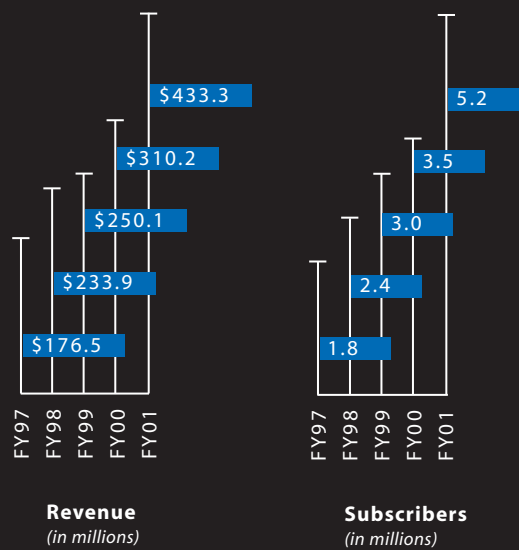


# S T A Y I N G <sup>power</sup> 20

CHECKFREE CORPORATION

ANNUAL REPORT FY01

financial\_highlights



(in thousands, except per-share data)			
year ended June 30	1999	2000	2001
Statement of Operations Data			
Total revenues	\$ 250,131	\$ 310,195	\$ 433,320
Net income (loss)	\$ 10,457	\$ (32,320)	\$ (363,135)
Net income (loss) per common equivalent shares outstanding	\$ 0.18	\$ (0.61)	\$ (4.49)
Weighted average common and equivalent shares outstanding	56,529	53,367	80,863
Balance Sheet Data			
Working capital	\$ 24,245	\$ 178,761	\$ 142,661
Total assets	\$ 252,761	\$ 713,114	\$ 2,183,953
Total stockholders' equity	\$ 186,903	\$ 445,894	\$ 1,732,186
Net book value per share outstanding	\$ 3.61	\$ 7.63	\$ 19.93

# LEADING power<sup>20</sup>

**In 1981, we started CheckFree with a simple idea.**

**A way to make bill paying easier.**

Today we've built upon that idea to become  
the leader in shaping the world's most  
complex financial electronic commerce systems.

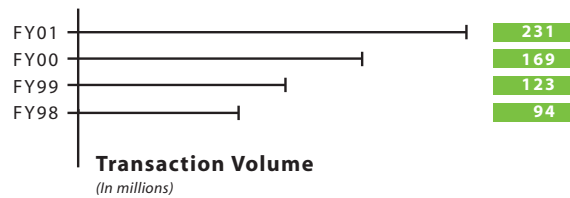
Together with financial institutions, investment  
organizations, global corporations and  
everyday consumers, we are continuing  
the tradition of **innovation, quality** and  
**convenience** that has defined our market  
leadership for more than twenty years.

CHECKFREE CORPORATION

ANNUAL REPORT FY01

# Innovation makes new markets.

With the introduction of the first e-bill in 1997, the future of financial electronic commerce has been altered forever.



### Fellow Shareholders:

Fiscal 2001 marked CheckFree's 20th year of providing financial electronic commerce services and software. In 1981 we weren't thinking 20 years out; our mission was simply to make financial transactions easier. Our first objective was to deliver an easier, more convenient, paperless way to pay bills. We built the leading electronic bill payment system, and in 1997 we introduced the first end-to-end, fully electronic billing and payment system, pioneering a new industry.

Today each of our three divisions — Electronic Commerce, Software and Investment Services — leads the market it serves. While they differ in some respects — the products and services they offer, the maturity of the markets they serve — they each advance the core of our original vision in 1981: making financial transactions easier.

### 2001: Integrating Assets, Advancing Convenience

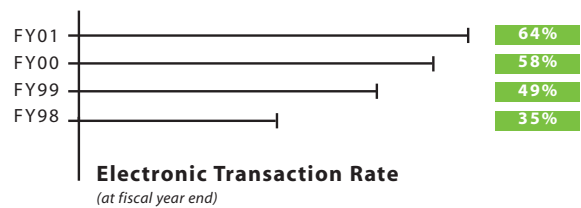
Fiscal 2001 was a year of very solid execution. We continued to advance key metrics, fortifying our leadership with excellence in quality, continuous innovation, strong partnerships and unstoppable commitment to making financial electronic commerce easier. At the same time, we continued to grow revenue and margins in each division at targeted rates.

The most critical strategic objective we achieved was integrating the assets, people and technology from our acquisitions of BlueGill Technologies and TransPoint, and from our strategic alliance with Bank of America. Our intense focus on integration efforts in fiscal 2001 has set the stage for leveraging these assets to drive efficiency and bottom-line improvements in fiscal 2002.

From a market perspective, we continued to set the bar for operational performance, and to advance consumer convenience, again raising the level at which others will have to compete. Our Sigma Challenge program delivered quality improvements that translate to the lowest inquiry rates in the industry. Consumer convenience improvements such as e-bill over e-mail and e-payments over e-mail tie the ease of use that consumers want with the security that they demand. Our Investment Services and Software divisions each advanced the level at which others will have to compete. Notably, CheckFree i-Solutions made numerous advancements to its i-Series e-billing and e-statement software, extending again the lead it holds over all e-billing solution providers in the span of functionality, scalability and flexibility afforded to billers. In short: we lead our markets.

### 2002: Execution, Advancement, Profitability

In 2001 we demonstrated efficiencies, best practices and economies of scale far beyond our competitors. In 2002 we'll focus on using these assets to drive an increasing percentage of our top-line revenue growth to the bottom line. Service quality, customer satisfaction and operating efficiency will continue to be hallmarks of our business. Continued gains in these areas will drive profitability — without sacrificing continued investments in innovation in early stage markets that will fuel our long-term growth.



Innovations will continue to focus on quality, convenience and security, further defining the direction of the industry. Making enrolling in and using e-billing and payment services easier — both for consumers and businesses — will continue to be our priority. Working with Consumer Service Providers and billers to educate consumers and motivate them to enroll will be core to our market development efforts. As subscriber volumes and transactions increase, we will leverage these efficiencies in a number of ways, including fueling more innovations. Our focus will be on extending our core financial electronic commerce assets and expertise — and our ability to internetwork different systems with high quality reliability — to embrace broader opportunities.

The Dividends of Internetworking

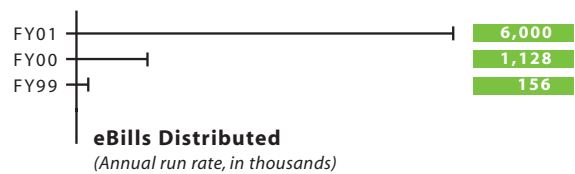
A core competency in internetworking systems — and in building and maintaining the infrastructure required — erects a formidable obstacle for existing competitors and a very high cost of entry for newcomers. This is because the infrastructure must enable a variety of networks to exchange transactions, or interoperate — a complex task that requires technology, process expertise, and people with exceptional domain knowledge. This competency is the cornerstone of CheckFree’s competitive advantage today, and will be the foundation for our continued market leadership.

Here is a simple example that illustrates the nature of an internetworking infrastructure: Remittance transactions we handle today can take a variety of routes, such as a direct connection from CheckFree to the merchant, a proprietary EDI connection managed by the merchant, Visa’s ePay, MasterCard’s RPS or a check-disbursement system for paper remittance if none of these electronic paths is available. Our internetworking infrastructure carries intelligence about the transaction and provides a decision-making engine to select the best of these courses. We analyze the payment requirements, weigh criteria such as cost, risk and timeliness, recognize changes such as mergers of merchants or financial institutions and choose the best remittance route.

Internetworking Requires Interoperating

Although this example covers only a relatively simple process among all those that CheckFree handles, it illustrates why internetworking requires exchanges among disparate legacy systems. This is why CheckFree is one of the companies working to create systems that can interoperate flexibly among differing systems and standards — and that can interoperate reliably and predictably where no standards are yet defined.

Expanding profitability on the Internet requires interoperability. Interoperability requires internetworking disparate systems so that it becomes progressively easier for businesses to connect with consumers and other businesses with minimal friction. CheckFree’s focus for fiscal 2002 will be on removing this friction by advancing the capabilities of our internetworking infrastructure. Our goal will be to enable financial transactions to interoperate more efficiently, reliably and securely on the expanding “commerce grid” that signifies the authentic potential of the Internet.



Interoperating extends internally as well. We are increasing the rate of innovation and advancing our service infrastructure in Investment Services as we continue to build this valuable business. We intend to broaden our markets by providing more services to our clients and increasing the scope of our market reach by expanding upon our existing systems.

Continuing to Raise the Competitive Bar

The next 20 years will be about continual reinvention. They won't be different from the last 20 years in that respect — we've been incubating ideas, pioneering markets and reinventing our Company since 1981.

In fiscal 2002, we're taking our heritage of continuous reinvention to a new level. We are expanding our Sigma quality programs to reach all business units, all operational areas, and all touch points with the customer. These include improving customer satisfaction, self-care capabilities, responsiveness to inquiries and the efficiency of all our transaction service systems.

An important initiative for fiscal 2002 is CheckFree Peak Performance. Its premise: Every CheckFree associate — all 3,400 of us — will be held accountable for performance and innovations that reach the bottom line. Innovation goes beyond creating new technologies. It means finding new and better ways to do everything, no matter how large or small the task. It means improving not only financial performance, but improving customer satisfaction ratings, perceptions and experiences of convenience, and the delivery of market-defining quality, reliability and security. These day-to-day innovations will build upon each other to deliver superior results. Superior results will translate to greater shareholder value, and to an increasingly stronger leadership position.

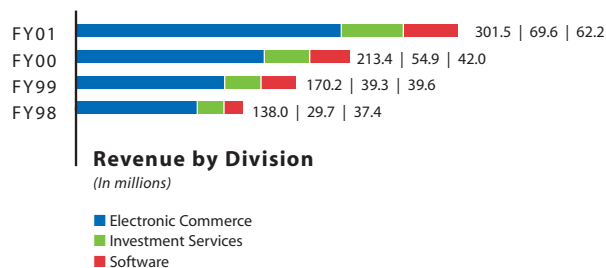
Pete Kight

Chairman and CEO

# Quality builds loyalty.

Quality is the foundation of a positive customer experience, essential to the growth of a successful company.





We had another very successful year in fiscal 2001 as we continued to set the standard for leadership in our industries. Our Electronic Commerce, Software and Investment Services divisions each performed well last year and strengthened our competitive advantage in each of the markets we serve.

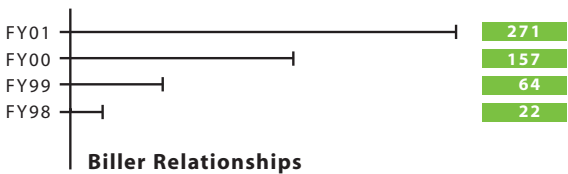
In fiscal 2002 we will continue to enhance our market position by driving improvements in quality and product functionality, and by directing more of our revenue growth to the bottom line. Once again, we will focus heavily on executing our business plans with precision.

### Leading By Any Measure

The test of a true market leader is whether its contributions advance the industry. In fiscal 2001, each of our divisions led not only in mass but also in innovation and execution. Below are the benchmarks that set the stage for continued strong performance in fiscal 2002.

#### Electronic Commerce Leadership Benchmarks

- *Financial performance.* Fiscal 2001 revenue was \$301.5 million, up 41% over fiscal 2000. The division's operating loss was \$13.1 million, an improvement from the \$18.2 million loss in fiscal 2000. As investments improving quality, efficiency and scale continue to pay off, we expect to drive even more revenue growth to the bottom line in fiscal 2002.
- *EBP distribution sites.* Two years ago, one financial institution offered full electronic billing and payment services through CheckFree; by the end of fiscal 2001, more than 300 sites enabled consumers to view and pay bills online.
- *Subscribers.* The number of consumers subscribing to electronic billing and payment increased to 5.2 million, a 49% gain from last year. This figure includes 300,000 subscribers added through Bank of America's EBP operations. Net of these subscribers, growth for the year was 40%.
- *Bill content.* The number of billers on distribution contracts has soared from 22 in fiscal 1998 to 271 this year, with 179 different e-bills already available to consumers. These figures compare to 157 agreements and 93 available bills at the end of fiscal 2000.
- *Bills distributed.* We distributed nearly 500,000 bills in June 2001, up from 94,000 in June 2000 and 13,000 in June 1999. This figure equates to a run rate of nearly six million bills distributed per year.
- *End-to-end electronic transactions.* We now handle 64% of payments electronically, up sharply from 49% two years ago. This rate positively impacts operating margins through lower exception rates, customer inquiry rates and processing costs, and far outstrips the electronic rates competitors deliver.
- *Transaction volumes.* We processed more than 22 million transactions in June — more than double the volumes of the next two competitors combined. In fiscal 2001, we processed 231 million transactions, up from 169 million in fiscal 2000 — a gain of 37%.
- *Quality.* We are proud to deliver the highest quality in the industry. An August 2001 report from analyst firm Tower Group confirms that CheckFree's error rate — about .003 — is dramatically lower than that of competitors.

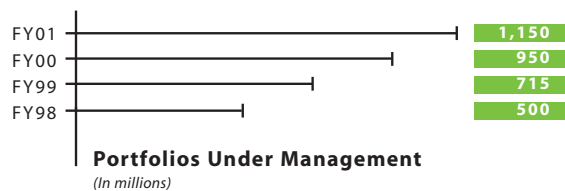


Software Leadership Benchmarks

- *Financial performance.* Fiscal 2001 revenue was \$62.2 million, up 48% over fiscal 2000. Operating income was \$800,000, down from \$10.5 million in fiscal 2000. This change reflects planned investments in integrating BlueGill Technologies to create CheckFree i-Solutions, which is now the leading provider of e-billing and e-statement software for business-to-consumer and business-to-business applications.
- *Customer relationships.* Each of the three units within our Software division leads in both the number and stature of its customer relationships. CheckFree i-Solutions enjoys e-bill distribution relationships with 271 billers. More than 100 companies use this unit's e-billing and e-statement software — significantly more than any competitor. In addition, we now provide full hosting services — either in a biller direct or bill distribution model — for 80 billers ...far more than any other competitor.
- *CheckFree ACH Solutions* provides automated clearinghouse processing for 40 of the top 50 ACH originators, and to 120 customers overall. This unit's software and services handle 85% of all ACH transactions enabling e-payments.
- *CheckFree Financial and Compliance Solutions* provides software and services to the top 30 bank holding companies, 7 of the top 10 life insurance companies and 7 of the top 10 health insurance companies. With 600 customers overall, this unit is the dominant supplier of reconciliation and compliance solutions.
- *Options for flexibility.* CheckFree i-Solutions leads the industry in delivering choice in e-billing and e-statement solutions. With the launch of i-Series Select — value-priced vertical market solutions — and expanded hosting options, i-Solutions flexibly meets biller needs. Unique in the industry, all software purchases include the ability to distribute bills through our unparalleled distribution network. Of course, billers also have the option of deploying a biller direct site and moving to bill distribution later. Billers also can choose to have CheckFree host and manage their e-billing and e-statement solutions, whether or not they purchase software.
- *Global reach.* Each unit in CheckFree's Software division enjoys a global reputation and sales success. Worldwide, the CheckFree name in software means quality, innovation, performance and value.

Investment Services Leadership Benchmarks

- *Financial Performance.* Fiscal 2001 revenue was \$69.6 million, up 27% over fiscal 2000. Operating income for this division was \$20.3 million, up 29% over fiscal 2000.
- *Infrastructure.* Protecting Investment Services' position as the leading provider of outsourced portfolio management solutions is a highly scalable, proven internetworking infrastructure that comprises more than 1,100 direct interfaces into 89 business partners.
- *Software and services.* With the acquisition of The Mobius Group in fiscal 1999, Investment Services expanded its leadership to financial planning software and money manager databases. Today, Investment Services continues to leverage its position as the leading provider of portfolio management solutions for institutional investment houses, financial planning software for the independent planner market, and money manager database information.



- *Customer relationships.* More than 250 investment firms — including the industry’s largest and most well respected — trust CheckFree Investment Services to manage more than 1.15 million portfolios and \$500 million in assets. In addition, more than 2,000 investment consultants and financial planners use this division’s software and services.
- *Domain expertise.* Flawlessly navigating the constantly changing landscape of portfolio accounting, tax-efficient trading and performance reporting requires the expertise of professionals well-versed in the nuances of investing. CheckFree Investment Services leads the industry in this dimension, with 300 highly skilled investment industry specialists.

### Driving Leadership to the Bottom Line

Fiscal 2002 will be another year of solid business plan execution. Each division, department, function and individual has been assigned a role in translating our excellence to profit. Each employee will monitor, measure, report and improve key operating metrics throughout the year. And achieving our goals for those metrics will help increase CheckFree’s competitive advantage.

In Electronic Commerce we will continue to assist our partners with marketing programs to spur subscriber growth and e-bill usage. We will continue to deliver refinements that make access, enrollment and e-bill activation easier for consumers and implementations easier for our customers. We will work to enable Consumer Service Providers with our latest WebPay technology, which integrates end-to-end EBP with e-mail billing and payment. This technology enables consumers to make and manage all electronic payments — whether for bills or other purposes — under a trusted brand. And we will continue to improve quality while at the same time lower unit cost.

In Software, we will enhance i-Series to enable billers to offer e-bills over e-mail directly in addition to through a Consumer Service Provider. We will also continue to extend our business-to-business e-billing and e-statement capabilities. Our ACH and CFACS units also will continue to extend both services and market reach.

Investment Services will continue to leverage its strong market position to drive revenue growth and greater profits. We will enhance customer relationships across our product offerings, extending software from the financial planner market to the institutional market and services from the institutional market to the financial planner market.

We are fortunate for, and respectful of, our continued leadership through 20 years of competition. Our successes will continue to inspire new challengers. We welcome the contest because it spurs us to greater performance. That, in turn, delivers greater efficiency, scalability and quality for our partners and their customers. And that leads to greater returns for our shareholders.

Pete Sinisgalli

President and Chief Operating Officer

# Convenience shifts behavior.

Genuine change means making something so easy and accessible that once experienced, a momentum is created that can't be stopped.

#### FY 2001

- Successfully integrates assets from acquisitions of BlueGill Technologies and TransPoint and strategic alliance with Bank of America
- Grows subscribers from 3.5 million to 5.2 million
- Attains Sigma Quality goal of 99.9% systems availability and transaction processing quality
- Introduces “Next Generation” e-bill and e-payment over e-mail capabilities

#### FY 2000

- Advances market leadership position through acquisitions of BlueGill Technologies and TransPoint, and through strategic alliance with Bank of America
- Achieves potential reach of over 100 million subscribers through multi-year contracts with banks, brokerages, portals and providers of personal financial management software
- Launches Genesis 2000 platform for secure transactions built to serve one-third of the U.S. population

#### FY 1999

- Transition in growth from CheckFree powered “home banking and bill payment services” to CheckFree powered “Internet-based electronic billing and payment services”
- CheckFree Investment Services purchases Mobius Group
- Billers begin signing agreements to distribute e-bills — 64 signed at end of fiscal year

#### FY 1998

- Significant gains in enabling trusted financial services providers, adding 48 new relationships
- Cements early lead in electronic bill presentment market by signing 12 new billers, including AT&T which sends the most bills per month
- Selected by Intuit as the preferred provider of bill presentment and payment through Quicken software and Quicken.com Web site

#### FY 1997

- CheckFree delivers the first “live” e-bill
- Subscriber base grows to 1.3 million
- Becomes the transaction processor for all leading software interfaces
- Customers can now receive and pay bills at consolidated financial services Web sites
- e-bill is selected for display at the Smithsonian Institute as having a “profound, positive and demonstrable impact on society...”
- Acquires Intuit Services Corporation

#### FY 1996

- Shifts strategy away from direct consumer delivery to delivery exclusively through financial institutions
- Acquires Servantis Systems, Inc., Interactive Solutions Corp. and Security APL
- Becomes home banking and bill payment transaction-processing provider for seven of the top 10 financial institutions in the country

#### FY 1995

- Initial Public Offering on Nasdaq
- Internet hits critical mass — stage is set for growth
- Receives U.S. patent on electronic bill payment system

#### FY 1994

- Strategic agreement with Fiserv, Inc. enables more than 3,000 financial institutions worldwide (representing 50 million consumer and business accounts) to use CheckFree’s remote access electronic banking

#### FY 1993

- After-tax profits exceed one million dollars
- Launch of MasterBanking alliance with MasterCard gives CheckFree national exposure
- Chemical Bank leaves the payment processing business, transferring its 35,000 customers to MasterBanking

#### FY 1992

- CheckFree’s electronic bill payment capability is now accessible from several popular money management programs on both Macintosh and PC platforms

#### FY 1991

- Launches first touch-tone telephone bill payment product

#### FY 1990

- Introduces Customer Service Tracking System and Customer Activity Tracking System

#### FY 1989

- Creates alliances with both leading providers of personal financial management software — Managing Your Money and Quicken

#### FY 1988

- Begins processing American Express and Discover Card payments
- Launches first electronic bill payment product for consumers
- Grows to 80 employees

#### FY 1985

- Payment processing grows from once a month to daily
- Creates Change Processing Unit
- Phone Change Department starts taking changes over the phone for a fee
- Offers automated reclears for items being returned for insufficient funds.

#### FY 1984

- Signs agreement with Compuserv to become the first interactive service customer

#### FY 1983

- More than 150 health clubs use Electronic Funds Transfer processing
- Aegis Systems is renamed CheckFree Systems

#### FY 1982

- Targets health club market for electronic payment of monthly membership dues

#### FY 1981

- Aegis Systems is founded by Pete Kight in his grandmother’s basement near Columbus, Ohio, with the goal of simplifying recurring payments. The first customers were three apartment complexes collecting rent through Electronic Funds Transfer.

selected\_financial\_data

The selected consolidated financial data for the years ended June 30, 1999, 2000 and 2001 have been derived from the Company's financial statements included elsewhere in this Annual Report, which have been audited by Deloitte and Touche, LLP, independent certified public accountants, whose report thereon is also included elsewhere in this Annual Report. The selected consolidated financial data for the years ended December 31, 1997 and 1998 have been derived from audited financial statements of the Company which are not included in this Annual Report. The selected consolidated financial data set forth below should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and Notes thereto elsewhere in this Annual Report. The earnings per share amounts for fiscal year 1997 have been restated to comply with Statement of Financial Accounting Standards No. 128 "Earnings per Share" (SFAS 128) as required. For further discussion of earnings per share and the impact of SFAS 128, see Note 1 to the consolidated financial statements. The financial information for the periods presented below includes all adjustments necessary for a fair presentation of results of operations.

Statement of Operations:	
Revenues:	
	Processing, servicing and merchant discount
	License fees
	Maintenance fees
	Other
	Total revenues
Expenses:	
	Cost of processing, servicing and support
	Research and development
	Sales and marketing
	General and administrative
	Depreciation and amortization
	In-process research and development
	Charge for stock warrants
	Exclusivity amortization
	Total expenses
	Net gain on dispositions of assets
	Loss from operations
Interest:	
	Income
	Expense
	Loss on investments
	Loss before income tax
	Income tax benefit
	Net income (loss)
Diluted income (loss) per common share	
Equivalent number of shares outstanding	
Balance Sheet Data:	
	Working capital
	Total assets
	Long-term obligations, less current portion
	Total stockholders' equity

Year ended June 30,				
1997	1998	1999	2000	2001
(In thousands, except per-share data)				
\$ 104,522	\$ 159,255	\$ 201,059	\$ 261,621	\$ 362,051
33,088	28,952	15,975	16,818	30,180
22,567	25,848	17,746	18,752	21,332
16,268	19,809	15,351	13,004	19,757
176,445	233,864	250,131	310,195	433,320
102,721	129,924	146,704	182,540	255,528
32,869	36,265	21,085	35,631	55,621
32,670	28,839	32,354	44,782	90,283
18,707	20,677	31,466	40,931	50,474
24,919	24,999	24,630	42,830	427,495
140,000	719	2,201	6,900	18,600
-	32,827	-	-	-
5,958	2,963	-	-	-
357,844	277,213	258,440	353,614	898,001
6,250	36,173	4,576	-	-
(175,149)	(7,176)	(3,733)	(43,419)	(464,681)
2,153	3,464	2,799	7,689	15,415
(834)	(632)	(618)	(8,027)	(13,154)
-	-	-	-	(16,077)
(173,830)	(4,344)	(1,522)	(43,757)	(478,497)
(12,017)	(641)	(12,009)	(11,437)	(115,362)
\$ (161,813)	\$ (3,703)	\$ 10,457	\$ (32,320)	\$ (363,135)
\$ (3.44)	\$ (0.07)	\$ 0.18	\$ (0.61)	\$ (4.49)
46,988	55,087	56,529	53,367	80,863
\$ 20,002	\$ 78,238	\$ 24,245	\$ 178,761	\$ 142,661
223,836	250,112	252,761	713,114	2,183,953
8,401	6,467	3,882	173,236	176,541
148,644	183,854	186,903	445,894	1,732,186

## management s\_discussion\_and\_analysis

### *of Financial Condition and Results of Operations*

#### Overview

We are the leading provider of electronic billing and payment services. We operate our business through three independent but inter-related divisions:

- Electronic Commerce;
- Investment Services; and
- Software.

Our Electronic Commerce business provides services that allow consumers to:

- receive electronic bills through the Internet;
- pay any bill — electronic or paper — to anyone; and
- perform customary banking transactions, including balance inquiries, transfers between accounts and on-line statement reconciliations.

We provide electronic billing and payment services for over 5.2 million consumers as of June 30, 2001. Our services reach hundreds of sources, either directly or through reseller relationships, including:

- 9 of the 10 largest U.S. banks;
- 8 of the top 10 U.S. brokerage firms;
- Internet portals;
- Internet-based banks;
- Internet financial sites like Quicken.com; and
- Personal financial management software like Quicken and Microsoft Money.

We have developed contracts with over 1,100 merchants nationwide that allow us to remit approximately 64% of all of our bill payments electronically. We processed over 22 million transactions for the month of June 2001 and, for the year ended June 30, 2001, we processed over 231 million transactions.

In March 1997, we introduced electronic billing — “E-Bill” — which enables merchants to deliver billing as well as marketing materials interactively to their customers over the Internet. In March 2001, we introduced the latest version of our electronic billing and payment products, “WebPay for Consumers” (or WebPay 3.2), which provides consumers with the ability to receive and pay e-bills over e-mail and to exchange money with each other using e-mail “invitations” to send or receive money. As of June 30, 2001, we have 173 billers in production and are delivering nearly 500,000 electronic bills monthly. Additional biller content became available in the fourth quarter of fiscal 2001 through our ability to deliver bills scraped from biller-direct sites, which added six national credit card bills to the 173 bills available through traditional electronic and billing payment services.

When a customer instructs us to pay a bill, we have the ability to process the payment either by electronic funds transfer, by paper check, or by draft drawn on the customer’s account. Our patented bill payment processing system in Norcross, Georgia determines the preferred method of payment based on a credit analysis of the customer, assessing the customer’s payment history, the amount of the bill to be paid and other relevant factors. If the results of the credit analysis are favorable, we will assume the risk of collection of the funds from the customer’s account, and if we have an electronic connection to the merchant, the remittance will be sent electronically, otherwise, it will be sent by check. If the results are not favorable, the remittance will be sent to the merchant by a draft drawn directly on the customer’s checking account. In an electronic remittance, the funds are transmitted electronically to the merchant with the customer’s account number included as an addenda record. For a paper draft, the customer’s name, address, and account number are printed on the face of the check. In addition, our processing system is able to aggregate multiple electronic and paper remittances due to merchants. Thus, if multiple payments are going to the same merchant on the same day, we may send one check for the sum of these payments and include a remittance statement that provides the customers’ names, addresses, account numbers, and payment amounts. Our strategy is to drive operational efficiency and improve profitability by increasing the percentage of transactions we process electronically. Since June 1998, we have increased our electronic payments ratio from 32% of total payments processed electronically to approximately 64% by June 2001.



We are also a leading provider of institutional portfolio management and information services and financial application software. Our Investment Services business offers portfolio accounting and performance measurement services to investment advisors, brokerage firms, banks and insurance companies and financial planning application software to financial planners. Our portfolio management system solution includes:

- data conversion;
- personnel training;
- trading system;
- graphical client reporting;
- performance measurement;
- technical network support and interface setup; and
- Depository Trust Corporation interfacing.

Our financial planning software applications include:

- retirement and estate planning modules;
- cash flow, tax and education planning modules;
- asset allocation module; and
- investment manager performance database system.

Our fee-based money manager clients are typically sponsors or managers of wrap money management products or traditional money managers, managing investments of institutions and high net worth individuals. Our portfolios under management have grown to over 1.1 million as of June 30, 2001.

Our Software businesses provide electronic commerce and financial applications software and services for businesses and financial institutions. We design, market, license and support the following software applications, among others:

#### **i-Solutions.**

The i-Solutions product line, which is a set of electronic billing software products developed for various industry segments, was added through our acquisition of BlueGill Technologies, Inc. in April 2000. These products allow billers to install and launch an electronic billing product, send e-mail notifications and present electronic bills through the Internet, and connect to a variety of bill aggregators and payment methods. Each product includes an electronic billing web site template that is unique to a specific industry segment. Using the template as a sample design of their Internet billing site, our customers spend less time developing and designing the look and feel of their Internet billing sites, which accelerates the product implementation process. Given the nature of the process we use to convert billing and/or statement information for use over the Internet, these products are equally marketable in international markets as well.

#### **Electronic Funds Transfer.**

Through our Paperless Entry Processing System Plus software, we offer an online, real-time system providing an operational interface for originating and receiving payments through the automated clearinghouse. The automated clearinghouse is a nationwide electronic clearing and settlement system that processes electronically originated credit and debit transfers among participating depository institutions. These electronic transactions are substitutes for paper checks and are typically used for recurring payments like direct deposit payroll payments and corporate payments to contractors and vendors, debit transfers that consumers make to pay insurance premiums, mortgages, loans and other bills, and business to business payments. You may obtain additional information on the automated clearinghouse at the Federal Reserve Commission's web site at <http://www.federalreserve.gov>. We do not maintain a direct connection with the automated clearinghouse, but rather, clear our electronic transactions through KeyBank, N.A., under the terms of an automated clearinghouse agreement.

## management s\_discussion\_and\_analysis

### *of Financial Condition and Results of Operations*

#### **Reconciliation.**

Through our ReconPlus software, we provide U.S. banks, international banks and corporate treasury operations with automated check and non-check reconciliations in high volume, multi-location environments. Some of the services provided by ReconPlus are automated deposit verification, consolidated bank account reconciliation and cash mobilization, immediate and accurate funds availability data and improved cash control.

#### **Other.**

We also provide software solutions such as regulatory compliance solutions for Form 1099 processing, safe box accounting and other applications.

During the fiscal year ended June 30, 2001, Electronic Commerce accounted for 70% of our revenues, Investment Services accounted for 16% of our revenues, and Software accounted for 14% of our revenues.

Our current business was developed through expansion of our core Electronic Commerce business and the acquisition of companies operating in similar or complementary businesses. Our major acquisitions include Servantis Systems Holdings, Inc. in February 1996, Security APL, Inc. in May 1996, Intuit Services Corporation in January 1997, Mobius Group, Inc. in March 1999, BlueGill Technologies, Inc. in April 2000, and MSFDC, L.L.C (TransPoint) in September 2000. In October 2000, we completed the strategic agreement we entered into with Bank of America in April 2000, under which we acquired certain of Bank of America's electronic billing and payment assets.

#### **Results of Operations**

The following table sets forth percentages of revenue represented by consolidated statements of operations data:

	Year ended June 30,		
	1999	2000	2001
Total revenues	100.0%	100.0%	100.0%
Expenses:			
Cost of processing, servicing and support	58.7	58.8	59.0
Research and development	8.4	11.5	12.8
Sales and marketing	12.9	14.4	20.8
General and administrative	12.6	13.2	11.7
Depreciation and amortization	9.8	13.8	98.7
In-process research and development	0.9	2.2	4.3
Total expenses	103.3	114.0	207.2
Net gain on dispositions of assets	1.8	-	-
Loss from operations	(1.5)	(14.0)	(107.2)
Interest:			
Income	1.1	0.2	3.6
Expense	(0.2)	(0.3)	(3.1)
Loss on investments	-	-	(3.7)
Loss before income taxes	(0.6)	(14.1)	(110.4)
Income tax benefit	(4.8)	(3.7)	(26.6)
Net income (loss)	4.2%	(10.4)%	(83.8)%

### Years Ended June 30, 2000 and 2001

*Revenues.* Our total revenue increased by 40%, from \$310.2 million for the year ended June 30, 2000 to \$433.3 million for the year ended June 30, 2001. The increase in revenue resulted from the acquisition of BlueGill in April 2000, the acquisition of TransPoint in September 2000, our strategic alliance with Bank of America in October 2000, and underlying revenue growth in the mid 20% range on a year over year basis. Overall revenue growth was driven primarily by an increase in subscribers in our Electronic Commerce business from 3.5 million at June 30, 2000 to just over 5.2 million at June 30, 2001, (0.3 million of which were added from Bank of America in October 2000) and an increase in portfolios managed in our Investment Services business from approximately 950,000 at June 30, 2000 to over 1.1 million at June 30, 2001, and incremental revenue from the BlueGill acquisition in our Software business. Refer to *Segment Information* later in this commentary for further information regarding results of our three business segments.

Our processing and servicing revenue increased by 38%, from \$261.6 million for the year ended June 30, 2000 to \$362.1 million for the year ended June 30, 2001. Our acquisition of TransPoint included a five-year strategic agreement with Microsoft and a five-year marketing agreement with First Data Corporation, each of which includes minimum quarterly revenue guarantees, as does our ten-year strategic agreement with Bank of America. In each case, actual subscriber revenue is below minimums as of June 30, 2001 and, as a result, overall subscriber based revenue growth will correlate less directly with subscriber growth until Bank of America-related and TransPoint-related subscribers generate sufficient revenue to exceed the quarterly minimums. Net of the incremental revenue from these agreements, underlying growth in processing and servicing revenue increased by 25% on a year over year basis. Growth in underlying processing and servicing revenue is driven by the previously mentioned growth in subscribers in our Electronic Commerce business and portfolios managed in our Investment Services business. Additionally, we now have 173 billers in production, including 30 that were added through the TransPoint acquisition, that presented nearly 500,000 bills in the month ended June 30, 2001. This has increased significantly from the 94 billers that presented about 94,000 bills in June 2000. In the month ended June 30, 2001, we processed over 22 million transactions, an increase of 38% compared to the 16 million transactions we processed in the month of June 2000. As mentioned in previous reports, we are offering a transaction based pricing model for our largest customers, and when combined with strategic agreements operating below minimum quarterly revenue thresholds, it will become increasingly difficult to correlate revenue solely to the number of subscribers, with transactions processed becoming an additional revenue indicator.

Our license fee revenue increased by 79%, from \$16.8 million for the year ended June 30, 2000 to \$30.2 million for the year ended June 30, 2001. Growth in license revenue is primarily attributable to new revenue resulting from our acquisition of BlueGill in April 2000. We achieved modest license revenue growth in the mid single digits from our more mature software product lines in the year ended June 30, 2001. Although we anticipate continued growth in license revenue, we expect current economic conditions to have a dampening effect on the rate of growth, at least in the near term.

Our maintenance revenue increased by 14%, from \$18.8 million for the year ended June 30, 2000 to \$21.3 million for the year ended June 30, 2001. We have achieved modest increases in maintenance revenue as a result of our acquisition of BlueGill. This line of billing software, however, is new and our related annual maintenance revenue is just now beginning to grow as customers complete their initial maintenance period and we begin to establish a renewal maintenance base. Additionally, since last year, we modified our maintenance revenue recognition policy. While we continue to recognize maintenance revenue ratably over the related service period, we now delay the onset of revenue recognition until cash is received, as opposed to estimating renewals in advance of cash receipt. Although this change caused some initial timing differences between the quarters ended September 30, 2000 and December 31, 2000, we do not expect any significant timing impact going forward. Customer retention rates in our more mature businesses continue to exceed 80% and price increases did not have a material impact on maintenance revenue in the year ended June 30, 2001.

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Our other revenue, which consists mostly of consulting fees, increased by 52%, from \$13.0 million for the year ended June 30, 2000 to \$19.8 million for the year ended June 30, 2001. Growth in other revenue is driven by increased consulting fees resulting from our BlueGill acquisition and increases related to biller implementations in our Electronic Commerce business. We placed 50 additional billers into production in the year ended June 30, 2001, bringing our total to 173.

*Cost of processing, servicing and support.* Our cost of processing, servicing and support was \$182.5 million, or 58.8% of total revenue for the year ended June 30, 2000, and was \$255.5 million, or 59.0% of total revenue for the year ended June 30, 2001. Cost of processing, servicing and support as a percentage of servicing only revenue (total revenue less license fees) was 62.2% for the year ended June 30, 2000, and 63.3% for the year ended June 30, 2001. As previously mentioned, we acquired TransPoint in September 2000 and the electronic billing and payment assets of Bank of America in October 2000. As a result of these transactions, we have supported two additional billing and payment processing platforms for much of the year ended June 30, 2001. Although expected, this has resulted in an increase in our cost of processing as a percentage of servicing only revenue as the acquired platforms are less efficient than our Genesis processing platform. We completed the conversion of TransPoint subscribers and billers to the Genesis processing platform in the quarter ended June 30, 2001. We completed the conversion of a portion of the Bank of America East operations in the quarter ended March 31, 2001, which includes subscribers in Georgia, Tennessee, Florida, Missouri, Arkansas, Iowa, Kansas, Arizona, New Mexico, North Carolina, South Carolina, Virginia, Maryland, and the District of Columbia. The remaining Bank of America subscribers, referred to as Bank of America West, are expected to be converted in the quarter ended December 31, 2001, with the remainder of legacy Bank of America subscribers converting from our Austin processing platform in the following quarter. Until the final conversion is completed, we will continue to experience higher than normal incremental processing costs, but at a decreasing rate, as new subscriber transactions are processed on the more efficient Genesis processing system. Somewhat masked by less efficient incremental costs resulting from TransPoint and Bank of America are underlying improvements in efficiency and processing quality within Genesis. Our ratio of electronic payments to total payments has improved from approximately 58% at June 30, 2000 to about 64% as of June 30, 2001. Electronic payments carry a significantly lower variable cost per unit than paper based transactions and are far less likely to result in a costly customer claim.

*Research and Development.* Our research and development costs were \$35.6 million, or 11.5% of total revenue for the year ended June 30, 2000, and were \$55.6 million, or 12.8% of total revenue for the year ended June 30, 2001. Adjusted for capitalized development costs of \$7.9 million for the year ended June 30, 2000 and \$4.9 million for the year ended June 30, 2001, our gross expenditures for research and development were \$43.5 million, or 14.0% of total revenue for the year ended June 30, 2000, and \$60.5 million, or 14.0% of total revenue for the year ended June 30, 2001. As a result of our acquisition of BlueGill, we added a large number of software development engineers and we have continued to invest heavily in our i-Solutions electronic billing software line of products. In addition, we released WebPay for Consumers, or WebPay 3.2, on our Genesis processing platform in our Electronic Commerce business in March 2001. This product offering provides consumers the ability to receive and pay e-bills over e-mail and to exchange money with each other using e-mail "invitations" to send or receive money. While we plan to continue to invest a significant portion of our revenue into research and development activities in all business segments in anticipation and support of revenue growth, quality enhancement and efficiency improvement opportunities, we expect that research and development will decline as a percentage of revenue in future periods.

*Sales and Marketing.* Our sales and marketing costs were \$44.8 million, or 14.4% of total revenue for the year ended June 30, 2000, and were \$90.3 million, or 20.8% of total revenue for the year ended June 30, 2001. The terms of our strategic agreement with Bank of America called for us to provide \$25.0 million at closing to help support an agreed upon two-year \$45.0 million marketing campaign by Bank of America. Because we cannot directly impact the specific nature, timing or extent of the use of the marketing funds, we expensed the entire \$25.0 million as a period cost in the quarter ended December 31, 2000. Net of this one-time charge, sales and marketing costs were \$65.3 million, or 15.0% of total revenue for the year ended June 30, 2001. We initiated specific marketing programs during fiscal 2001 to provide direct assistance to our Consumer Service Provider and biller customers in designing effective marketing and advertising campaigns geared toward accelerated consumer adoption of electronic billing and payment services. In addition to the marketing programs, the increase in our sales and marketing expenses are the result of increased sales and marketing staff resulting from the BlueGill acquisition, royalty costs resulting from the TransPoint acquisition, costs associated with the launch of the new i-Solutions product line, and further investments in core marketing and communications areas in support of the continued growth of the business.

*General and Administrative.* Our general and administrative expenses were \$40.9 million or 13.2% of total revenue for the year ended June 30, 2000, and were \$50.5 million, or 11.7% of total revenue for the year ended June 30, 2001. While we have incurred incremental facility and administrative staff costs in support of the BlueGill, TransPoint, and Bank of America transactions, and in support of the overall growth of the Company, our general and administrative costs as a percentage of revenue continue to decline due to the inherent leverage in our existing business model.

*Depreciation and Amortization.* Depreciation and amortization cost increased from \$42.8 million for the year ended June 30, 2000 to \$427.5 million for the year ended June 30, 2001. The significant increase is the direct result of amortization of intangible assets from the acquisitions of BlueGill and TransPoint, and the purchase of the electronic billing and payment assets from Bank of America. Net of intangible asset amortization from all acquisitions, our depreciation costs related solely to fixed assets, increased from \$24.3 million for the year ended June 30, 2000 to \$34.1 million for the year ended June 30, 2001. The increase in fixed asset related amortization is the result of fixed assets obtained in the BlueGill and TransPoint acquisitions, and increasing capital expenditures for data processing equipment, related software and new and improved facilities in support of the continued growth of the business.

*In-Process Research and Development.* In the quarter ended June 30, 2000, we incurred \$6.9 million of in-process research and development costs in relation to our acquisition of BlueGill. In the quarter ended September 30, 2000, we incurred \$18.6 million of in-process research and development costs in relation to our acquisition of TransPoint. Please refer to the Notes to Consolidated Financial Statements included herein for a detailed discussion of these charges.

*Interest.* Our interest income increased from \$7.7 million for the year ended June 30, 2000 to \$15.4 million for the year ended June 30, 2001. Our balance of cash and invested assets was \$207.6 million at June 30, 2000 and \$256.1 million at June 30, 2001. Although interest rates have declined throughout the year ended June 30, 2001, we have seen a significant increase in average invested assets from \$116.1 million at June 30, 2000 to \$231.9 million at June 30, 2001. While cash and invested assets fluctuate quarter to quarter, the primary transactions influencing our cash and investment balances were the \$97.2 million we received in cash as part of the TransPoint acquisition in September 2000 and the \$35.0 million of cash we used in connection with our asset purchase agreement with Bank of America.

Our interest expense increased from \$8.0 million for the year ended June 30, 2000 to \$13.2 million for the year ended June 30, 2001. While we also incur interest expense on leases, the increase in interest expense is due primarily to the \$172.5 million of 6.5% convertible subordinated notes we issued in November 1999, which created slightly over 7 months of interest expense in the year ended June 30, 2000 and 12 months of interest expense in the year ended June 30, 2001. None of the 6.5% convertible debt had been converted to shares of our common stock as of June 30, 2001.

*Loss on Investments.* Due to overall market conditions, certain of our investments have incurred an "other than temporary" decline in market value. As a result, in the year ended June 30, 2001, we recorded charges of \$16.1 million to appropriately reflect the decline in value of these investments.

*Income Taxes.* We recorded an income tax benefit of \$11.4 million with an effective rate of 26.1% for the year ended June 30, 2000 and an income tax benefit of \$115.4 million with an effective rate of 24.1% for the year ended June 30, 2001. The reported effective rates differ from the blended statutory rate of 40% in both periods due to certain non-deductible goodwill, in-process research and development and other non-deductible expenses, offset somewhat by jobs credits and tax exempt interest income.

#### **Years Ended June 30, 1999 and 2000**

*Revenues.* Our total revenue increased by 24%, from \$250.1 million for the year ended June 30, 1999 to \$310.2 million for the year ended June 30, 2000. On a pro forma basis, net of the divestitures of our mortgage business in September 1998 and our imaging business in October 1998, and adjusting for the acquisition of Mobius Group in March 1999 and BlueGill in April 2000, revenue increased 22%, from \$252.9 million for the year ended June 30, 1999 to \$308.5 million for the year ended June 30, 2000. The increase in pro forma revenue was driven by increases of 26% in our Electronic Commerce segment, 25% in our Investment Services segment, and 1% in our Software segment. Growth in Electronic Commerce revenue is driven primarily by an increase in subscribers from nearly 3.0 million at June 30, 1999 to over 3.5 million at June 30, 2000. The 3.5 million subscriber number is net of approximately 0.4 million subscribers utilizing old legacy or non-Year 2000 compliant front ends that were purged by financial

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institutions during the six months ended December 31, 2000. Pro forma growth in Investment Services revenue is driven primarily by an increase in portfolios managed from approximately 715,000 at June 30, 1999 to approximately 950,000 at June 30, 2000. In spite of dampened demand caused by customer focus on Year 2000 projects early in the fiscal year, the Software segment was able to achieve nominal growth on a pro forma basis for the year ended June 30, 2000.

Our processing and servicing revenue increased by 30%, from \$201.1 million for the year ended June 30, 1999 to \$261.6 million for the year ended June 30, 2000. On a pro forma basis, adjusting for the acquisition of Mobius Group in March 1999, processing and servicing revenue increased by 27%, from \$205.4 million for the year ended June 30, 1999, to \$261.9 million for the year ended June 30, 2000. Pro forma growth in processing and servicing revenue is primarily the result of the previously mentioned growth in subscribers in our Electronic Commerce segment and portfolios managed in our Investment Services segment. Our processing agreements with portals allow for a free trial period for subscribers who enroll through the portal. Because these subscribers did not generate revenue during this free period, we did not count them in our active subscriber base. Additionally, we had 93 billers in production that presented approximately 94,000 bills in the month ended June 30, 2000. The number of bills we presented electronically has increased by 52% since the month ended March 31, 2000 and was up significantly from just over 13,000 per month at June 30, 1999. We exited the quarter ended June 30, 2000 processing about 16 million transactions on a monthly basis, compared to about 12 million as of June 30, 1999.

Our license fee revenue increased by 5%, from \$16.0 million for the year ended June 30, 1999 to \$16.8 million for the year ended June 30, 2000. On a pro forma basis, adjusting for the impact of divested software businesses and the acquisition of BlueGill in April 2000, license revenue declined by 3% from \$15.7 million for the year ended June 30, 1999 to \$15.3 million for the year ended June 30, 2000. In spite of dampened demand caused by customer focus on Year 2000 projects early in the fiscal year, the Software segment was able to generate fairly consistent license sales on a year over year basis.

Our maintenance fee revenue increased by 6%, from \$17.7 million for the year ended June 30, 1999 to \$18.8 million for the year ended June 30, 2000. On a pro forma basis, adjusting for the impact of divested software businesses and the acquisition of BlueGill, maintenance revenue increased by 10%, from \$16.9 million for the year ended June 30, 1999 to \$18.6 million for the year ended June 30, 2000. This increase was due to first year maintenance fees from new maintenance paying customers added late in fiscal 1999 and throughout fiscal 2000 and moderate price increases, offset by maintenance retention rates in the mid to upper 80% range for the renewal maintenance base in the Software segment.

Our other revenue decreased by 16%, from \$15.4 million for the year ended June 30, 1999 to \$13.0 million for the year ended June 30, 2000. On a pro forma basis, adjusting for the impact of divested software businesses and the acquisitions of Mobius Group and BlueGill, other revenue decreased by 15%, from \$14.9 million for the year ended June 30, 1999 to \$12.7 million for the year ended June 30, 2000. The decrease in pro forma revenue was due primarily to the decline in software implementations and other software consulting engagements resulting from customer software implementation freezes earlier in fiscal 2000 in preparation for and follow up from the Year 2000.

*Cost of Processing, Servicing and Support.* Our cost of processing, servicing and support was \$146.7 million or 58.7% of total revenue for the year ended June 30, 1999, and was \$182.5 million or 58.8% of total revenue for the year ended June 30, 2000. Cost of processing, servicing and support as a percentage of servicing only revenue was 62.7% for the year ended June 30, 1999, and was 62.2% for the year ended June 30, 2000. From an efficiency perspective, our ratio of electronic payments to total payments improved from 49% at June 30, 1999 to 58% at June 30, 2000. Electronic payments carry a significantly lower variable cost per unit than paper based payments. Additionally, we saw improvements from the leverage inherent in converting the majority of our subscribers from two legacy systems to our Genesis processing system. These improvements, however, were offset by E-Bill implementation costs as we continued to move an increasing number of billers into live production, and by transaction costs generated by portal subscribers operating within their free period. Additionally, throughout the year ended June 30, 2000, we invested significantly in quality improvement and infrastructure improvement initiatives to prepare for future growth.

*Research and Development.* Our research and development costs were \$21.1 million or 8.4% of total revenue for the year ended June 30, 1999, and were \$35.6 million or 11.5% of total revenue for the year ended June 30, 2000. Adjusted for capitalized development costs of \$7.4 million for the year ended June 30, 1999 and \$7.9 million for the year ended June 30, 2000, our gross research and development costs were \$28.5 million, or 11.4% of total revenue for the year ended June 30, 1999, and \$43.5 million, or 14.0% of total revenue for the year ended June 30, 2000. While \$0.9 million of the increase was attributable to BlueGill, we have continued to invest a significant portion of our revenue into research and development activities in all business segments in anticipation and support of revenue growth, quality enhancement and efficiency improvement opportunities.

*Sales and Marketing.* Our sales and marketing costs were \$32.4 million or 12.9% of total revenue for the year ended June 30, 1999, and were \$44.8 million or 14.4% of total revenue for the year ended June 30, 2000. While BlueGill accounted for \$2.3 million of the increase, we increased our sales staff to sign additional billers in support of our electronic billing offerings, and we increased program management staff in support of new non-subscriber based products designed to leverage our existing electronic payment infrastructure.

*General and Administrative.* Our general and administrative expenses were \$31.5 million or 12.6% of total revenue for the year ended June 30, 1999, and were \$40.9 million or 13.2% of total revenue for the year ended June 30, 2000. Aside from the \$0.9 million of added cost directly attributable to BlueGill and a full year of Mobius Group operations, the increase in general and administrative expense is due principally to an increase in facilities costs resulting from upgraded facilities in Dublin, Ohio and Jersey City, New Jersey and a new facility in Phoenix, Arizona, and increased administrative staff required to manage growth in all areas of the Company.

*Depreciation and amortization.* Our depreciation and amortization costs increased from \$24.6 million for the year ended June 30, 1999 to \$42.8 million for the year ended June 30, 2000. The increase was primarily the result of amortization of intangible assets resulting from the Mobius Group and BlueGill acquisitions. The amount of the increase directly attributable to BlueGill alone was \$10.2 million. The remaining increase is the result of capital spending in support of continued growth and quality improvement initiatives.

*In-Process Research and Development.* The in-process research and development charge of \$2.2 million for the year ended June 30, 1999 resulted from our purchase of the Mobius Group in March 1999 and the charge of \$6.9 million for the year ended June 30, 2000 resulted from our purchase of BlueGill in April 2000. Please refer to the Notes to Consolidated Financial Statements included herein for a detailed discussion of these charges.

*Interest.* Our interest income increased from \$2.8 million for the year ended June 30, 1999 to \$7.7 million for the year ended June 30, 2000. The increase was primarily due to an increase in average cash and investments from \$43.3 million for the year ended June 30, 1999 to \$116.1 million for the year ended June 30, 2000. The increase in average cash and investments is primarily the result of proceeds from the convertible subordinated debenture offering in November 1999.

Our interest expense increased from \$0.6 million for the year ended June 30, 1999 to \$8.0 million for the year ended June 30, 2000. The increase is due primarily to \$172.5 million of 6.5% convertible subordinated notes that we issued in November 1999 which resulted in just over seven months of interest expense in the year ended June 30, 2000.

*Income Taxes.* For the year ended June 30, 1999, we recorded an income tax benefit of \$12.0 million (effective rate not meaningful) and for the year ended June 30, 2000, we recorded an income tax benefit of \$11.4 million with an effective rate of 26%. In the year ended June 30, 1999, we recorded a one-time tax benefit of approximately \$12.2 million arising out of our medical benefits management subsidiary. Net of this one-time benefit, the effective rates in both years differ from the statutory rate of 35% due to goodwill, in-process research and development and other non deductible expenses; jobs credits; state income taxes; and tax exempt interest income.



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#### Segment Information

The following table sets forth our operating revenue and operating income by industry segment for the periods noted. Charges identified as purchase accounting amortization, in-process research and development, a one time marketing charge, and net gain on dispositions of assets were separated from the operating results for a better understanding of the underlying performance of each segment. Explanations of these charges can be found in the discussions above.

	Year ended June 30,		
	1999	2000	2001
	(In thousands)		
Operating Revenue:			
Electronic Commerce	\$ 169,443	\$ 213,391	\$ 301,532
Investment Services	39,304	54,792	69,613
Software	41,384	42,012	62,175
Total Operating Revenue	\$ 250,131	\$ 310,195	\$ 433,320
Operating Income (Loss):			
Operating Income (Loss) Excluding Specific Items:			
Electronic Commerce	\$ (3,126)	\$ (18,248)	\$ (13,083)
Investment Services	11,250	15,830	20,347
Software	15,931	10,536	837
Corporate	(23,348)	(26,120)	(35,746)
Specific Items:			
Purchase accounting amortization	(6,815)	(18,517)	(393,436)
In-process research and development	(2,201)	(6,900)	(18,600)
One time marketing charge	-	-	(25,000)
Net gain on dispositions of assets	4,576	-	-
Total Operating Loss	\$ (3,733)	\$ (43,419)	\$ (464,681)

#### Years Ended June 30, 2000 and 2001

Revenue in our Electronic Commerce business increased by 41%, from \$213.4 million for the year ended June 30, 2000 to \$301.5 million for the year ended June 30, 2001. Net of approximately \$35.0 million of incremental revenue provided from TransPoint and Bank of America as described below, underlying revenue in our Electronic Commerce business grew in the mid 20% range. The primary driver of this underlying revenue growth was an increase in subscribers from 3.5 million at June 30, 2000 to just over 5.2 million at June 30, 2001, 0.3 million of which were added from Bank of America in October 2000.

We completed our acquisition of TransPoint in September 2000 and, with this acquisition, became the preferred provider of electronic billing and payment services to customers offered through Microsoft's MSN and Money Central product offerings. The agreement with Microsoft provides guaranteed revenue of \$120 million over a five-year period, which commenced in January 2001. Additionally, as part of the TransPoint acquisition, we received \$60 million of guaranteed revenue and/or cost saving opportunities through First Data Corporation over a five-year period, which began in September 2000. Effective October 1, 2000, we completed a strategic agreement with Bank of America, the largest bank in the U.S., to offer electronic billing and payment services to its customer base. This ten-year agreement provides annual revenue guarantees of \$50 million (\$12.5 million on a quarterly basis) and Bank of America has agreed to invest \$45 million over a two year period to promote the awareness and adoption of electronic billing and payment services by their customers. We had been processing certain transactions for Bank of America before the strategic alliance was completed and, therefore, the \$50 million annual revenue guarantee should not be considered entirely incremental to our underlying revenue. We did, however, add 300,000 incremental subscribers to our subscriber base upon completion of the agreement. In each of these agreements, actual subscriber revenue is below minimums as of June 30, 2001, and as a result, overall subscriber based revenue growth will correlate less closely with the growth in the number of subscribers until Bank of America and Microsoft subscribers generate sufficient subscriber revenue to exceed the quarterly minimums.



To date, we have signed 241 named billers to our E-Bill electronic billing product offering. Combined with the 30 net new billers we assumed with the TransPoint acquisition, this brings our signed biller total to 271. We now have 173 billers in production that delivered nearly 500,000 electronic bills in the month ended June 30, 2001. Our acquisition of BlueGill is expected to facilitate our efforts to provide quality billing content by simplifying and accelerating the process of taking bills from paper to electronic. Also, we are adding bill aggregation technology to our Genesis platform and currently plan to add access to up to 30 additional billers through "bill scraping" over the course of calendar 2001, which will be available to our consumer service provider partners as they upgrade to Web Pay for Consumers. As of June 30, 2001, we are distributing six popular credit card bills through scraping technology for a total consumer choice of among 179 electronic bills. We believe that a complete, integrated round trip electronic billing and payment experience for an average of six to ten bills per customer per month is an important factor in driving subscriber growth. As of June 30, 2001, we estimate that the average consumer has the potential to receive from five to eight electronic bills and, by the end of the calendar year, we expect to extend that number to eight to ten electronic bills for consumers in major strategic marketing areas throughout the United States.

When combining subscriber growth within guaranteed revenue minimums and increasing electronic billing revenue with a transaction based pricing model available to our largest bill payment customers, it has become more difficult to correlate revenue solely to the number of subscribers, with transactions processed becoming an additional key indicator. During the month ended June 30, 2001, we processed over 22 million transactions, compared to about 16 million in the quarter ended June 30, 2000.

The operating loss in our Electronic Commerce segment, excluding purchase accounting amortization, a one time marketing charge of \$25.0 million, and in-process research and development, has improved from \$18.2 million for the year ended June 30, 2000 to \$13.1 million for the year ended June 30, 2001. As a result of the TransPoint acquisition and the purchase of Bank of America's electronic billing and payment assets, we have supported two additional and less efficient billing and payment processing platforms for most of fiscal 2001. Although expected, this has resulted in a significant increase in our cost of processing, servicing and support during the year. We completed the conversion of TransPoint subscribers and billers to the Genesis processing platform in the quarter ended June 30, 2001. We completed the conversion of a portion of the Bank of America East subscribers within the quarter ended March 31, 2001. The remaining Bank of America subscribers, referred to internally as Bank of America West, are expected to be converted in the quarter ended December 31, 2001 with the remainder of legacy Bank of America subscribers converting from our Austin processing platform in the following quarter. Until the final conversion is completed, we will continue to experience higher than normal incremental processing costs, but at a decreasing rate, as new subscriber transactions are processed on the more efficient Genesis processing system. Somewhat masked by less efficient incremental costs resulting from TransPoint and Bank of America are underlying improvements in efficiency and processing quality within Genesis. Our ratio of electronic payments to total payments has improved from approximately 58% at June 30, 2000 to about 64% as of June 30, 2001. Electronic payments carry a significantly lower variable cost per unit than paper based transactions and are far less likely to result in a costly customer claim. We have also incurred additional sales and marketing and general and administrative expenses as a result of the two transactions. Throughout fiscal 2001, we have continued to focus attention on the following four areas within our Electronic Commerce business:

- delivery of an increasing number of bills electronically over the Internet;
- extension of the payment capabilities of our Genesis infrastructure while continuing to deliver market-leading quality and cost efficiency;
- co-marketing programs designed to bring billers and channel partners together to strengthen incentives and value delivered to consumers; and
- expansion of the number of sites where consumers can receive and pay bills.

While there are no guarantees as to the timing or extent of accelerated adoption of electronic billing and payment services, we believe that with our recent transactions with BlueGill, TransPoint and Bank of America, along with other previously described strategic alliances, we are better positioned to maintain our market leadership position throughout an accelerated growth cycle should it occur.

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Revenue in our Investment Services business increased by 27%, from \$54.8 million for the year ended June 30, 2000 to \$69.6 million for the year ended June 30, 2001. Growth in this business is due primarily to an increase in portfolios managed from approximately 950,000 at June 30, 2000 to over 1.1 million at June 30, 2001. Much of the revenue growth has occurred in retail versus institutional accounts that carry a lower unit price. During the quarter ended March 31, 2001, the business released a significantly enhanced version of M-Search, a money manager database system, and APL-ASP, an innovative and flexible new portfolio management services offering for start-up and break away money managers. When combined with the emergence of Internet-based wrap services, which is creating a highly visible new distribution channel for money managers and brokers, these product enhancements and new distribution channel opportunities could fuel further growth for our Investment Services business.

Operating income in our Investment Services business, net of purchase accounting amortization, increased by 29%, from \$15.8 million for the year ended June 30, 2000 to \$20.3 million for the year ended June 30, 2001. Although much of our revenue growth has occurred in retail versus institutional accounts that carry a lower unit price, which in turn places downward pressure on margins as the cost to process this business is not proportionally lower, we have been able offset this pressure with efficiencies elsewhere in the business, as our operating margins have remained consistent year over year.

Revenue in our Software business increased by 48%, from \$42.0 million for the year ended June 30, 2000 to \$62.2 million for the year ended June 30, 2001. The growth in software revenue is primarily attributable to the acquisition of BlueGill, now operating as CheckFree i-Solutions, as revenue in our more mature software businesses has increased modestly on a year over year basis. Growth from i-Solutions sales has come from successful efforts both domestically and internationally. While we expect software revenue to continue to grow, current market conditions have placed a dampening effect on the rate of growth in the near term.

Operating income in our Software business, net of purchase accounting amortization, has declined from \$10.5 million for the year ended June 30, 2000 to \$0.8 million for the year ended June 30, 2001. As expected, the operations acquired from BlueGill have provided downward pressure on operating margins throughout fiscal 2001 as we have invested significantly in this emerging product line. The electronic billing and statement software product line acquired from BlueGill provides significant synergies to the electronic billing and payment products within our Electronic Commerce business. Investments in this area are expected to facilitate our efforts to provide high quality billing content, and simplify and accelerate the process of taking bills and statements from paper to electronic form.

Our Corporate segment represents costs for legal, human resources, finance and various other unallocated overhead expenses. Our Corporate segment incurred operating expenses of \$26.1 million or 8.4% of total revenue for the year ended June 30, 2000 and \$35.7 million or 8.2% of total revenue for the year ended June 30, 2001. Although we continue to add corporate resources in support of the growth of the business, our overhead costs as a percentage of revenue have begun to decline, and are starting to reflect the expected leverage in our business model.

The purchase accounting amortization line represents amortization of intangible assets resulting from all of our various acquisitions from 1996 forward. The total amount of purchase accounting amortization has increased from \$18.5 million for the year ended June 30, 2000 to \$393.4 million for the year ended June 30, 2001. The increases are the result of intangible assets created by the acquisitions of BlueGill in April 2000 and TransPoint in September 2000 and the acquisition of the electronic billing and payment assets of Bank of America effective in October 2000. For comparative purposes, the breakout of purchase accounting amortization by segment is as follows (in thousands):

	Year ended June 30,		
	1999	2000	2001
Electronic Commerce	\$ 2,364	\$ 2,371	\$ 328,072
Investment Services	3,157	4,920	5,369
Software	1,294	11,226	59,995
Total	\$ 6,815	\$ 18,517	\$ 393,436

In the quarter ended June 30, 2000, we incurred \$6.9 million of in-process research and development costs related to the acquisition of BlueGill and, in the quarter ended September 30, 2000, we incurred \$18.6 million of in-process research and development costs as a result of the acquisition of TransPoint. Please refer to the Notes to Consolidated Financial Statements included herein for a complete description of the in-process research and development charges.

The one time marketing charge took place in the quarter ended December 31, 2000. Our strategic alliance with Bank of America called for us to provide \$25.0 million of cash at closing to help support a two-year \$45.0 million marketing campaign by Bank of America. Because we do not have the ability to directly impact the specific nature, timing or extent of the use of the funds, we expensed the \$25.0 million as a period cost in the quarter ended December 31, 2000. Additionally, because we do not market directly to subscribers but rather leave that to our various consumer service provider customers, we have separated this charge from ongoing operations as an unusual, non-recurring event.

#### **Years Ended June 30, 1999 and 2000**

Revenue in our Electronic Commerce segment increased by 26%, from \$169.4 million for the year ended June 30, 1999 to \$213.4 million for the year ended June 30, 2000. This increase was primarily due to an increase in subscribers from nearly 3.0 million at June 30, 1999 to 3.5 million at June 30, 2000. During the quarter ended September 30, 1999, a few of our financial institution customers removed approximately 200,000 subscribers from our system that were either utilizing our low fee maintenance only processing services through proprietary PC-based front ends or that no longer promoted certain legacy financial manager software. Additionally, in the quarter ended December 31, 1999, we assisted our financial institution customers in removing another 200,000 subscribers who were utilizing personal financial management software that was not Year 2000 compliant. The majority of these combined reductions were on older contracts with lower than average associated monthly fees.

As of June 30, 2000, we had signed 157 billers to our E-Bill electronic billing product offering, and we had 93 billers in production that presented approximately 94,000 bills in the final month of fiscal 2000. The number of bills we presented electronically had increased by 52% since the month ended March 31, 2000 and was up significantly from just over 13,000 per month at June 30, 1999. As of June 30, 2000, we had the potential to process an average of four to five bills per month for our existing customer base. We exited the quarter ended June 30, 2000 processing about 16 million transactions on a monthly basis, compared to about 12 million as of June 30, 1999.

Our operating loss in our Electronic Commerce segment, net of purchase accounting amortization, increased from \$3.1 million for the year ended June 30, 1999, to \$18.2 million for the year ended June 30, 2000. In April 1999, we experienced a system error that led some users of our electronic payment service to experience intermittent problems accessing and using the system. As a result of this outage, we recorded charges totaling \$2.7 million. Net of these charges, the operating loss in our Electronic Commerce segment would have been \$0.4 million in the year ended June 30, 1999. During the year ended June 30, 2000, we invested heavily in the following four areas:

- marketing and price incentives to spur industry growth;
- compressing the time from E-Bill contract execution to live billing;
- improved infrastructure and programs that improve quality and performance; and
- extension of payment offerings through leverage of our existing payment infrastructure.

From an efficiency perspective, our ratio of electronic payments to total payments improved from 49% at June 30, 1999 to 58% at June 30, 2000. Additionally, we saw improvements from the leverage inherent in converting two-thirds of our subscribers from two legacy systems to our Genesis processing system. However, as subscribers signed up for electronic billing and payment offerings through portals and other sponsors that offer free trial periods, we incurred the variable costs associated with processing transactions from these customers with no revenue to offset the costs.

## management s\_discussion\_and\_analysis

### *of Financial Condition and Results of Operations*

Revenue in our Investment Services segment increased by 39%, from \$39.3 million for the year ended June 30, 1999 to \$54.5 million for the year ended June 30, 2000. On a pro forma basis, assuming that Mobius Group had been in place for a full year in fiscal 1999, revenue increased by 25%, from \$43.9 million for the year ended June 30, 1999 to \$54.8 million for the year ended June 30, 2000. Growth in pro forma revenue was primarily the result of an increase in portfolios managed from approximately 715,000 at June 30, 1999 to over 950,000 at June 30, 2000. A significant portion of portfolio growth over fiscal 2000 occurred in retail versus institutional accounts that carry a lower unit price. In October 1999, we launched our new M-Plan product from Mobius Group. Consultants, plan sponsors, investment managers and financial planners use M-Plan for integrating retirement, capital needs, tax, education and real estate planning needs for their customers. Additionally, in March 2000, we released revisions to our M-Search product from Mobius Group that allows Internet based data collection capabilities to the product which will make data collection on money manager returns and asset allocations more timely.

Reported operating income in our Investment Services segment, net of purchase accounting amortization, increased from \$11.3 million for the year ended June 30, 1999 to \$15.8 million for the year ended June 30, 2000. On a pro forma basis, adjusting for the Mobius Group acquisition, operating income increased from \$11.8 million for the year ended June 30, 1999 to \$15.8 million for the year ended June 30, 2000. As indicated earlier, much of the portfolio growth over the year had occurred in retail versus institutional accounts that carried a lower unit price, which placed downward pressure on margins as the cost to process this business was not proportionally lower.

Reported revenue in our Software segment increased by 2%, from \$41.4 million for the year ended June 30, 1999 to \$42.0 million for the year ended June 30, 2000. On a pro forma basis, net of the impact of divestitures in fiscal 1999 and the acquisition of BlueGill in fiscal 2000, revenue increased by 1%, from \$39.6 million for the year ended June 30, 1999 to \$40.1 million for the year ended June 30, 2000. The revenue results were expected, given purchasing moratoriums by customers concerned with Year 2000 issues through calendar year 1999 and into calendar year 2000.

Reported operating income in our Software segment, net of purchase accounting amortization, declined from \$15.9 million for the year ended June 30, 1999 to \$10.5 million for the year ended June 30, 2000. The decrease in operating income reflects investments in new initiatives such as the launch of missingmoney.com, a state-sponsored Internet site developed with the National Association of Unclaimed Property Administrators designed to enable individuals to find and claim money owed to them from non-refunded deposits, unclaimed securities and other accounts held by states. Also, incremental resources had been assigned to a new automated clearinghouse alliance services program that carries a profit margin that is inherently lower than that of our traditional product offerings in this area and the acquisition of BlueGill in April 2000 provided a few months of loss from operations due to significant investment inherent in this new business.

Our Corporate segment operating loss increased from \$23.3 million, or 9.3% of total revenue for the year ended June 30, 1999 to \$26.1 million, or 8.4% of total revenue for the year ended June 30, 2000. During the year ended June 30, 1999, we incurred \$1.9 million of non-recurring costs related to a terminated follow-on stock offering, the creation of a special-purpose employee medical benefits management subsidiary, and the sale of a building in Columbus, Ohio. Net of these one-time charges, our operating loss for the year ended June 30, 1999 would have been \$21.4 million, or 8.6% of total revenue. On an adjusted basis, our corporate overhead as a percentage of revenue continued to decrease.

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## Liquidity and Capital Resources

The following table sets forth a summary of cash flow activity and should be referred to in conjunction with statements regarding our liquidity and capital resources (in thousands):

	Summary of Cash Flows for the Year ended June 30,		
	1999	2000	2001
Cash flow provided by (used in) operating activities	\$ 25,571	\$ 21,016	\$ (234)
Cash flow used in investing activities	(16,217)	(108,935)	(26,888)
Cash flow provided by (used in) financing activities	(33,443)	203,547	23,170
Net increase (decrease) in cash and cash equivalents	\$ (24,089)	\$ 115,628	\$ (3,952)

As of June 30, 2001, we have \$160.1 million in cash, cash equivalents and short-term investments on hand and an additional \$96.0 million in long-term investments. Our balance sheet reflects a current ratio of 2.11 and working capital of \$142.7 million. We believe that existing cash, cash equivalents and investments will be more than sufficient to meet our presently anticipated requirements for the foreseeable future. To the extent that additional capital resources are required, we have access to an untapped \$30 million line of credit.

For the year ended June 30, 2001, we used \$0.2 million of cash flow from operations. Of this amount, \$6.7 million represents net proceeds from trading securities transactions, which GAAP requires us to reflect in cash flow from operations. Also of note, included in cash used in operations was a one time \$25.0 million cash marketing charge related to our strategic alliance with Bank of America.

From an investing perspective, we used \$41.7 million of cash for the purchase of property and software and we capitalized \$4.9 million of software development costs. We used \$67.0 million for the net purchase of held-to-maturity securities and we capitalized another \$10.3 million of strategic agreement costs. Finally, we received \$96.6 million in cash and cash equivalents through the purchase of TransPoint, net of related acquisition costs.

From a financing perspective, we received \$15.7 million in proceeds from the exercise of common stock warrants. We received an additional \$6.9 million from the exercise of options from our employee stock option plan and \$4.4 million from the purchase of stock from our employee stock purchase plan. Finally, we used \$3.8 million of cash for principal payments under capital lease obligations.

For the year ended June 30, 2000, we generated \$21.0 million of cash flow from operations. Of this amount, \$3.6 million represented net proceeds from trading securities transactions, which GAAP requires us to reflect in cash flow from operations.

From an investing perspective, we used \$39.5 million of cash for the purchase of property and software, and capitalized \$7.6 million of software development costs. We used \$61.0 million for the net purchase of held-to-maturity securities and another \$10.0 million in the purchase of common stock. Finally, we received \$9.2 million in cash and cash equivalents through the purchase of BlueGill, net of related acquisition costs.

From a financing perspective, we received \$166.9 million of net proceeds from the issuance of \$172.5 million in 6.5% convertible subordinated notes and another \$25.5 million in proceeds from the exercise of common stock warrants and the purchase of our common stock by third parties. We received additional cash of \$9.7 million from the exercise of options from our employee stock option plans and \$2.9 million from the purchase of stock from our employee stock purchase plan. Finally, we used \$1.5 million of cash for principal payments under capital lease obligations.

continued >>

## management s\_discussion\_and\_analysis

### *of Financial Condition and Results of Operations*

For the year ended June 30, 1999, we generated \$25.6 million of cash flow from operations. Of this amount, \$14.3 million represented net proceeds from trading securities transactions, which are reflected as operating in nature for accounting purposes.

From an investing perspective, we used \$40.4 million of cash for the purchase of property and software, of which approximately \$14.9 million was for the purchase of land and a building in Dublin, Ohio and another \$6.4 million in leasehold improvements to ready the building for occupancy. The remaining \$19.1 million was used for computer equipment, software and leasehold improvements in support of initiatives to grow the business and improve quality. We received \$18.4 million from the net sale of the various software business divestitures during the year and the sale of a building in Columbus, Ohio and \$14.9 million from the repayment of a note receivable established in fiscal 1998 related to the purchase of the Dublin, Ohio facility. We capitalized \$8.0 million in software development costs related to new business initiatives in all three of our business segments. Additionally, we spent approximately \$0.2 million in cash in connection with the acquisition of Mobius Group, purchased \$1.9 million in held-to-maturity securities and received \$1.0 million in proceeds from the sale of held-to-maturity securities.

From a financing perspective, we used \$31.3 million in the purchase of approximately 4.7 million shares of treasury stock for an average price of approximately \$6.65 per share. We used \$3.3 million of cash for principal payments under capital leases and another \$3.6 million to fund an escrow account to release our obligation for bonds with the Department of Economic Development of the State of Ohio to facilitate the sale of land and a building in Columbus, Ohio. We received \$2.9 million in proceeds from the exercise of options under the employee stock option plan and \$1.9 million from the purchase of shares under the employee stock purchase plan.

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#### **Inflation**

We believe the effects of inflation have not had a significant impact on our results of operations.

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#### **Market Risk**

With the acquisition of BlueGill in April 2000, we obtained operations in Canada and recently opened offices in the United Kingdom, Singapore and Australia. As a result, we now have assets and liabilities outside the United States that are subject to fluctuations in foreign currency exchange rates. Due to the start up nature of each of these operations, however, we currently utilize the U.S. dollar as the functional currency for all international operations. As these operations begin to generate sufficient cash flow to provide for their own cash flow requirements, we will convert to local currency as the functional currency in each related operating unit as appropriate. Because we utilize the U.S. dollar as the functional currency and due to the immaterial nature of the amounts involved, our economic exposure from fluctuations in foreign exchange rates is not significant enough at this time to engage in forward foreign exchange and other similar instruments.

While our international sales represented less than 2% of our revenue for the year ended June 30, 2001, we now market, sell and license our products throughout the world. As a result, our future revenue could be somewhat affected by weak economic conditions in foreign markets that could reduce demand for our products.

Our exposure to interest rate risk is limited to the yield we earn on invested cash, cash equivalents and investments and interest based revenue earned on products such as our account balance transfer business. Our convertible debt carries a fixed rate, as do any outstanding capital lease obligations. Although our Investment Policy currently prohibits the use of derivatives for trading or hedging purposes, we believe that our limited interest rate risk currently does not warrant the use of such instruments.

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## Recent Accounting Pronouncements

On July 20, 2001, the Financial Accounting Standards Board (FASB) issued SFAS 141, "Business Combinations" and SFAS 142, "Goodwill and Other Intangible Assets." SFAS 141 requires all business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting. In addition, it requires application of the provisions of SFAS 142 for goodwill and other intangible assets related to any business combinations completed after June 30, 2001, but prior to the adoption date of SFAS 142. SFAS 142 changes the accounting for goodwill and other intangible assets. Goodwill will no longer be subject to amortization over its estimated useful life. Rather, goodwill will be subject to at least an annual assessment for impairment by applying a fair-value-based test. All other acquired intangibles will be separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the intangible asset can be sold, transferred, licensed, or exchanged, regardless of our intent to do so. Other intangibles will be amortized over their useful lives.

SFAS 142 becomes effective for us on July 1, 2002. We are still assessing the impact of all the statement provisions on our financial position and results of operations; however, based on our review to date, we expect the following significant impacts:

- Upon adoption, we will be required to reclassify approximately \$2 million of unamortized workforce in place intangible assets into goodwill.
- Upon adoption, the balance of goodwill and workforce in place is expected to be \$624 million and we will discontinue amortizing these assets at that time. The resulting reduction in amortization expense is estimated at approximately \$200 million for each of our fiscal years 2003 and 2004, and approximately \$192 million for our 2005 fiscal year.
- We will be required to perform a transitional goodwill impairment test as of July 1, 2002. The impairment test will require us to: (1) identify our reporting units, (2) determine the carrying value of each reporting unit by assigning assets and liabilities, including existing goodwill and intangible assets, to those reporting units, and (3) determine the fair value of each reporting unit. If the carrying value of any reporting unit exceeds its fair value, we will determine the amount of any goodwill impairment through a detailed fair value analysis of each of the assigned assets (excluding goodwill). At this time, we do not anticipate any charge resulting from the transitional impairment test; however, due to the extensiveness of the efforts involved, that test has not yet been performed. Under the provisions of SFAS 142, we are required to complete the test before December 31, 2002.
- Following the transitional impairment test, our goodwill balances will be subject to annual impairment tests using the same process described above. If any impairment is indicated as a result of the annual test, an impairment charge would be recorded as part of income from operations.

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**Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995**

Except for the historical information contained herein, the matters discussed in our Annual Report include certain forward-looking statements within the meaning of Section 27A of the Securities Act, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which are intended to be covered by the safe harbors created thereby. Those statements include, but may not be limited to, all statements regarding our and management's intent, belief and expectations, such as statements concerning our future profitability, and our operating and growth strategy. Investors are cautioned that all forward-looking statements involve risks and uncertainties including, without limitation, the factors set forth under the caption "Business – Business Risks" in the Annual Report on Form 10-K for the year ended June 30, 2001 and other factors detailed from time to time in our filings with the Securities and Exchange Commission. One or more of these factors have affected, and in the future could affect, our businesses and financial results in the future and could cause actual results to differ materially from plans and projections. Although we believe that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate. Therefore, there can be no assurance that the forward-looking statements included in this Annual Report will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as representations by us or any other person that our objectives and plans will be achieved. All forward-looking statements made in this Annual Report are based on information presently available to our management. We assume no obligation to update any forward-looking statements.



## INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders of  
CheckFree Corporation and Subsidiaries:

We have audited the accompanying consolidated balance sheets of CheckFree Corporation (the "Company") and its subsidiaries as of June 30, 2000 and 2001, and the related consolidated statements of operations, stockholders' equity and cash flows for the years ended June 30, 1999, 2000, and 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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, such consolidated financial statements present fairly, in all material respects, the financial position of the Company and its subsidiaries at June 30, 2000 and 2001, and the results of their operations and their cash flows for the years ended June 30, 1999, 2000, and 2001 in conformity with accounting principles generally accepted in the United States of America.

*Deloitte + Touche LLP*

Atlanta, Georgia  
August 3, 2001

CheckFree Corporation and Subsidiaries  
consolidated\_balance\_sheets

	Year Ended June 30,	
	2000	2001
	(In thousands, except share data)	
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 128,074	\$ 124,122
Investments	56,548	35,930
Accounts receivable, net	58,308	88,818
Prepaid expenses and other assets	12,813	8,681
Deferred income taxes	9,733	13,725
Total current assets	265,476	271,276
PROPERTY AND EQUIPMENT, Net	93,214	109,226
OTHER ASSETS:		
Capitalized software, net	37,189	187,021
Goodwill, net	213,305	820,169
Strategic agreements, net	-	643,212
Other intangible assets, net	37,975	47,118
Investments	23,003	96,042
Deferred income taxes	29,248	-
Other noncurrent assets	13,704	9,889
Total other assets	354,424	1,803,451
	\$ 713,114	\$ 2,183,953
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$ 10,158	\$ 19,084
Accrued liabilities	43,958	60,090
Current portion of long-term obligations	5,955	4,528
Deferred revenue	26,644	44,913
Total current liabilities	86,715	128,615
ACCRUED RENT AND OTHER	7,269	4,758
DEFERRED INCOME TAXES	-	141,853
OBLIGATIONS UNDER CAPITAL LEASES – Less current portion	736	4,041
CONVERTIBLE SUBORDINATED NOTES	172,500	172,500
COMMITMENTS (Note 21)		
STOCKHOLDERS' EQUITY:		
Preferred stock – 15,000,000 and 50,000,000 authorized shares, respectively, \$0.01 par value; no amounts issued or outstanding	-	-
Common stock – 150,000,000 and 500,000,000 authorized shares, respectively, \$0.01 par value; issued 63,957,859 and 92,472,299 shares, respectively; outstanding 58,414,035 and 86,928,475 shares, respectively	584	869
Additional paid-in-capital	771,892	2,420,957
Accumulated deficit	(326,320)	(689,455)
Unearned compensation	(262)	(185)
Total stockholders' equity	445,894	1,732,186
	\$ 713,114	\$ 2,183,953

See notes to consolidated financial statements.

CheckFree Corporation and Subsidiaries  
consolidated\_statements\_of\_operations

	Year Ended June 30,		
	1999	2000	2001
	(In thousands, except share data)		
REVENUES:			
Processing and servicing	\$ 201,059	\$ 261,621	\$ 362,051
License fees	15,975	16,818	30,180
Maintenance fees	17,746	18,752	21,332
Other	15,351	13,004	19,757
Total revenues	250,131	310,195	433,320
EXPENSES:			
Cost of processing, servicing and support	146,704	182,540	255,528
Research and development	21,085	35,631	55,621
Sales and marketing	32,354	44,782	90,283
General and administrative	31,466	40,931	50,474
Depreciation and amortization	24,630	42,830	427,495
In-process research and development	2,201	6,900	18,600
Total expenses	258,440	353,614	898,001
Net gain on dispositions of assets	4,576	-	-
LOSS FROM OPERATIONS	(3,733)	(43,419)	(464,681)
OTHER:			
Interest income	2,799	7,689	15,415
Interest expense	(618)	(8,027)	(13,154)
Loss on investments	-	-	(16,077)
LOSS BEFORE INCOME TAXES	(1,552)	(43,757)	(478,497)
INCOME TAX BENEFIT	(12,009)	(11,437)	(115,362)
NET INCOME (LOSS)	\$ 10,457	\$ (32,320)	\$ (363,135)
BASIC EARNINGS (LOSS) PER SHARE:			
Net income (loss) per common share	\$ 0.20	\$ (0.61)	\$ (4.49)
Equivalent number of shares	52,444,375	53,367,339	80,863,100
DILUTED EARNINGS (LOSS) PER SHARE:			
Net income (loss) per common share	\$ 0.18	\$ (0.61)	\$ (4.49)
Equivalent number of shares	56,529,165	53,367,339	80,863,100

See notes to consolidated financial statements.

CheckFree Corporation and Subsidiaries  
consolidated\_statements\_of\_stockholders \_e uity

(In thousands, except share data)

	Number of Shares of Common Stock	Common Stock At Par	Additional Paid-In Capital
BALANCE – JUNE 30, 1998	56,364,839	\$ 564	\$ 492,109
Net income	-	-	-
Stock options exercised	354,758	3	1,605
Employee stock purchases	48,748	1	968
401(k) match	-	-	-
Treasury stock acquired	-	-	-
Treasury stock retired	(5,549,381)	(55)	(33,610)
Issuance of common stock pursuant to acquisition	537,314	5	17,995
Tax benefit associated with exercise of stock options	-	-	1,318
BALANCE – JUNE 30, 1999	51,756,278	518	480,385
Net loss	-	-	-
Stock options and warrants exercised	1,795,785	18	35,224
Employee stock purchases	99,010	1	2,285
401(k) match	36,226	-	1,059
Issuance of common stock pursuant to acquisition	4,713,736	47	239,447
Issuance of restricted stock	13,000	-	333
Amortization of unearned compensation	-	-	-
Tax benefit associated with exercise of stock options and warrants	-	-	13,159
BALANCE – JUNE 30, 2000	58,414,035	584	771,892
Net loss	-	-	-
Stock options and warrants exercised	1,369,885	14	22,609
Employee stock purchases	92,721	1	3,623
401(k) match	51,834	-	2,487
Issuance of common stock pursuant to acquisition	27,000,000	270	1,601,723
Amortization of unearned compensation	-	-	-
Tax benefit associated with exercise of stock options and warrants	-	-	18,623
BALANCE – JUNE 30, 2001	86,928,475	\$ 869	\$ 2,420,957

See notes to consolidated financial statements.

<b>Number of Shares of Treasury Stock</b>	<b>Treasury Stock At Cost</b>	<b>Unearned Compensation</b>	<b>Accumulated Deficit</b>	<b>Total Stockholders' Equity</b>
(963,295)	\$ (4,362)	\$ -	\$ (304,457)	\$ 183,854
-	-	-	10,457	10,457
-	-	-	-	1,608
48,631	1,070	-	-	2,039
74,981	963	-	-	963
(4,709,698)	(31,336)	-	-	(31,336)
5,549,381	33,665	-	-	-
-	-	-	-	18,000
-	-	-	-	1,318
-	-	-	(294,000)	186,903
-	-	-	(32,320)	(32,320)
-	-	-	-	35,242
-	-	-	-	2,286
-	-	-	-	1,059
-	-	-	-	239,494
-	-	(333)	-	-
-	-	71	-	71
-	-	-	-	13,159
-	-	(262)	(326,320)	445,894
-	-	-	(363,135)	(363,135)
-	-	-	-	22,623
-	-	-	-	3,624
-	-	-	-	2,487
-	-	-	-	1,601,993
-	-	77	-	77
-	-	-	-	18,623
-	\$ -	\$ (185)	\$ (689,455)	\$ 1,732,186

CheckFree Corporation and Subsidiaries  
consolidated\_statements\_of\_cash\_flo s

	Year Ended June 30,		
	1999	2000	2001
		(In thousands)	
OPERATING ACTIVITIES:			
Net income (loss)	\$ 10,457	\$ (32,320)	\$ (363,135)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Write off of in-process research and development	2,201	6,900	18,600
Loss on investments	-	-	16,077
Depreciation and amortization	24,630	42,830	427,495
Deferred income tax provision	854	(11,437)	(115,362)
Net (gain) loss on dispositions of assets	(4,576)	-	-
Net loss on sale of property and equipment	-	-	56
Purchases of investments – Trading	(10,416)	(19,002)	(12,369)
Proceeds from maturities and sales of investments, net – Trading	24,683	22,608	19,029
Change in certain assets and liabilities (net of acquisitions and dispositions):			
Accounts receivable	(6,976)	(14,499)	(30,510)
Prepaid expenses and other	1,434	644	1,688
Accounts payable	988	(4,153)	8,926
Accrued liabilities and other	(2,194)	20,259	16,808
Deferred revenue	1,739	9,188	10,698
Income tax accounts	(17,253)	(2)	1,765
Net cash provided by (used in) operating activities	25,571	21,016	(234)
INVESTING ACTIVITIES:			
Purchase of property and software	(40,444)	(39,495)	(41,701)
Proceeds from sale of assets	18,435	-	2,257
Proceeds from repayment of note receivable	14,882	-	-
Capitalization of software development costs	(8,031)	(7,576)	(4,927)
Purchase of business, net of cash acquired	(190)	9,152	96,599
Capitalization of strategic agreement costs	-	-	(10,279)
Purchases of investments – Held to maturity	(1,875)	(70,796)	(145,997)
Proceeds from maturities and sales of investments – Held to maturity	1,006	9,780	79,041
Purchase of other investments	-	(10,000)	(1,881)
Net cash provided by (used in) investing activities	(16,217)	(108,935)	(26,888)
FINANCING ACTIVITIES:			
Principal payments under capital lease obligations	(3,327)	(1,495)	(3,847)
Escrow deposit associated with capital lease obligation	(3,637)	-	-
Proceeds from stock options exercised	2,926	9,721	6,940
Proceeds from employee stock purchase plan	1,931	2,903	4,374
Purchase of treasury stock	(31,336)	-	-
Proceeds from sale of stock and exercise of warrants	-	25,515	15,703
Proceeds from issuance of convertible subordinated notes	-	166,903	-
Net cash provided by (used in) financing activities	(33,443)	203,547	23,170
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(24,089)	115,628	(3,952)
CASH AND CASH EQUIVALENTS:			
Beginning of period	36,535	12,446	128,074
End of period	\$ 12,446	\$ 128,074	\$ 124,122

See notes to consolidated financial statements.

## CheckFree Corporation and Subsidiaries

### notes\_to\_consolidated\_financial\_statements

As of and for the years ended June 30, 1999, 2000 and 2001

#### NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Organization** – CheckFree Corporation (the “Company”) is the parent company of CheckFree Services Corporation (“CFSC”), the principal operating company of the business. In April 2000, CFSC changed its name from CheckFree Corporation to CheckFree Services Corporation. Following that change, in August 2000, CheckFree Holdings Corporation changed its name to CheckFree Corporation. CFSC was organized in 1981 and is a leading provider of transaction processing services, software and related products to financial institutions and businesses and their customers throughout the United States. See Note 19 for a description of the Company’s business segments.

**Principles of Consolidation** – The accompanying consolidated financial statements include the results of operations of the Company, its wholly-owned subsidiaries, and CheckFree Management Corporation, of which the Company is the majority owner. All significant intercompany transactions have been eliminated.

**Use of Estimates** – The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Processing Agreements** – The Company has agreements with transaction processors to provide origination and settlement services for the Company. Under the agreements, the Company must fund service fees and returned transactions when presented. These agreements expire at various dates.

**Transaction Processing** – In connection with the timing of the Company’s financial transaction processing, the Company is exposed to credit risk in the event of nonperformance by other parties, such as returns and chargebacks. The Company utilizes credit analysis and other controls to manage its credit risk exposure. The Company also maintains a reserve for future returns and chargebacks.

**Cash and Cash Equivalents** – The Company considers all highly liquid debt instruments purchased with maturities of three months or less to be cash equivalents.

**Investments** – The Company has certain investments in debt and equity securities that are classified as either available-for-sale, trading or held-to-maturity securities in accordance with Statement of Financial Accounting Standards (“SFAS”) 115, “Accounting for Certain Investments in Debt and Equity Securities.” At June 30, 2000 and 2001, the Company does not have any investments classified as available-for-sale. Trading securities are carried at market value and unrealized holding gains and losses are included in income. Held-to-maturity securities are carried at amortized cost.

The Company has certain other investments that are accounted for under the cost method. Under the cost method of accounting, investments are carried at cost and are adjusted only for other-than-temporary declines in fair value, distributions of earnings and additional investments.

The Company has received equity instruments in connection with agreements with certain partners. In such cases, the Company’s initial cost is determined based on the estimated fair value of the equity instruments received. Subsequent changes in the fair value of these equity instruments are accounted for in accordance with the investment policies noted above.

continued >>

## CheckFree Corporation and Subsidiaries

### notes\_to\_consolidated\_financial\_statements

**Other Financial Instruments** – On July 1, 2000, the Company adopted SFAS 133, “Accounting for Derivative Instruments and Hedging Activities,” as amended by SFAS 138, “Accounting for Certain Derivative Instruments and Certain Hedging Activities,” which requires that all derivative financial instruments be recognized as either assets or liabilities in the balance sheet. SFAS 133, as amended, requires the Company to recognize all derivatives on the balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value through income. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives are either offset against the change in fair value of assets, liabilities, or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative’s change in fair value is immediately recognized in earnings.

The Company’s Investment Policy currently prohibits the use of derivatives for trading or hedging purposes. Additionally, the Company completed a review of its contracts and determined that they contained no “imbedded derivatives” that require separate reporting and disclosure under SFAS 133, as amended. As such, the adoption of SFAS 133, as amended, did not have a material impact on the Company’s financial position or results of operations.

**Property and Equipment** – Property and equipment are stated at cost. Property and equipment are depreciated using the straight-line method over the estimated useful lives as follows: land improvements, building and building improvements, 15 to 30 years; computer equipment, software, and furniture, 3 to 7 years. Equipment under capital leases are amortized using the straight-line method over the lesser of their estimated useful lives or the terms of the leases. Leasehold improvements are amortized over the lesser of the estimated useful lives or remaining lease periods.

**Capitalized Software Costs** – On July 1, 1999, the Company adopted Statement of Position (“SOP”) 98-1, “Accounting for the Costs of Computer Software Developed or Obtained for Internal Use.” The Statement distinguishes accounting for costs of computer software developed or obtained for internal use from guidance under SFAS 86, “Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed.” The Company determines whether software costs fall under the provisions of SFAS 86 or SOP 98-1 and accounts for them as follows:

- *SFAS 86* – Software development costs incurred prior to the establishment of technological feasibility are expensed as incurred. Software development costs incurred after the technological feasibility of the subject software product has been established are capitalized in accordance with SFAS 86. Capitalized software costs are amortized on a product-by-product basis using the estimated economic life of the product on a straight-line basis over three to five years. Unamortized software development costs in excess of estimated future net revenues from a particular product are written down to estimated net realizable value.
- *SOP 98-1* – Software costs incurred in the preliminary project stage are expensed as incurred. Software costs incurred after the preliminary project stage is complete, management has committed to the project, and it is probable the software will be used to perform the function intended are capitalized in accordance with SOP 98-1. Capitalized software costs are amortized on a product-by-product basis using the estimated economic life of the product on a straight-line basis over three to five years. Capitalized software costs not expected to be completed and placed in service are written down to estimated net realizable value.

**Intangible Assets** – The costs of identified intangible assets are generally amortized on a straight-line basis over periods from 8 months to 10 years. Goodwill is amortized on a straight-line basis over 5 to 10 years. In accordance with SFAS 121, “Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of,” the Company periodically reviews long-lived assets, including identifiable intangibles and goodwill related to those assets, to evaluate whether events or changes in circumstances have occurred that would indicate that the carrying amount of the asset may not be recoverable. If this review indicates that the remaining useful life of goodwill or other intangible assets requires revision or that the asset is not recoverable, the carrying amount is reduced by the estimated shortfall of cash flows on a discounted basis.



**Basic and Diluted Earnings (Loss) Per Share** – The Company reports Basic and Diluted Earnings (Loss) Per Share in accordance with the provisions of SFAS 128, “Earnings Per Share.” Basic earnings (loss) per common share is determined by dividing income (loss) available to common shareholders by the weighted average number of common shares outstanding. Diluted per-common-share amounts assume the issuance of common stock for all potentially dilutive equivalent shares outstanding.

**Advertising Costs** – The Company expenses advertising costs as incurred in accordance with SOP 97-3, “Reporting on Advertising Costs.” Advertising expenses were not significant for the years ended June 30, 1999 and 2000. Advertising expense for the year ended June 30, 2001 was \$29,925,000 and includes \$25,000,000 provided to Bank of America in connection with the Strategic Agreement described in Note 3.

**Comprehensive Income** – Where applicable, the Company reports comprehensive income in accordance with SFAS 130, “Reporting Comprehensive Income.” The Statement requires disclosure of total non-shareowner changes in equity and its components. Total non-shareowner changes in equity include all changes in equity during a period except those resulting from investments by and distributions to shareowners. The components of other comprehensive income applicable to the Company would be unrealized holding gains or losses on the Company’s available-for-sale securities and certain transactions associated with derivative instruments. There were no available-for-sale securities held or derivative instrument transactions during the years ended June 30, 1999, 2000 and 2001. As a result, there were no components of comprehensive income applicable to the Company during the years ending June 30, 1999, 2000 and 2001.

**Business Segments** – The Company reports information about its business segments in accordance with SFAS 131, “Disclosures about Segments of an Enterprise and Related Information.” The Statement defines how operating segments are determined and requires disclosure of certain financial and descriptive information about a company’s operating segments. See Note 19 for the Company’s segment information.

**Foreign Currency Translation** – Effective with the acquisition of BlueGill Technologies, Inc. on April 28, 2000, certain wholly-owned subsidiaries of the Company have foreign operations. The financial statements of these foreign subsidiaries are measured using the US dollar as the functional currency. Assets, liabilities, revenues, and expenses are remeasured using current and historical exchange rates in accordance with SFAS 52, “Foreign Currency Translation.” Transaction gains and losses resulting from the remeasurement process are included in the determination of net income. The net transaction losses for the year ended June 30, 2001 and the period from April 28, 2000 to June 30, 2000 were not significant.

**Recent Accounting Pronouncements** – On July 20, 2001, the Financial Accounting Standards Board (FASB) issued SFAS 141, “Business Combinations” and SFAS 142, “Goodwill and Other Intangible Assets.” SFAS 141 requires all business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting. In addition, it requires application of the provisions of SFAS 142 for goodwill and other intangible assets related to any business combinations completed after June 30, 2001, but prior to the adoption date of SFAS 142. SFAS 142 changes the accounting for goodwill and other intangible assets. Upon adoption, goodwill will no longer be subject to amortization over its estimated useful life. Rather, goodwill will be subject to at least an annual assessment for impairment by applying a fair-value-based test. All other acquired intangibles will be separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the intangible asset can be sold, transferred, licensed, or exchanged, regardless of the Company’s intent to do so. Other intangibles will be amortized over their useful lives.

SFAS 142 becomes effective for the Company on July 1, 2002. The Company is still assessing the impact of all the Statement provisions on its financial position and results of operations, however, based on its review to date, the Company expects the following significant impacts:

- Upon adoption, the Company will be required to reclassify approximately \$2 million of unamortized workforce in place intangible assets into goodwill.

## CheckFree Corporation and Subsidiaries

### notes\_to\_consolidated\_financial\_statements

- Upon adoption, the balance of goodwill and workforce in place is expected to be \$624 million and the Company will discontinue amortizing these assets at that time. The resulting reduction in amortization expense is estimated at approximately \$200 million for each of the Company's fiscal years 2003 and 2004, and approximately \$192 million for the Company's 2005 fiscal year.
- The Company will be required to perform a transitional impairment test as of July 1, 2002. This impairment test will require the Company to (1) identify its reporting units, (2) determine the carrying value of each reporting unit by assigning assets and liabilities, including existing goodwill and intangible assets, to those reporting units, and (3) determine the fair value of each reporting unit. If the carrying value of any reporting unit exceeds its fair value, then the amount of any goodwill impairment will be determined through a fair value analysis of each of the assigned assets (excluding goodwill) and liabilities.

At this time, the Company does not anticipate any charge resulting from the transitional impairment test, however, due to the extensiveness of the efforts involved, that test has not yet been performed. Under the provisions of SFAS 142, the Company is required to complete the test before December 31, 2002.

- Following the transitional impairment test, the Company's goodwill balances will be subject to annual impairment tests using the same process described above. If any impairment is indicated as a result of the annual test, an impairment charge would be recorded as part of income from operations.

**Reclassifications** – Certain amounts in the prior years' financial statements have been reclassified to conform to the 2001 presentation.

#### Revenue Recognition

In 1999, the SEC issued Staff Accounting Bulletin ("SAB") 101, "Revenue Recognition in Financial Statements." The SAB provides guidance on the recognition, presentation and disclosure of revenue in financial statements filed with the SEC. Although SAB 101 does not change any of the existing accounting standards on revenue recognition, it draws upon existing rules and explains how the SEC staff applies these rules, by analogy, to other transactions that existing rules do not specifically address. SAB 101, as amended by SAB 101B, became effective for the fourth quarter of the Company's 2001 fiscal year. The adoption of SAB 101 did not have an impact on the Company's results of operations or financial position.

- *Processing and Servicing* – Processing and servicing revenues include revenues from transaction processing, electronic funds transfer and monthly service fees on consumer funds transfer services. The Company recognizes revenue when the services are performed.

As part of processing certain types of transactions, the Company earns interest from the time money is collected from its customers until the time payment is made to the applicable merchants. These revenues, which are generated from trust account balances not included on the Company's balance sheet, are included in processing and servicing and totaled \$11,846,000, \$21,485,000 and \$30,186,000 for the years ended June 30, 1999, 2000 and 2001, respectively.

- *License Fees* – The Company recognizes revenue on software transactions in accordance with SOP 97-2, "Software Revenue Recognition". In accordance with the provisions of SOP 97-2, the Company recognizes revenue from software license agreements when there is persuasive evidence that an arrangement exists, the fee is fixed and determinable, collectibility is probable and the software has been shipped, provided that no significant obligation remains under the contract.
- *Maintenance Fees* – Upon receipt of payment, maintenance fee revenue is recognized ratably over the term of the related contractual support period, generally 12 months.

- *Other* – Other revenue consists primarily of consulting and training services. Consulting revenue is recognized principally on a percentage-of-completion basis and training revenue is recognized upon delivery of the related service.

Estimated losses, if any, on contracts are provided for when probable. Estimated loss provisions are based on excess costs over the revenues earned from the contract. Credit losses, if any, are contemplated in the establishment of our allowance for doubtful accounts.

### Expense Classification

- *Processing, Servicing and Support* – Processing, servicing and support costs consist primarily of data processing costs, customer care and technical support, and third party transaction fees, which consist primarily of ACH transaction fees.
- *Research and Development* – Research and development expenses consist primarily of salaries and consulting fees paid to software engineers and business development personnel, and are reported net of applicable capitalized development costs.
- *Sales and Marketing* – Sales and marketing expenses consist primarily of salaries and commissions of sales employees, public relations and advertising costs, customer acquisition fees and royalties paid to distribution partners.
- *General and Administrative* – General and administrative expenses consist primarily of salaries for administrative, executive, finance, and human resource employees.
- *Depreciation and Amortization* – Depreciation and amortization on capitalized assets is recorded on a straight-line basis over the appropriate useful lives.
- *In-process Research and Development* – In-process research and development consists of charges resulting from acquisitions whereby the purchase price allocated to in-process software development was based on the determination that in-process research and development had no alternative future use after taking into consideration the potential for usage of the software in different products, resale of the software, or other internal use.

## NOTE 2. ACQUISITIONS AND DISPOSITIONS

### TransPoint

On September 1, 2000, the Company acquired MSFDC, L.L.C. (TransPoint) for a total of \$1.4 billion, consisting of 17,000,000 shares of common stock valued at \$1.4 billion and \$2 million of acquisition costs. The acquisition was treated as a purchase for accounting purposes, and, accordingly, the assets and liabilities were recorded based on their fair values at the date of the acquisition. The values ascribed to acquired intangible assets and their respective future lives are as follows:

	Intangible Asset	Useful Life
	(In thousands)	
Goodwill	\$ 780,545	5.0 yrs
Strategic agreements	495,000	5.0 yrs
Existing product technology	209,300	3.0 yrs
Customer list	29,000	3.0 yrs
Tradename	28,300	1.0 yr

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## CheckFree Corporation and Subsidiaries

### notes\_to\_consolidated\_financial\_statements

Amortization of intangible assets is on a straight-line basis over the assets' respective useful life. TransPoint's operations are included in the consolidated statements of operations from the date of acquisition.

At the acquisition date, TransPoint had four technologies under development that had not demonstrated technological feasibility. These technologies include Biller Integration System and Communications, Service Center, Delivery Applications and Payment Systems Interface. The in-process technologies have no alternative use in the event that the proposed technologies do not prove to be feasible. These development efforts fall within the definition of In-Process Research and Development ("IPR&D") contained in SFAS 2.

**BIS/Communications Technology** – The Biller Integration System ("BIS") is provided to the biller to run on-site and supplies the web-hosting for the biller. The BIS helps implement the templates and develop the look and feel for marketing components. The BIS also includes automation interfaces, EI interfaces, and the console. The following features of the BIS/Communications technology were under development:

- Remote access or the Remote BIS Console, which will allow Biller operators and administrators to perform selected gateway operations from remote machines using a Web-based interface to the BIS;
- International enhancements, which are fixes to the BIS system to correct incompatibilities with international currency and date settings; and
- Platform updates that will support installation of the BIS gateway on the Windows 2000 Server platform.

**Service Center Technology** – The Service Center connects the TransPoint servers to the BIS on the biller site, the automated clearinghouse, other third-party servers, and the individual consumer. The Service Center includes the database and operational functions as well. The following features of the Service Center were under development:

- E-mail notification currently uses an internal Microsoft server. The system is being modified to incorporate the industry standard allowing the use of any server environment to send data over the Internet. In addition, service-generated e-mail messages will be in HTML format (rather than plain text) for a richer customer experience.
- SysAdmiral upgrade, in which the installation scripts for the service center are being upgraded to support the latest version of SysAdmiral.

**Delivery Applications** – The Delivery Applications generate the actual web pages through its user interface. This technology creates not only the TransPoint consumer site, but also the operations, corporate, and support sites. The following features of the Delivery Applications were under development:

- Passport Integration/Authorization, in which the security and authentication systems of the TransPoint service will be modified to use Microsoft Passport for user authentication. In addition, the user interface will be modified to allow migration of existing user accounts to Microsoft Passport.
- User Registration Improvement, in which consumer registration is being modified significantly, with the goal of retaining new consumers. Changes include sending consumers to the Microsoft Passport Web site to obtain a Passport account, and condensing the number of screens in registration. In addition, new consumers are permitted greater access to the system and features as they await identity and payment account verification.
- Recurring Payments, whereby consumers will now be able to set up automatic "pay anyone" payments recurring at set intervals, and automatic rules-based handling of electronic bills by payee.
- Batch Enabling, whereby biller operators and administrators will now be able to enable statement batches directly from the TransPoint Operations site. A new "Enable Batch" button will be added to the Preview Statements screen on the TransPoint Operations site.

- Reporting Upgrades, in which a variety of user-interface upgrades are underway to improve performance of the reporting subsystem, improve the reporting content available to billers, and increase the overall reliability of the TransPoint system.
- Payment Center User Interface Improvements, which includes a variety of user interface improvements to fix minor UI issues, enhance accessibility options, and improve overall site usability.

**Payment/Interface** – The Payment/Interface technology connects the Service Center to the ACH, Original Depository Financial Institutions, and other third-party servers as well as processing all payment and settlement information. The following features of the Payment/Interface technology were under development:

- Microsoft Money Download, in which this feature is being rearchitected and reimplemented in its entirety to correct incompatibilities between the existing Microsoft Money download feature and the newest version of Microsoft Money.
- Credit Card Payments, which provides code that allows the TransPoint system to support the use of credit cards for payment settlement.

There are risks and uncertainties associated with the completion of these in-process technologies. These risks include:

- *Not Technologically Feasible.* The acquired IPR&D had not demonstrated technological or commercial feasibility as of the transaction date for TransPoint. Significant risks exist because TransPoint is unsure of the obstacles it will encounter in the form of market acceptance, time and cost necessary to produce a technologically feasible product. SFAS No. 2 does not specifically require an analysis of the development effort expended relative to an acquisition date. It is reasonable to assume, however, that an IPR&D project would require a significant amount of time and cost in order to modify for the Company's use in the marketplace. Should the proposed technology fail to become viable, it is unlikely that the Company would realize any value from the sale of the technology to another party.
- *No Alternative Future Use.* The acquired IPR&D consists of TransPoint's work to date on its products. The products are very specific to the tasks and markets for which it is intended. As is typically the case with software, there are no alternative uses for the in-process work in the event that the product does not become feasible for the Company. The development effort for the acquired IPR&D does not possess an alternative future use for the Company under the terms of SFAS No. 2.

If the TransPoint project underway fails, there will be very limited life to the existing product because the continuing pace of technological developments in the marketplace will have rendered them non-competitive. In the event of a failure, the technology acquired, as embodied in either current or in-process products, will have no alternative use and would be written off as a loss by the Company.

The following table represents information regarding the status of the various in-process research and development projects acquired (as of the date of acquisition):

	Estimated Stage of Completion	Estimated Completion Date	Expected Cost to Complete	Valuation
(In thousands)				
BIS/Communications	80%	October 2000	\$ 100	\$ 1,200
Service Center	80%	October 2000	121	5,900
Delivery Applications	80%	October 2000	396	9,500
Payment/Interface	80%	October 2000	100	2,000
Total			\$ 717	\$ 18,600

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## CheckFree Corporation and Subsidiaries

### notes\_to\_consolidated\_financial\_statements

The method used to allocate the purchase consideration to IPR&D was the modified income approach. Under the income approach, fair value reflects the present value of the projected free cash flows that will be generated by the IPR&D projects and that is attributable to the acquired technology, if successfully completed. The modified income approach takes the income approach, modified to include the following factors:

- analysis of the stage of completion of each project;
- exclusion of value related to research and development yet-to-be completed as part of the on going IPR&D projects; and
- the contribution of existing technologies and applications.

The projected revenues used in the income approach are based upon the incremental revenues associated with a portion of the project related to TransPoint's technology likely to be generated upon completion of the project and the beginning of commercial sales, as estimated by management. The projections assume that the projects will be successful and the projects' development and commercialization are as set forth by management. The discount rate used in this analysis is an after tax rate of 24%.

#### BlueGill

On April 28, 2000, the Company acquired BlueGill Technologies, Inc. ("BlueGill") for a total of \$239.9 million, consisting of 4,713,736 shares of common stock valued at \$221.5 million, the issuance of 637,746 employee stock options valued at \$18.5 million and \$0.6 million of acquisition costs less \$0.7 million of cash received for the release of shares placed in escrow per the merger agreement. The acquisition was treated as a purchase for accounting purposes, and, accordingly, the assets and liabilities were recorded based on their fair market values at the date of the acquisition. The values ascribed to acquired intangible assets and their respective useful lives are as follows:

	Intangible Asset (In thousands)	Useful Life
Goodwill	\$ 191,072	5.0 yrs
Tradename	15,100	1.0 yrs
Existing product technology	13,700	3.7 yrs
Customer list	10,600	5.0 yrs
Workforce in place	2,600	3.0 yrs
Covenants not to compete	1,200	1.0 yr

Amortization of intangible assets is on a straight-line basis over the assets' respective useful life. BlueGill's operations are included in the consolidated statements of operations from the date of acquisition.

In connection with the acquisition of BlueGill, the Company recorded a charge of \$6.9 million for purchased IPR&D. This charge related to five technologies which had not demonstrated technological or commercial feasibility as of the transaction date. They were print and extraction technology, data management engine technology, API technology, web application technologies and payment/OFX technology. As of the acquisition date, the Company estimated that these projects ranged from 10% to 50% complete, that an aggregate of \$2.1 million would be required to complete these five projects, and that, depending upon the project, product revenues would begin in mid to late 2000. An after-tax discount rate of 25% was used in this analysis. As of June 30, 2001, these projects were substantially complete.

## Mobius

On March 8, 1999, the Company acquired Mobius Group, Inc. ("Mobius Group") for a total of \$19.1 million, consisting of 537,314 shares of common stock valued at \$18 million, \$0.2 million of acquisition costs, and \$0.9 million of assumed debt. The acquisition was treated as a purchase for accounting purposes, and, accordingly, the assets and liabilities were recorded based on their fair values at the date of the acquisition. The values ascribed to acquired intangible assets and their respective useful lives are as follows:

	<b>Intangible Asset</b>	<b>Useful Life</b>
	<b>(In thousands)</b>	
Goodwill	\$ 10,552	10.0 yrs
Customer base	4,429	8.0 yrs
Tradenames	3,709	10.0 yrs
Existing product technology	1,864	5.0 yrs
Workforce	940	3.0 yrs

Amortization of intangible assets is on a straight-line basis over the assets' respective useful life. Mobius Group's operations are included in the consolidated statements of operations from the date of acquisition.

At the acquisition date, Mobius Group had four products under development that had not demonstrated technological or commercial feasibility. These products included M-Plan Retirement & Estate Planning Modules, M-Plan Cash Flow, Tax and Education Planning Modules, new version of M-Search and a new version of M-Vest. As of the acquisition date, the Company estimated that these projects ranged from 20% to 92% complete, that an aggregate of \$0.7 million would be necessary to complete these four projects, and product revenues would begin on dates ranging from May 1999 to December 1999. An after-tax discount rate of 20% was used in this analysis. As of June 30, 2001, these projects were substantially complete.

## Pro Forma Information

The unaudited pro forma results of operations of the Company for the years ended June 30, 2000 and 2001, assuming the acquisitions occurred at the beginning of each period are as follows (in thousands):

	<b>Year Ended June 30,</b>	
	<b>2000</b>	<b>2001</b>
Total revenues	\$ 316,830	\$ 433,329
Net income (loss)	\$ (406,582)	\$ (402,193)
Basic and Diluted earnings per share:		
Net income (loss) per common share	\$ (5.42)	\$ (4.80)
Equivalent number of shares	75,078	83,797

This information is presented to facilitate meaningful comparisons to on going operations and to other companies. The unaudited pro forma amounts above do not include a charge for in-process research and development of \$18.6 million arising from the TransPoint acquisition in 2001 and \$6.9 million arising from the BlueGill acquisition in 2000. The unaudited pro forma information is not necessarily indicative of the actual results of operations had the transactions occurred at the beginning of the periods presented, nor should it be used to project the Company's results of operations for any future periods.

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## CheckFree Corporation and Subsidiaries

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#### Dispositions

On October 1, 1998 the Company sold certain software and other assets related to its imaging line of business for \$0.8 million consisting of a note receivable of \$0.5 million and future services of \$0.3 million. Loss on the sale amounted to \$2.9 million.

On September 11, 1998 the Company sold certain software and other assets related to its mortgage line of business for \$19.1 million, net of a working capital adjustment. As part of the sales agreement, the Company retained responsibility for certain customer obligations and agreed to subcontract with the acquiring company to perform consulting services at retail hourly rates for these retained obligations. The Company received cash of \$15 million, net of \$4.0 million of prepaid subcontract services due the acquiring company. Net gain on the sale amounted to \$6.4 million.

The gain or loss on sale of assets described above is included in Net Gain on Dispositions of Assets in the Company's Consolidated Statements of Operations.

#### NOTE 3. STRATEGIC AGREEMENT

Effective October 1, 2000, the Company completed a previously announced 10-year strategic agreement with Bank of America, whereby the Company acquired the electronic billing and payment assets of Bank of America and will provide electronic billing and payment services to Bank of America's customer base in exchange for 10 million shares of the Company's common stock valued at approximately \$253 million and \$35 million of cash. Of the cash portion of the purchase price, \$25 million was provided to help support an agreed upon two year \$45 million marketing campaign by Bank of America. Because the Company cannot directly impact the specific nature, timing or extent of the use of the marketing funds, the entire \$25 million was expensed upon completion of the agreement. This amount is included in sales and marketing expense in the accompanying consolidated statement of operations for the year ended June 30, 2001.

The values ascribed to intangible assets acquired as a result of the agreement and their respective useful lives are as follows:

	Intangible Asset	Useful Life
	(In thousands)	
Strategic agreement	\$ 249,424	10.0 yrs
Existing product technology	7,659	1.5 yrs
Workforce	3,173	3.0 yrs

The agreement provides for a revenue guarantee of \$500 million to the Company over the next 10 years. Bank of America also has the ability to earn warrants on up to 10 million additional shares upon achievement of certain milestones more fully described in Note 16.



As a result of the agreement, as of June 30, 2001, Bank of America owns 11.5% of the Company. The following amounts related to Bank of America are included in the Company's consolidated financial statements for the periods indicated (in thousands):

	June 30,	
	2000	2001
Current assets:		
Accounts receivable, net	\$ 2,219	\$ 9,655
Total current assets	\$ 2,219	\$ 9,655
Current liabilities:		
Accounts payable	\$ -	\$ 5,983
Accrued liabilities	-	2,111
Deferred revenues	241	477
Total current liabilities	\$ 241	\$ 8,571

	Year Ended June 30,		
	1999	2000	2001
Revenues:			
Processing and servicing	\$ 10,369	\$ 14,796	\$ 42,503
License fees	109	2	1,187
Maintenance fees	112	209	460
Other	122	142	337
Total revenues	\$ 10,712	\$ 15,149	\$ 44,487
Expenses:			
Cost of processing, servicing and support	\$ -	\$ -	\$ 23,154
Sales and marketing	-	-	25,000
Total expenses	\$ -	\$ -	\$ 48,154

Revenues and accounts receivable relate primarily to electronic billing and payment services provided to Bank of America. Accounts payable, accrued liabilities and cost of processing expenses relate to reimbursements to Bank of America in connection with a transition services agreement in place while the Company completes the conversion of Bank of America customers to its processing platform.

#### NOTE 4. INVESTMENTS

Investments consist of the following (in thousands):

	June 30,	
	2000	2001
Held-to-Maturity	\$ 162,989	\$ 239,507
Trading	6,660	-
Other investments	11,171	3,296
Less: Amounts classified as cash equivalents	(101,269)	(110,831)
Total investments	\$ 79,551	\$ 131,972

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The following is a summary of Held-to-Maturity investment securities (in thousands):

	Amortized Cost	Gross Unrealized		Fair Value
		Gains	Losses	
<b>June 30, 2000:</b>				
Corporate bonds	\$ 50,824	\$ -	\$ (148)	\$ 50,676
Asset-backed securities	-	-	-	-
Commercial paper	68,886	211	-	69,097
Certificates of deposit	29,981	-	(86)	29,895
U.S. Government and federal agency obligations	2,824	4	(18)	2,810
Money market funds	10,474	-	-	10,474
Held-to-Maturity investments	162,989	215	(252)	162,952
Less: amounts classified as cash equivalents	(101,269)	(215)	19	(101,465)
<b>Total Held-to-Maturity Investments</b>	<b>\$ 61,720</b>	<b>\$ -</b>	<b>\$ (233)</b>	<b>\$ 61,487</b>
<b>June 30, 2001:</b>				
Corporate bonds	\$ 75,627	\$ 226	\$ (404)	\$ 75,449
Asset-backed securities	29,259	74	-	29,333
Commercial paper	51,186	43	(9)	51,220
Certificates of deposit	-	-	-	-
U.S. Government and federal agency obligations	22,466	254	-	22,720
Money market funds	60,969	-	-	60,969
Held-to-Maturity investments	239,507	597	(413)	239,691
Less: amounts classified as cash equivalents	(110,831)	-	-	(110,831)
<b>Total Held-to-Maturity Investments</b>	<b>\$ 128,676</b>	<b>\$ 597</b>	<b>\$ (413)</b>	<b>\$ 128,860</b>

The fair value of Held-to-Maturity securities is based on quoted market values.

The amortized cost and fair value of held-to-maturity investment securities at June 30, 2001 by contractual maturity or repricing date are as follows (in thousands):

	Amortized Cost	Fair Value
Due in one year or less	\$ 35,930	\$ 36,097
Due after one year through five years	92,746	92,763
	<b>\$ 128,676</b>	<b>\$ 128,860</b>

Expected maturities may differ from contractual maturities because debt issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

Other investments are accounted for under the cost method and include the following (in thousands):

	June 30,	
	2000	2001
Common stock and warrants	\$ 11,171	\$ 2,198
Convertible debenture	-	1,000
Preferred stock	-	98
<b>Total other investments</b>	<b>\$ 11,171</b>	<b>\$ 3,296</b>

Common stock and warrants consist primarily of the Company's strategic investment in BillServ.com common stock, which is subject to certain trading restrictions. The remainder of common stock and warrants, convertible debenture, and preferred stock investments are in non-publicly traded e-billing related companies. The convertible debenture bears interest at 6.5% per annum and is payable in full on September 12, 2003. Interest is paid on December 31 and June 30 each year. The debenture agreement allows the Company, at its option, to convert the note into common shares of the issuer, the number of which is dependent upon the valuation of the issuer at that time. Conversion into common stock is automatic if the issuer completes an initial public offering.

During the year ended June 30, 2001, the Company recorded a loss on certain of its investments accounted for under the cost method. The loss was the result of the Company's evaluation of any other-than-temporary decline in the value of these investments. In performing this evaluation the Company considered various factors including any decline in market price, where available, the investee's financial condition, results of operations, operating trends and other financial ratios. Based on these factors, the Company recorded a loss of \$16,077,000.

## **NOTE 5. ACCOUNTS RECEIVABLE**

Accounts receivable consist of the following (in thousands):

	June 30,	
	2000	2001
Trade accounts receivable	\$ 46,609	\$ 76,973
Unbilled trade accounts receivable	10,302	8,875
Other receivables	5,400	5,933
Total	62,311	91,781
Less allowance for doubtful accounts	4,003	2,963
Accounts receivable, net	\$ 58,308	\$ 88,818

Trade accounts receivable represents amounts billed to customers. Revenue is recognized and customers are billed under service agreements as the services are performed. Unbilled trade accounts receivable result primarily from extended payment terms on software license agreements. For software contracts, revenue is recognized under the provisions of SOP 97-2 as described in Note 1, and unbilled amounts under those software contracts are billed on specific dates according to contractual terms. Other receivables are comprised primarily of interest receivable and amounts due from employees for travel and other advances. The allowance for doubtful accounts represents management's estimate of uncollectible accounts receivable.

## **NOTE 6. INCOME TAXES**

The Company accounts for income taxes in accordance with SFAS 109, "Accounting for Income Taxes," which requires an asset and liability approach to financial accounting and reporting for income taxes. In accordance with SFAS 109, deferred income tax assets and liabilities are computed annually for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Income tax expense (benefit) is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities.

The Company's income tax benefit consists of the following (in thousands):

	Year Ended June 30,		
	1999	2000	2001
Current:			
Federal	\$ (10,555)	\$ -	\$ -
State and local	(2,308)	-	-
Total current	(12,863)	-	-
Deferred federal and state	854	(11,437)	(115,362)
Total income tax benefit	\$ (12,009)	\$ (11,437)	\$ (115,362)

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Income tax expense differs from the amounts computed by applying the U.S. federal statutory income tax rate of 35% to income before income taxes as a result of the following (in thousands):

	Year Ended June 30,		
	1999	2000	2001
Computed "expected" tax benefit	\$ (543)	\$ (15,315)	\$ (167,243)
Nondeductible in-process research and development of acquired businesses	770	2,415	6,510
Nondeductible intangible amortization	1,137	3,572	60,346
State and local taxes, net of federal income tax benefits	(1,741)	(1,636)	(14,917)
Loss from medical benefits subsidiary	(10,665)	-	-
Other, net	(967)	(473)	(58)
Total income tax benefit	\$ (12,009)	\$ (11,437)	\$ (115,362)

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at June 30, 2000 and 2001 are as follows (in thousands):

	June 30,	
	2000	2001
Deferred tax assets:		
Federal and state net operating loss carryforwards	\$ 32,219	\$ 72,972
Federal and state tax credit carryforwards	3,867	4,300
Allowance for bad debts and returns	1,774	1,278
Accrued compensation and related items	5,429	1,420
Stock warrants	19,331	21,484
Property and equipment	-	602
Other investments	-	3,335
Deferred revenue	-	2,749
Reserve accruals	3,558	8,172
Total deferred tax assets	66,178	116,312
Deferred tax liabilities:		
Capitalized software	(12,792)	(69,864)
Property and equipment	(1,850)	-
Deferred revenue	(49)	-
Intangible assets	(11,526)	(174,482)
Prepaid expenses	(980)	(94)
Total deferred tax liabilities	(27,197)	(244,440)
Net deferred tax asset (liabilities)	\$ 38,981	\$ (128,128)

At June 30, 2001, the Company has approximately \$187,693,000 of state and \$181,672,000 of federal net operating loss carryforwards available, expiring in 2009 to 2015 and 2009 to 2021, respectively. Additionally, at June 30, 2001, the Company has approximately \$812,000 of state and \$3,723,000 of federal tax credit carryforwards available, expiring in 2008 to 2011 and 2009 to 2021, respectively.

The realization of the Company's deferred tax assets, which relate primarily to net operating loss carryforwards and temporary differences is dependent on generating sufficient taxable income in future periods. Although realization is not assured, management believes it is more likely than not that the net deferred tax assets will be realized.

**NOTE 7. PROPERTY AND EQUIPMENT**

The components of property and equipment are as follows (in thousands):

	June 30,	
	2000	2001
Land and land improvements	\$ 4,944	\$ 4,944
Building and building improvements	39,992	50,732
Computer equipment and software licenses	101,662	132,850
Furniture and equipment	14,071	16,894
Total	160,669	205,420
Less accumulated depreciation and amortization	67,455	96,194
Property and equipment, net	\$ 93,214	\$ 109,226

Depreciation expense totaled \$17,801,000, \$22,915,000 and \$30,442,000 for the years ended June 30, 1999, 2000 and 2001, respectively.

**NOTE 8. INTANGIBLE ASSETS**

The components of the Company's various intangible assets are as follows (in thousands):

	June 30,	
	2000	2001
Capitalized Software:		
Product technology from acquisitions and strategic agreement	\$ 35,427	\$ 252,378
Internal development costs	16,799	21,771
Total	52,226	274,149
Less: accumulated amortization	15,037	87,128
Capitalized software, net	\$ 37,189	\$ 187,021
Goodwill:		
Goodwill	\$ 230,550	\$ 1,009,834
Less: accumulated amortization	17,245	189,665
Goodwill, net	\$ 213,305	\$ 820,169
Strategic agreements:		
Strategic agreements	\$ -	\$ 744,424
Less: accumulated amortization	-	101,212
Strategic agreements, net	\$ -	\$ 643,212
Other intangible assets:		
Workforce	\$ 8,771	\$ 11,944
Tradenames	19,668	47,968
Customer base	16,358	45,358
Covenants not to compete	1,200	1,200
Total	45,997	106,470
Less accumulated amortization	8,022	59,352
Other intangible assets, net	\$ 37,975	\$ 47,118

Significant additions to intangible assets resulted from the acquisitions and strategic agreement described in Notes 2 and 3, respectively.

Amortization of intangible assets totaled \$6,829,000, \$19,915,000 and \$397,053,000 for the years ended June 30, 1999, 2000 and 2001, respectively.

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#### NOTE 9. ACCRUED LIABILITIES

The components of accrued liabilities are as follows (in thousands):

	June 30,	
	2000	2001
Compensation and benefits	\$ 25,288	\$ 33,141
Other	18,670	26,949
Total	\$ 43,958	\$ 60,090

#### NOTE 10. LINE OF CREDIT

On October 25, 1999, the Company executed an amendment to its existing working capital line-of-credit agreement. The amendment extended the term of the line through December 31, 1999, and changed certain financial covenants contained in the agreement.

In January 2000, the Company completed a new line-of credit agreement, which matures on December 30, 2002. The agreement, which carries an interest rate of LIBOR plus 200 basis points or Prime, enables the Company to borrow up to \$30 million and contains certain financial and operating covenants.

On February 20, 2001, the Company executed an amendment to the working capital line-of-credit agreement dated January 2000 to extend the term of the line through December 30, 2003. In addition, certain financial covenants contained in the agreement were changed to reflect acquisitions made during the fiscal year.

No amounts were outstanding under the line at June 30, 2000 and 2001.

#### NOTE 11. CONVERTIBLE SUBORDINATED NOTES

On November 29, 1999, the Company issued \$172.5 million of 6.5% convertible subordinated notes that are due on December 1, 2006. Interest on the notes is payable on June 1 and December 1 of each year, commencing June 1, 2000. The notes may be converted, at the holder's option, into 13.6612 shares of common stock per \$1,000 of note value and the Company may redeem the notes at any time on or after December 1, 2002. At June 30, 2001, none of the notes had been converted to common stock. Interest expense on the notes for the years ended June 30, 2000 and 2001 was \$7,307,000 and \$12,119,000, respectively.

#### NOTE 12. OBLIGATIONS UNDER CAPITAL LEASES

During 1993, the Company entered into a 20-year lease with the Department of Development of the State of Ohio for land and an office building located in Columbus, Ohio. The Company had the option to purchase the land and building for \$1 at the termination of the lease and thus, the Company recorded the transaction as a capital lease. In June 1999, the Company completed a tax-free exchange of property involving the land and building under this capital lease. In order to exercise its purchase option and complete the transaction, the Company paid \$2.5 million of principal obligations under the lease, and placed an additional \$3.6 million in escrow. The Company and the State of Ohio entered into an escrow agreement whereby the funds deposited were used to make scheduled principal and interest payments through September 1, 2000, and retire the remaining principal obligation at that date. The net gain resulting from the sale of the property amounted to \$1.1 million and is included in the Net Gain on Dispositions of Assets in the Company's 1999 Consolidated Statement of Operations. Amounts deposited with the escrow trustee are included in current and noncurrent assets and liabilities, based on the respective principal repayment dates, in the Company's June 30, 2000 Consolidated Balance Sheet.

The Company also leases certain equipment and software licenses under capital leases. The Company is required to pay certain taxes, insurance and other expenses related to the leased property.

The following is a summary of property under capital leases included in the accompanying consolidated balance sheets (in thousands):

	June 30,	
	2000	2001
Equipment and software licenses	\$ 3,654	\$ 8,122
Less accumulated depreciation and amortization	2,585	3,190
Property under capital leases, net	\$ 1,069	\$ 4,932

Future minimum lease payments required by the capital leases and the net future minimum lease payments are as follows (in thousands):

Fiscal Year Ending June 30,		
2002		\$ 1,610
2003		1,610
2004		1,610
2005		1,364
2006		177
Thereafter		-
Total future minimum lease payments		6,371
Less amount representing interest		1,231
Net future minimum lease payments		\$ 5,140

### NOTE 13. OPERATING LEASES

The Company leases certain office space and equipment under operating leases. Certain leases contain renewal options and generally provide that the Company shall pay for insurance, taxes and maintenance. In addition, certain leases include rent escalations throughout the terms of the leases. Total expense under all operating lease agreements for the years ended June 30, 1999, 2000 and 2001, was \$13,413,000, \$19,095,000 and \$26,519,000, respectively.

Minimum future rental payments under these leases are as follows (in thousands):

Fiscal Year Ending June 30,		
2002		\$ 23,625
2003		20,159
2004		14,465
2005		8,866
2006		8,077
Thereafter		44,703
Net future minimum lease payments		\$ 119,895

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#### NOTE 14. EMPLOYEE BENEFIT PLANS

**Retirement Plan** – The Company has a defined contribution 401(k) retirement plan covering substantially all of its employees. Under the plan eligible employees may contribute a portion of their salary until retirement and the Company, at its discretion, may match a portion of the employee's contribution. Total expense under the plan amounted to \$1,218,000, \$2,886,000 and \$3,528,000, for the years ended June 30, 1999, 2000 and 2001, respectively.

**Deferred Compensation Plan** – In January 1999, the Company established a deferred compensation plan (the "DCP") covering highly compensated employees as defined by the DCP. Under the plan, eligible employees may contribute a portion of their salary on a pre-tax basis. The DCP is a non-qualified plan, therefore the associated liabilities are included in the Company's June 30, 2000 and 2001 Consolidated Balance Sheets. In addition, the Company has established a rabbi trust to finance obligations under the DCP with corporate-owned life insurance policies on participants. The cash surrender value of such policies is also included in the Company's June 30, 2000 and 2001 Consolidated Balance Sheets. Total expense under the DCP for the periods ended June 30, 2000 and 2001 amounted to \$162,000 and \$77,000, respectively.

**Group Medical Plans** – Effective January 1, 2000, the Company converted all of its employees to a group medical self-insurance plan. The Company has employed an administrator to manage this plan. Under terms of this plan, both the Company and eligible employees are required to make contributions. The administrator reviews all claims filed and authorizes the payment of benefits. The Company has stop-loss insurance coverage on all individual claims exceeding \$150,000. Prior to January 1, 2000, the Company had a group medical self-insurance plan covering certain of its employees, and medical insurance coverage under managed care health plans covering the remaining employees. Total expense for medical insurance coverage amounted to \$4,430,000, \$7,359,000, and \$11,116,000 for the years ended June 30, 1999, 2000 and 2001, respectively. Under the self-insurance plans, the Company expenses amounts as claims are incurred and recognizes a liability for incurred but not reported claims. At June 30, 2000 and 2001, the Company accrued \$2,513,000 and \$4,061,000, respectively, as a liability for costs incurred but not paid under these plans.

In December 1998, a subsidiary, CheckFree Management Corporation, was created to administer the Company's employee medical benefits program. The Company owns a controlling interest in the subsidiary, and therefore, the accompanying consolidated financial statements include the subsidiary's results of operations.

#### NOTE 15. CAPITAL STOCK

On November 1, 2000, the Company's stockholders approved an increase in the number of authorized shares of the Company from 165,000,000 to 550,000,000, consisting of 500,000,000 shares of common stock, \$.01 par value, 48,500,000 shares of preferred stock, \$.01 par value, and 1,500,000 shares of Series A Junior Participating Cumulative Preferred Stock, \$.01 par value. The preferred stock may be issued in one or more series and may be established with such relative voting, dividend, redemption, liquidation, conversion and other powers, preferences, rights, qualifications, limitations and restrictions as the Board of Directors may determine without further stockholder approval. No preferred shares have been issued.

In January 1997, the Company's Board of Directors declared a dividend distribution of Preferred Share Purchase Rights to protect its stockholders in the event of an unsolicited attempt to acquire the Company. On February 14, 1997, the Rights were issued to the Company's stockholders of record, with an expiration date of 10 years. Until a person or group acquires 15% or more of the Company's Common Stock, the Rights will automatically trade with the shares of Common Stock. Only when a person or group has acquired 15% or more of the Company's Common Stock, will the Rights become exercisable and separate certificates issued. Prior to the acquisition by a person or group of beneficial ownership of 15% or more of the Company's Common Stock, the Rights are redeemable for \$.001 per Right at the option of the Board of Directors.



## NOTE 16. TRANSACTIONS INVOLVING EQUITY INSTRUMENTS

### Employee Plans

During 1995, the Company adopted the 1995 Stock Option Plan (the “1995 Plan”). The 1995 Plan replaces in its entirety the 1993 Stock Option Plan (the “1993 Plan”). The options granted under the 1995 and 1993 Plans may be either incentive stock options or non-statutory stock options. The terms of the options granted under the 1995 and 1993 Plans are at the sole discretion of a committee of members of the Company’s Board of Directors, not to exceed ten years. Generally, options vest at either 33% or 20% per year from the dated of grant. The 1995 Plan originally provided that the Company may grant options for not more than 5,000,000 shares of common stock to certain key employees, officers and directors. In November of 1998 and again in November of 2000, the 1995 Plan was amended by a vote of the Company’s shareholders to extend the maximum option grants to not more than 8,000,000 shares and not more than 12,000,000 shares, respectively. Options granted under the 1995 and 1993 Plans are exercisable according to the terms of each option, however, in the event of a change in control or merger as defined, the options shall become immediately exercisable. At June 30, 2001, 4,100,085 additional shares are available for grant in the aggregate for all Plans.

Previously, the Company had adopted the 1983 Incentive Stock Option Plan and the 1983 Non-Statutory Stock Option Plan (collectively, the “1983 Plans”), which provided that the Board of Directors may grant options for shares of common stock to certain employees and directors. Under the terms of the 1983 Plans, options are exercisable over a period up to ten years from the grant date. In the event the Company is sold, options outstanding under the 1983 Plans must be repurchased at a price calculated as if the options had been fully exercised.

All options granted under the 1983 Plans, the 1993 Plan and the 1995 Plan were granted at exercise prices not less than the fair market value of the underlying common stock at the date of grant. In the event that shares purchased through the exercise of incentive stock options are sold within one year of exercise, the Company is entitled to a tax deduction. The tax benefit of the deduction is not reflected in the consolidated statements of operations but is reflected as an increase in additional paid-in capital.

The following table summarizes stock option activity from July 1, 1998 to June 30, 2001:

	Year Ended					
	June 30, 1999		June 30, 2000		June 30, 2001	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding – Beginning of period	4,365,562	\$ 15.23	5,196,600	\$ 18.69	6,161,785	\$ 30.86
Granted	1,575,057	36.40	1,476,957	74.45	2,049,049	46.71
Assumed with BlueGill acquisition	-	-	637,746	4.31	-	-
Exercised	(354,758)	4.56	(794,778)	12.32	(635,205)	10.92
Cancelled	(389,261)	16.12	(354,740)	27.16	(447,488)	34.24
Outstanding – End of period	5,196,600	\$ 18.69	6,161,785	\$ 30.86	7,128,141	\$ 36.96
Options exercisable at end of period	1,394,269	\$ 9.00	1,850,887	\$ 13.58	2,588,418	\$ 26.40
Weighted average per share value of options granted during the year		\$ 17.65		\$ 48.16		\$ 32.06

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The following table summarizes information about options outstanding at June 30, 2001:

Range of Exercise Price	Options Outstanding			Options Exercisable	
	Weighted Average			Weighted Average	
	Number	Remaining Contractual Life	Exercise Price	Number	Exercise Price
\$ 0.01 - \$ 15.00	2,401,968	5.5	\$ 8.55	1,353,596	\$ 6.16
\$15.01 - \$ 30.00	461,833	6.7	22.24	308,218	22.49
\$30.01 - \$ 60.00	3,467,498	8.8	45.24	702,933	43.95
\$60.01 - \$ 90.00	275,050	8.6	77.43	48,070	79.54
\$90.01 - \$120.00	521,792	8.5	104.50	175,601	104.50
	7,128,141		\$ 36.96	2,588,418	\$ 26.40

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in the years ended June 30, 1999, 2000 and 2001, respectively: dividend yield of 0% in all periods; expected volatility of 49%, 83% and 98%; risk-free interest rates of 5.87%, 6.30%, and 5.62%; and expected lives of two to seven years.

The Company agreed to assume responsibility for the 1997 and 1998 Employee Incentive Stock Option Plans of BlueGill Technologies, Inc. in conjunction with the acquisition of BlueGill in April 2000. All outstanding options were converted to equivalent CheckFree options as specifically prescribed in the Asset Purchase Agreement. The fair value of the options assumed of \$18.5 million was estimated on the acquisition date using the Black-Scholes option pricing model with the following weighted-average assumptions used: dividend yield of 0%, expected volatility of 83%; risk-free interest rate of 6.60% and expected lives of one half to seven years. The estimated fair value of the assumed option plans was added to the fair value of Company stock issued in determining the purchase price of BlueGill.

In September 1998, the Company offered an option repricing program to its employees. Under the terms of the offer, employees had one week to return any outstanding option grant in its entirety and replace it on a share-for-share basis for an option grant with an exercise price equal to the fair market value of the Company's Common Stock at the new grant date. Only those exchanges received within one day of the designated grant date were accepted and any vested options in such returned grants were forfeited. The lives of returned historical grants typically ranged from three to five years with straight line vesting beginning one year from the original grant date. All newly issued option grants had a life of five years with vesting to occur at 40% beginning two years from the new grant date and 20% for each year thereafter. A total of 1,418,403 options were returned and had the offer taken place at June 30, 1998, the options exercisable would have decreased by 95,614.

Under the 1997 Associate Stock Purchase Plan, effective for the six-month period beginning January 1, 1997, the Company is authorized to issue up to 1,000,000 shares of Common Stock to its full-time employees, nearly all of whom are eligible to participate. Under the terms of the Plan, employees can choose, every six months, to have up to 15% of their salary withheld to purchase the Company's Common Stock. The purchase price of the stock is 85% of the lower of its beginning-of-period or end-of-period market price. Participation in the plan by eligible employees has ranged from 30% to 50% in any given six-month period. Under the Plan, 48,748 shares were issued in January of 1999, 46,819 in July of 1999, 52,191 in January of 2000 and 34,941 in July of 2000, 56,901 in January of 2001 and 79,058 in July of 2001 from employees' salary withholdings from the respective previous six-month period. As of June 30, 2001 there were 601,973 shares available for future issuance to the

Associate Stock Purchase Plan. Following is a summary of the weighted average fair market value of this look-back option estimated on the grant date using the Black-Scholes option pricing model, and the related assumptions used:

	December 31, 1998	June 30, 1999	December 31, 1999	June 30, 2000	December 31, 2000	June 30, 2001
Fair value of options	\$7.18	\$5.51	\$8.93	\$29.15	\$11.63	\$9.28
Assumptions:						
Risk-free interest rate	4.9%	4.9%	5.8%	5.8%	4.4%	4.4%
Expected life	3 months	3 months	3 months	3 months	3 months	3 months
Volatility	49.0%	49.0%	83.4%	83.4%	98.2%	98.2%
Dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

The Company applies APB Opinion 25, "Accounting for Stock Issued to Employees" and related Interpretations in accounting for its stock option plans and employee stock purchase plan. Had compensation cost for the Company's stock-based compensation plans been determined based on the fair value at the grant dates for awards under those plans in accordance with the provisions of SFAS 123, "Accounting for Stock-Based Compensation," the Company's net income (loss) and net income (loss) per share would have been as follows (in thousands, except per share data):

	Year Ended June 30,		
	1999	2000	2001
Pro forma net income (loss)	\$ 1,032	\$ (54,030)	\$ (402,340)
Pro forma net income (loss) per share; Basic and Diluted	\$ 0.02	\$ (1.01)	\$ (4.98)

The pro forma amounts are not representative of the effects on reported net income (loss) for future years.

In the year ended June 30, 2000 the Company issued 13,000 shares of restricted stock to certain of its key employees. Under the terms of the grants the shares vest annually over a five-year period and full vesting is dependent upon the continued employment of the employee for the duration of the vesting period. Shares issued were recorded at fair market value on the date of the grant with a corresponding charge to stockholders' equity. The unearned portion is being amortized as compensation expense on a straight-line basis over the related vesting period.

In January 1997 the Board of Directors approved an amendment to the Company's 401(k) plan, which authorized up to 1,000,000 shares of Common Stock for the Company's matching contribution. The Company issued 74,981 shares in August 1998, 36,226 shares in August of 1999 and 51,834 shares in August 2000 to fund its 401(k) match that had accrued during the years ended June 30, 1998, 1999 and 2000, respectively. As of June 30, 2001 there were 758,702 shares available for future contributions to the 401(k) plan.

#### Stock Related Transactions With Third Parties

As described below, the Company has issued certain stock warrants to third parties and has accounted for the issuance of such warrants in accordance with the provisions of EITF 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services."

continued >>

## CheckFree Corporation and Subsidiaries

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In October 2000, the Company completed an agreement to acquire various electronic billing and payment assets from Bank of America in exchange for 10 million shares of the Company's common stock. Bank of America has the ability to earn warrants on up to 10 million additional shares, eight million of which vest upon achievement of specific levels of subscriber adoption of electronic billing and payment services and separately, two million upon achievement of specific levels of electronic bills presented to those subscribers. Upon the vesting of these warrants becoming probable, the Company will record a charge for the fair value of the warrants, based on a Black-Scholes valuation which will take into consideration the market value of our stock, the \$32.50 strike price of the warrants, the volatility of our stock and the applicable risk-free interest rate at that time.

In October 1999, the Company entered into an agreement with one of its customers. Under the terms of the agreement, the customer purchased 250,000 shares of the Company's stock, has been issued warrants on one million shares, and has the ability to earn warrants on up to two million additional shares. All warrants are exercisable on September 15, 2002 contingent upon achievement of various annual revenue targets and maintaining the continued existence of the agreement through that date. Upon the vesting becoming probable, the Company will record a charge for the fair value of the warrants, based on a Black-Scholes valuation which will take into consideration the market value of our stock, the \$39.25 strike price, the volatility of our stock and the applicable risk-free interest rate at that time.

In January 1998 the Company entered into a 10-year processing agreement with a strategic partner. Under the terms of the agreement, the partner acquired 10-year warrants exercisable at \$20 15/16 for 10 million shares of the Company's Common Stock. Three million warrants vested upon the execution of a related processing outsourcing agreement on March 9, 1998 which resulted in the Company recording a non-cash charge of \$32.4 million. The charge was based on a Black-Scholes option pricing model valuation of \$10.80 per share using the following assumptions: risk-free rate of 5.7%, expected life of 10 years, and volatility rate of 56.4%. Any shares acquired by the strategic partner under the terms of this agreement are subject to certain transfer and other restrictions. During each of the fiscal years ended June 30, 2000 and 2001 the strategic partner exercised 750,000 of the vested options and 1,500,000 remain outstanding. During the year ended June 30, 2001, the strategic partner's business was dissolved and therefore does not have the ability to earn any of the remaining seven million warrants.

In March 1997 the Company entered into a consulting agreement with a third party. Under the terms of the agreement the consultant acquired 5-year options exercisable at \$13.00 for up to 50,000 shares of the Company's Common Stock. In June of 1998, upon the execution of a processing agreement with a key customer, 25,000 of the options vested, which resulted in the Company recording a non-cash charge of \$418,000. The charge was based on a Black-Scholes option pricing model valuation of \$16.73 per vested share using the following assumptions: risk-free rate of 5.6%, expected life of 4 years, and volatility rate of 56.4%. The remaining 25,000 options are to vest upon achievement of specific performance targets by key customers set forth in the agreement. Any shares acquired by the consultant under the terms of the agreement are subject to certain transfer restrictions.

In accordance with the terms of a joint marketing agreement, a strategic partner has warrants to purchase up to 650,000 shares of the Company's Common Stock should the partner attain certain customer acquisition targets.

#### **Convertible Subordinated Notes**

In November 1999 the Company issued \$172.5 million of convertible subordinated notes. Each \$1,000 note may be converted, at the holder's option, into 13.6612 shares of common stock at a conversion rate of \$73.20 per share. The fair market value of the Company's stock on June 30, 2001 was \$35.07 per share. Please refer to Note 11 for further information regarding the convertible subordinated notes.

## NOTE 17. EARNINGS PER SHARE

The following table reconciles the differences in income and shares outstanding between basic and dilutive for the periods indicated (in thousands, except per share data):

	Year Ended June 30, 1999			Year Ended June 30, 2000			Year Ended June 30, 2001		
	Income (Numerator)	Shares (Denominator)	Per-Share Amount	Income (Numerator)	Shares (Denominator)	Per-Share Amount	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Basic EPS	\$ 10,457	52,444	\$ 0.20	\$ (32,320)	53,367	\$ (0.61)	\$ (363,135)	80,863	\$ (4.49)
Effective of dilutive securities:									
Options and warrants	-	4,085		-	-		-	-	
Convertible notes	-	-		-	-		-	-	
Diluted EPS	\$ 10,457	56,529	\$ 0.18	\$ (32,320)	53,367	\$ (0.61)	\$ (363,135)	80,863	\$ (4.49)

Anti-dilution provisions of SFAS 128 require consistency between diluted per-common-share amounts and basic per-common-share amounts in loss periods. The number of anti-dilutive equivalent shares excluded from the per-share calculations is 6,157,241 and 5,561,894 for the years ended June 30, 2000 and 2001, respectively. The after-tax effect of interest expense on the convertible subordinated notes of approximately \$4,384,000 and \$9,198,000 for the years ended June 30, 2000 and 2001, respectively, has not been added back to the numerator, as its effect would be anti-dilutive.

## NOTE 18. SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

	Year Ended June 30,		
	1999	2000	2001
	(In thousands)		
Interest paid	\$ 618	\$ 5,982	\$ 12,119
Income taxes paid (received), net	\$ 1,688	\$ (229)	\$ (1,442)
Supplemental disclosure of non-cash investing and financing activities:			
Capital lease additions and purchase of other long-term assets	\$ 3,379	\$ 5,688	\$ 5,716
Stock funding of 401(k) match	\$ 963	\$ 1,059	\$ 2,487
Purchase price of business acquisitions	\$ 19,100	\$ 239,900	\$ 1,351,649
Issuance of common stock and stock options pursuant to acquisitions	(18,000)	(240,000)	(1,350,083)
Liabilities assumed	(887)	-	-
Cash acquired in acquisitions	(23)	(9,052)	(97,200)
Acquisition costs paid in prior period	-	-	(965)
Net cash paid (received)	\$ 190	\$ (9,152)	\$ (96,599)

continued >>

**NOTE 19. BUSINESS SEGMENTS**

The Company operates in three business segments – Electronic Commerce, Software, and Investment Services. These reportable segments are strategic business units that offer different products and services. A further description of each business segment along with the Corporate services area follows:

- *Electronic Commerce* – Electronic Commerce provides services that allow consumers to receive electronic bills through the Internet, pay bills received electronically or in paper form to anyone, and perform ordinary banking transactions including balance inquiries, transfers between accounts and on-line statement reconciliation. These services are primarily directed to financial institutions, Internet financial sites, personal financial management software providers and the customers of these businesses.
- *Software* – Software includes software products and related services for electronic billing, ACH processing and account reconciliation. These products and services are primarily directed to large corporations and financial institutions.
- *Investment Services* – Investment Services includes investment portfolio management services and investment trading and reporting services. These products and services are primarily directed to fee based money managers and financial planners who manage investments of institutions and high net worth individuals.
- *Corporate* – Corporate services include human resources, legal, accounting and various other of the Company's unallocated overhead charges.

The accounting policies of the segments are the same as those described in Note 1 "Summary of Significant Accounting Policies." The Company evaluates performance based on revenues and operating income (loss) of the respective segments. Segment operating income (loss) excludes intangible asset amortization, in-process research and development costs and significant one-time charges related to various business and asset acquisitions. There are no intersegment sales.

The following sets forth certain financial information attributable to the Company's business segments for the years ended June 30, 1999, 2000 and 2001 (in thousands):

	Year Ended June 30,		
	1999	2000	2001
Revenues:			
Electronic Commerce	\$ 169,443	\$ 213,391	\$ 301,532
Software	41,384	42,012	62,175
Investment Services	39,304	54,792	69,613
Total	\$ 250,131	\$ 310,195	\$ 433,320
Operating income (loss):			
Electronic Commerce	\$ (3,126)	\$ (18,248)	\$ (13,083)
Software	15,931	10,536	837
Investment Services	11,250	15,830	20,347
Corporate	(23,348)	(26,120)	(35,746)
Purchase accounting amortization	(6,815)	(18,517)	(393,436)
One time marketing charge	-	-	(25,000)
In-process research and development	(2,201)	(6,900)	(18,600)
Net gain on disposition of assets	4,576	-	-
Total Operating Loss	\$ (3,733)	\$ (43,419)	\$ (464,681)
Identifiable assets:			
Electronic Commerce	\$ 80,223	\$ 102,220	\$ 1,603,069
Software	34,194	273,120	206,746
Investment Services	49,098	47,246	50,113
Corporate	89,246	290,528	324,025
Total	\$ 252,761	\$ 713,114	\$ 2,183,953
Capital expenditures:			
Electronic Commerce	\$ 9,258	\$ 18,299	\$ 28,355
Software	1,189	1,773	2,938
Investment Services	4,764	2,868	6,771
Corporate	25,233	16,555	9,317
Total	\$ 40,444	\$ 39,495	\$ 47,381
Depreciation and amortization:			
Electronic Commerce	\$ 14,214	\$ 19,282	\$ 350,277
Software	2,069	12,317	62,485
Investment Services	5,336	7,634	9,421
Corporate	3,011	3,597	5,312
Total	\$ 24,630	\$ 42,830	\$ 427,495

No single customer accounted for 10% or more of consolidated revenues for the years ended June 30, 1999 and 2000. For the year ended June 30, 2001, one customer accounted for \$44.5 million of consolidated revenues. Revenues for that customer were generated through the Electronic Commerce and Software segments. Foreign sales for the years ended June 30, 1999 and 2000 were insignificant. Foreign sales, based on the location of the customer, for the year ended June 30, 2001 were \$7,636,000.

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Long-lived assets by geographic area are as follows (in thousands):

	Year Ended June 30,	
	2000	2001
United States	\$ 380,695	\$ 1,804,275
Other	988	2,471
Total	\$ 381,683	\$ 1,806,746

**NOTE 20. SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)**

The following quarterly financial information for the years ended June 30, 2000 and 2001 includes all adjustments necessary for a fair presentation of quarterly results of operations: (In thousands, except per share data):

	Quarter Ended			
	September 30	December 31	March 31	June 30
<b>FISCAL 2000</b>				
Total revenue	\$ 69,020	\$ 72,969	\$ 79,706	\$ 88,500
Loss from operations	(6,365)	(6,275)	(5,773)	(25,006)
Net loss	(3,936)	(3,969)	(3,873)	(20,542)
Basic earnings per share:				
Net loss per common share	\$ (0.08)	\$ (0.08)	\$ (0.07)	\$ (0.36)
Equivalent number of shares	51,848	52,200	52,716	56,721
Diluted earnings per share:				
Net loss per common share	\$ (0.08)	\$ (0.08)	\$ (0.07)	\$ (0.36)
Equivalent number of shares	51,848	52,200	52,716	56,721
<b>FISCAL 2001</b>				
Total revenue	\$ 90,757	\$ 107,721	\$ 113,069	\$ 121,773
Loss from operations	(76,363)	(150,570)	(123,255)	(114,493)
Net loss	(58,358)	(116,022)	(101,067)	(87,688)
Basic earnings per share:				
Net loss per common share	\$ (0.91)	\$ (1.34)	\$ (1.17)	\$ (1.01)
Equivalent number of shares	64,216	86,286	86,682	86,774
Diluted earnings per share:				
Net loss per common share	\$ (0.91)	\$ (1.34)	\$ (1.17)	\$ (1.01)
Equivalent number of shares	64,216	86,286	86,682	86,774

The sum of the quarterly loss per share does not equal the year-to-date loss per share for the respective fiscal periods, due to changes in the number of shares outstanding at each quarter-end.

**NOTE 21. COMMITMENTS**

In March 2001 the Company amended an existing agreement for the purchase of software to be used in conjunction with its electronic commerce business. The software is to be licensed in incremental units over the term of the agreement to coincide with the growth of the Company's business. Total commitments under the amended agreement amount to \$11 million over the next five years.



## **NOTE 22. GUARANTOR FINANCIAL INFORMATION**

CheckFree Management Corporation is a guarantor of the Company's \$172,500,000 convertible subordinated notes that were issued November 29, 1999. CheckFree Management Corporation was formed as a medical claims management subsidiary in order to appropriately minimize, control, and manage the medical claims liabilities of the Company and its subsidiaries. As of June 30, 2000 and 2001, the Company and its subsidiaries own approximately 89% of CheckFree Management Corporation. In previous years, due to the relative value of the total assets of CheckFree Management Corporation to the total consolidated assets of the Company, we were required to provide separate financial statements for and disclose certain financial information about CheckFree Management Corporation. As of June 30, 2001, the assets of CheckFree Management Corporation represent less than 2% of the total consolidated assets of the Company, and therefore, separate financial statements and financial disclosures are not deemed significant.

### Executive Officers

**Peter J. Kight**

Chairman & Chief Executive Officer

**Peter F. Sinisgalli**

President & Chief Operating Officer

**David E. Mangum**

Executive Vice President & Chief Financial Officer

**Tacio Carvalho**

Executive Vice President and General Manager  
CheckFree Investment Services

**Stephen Olsen**

Executive Vice President and General Manager  
Electronic Commerce Division

**Tom Stampiglia**

Executive Vice President & President  
Software Division

**Matthew S. Lewis**

Executive Vice President, Corporate Development

**Randal A. McCoy**

Executive Vice President & Chief Technology Officer

**Terrie R. O'Hanlon**

Executive Vice President, Marketing

**Harley Ostis**

Executive Vice President  
Human Resources & Administration

**Allen L. Shulman**

Executive Vice President & General Counsel

### Board of Directors

**Peter J. Kight**

Chairman & Chief Executive Officer  
CheckFree Corporation

**Mark A. Johnson**

President  
eRM Partners

**William P. Boardman**

Chairman & Chief Executive Officer (retired)  
First USA Bank

**Jeffrey M. Wilkins**

Chairman & Chief Executive Officer  
Metatec Corporation

**Eugene F. Quinn**

President  
Confluence Capital Partners, LLC

**James D. Dixon**

President, bankofamerica.com  
Bank of America Corporation

**Ric Duques**

Chairman & Chief Executive Officer  
First Data Corporation

**Lewis C. Levin**

Vice President  
Microsoft

**Curtis Loveland**

Secretary  
Porter, Wright, Morris & Arthur

### Corporate Headquarters

CheckFree Corporation  
4411 East Jones Bridge Road  
Norcross, Georgia 30092  
678-375-3000 tel  
www.checkfree.com

### Stock Listing

Exchange: NASDAQ  
Ticker Symbol: CKFR

### Transfer Agent and Registrar

Fifth Third Bank  
Corporate Trust Services  
Mail Drop 1090F5-4129  
38 Fountain Square Plaza  
Cincinnati, OH 45263  
800-837-2755 toll free  
513-579-5320 local tel

### Independent Auditors

Deloitte & Touche, LLP  
Atlanta, GA

### Investor Information

Tina Moore  
Investor Relations Manager  
678-375-1278 tel  
tmoore@checkfree.com

All aspects of employment with CheckFree are governed on the basis of merit, job performance, competence and qualifications, and will not be influenced in any manner by race, religion, color, creed, national origin, sex, age, disability or veteran status.

### News Releases

Available at [www.checkfree.com](http://www.checkfree.com)

### Common Stock Table

	<i>High</i>		<i>Low</i>	
2001	\$	64.05	\$	24.06
2000	\$	125.63	\$	23.13
1999	\$	69.13	\$	5.75
1998	\$	31.44	\$	16.50
1997	\$	25.00	\$	9.5

### Locations

Ann Arbor, MI  
Atlanta, GA  
Aurora, IL  
Austin, TX  
Baltimore, MD  
Boston, MA  
Chicago, IL  
Columbus, OH  
Houston, TX  
Jersey City, NJ  
Phoenix, AZ  
Research Triangle, NC  
San Diego, CA  
San Francisco, CA  
Waterloo, Ontario, Canada  
Singapore  
Slough, England  
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