ALLIANCE DATA SYSTEMS CORP
Form 10-K/A
March 07, 2006

Table of Contents

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

Form 10-K/A
Amendment No. 1

(Mark One)

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

For the fiscal year ended December 31, 2005
or

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

For the transition period from to

Commission file number 001-15749

ALLIANCE DATA SYSTEMS CORPORATION
(Exact name of registrant as specified in its charter)

Delaware *(State or Other Jurisdiction of Incorporation or Organization)*	**31-1429215** *(I.R.S. Employer Identification No.)*
17655 Waterview Parkway, Dallas, Texas *(Address of Registrant s Principal Executive Offices)*	**75252** *(Zip Code)*

(972) 348-5100
(Registrant s telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, par value $0.01 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes þ No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

Indicate by check mark whether the registrant: (1) has filed all reports required by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past

90 days. Yes þ No o

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

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

As of June 30, 2005, the last business day of the registrant s most recently completed second fiscal quarter, 83,175,616 shares of common stock were outstanding and the aggregate market value of the common stock held by non-affiliates of the registrant on that date was approximately $2.8 billion (based upon the closing price on the New York Stock Exchange on June 30, 2005 of $40.56 per share). Aggregate market value is estimated solely for the purposes of this report. This shall not be construed as an admission for the purposes of determining affiliate status.

As of February 28, 2006, 80,478,288 shares of common stock were outstanding.

Documents Incorporated By Reference

Certain information called for by Part III is incorporated by reference to certain sections of the Proxy Statement for the 2006 Annual Meeting of our stockholders which will be filed with the Securities and Exchange Commission not later than 120 days after December 31, 2005.

EXPLANATORY NOTE

We are filing this Amendment No. 1 on Form 10-K/A to correct two typographical errors in our Form 10-K filed on March 3, 2006 (the Original Filing). Under Item 1A. Risk Factors, page 13, the percentage of consolidated revenue with the Limited Brands and its retail affiliates was incorrectly stated as 17.7% and has been corrected to 11.7%. Under Item 8., Note 8, Deferred Revenue , the amount of total revenue recognized for 2005 was incorrectly stated as (225,730) and has been corrected to (255,730).

Except for the matters described above, this amendment does not modify or update disclosures in the Original Filing. Furthermore, except for the matters described above, this amendment does not change any previously reported financial results, nor does it reflect events occurring after the date of the Original Filing.

ALLIANCE DATA SYSTEMS CORPORATION
INDEX

Caution Regarding Forward-Looking Statements

This Form 10-K and the documents incorporated by reference herein contain forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such statements may use words such as anticipate, believe, estimate, expect, intend, project and similar expressions as they relate to us or our management. When we make forward-looking statements, we are basing them on our management s beliefs and assumptions, using information currently available to us. Although we believe that the expectations reflected in the forward-looking statements are reasonable, these forward-looking statements are subject to risks, uncertainties and assumptions, including those discussed in the Risk Factors section in Item 1A of this Form 10-K and elsewhere in this Form 10-K and the documents incorporated by reference in this Form 10-K.

If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may vary materially from what we projected. Any forward looking statements contained in this annual report or in the documents incorporated herein by reference reflect our current views with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. We have no intention, and disclaim any obligation, to update or revise any forward looking statements, whether as a result of new information, future results or otherwise.

PART I

Item 1. Business

Our Company

We are a leading provider of transaction services, credit services and marketing services in North America. We partner with our clients to develop unique insight into consumer behavior. We use that insight to create and manage customized solutions that we believe change consumer behavior and enable our clients to build stronger, mutually-beneficial relationships with their customers. We focus on facilitating and managing interactions between our clients and their customers through multiple distribution channels including in-store, catalogs and on-line. Our credit and marketing services assist our clients in identifying and acquiring new customers, as well as in increasing the loyalty and profitability of their existing customers. We have a client base in excess of 450 companies, consisting mostly of specialty retailers, petroleum retailers, utilities, supermarkets and financial services companies. We generally have long-term relationships with our clients, with contracts typically ranging from three to five years in duration.

We are the result of the 1996 merger of two entities acquired by Welsh Carson Anderson & Stowe: J.C. Penney s transaction services business, BSI Business Services, Inc., and Limited Brands, Inc. s credit card bank operation, World Financial Network National Bank. In June 2001, we concluded the initial public offering of our common stock, which is listed on the New York Stock Exchange. During 2003, we completed two secondary public offerings whereby Limited Commerce Corp., which is a wholly owned subsidiary of Limited Brands and was our second largest stockholder, sold all of our shares of common stock it beneficially owned.

We continue to execute on our growth strategy through a combination of internal growth and acquisitions. In early 2005, we entered into long-term agreements to provide private label credit card services to Z Gallerie and to provide private label credit card and co-brand services to Hanover Direct. In April 2005, we signed an agreement with Blair Corporation to purchase Blair s private label credit card portfolio and a ten-year agreement with Blair to provide a fully integrated private label credit card program. In April 2005, we expanded our existing commercial credit card relationship with Carter Lumber by signing a five-year agreement with Carter Lumber to provide an integrated commercial credit card and consumer private label credit card program. In May 2005, we signed a multi-year renewal with The Dress

Barn, Inc. and Maurices Incorporated to continue providing private label credit card services, and in July we entered into a multi-year agreement with Gander Mountain Company to provide a co-brand credit card program. In October 2005, we expanded our relationship with each of Spiegel Catalog and Newport News by entering into long-term agreements to provide co-brand credit card programs for both the Spiegel and Newport News brands. In November 2005, we extended our previous agreements with Limited Brands, one of our top-ten clients, to continue providing credit and programs across the following brands: Victoria s Secret, The Limited, Express, Bath and Body Works and Henri Bendel.

In May 2005, we signed a five-year extension with Hilton HHonors Worldwide, one of our top-fifteen clients, to continue to provide integrated relationship management services for the Hilton HHonors® Guest Rewards Program. In July 2005, we expanded our relationship with Bank of America by signing a multi-year renewal to complete the construction of an enhanced consumer marketing database and to host and manage the system on behalf of Bank of America. In September 2005, we expanded our marketing capabilities with the acquisition of Bigfoot Interactive, Inc., now known as Epsilon Interactive, Inc., a leading full-service provider of strategic ROI-focused e-mail communications and marketing automation solutions.

In 2005, we renewed the participation of several of the top-ten sponsors in our AIR MILES® Reward Program in Canada. In July 2005, we signed multi-year renewals with the operating subsidiaries of Sobeys Inc. in Atlantic Canada and the Province of Quebec to continue as participating regional grocery sponsors. In October 2005, we signed a multi-year renewal with the Liquor Control Board of Ontario and a long-term renewal with Amex Bank of Canada, to continue to issue AIR MILES reward miles to Canadians holding its American Express AIR MILES Credit Cards. In December 2005, we signed a multi-year renewal with Canada Safeway Limited to continue as the Western Canada participating grocery sponsor in the AIR MILES Reward Program.

In April 2005, we signed an agreement to provide project management and systems integration services to Cobb Energy, a large co-op electric utility. In May 2005, we acquired Atrana Solutions, Inc., a leading provider of point-of-sale technology solutions that gave us additional capabilities, product offerings and client relationships. In July 2005, we signed a long-term contract renewal with Pepco Energy Services, Inc. to continue providing customer information systems services and customer care solutions. In August 2005, we signed an agreement with Hampton Roads Sanitation District to provide consulting services and an agreement with Greenville Utilities Commission to provide customer care solutions. In November 2005, we signed a seven-year agreement with PNM Resources retail energy provider in Texas, First Choice Power, to provide a full-service customer care solution.

Our corporate headquarters are located at 17655 Waterview Parkway, Dallas, Texas 75252, and our telephone number is 972-348-5100.

Our Market Opportunity and Growth Strategy

Our services are applicable to the full spectrum of commerce opportunities involving companies that sell products and services to individual consumers. We are well positioned to benefit from trends favoring outsourcing and electronic transactions. Many companies lack the economies of scale and core competencies necessary to support their own transaction processing infrastructure and credit card and loyalty or database operations. Companies are also increasingly outsourcing the development and management of their marketing programs.

Our growth strategy is to pursue initiatives to capitalize on our market position and core competencies. Key elements of our strategy are:

Expanding relationships with our base of over 450 clients by offering them integrated transaction and marketing services. We offer our clients products and services that will help them more effectively understand and service their customers and allow them to build and maintain long-term relationships with their customers. By providing services directly to our clients customers we are able to become an integral part of our clients business.

Table of Contents

Expanding our client base in our existing market sectors. We will continue focusing on particular markets that are experiencing rapid growth and increasingly utilizing outsourcing, such as transaction and credit services related to our private label credit card programs for retailers, marketing services related to the AIR MILES Reward Program in Canada and database marketing in the United States, and billing and customer care services for the utility industry.

Continuing to establish long-term relationships with our clients that result in a stable and recurring revenue base. We seek to maintain a stable and recurring revenue base by building and maintaining long-term relationships with our clients and entering into contracts that typically extend for three to five years. Most of our services require the payment of monthly fees based on the number of customer interactions we process, allowing us to generate recurring revenues.

Pursuing focused, strategic acquisitions and alliances to enhance our core capabilities, increase our scale and expand our range of services. Since our inception, we have grown in part through selective acquisitions. We intend to continue to acquire other companies with complementary products, services or relationships to enhance and expand our offering and increase our market share. We also seek to enter into other strategic relationships that extend our customer reach and generate additional revenue.

Products and Services

Our products and services are centered around three core capabilities Transaction Services, Credit Services and Marketing Services. We have traditionally marketed and sold our products and services on a stand-alone basis but increasingly market and sell them on an integrated basis. Our products and services and target markets are listed below. Financial information about our segments and geographic areas appears in Note 18 of our consolidated financial statements.

Segment	Products and Services	Target Markets
Transaction Services	Issuer Services	Specialty Retail
	Card Processing	
	Billing and Payment Processing	
	Customer Care	
	Utility Services	Utility
	Customer Information System Hosting	
	Customer Care	
	Billing and Payment Processing	
	Merchant Services	Petroleum Retail
	Point-of-Sale Services	
	Merchant Bankcard Services	
Credit Services	Private Label Receivables Financing	Specialty Retail
	Underwriting and Risk Management	
	Merchant Processing	
	Receivables Funding	
Marketing Services	Loyalty Programs	Financial Services
	Coalition Loyalty	Supermarkets
	One-to-One Loyalty	Petroleum Retail
	Marketing Services	Specialty Retail
	Database Marketing	Utility
	E-mail Communication Solutions	Pharmaceuticals

Transaction Services

We facilitate and manage transactions between our clients and their customers through our scalable processing systems. Our largest clients within this segment include Limited Brands and its retail affiliates, representing approximately 13.6% of this segment s 2005 revenue.

Issuer Services. We assist clients in issuing private label credit cards with the retailers brand that can be used by customers at the clients store locations, catalogs or on-line. We also provide service and maintenance to our clients private label credit card programs and assist our clients in acquiring, retaining and managing valuable repeat customers. Our Transaction Services segment performs issuer services for our Credit Services segment in connection with that segment s private label credit card programs. The inter-segment services accounted for 44.7% of Transaction Services revenue in 2005.

We have developed a proprietary private label credit card system designed specifically for retailers with the flexibility to make changes to accommodate our clients specific needs. We have also built into the system marketing tools to assist our clients in increasing sales. We utilize our Quick Credit and On-Line Prescreen products to originate new private label credit card accounts. We believe that these products provide an effective marketing advantage over competing services.

We use automated technology for bill preparation, printing and mailing. Commingling statements, presorting and bar coding allow us to take advantage of postal discounts. In addition, we also process customer payments using image processing technology to maximize efficiency. By doing so, we improve the funds availability for both our clients and for those private label credit card receivables that we own or securitize.

Our customer care operations are influenced by our retail heritage. We focus our training programs in all areas on achieving the highest possible standards. We monitor our performance by conducting surveys with our clients and their customers. Our call centers are equipped to handle phone, mail, fax and on-line inquiries. We also provide collection activities on delinquent accounts to support our retail private label credit card programs.

Utility Services. We believe that we are one of the largest independent service providers of customer information systems for utilities in North America. We provide a comprehensive single source business solution for customer care and billing solutions. We have solutions for the regulated, de-regulated and municipal marketplace. These solutions provide not only hosting of the customer information system, but also customer care, statement generation and payment processing, focusing on successful acquisition, value enhancement and retention of our clients customers.

In both a regulated and de-regulated environment, providers will need more sophisticated and complex billing and customer information systems to effectively compete in the marketplace. We believe that our ability to integrate transaction and marketing services effectively provides a competitive advantage for us.

Merchant Services. We are a provider of transaction processing services that based on transactions processed reflects an emphasis on the U.S. petroleum retail industry. We have built a network that enables us to process virtually all electronic payment types including credit card, debit card, prepaid card, electronic benefits and check transactions.

Credit Services

Through our Credit Services segment we are able to finance and operate private label credit card programs more effectively than a typical retailer can operate a stand alone program. We are able to use our expertise in loyalty and one-to-one marketing to help our retail partners develop deeper relationships with their customers and our cardholders. In addition, we are able to fund receivables through our securitization program to achieve lower borrowing costs while having the infrastructure to support and leverage a variety of portfolio types and a large number of account holders. Through our subsidiaries, World Financial Network National Bank and World Financial Capital Bank, we underwrite the accounts

Table of Contents

and fund purchases for over 80 private label credit card and commercial credit clients, representing almost 100 million cardholders and over $3.7 billion of managed receivables as of December 31, 2005. Our clients are predominately specialty retailers, and the largest within this segment include Limited Brands and its retail affiliates, representing 30.5% of this segment s 2005 revenue, and Redcats, representing 13.6% of this segment s 2005 revenue.

We believe that an effective risk management process is important in both account underwriting and servicing. We use a risk analysis in establishing initial credit limits with cardholders. Because we process a large number of credit applications each year, we use automated proprietary scoring technology and verification procedures to process these applications. Our underwriting process involves the purchase of credit bureau information for each credit applicant. We continuously validate, monitor and maintain the scorecards, and we use the resulting data to ensure optimal risk performance. These models help segment prospects into narrower ranges within each risk score provided by credit bureau services, allowing us to better evaluate individual credit risk and to tailor our risk-based pricing accordingly. We generally receive a merchant fee for processing sales transactions charged to a private label credit card program for which we provide receivables funding. Processing includes authorization and settlement of the funds to the retailer, net of our merchant fee.

We utilize a securitization program as our primary funding vehicle for private label credit card receivables. Securitizations involve the packaging and selling of both current and future receivable balances of credit card accounts to a special purpose entity that then sells them to a master trust. Our Transaction Services segment retains rights to service the managed accounts. Our securitizations are treated as sales for accounting purposes and, accordingly, the receivable is removed from our balance sheet. We retain an ownership interest in the receivables, which is commonly referred to as a seller s interest, and a residual interest in the trust, which is commonly referred to as an interest-only strip. The fair value of the interest-only strip is based on assumptions regarding future payments and credit losses and is subject to volatility that could materially affect our operating results. Both the amount and timing of estimated cash flows are dependent on the performance of the underlying credit card receivables, and actual cash flows may vary significantly from expectations. If payments from cardholders or defaults by cardholders exceed our estimates, we may be required to decrease the carrying value of the interest-only strips through a charge against earnings. Limited Brands and its retail affiliates and Redcats accounted for approximately 25.2% and 11.7%, respectively of the receivables in the trust portfolio as of December 31, 2005.

Marketing Services

Our clients are focused on targeting, acquiring and retaining loyal and profitable customers. We create and manage marketing programs that result in securing more frequent and sustained customer purchasing. We utilize the information gathered through our loyalty and database marketing programs to help our clients design and implement effective marketing programs. Our largest service provided by this segment is coalition loyalty, which is branded as the AIR MILES Reward Program and which represents the substantial majority of this segment s 2005 revenue. Our clients within this segment are financial services providers, supermarkets, petroleum retailers, specialty retailers and pharmaceutical companies. BMO Bank of Montreal, Canada Safeway, Shell Canada and Amex Bank of Canada were the four largest Marketing Services clients in 2005, and represented approximately 44.6% of our 2005 Marketing Services revenue. BMO Bank of Montreal represented approximately 24.6% of this segment s 2005 revenue.

Coalition Loyalty. We operate what we believe to be the largest coalition loyalty program in Canada. The AIR MILES Reward Program enables consumers to earn AIR MILES reward miles as they shop across a range of retailers and other sponsors participating in the AIR MILES Reward Program. The AIR MILES Reward Program has enabled sponsors to use this tool to increase their revenues by attracting new customers, retaining existing customers and increasing the amount spent by customers.

We deal with three primary parties in connection with our AIR MILES Reward Program: sponsors, collectors and suppliers.

Sponsors

A sponsor enters into an agreement with us to secure exclusive rights for its particular region and product or service category, to reward customers for changing their shopping behavior and to increase sales from collectors. Collectors can collect AIR MILES reward miles at over 12,000 retail and service locations operated by more than 100 brand name sponsors in every province across Canada, including BMO Bank of Montreal, Canada Safeway, Amex Bank of Canada, Shell Canada, A&P Canada and Sobeys.

Collectors

Members of the AIR MILES Reward Program, known as collectors, accumulate AIR MILES reward miles based on their purchasing behavior at sponsor locations. The AIR MILES Reward Program offers a reward structure that provides a quick and easy way for collectors to earn a broad selection of travel, entertainment and other lifestyle rewards by shopping at participating sponsors. Our active participants represent over two-thirds of all Canadian households. We have issued over seventeen billion AIR MILES reward miles since the program s inception in 1992.

Suppliers

We enter into supply agreements with suppliers of rewards to the program such as airlines, movie theaters and manufacturers of consumer electronics. We make more than 800 different reward opportunities available through over 300 suppliers.

Marketing Services. Epsilon Data Management, Inc. and Epsilon Interactive, which were acquired by us during 2004 and 2005, respectively, are leaders in providing integrated direct marketing solutions that combine database marketing technology and analytics with a broad range of direct marketing services, including e-mail marketing campaigns. Epsilon leverages its deep technology, analytic and direct marketing capabilities to develop integrated marketing solutions for clients in a targeted group of industries including travel, financial services, pharmaceuticals, telecommunications, not-for-profit and insurance. Our integrated direct marketing services include the following:

Technology Services

We provide design and management of integrated marketing databases; customer and prospect data integration and hygiene; campaign management and marketing application integration; loyalty management; web design and development; and e-mail marketing.

Analytical Services

We provide behavior-based, demographic and attitudinal segmentation; acquisition, attrition, cross-sell and upsell, retention, loyalty and value predictive modeling; and program evaluation, testing and measurement.

Direct Marketing Services

We provide direct marketing program design, development and management; campaign design and execution; value proposition and business case development; concept development and creative media consulting; print, imaging and personalization services; data processing services; fulfillment services; and mailing services.

E-mail Communication Solutions

We provide strategic, focused e-mail communication solutions and marketing technologies. Our end-to-end suite of industry specific products and services includes scalable e-mail campaign technology, delivery optimization, marketing automation tools, turnkey integration solutions, strategic consulting and creative expertise to produce e-mail programs that generate measurable results throughout the customer lifecycle.

Table of Contents

Safeguards to Our Business; Disaster and Contingency Planning

We have a number of safeguards to protect our company from the risks we face as a business. Given the significant amount of data that we manage, much of which is real-time data to support our clients commerce initiatives, we have established redundant capabilities within our data centers. We operate multiple data processing centers. In the event of a disaster we can restore our data centers systems at a third party-provided disaster recovery center for the majority of our clients data, and recover internally for the remaining critical systems. Our approach to disaster recovery is consistent with best practices in our industry and our clients needs.

Protection of Intellectual Property and Other Proprietary Rights

We rely on a combination of copyright, trade secret and trademark laws, confidentiality procedures, contractual provisions and other similar measures to protect our proprietary information and technology used in each segment of our business. We currently have four patent applications with the U.S Patent and Trademark Office and one international application that has entered the national phase in two countries. We generally enter into confidentiality or license agreements with our employees, consultants and corporate partners, and generally control access to and distribution of our technology, documentation and other proprietary information. Despite the efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain the use of our products or technology that we consider proprietary and third parties may attempt to develop similar technology independently. We pursue registration and protection of our trademarks primarily in the United States and Canada, although we do have applications pending in Mexico, South America and Europe. Effective protection of intellectual property rights may be unavailable or limited in some countries. The laws of some countries do not protect our proprietary rights to the same extent as in the United States and Canada. We are the exclusive Canadian licensee of the AIR MILES family of trademarks pursuant to a license agreement with Air Miles International Trading B.V. We believe that the AIR MILES family of trademarks and our other trademarks are important for our branding and corporate identification and marketing of our services in each segment.

Competition

The markets for our products and services are highly competitive. We compete with data processing companies, credit card issuers and marketing services companies, as well as with the in-house staffs of our current and potential clients.

Transaction Services. We are a leading provider of transaction services. Our focus has been on industry segments characterized by companies with large customer bases, detail-rich data and high transaction volumes. Targeting these specific market sectors allows us to develop and deliver solutions that meet the needs of these sectors. This focus is consistent with our marketing strategy for all products and services. Additionally, we believe we effectively distinguish ourselves from other transaction processors by providing solutions that help our clients leverage investments they have made in payment systems by using these systems for electronic marketing programs. Competition in the area of utility services comes primarily from larger, more well-funded and well-established competitors and from companies developing in-house solutions and capabilities.

Credit Services. Our credit services business competes primarily with financial institutions whose marketing focus has been on developing credit card programs with large revolving balances. These competitors further drive their businesses by cross selling their other financial products to their cardholders. Our focus has been on targeting retailers that understand the competitive advantage of developing loyal customers. Typically these retailers have customers that make more frequent and smaller transactions. This results in the effective capture of detail-rich data within our database marketing services, allowing us to mine and analyze this data to develop successful customer relationship management strategies for our clients. As an issuer of private label credit cards, we compete with other payment methods, primarily general purpose credit cards like Visa and MasterCard, which we also issue, and American Express, as well as cash, checks and debit cards.

Marketing Services. As a provider of marketing services, we generally compete with advertising and other promotional and loyalty programs, both traditional and on-line, for a portion of a client s total marketing budget. In addition, we compete against internally developed products and services created by our existing and potential clients. For each of our marketing services, we expect competition to intensify as more competitors enter our market. In addition, new competitors with our AIR MILES Reward Program may target our sponsors and collectors as well as draw rewards from our rewards suppliers. Our ability to generate significant revenue from clients and loyalty partners will depend on our ability to differentiate ourselves through the products and services we provide and the attractiveness of our loyalty and rewards programs to consumers. The continued attractiveness of our loyalty and rewards programs will depend in large part on our ability to remain affiliated with sponsors that are desirable to consumers and to offer rewards that are both attainable and attractive to consumers. Intensifying competition will make it more difficult for us to do this. For our database marketing services, our ability to continue to capture detailed transaction data on consumers is critical in providing effective customer relationship management strategies for our clients.

Regulation

Federal and state laws and regulations extensively regulate the operations of our credit card services bank subsidiary, World Financial Network National Bank, as well as our industrial bank, World Financial Capital Bank. Many of these laws and regulations are intended to maintain the safety and soundness of World Financial Network National Bank and World Financial Capital Bank, and they impose significant restraints on them to which other non-regulated companies are not subject. Because World Financial Network National Bank is deemed a credit card bank and World Financial Capital Bank is an industrial bank within the meaning of the Bank Holding Company Act, we are not subject to regulation as a bank holding company. If we were subject to regulation as a bank holding company, we would be constrained in our operations to a limited number of activities that are closely related to banking or financial services in nature. Nevertheless, as a national bank, World Financial Network National Bank is still subject to overlapping supervision by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation; and, as an industrial bank, World Financial Capital Bank is still subject to overlapping supervision by the Federal Deposit Insurance Corporation and the State of Utah.

World Financial Network National Bank and World Financial Capital Bank must maintain minimum amounts of regulatory capital. If World Financial Network National Bank or World Financial Capital Bank do not meet these capital requirements, their respective regulators have broad discretion to institute a number of corrective actions that could have a direct material effect on our financial statements. Under the Federal Deposit Insurance Corporation s Order approving World Financial Capital Bank s application for deposit insurance, World Financial Capital Bank must meet specific capital ratios and paid-in capital minimums, must maintain adequate allowances for loan losses, and must operate within its three-year business plan, among other restrictions. If World Financial Capital Bank fails to meet the terms of the Federal Deposit Insurance Corporations Order, the Federal Deposit Insurance Corporation may withdraw insurance coverage from World Financial Capital Bank and the State of Utah may withdraw its approval of World Financial Capital Bank. Under capital adequacy guidelines and the regulating framework for prompt corrective action, World Financial Network National Bank must meet specific guidelines that involve measures and ratios of its assets, liabilities, regulatory capital, interest rate exposure and certain off-balance sheet items under regulatory accounting standards, among other factors. Under the National Bank Act, if the capital stock of World Financial Network National Bank is impaired by losses or otherwise, we, as the sole shareholder, may be assessed the deficiency. To the extent necessary, if a deficiency in capital still exists, the FDIC may be appointed as a receiver to wind up World Financial Network National Bank s affairs.

Before World Financial Network National Bank can pay dividends to us, it must obtain prior regulatory approval if all dividends declared in any calendar year would exceed its net profits for that year plus its retained net profits for the preceding two calendar years, less any transfers to surplus. In addition,

Table of Contents

World Financial Network National Bank may only pay dividends to the extent that retained net profits, including the portion transferred to surplus, exceed bad debts. Moreover, to pay any dividend, World Financial Network National Bank must maintain adequate capital above regulatory guidelines. Further, if a regulatory authority believes that World Financial Network National Bank is engaged in or is about to engage in an unsafe or unsound banking practice, which, depending on its financial condition, could include the payment of dividends, the authority may require, after notice and hearing, that World Financial Network National Bank cease and desist from the unsafe practice. Before World Financial Capital Bank can pay dividends to us, it must obtain prior written regulatory approval.

As part of an acquisition in 2003 by World Financial Network National Bank, which required approval by the Office of the Comptroller of the Currency, the Office of the Comptroller of the Currency required World Financial Network National Bank to enter into an operating agreement with it and a capital adequacy and liquidity maintenance agreement with us. The operating agreement requires World Financial Network National Bank to continue to operate in a manner consistent with its current practices, regulatory guidelines and applicable law, including those related to affiliate transactions, maintenance of capital and corporate governance. World Financial Network National Bank does not expect that the operating agreement will require any changes in World Financial Network National Bank s current operations. The capital adequacy and liquidity maintenance agreement memorializes our current obligations to World Financial Network National Bank.

We are limited under Sections 23A and 23B of the Federal Reserve Act in the extent to which we can borrow or otherwise obtain credit from or engage in other covered transactions with World Financial Network National Bank or World Financial Capital Bank, which may have the effect of limiting the extent to which World Financial Network National Bank or World Financial Capital Bank can finance or otherwise supply funds to us. Covered transactions include loans or extensions of credit, purchases of or investments in securities, purchases of assets, including assets subject to an agreement to repurchase, acceptance of securities as collateral for a loan or extension of credit, or the issuance of a guarantee, acceptance or letter of credit. Although the applicable rules do not serve as an outright bar on engaging in covered transactions, they do require that we engage in covered transactions with World Financial Network National Bank or World Financial Capital Bank only on terms and under circumstances that are substantially the same, or at least as favorable to World Financial Network National Bank or World Financial Capital Bank, as those prevailing at the time for comparable transactions with nonaffiliated companies. Furthermore, with certain exceptions, each loan or extension of credit by World Financial Network National Bank or World Financial Capital Bank to us or our other affiliates must be secured by collateral with a market value ranging from 100% to 130% of the amount of the loan or extension of credit, depending on the type of collateral.

We are required to monitor and report unusual or suspicious account activity as well as transactions involving amounts in excess of prescribed limits under the Bank Secrecy Act, IRS rules and other regulations. Congress, the IRS and the bank regulators have focused their attention on banks monitoring and reporting of suspicious activities. Additionally, Congress and the bank regulators have proposed, adopted or passed a number of new laws and regulations that may increase reporting obligations of banks.

We are also subject to numerous laws and regulations that are intended to protect consumers, including state law, the Truth in Lending Act, Equal Credit Opportunity Act and Fair Credit Reporting Act. These laws and regulations mandate various disclosure requirements and regulate the manner in which we may interact with consumers. These and other laws also limit finance charges or other fees or charges earned in our activities. We conduct our operations in a manner that we believe excludes us from regulation as a consumer reporting agency under the Fair Credit Reporting Act. If we were deemed a consumer reporting agency, however, we would be subject to a number of additional complex regulatory requirements and restrictions.

A number of privacy regulations have been implemented in the United States and Canada in recent years. These regulations place many new restrictions on our ability to collect and disseminate customer information.

Under the Gramm Leach Bliley Act, we are required to maintain a comprehensive written information security program that includes administrative, technical and physical safeguards relating to customer information. We also were required to develop an initial privacy notice and we are required to provide annual privacy notices to customers that describe in general terms our information sharing practices. If we intend to share nonpublic personal information about customers with nonaffiliated third parties, we must provide our customers with a notice and a reasonable period of time for each customer to opt out of any such disclosure.

In addition to the federal privacy laws with which we must comply, states also have adopted statutes, regulations or other measures governing the collection and distribution of personal information about customers. In some cases these state measures are preempted by federal law, but if not, we make efforts to monitor and comply with individual state privacy laws in the conduct of our business.

We also have systems and processes to comply with the USA PATRIOT ACT of 2001, which is designed to deter and punish terrorist acts in the United States and around the world, to enhance law enforcement investigatory tools, and for other purposes.

Canada has likewise enacted privacy legislation known as the Personal Information Protection and Electronic Documents Act. This act requires organizations to obtain a consumer s consent to collect, use or disclose personal information. Under this act, which took effect on January 1, 2001, the nature of the required consent depends on the sensitivity of the personal information, and the act permits personal information to be used only for the purposes for which it was collected. Some provinces have enacted substantially similar privacy legislation. We believe we have taken appropriate steps with our AIR MILES Reward Program to comply with the law.

Employees

As of December 31, 2005 we had approximately 8,000 employees in the United States and Canada. We believe our relations with our employees are good. We have no collective bargaining agreements with our employees.

Available Information

We file or furnish annual, quarterly, current and special reports and proxy statements and other information with the SEC. You may read and copy any document we file or furnish at the SEC s Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. Our SEC filings are also available to the public at the SEC s web site at *www.sec.gov.* Our web site is *www.AllianceDataSystems.com.* No information from this web site is incorporated by reference herein. You may also obtain copies of our annual, quarterly and current reports, proxy statements and certain other information filed or furnished with the SEC, as well as amendments thereto, free of charge from our web site. These documents are posted to our web site as soon as reasonably practicable after we have filed or furnished these documents with the SEC. We post our audit committee, compensation committee, nominating and corporate governance committee, and executive committee charters, our corporate governance guidelines, and our code of ethics, code of ethics for Senior Financial Executives and Chief Executive Officer, and code of ethics for Board Members on our web site. These documents are available free of charge to any stockholder upon request.

We submitted the certification of the Chief Executive Officer required by Section 303A.12(a) of the New York Stock Exchange Listed Company Manual, relating to our compliance with the NYSE s corporate governance listing standards, to the NYSE on June 8, 2005 with no qualification. In addition, we included the certifications of our Chief Executive Officer and Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002 and related rules, relating to the quality of our public disclosure, in this Annual Report on Form 10-K as Exhibits 31.1 and 31.2.

Item 1A. Risk Factors

Risk Factors

Risks Related to General Business Operations

Our 10 largest clients represented 43.1% of our consolidated revenue in 2005, and the loss of any of these clients could cause a significant drop in our revenue.

We depend on a limited number of large clients for a significant portion of our consolidated revenue. Our 10 largest clients represented approximately 43.1% of our consolidated revenue during the year ended December 31, 2005, with Limited Brands and its retail affiliates representing approximately 11.7% of our 2005 consolidated revenue. Our contract with Limited Brands and its retail affiliates expires in 2012. A decrease in revenue from any of our significant clients for any reason, including a decrease in pricing or activity, or a decision to either utilize another service provider or to no longer outsource some or all of the services we provide, could have a material adverse effect on our consolidated revenue.

Transaction Services. Our 10 largest clients in this segment represented approximately 48.7% of our Transaction Services revenue in 2005. Limited Brands and its retail affiliates were the largest Transaction Services client in 2005, representing approximately 13.6% of this segment s 2005 revenue. Our contracts with Limited Brands and its retail affiliates expire in 2012.

Credit Services. Our two largest clients in this segment represented approximately 44.1% of our Credit Services revenue in 2005. Limited Brands and its retail affiliates represented approximately 30.5%, and Redcats represented approximately 13.6% of our Credit Services revenue in 2005. Our contracts with Limited Brands and its retail affiliates expire in 2012, and our contract with Redcats expires in 2013.

Marketing Services. Our 10 largest clients in this segment represented approximately 61.1% of our Marketing Services revenue in 2005. BMO Bank of Montreal, Canada Safeway, Shell Canada and Amex Bank of Canada were the four largest Marketing Services clients in 2005, representing approximately 44.6% of our 2005 Marketing Services revenue. BMO Bank of Montreal represented approximately 24.6% of this segment s 2005 revenue. Our contract with BMO Bank of Montreal expires in 2009.

Competition in our industries is intense and we expect it to intensify.

The markets for our products and services are highly competitive, and we expect competition to intensify in each of those markets. Many of our current competitors have longer operating histories, stronger brand names and greater financial, technical, marketing and other resources than we do. We cannot assure you that we will be able to compete successfully against our current and potential competitors.

The markets for the services that we offer may fail to expand or may contract and this could negatively impact our growth and profitability.

Our growth and continued profitability depend on acceptance of the services that we offer. If demand for transaction, credit or marketing services decreases, the price of our common stock could fall and you could lose value in your investment. We cannot guarantee that retailers will continue to use loyalty and database marketing strategies. Changes in technology may enable merchants and retail companies to directly process transactions in a cost-efficient manner without the use of our services. Additionally, downturns in the economy or the performance of retailers may result in a decrease in the demand for our marketing strategies. Further, if our customers make fewer sales of their products and services, we will have fewer transactions to process, resulting in lower revenue. Any decrease in the demand for our services for the reasons discussed above or any other reasons could have a material adverse effect on our growth and revenue.

Table of Contents

We cannot assure you that we will effectively integrate acquisitions or realize their full benefits, and future acquisitions may result in dilutive equity issuances or increases in debt.

Historically, we have completed several acquisitions each year. We expect to continue to seek selective acquisitions as an element of our growth strategy. If we are unable to successfully integrate completed or any future acquisitions, we may incur substantial costs and delays or other operational, technical or financial problems, any of which could harm our business and impact the trading price of our common stock. In addition, the failure to successfully integrate any future acquisition may divert management s attention from our core operations or could harm our ability to timely meet the needs of our customers. To finance future acquisitions, we may need to raise funds either by issuing equity securities or incurring debt. If we issue additional equity securities, such sales could reduce the current value of our stock by diluting the ownership interest of our stockholders.

Failure to safeguard our databases and consumer privacy could affect our reputation among our clients and their customers, and may expose us to legal claims from consumers.

An important feature of our marketing and credit services is our ability to develop and maintain individual consumer profiles. As part of our AIR MILES Reward Program, database marketing program and private label credit card program, we maintain marketing databases containing information on consumers account transactions. Although we have extensive security procedures, our databases may be subject to unauthorized access. If we experience a security breach, the integrity of our marketing databases could be affected. Security and privacy concerns may cause consumers to resist providing the personal data necessary to support our profiling capability. The use of our loyalty, database marketing or private label credit card programs could decline if any compromise of security occurred. Any public perception that we released consumer information without authorization could subject us to legal claims from consumers and adversely affect our client relationships.

Loss of data center capacity, interruption of telecommunication links, or inability to utilize proprietary software of third-party vendors could affect our ability to timely meet the needs of our clients and their customers.

Our ability to protect our data centers against damage from fire, power loss, telecommunications failure and other disasters is critical. In order to provide many of our services, we must be able to store, retrieve, process and manage large databases and periodically expand and upgrade our capabilities. Any damage to our data centers, any failure of our telecommunication links that interrupts our operations or any impairment of our ability to use software used by or licensed to us could adversely affect our ability to meet our clients needs and their confidence in utilizing us for future services.

As a result of our significant Canadian operations, our reported financial information will be affected by fluctuations in the exchange rate between the U.S. and Canadian dollars.

A significant portion of our Marketing Services revenue is derived from our operations in Canada, which transacts business in Canadian dollars. Therefore, our reported financial information from quarter-to-quarter will be affected by changes in the exchange rate between the U.S. and Canadian dollars over the relevant periods. We do not hedge any of our net investment exposure in our Canadian subsidiary.

The hedging activity related to our securitization trusts subjects us to off-balance sheet counterparty risks relating to the creditworthiness of the commercial banks with whom we enter into hedging transactions.

In order to execute our hedging strategies, our securitization trusts have entered into interest rate derivative contracts with commercial banks. These banks are otherwise known as counterparties. It is our policy to enter into such contracts with counterparties that are deemed to be creditworthy. However, if macro- or micro-economic events were to negatively impact the respective banks, the banks might not be able to honor their obligations to the securitization trusts and we might suffer a loss related to our residual interest in the securitization trusts.

Table of Contents

Our failure to protect our intellectual property rights may harm our competitive position, and litigation to protect our intellectual property rights or defend against third party allegations of infringement may be costly.

Third parties may infringe or misappropriate our trademarks or other intellectual property rights, which could have a material adverse effect on our business, financial condition or operating results. The actions we take to protect our trademarks and other proprietary rights may not be adequate. Litigation may be necessary to enforce our intellectual property rights, protect our trade secrets or determine the validity and scope of the proprietary rights of others. We cannot assure you that we will be able to prevent infringement of our intellectual property rights or misappropriation of our proprietary information. Any infringement or misappropriation could harm any competitive advantage we currently derive or may derive from our proprietary rights. Third parties may assert infringement claims against us. Any claims and any resulting litigation could subject us to significant liability for damages. An adverse determination in any litigation of this type could require us to design around a third party s patent or to license alternative technology from another party. In addition, litigation is time-consuming and expensive to defend and could result in the diversion of our time and resources. Any claims from third parties may also result in limitations on our ability to use the intellectual property subject to these claims.

If we are required to pay state taxes on transaction processing, it could negatively impact our profitability.

Transaction processing companies may be subject to state taxation of certain portions of their fees charged to merchants for their services. If we are required to pay such taxes and are unable to pass this tax expense through to our merchant clients, these taxes would negatively impact our profitability.

Risks Particular to Transaction Services

In 2005, our Transaction Services segment derived approximately 44.7% of its revenue from servicing cardholder accounts for the Credit Services segment. If the Credit Services segment suffered a significant client loss, our revenue and profitability attributable to the Transaction Services segment could be materially and adversely affected.

Our Transaction Services segment performs card processing and servicing activities for cardholder accounts generated by our Credit Services segment. During 2005, our Transaction Services segment derived $313.0 million, or 44.7% of its revenues, from these services for our Credit Services segment. The financial performance of our Transaction Services segment, therefore, is linked to the activities of our Credit Services segment. If the Credit Services segment were to lose a significant client, our revenue and profitability attributable to the Transaction Services segment could be materially and adversely affected.

Risks Particular to Credit Services

If we are unable to securitize our credit card receivables due to changes in the market, the unavailability of credit enhancements, an early amortization event or for other reasons, we would not be able to fund new credit card receivables, which would have a negative impact on our operations and earnings.

Since January 1996, we have sold substantially all of the credit card receivables originated by our private label credit card bank, World Financial Network National Bank, to WFN Credit Company, LLC and WFN Funding Company II, LLC, which in turn sold them to World Financial Network Credit Card Master Trust, World Financial Network Credit Card Master Note Trust and World Financial Network Credit Card Master Trust III, which we refer to as the WFN Trusts, as part of our securitization program. This securitization program is the primary vehicle through which World Financial Network National Bank finances our private label credit card receivables. We have approximately $450.0 million of asset-backed notes that will come due in 2006. If World Financial Network National Bank were not able to regularly securitize the receivables it originates, our ability to grow or even maintain our credit services business would be materially impaired. World Financial Network National Bank s ability to effect securitization transactions is impacted by the following factors, some of which are beyond our control:

- conditions in the securities markets in general and the asset-backed securitization market in particular;
- conformity in the quality of credit card receivables to rating agency requirements and changes in those requirements; and
- our ability to fund required overcollateralizations or credit enhancements, which we routinely utilize in order to achieve better credit ratings to lower our borrowing costs.

Once World Financial Network National Bank securitizes receivables, the agreement governing the transaction contains covenants that address the receivables performance and the continued solvency of the retailer where the underlying sales were generated. In the event such a covenant or other similar covenant is breached, an early amortization event could be declared, in which case the trustee for the securitization trust would retain World Financial Network National Bank s interest in the related receivables, along with the excess interest income that would normally be paid to World Financial Network National Bank, until such time as the securitization investors are fully repaid. The occurrence of an early amortization event would significantly limit, or even negate, our ability to securitize additional receivables.

Increases in net charge-offs beyond our current estimates could have a negative impact on our operating income and profitability.

The primary risk associated with unsecured consumer lending is the risk of default or bankruptcy of the borrower, resulting in the borrower s balance being charged-off as uncollectible. We rely principally on the customer s creditworthiness for repayment of the loan and therefore have no other recourse for collection. We may not be able to successfully identify and evaluate the creditworthiness of cardholders to minimize delinquencies and losses. An increase in defaults or net charge-offs beyond historical levels will reduce the net spread available to us from the securitization master trust and could result in a reduction in finance charge income or a write-down of the interest-only strip. General economic factors, such as the rate of inflation, unemployment levels and interest rates, may result in greater delinquencies that lead to greater credit losses among consumers. In addition to being affected by general economic conditions and the success of our collection and recovery efforts, our delinquency and net credit card receivable charge-off rates are affected by the credit risk of our private label credit card receivables and the average age of our various private label credit card account portfolios. The average age of our private label credit card receivables affects the stability of delinquency and loss rates of the portfolio. An older private label credit card portfolio generally drives a more stable performance in the portfolio. At December 31, 2005, 61.9% of the total number of our securitized accounts with outstanding balances and 58.0% of the amount of our outstanding securitized receivables were for accounts with origination dates greater than 24 months old. For 2005, our managed receivables net charge-off ratio was 6.5% compared to 6.8% for 2004 and 7.4% for 2003. We cannot assure you that our pricing strategy can offset the negative impact on profitability caused by increases in delinquencies and losses. Any material increases in delinquencies and losses beyond our current estimates could have a material adverse impact on us and the value of our net retained interests in loans that we sell through securitizations.

Changes in the amount of payments and defaults by cardholders on credit card balances may cause a decrease in the estimated value of interest-only strips.

The estimated fair value of interest-only strips depends upon the anticipated cash flows of the related credit card receivables. A significant factor affecting the anticipated cash flows is the rate at which the underlying principal of the securitized credit card receivables is reduced. Other assumptions used in estimating the value of the interest-only strips include estimated future credit losses and a discount rate commensurate with the risks involved. The rate of cardholder payments or defaults on credit card balances may be affected by a variety of economic factors, including interest rates and the availability of alternative financing, most of which are not within our control. A decrease in interest rates could cause cardholder

payments to increase, thereby requiring a write down of the interest-only strips. If payments from cardholders or defaults by cardholders exceed our estimates, we may be required to decrease the estimated value of the interest-only strips through a charge against earnings.

Interest rate increases could significantly reduce the amount we realize from the spread between the yield on our assets and our cost of funding.

An increase in market interest rates could reduce the amount we realize from the spread between the yield on our assets and our cost of funding. A rise in market interest rates may indirectly impact the payment performance of consumers or the value of, or the amount we could realize from the sale of interest-only strips. At December 31, 2005, we had $4.1 billion of debt, including $3.3 billion of off-balance sheet debt from our securitization program.

At December 31, 2005, 69.8% of our $4.1 billion of debt was fixed or effectively fixed through swap agreements.

At December 31, 2005, 63.1% of our total debt, or 79.2% of our off-balance sheet debt, was locked at a current effective interest rate of 4.6% through interest rate swap agreements with notional amounts totaling $2.6 billion. Of the remaining 20.8% of our off-balance sheet debt, we have variable rate private label credit cards that are equal to or greater than the variable rate debt.

At December 31, 2005, approximately 6.7% of our total debt, or 32.8% of our on-balance sheet debt, was subject to fixed rates with a weighted average interest rate of 4.2%.

Assuming we do not take any counteractive measures, a 1.0% increase in interest rates would result in an annual decrease to pretax income of approximately $5.6 million related to our on-balance sheet debt. The foregoing sensitivity analysis is limited to the potential impact of an interest rate increase of 1.0% on cash flows and fair values, and does not address default or credit risk.

We expect growth in our credit services segment to result from new and acquired private label credit card programs whose credit card receivable performance could result in increased portfolio losses and negatively impact our net retained interests in loans securitized.

We expect an important source of growth in our private label credit card operations to come from the acquisition of existing private label credit card programs and initiating private label credit card programs with retailers who do not currently offer a private label credit card. Although we believe our pricing and models for determining credit risk are designed to evaluate the credit risk of existing programs and the credit risk we are willing to assume for acquired and start-up programs, we cannot assure you that the loss experience on acquired and start-up programs will be consistent with our more established programs. The failure to successfully underwrite these private label credit card programs may result in defaults greater than our expectations and could have a material adverse impact on us and the value of our net retained interests in loans securitized.

Current and proposed regulation and legislation relating to our credit services could limit our business activities, product offerings and fees charged.

Various Federal and state laws and regulations significantly limit the credit services activities in which we are permitted to engage. Such laws and regulations, among other things, limit the fees and other charges that we can impose on consumers, limit or prescribe certain other terms of our products and services, require specified disclosures to consumers, or require that we maintain certain licenses, qualifications and minimum capital levels. In some cases, the precise application of these statutes and regulations is not clear. In addition, numerous legislative and regulatory proposals are advanced each year which, if adopted, could have a material adverse effect on our profitability or further restrict the manner in which we conduct our activities. The failure to comply with, or adverse changes in, the laws or regulations to which our business is subject, or adverse changes in their interpretation, could have a material adverse effect on our ability to collect our receivables and generate fees on the receivables, thereby adversely affecting our profitability.

If our bank subsidiaries fail to meet certain bank criteria, we may become subject to regulation under the Bank Holding Company Act, which would force us to cease all of our non-banking activities and thus cause a drastic reduction in our profits and revenue.

If either of our depository institution subsidiaries failed to meet the criteria for the exemption from the definition of bank in the Bank Holding Company Act under which it operates (which exemptions are described below), and if we did not divest such depository institution upon such an occurrence, we would become subject to regulation under the Bank Holding Company Act. This would require us to cease certain of our activities that are not permissible for companies that are subject to regulation under the Bank Holding Company Act.

One of our depository institution subsidiaries, World Financial Network National Bank, is a limited-purpose national credit card bank located in Ohio. World Financial Network National Bank is not a bank as defined under the Bank Holding Company Act because it is in compliance with the following requirements:

- it engages only in credit card operations;
- it does not accept demand deposits or deposits that the depositor may withdraw by check or similar means for payment to third parties;
- it does not accept any savings or time deposits of less than $100,000, except for deposits pledged as collateral for its extensions of credit;
- it maintains only one office that accepts deposits; and
- it does not engage in the business of making commercial loans.

Our other depository institution subsidiary, World Financial Capital Bank, is a Utah industrial bank that is authorized to do business by the State of Utah and the Federal Deposit Insurance Corporation. World Financial Capital Bank is not a bank as defined under the Bank Holding Company Act because it is an industrial bank in compliance with the following requirements:

- it is an institution organized under the laws of a state which, on March 5, 1987, had in effect or had under consideration in such state s legislature a statute which required or would require such institution to obtain insurance under the Federal Deposit Insurance Act.
- it does not accept demand deposits that the depositor may withdraw by check or similar means for payment to third parties.

While the consequences of being subject to regulation under the Bank Holding Company Act would be severe, we believe that the risk of becoming subject to such regulation is minimal as a result of the precautions we have taken in structuring our business.

If our industrial bank fails to meet the terms of the Federal Deposit Insurance Corporation or State of Utah Orders, we may be subject to termination of our industrial bank.

Our industrial bank, World Financial Capital Bank, is authorized to do business by the State of Utah and the Federal Deposit Insurance Corporation. World Financial Capital Bank is subject to capital ratios and paid-in capital minimums and must maintain adequate allowances for loan losses and operate within its three-year business plan. While the consequence of losing the World Financial Capital Bank authority to do business would be significant, we believe that the risk of such loss is minimal as a result of the precautions we have taken and the management team we have in place.

Table of Contents

Risks Particular to Marketing Services

If actual redemptions by AIR MILES collectors are greater than expected, our profitability could be adversely affected.

A portion of our revenue is based on our estimate of the number of AIR MILES reward miles that will go unused by the collector base. The percentage of unredeemed reward miles is known as breakage in the loyalty industry. AIR MILES reward miles currently do not expire. We experience breakage when reward miles are not redeemed by collectors for a number of reasons, including:

- loss of interest in the program or sponsors;
- collectors moving out of the program area; and
- death of a collector.

If actual redemptions are greater than our estimates, our profitability could be adversely affected due to the cost of the excess redemptions.

We could face increased competition from other loyalty programs, including Aeroplan, Air Canada s frequent flyer program.

As a result of increased competition in the loyalty market, including from Aeroplan, Air Canada s frequent flyer program, we may experience greater competition in attracting and retaining sponsors in our AIR MILES Reward Program.

The loss of our most active AIR MILES collectors could negatively impact our growth and profitability.

Our most active AIR MILES reward miles collectors affect a disproportionately large percentage of our AIR MILES Reward Program revenue. We estimate that over half of the AIR MILES Reward Program revenues for 2006 will be associated with our AIR MILES collectors who participate most actively. The loss of a significant portion of these collectors, for any reason, could impact our ability to generate significant revenue from sponsors and loyalty partners. The continued attractiveness of our loyalty and rewards programs will depend in large part on our ability to remain affiliated with sponsors that are desirable to consumers and to offer rewards that are both attainable and attractive.

Airline or travel industry disruptions, such as an airline insolvency, could negatively affect the AIR MILES Reward Program, our revenues and profitability.

Air travel is one of the appeals of the AIR MILES Reward Program to collectors. As a result of airline insolvencies and restructurings, we may experience service disruptions that prevent us from fulfilling collectors flight redemption requests. If one of our existing airline suppliers sharply reduces its fleet capacity and route network, we may not be able to satisfy our collectors demands for airline tickets. Tickets from other airlines, if available, could be more expensive than a comparable ticket under our current supply agreements with existing suppliers, and the routes offered by the other airlines may be inadequate, inconvenient or undesirable to the redeeming collectors. As a result, we may experience higher air travel redemption costs and collector satisfaction with the AIR MILES Reward Program might be adversely affected.

As a result of airline or travel industry disruptions, or as might result from political instability, terrorist acts or war, some collectors could determine that air travel is too dangerous or, given new airport regulations, too burdensome. Consequently, collectors might forego redeeming reward miles for air travel and therefore might not participate in the AIR MILES Reward Program to the extent they previously did, which could adversely affect our revenue from the program. A reduction in collector use of the program could impact our ability to attract new sponsors and loyalty partners and to generate revenue from current sponsors and loyalty partners.

Legislation relating to consumer privacy may affect our ability to collect data that we use in providing our marketing services, which could negatively affect our ability to satisfy our clients needs.

The enactment of legislation or industry regulations arising from public concern over consumer privacy issues could have a material adverse impact on our marketing services. Any such legislation or industry regulations could place restrictions upon the collection and use of information that is currently legally available, which could materially increase our cost of collecting some data. Legislation or industry regulation could also prohibit us from collecting or disseminating certain types of data, which could adversely affect our ability to meet our clients requirements.

In the United States, the federal Gramm Leach Bliley Act makes it more difficult to collect and use information that has been legally available and may increase our costs of collecting some data. Regulations under this act give cardholders the ability to opt out of having information generated by their credit card purchases shared with other parties or the public. Our ability to gather and utilize this data will be adversely affected if a significant percentage of the consumers whose purchasing behavior we track elect to opt out, thereby precluding us from using their data. Under the regulations, we generally are required to refrain from sharing data generated by our new cardholders until such cardholders are given the opportunity to opt out.

In the United States, the federal Do-Not-Call Implementation Act makes it more difficult to telephonically communicate with customers. Regulations under this act give consumers the ability to opt out, through a national do-not-call list, a state do-not-call list or an internal do-not-call list which is required by the regulation, of having telephone calls placed to them by telemarketers who do not have an existing business relationship with the consumer. This act could limit our ability to provide services and information to our clients. Failure to comply with the terms of this act could have a negative impact to our reputation and subject us to significant penalties.

In the United States, the federal Controlling the Assault of Non-Solicited Pornography and Marketing Act restricts our ability to send commercial electronic mail messages to customers. The act requires that a customer provide consent prior to a commercial electronic mail message being sent to the customer and further restricts the transmission information (header/subject line) and content of the electronic mail message. Under the regulation, we generally are prohibited from issuing electronic mail or obtaining a benefit from an electronic mail message until such time as the customer has affirmatively granted permission for us to do so. Failure to comply with the terms of this act could have a negative impact to our reputation and subject us to significant penalties.

In Canada, the Personal Information Protection and Electronic Documents Act requires organizations to obtain a consumer s consent to collect, use or disclose personal information. Under this act, which took effect on January 1, 2001, the nature of the required consent depends on the sensitivity of the personal information, and the act permits personal information to be used only for the purposes for which it was collected. We allow our customers to voluntarily opt out from receiving either one or both promotional and marketing mail or promotional and marketing electronic mail. Heightened consumer awareness of, and concern about, privacy may result in customers opting out at higher rates than they have historically. This would mean that a reduced number of customers would receive bonus mile offers and therefore would collect fewer AIR MILES reward miles.

Risks Related to Our Company

The affiliated entities of Welsh Carson currently own a significant amount of our common stock. These stockholders may have interests that conflict with yours and may be able to control the election of directors and the approval of significant corporate transactions, including a change in control.

As of February 28, 2006, the affiliated entities of Welsh Carson beneficially owned approximately 17.3% of our outstanding common stock. Welsh Carson is able to exercise significant influence over matters requiring stockholder approval, including the election of directors, changes to our charter documents and significant corporate transactions. Welsh Carson may have interests that conflict with our interests or those of other stockholders. Welsh Carson s continued concentrated ownership will make it difficult for another company to acquire us and for you to receive any related takeover premium for your shares unless Welsh Carson approves the acquisition.

Delaware law and our charter documents could prevent a change of control that might be beneficial to you.

Delaware law, as well as provisions of our certificate of incorporation and bylaws, could discourage unsolicited proposals to acquire us, even though such proposals may be beneficial to you. These provisions include:

- a board of directors classified into three classes of directors with the directors of each class having staggered, three-year terms;
- our board s authority to issue shares of preferred stock without further stockholder approval; and
- provisions of Delaware law that restrict many business combinations and provide that directors serving on staggered boards of directors, such as ours, may be removed only for cause.

These provisions of our certificate of incorporation, bylaws and Delaware law could discourage tender offers or other transactions that might otherwise result in our stockholders receiving a premium over the market price for our common stock.

Future sales of our common stock, or the perception that future sales could occur, may adversely affect our common stock price.

As of February 28, 2006, we had an aggregate of 98,951,592 shares of our common stock authorized but unissued and not reserved for specific purposes. In general, we may issue all of these shares without any action or approval by our stockholders. We have reserved 21,003,000 shares of our common stock for issuance under our employee stock purchase plan and our long term incentive plans, of which 7,965,192 shares are issuable upon vesting of restricted stock awards, restricted stock units, and upon exercise of options granted as of February 28, 2006, including options to purchase approximately 3,921,897 shares exercisable as of February 28, 2006 or that will become exercisable within 60 days after February 28, 2006. We have reserved for issuance 1,500,000 shares of our common stock, all of which remain issuable, under our 401(k) and Retirement Savings Plan. In addition, we may pursue acquisitions of competitors and related businesses and may issue shares of our common stock in connection with these acquisitions. Sales or issuances of a substantial number of shares of common stock, or the perception that such sales could occur, could adversely affect prevailing market prices of our common stock, and any sale or issuance of our common stock will dilute the percentage ownership held by our stockholders. Further, sales of a substantial number of shares of common stock by our largest stockholder, Welsh Carson, or the perception that such sales could occur, could also adversely affect prevailing market prices of our common stock.

Item 1B. Unresolved Staff Comments

None.

Table of Contents

Item 2. Properties

As of December 31, 2005, we leased over 35 general office properties throughout the United States and Canada, comprising over 2.1 million square feet. These facilities are used to carry out our operational, sales and administrative functions. Our principal facilities are as follows:

Location	Segment	Approximate Square Footage	Lease Expiration Date
Dallas, Texas	Corporate, Transaction Services	230,061	October 31, 2010
Dallas, Texas	Corporate	61,750	July 31, 2007
Dallas, Texas	Transaction Services	247,618	July 31, 2009
San Antonio, Texas	Transaction Services	67,540	October 31, 2007
Columbus, Ohio	Credit Services	103,161	January 31, 2008
Westerville, Ohio	Transaction Services	100,800	May 31, 2006
Toronto, Ontario, Canada	Marketing Services	143,068	September 16, 2007
Wakefield, Massachusetts	Marketing Services	96,726	April 30, 2013
Earth City, Missouri	Marketing Services	116,783	September 30, 2012

We believe our current and proposed facilities are suitable to our businesses and that we will be able to lease, purchase or newly construct additional facilities as needed.

Item 3. Legal Proceedings

From time to time, we are involved in various claims and lawsuits arising in the ordinary course of our business that we believe will not have a material adverse affect on our business or financial condition, including claims and lawsuits alleging breaches of contractual obligations.

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

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

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information

Our common stock is listed on the New York Stock Exchange and trades under the symbol ADS. The following table sets forth for the periods indicated the high and low composite per share closing sales prices as reported by the New York Stock Exchange.

	High	Low
Fiscal Year Ended December 31, 2004		
First quarter	$ 33.55	$ 26.92
Second quarter	42.25	33.07
Third quarter	42.00	35.73
Fourth quarter	48.52	40.64
Fiscal Year Ended December 31, 2005		
First quarter	$ 46.66	$ 37.79
Second quarter	42.79	35.32
Third quarter	43.65	38.98
Fourth quarter	39.25	32.79

Table of Contents

Holders

As of February 28, 2006, the closing price of our common stock was $43.26 per share, there were 80,478,288 shares of our common stock outstanding, and there were approximately 160 holders of record of our common stock.

Dividends

We have never declared or paid any dividends on our common stock, and we do not anticipate paying any cash dividends on our common stock in the foreseeable future. We currently intend to retain future earnings, if any, to finance operations and the expansion of our business. Any future determination to pay cash dividends on our common stock will be at the discretion of our board of directors and will be dependent upon our financial condition, operating results, capital requirements and other factors that our board deems relevant. In addition, under the terms of our credit facilities, we cannot declare or pay dividends or return capital to our common stockholders, and we are restricted in the amount of any other distribution, payment or delivery of property or cash to our common stockholders.

Issuer Purchases of Equity Securities

On June 8, 2005, our Board of Directors authorized a stock repurchase program to acquire up to an aggregate of $80.0 million of our outstanding common stock through June 2006. On October 27, 2005, our Board of Directors authorized a new stock repurchase program to acquire up to an additional $220.0 million of our outstanding common stock through October 2006. At December 31, 2005, we had repurchased 3,942,100 shares of our common stock for approximately $148.8 million under these programs. Additionally, the administrator of our 401(k) and Retirement Savings Plan purchased shares of our common stock for the benefit of the employees who participated in that portion of the plan during the fourth quarter of 2005. The following table presents information with respect to those purchases of our common stock made during the three months ended December 31, 2005:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (In millions)
During 2005:				
October	529,768	$ 36.97	517,900	$ 215.6(1)
November	717,238	36.30	706,500	190.0(1)
December	1,068,834	36.40	1,065,300	151.2(1)
Total	2,315,840	$ 36.50	2,289,700	$ 151.2

(1) On June 8, 2005, our Board of Directors authorized a stock repurchase program to acquire up to an aggregate of $80.0 million of our outstanding common stock through June 2006. On October 27, 2005, our Board of Directors authorized a new stock repurchase program to acquire up to an additional $220.0 million of our outstanding common stock through October 2006.

Table of Contents

Equity Compensation Plan Information

The following table provides information as of December 31, 2005 with respect to shares of our common stock that may be issued under the 2003 Long Term Incentive Plan, the Amended and Restated Stock Option Plan, the 2005 Long Term Incentive Plan, the Executive Annual Incentive Plan or the Amended and Restated Employee Stock Purchase Plan:

Plan Category	Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in the First Column)
Equity compensation plans approved by security holders	6,679,909	$ 27.19	6,477,028(1)
Equity compensation plans not approved by security holders	None	N/A	None
Total	6,679,909	$ 27.19	6,477,028

(1) Includes 936,046 shares available for future issuance under the Amended and Restated Employee Stock Purchase Plan.

Table of Contents

Item 6. Selected Financial Data

SELECTED HISTORICAL CONSOLIDATED FINANCIAL AND OPERATING INFORMATION

The following table sets forth our summary historical financial information for the periods ended and as of the dates indicated. You should read the following historical financial information along with Management s Discussion and Analysis of Financial Condition and Results of Operations contained in this Form 10-K and the financial statements and related notes that are incorporated by reference in this Form 10-K. The fiscal year financial information included in the table below is derived from audited financial statements.

	Year Ended December 31,				
	2001	2002	2003	2004	2005
	(Amounts in thousands, except per share amounts)				
Income statement data					
Total revenue	$ 769,867	$ 865,297	$ 1,046,544	$ 1,257,438	$ 1,552,437
Cost of operations	607,623	670,544	788,874	916,201	1,124,590
General and administrative[(1)]	41,301	53,784	52,320	77,740	91,532
Depreciation and other amortization	30,698	41,768	53,948	62,586	58,565
Amortization of purchased intangibles	43,506	24,707	20,613	28,812	41,142
Total operating expenses	723,128	790,803	915,755	1,085,339	1,315,829
Operating income	46,739	74,494	130,789	172,099	236,608
Other expenses	6,025	834	4,275		
Fair value loss on interest rate derivative	15,131	12,017	2,851	808	
Interest expense, net	26,245	19,924	14,681	6,972	14,482
(Loss) income from continuing operations before income taxes	(662)	41,719	108,982	164,319	222,126
Provision for income taxes	9,700	18,060	41,684	61,948	83,381
Net (loss) income	$ (10,362)	$ 23,659	$ 67,298	$ 102,371	$ 138,745
Net (loss) income per share basic	$ (0.21)	$ 0.32	$ 0.86	$ 1.27	$ 1.69
Net (loss) income per share diluted	$ (0.21)	$ 0.31	$ 0.84	$ 1.22	$ 1.64
Weighted average shares used in computing per share amounts basic	64,555	74,422	78,003	80,614	82,208
Weighted average shares used in computing per share amounts diluted	64,555	76,696	80,313	84,040	84,637

(1) Included in general and administrative is stock compensation expense of $1.8 million, $2.9 million, $5.9 million, $15.8 million and $14.1 million for the years ended December 31, 2001, 2002, 2003, 2004 and 2005, respectively.

Table of Contents

	Year Ended December 31,				
	2001	2002	2003	2004	2005
	(Amounts in thousands, except per share amounts)				
Adjusted EBITDA and Operating EBITDA(2)					
Adjusted EBITDA	$ 122,729	$ 143,917	$ 211,239	$ 279,264	$ 350,458
Operating EBITDA	$ 154,009	$ 162,781	$ 276,138	$ 321,779	$ 396,397
Other financial data					
Cash flows from operating activities	$ 166,409	$ 122,569	$ 116,876	$ 348,629	$ 109,081
Cash flows from investing activities	$ (190,982)	$ (192,603)	$ (247,729)	$ (399,859)	$ (330,951)
Cash flows from financing activities	$ 30,711	$ (15,670)	$ 165,003	$ 66,369	$ 278,579
Segment operating data					
Statements generated	131,253	138,669	167,118	190,976	190,910
Credit sales	$ 4,050,554	$ 4,924,952	$ 5,604,233	$ 6,227,421	$ 6,582,800
Average managed receivables	$ 2,128,365	$ 2,344,334	$ 2,654,087	$ 3,021,800	$ 3,170,485
AIR MILES reward miles issued	2,153,550	2,348,133	2,571,501	2,834,125	3,246,553
AIR MILES reward miles redeemed	984,926	1,259,951	1,512,788	1,782,185	2,023,218

(2) See Use of Non-GAAP Financial Measures set forth in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations for a discussion of our use of adjusted EBITDA and operating EBITDA and a reconciliation to net (loss) income, the most directly comparable GAAP financial measure.

	As of December 31,				
	2001	2002	2003	2004	2005
	(Amounts in thousands)				
Balance sheet data					
Cash and cash equivalents	$ 117,535	$ 30,439	$ 67,745	$ 84,409	$ 143,213
Seller s interest and credit card receivables, net	128,793	147,899	271,396	248,074	479,108
Redemption settlement assets, restricted	150,330	166,293	215,271	243,492	260,963
Intangible assets, net	74,964	75,399	143,733	233,779	265,000
Goodwill	404,797	429,720	484,415	709,146	858,470
Total assets	1,464,428	1,447,462	1,867,424	2,239,080	2,926,082
Deferred revenue	327,683	362,510	476,387	547,123	610,533
Certificates of deposit	120,800	96,200	200,400	94,700	379,100

Credit facilities, subordinated debt and other debt	189,625	196,711	189,751	342,823	457,844
Total liabilities	958,787	904,904	1,165,093	1,368,560	2,004,975
Total stockholders equity	505,641	542,558	702,331	870,520	921,107

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

Overview

We are a leading provider of transaction services, credit services and marketing services in North America. We partner with our clients to develop unique insight into consumer behavior. We use that insight to create and manage customized solutions that we believe change consumer behavior and enable our clients to build stronger, mutually-beneficial relationships with their customers. We focus on facilitating and managing interactions between our clients and their customers. We operate in three business segments: Transaction Services, Credit Services and Marketing Services.

Transaction Services. Transaction Services is our largest segment. The Transaction Services segment primarily generates revenue based on the number of statements generated, customer calls handled and transactions processed. Statements generated is the primary driver of revenue for this segment and represents the majority of revenue.

Statements Generated: This driver represents the number of statements generated for our private label credit card and utility clients. The number of statements generated in any given period is a fairly reliable indicator of the number of active account holders during that period. In addition to receiving payment for each statement generated, we also are paid for other services such as remittance processing, customer care and various marketing services.

Transaction Services primarily is affected by increased outsourcing in our targeted industry verticals. Companies are increasingly outsourcing their non-core processes such as customer information systems, billing and customer care. We are impacted by this trend with our clients in utility services and issuer services.

Credit Services. The Credit Services segment primarily generates revenue from servicing fees from our securitization trusts, merchant discount fees, and securitization income. Private label credit sales and average managed receivables are the two primary drivers of revenue for this segment.

Private Label Credit Sales: This driver represents the dollar value of private label credit card sales that occur at our clients point of sale terminals or through catalogs or web sites. Generally, we are paid a percentage of these sales, referred to as merchant discount, from the retailers that utilize our private label credit card program. Private label credit sales typically lead to higher portfolio balances as cardholders finance their purchases through our credit card banks.

Average Managed Receivables: This represents the average balance of outstanding receivables from our cardholders, excluding receivables for which we do not bear the risk of loss. Customers are assessed a finance charge based on their outstanding balance at the end of a billing cycle. There are many factors that drive the outstanding balances such as payment rates, charge-offs, recoveries and delinquencies. Management actively monitors all of these factors. Generally we securitize our receivables, which results in a sale for accounting purposes and effectively removes them from our balance sheet to one of the securitization trusts.

Credit Services is affected by industry trends similar to Transaction Services. The growing trend of outsourcing of private label credit card programs leads to increased accounts and balances to finance. We focus our sales efforts on prime borrowers and do not target sub-prime borrowers. Additionally, economic trends can impact this segment. Interest expense is a significant component of operating costs for the securitized trusts. Over the last three years we have experienced a historically low interest rate environment. We have refinanced our recent bond maturities with instruments that lock in our effective interest rate for up to five year terms and in some cases entered into declining swap rates. Interest rates in 2005 were similar to the rates in 2004. A low interest rate environment is usually indicative of a slower economic environment, which can negatively impact our net charge-offs, a significant cost of financing receivables. In the last five years, our net charge-offs decreased from a peak of 8.4% in 2001 to our current 2005 rate of 6.5%. During the fourth quarter of 2005, Congress enacted new bankruptcy legislation with a two-fold impact. First, an acceleration of bankruptcies occurred in October and November as the result of cardholders filing under the previous bankruptcy legislation, which was more lenient. Second, future filings under the new legislation will make it more difficult for cardholders to dispose of their obligations. Our expectation for 2006 is that we will experience similar or better levels of net charge-offs and cost of funds as we experienced during 2005.

Marketing Services. Marketing Services has historically been represented primarily by our AIR MILES Reward Program, which we believe to be the largest coalition loyalty program in Canada. We primarily collect fees from our clients based on the number of AIR MILES reward miles issued and in limited circumstances the number of AIR MILES reward miles redeemed. All of the fees collected for AIR MILES reward miles issued are deferred and recognized over time. AIR MILES reward miles issued and AIR MILES reward miles redeemed are the two primary drivers of revenue for this segment, and as a result they are both indicators of the success of the program. These two drivers are also important in the revenue recognition process.

AIR MILES Reward Miles Issued: The number of AIR MILES reward miles issued depends upon the buying activity of the collectors at our participating sponsors. The fees collected from sponsors for the issuance of AIR MILES reward miles represents future revenue and earnings for us.

AIR MILES Reward Miles Redeemed: A majority of the revenue we recognize in this segment is derived from the redemptions of AIR MILES reward miles by collectors. Redemptions also show that collectors are attaining the rewards that are offered through our programs.

Our AIR MILES Reward Program tends not to be significantly impacted by economic swings as the majority of the sponsors are in non-discretionary categories such as grocery, petroleum and financial institutions. Additionally, we target the sponsors most loyal customers, who are unlikely to change their spending patterns. We are impacted by changes in the exchange rate between the U.S. dollar and the Canadian dollar. The Canadian dollar appreciated this year, which benefited our operating results. Our expectation is that the Canadian dollar/ U.S. dollar exchange rate will be more stable in 2006 than in 2005 and remain at its current relative levels. Beginning in late 2004, with the acquisition of Epsilon, we began an expansion of our marketing services in the U.S. We continued our U.S. expansion in 2005 with the acquisition of Bigfoot Interactive, now known as Epsilon Interactive. Epsilon Interactive gives us a significant presence in e-mail communication solutions.

Year in Review Highlights

Our 2005 results included significant new and renewed agreements with significant clients and continued selective execution of our acquisition strategy.

In February 2005, we announced a multi-year renewal to continue providing private label credit card services to Pacific Sunwear of California, Inc., a leading specialty retailer of everyday casual apparel, accessories and footwear.

In February 2005, we signed a long-term agreement to provide a fully integrated private label credit card and co-brand bankcard solution for Hanover Direct, a leading catalog and Web retailer of home furnishings and accessories and men s and women s apparel.

In March 2005, we announced a long-term agreement to provide private label credit card services for Z Gallerie, a leading retailer specializing in high-quality, distinctive furnishings and decorative accessories for the home.

In April 2005, we signed an agreement to provide project management and systems integration services to Cobb Energy, one of the largest co-op electric utilities in the United States.

In April 2005, we signed an agreement with Blair Corporation to purchase Blair s private label credit card portfolio and a ten-year agreement with Blair to provide a fully integrated private label credit card program. Blair, through its Blair and Irvine Park brands, sells quality men s and women s business and casual fashion attire and home accessories. This transaction closed in the fourth quarter of 2005.

Table of Contents

In April 2005, we signed a long-term agreement to provide private label credit card services for Crescent Jewelers, a top-ten jewelry retailer that sells quality fine jewelry, including unique and exclusive jewelry collections targeted to mid- and upper-end consumers.

In April 2005, we signed a five-year agreement with Carter Lumber, one of the nation s top building materials retailers and an existing commercial card client, to provide an integrated consumer private label credit card program.

In May 2005, we acquired Atrana Solutions Inc., a leading provider of point-of-sale technology solutions that gave us additional capabilities, product offerings and client relationships.

In May 2005, we signed a five-year extension with Hilton HHonors Worldwide, one of our top-fifteen clients, to continue to provide integrated relationship management services, including database hosting and development, for the Hilton HHonors® Guest Rewards Program.

In May 2005, we signed a multi-year renewal agreement to continue providing private label credit card services for leading specialty retailers The Dress Barn, Inc. and Maurices Incorporated.

In June 2005, we completed the construction of a comprehensive database system for Pfizer Inc. to manage and host Pfizer s database solution geared toward enhancing Pfizer s overall consumer outreach efforts.

In July 2005, we signed an agreement to provide an integrated private label and co-brand credit card program for Gander Mountain Company, one of the fastest-growing retailers in the outdoor lifestyle industry.

In July 2005, we signed a long-term contract renewal with Pepco Energy Services, Inc. to continue hosting the customer information system and to provide traditional and electronic billing, payment processing and other services related to the support and maintenance of the customer information system.

In July 2005, we signed a multi-year renewal and expanded agreement with Bank of America to complete the build of an enhanced consumer marketing database and to host and manage the system on behalf of Bank of America.

In July 2005, we signed multi-year renewals with the operating subsidiaries of Sobeys Inc. in Atlantic Canda and the Province of Quebec to continue as participating regional grocery sponsors in the AIR MILES Reward Program.

In July 2005, we signed an agreement with Gordmans, Inc., an existing private label credit card client, to also provide a comprehensive servicing solution for their gift card program.

In August 2005, we signed an agreement with Hampton Roads Sanitation District to provide consulting services related to CIS selection, improvement of business processes and project management.

In August 2005, we signed an agreement to provide customer care maintenance and support services for Greenville Utilities Commission, a provider of electric, gas, water and wastewater services in North Carolina.

In September 2005, we acquired Bigfoot Interactive, now known as Epsilon Interactive, Inc., a leading full-service provider of strategic ROI-focused e-mail communications and marketing automation solutions.

In September 2005, we signed a multi-year agreement with Orion Payment Systems, a leading reseller of innovative payment solutions, to provide a complete suite of point-of-sale based services.

In September 2005, we entered into an agreement with CompUSA, Inc., one of the nation s leading retailers and resellers of technology products and services, to provide a full suite of loyalty marketing services for *The CompUSA Network*tm *For Business* loyalty program.

In October 2005, we signed a multi-year renewal with the Liquor Control Board of Ontario, a top-ten AIR MILES sponsor, to continue as a participating sponsor in the AIR MILES Reward Program.

In October 2005, we signed a long-term contract renewal with Amex Bank of Canada, a top-five AIR MILES sponsor, to continue to offer Canadians its American Express AIR MILES Credit Cards.

In October 2005, we signed long-term agreements with Spiegel Catalog and Newport News to provide co-brand credit card programs for both Spiegel and Newport News brands through 2013. The agreements expand the relationship with Spiegel and Newport News by adding a co-brand solution to the existing private label credit card programs we provide for each brand s catalog and online channels. Spiegel is a leading specialty retailer of women s fashions and home furnishings and Newport News markets women s apparel and accessories.

In November 2005, we entered into a seven-year agreement with PNM Resources retail energy provider in Texas, First Choice Power, to provide a full-service customer care solution for First Choice Power s 215,000-plus residential and business customers throughout Texas.

In November 2005, we extended our agreements with Limited Brands, one of our top-ten clients, to continue providing credit and programs extending across the following brands: Victoria s Secret, The Limited, Express, Bath and Body Works and Henri Bendel.

In December 2005, we signed a multi-year renewal with Canada Safeway Limited, a top-five AIR MILES sponsor, to continue as the Western Canadian regional grocery sponsor in the AIR MILES Reward Program.

Discussion of Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting policies that are described in the Notes to the Consolidated Financial Statements. The preparation of the consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We continually evaluate our judgments and estimates in determination of our financial condition and operating results. Estimates are based on information available as of the date of the financial statements and, accordingly, actual results could differ from these estimates, sometimes materially. Critical accounting policies and estimates are defined as those that are both most important to the portrayal of our financial condition and operating results and require management s most subjective judgments. The most critical accounting policies and estimates are described below.

Securitization of credit card receivables. We utilize a securitization program to finance substantially all of the credit card receivables that we underwrite. Our securitization trusts allow us to sell credit card receivables to the trusts on a daily basis. We use our off-balance sheet securitization program to lower our cost of funds and more efficiently use capital. In a securitization transaction, we sell credit card receivables originated by our Credit Services segment to a trust and retain servicing rights to those receivables, an equity interest in the trust, and an interest in the receivables. The securitization trusts are deemed to be qualifying special purpose entities under accounting principles generally accepted in the United States (GAAP) and are appropriately not included in our Consolidated Financial Statements. Our interest in the trusts is represented on our consolidated balance sheets as seller s interest (our interest in the receivables) and due from securitizations (our retained interests and credit enhancement components).

In turn, the trusts issue bonds in the capital markets and notes in private transactions. The proceeds from the debt are used to fund the receivables, while cash collected from cardholders is used to finance new receivables and repay borrowings and related borrowing costs. The excess spread is remitted to us as securitization income.

Our retained interest, often referred to as an interest-only strip, is recorded at fair value. Our interest-only strip has historically been valued between 1.75% and 2.50% of average securitized receivables. The fair value of our interest-only strip represents the present value of the anticipated cash flows we will receive over the estimated life of the receivables, or 7.5 months. This anticipated excess cash flow consists of the excess of finance charges and past-due fees net of the sum of the return paid to bond holders, estimated contractual servicing fees and credit losses. Because there is not a highly liquid market for these assets, we estimated the fair value of the interest-only strip primarily based upon discount, payment and default rates, which is the method we assume that another market participant would use to purchase the interest-only strip. The fair value of the interest-only strip, and the corresponding gain or loss, will be impacted by the estimated excess spread over the next two or three quarters. The excess spread is impacted primarily by finance and late fees collected, net charge-offs and interest rates.

Changes in the fair value of the interest-only strip are reflected in our consolidated financial statements as additional gains related to new receivables originated and securitized or other comprehensive income related to mark to market changes.

In recording and accounting for interest-only strips, we make assumptions about rates of payments and defaults that we believe reasonably reflect economic and other relevant conditions that affect fair value. Due to subsequent changes in economic and other relevant conditions, the actual rates of payments and defaults generally differ from our initial estimates, and these differences could sometimes be material. If actual payment and default rates are higher than previously assumed, the value of the interest-only strip could be impaired and the decline in the fair value recorded in earnings. Further sensitivity information is provided in Note 6 to the Consolidated Financial Statements.

We recognize the implicit forward contract to sell new receivables during a revolving period at its fair value at the time of sale. The implicit forward contract is entered into at the market rate and thus, its initial measure is zero at inception. In addition, we do not mark the forward contract to fair value in accounting periods following the securitization as we do not believe the fair value of the implicit forward contract in subsequent periods to be material.

AIR MILES Reward Program. Because management has determined that the earnings process is not complete at the time an AIR MILES reward mile is issued, the recognition of revenue on all fees received based on issuance is deferred. We allocate the proceeds from issuances of AIR MILES reward miles into two components based on the relative fair value of the related element:

Redemption element. The redemption element is the larger of the two components. For this component, we recognize revenue at the time an AIR MILES reward mile is redeemed, or, for those AIR MILES reward miles that we estimate will go unredeemed by the collector base, known as breakage, over the estimated life of an AIR MILES reward mile. The total amount of deferred revenue related to the redemption element is shown on the balance sheet as Deferred Revenue Redemption.

Service element. For this component, which consists of marketing and administrative services provided to sponsors, we recognize revenue pro rata over the estimated life of an AIR MILES reward mile. The total amount of deferred revenue related to the service element is shown on the balance sheet as Deferred Revenue Service.

Under certain of our contracts, a portion of the proceeds is paid to us at the issuance of AIR MILES reward miles and a portion is paid at the time of redemption. Under such contracts the proceeds received at issuance are initially deferred as service revenue and the revenue and earnings are recognized pro rata over the estimated life of an AIR MILES reward mile.

The amount of revenue recognized in a period is subject to the estimated life of an AIR MILES reward mile. Based on our historical analysis, we make a determination as to average life of an AIR MILES reward mile. The estimated life of an AIR MILES reward mile of 42 months and breakage of one-third has remained constant. Breakage and the life of an AIR MILES reward mile is based on management s estimate after viewing and analyzing various historical trends including vintage analysis,

Table of Contents

current run rates and other pertinent analysis. During 2005, we engaged a nationally recognized accounting firm to perform an independent analysis of our breakage assumptions. Their conclusion supports management s breakage estimate of one-third. The estimated life of an AIR MILES reward mile and breakage is actively monitored by management and subject to external influences that may cause actual performance to differ from estimates.

We believe that the issuance and redemption of AIR MILES reward miles is influenced by the nature and volume of sponsors, the type of rewards offered, the overall health of the Canadian economy, the nature and extent of AIR MILES promotional activity in the marketplace and the extent of competing loyalty programs. These influences will primarily affect the average life of an AIR MILES reward mile. We do not believe that the estimated life will vary significantly over time, consistent with historical trends. The shortening of the life of an AIR MILES reward mile will accelerate the recognition of revenue and may affect the breakage rate. As of December 31, 2005, we had $610.5 million in deferred revenue related to the AIR MILES Reward Program that will be recognized in the future. Further information is provided in Note 8 to the Consolidated Financial Statements.

Inter-Segment Sales

Our Transaction Services segment performs card processing and servicing activities related to our Credit Services segment. For this, our Transaction Services segment receives a fee equal to its direct costs before corporate overhead plus a margin. The margin is based on current estimated market rates for similar services. This fee represents an operating cost to the Credit Services segment and a corresponding revenue for our Transaction Services segment. Inter-segment sales are eliminated upon consolidation. Revenues earned by our Transaction Services segment from servicing our Credit Services segment, and consequently paid by our Credit Services segment to our Transaction Services segment, are set forth opposite Other/eliminations in the tables presented in the annual comparisons in our Results of Operations.

Use of Non-GAAP Financial Measures

Adjusted EBITDA is a non-GAAP financial measure equal to net income (loss), the most directly comparable GAAP financial measure, plus stock compensation expense, provision for income taxes, interest expense, net, fair value loss on interest rate derivative, depreciation and other amortization and amortization of purchased intangibles. Operating EBITDA is a non-GAAP financial measure equal to adjusted EBITDA plus the change in deferred revenue plus the change in redemption settlement assets. We have presented operating EBITDA because we use the financial measure as part of our monitoring of compliance with the financial covenants in our credit facilities. For the twelve months ended December 31, 2005, senior debt-to-operating EBITDA was 1.1x compared to a maximum ratio of 2.5x permitted in the credit facilities and operating EBITDA to interest expense was 22.0x compared to a minimum ratio of 3.5x permitted in the credit facilities. As discussed in more detail in the liquidity section of the Management s Discussion and Analysis of Financial Condition and Results of Operations , our credit facilities together with cash flow from operations are the two main sources of funding for our acquisition strategy and for our future working capital needs and capital expenditures. As of December 31, 2005, we had borrowings of $441.0 million outstanding under these credit facilities and had approximately $74.0 million in unused borrowing capacity. During January 2006, we increased our borrowing capacity by an incremental $300.0 million through entering into an additional credit agreement. We were in compliance with our covenants at December 31, 2005, and we expect to be in compliance with these covenants during the year ending December 31, 2006.

We use adjusted EBITDA as an integral part of our internal reporting to measure the performance of our reportable segments and to evaluate the performance of our senior management. Adjusted EBITDA is considered an important indicator of the operational strength of our businesses. Adjusted EBITDA eliminates the uneven effect across all business segments of considerable amounts of non-cash depreciation of tangible assets and amortization of certain intangible assets that were recognized in business combinations. A limitation of this measure, however, is that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in our businesses. Management evaluates the costs of such tangible and intangible assets, the impact of related impairments, as well as asset sales through other financial measures, such as capital expenditures, investment spending and return on capital. Adjusted EBITDA also eliminates the non-cash effect of stock compensation expense. Stock compensation expense is not included in the measurement of segment adjusted EBITDA provided to the chief operating decision maker for purposes of assessing segment performance and decision making with respect to resource allocations. Therefore, we believe that adjusted EBITDA provides useful information to our investors regarding our performance and overall results of operations. Adjusted EBITDA and operating EBITDA are not intended to be performance measures that should be regarded as an alternative to, or more meaningful than, either operating income or net income as an indicator of operating performance or to cash flows from operating activities as a measure of liquidity. In addition, adjusted EBITDA and operating EBITDA are not intended to represent funds available for dividends, reinvestment or other discretionary uses, and should not be considered in isolation or as a substitute for measures of performance prepared in accordance with GAAP. The adjusted EBITDA and operating EBITDA measures presented in this Annual Report on Form 10-K may not be comparable to similarly titled measures presented by other companies, and may not be identical to corresponding measures used in our various agreements.

	Year Ended December 31,				
	2001	2002	2003	2004	2005
	(Amounts in thousands)				
Net (loss) income	$ (10,362)	$ 23,659	$ 67,298	$ 102,371	$ 138,745
Stock compensation expense	1,786	2,948	5,889	15,767	14,143
Provision for income taxes	9,700	18,060	41,684	61,948	83,381
Interest expense, net	26,245	19,924	14,681	6,972	14,482
Fair value loss on interest rate derivative	15,131	12,017	2,851	808	
Other expenses[(1)]	6,025	834	4,275		
Depreciation and other amortization	30,698	41,768	53,948	62,586	58,565
Amortization of purchased intangibles	43,506	24,707	20,613	28,812	41,142
Adjusted EBITDA	122,729	143,917	211,239	279,264	350,458
Change in deferred revenue	29,603	34,827	113,877	70,736	63,410
Change in redemption settlement assets	1,677	(15,963)	(48,978)	(28,221)	(17,471)
Operating EBITDA	$ 154,009	$ 162,781	$ 276,138	$ 321,779	$ 396,397

Note: Change in deferred revenue and redemption settlement assets are affected by fluctuations in foreign exchange rates. Change in redemption settlement assets is also affected by transfers of cash.

(1) For the year ended December 31, 2001, other expenses primarily relate to the write off of equity investments. For the years ended December 2002 and 2003, other expenses are debt related.

Table of Contents

Results of Operations

Year ended December 31, 2004 compared to the year ended December 31, 2005

	Year Ended December 31,		Growth	
	2004	2005	$	%
	(In thousands, except percentages)			
Revenue:				
Transaction Services	$ 681,736	$ 699,884	$ 18,148	2.7%
Credit Services	513,988	561,413	47,425	9.2
Marketing Services	375,630	604,145	228,515	60.8
Other/ Eliminations	(313,916)	(313,005)	911	(0.3)
Total	$ 1,257,438	$ 1,552,437	$ 294,999	23.5%
Adjusted EBITDA:				
Transaction Services	$ 97,465	$ 90,074	$ (7,391)	(7.6)%
Credit Services	125,718	162,481	36,763	29.2
Marketing Services	56,081	97,903	41,822	74.6
Total	$ 279,264	$ 350,458	$ 71,194	25.5%
Stock compensation expense:				
Transaction Services	$ 5,255	$ 4,715	$ (540)	(10.3)%
Credit Services	5,256	4,714	(542)	(10.3)
Marketing Services	5,256	4,714	(542)	(10.3)
Total	$ 15,767	$ 14,143	$ (1,624)	(10.3)%
Depreciation and amortization:				
Transaction Services	$ 61,786	$ 56,583	$ (5,203)	(8.4)%
Credit Services	7,938	6,647	(1,291)	(16.3)
Marketing Services	21,674	36,477	14,803	68.3
Total	$ 91,398	$ 99,707	$ 8,309	9.1%
Operating income:				
Transaction Services	$ 30,424	$ 28,776	$ (1,648)	(5.4)%
Credit Services	112,524	151,120	38,596	34.3
Marketing Services	29,151	56,712	27,561	94.5
Total	$ 172,099	$ 236,608	$ 64,509	37.5%
Adjusted EBITDA margin[1]:				
Transaction Services	14.3%	12.9%	(1.4)%	
Credit Services	24.5	28.9	4.4	
Marketing Services	14.9	16.2	1.3	

Total	22.2%	22.6%	0.4%	
Segment operating data:				
Statements generated	190,976	190,910	(66)	
Credit Sales	$ 6,227,421	$ 6,582,800	$ 355,379	5.7%
Average managed receivables(2)	$ 3,021,800	$ 3,170,485	$ 148,685	4.9%
AIR MILES reward miles issued	2,834,125	3,246,553	412,428	14.6%
AIR MILES reward miles redeemed	1,782,185	2,023,218	241,033	13.5%

(1) Adjusted EBITDA margin is adjusted EBITDA divided by revenue. Management uses adjusted EBITDA margin to analyze the operating performance of the segments and the impact revenue growth has on operating expenses.

(2) Effective September 30, 2005, we will report average managed receivables as it better reflects our future business strategy. The difference between the previously reported metric, average securitized portfolio, and the current one is private label credit card receivables which are not securitized will also be included. Historically, this difference has not been meaningful but will be in the future as some private label credit card portfolios are not anticipated to be securitized for a period of time.

Revenue. Total revenue increased $295.0 million, or 23.5%, to $1,552.4 million for 2005 from $1,257.4 million for 2004. The increase was due to a 2.7% increase in Transaction Services revenue, a 9.2% increase in Credit Services revenue and a 60.8% increase in Marketing Services revenue as follows:

Transaction Services. Transaction Services revenue increased $18.1 million, or 2.7%, primarily due to new customers in utility services such as Cobb Energy. In addition, merchant services and private label had small increases in revenue. Utility services statement growth should increase in 2006 as existing and recently signed new clients complete their conversion to our billing platforms. The slight decrease in the number of statements generated is primarily attributable to one private label client that experienced a significant reduction in private label credit sales, which resulted in a corresponding reduction in statements generated for private label clients and the loss of a client that ceased operations in the fourth quarter of 2004 due to bankruptcy. Private label statements should also increase in 2006 from new portfolios brought on in the fourth quarter of 2005 and start-up programs.

Credit Services. Credit Services revenue increased $47.4 million, or 9.2%, primarily due to a 14.3% increase in securitization income, offset in part by decreases in merchant discount and servicing fees. Securitization income increased $53.9 million primarily as a result of an increase in the net yield from the securitization trusts in addition to a 4.9% increase in our average managed receivables. The net yield increased principally as a result of an approximate 100 basis point increase in the excess spread in addition to a 20 basis point decrease in cost of funds. Excess spread, which represents interest and late fees collected from cardholders, other trust-related fees, fair value changes related to the interest-only strips and charge-offs, increased due to lower charge-offs and higher collected fees from cardholders. The decrease in merchant discount is primarily the result of a change in mix of fees received from merchants compared to fees received from cardholders.

Marketing Services. Marketing Services revenue increased $228.5 million, or 60.8%, primarily due to an increase in database marketing fees attributable to the acquisition of Epsilon in the fourth quarter of 2004 and the subsequent acquisition of Epsilon Interactive in the fourth quarter of 2005, an increase in redemption revenue related to a 13.5% increase in the redemption of AIR MILES reward miles and an increase in the amortization of deferred services revenue. Changes in the exchange rate of the Canadian dollar accounted for approximately $21.8 million of the $228.5 million increase in our Marketing Services revenue, or 9.5% of the change. Deferred revenue is impacted by both the number of AIR MILES reward miles issued and redeemed, as well as foreign currency movements. Our deferred revenue balance increased 11.6% to $610.5 million at December 31, 2005 from $547.1 million at December 31, 2004 due to continued growth in the program, including a 14.6% increase in AIR MILES reward miles issued during the twelve months ended December 31, 2005 over the comparable period in 2004.

Operating Expenses. Total operating expenses, excluding depreciation, amortization and stock compensation expense increased $223.8 million, or 22.9%, to $1,202.0 million for 2005 from $978.2 million for 2004. Total adjusted EBITDA margin increased to 22.6% for 2005 from 22.2% for 2004. The increase in adjusted EBITDA margin is due to increases in Marketing Services and Credit Services margins, partially offset by a decrease in Transaction Services.

Transaction Services. Transaction Services operating expenses, excluding depreciation, amortization and stock compensation expense, increased $25.5 million, or 4.4%, to $609.8 million for 2005 from $584.3 million for 2004, and adjusted EBITDA margin decreased to 12.9% for 2005 from 14.3% for 2004. Operating expenses in the first half of 2005 included streamlining efforts in utility services. The decrease in adjusted EBITDA margin was primarily the result of higher expenses associated with corporate overhead, private label credit card clients and lower than expected volume growth.

Credit Services. Credit Services operating expenses, excluding depreciation, amortization and stock compensation expense, increased $10.6 million, or 2.7%, to $398.9 million for 2005 from

Table of Contents

$388.3 million for 2004, and adjusted EBITDA margin increased to 28.9% for 2005 from 24.5% for 2004. The increased adjusted EBITDA margin is the result of favorable revenue trends from increases in both our average managed receivables and net yield.

Marketing Services. Marketing Services operating expenses, excluding depreciation, amortization and stock compensation expense, increased $186.6 million, or 58.4%, to $506.2 million for 2005 from $319.6 million for 2004. The increase in operating expenses is primarily attributable to the acquisition of Epsilon in the fourth quarter of 2004 and the subsequent acquisition of Epsilon Interactive in the fourth quarter of 2005. Adjusted EBITDA margin increased to 16.2% for 2005 from 14.9% for 2004. The increase in adjusted EBITDA margin is the result of increased higher-margin revenue from both the AIR MILES reward program and database marketing fees from Epsilon and Epsilon Interactive, partially offset by additional corporate overhead expense.

Stock compensation expense. Stock compensation expense decreased $1.6 million, or 10.3%, to $14.1 million for 2005 from $15.8 million for 2004. The decrease is primarily related to a decline in the fair value of the restricted stock awards issued in 2005.

Depreciation and Amortization. Depreciation and amortization increased $8.3 million, or 9.1%, to $99.7 million for 2005 from $91.4 million for 2004. The increase is primarily due to an increase of $12.3 million in amortization of purchased intangibles related to recent acquisitions and new depreciation on 2005 capital expenditures, offset by a decrease of $4.0 million as a result of certain assets completing their depreciable lives in late 2004 and early 2005.

Operating Income. Operating income increased $64.5 million, or 37.5%, to $236.6 million for 2005 from $172.1 million for 2004. Operating income increased primarily from revenue gains and an increase in adjusted EBITDA margins partially offset by an increase in depreciation and amortization and stock compensation expense.

Interest Expense, net. Interest expense, net, increased $7.5 million, or 107.1%, to $14.5 million for 2005 from $7.0 million for 2004 due to higher average balances under our credit facilities and certificates of deposit.

Provision for Income Taxes. The provision for income taxes increased $21.5 million to $83.4 million in 2005 from $61.9 million in 2004 primarily due to an increase in taxable income. The effective rate remained relatively flat, decreasing to 37.5% in 2005 from 37.7% in 2004.

Year ended December 31, 2003 compared to the year ended December 31, 2004

	Year Ended December 31,		Growth	
	2003	**2004**	**$**	**%**
	(In thousands, except percentages)			
Revenue:				
Transaction Services	$ 614,454	$ 681,736	$ 67,282	10.9%
Credit Services	433,701	513,988	80,287	18.5
Marketing Services	289,764	375,630	85,866	29.6
Other/ Eliminations	(291,375)	(313,916)	(22,541)	7.7
Total	$ 1,046,544	$ 1,257,438	$ 210,894	20.2%
Adjusted EBITDA:				
Transaction Services	$ 88,001	$ 97,465	$ 9,464	10.8%
Credit Services	76,957	125,718	48,761	63.4
Marketing Services	46,281	56,081	9,800	21.2
Total	$ 211,239	$ 279,264	$ 68,025	32.2%
Stock compensation expense:				
Transaction Services	$ 1,963	$ 5,255	$ 3,292	167.7%
Credit Services	1,963	5,256	3,293	167.8
Marketing Services	1,963	5,256	3,293	167.8
Total	$ 5,889	$ 15,767	$ 9,878	167.7%
Depreciation and amortization:				
Transaction Services	$ 51,508	$ 61,786	$ 10,278	20.0%
Credit Services	5,581	7,938	2,357	42.2
Marketing Services	17,472	21,674	4,202	24.0
Total	$ 74,561	$ 91,398	$ 16,837	22.6%
Operating income:				
Transaction Services	$ 34,530	$ 30,424	$ (4,106)	(11.9)%
Credit Services	69,413	112,524	43,111	62.1
Marketing Services	26,846	29,151	2,305	8.6
Total	$ 130,789	$ 172,099	$ 41,310	31.6%
Adjusted EBITDA margin[1]:				
Transaction Services	14.3%	14.3%	%	
Credit Services	17.7	24.5	6.8	
Marketing Services	16.0	14.9	(1.1)	
Total	20.2%	22.2%	2.0%	

Segment operating data:				
Statements generated	167,118	190,976	23,858	14.3%
Credit Sales	$ 5,604,233	$ 6,227,421	$ 623,188	11.1%
Average managed receivables[(2)]	$ 2,654,087	$ 3,021,800	$ 367,713	13.9%
AIR MILES reward miles issued	2,571,501	2,834,125	262,624	10.2%
AIR MILES reward miles redeemed	1,512,788	1,782,185	269,397	17.8%

(1) Adjusted EBITDA margin is adjusted EBITDA divided by revenue. Management uses adjusted EBITDA margin to analyze the operating performance of the segments and the impact revenue growth has on operating expenses.

(2) Effective September 30, 2005, we will report average managed receivables as it better reflects our future business strategy. The difference between the previously reported metric, average securitized portfolio, and the current one is private label credit card receivables which are not securitized will also be included. Historically, this difference has not been meaningful but will be in the future as some private label credit card portfolios are not anticipated to be securitized for a period of time.

38

Revenue. Total revenue increased $210.9 million, or 20.2%, to $1,257.4 million for 2004 from $1,046.5 million for 2003. The increase was due to the following:

Transaction Services. Transaction Services revenue increased $67.3 million, or 10.9%, primarily due to an increase in the number of statements generated. Approximately one-half of the revenue increase is related to the increase in utility statements generated, which grew 27.9%. The growth in utility statements is primarily related to Conservation Billing Services Inc. (acquired in September 2003) and Orcom Solutions, Inc. (acquired in December 2003). Approximately one-third of the revenue increase is related to the increase in private label credit card statements generated, which grew 9.2%. The growth in private label credit card statements is primarily related to Stage Stores, Inc. (signed in September 2003) and Peebles Inc. (signed in January 2004) and core growth in existing clients. Additional growth in Transaction Services revenue came from an increase in merchant services revenue of 6.4% as our petroleum clients experienced higher transaction volume due to higher gas prices. Higher gas prices drive more frequent visits by consumers to our petroleum clients.

Credit Services. Credit Services revenue increased $80.3 million, or 18.5%, primarily due to an increase in securitization income. Approximately three-quarters of the increase in revenue is related to securitization income. Securitization income increased as a result of a 13.9% higher average managed receivables. The increase in average managed receivables is the result of new client signings and growth in our existing programs. The net yield on our retail portfolio for 2004 was approximately 60 basis points higher than in 2003. The increase in the net yield is largely related to lower net charge-offs of 20 basis points in addition to an increase in collected yield, partially offset by an increase in cost of funds. Additional revenue increases came from servicing fees and merchant fees. Servicing fees increased as a result of a 13.9% increase in average managed receivables. Merchant discount fees increased as a result of an 11.1% increase in credit sales.

Marketing Services. Marketing Services revenue increased $85.9 million, or 29.6%, primarily due to an increase in redemption, issuance and database marketing revenue. Approximately one-half of the increase in revenue is related to redemption revenue, which increased as a result of a 17.8% increase in the redemption of AIR MILES reward miles. Additionally, services revenue increased 16.3% as a result of a 10.2% increase in the number of AIR MILES reward miles issued and the corresponding recognition of deferred revenue balances. As a result of the increased issuance activity and the appreciation of the Canadian dollar as of December 31, 2004, our deferred revenue balance increased 14.8% to $547.1 million at December 31, 2004 from $476.4 million at December 31, 2003. The growth rate in the number of AIR MILES reward miles redeemed continues to outpace the growth rate in the number of AIR MILES reward miles issued, currently a positive indicator as to the success of the program. The increase in redemptions relates to the continued trend to offer more redemption options to our collectors, such as merchandise and certificates. Database marketing fees, including our historical database products in the United States and Canada, increased $24.4 million primarily as a result of our acquisition of Epsilon during the fourth quarter of 2004.

Operating Expenses. Total operating expenses, excluding depreciation, amortization and stock compensation expense increased $142.9 million, or 17.1%, to $978.2 million for 2004 from $835.3 million for 2003. Total adjusted EBITDA margin increased to 22.2% for 2004 from 20.2% for 2003. The increase in adjusted EBITDA margin is due to increases in Marketing Services and Credit Services margins.

Transaction Services. Transaction Services operating expenses, excluding depreciation, amortization and stock compensation expense, increased $57.8 million, or 11.0%, to $584.3 million for 2004 from $526.5 million for 2003, and adjusted EBITDA margin remained constant at 14.3% for 2004 and 2003. The lack of growth in adjusted EBITDA margin was primarily driven by excess capacity in our utility services business. We are currently streamlining processes to eliminate the excess capacity. The benefit from these consolidation efforts should begin to occur later in 2005 and

2006. Revenue gains and leverage in merchant services contributed positive adjusted EBITDA margin increases to offset the utility services decline.

Credit Services. Credit Services operating expenses, excluding depreciation, amortization and stock compensation expense, increased $31.6 million, or 8.9%, to $388.3 million for 2004 from $356.7 million for 2003, and adjusted EBITDA margin increased to 24.5% for 2004 from 17.7% for 2003. The increase in adjusted EBITDA margin is the result of favorable revenue trends from increased receivable balances, higher collected yield, lower net charge-offs, partially offset by an increase in cost of funds.

Marketing Services. Marketing Services operating expenses, excluding depreciation, amortization and stock compensation expense, increased $76.1 million, or 31.3%, to $319.6 million for 2004 from $243.5 million for 2003, and adjusted EBITDA margin decreased to 14.9% for 2004 from 16.0% for 2003. The decrease in adjusted EBITDA margin is the result of a higher mix of lower margin redemption revenue during the year.

Stock compensation expense. Stock compensation expense increased $9.9 million, or 167.7%, to $15.8 million for 2004 from $5.9 million for 2003. The increase is primarily related to the issuance and vesting of 199,120 shares of performance based restricted stock issued in 2001. Vesting occurred because we exceeded specific performance targets based on the stock performance over the last three years, among other performance measures.

Depreciation and Amortization. Depreciation and amortization increased $16.8 million, or 22.6%, to $91.4 million for 2004 from $74.6 million for 2003. The increase is primarily due to an increase of $8.2 million in amortization of purchased intangibles primarily related to the Orcom and Epsilon transactions. In addition, depreciation and amortization increased $8.6 million as a result of increased capital expenditures.

Operating Income. Operating income increased $41.3 million, or 31.6%, to $172.1 million for 2004 from $130.8 million for 2003. Operating income increased primarily from revenue gains, an increase in adjusted EBITDA margins offset by an increase in depreciation and amortization and stock compensation expense.

Interest Expense, net. Interest expense, net, decreased $7.7 million, or 52.4%, to $7.0 million for 2004 from $14.7 million for 2003 due to lower average debt outstanding.

Fair Value Loss on Derivatives. During 2004, we incurred a $0.8 million fair value loss on an interest rate swap compared to a $2.9 million loss in 2003. Part of the fair value loss was associated with cash payments we made to counterparties of $5.5 million and $11.1 million in 2004 and 2003, respectively. In accordance with Statement of Financial Accounting Standard (SFAS) No. 133, Accounting for Derivative Instruments and Hedging Activities , as amended, fair value changes in derivative instruments that do not meet the accounting criteria for hedge treatment are recorded as part of earnings. The related derivative was a $200.0 million notional amount interest rate swap that swapped a LIBOR based variable interest rate for a fixed interest rate, and expired in May 2004.

Provision for Income Taxes. The provision for income taxes increased $20.2 million to $61.9 million in 2004 from $41.7 million in 2003 primarily due to an increase in taxable income. The effective rate remained relatively flat, decreasing to 37.7% in 2004 from 38.3% in 2003.

Asset Quality

Our delinquency and net charge-off rates reflect, among other factors, the credit risk of our private label credit card receivables, the average age of our various private label credit card account portfolios, the success of our collection and recovery efforts, and general economic conditions. The average age of our private label credit card portfolio affects the stability of delinquency and loss rates of the portfolio. We continue to focus our resources on refining our credit underwriting standards for new accounts and on collections and post charge-off recovery efforts to minimize net losses.

Table of Contents

An older private label credit card portfolio generally drives a more stable performance in the portfolio. At December 31, 2005, 61.9% of securitized accounts with balances and 58.0% of securitized receivables were for accounts with origination dates greater than 24 months old. As of December 31, 2005, our allowance for doubtful accounts related to on-balance sheet private label credit card receivables was $38.4 million compared to $11.7 million as of December 31, 2004. The increase is primarily related to the acquisition of the Blair portfolio and secondarily on-balance sheet receivable growth and the related allowance for doubtful accounts.

Delinquencies. A credit card account is contractually delinquent if we do not receive the minimum payment by the specified due date on the cardholder s statement. It is our policy to continue to accrue interest and fee income on all credit card accounts, except in limited circumstances, until the account balance and all related interest and other fees are charged off or paid, beyond 90 days delinquent. When an account becomes delinquent, we print a message on the cardholder s billing statement requesting payment. After an account becomes 30 days past due, a proprietary collection scoring algorithm automatically scores the risk of the account rolling to a more delinquent status. The collection system then recommends a collection strategy for the past due account based on the collection score and account balance and dictates the contact schedule and collections priority for the account. Our proprietary system will zero out a customer s credit limit when charging privileges are removed from the account. If we are unable to make a collection after exhausting all in-house efforts, we engage collection agencies and outside attorneys to continue those efforts.

The following table presents the delinquency trends of our managed credit card portfolio:

	December 31, 2004	% of Total	December 31, 2005	% of Total
		(Dollars in thousands)		
Receivables outstanding	$ 3,352,870	100%	$ 3,714,548	100%
Receivables balances contractually delinquent:				
31 to 60 days	52,481	1.6%	59,018	1.6%
61 to 90 days	32,872	1.0	35,342	1.0
91 or more days	69,359	2.1	69,343	1.9
Total	$ 154,712	4.6%	$ 163,703	4.4%

Net Charge-Offs. Net charge-offs comprise the principal amount of losses from cardholders unwilling or unable to pay their account balances, as well as bankrupt and deceased cardholders, less current period recoveries. The following table presents our net charge-offs for the periods indicated on a managed basis. Average managed receivables represents the average balance of the cardholder receivables, excluding those which we do not bear the risk of loss, at the beginning of each month in the year indicated.

	Year Ended December 31,		
	2003	2004	2005
		(Dollars in thousands)	
Average managed receivables	$ 2,654,087	$ 3,021,800	$ 3,170,485
Net charge-offs	196,631	205,454	207,397
Net charge-offs as a percentage of average managed receivables	7.4%	6.8%	6.5%

We believe, consistent with our statistical models and other credit analyses, that our net charge-off ratio will continue to fluctuate.

Age of Portfolio. The median age of the portfolio is 36 months. The following table sets forth, as of December 31, 2005, the number of securitized accounts with balances and the related balances outstanding, based upon the age of the securitized accounts:

Age Since Origination	Number of Accounts	Percentage of Accounts	Balances Outstanding	Percentage of Balances Outstanding
		(Dollars in thousands)		
0-12 Months	3,116	27.4%	$ 844,662	24.2%
13-24 Months	1,656	14.6	482,638	13.8
25-36 Months	1,357	11.9	410,904	11.8
37-48 Months	1,046	9.2	334,244	9.6
49-60 Months	789	7.0	258,154	7.4
Over 60 Months	3,392	29.9	1,155,955	33.2
Total	11,356	100.0%	$ 3,486,557	100.0%

Liquidity and Capital Resources

Operating Activities. We have historically generated cash flows from operations, although that amount may vary based on fluctuations in working capital and the timing of merchant settlement activity. Our operating cash flow is seasonal, with cash utilization peaking at the end of December due to increased activity in our Credit Services segment related to holiday retail sales.

	Year Ended December 31,		
	2003	2004	2005
	(Dollars in thousands)		
Cash provided by operating activities before changes in credit card portfolio activity and merchant settlement activity	$ 189,606	$ 259,572	$ 293,863
Net change in credit card portfolio activity	(100,010)	71,121	(186,419)
Net change in merchant settlement activity	27,280	17,936	1,637
Cash provided by operating activities	$ 116,876	$ 348,629	$ 109,081

Net change in credit card portfolio activity represents the difference in portfolios purchased from new clients and their subsequent sale to our securitization trusts. There is typically a several month lag between the purchase and sale of credit card portfolios. During late 2005, we purchased credit card portfolios from Blair that have not been securitized. We securitized no portfolios in 2005. Merchant settlement activity is driven by the number of days of float at the end of the period. For these purposes, float means the difference between the number of days we hold cash before remitting the cash to our merchants and the number of days the card associations hold cash before remitting the cash to us. Merchant settlement activity fluctuates significantly depending on the day in which the period ends.

We generated cash flow from operating activities before changes in credit card portfolio activity and merchant settlement activity of $293.9 million for the year ended December 31, 2005 compared to $259.6 million for the comparable period in 2004 or a 13.2% increase. The increase in operating cash flows before changes in credit card portfolio activity and merchant settlement activity is primarily related to our increased earnings. We utilize our cash flow from operations for ongoing business operations, acquisitions and capital expenditures.

Investing Activities. We use a significant portion of our cash flows from operations for acquisitions and capital expenditures. We utilized cash flow for investing activities of $331.0 million for the year ended

December 31, 2005 compared to $399.9 million for the comparable period in 2004. Significant components of investing activities are as follows:

Acquisitions. During the year ended December 31, 2005, we had payments for acquired businesses totaling $140.9 million compared to $329.5 million in 2004. In 2005, we acquired Atrana Solutions, Inc. in a cash for common stock transaction and Bigfoot Interactive, now known as Epsilon Interactive, Inc., in a cash for equity transaction compared to the acquisitions of Epsilon Data Management, Inc. and Capstone Consulting Partners, Inc. in 2004.

Securitizations and Receivables Funding. We generally fund all private label credit card receivables through a securitization program that provides us with both liquidity and lower borrowing costs. As of December 31, 2005, we had over $3.4 billion of securitized credit card receivables. Securitizations require credit enhancements in the form of cash, spread accounts and additional receivables. The credit enhancement is funded through the use of certificates of deposit issued through our subsidiary, World Financial Network National Bank. Net securitization and credit card receivable activity utilized $107.8 million for the year ended December 31, 2005 compared to $8.3 million in 2004. We intend to utilize our securitization program for the foreseeable future.

Capital Expenditures. Our capital expenditures for the year ended December 31, 2005 were $65.9 million compared to $48.3 million for the prior year. Capital expenditures for 2005 increased in support of systems development work for new clients and contracts added during the year along with information technology infrastructure enhancements. We anticipate that capital expenditures will continue to remain at approximately 5% of annual revenues for the foreseeable future.

Financing Activities. Our cash flows provided by financing activities were $278.6 million in 2005 compared to $66.4 million used in financing activities in 2004. Our financing activities for 2005 relate to borrowings and repayments of debt in the normal course of business, an increase in borrowings of certificates of deposit related to the higher level of credit card receivables held on our balance sheet, $145.0 million from the repurchase of our common stock on the open market, and proceeds from the exercise of stock options.

Liquidity Sources. In addition to cash generated by operating activities, we have four main sources of liquidity: our securitization program; certificates of deposit issued by World Financial Network National Bank; our credit facilities; and issuances of equity securities. We believe that internally generated funds and existing sources of liquidity are sufficient to meet current and anticipated financing requirements during the next 12 months.

Securitization Program and Off-Balance Sheet Transactions. Since January 1996, we have sold, sometimes through WFN Credit Company, LLC and WFN Funding Company II, LLC, substantially all of the credit card receivables owned by our credit card bank, World Financial Network National Bank, to the WFN Trusts as part of our securitization program. This securitization program is the primary vehicle through which we finance our private label credit card receivables. The following table shows expected maturities for borrowing commitments of the WFN Trusts under our securitization program by year:

	2006	2007	2008	2009	2010 & Thereafter	Total
			(In thousands)			
Public notes	$ 450,000	$ 600,000	$ 600,000	$ 500,000	$ 450,000	$ 2,600,000
Private conduits[1]	982,857					982,857
Total	$ 1,432,857	$ 600,000	$ 600,000	$ 500,000	$ 450,000	$ 3,582,857

(1) Represents borrowing capacity, not outstanding borrowings.

As of December 31, 2005, the WFN Trusts had over $3.4 billion of securitized credit card receivables. Securitizations require credit enhancements in the form of cash, spread deposits and additional receivables. The credit enhancement is principally based on the outstanding balances of the series issued by the WFN Trusts and by the performance of the private label credit cards in the securitization trust. During the period from November to January, the WFN Trusts are required to maintain a credit enhancement level of between 6% and 10% of securitized credit card receivables. Certain of the WFN Trusts are required to maintain a level of between 4% and 9% for the remainder of the year. Accordingly, at December 31, 2005 the WFN Trusts typically have their highest balance of credit enhancement assets as a result of the increased balances during the holiday season. We intend to utilize our securitization program for the foreseeable future.

If World Financial Network National Bank were not able to regularly securitize the receivables it originates, our ability to grow or even maintain our credit services business would be materially impaired as we would be severely limited in our financing ability. World Financial Network National Bank s ability to effect securitization transactions is impacted by the following factors, some of which are beyond our control:

conditions in the securities markets in general and the asset-backed securitization market in particular;

conformity in the quality of credit card receivables to rating agency requirements and changes in those requirements; and

our ability to fund required overcollateralizations or credit enhancements, which we routinely utilize in order to achieve better credit ratings to lower our borrowing costs.

We believe that the conditions to securitize private label credit card receivables are favorable for us. We plan to continue using our securitization program as our primary financing vehicle.

Once World Financial Network National Bank securitizes receivables, the agreement governing the transaction contains covenants that address the receivables performance and the continued solvency of the retailer where the underlying sales were generated. In the event one of those or other similar covenants is breached, an early amortization event could be declared, in which case the trustee for the securitization trust would retain World Financial Network National Bank s interest in the related receivables, along with the excess interest income that would normally be paid to World Financial Network National Bank, until such time as the securitization investors are fully repaid. The occurrence of an early amortization event would significantly limit, or even negate, our ability to securitize additional receivables.

Certificates of Deposit. We utilize certificates of deposit to finance the operating activities and fund securitization enhancement requirements of our credit card bank subsidiaries, World Financial Network National Bank and World Financial Capital Bank. World Financial Network National Bank and World Financial Capital Bank issue certificates of deposit in denominations of $100,000 in various maturities ranging between three months and two years and with effective annual fixed rates ranging from 3.9% to 5.0%. As of December 31, 2005, we had $379.1 million of certificates of deposit outstanding. Certificate of deposit borrowings are subject to regulatory capital requirements.

Credit Facilities. On April 7, 2005, we entered into amendments to our three credit facilities. The amendment to the 3-year credit facility extended the maturity date from April 10, 2006 to April 3, 2008. The amendment to the 364-day credit facility extended the maturity date from April 7, 2005 to April 6, 2006. The amendment to the Canadian credit facility extended the maturity date from April 10, 2006 to April 3, 2008 and reduced the aggregate amount of the commitments permitted thereunder by $15.0 million from $50.0 million to $35.0 million.

On October 28, 2005, we entered into amendments to our three credit facilities to increase the amount of revolving commitments under the facilities and amend certain covenants. The amendment to the 3-year credit facility increased the amount of revolving commitments thereunder from $200.0 million to $250.0 million. The amendment to the 364-day credit facility increased the amount of revolving commitments thereunder from $205.0 million to $230.0 million. We anticipate extending this facility prior to its expiration. After giving effect to the three amendments, the aggregate amount of revolving commitments under the three credit facilities is $515.0 million. In addition, the amendments increased the aggregate amounts of commitments permitted under the three facilities from $500.0 million to $550.0 million. In addition, the amendments increased the amount of restricted payments permitted under the credit facilities.

On December 21, 2005, we entered into amendments to our three credit facilities to amend the definition of Senior Leverage Ratio under the applicable credit facility, the maximum Senior Leverage Ratio for the applicable credit facility and the maximum Total Capitalization Ratio for the applicable credit facility, and to revise the pricing grid set forth on the appendix to the applicable credit facility in connection with the foregoing. In addition, each amendment amended the applicable credit facility to allow us to incur certain indebtedness that is pari passu to or junior to the indebtedness incurred by us under such credit facility.

At December 31, 2005, we had borrowings of $441.0 million outstanding under these credit facilities (with an average interest rate of 4.6%), we issued no letters of credit, and we had available unused borrowing capacity of approximately $74.0 million. The credit facilities limit our aggregate outstanding letters of credit to $50.0 million.

During January 2006, we entered into an additional credit agreement to increase our borrowing capacity by an incremental $300.0 million. The principal amount of all outstanding loans under this credit agreement, together with any accrued but unpaid interest, are due and payable on June 30, 2006, unless otherwise paid earlier pursuant to the terms of the credit agreement. This credit agreement includes usual and customary negative covenants for credit agreements of this type. Payment of amounts due under this credit agreement are secured by guaranties, pledges of the ownership interests of certain of our subsidiaries and pledges of certain intercompany promissory notes. On January 5, 2006, we borrowed $300.0 million under this credit agreement, which we are using for general corporate purposes, including other debt repayment, repurchases of our common stock in connection with our stock repurchase program, mergers and acquisitions, and working capital expenditures. We anticipate refinancing this facility into a new term agreement.

Advances under the credit facilities are in the form of either base rate loans or Eurodollar loans. The interest rate on base rate loans fluctuates based upon the higher of (1) the interest rate announced by the administrative agent as its prime rate and (2) the Federal funds rate plus 0.5%, in each case with no additional margin. The interest rate on Eurodollar loans fluctuates based upon the rate at which Eurodollar deposits in the London interbank market are quoted plus a margin of 0.5% to 1.0% based upon the ratio of total debt under the credit facilities to consolidated Operating EBITDA, as each term is defined in the credit facilities. The credit facilities are secured by pledges of stock of certain of our subsidiaries and pledges of certain intercompany promissory notes.

We utilize our credit facilities and excess cash flows from operations to support our acquisition strategy and to fund working capital and capital expenditures.

Issuances of Equity Securities. In April 2003, we completed a public offering of 10,350,000 shares of our common stock at $19.65 per share. Limited Commerce Corp. sold 7,000,000 of those shares and the remaining 3,350,000 shares were sold by us. The net proceeds to us from the offering were $61.9 million after deducting offering expenses and our pro-rata underwriting discounts and commissions. Concurrently with the closing of the public offering, we used $52.7 million of the net proceeds to repay in full $52.0 million of debt outstanding, plus accrued interest, under a 10% subordinated note that we issued in September 1998 to an affiliated entity of Welsh Carson.

In November 2003, we facilitated a secondary public offering of 8,663,382 shares of common stock at $26.95 per share. 7,533,376 shares were sold by Limited Commerce Corp. and the remaining 1,130,006 shares were sold by Welsh Carson through two of its affiliated entities. We sold no stock and received none of the proceeds from the secondary offering. In connection with the secondary offering, we incurred approximately $450,000 in registration costs, which were expensed in the fourth quarter. As a result of the secondary offering, Limited Commerce Corp. is no longer a stockholder.

Repurchase of Equity Securities. During 2005, we repurchased approximately 3.9 million shares of our common stock for an aggregate amount of $148.8 million. We have Board authorization to purchase an additional $151.2 million of our common stock in 2006 and expect to finance the repurchase program with borrowing under our credit facilities.

Contractual Obligations. The following table highlights, as of December 31, 2005, our contractual obligations and commitments to make future payments by type and period:

	2006	2007 & 2008	2009 & 2010	2011 & Thereafter	Total[1]
			(Dollars in thousands)		
Certificates of deposit [2]	$ 348,760	$ 37,140	$	$	$ 385,900
Credit facilities[2]	244,327	225,099			469,426
Operating leases	41,419	62,632	35,646	59,431	199,128
Capital leases	7,340	11,457	1,025		19,822
Software licenses	21,445	45,273	48,619	25,629	140,966
Purchase obligations[3]	61,943	77,339	17,211		156,493
	$ 725,234	$ 458,940	$ 102,501	$ 85,060	$ 1,371,735

(1) The table does not include an estimate for income taxes that we are required to pay, but are not required to include above.

(2) The certificates of deposit and credit facilities represent our estimated debt service obligations, including both principle and interest. Interest was based on the interest rates in effect as of December 31, 2005, applied to the contractual repayment period.

(3) Purchase obligations include purchase commitments under our AIR MILES Reward Program, minimum payments under support and maintenance contracts and agreements to purchase other goods and services.

We believe that we will have access to sufficient resources to meet these commitments.

Economic Fluctuations

Although we cannot precisely determine the impact of inflation on our operations, we do not believe that we have been significantly affected by inflation. For the most part, we have relied on operating efficiencies from scale and technology, as well as decreases in technology and communication costs, to offset increased costs of employee compensation and other operating expenses.

Portions of our business are seasonal. Our revenues and earnings are favorably affected by increased transaction volume and credit card balances during the holiday shopping period in the fourth quarter and, to a lesser extent, during the first quarter as credit card balances are paid down. Similarly, our petroleum related businesses are favorably affected by increased volume in the latter part of the second quarter and the first part of the third quarter as consumers make more frequent purchases of gasoline in connection with summer travel.

Regulatory Matters

World Financial Network National Bank is subject to various regulatory capital requirements administered by the Office of the Comptroller of the Currency, or OCC. World Financial Capital Bank is subject to regulatory capital requirements administered by both the Federal Deposit Insurance Corporation, or FDIC, and the State of Utah. Failure to meet minimum capital requirements can trigger certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a material adverse effect on our financial statements. Under the FDIC s order approving World Financial Capital Bank s application for deposit insurance, World Financial Capital Bank must meet specific capital ratios and paid-in capital minimums, must maintain adequate allowances for loan losses and must operate within its three-year business plan. If World Financial Capital Bank fails to meet the terms of the FDIC s order, the FDIC may withdraw insurance coverage from World Financial Capital Bank, and the State of Utah may withdraw its approval of World Financial Capital Bank. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, World Financial Network National Bank must meet specific capital guidelines that involve quantitative measures of its assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. World Financial Network National Bank is limited in the amounts that it can dividend to us. World Financial Capital Bank is restricted from providing dividends to us at this time.

Quantitative measures established by regulations to ensure capital adequacy require World Financial Network National Bank to maintain minimum amounts and ratios of total and Tier 1 capital to risk weighted assets and of Tier 1 capital to average assets. Under the regulations, a well capitalized institution must have a Tier 1 capital ratio of at least 6%, a total capital ratio of at least 10% and a leverage ratio of at least 5% and not be subject to a capital directive order. An adequately capitalized institution must have a Tier 1 capital ratio of at least 4%, a total capital ratio of at least 8% and a leverage ratio of at least 4%, but 3% is allowed in some cases. Under these guidelines, World Financial Network National Bank is considered well capitalized. As of December 31, 2005, World Financial Network National Bank s Tier 1 capital ratio was 33.1%, total capital ratio was 34.6% and leverage ratio was 54.0%, and World Financial Network National Bank was not subject to a capital directive order. On April 22, 2005, World Financial Capital Bank received non-disapproval notification for a modification of the original three-year business plan. The letter of non-disapproval was issued jointly by the State of Utah and the FDIC. World Financial Capital Bank, under the terms of the letter, must maintain Total Risk-Based Capital equal to or exceeding 10% of total risk-based assets and must maintain Tier 1 capital to total assets ratio of not less than 16%. Both capital ratios must be maintained at or above the indicated levels until the end of the bank s de novo period on November 30, 2006.

As part of an acquisition in 2003 by World Financial Network National Bank, which required approval by the OCC, the OCC required World Financial Network National Bank to enter into an operating agreement with the OCC and a capital adequacy and liquidity maintenance agreement with us. The operating agreement requires World Financial Network National Bank to continue to operate in a manner consistent with its current practices, regulatory guidelines and applicable law, including those related to affiliate transactions, maintenance of capital and corporate governance. World Financial Network National Bank does not expect that the operating agreement will require any changes in World Financial Network National Bank s current operations. The capital adequacy and liquidity maintenance agreement memorializes our current obligations to World Financial Network National Bank.

Recent Accounting Pronouncements

In December 2003, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer . SOP 03-3 requires acquired loans, including debt securities, to be recorded at the amount of the purchaser s initial investment and prohibits carrying over valuation allowances from the seller for those individually evaluated loans that have evidence of deterioration in credit quality since origination, and it is probable all contractual cash flows on the loan will be unable to be collected. SOP 03-3 also requires the excess of all undiscounted cash flows expected to be collected at acquisition over the purchaser s initial investment to be recognized as interest income on a level-yield basis over the life of the loan. Subsequent increases in cash flows expected to be collected are recognized prospectively through an adjustment of the loan s yield over its remaining life, while subsequent decreases are recognized as impairment. We adopted the provisions of SOP 03-03 effective January 1, 2005. The adoption of this standard did not have a material impact on our financial condition, statements of income, or liquidity.

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 123 (revised 2004), Share-Based Payment , which replaces SFAS No. 123 Accounting for Stock-Based Compensation and supersedes Accounting Principles Board (APB) Opinion No. 25. SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. In addition, SFAS No. 123(R) will cause unrecognized expense (based on the fair values determined for the pro forma footnote disclosure, adjusted for estimated forfeitures) related to options vesting after the date of initial adoption to be recognized as a charge to results of operations over the remaining vesting period. Under SFAS No. 123(R), we must determine the appropriate fair value model to be used for valuing share-based payments, the amortization method for compensation cost and the transition method to be used at the date of adoption. The transition alternatives include the modified prospective or the modified retrospective adoption methods. Under the modified retrospective method, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented. The modified prospective method requires that compensation expense be recorded for all unvested stock options and share awards at the beginning of the first quarter of adoption of SFAS No. 123(R), while the modified retrospective methods would record compensation expense for all unvested stock options and share awards beginning with the first period restated.

In March 2005, the SEC released SAB 107, Share-Based Payment , which expresses views of the SEC Staff about the application of SFAS No. 123(R). SFAS No. 123(R) was to be effective for interim or annual reporting periods beginning on or after June 15, 2005, but in April 2005 the SEC issued a rule that SFAS No. 123(R) will be effective for annual reporting periods beginning on or after June 15, 2005. We expect to adopt the modified prospective method and expect it to have a material impact on our statements of income and earnings per share.

We will adopt SFAS No. 123(R) in the first quarter of 2006. In 2006, we will recognize approximately $21.8 million in expense for stock options issued prior to January 1, 2006, which were previously not expensed under APB No. 25. In 2005, the amount included in our pro forma disclosure was approximately $22.0 million for stock option expense. The total expense in 2006 and beyond will depend on several variables, including the number of share-based awards granted, the fair value of those awards, and the period over which the vesting of those awards is recognized; therefore, the actual expense may differ from this estimate.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3 . Opinion 20 previously required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. SFAS No. 154 requires retrospective application to prior periods financial statements of changes in accounting principle, unless it is impracticable to determine either the period specific effects or the cumulative effect of the change. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. We do not expect the adoption of SFAS No. 154 to have an impact on our consolidated financial statements.

In November 2005, the FASB issued FASB Staff Position (FSP) No. 115-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments . This FSP provides additional guidance on when an investment in a debt or equity security should be considered impaired and when that impairment should be considered other-than-temporary and recognized as a loss in earnings. Specifically, the guidance clarifies that an investor should recognize an impairment loss no later than when the impairment is deemed other-than-temporary, even if a decision to sell has not been made. The FSP also requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. FSP 115-1 nullifies certain provisions of Emerging Issues Task Force (EITF) Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments, while retaining the disclosure requirements of EITF 03-1 which were adopted in 2003. FSP 115-1 is effective for reporting periods beginning after December 15, 2005. We do not expect FSP 115-1 will significantly impact our financial condition or statements of income upon its adoption on January 1, 2006.

Table of Contents

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Market Risk

Market risk is the risk of loss from adverse changes in market prices and rates. Our primary market risks include off-balance sheet risk, interest rate risk, credit risk, foreign currency exchange rate risk and redemption reward risk.

Off-Balance Sheet Risk. We are subject to off-balance sheet risk in the normal course of business, including commitments to extend credit and through our securitization program. We sell substantially all of our credit card receivables to the WFN Trusts, qualifying special purpose entities. The trusts enter into interest rate swaps to reduce the interest rate sensitivity of the securitization transactions. The securitization program involves elements of credit, market, interest rate, legal and operational risks in excess of the amount recognized on the balance sheet through our retained interests in the securitization and the interest-only strips.

Interest Rate Risk. Interest rate risk affects us directly in our lending and borrowing activities. Our total interest incurred was approximately $151.7 million for 2005, which includes both on-and off-balance sheet transactions. Of this total, $14.5 million of the interest expense, net for 2005 was attributable to on-balance sheet indebtedness and the remainder to our securitized credit card receivables, which are financed off-balance sheet. To manage our risk from market interest rates, we actively monitor the interest rates and the interest sensitive components both on- and off-balance sheet to minimize the impact that changes in interest rates have on the fair value of assets, net income and cash flow. To achieve this objective, we manage our exposure to fluctuations in market interest rates by matching asset and liability repricings and through the use of fixed-rate debt instruments to the extent that reasonably favorable rates are obtainable with such arrangements. In addition, we enter into derivative financial instruments such as interest rate swaps and treasury locks to mitigate our interest rate risk on a related financial instrument or to lock the interest rate on a portion of our variable debt. We do not enter into derivative or interest rate transactions for trading or other speculative purposes. At December 31, 2005, we had $4.1 billion of debt, including $3.3 billion of off-balance sheet debt from our securitization program.

At December 31, 2005, 69.8% of our $4.1 billion of debt was fixed or effectively fixed through swap agreements.

- At December 31, 2005, 63.1% of our total debt, or 79.2% of our off-balance sheet debt, was locked at a current effective interest rate of 4.6% through interest rate swap agreements with notional amounts totaling $2.6 billion. Of the remaining 20.8% of our off-balance sheet debt, we have variable rate private label credit cards that are equal to or greater than the variable rate debt.

- At December 31, 2005, approximately 6.7% of our total debt, or 32.8% of our on-balance sheet debt, was subject to fixed rates with a weighted average interest rate of 4.2%.

The approach we use to quantify interest rate risk is a sensitivity analysis which we believe best reflects the risk inherent in our business. This approach calculates the impact on pretax income from an instantaneous and sustained increase in interest rates of 1.0%. In 2005, a 1.0% increase in interest rates would have resulted in an annual decrease to pretax income of approximately $5.6 million. Conversely, a corresponding decrease in interest rates would result in a comparable increase to pretax income. Our use of this methodology to quantify the market risk of financial instruments should not be construed as an endorsement of its accuracy or the accuracy of the related assumptions.

Credit Risk. We are exposed to credit risk relating to the credit card loans we make to our clients   customers. Our credit risk relates to the risk that consumers using the private label credit cards that we issue will not repay their revolving credit card loan balances. We have developed credit risk models designed to identify qualified consumers who fit our risk parameters. To minimize our risk of loan write-offs, we control approval rates of new accounts and related credit limits and follow strict collection practices. We monitor the buying limits, as well as set pricing regarding fees and interest rates charged.

Foreign Currency Exchange Rate Risk. We are exposed to fluctuations in the exchange rate between the U.S. and the Canadian dollar through our significant Canadian operations. We do not hedge any of our net investment exposure in our Canadian subsidiary.

Redemption Reward Risk. Through our AIR MILES Reward Program, we are exposed to potentially increasing reward costs associated primarily with travel rewards. To minimize the risk of rising travel reward costs, we:

- have multi-year supply agreements with several Canadian, U.S. and international airlines;
- are seeking new supply agreements with additional airlines;
- periodically alter the total mix of rewards available to collectors with the introduction of new merchandise rewards, which are typically lower cost per AIR MILES reward mile than air travel;
- allow collectors to obtain certain travel rewards using a combination of reward miles and cash or cash alone in addition to using AIR MILES reward miles alone; and
- periodically adjust the number of AIR MILES reward miles required to be redeemed to obtain a reward.

Item 8. Financial Statements and Supplementary Data

Our consolidated financial statements begin on page F-1 of this Form 10-K.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Table of Contents

Item 9A. Controls and Procedures

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

As of December 31, 2005, we carried out an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15 of the Securities Exchange Act of 1934. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that as of December 31, 2005, our disclosure controls and procedures are effective. Disclosure controls and procedures are controls and procedures designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms and include controls and procedures designed to ensure that information we are required to disclose in such reports is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Management s Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles in the United States.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree or compliance with the policies or procedures may deteriorate.

Our evaluation of and conclusion on the effectiveness of internal control over financial reporting did not include the internal controls of Atrana Solutions Inc., and Bigfoot Interactive, Inc., now known as Epsilon Interactive, entities we acquired during 2005, which are included in the 2005 consolidated financial statements and that constituted $164.6 million of total assets of as December 31, 2005 and an immaterial amount of revenues and net income for the year then ended. We did not assess the effectiveness of internal control over financial reporting at Atrana or Epsilon Interactive because of the timing of the acquisitions, which were completed in May 2005 and September 2005, respectively.

Under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of internal control over financial reporting. In conducting this evaluation, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control Integrated Framework.* Based on our evaluation and those criteria, our internal control over financial reporting was effective as of December 31, 2005.

During the fourth quarter of 2005, we completed the process of converting the Epsilon Data Management, Inc. legacy general ledger platform to the platform utilized by the majority of our business units. There have been no other changes in our internal control over financial reporting during the fourth quarter ended December 31, 2005 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management s assessment of the effectiveness of internal control over financial reporting as of December 31, 2005, has been audited by Deloitte & Touche LLP, the independent registered public accounting firm who also audited our consolidated financial statements. Deloitte & Touche s attestation report on management s assessment of our internal control over financial reporting appears on page F-3 hereof.

Item 9B. Other Information

None.

PART III

Item 10. Directors and Executive Officers of the Registrant

Incorporated by reference to the Proxy Statement for the 2006 Annual Meeting of our stockholders, which will be filed with the Securities and Exchange Commission not later than 120 days after December 31, 2005.

Item 11. Executive Compensation

Incorporated by reference to the Proxy Statement for the 2006 Annual Meeting of our stockholders, which will be filed with the Securities and Exchange Commission not later than 120 days after December 31, 2005.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Incorporated by reference to the Proxy Statement for the 2006 Annual Meeting of our stockholders, which will be filed with the Securities and Exchange Commission not later than 120 days after December 31, 2005.

Item 13. Certain Relationships and Related Transactions

Incorporated by reference to the Proxy Statement for the 2006 Annual Meeting of our stockholders, which will be filed with the Securities and Exchange Commission not later than 120 days after December 31, 2005.

Item 14. Principal Accountant Fees and Services

Incorporated by reference to the Proxy Statement for the 2006 Annual Meeting of our stockholders, which will be filed with the Securities and Exchange Commission not later than 120 days after December 31, 2005.

PART IV

Item 15. Exhibits, Financial Statement Schedules.

(a) The following documents are filed as part of this report:

(1) Financial Statements

(2) Financial Statement Schedule

(3) The following exhibits are filed as part of this Annual Report or, where indicated, were previously filed and are hereby incorporated by reference.

Exhibit No.	Description
2.1	Purchase and Sale Agreement, dated September 5, 2002, among ADS Alliance Data Systems, Inc., Loyalty Management Group Canada, Inc. and Westcoast Energy Inc. carrying on business as Duke Energy Gas Transmission (incorporated by reference to Exhibit No. 2.1 to our Current Report on Form 8-K filed with the SEC on September 10, 2002, File No. 001-15749).
2.2	Agreement and Plan of Merger, dated as of October 8, 2004, by and among Alliance Data Systems Corporation, ADS Alliance Data Systems, Inc., Everest Nivole, Inc., The Relizon e-CRM Company and Relizon Holding,s LLC (incorporated by reference to Exhibit No. 2.1 to our Current Report on Form 8-K filed with the SEC on October 29, 2004, File No. 0001-15749).

Table of Contents

Exhibit No.	Description
2.3	First Amendment to Agreement and Plan of Merger, dated as of October 8, 2004, by and among Alliance Data Systems Corporation, ADS Alliance Data Systems, Inc., Everest Nivole, Inc., The Relizon e-CRM Company and Relizon Holdings, LLC (incorporated by reference to Exhibit No. 2.2 to our Current Report on Form 8-K filed with the SEC on October 29, 2004, File No. 0001-15749).
3.1	Second Amended and Restated Certificate of Incorporation of the Registrant (incorporated by reference to Exhibit No. 3.1 to our Registration Statement on Form S-1 filed with the SEC on March 3, 2000, File No. 333-94623).
3.2	Second Amended and Restated Bylaws of the Registrant (incorporated by reference to Exhibit No. 3.2 to our Registration Statement on Form S-1 filed with the SEC on March 3, 2000, File No. 333-94623).
3.3	First Amendment to the Second Amended and Restated Bylaws of the Registrant (incorporated by reference to Exhibit No. 3.3 to our Registration Statement on Form S-1 filed with the SEC on May 4, 2001, File No. 333-94623).
3.4	Second Amendment to the Second Amended and Restated Bylaws of the Registrant (incorporated by reference to Exhibit No. 3.4 to our Annual Report on Form 10-K, filed with the SEC on April 1, 2002, File No. 001-15749).
4	Specimen Certificate for shares of Common Stock of the Registrant (incorporated by reference to Exhibit No. 4 to our Quarterly Report on Form 10-Q filed with the SEC on August 8, 2003, File No. 001-15749).
10.1	Build-to-Suit Net Lease between Opus South Corporation and ADS Alliance Data Systems, Inc., dated January 29, 1998, as amended (incorporated by reference to Exhibit No. 10.10 to our Annual Report on Form 10-K, filed with the SEC on April 1, 2002, File No. 001-15749).
10.2	Commercial Lease Agreement by and between Waterview Parkway L.P. and ADS Alliance Data Systems, Inc., dated July 16, 1997 (incorporated by reference to Exhibit No. 10.22 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623).
10.3	Lease between YCC Limited and London Life Insurance Company and Loyalty Management Group Canada Inc. dated May 28, 1997 and amended June 19, 1997 and January 15, 1998 (incorporated by reference to Exhibit No. 10.15 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623).
10.4	Amendments of April 14, 2000, January 17, 2001, and June 12, 2002 to lease between YCC Limited and London Life Insurance Company and Loyalty Management Group Canada Inc. dated May 28, 1997, as amended (incorporated by reference to Exhibit No. 10.12 to our Annual Report on Form 10-K filed with the SEC on March 12, 2003, File No. 001-15749).
10.5	Amendment, dated September 27, 2002, to Lease between YCC Limited and London Life Insurance Company and Loyalty Management Group Canada, Inc., dated May 28, 1997, as amended (incorporated by reference to Exhibit No. 10.5 to our Annual Report on Form 10-K, filed with the SEC on March 3, 2006).
10.6	Amendment, dated February 18, 2005, to Lease between Cadillac Fairview Corporation Limited and Loyalty Management Group Canada, Inc., dated May 28, 1997, as amended (incorporated by reference to Exhibit No. 10.6 to our Annual Report on Form 10-K, filed with the SEC on March 3, 2006).
10.7	Office Lease between Office City, Inc. and World Financial Network National Bank, dated December 24, 1986, and amended January 19, 1987, May 11, 1988, August 4, 1989 and

	August 18, 1999 (incorporated by reference to Exhibit No. 10.17 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623).
10.8	Lease Agreement by and between Continental Acquisitions, Inc. and World Financial Network National Bank, dated July 2, 1990, and amended September 11, 1990, November 16, 1990 and February 18, 1991 (incorporated by reference to Exhibit No. 10.18 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623).

Table of Contents

Exhibit No.	Description
10.9	Fourth Amendment to Lease Agreement by and between Partners at Brooksedge and ADS Alliance Data Systems, Inc., dated June 1, 2000 (incorporated by reference to Exhibit No. 10.1 to our Quarterly Report on Form 10-Q filed with the SEC on May 14, 2003, File No. 001-15749).
10.10	Fifth Amendment to Lease Agreement by and between Partners at Brooksedge and ADS Alliance Data Systems, Inc., dated June 30, 2001 (incorporated by reference to Exhibit No. 10.10 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
10.11	Indenture of Lease by and between OTR and ADS Alliance Data Systems, Inc., dated as of February 1, 2002, as amended (incorporated by reference to Exhibit No. 10.2 to our Quarterly Report on Form 10-Q filed with the SEC on May 14, 2003, File No. 001-15749).
10.12	Lease Agreement by and between Petula Associates, Ltd. and Compass International Services, dated August 28, 1998, as amended (incorporated by reference to Exhibit No. 10.1 to our Quarterly Report on Form 10-Q filed with the SEC on August 8, 2003, File No. 001-15749).
10.13	Lease Agreement by and between 601 Edgewater LLC and Epsilon Data Management, Inc., dated July 30, 2002 (incorporated by reference to Exhibit No. 10.17 to our Annual Report on Form 10-K filed with the SEC on March 4, 2005, File No. 001-15749).
10.14	Lease Agreement by and between Sterling Direct, Inc. and Sterling Properties, L.L.C., dated September 22, 1997, as subsequently assigned (incorporated by reference to Exhibit No. 10.18 to our Annual Report on Form 10-K filed with the SEC on March 4, 2005, File No. 001-15749).
10.15	Sublease by and between SonicNet, Inc. and Bigfoot Interactive, Inc., dated as of March 2003 (incorporated by reference to Exhibit No. 10.15 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
10.16	Lease Agreement by and between TM Park Avenue, LLC and Epsilon Interactive, LLC, dated February 10, 2006 (incorporated by reference to Exhibit No. 10.16 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
10.17	Lease Agreement by and between KDC-Regent I Investments, LP and Epsilon Data Management, Inc., dated May 31, 2005 (incorporated by reference to Exhibit No. 10.17 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
10.18	Offer to Lease by and between 592423 Ontario, Inc. and Loyalty Management Group Canada, Inc., dated November 3, 2005, to commence on September 17, 2007 (incorporated by reference to Exhibit No. 10.18 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
10.19	Lease Agreement by and between Milford Partners, LLC and ADS Alliance Data Systems, Inc. dated as of July 15, 2004 (incorporated by reference to Exhibit No. 10.19 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
10.20	Lease Agreement by and between 2855 E. Cottonwood Parkway, L.C. and ADS Alliance Data Systems, Inc., dated August 27, 2002 (incorporated by reference to Exhibit No. 10.20 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
10.21	Lease of Office Space by and between Morguard Real Estate Investment Trust and Alliance Data L.P., dated December 19, 2005 (incorporated by reference to Exhibit No. 10.21 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
10.22	

	Lease Agreement by and between Morrison Taylor, Ltd. and ADS Alliance Data Systems, Inc. dated July 1, 1997, and amended June 18, 1998 (incorporated by reference to Exhibit No. 10.21 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000).
10.23	Capital Assurance and Liquidity Maintenance Agreement, dated August 28, 2003, by and between Alliance Data Systems Corporation and World Financial Network National Bank (incorporated by reference to Exhibit No. 10.3 to our Registration Statement on Form S-3 filed with the SEC on October 15, 2003, File No. 333-109713).
+10.24	Alliance Data Systems Corporation Executive Deferred Compensation Plan (incorporated by reference to Exhibit No. 10.23 to our Annual Report on Form 10-K filed with the SEC on March 4, 2005, File No. 001-15749).

Exhibit No.	Description
+10.25	Alliance Data Systems Corporation Executive Annual Incentive Plan (incorporated by reference to Exhibit B to our Definitive Proxy Statement filed with the SEC on April 29, 2005, File No. 001-15749).
+10.26	Alliance Data Systems Corporation 2004 Incentive Compensation Plan (incorporated by reference to Exhibit No. 10.2 to our Quarterly Report on Form 10-Q, filed with the SEC on May 7, 2004, File No. 001-15749).
+10.27	Alliance Data Systems Corporation 2005 Incentive Compensation Plan (incorporated by reference to Exhibit No. 10.1 to our Quarterly Report on Form 10-Q, filed with the SEC on May 6, 2005, File No. 001-15749).
+10.28	Alliance Data Systems Corporation 2006 Incentive Compensation Plan. (incorporated by reference to Exhibit No. 10.28 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
+10.29	Amended and Restated Alliance Data Systems Corporation and its Subsidiaries Stock Option and Restricted Stock Plan (incorporated by reference to Exhibit No. 10.34 to our Registration Statement on Form S-1 filed with the SEC on May 4, 2001, File No. 333-94623).
+10.30	Form of Alliance Data Systems Corporation Incentive Stock Option Agreement (incorporated by reference to Exhibit No. 10.35 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623)
+10.31	Form of Alliance Data Systems Corporation Non-Qualified Stock Option Agreement (incorporated by reference to Exhibit No. 10.36 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623).
+10.32	Alliance Data Systems Corporation Amended and Restated Employee Stock Purchase Plan (incorporated by reference to Exhibit C to our Definitive Proxy Statement filed with the SEC on April 29, 2005, File No. 001-15749).
+10.33	Alliance Data Systems Corporation 2003 Long-Term Incentive Plan (incorporated by reference to Exhibit No. 4.6 to our Registration Statement on Form S-8 filed with the SEC on June 18, 2003, File No. 333-106246).
+10.34	Alliance Data Systems Corporation 2005 Long-Term Incentive Plan (incorporated by reference to Exhibit A to our Definitive Proxy Statement filed with the SEC on April 29, 2005, File No. 001-15749).
+10.35	Form of Nonqualified Stock Option Agreement for awards under the Alliance Data Systems Corporation 2005 Long Term Incentive Plan (incorporated by reference to Exhibit 10.4 to our Current Report on Form 8-K filed with the SEC on August 4, 2005, File No. 001-15749).
+10.36	Form of Restricted Stock Award Agreement for awards under the Alliance Data Systems Corporation 2005 Long Term Incentive Plan (incorporated by reference to Exhibit 10.5 to our Current Report on Form 8-K filed with the SEC on August 4, 2005, File No. 001-15749).
+10.37	Form of Non-Employee Director Nonqualified Stock Option Agreement (incorporated by reference to Exhibit No. 10.1 to our Current Report on Form 8-K filed with the SEC on June 13, 2005, File No. 001-15749).
+10.38	Form of Non-Employee Director Share Award Letter (incorporated by reference to Exhibit No. 10.2 to our Current Report on Form 8-K filed with the SEC on June 13, 2005, File No. 001-15749).

+10.39	Form of Alliance Data Systems Associate Confidentiality Agreement (incorporated by reference to Exhibit No. 10.24 to our Annual Report on Form 10-K filed with the SEC on March 12, 2003, File No. 001-15749).
+10.40	Form of Alliance Data Systems Corporation Indemnification Agreement for Officers and Directors (incorporated by reference to Exhibit No. 10.1 to our Current Report on Form 8-K filed with the SEC on February 1, 2005, File No. 001-15749).
+10.41	Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit 99.1 to our Registration Statement on Form S-8 filed with the SEC on July 20, 2001, File No. 333-65556).

Table of Contents

Exhibit No.	Description
+10.42	Amendment, dated February 4, 2003, to Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit No. 10.7 to our Quarterly Report on Form 10-Q filed with the SEC on May 14, 2003, File No. 001-15749).
+10.43	Amendment No. 2, dated April 7, 2003, to Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit No. 10.8 to our Quarterly Report on Form 10-Q filed with the SEC on May 14, 2003, File No. 001-15749).
+10.44	Amendment No. 3, dated May 8, 2003, to Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit No. 10.9 to our Quarterly Report on Form 10-Q filed with the SEC on May 14, 2003, File No. 001-15749).
+10.45	Amendment No. 4, dated June 9, 2003, to Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit No. 10.32 to our Annual Report on Form 10-K filed with the SEC on March 5, 2004, File No. 001-15749).
+10.46	Amendment No. 5, dated September 29, 2003, to Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit No. 10.33 to our Annual Report on Form 10-K filed with the SEC on March 5, 2004, File No. 001-15749).
+10.47	Amendment No. 6, dated December 12, 2003, to Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit No. 10.34 to our Annual Report on Form 10-K filed with the SEC on March 5, 2004, File No. 001-15749).
+10.48	Amendment No. 7, dated December 12, 2003, to Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit No. 10.35 to our Annual Report on Form 10-K filed with the SEC on March 5, 2004, File No. 001-15749).
+10.49	Amendment No. 8, dated December 12, 2003, to Alliance Data Systems 401(k) Retirement and Savings Plan (incorporated by reference to Exhibit No. 10.36 to our Annual Report on Form 10-K filed with the SEC on March 5, 2004, File No. 001-15749).
+10.50	Letter employment agreement with J. Michael Parks, dated February 19, 1997 (incorporated by reference to Exhibit 10.39 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623).
+10.51	Letter employment agreement with Ivan Szeftel, dated May 4, 1998 (incorporated by reference to Exhibit 10.40 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623).
10.52	Amended and Restated License to Use the Air Miles Trade Marks in Canada, dated as of July 24, 1998, by and between Air Miles International Holdings N.V. and Loyalty Management Group Canada Inc. (incorporated by reference to Exhibit No. 10.43 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333 - 94623) (assigned by Air Miles International Holdings N.V. to Air Miles International Trading B.V. by a novation agreement dated as of July 18, 2001).
10.53	Amended and Restated License to Use and Exploit the Air Miles Scheme in Canada, dated July 24, 1998, by and between Air Miles International Trading B.V. and Loyalty Management Group Canada Inc. (incorporated by reference to Exhibit No. 10.44 to our Registration Statement on Form S-1 filed with the SEC on January 13, 2000, File No. 333-94623).
10.54	Second Amended and Restated Pooling and Servicing Agreement, dated as of January 17, 1996 amended and restated as of September 17, 1999 and August 2001 by and among WFN Credit Company, LLC, World Financial Network National Bank, and BNY Midwest Trust Company (incorporated by reference to Exhibit No. 4.6 to the Registration Statement on

	Form S-3 of world financial network credit card master trust filed with the SEC on July 5, 2001, File No. 333-60418).
10.55	Second Amendment to the Second Amended and Restated Pooling and Servicing Agreement, dated as of May 19, 2004, among World Financial Network National Bank, WFN Credit Company, LLC and BNY Midwest Trust Company (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K filed by WFN Credit Company, LLC, World Financial Network Credit Card Master Trust and World Financial Network Credit Card Master Note Trust on August 4, 2004, File Nos. 333-60418, 333-60418-01 and 333-113669).

Exhibit No.	Description
10.56	Third Amendment to the Second Amended and Restated Pooling and Servicing Agreement, dated as of March 30, 2005, among World Financial Network National Bank, WFN Credit Company, LLC and BNY Midwest Trust Company (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K filed by World Financial Network Credit Card Master Trust and World Financial Network Credit Card Master Note Trust on April 4, 2005, File Nos. 333-60418, 333-60418-01 and 333-113669).
10.57	Omnibus Amendment, dated as of March 31, 2003, among WFN Credit Company, LLC, World Financial Network Credit Card Master Trust, World Financial Network National Bank and BNY Midwest Trust Company (incorporated by reference to Exhibit 4 to the Current Report on Form 8-K filed by WFN Credit Company, LLC and World Financial Network Credit Card Master Trust on April 22, 2003, File Nos. 333-60418 and 333-60418-01).
10.58	Transfer and Servicing Agreement, dated as of August 1, 2001, between WFN Credit Company, LLC, World Financial Network National Bank, and World Financial Network Credit Card Master Note Trust (incorporated by reference to Exhibit No. 4.3 to the Registration Statement on Form S-3 of World Financial Network Credit Card Master Trust filed with the SEC on July 5, 2001, File No. 333-60418).
10.59	First Amendment to the Transfer and Servicing Agreement, dated as of November 7, 2002, among WFN Credit Company, LLC, World Financial Network National Bank and World Financial Network Credit Card Master Note Trust (incorporated by reference to Exhibit 4.2 to the Current Report on Form 8-K filed by WFN Credit Company, LLC and World Financial Network Credit Card Master Trust on November 20, 2002, File Nos. 333-60418 and 333-60418-01).
10.60	Third Amendment to the Transfer and Servicing Agreement, dated as of May 19, 2004, among WFN Credit Company, LLC, World Financial Network National Bank and World Financial Network Credit Card Master Note Trust (incorporated by reference to Exhibit 4.2 of the Current Report on Form 8-K filed by WFN Credit Company, LLC, World Financial Network Credit Card Master Trust and World Financial Network Credit Card Master Note Trust on August 4, 2004, File Nos. 333- 60418, 333-60418-01 and 333-113669).
10.61	Fourth Amendment to the Transfer and Servicing Agreement, dated as of March 30, 2005, among WFN Credit Company, LLC, World Financial Network National Bank and World Financial Network Credit Card Master Note Trust (incorporated by reference to Exhibit 4.2 to the Current Report on Form 8-K filed by World Financial Network Credit Card Master Trust and World Financial Network Credit Card Master Note Trust on April 4, 2005, File Nos. 333-60418, 333-60418-01 and 333- 113669).
10.62	Receivables Purchase Agreement, dated as of August 1, 2001, between World Financial Network National Bank and WFN Credit Company, LLC (incorporated by reference to Exhibit 4.8 to the Registration Statement on Form S-3 of World Financial Network Credit Card Master Trust filed with the SEC on July 5, 2001, File No. 333-60418).
10.63	Master Indenture, dated as of August 1, 2001, between World Financial Network Credit Card Master Note Trust and BNY Midwest Trust Company, as supplemented by the Series 2001-A Indenture Supplement, the Series 2002-A Indenture Supplement, the Series 2002-VFN Supplement (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form S-3 filed with the SEC by WFN Credit Company, LLC and World Financial Network Credit Card Master Trust on July 5, 2001, File Nos. 333-60418 and 333-60418-01).
10.64	

	Series 2003-A Indenture Supplement, dated as of June 19, 2003 (incorporated by reference to Exhibit No. 4.1 to the Current Report on Form 8-K filed by World Financial Network Credit Card Master Trust filed with the SEC on August 28, 2003, File No. 333-60418-01).
10.65	Series 2004-A Indenture Supplement, dated as of May 19, 2004 (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K filed with the SEC by WFN Credit Company, LLC, World Financial Network Credit Card Master Trust and World Financial Network Credit Card Master Note Trust on May 27, 2004, File Nos. 333-60418, 333-60418-01 and 333-113669).

Exhibit No.	Description
10.66	Series 2004-B Indenture Supplement, dated as of September 22, 2004 (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K filed with the SEC by WFN Credit Company, LLC, World Financial Network Credit Card Master Trust and World Financial Network Credit Card Master Note Trust on September 28, 2004, File Nos. 333-60418, 333-60418-01 and 333-113669).
10.67	Series 2004-C Indenture Supplement, dated as of September 22, 2004 (incorporated by reference to Exhibit 4.2 of the Current Report on Form 8-K filed with the SEC by WFN Credit Company, LLC, World Financial Network Credit Card Master Trust and World Financial Network Credit Card Master Note Trust on September 28, 2004, File Nos. 333-60418, 333-60418-01 and 333-113669).
10.68	Supplemental Indenture No. 1, dated as of August 13, 2003, between World Financial Network Credit Card Master Note Trust and BNY Midwest Trust Company (incorporated by reference to Exhibit 4.2 of the Current Report on Form 8-K filed with the SEC by WFN Credit Company, LLC and World Financial Network Credit Card Master Trust on August 28, 2003, File Nos. 333-60418 and 333-60418-01).
10.69	Issuance Supplement to Series 2003-A Indenture Supplement, dated as of August 14, 2003, between World Financial Network Credit Card Master Note Trust and BNY Midwest Trust Company (incorporated by reference to Exhibit No. 4.3 of the Current Report on Form 8-K filed with the SEC by World Financial Network Credit Card Master Trust on August 28, 2003, File No. 333-60418-01).
10.70	Credit Agreement (3-Year), dated as of April 10, 2003, by and among Alliance Data Systems Corporation, the guarantors from time to time party thereto, the lenders from time to time party thereto, and Harris Trust and Savings Bank, as Administrative Agent (incorporated by reference to Exhibit No. 10.2 to Amendment No. 1 to our Registration Statement on Form S-3 filed with the SEC on April 16, 2003, File No. 333-104314).
10.71	First Amendment to Credit Agreement (3-Year), dated as of October 21, 2004, by and among Alliance Data Systems Corporation, the Guarantor party thereto, the Banks party thereto, and Harris Trust and Savings Bank, as Administrative Agent and Letter of Credit Issuer (incorporated by reference to Exhibit 10.3 to our Quarterly Report on Form 10-Q filed with the SEC on November 5, 2004, File No. 001-15749).
10.72	Second Amendment to Credit Agreement (3-Year), dated as of April 7, 2005, by and among Alliance Data Systems Corporation, the Guarantor party thereto, the Banks party thereto, and Harris Trust and Savings Bank, as Administrative Agent and Letter of Credit Issuer (incorporated by reference to Exhibit 99.1 to our Current Report on Form 8-K filed with the SEC on April 13, 2005, File No. 001-15749).
10.73	Third Amendment to Credit Agreement (3-Year), dated as of October 28, 2005, by and among Alliance Data Systems Corporation, the Guarantor party thereto, the Banks party thereto, and Harris N.A., as Administrative Agent and Letter of Credit Issuer (incorporated by reference to Exhibit 99.1 to our Current Report on Form 8-K filed with the SEC on October 31, 2005, File No. 001-15749).
10.74	Fourth Amendment to Credit Agreement (3-Year), dated as of December 21, 2005, by and among Alliance Data Systems Corporation, the Guarantor party thereto, the Banks party thereto, and Harris N.A., as Administrative Agent and Letter of Credit Issuer (incorporated by reference to Exhibit 99.1 to our Current Report on Form 8-K filed with the SEC on December 27, 2005, File No. 001-15749).

10.75	Credit Agreement (364-Day), dated as of April 10, 2003, by and among Alliance Data Systems Corporation, the guarantors from time to time party thereto, the lenders from time to time party thereto, and Harris Trust and Savings Bank, as Administrative Agent (incorporated by reference to Exhibit No. 10.3 to Amendment No. 1 to our Registration Statement on Form S-3 filed with the SEC on April 16, 2003, File No. 333-104314).

Exhibit No.	Description
10.76	First Amendment to Credit Agreement (364-Day) dated as of April 8, 2004, by and among Alliance Data Systems Corporation, the guarantors from time to time party thereto, the lenders from time to time party thereto, and Harris Trust and Savings Bank, as Administrative Agent (incorporated by reference to Exhibit 10.1 to our Quarterly Report on Form 10-Q filed with the SEC on May 7, 2004, File No. 001-15749).
10.77	Second Amendment to Credit Agreement (364-Day), dated as of October 21, 2004, by and among Alliance Data Systems Corporation, the Guarantor party thereto, the Banks party thereto, and Harris Trust and Savings Bank, as Administrative Agent and Letter of Credit Issuer (incorporated by reference to Exhibit 10.4 to our Quarterly Report on Form 10-Q filed with the SEC on November 5, 2004, File No. 001-15749).
10.78	Third Amendment to Credit Agreement (364-Day), dated as of April 7, 2005, by and among Alliance Data Systems Corporation, the Guarantor party thereto, the Banks party thereto, and Harris Trust and Savings Bank, as Administrative Agent and Letter of Credit Issuer (incorporated by reference to Exhibit 99.2 to our Current Report on Form 8-K filed with the SEC on April 13, 2005, File No. 001-15749).
10.79	Fourth Amendment to Credit Agreement (364-Day), dated as of October 28, 2005, by and among Alliance Data Systems Corporation, the Guarantor party thereto, the Banks party thereto, and Harris N.A., as Administrative Agent and Letter of Credit Issuer (incorporated by reference to Exhibit 99.2 to our Current Report on Form 8-K filed with the SEC on October 31, 2005, File No. 001-15749).
10.80	Fifth Amendment to Credit Agreement (364-Day), dated as of December 21, 2005, by and among Alliance Data Systems Corporation, the Guarantor party thereto, the Banks party thereto, and Harris N.A., as Administrative Agent and Letter of Credit Issuer (incorporated by reference to Exhibit 99.2 to our Current Report on Form 8-K filed with the SEC on December 27, 2005, File No. 001-15749).
10.81	Credit Agreement (Canadian), dated as of April 10, 2003, by and among Loyalty Management Group Canada Inc., the guarantors from time to time party thereto, the lenders from time to time party thereto, and Harris Trust and Savings Bank, as Administrative Agent (incorporated by reference to Exhibit No. 10.4 to Amendment No. 1 to our Registration Statement on Form S-3 filed with the SEC on April 16, 2003, File No. 333-104314).
10.82	First Amendment to Credit Agreement (Canadian), dated as of October 21, 2004, by and among Loyalty Management Group Canada Inc., the Guarantors party thereto, the Banks party thereto, Bank of Montreal, as Letter of Credit Issuer, and Harris Trust and Savings Bank, as Administrative Agent (incorporated by reference to Exhibit 10.5 to our Quarterly Report on Form 10-Q filed with the SEC on November 5, 2004, File No. 001-15749).
10.83	Second Amendment to Credit Agreement (Canadian), dated as of April 7, 2005, by and among Loyalty Management Group Canada Inc., the Guarantors party thereto, the Banks party thereto, Bank of Montreal, as Letter of Credit Issuer, and Harris Trust and Savings Bank, as Administrative Agent (incorporated by reference to Exhibit 99.3 to our Current Report on Form 8-K filed with the SEC on April 13, 2005, File No. 001-15749).
10.84	Third Amendment to Credit Agreement (Canadian), dated as of October 28, 2005, by and among Loyalty Management Group Canada Inc., the Guarantors party thereto, the Banks party thereto, Bank of Montreal, as Letter of Credit Issuer, and Harris N.A., as Administrative Agent (incorporated by reference to Exhibit 99.3 to our Current Report on Form 8-K filed with the SEC on October 31, 2005, File No. 001-15749).

10.85	Fourth Amendment to Credit Agreement (Canadian), dated as of December 21, 2005, by and among Loyalty Management Group Canada Inc., the Guarantors party thereto, the Banks party thereto, Bank of Montreal, as Letter of Credit Issuer, and Harris N.A., as Administrative Agent (incorporated by reference to Exhibit 99.3 to our Current Report on Form 8-K filed with the SEC on December 27, 2005, File No. 001-15749).

Exhibit No.	Description
10.86	Credit Agreement, dated as of January 3, 2006, by and among Alliance Data Systems Corporation, ADS Alliance Data Systems, Inc., as Guarantor, the Banks party thereto, and Harris N.A., as Administrative Agent and Lead Arranger (incorporated by reference to Exhibit 99.1 to our Current Report on Form 8-K filed with the SEC on January 9, 2006, File No. 001-15749).
+10.87	Form of Change in Control Agreement, dated as of September 25, 2003, by and between ADS Alliance Data Systems, Inc. and each of Daniel P. Finkelman, Edward J. Heffernan, John W. Scullion, Ivan M. Szeftel, Transient C. Taylor, Dwayne H. Tucker and Alan M. Utay (incorporated by reference to Exhibit No. 10.1 to our Registration Statement on Form S-3 filed with the SEC on October 15, 2003, File No. 333-109713).
+10.88	Change in Control Agreement, dated as of September 25, 2003, by and between ADS Alliance Data Systems, Inc. and J. Michael Parks (incorporated by reference to Exhibit No. 10.2 to our Registration Statement on Form S-3 filed with the SEC on October 15, 2003, File No. 333-109713).
10.89	Stockholders Agreement dated as of June 12, 2001, among Alliance Data Systems Corporation, Limited Commerce Corp., Welsh, Carson, Anderson, and Stowe VI, L.P., Welsh, Carson, Anderson & Stowe VII, L.P., Welsh, Carson, Anderson & Stowe VIII, L.P., WCAS Information Partners, L.P., WCAS Capital Partners II, L.P., and WCAS Capital Partners III, L.P. (incorporated by reference to Exhibit 10.14 to our Annual Report on Form 10-K, filed with the SEC on April 1, 2002, File No. 001-15749).
10.90	First Amendment, dated as of April 9, 2003, to Stockholders Agreement, dated as of June 12, 2001, among Alliance Data Systems Corporation, Limited Commerce Corp., Welsh, Carson, Anderson, and Stowe VI, L.P., Welsh, Carson, Anderson & Stowe VII, L.P., Welsh, Carson, Anderson & Stowe VIII, L.P., WCAS Information Partners, L.P., WCAS Capital Partners II, L.P., and WCAS Capital Partners III, L.P. (incorporated by reference to Exhibit No. 10.1 to Amendment No. 1 to our Registration Statement on Form S-3 filed with the SEC on April 16, 2003, File No. 333-104314).
21	Subsidiaries of the Registrant (incorporated by reference to Exhibit No. 21 to our Annual Report on Form 10-K filed with the SEC on March 3, 2006).
*23.1	Consent of Deloitte & Touche LLP.
*31.1	Certification of Chief Executive Officer of Alliance Data Systems Corporation pursuant to Rule 13a-14(a) promulgated under the Securities Exchange Act of 1934, as amended.
*31.2	Certification of Chief Financial Officer of Alliance Data Systems Corporation pursuant to Rule 13a-14(a) promulgated under the Securities Exchange Act of 1934, as amended.
*32.1	Certification of Chief Executive Officer of Alliance Data Systems Corporation pursuant to Rule 13a-14(b) promulgated under the Securities Exchange Act of 1934, as amended, and Section 1350 of Chapter 63 of Title 18 of the United States Code.
*32.2	Certification of Chief Financial Officer of Alliance Data Systems Corporation pursuant to Rule 13a-14(b) promulgated under the Securities Exchange Act of 1934, as amended, and Section 1350 of Chapter 63 of Title 18 of the United States Code.

* Filed herewith.
+ Management contract, compensatory plan or arrangement.

Table of Contents

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS
ALLIANCE DATA SYSTEMS CORPORATION

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders of
Alliance Data Systems Corporation

We have audited the accompanying consolidated balance sheets of Alliance Data Systems Corporation and subsidiaries (the Company) as of December 31, 2005 and 2004, and the related consolidated statements of income, stockholders equity, and cash flows for each of the three years in the period ended December 31, 2005. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and financial statement schedule are the responsibility of the Company s management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Alliance Data Systems Corporation and subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 31, 2005, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 2, 2006 expressed an unqualified opinion on management s assessment of the effectiveness of the Company s internal control over financial reporting and an unqualified opinion on the effectiveness of the Company s internal control over financial reporting. As described in our report dated March 2, 2006, management excluded from their assessment the internal control over financial reporting of Atrana Solutions, Inc. (Atrana) and Epsilon Interactive, Inc. (Epsilon Interactive), which were acquired in May and September, 2005, respectively; accordingly, our audit did not include the internal control over financial reporting at Atrana or Epsilon Interactive.

/s/ Deloitte & Touche LLP
Dallas, Texas
March 2, 2006

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders of
Alliance Data Systems Corporation

We have audited management s assessment, included in the accompanying Management s Report on Internal Control Over Financial Reporting, that Alliance Data Systems Corporation and subsidiaries (the Company) maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. As described in Management s Report on Internal Control Over Financial Reporting, management excluded from their assessment the internal control over financial reporting at Atrana Solutions, Inc. (Atrana) and Epsilon Interactive, Inc. (Epsilon Interactive) which were acquired in May and September, 2005, respectively, and whose collective financial statements reflect total assets and revenues constituting six and one percent, respectively, of the related consolidated financial statement amounts as of and for the year ended December 31, 2005. Accordingly, our audit did not include the internal control over financial reporting at Atrana or Epsilon Interactive. The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management s assessment and an opinion on the effectiveness of the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management s assessment that the Company maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements and financial statement schedule as of and for the year ended December 31, 2005 of the Company and our report dated March 2, 2006 expressed an unqualified opinion on those financial statements and financial statement schedule.

/s/ Deloitte & Touche LLP
Dallas, Texas
March 2, 2006

Table of Contents

ALLIANCE DATA SYSTEMS CORPORATION
CONSOLIDATED STATEMENTS OF INCOME

	Year Ended December 31,		
	2003	**2004**	**2005**
	(In thousands, except per share amounts)		
Revenues			
Transaction	$ 530,242	$ 599,969	$ 626,055
Redemption	180,782	226,726	275,840
Securitization income	294,816	355,912	405,868
Database marketing fees and marketing services	17,803	44,880	185,309
Other revenue	22,901	29,951	59,365
Total revenue	1,046,544	1,257,438	1,552,437
Operating expenses			
Cost of operations	788,874	916,201	1,124,590
General and administrative	52,320	77,740	91,532
Depreciation and other amortization	53,948	62,586	58,565
Amortization of purchased intangibles	20,613	28,812	41,142
Total operating expenses	915,755	1,085,339	1,315,829
Operating income	130,789	172,099	236,608
Other expenses	4,275		
Fair value loss on interest rate derivative	2,851	808	
Interest expense, net	14,681	6,972	14,482
Income before income taxes	108,982	164,319	222,126
Provision for income taxes	41,684	61,948	83,381
Net income	$ 67,298	$ 102,371	$ 138,745
Net income per share:			
Basic	$ 0.86	$ 1.27	$ 1.69
Diluted	$ 0.84	$ 1.22	$ 1.64
Weighted average shares:			
Basic	78,003	80,614	82,208
Diluted	80,313	84,040	84,637

See accompanying notes to consolidated financial statements.

Table of Contents

ALLIANCE DATA SYSTEMS CORPORATION
CONSOLIDATED BALANCE SHEETS

	December 31,	
	2004	2005
	(In thousands, except per share amounts)	
ASSETS		
Cash and cash equivalents	$ 84,409	$ 143,213
Due from card associations	10,995	58,416
Trade receivables, less allowance for doubtful accounts ($1,458 and $2,079 at December 31, 2004 and 2005, respectively)	158,236	203,883