 2007. In the event Borrowers terminate the Credit Agreement prior to its expiration or make certain prepayments, the Borrowers will be required to pay the Lender a termination or prepayment fee equal to 1% of the maximum credit amount in the event of termination or 1% of the prepayment amount in the event of prepayments, subject to specified exceptions.

The Credit Agreement contains customary affirmative and negative covenants for credit facilities of this type, including limitations on the Borrowers with respect to indebtedness, liens, investments, distributions, mergers and acquisitions, dispositions of assets and transactions with affiliates of the Borrowers. The Credit Agreement also includes financial covenants including minimum EBITDA, minimum liquidity, minimum recurring revenue (which includes outsourced business services and software maintenance revenue—see Note 16) and maximum capital expenditures.

The Company has initially drawn down \$75.0 million from the Term Loan to help fund its acquisition of QCSI. The Company expects to use the remaining available credit for general working capital purposes. All borrowings under the Term Loan must be repaid in quarterly installments commencing on July 1, 2007 through January 5, 2010 in amounts equal to the amount outstanding under the term loan on June 30, 2007, divided by 28. Under the Credit Agreement, the Borrowers have granted the Lender a security interest in all of the assets of the Borrowers.

**MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS
AND ISSUER PURCHASES OF EQUITY SECURITIES**

Our common stock has been traded on the NASDAQ National Market under the symbol “TZIX” since October 8, 1999.

The following table shows the high and low sales prices of our common stock as reported on the NASDAQ Stock Market for the periods indicated:

QUARTERS ENDED	HIGH	LOW
December 31, 2006	\$18.95	\$14.25
September 30, 2006	\$15.53	\$11.89
June 30, 2006	\$17.68	\$12.69
March 31, 2006	\$19.74	\$16.11
December 31, 2005	\$17.49	\$12.77
September 30, 2005	\$17.34	\$13.61
June 30, 2005	\$14.40	\$ 8.60
March 31, 2005	\$ 9.94	\$ 8.00

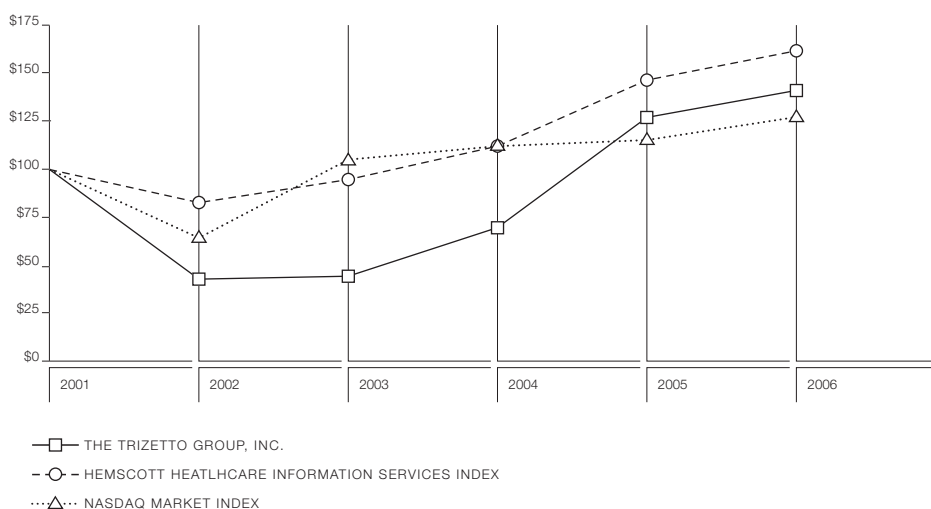
As of March 13, 2007, there were 214 holders of record based on the records of our transfer agent.

We have never paid cash dividends on our common stock. We currently anticipate that we will retain earnings, if any, to support operations and to finance the growth and development of our business and do not anticipate paying cash dividends in the foreseeable future. The payment of cash dividends by us is restricted by our current bank credit facility, which contains a restriction prohibiting us from paying any cash dividends without the bank’s prior approval.

STOCK PERFORMANCE GRAPH

The graph below compares the five-year cumulative total stockholder return on our common stock for the five-year period ended December 31, 2006, with the cumulative total return of (a) the Nasdaq Market Index and (b) Hemscott Industry Group Index 825—Healthcare Information Services over the same period. The graph assumes \$100.00 invested at the beginning of the period in our common stock and the stocks represented by the above named indices and the reinvestment of all dividends; we have paid no dividends on our common stock. The performance graph is not necessarily an indicator of future performance. This information has been provided by Hemscott, Inc.

COMPARISON OF FIVE-YEAR CUMULATIVE TOTAL RETURNS TO STOCKHOLDERS



COMPANY/INDEX/MARKET	Year Ended December 31,					
	2001	2002	2003	2004	2005	2006
The TriZetto Group, Inc.	\$100.00	\$46.80	\$49.16	\$72.41	\$129.50	\$140.02
Hemscott Healthcare Information Services Index	100.00	81.29	96.61	113.36	149.70	160.74
Nasdaq Market Index	100.00	69.75	104.88	113.70	116.19	128.12

DEFINITION AND RECONCILIATION OF NON-GAAP FINANCIAL MEASURES

BOOKINGS

Contract bookings comprise a mix of current and future period revenue and represent the expected minimum total revenue to be generated under each contract.

BACKLOG

Total backlog is defined as revenue we expect to generate in future periods from existing customer contracts. Our 12-month backlog is defined as the revenue we expect to generate from existing customer contracts over the next 12 months. Most of the revenue in our backlog is derived from multi-year recurring revenue contracts (including software hosting, business process outsourcing, IT outsourcing, and software maintenance). For purposes of calculating our backlog and based upon our previous experience, we assume software maintenance contracts will be renewed for a period of up to seven years. We classify revenue from software license and consulting contracts as non-recurring. Consulting revenue is included in the backlog when the revenue from such consulting contract will be recognized over a period exceeding 12 months.

ADJUSTED EBITDA

In this report we use the non-GAAP financial measure, "Adjusted EBITDA," as originally defined in our press release dated October 25, 2005. We define Adjusted EBITDA as net income, excluding the impact of interest expense, income taxes, depreciation and amortization, charges for legal settlements, charges for facility closures and asset impairment, stock-based compensation expense and charges for expected future loss on contracts. We use Adjusted EBITDA to provide meaningful supplemental information regarding our operating performance and profitability by excluding certain expenses and expenditures that may not be indicative of our core business operating results. Because our capital structure, effective income tax rates, capitalized asset values and equity-based compensation levels are different than those of other companies, we believe that Adjusted EBITDA facilitates comparisons of our results of operations with those of other companies. Further, we believe that Adjusted EBITDA, which excludes certain factors which are not indicative of ongoing operations such as charges for legal settlements, facility closures, asset impairment and future loss on contracts, can assist management and investors in assessing the financial operating performance and underlying strength of our core business. We use Adjusted EBITDA in our cash bonus program to evaluate management's performance for compensation purposes, and we have agreed with our lender to maintain levels of an adjusted form of EBITDA as specified in financial covenants to our secured debt facility.

In the third quarter of 2006, we entered into a settlement agreement with McKesson Information Solutions LLC ("McKesson") to settle a lawsuit. As part of the settlement agreement, TriZetto agreed to pay McKesson a one-time royalty fee of \$15 million. We excluded this one-time charge from Adjusted EBITDA as it was not indicative of our ongoing operations.

During the fourth quarter of 2003, we decided to wind-down our outsourcing services to physician group customers. In the second quarter of 2005, we executed termination agreements with our two remaining physician group customers. This resulted in the reversal of the remaining balance in our loss on contracts accrual of \$2.9 million. This amount was excluded from Adjusted EBITDA as it is not indicative of ongoing operations.

We also excluded from Adjusted EBITDA losses for facility closures and a gain from the sale of our credentialing and verification business. The losses for facility closures were approximately \$187,000 in the 2006 and approximately \$1.1 million in 2005. The charges reflected our remaining payment obligations under lease agreements for closed facilities. Because the facilities were non-performing, we excluded the charges from Adjusted EBITDA as they were not indicative of our ongoing operations. The gain from the sale of our credentialing and verification business was \$75,000, partially offsetting the losses for facility closures in 2006. We excluded this gain from Adjusted EBITDA as it related to a business we had decided to exit and therefore is not indicative of our ongoing operations.

Additionally, in 2006, we recognized a gain of \$180,000 from the sale of a domain name, which was eliminated from Adjusted EBITDA. We excluded this gain from Adjusted EBITDA as it related to a one-time sale of an asset and therefore is not indicative of our ongoing operations.

In December 2004, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") 123R, "Share-Based Payment." This statement requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS 123R, using the modified prospective method. Under this method, the provisions of SFAS 123R apply to all awards granted or modified after the date of adoption. Consistent with our definition noted above to exclude stock-based compensation expense, Adjusted EBITDA excludes the impact of the equity expense of SFAS 123R and other stock-based compensation expenses.

Adjusted EBITDA is not a recognized term under GAAP and should not be considered in isolation of, or as a substitute for, the information prepared and presented in accordance with GAAP. In addition, Adjusted EBITDA should not be considered as a measure of liquidity or free cash flow for management's discretionary use, as it excludes certain cash requirements such as interest expense, income taxes, costs to replace depreciated or amortized assets, costs arising from certain facility closures and losses on contracts. Because not all companies calculate Adjusted EBITDA identically, our definition of Adjusted EBITDA may not be comparable to similarly titled measures of other companies. We compensate for these limitations by relying primarily on our GAAP results and use Adjusted EBITDA supplementally.

RECONCILIATION OF HISTORICAL ADJUSTED EBITDA

RECONCILIATION OF HISTORICAL ADJUSTED EBITDA TO NET INCOME

The following schedule provides a reconciliation of GAAP Net income to Adjusted EBITDA for the periods indicated (in thousands):

YEARS ENDED DECEMBER 31	2002	2003	2004	2005	2006
Net (loss) income	\$(148,364)	\$(27,475)	\$ 8,458	\$22,021	\$15,115
Interest (income) expense, net	(130)	1,035	786	(40)	(481)
Provision for income taxes	250	1,124	1,101	412	2,494
Operating depreciation and amortization	12,794	18,407	21,106	23,282	22,237
Amortization of acquired technology	18,335	7,120	440	660	4,120
Amortization of acquired other intangible assets	9,692	3,788	3,804	2,225	867
Stock-based compensation	2,953	1,839	594	1,397	7,426
Legal settlement	—	—	—	—	15,000
Loss on (recovery from) contracts	—	14,951	(1,353)	(2,877)	—
Restructuring, impairment and other charges	651	3,769	870	1,111	112
Impairment of goodwill and other intangible assets	131,019	—	—	—	—
Other income	—	—	—	—	(180)
Adjusted EBITDA	\$ 27,200	\$ 24,558	\$35,806	\$48,191	\$66,710

Corporate and Stockholder Information

Board of Directors

Jeffrey H. Margolis

Chairman and Chief Executive Officer,
The TriZetto Group, Inc.

Paul F. LeFort ^(A) ^(C)

Lead Independent Director
Former Chief Information Officer,
UnitedHealth Group Incorporated

Nancy H. Handel ^(C) ^(N)

Retired Chief Financial Officer,
Applied Materials, Inc.

Thomas B. Johnson ^(A - Chair)

Former Chairman and
Chief Executive Officer,
CNA Health Partners, Inc.

L. William Krause ^(C - Chair)

Retired Chairman, Chief Executive
Officer and President,
3Com Corporation

Donald J. Lothrop ^(N - Chair)

Managing Member,
New Vista Partners, LLC

Jerry P. Widman ^(A) ^(C)

Former Chief Financial Officer,
Ascension Health

^(A) Audit Committee

^(C) Compensation Committee

^(N) Nominating and Corporate
Governance Committee

Executive Officers

Jeffrey H. Margolis

Chairman and Chief Executive Officer

Kathleen Earley

President and Chief Operating Officer

Anthony Bellomo

Executive Vice President,
Product Management

Patricia E. Gorman

Chief Information Officer

James C. Malone

Executive Vice President and
Chief Financial Officer

Philip J. Tamminga

Executive Vice President,
Development and Professional Services

John G. Jordan

Senior Vice President, Sales and
Account Management

Alan M. Ross

Senior Vice President,
Human Capital Management

Daniel J. Spirek

Senior Vice President,
Chief Solutions Officer

James J. Sullivan

Senior Vice President,
General Counsel and Secretary

Mark M. Tomaino

Senior Vice President,
Corporate Development

Corporate Information

Corporate Office

The TriZetto Group, Inc.
567 San Nicolas Drive, Suite 360
Newport Beach, CA 92660
949-719-2200

Independent Registered Public Accounting Firm

Ernst & Young LLP
18111 Von Karman Avenue
Suite 1000
Irvine, CA 92612

Corporate Counsel

Stradling Yocca Carlson & Rauth
660 Newport Center Drive, Suite 1600
Newport Beach, CA 92660

Product Information

Information about TriZetto's
software products, services and
consulting is available on our
website at www.trizetto.com
or by contacting our Marketing
Department at 800-569-1222.

Stockholder Information

Fiscal Year End

December 31

Common Stock

The company's common shares are
quoted on the Nasdaq Stock Market
under the symbol TZIX.

Transfer Agent and Registrar

Questions regarding stock transfer
requirements or requests for change
of address should be directed to:
U.S. Stock Transfer Corporation
1745 Gardena Avenue
Glendale, CA 91204
818-502-1404

Reports to the SEC

Reports filed with the SEC on Forms
10-Q and 10-K are available at no
charge upon request to our Investor
Relations Department at the Corporate
Office address or telephone number
listed on the back cover. These reports
are also available electronically on the
company's website, www.trizetto.com,
as well as from the SEC's website at
www.sec.gov.

Company News

TriZetto press releases and additional
company information are available
on our web site at www.trizetto.com.
You may also register there to be
notified by e-mail of upcoming news
and announcements, including
quarterly results.

Investor and Media Contact

Brad Samson, 949-719-2220
brad.samson@trizetto.com

IMPORTANT NOTICE REGARDING FORWARD-LOOKING STATEMENTS: This report contains forward-looking statements that involve risks and uncertainties. The forward-looking statements are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements may include statements about future revenue, profits, cash flows and financial results, the market for TriZetto's services, future service offerings, industry trends, client and partner relationships, TriZetto's operational capabilities, future financial structure, uses of cash, the closing of and anticipated dilution or accretion of acquisitions, and other acquisitions or proposed transactions. Actual results may differ materially from those stated in any forward-looking statements based on a number of factors, including the ability of TriZetto to successfully integrate the businesses of TriZetto and its acquisitions or partners; the contributions of acquisitions to TriZetto's operating results; the effectiveness of TriZetto's implementation of its business plan, the market's acceptance of TriZetto's new and existing products and services, the timing of new bookings, risks associated with management of growth, reliance on third parties to supply key components of TriZetto's services, attraction and retention of employees, variability of quarterly operating results, competitive factors, other risks associated with acquisitions, changes in demand for third party products or solutions which form the basis of TriZetto's service and product offerings, financial stability of TriZetto's customers, the ability of TriZetto to meet its contractual obligations to customers, including service level and disaster recovery commitments, changes in government laws and regulations; and risks associated with rapidly changing technology, as well as the other risks identified in TriZetto's SEC filings, including, but not limited to, its annual report on Form 10-K and quarterly reports on Form 10-Q, copies of which may be obtained by contacting TriZetto's Investor Relations department at 949-719-2225 or at TriZetto's web site at www.trizetto.com. All information in this release is as of April 30, 2007. TriZetto undertakes no duty to update any forward-looking statement to conform the statement to actual results or changes in the company's expectations.

The TriZetto Group, Inc.
567 San Nicolas Drive, Suite 360
Newport Beach, CA 92660

www.trizetto.com
Telephone 949-719-2200

Our Mission: TriZetto is distinctly focused on accelerating the ability of healthcare payers to lead the industry's transformation by providing premier information technology solutions that enhance our customers' revenue growth, drive their administrative efficiency, and improve the cost and quality of care for their members.