FAIR ISAAC CORP
Form 10-Q
February 07, 2007

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

(Mark One)

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

For the quarterly period ended December 31, 2006

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
[NO FEE REQUIRED]

For the transition period from _________ to _________

Commission File Number 0-16439

Fair Isaac Corporation

(Exact name of registrant as specified in its charter)

Delaware	**94-1499887**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
901 Marquette Avenue, Suite 3200 Minneapolis, Minnesota	**55402-3232**
(Address of principal executive offices)	*(Zip Code)*

Registrant s telephone number, including area code:
612-758-5200

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

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 Exchange Act). o Yes þ No

The number of shares of common stock outstanding on January 31, 2007 was 57,118,843 (excluding 31,737,940 shares held by the Company as treasury stock).

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PART I FINANCIAL INFORMATION

Item 1. *Financial Statements*

FAIR ISAAC CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except par value data)
(Unaudited)

	December 31, 2006	September 30, 2006
Assets		
Current assets:		
Cash and cash equivalents	$ 99,149	$ 75,154
Marketable securities available for sale, current portion	122,812	152,141
Receivables, net	176,547	165,806
Prepaid expenses and other current assets	16,680	17,998
Deferred income taxes		2,211
Total current assets	415,188	413,310
Marketable securities available for sale, less current portion	47,362	38,318
Other investments	2,374	2,161
Property and equipment, net	54,650	56,611
Goodwill	701,068	695,162
Intangible assets, net	85,467	90,900
Deferred income taxes	17,637	20,010
Other assets	4,424	4,733
	$ 1,328,170	$ 1,321,205
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 14,912	$ 12,162
Senior convertible notes	400,000	400,000
Revolving line of credit	70,000	
Accrued compensation and employee benefits	40,567	34,936
Other accrued liabilities	41,698	41,647
Deferred revenue	47,131	48,284
Total current liabilities	614,308	537,029
Other liabilities	14,166	14,148
Total liabilities	628,474	551,177
Stockholders equity:		
Preferred stock ($0.01 par value; 1,000 shares authorized; none issued and outstanding)		

Common stock ($0.01 par value; 200,000 shares authorized, 88,857 shares issued and 57,004 and 59,369 shares outstanding at December 31, 2006 and September 30, 2006, respectively)	570	594
Paid-in-capital	1,077,466	1,073,886
Treasury stock, at cost (31,853 and 29,488 shares at December 31, 2006 and September 30, 2006, respectively)	(1,062,725)	(952,979)
Retained earnings	674,925	644,836
Accumulated other comprehensive income	9,460	3,691
Total stockholders equity	699,696	770,028
	$ 1,328,170	$ 1,321,205

See accompanying notes to condensed consolidated financial statements.

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FAIR ISAAC CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except per share data)
(Unaudited)

	Quarter Ended December 31, 2006	Quarter Ended December 31, 2005
Revenues	$ 208,227	$ 202,790
Operating expenses:		
Cost of revenues (1)	70,569	67,045
Research and development	17,719	22,730
Selling, general and administrative (1)	68,648	63,383
Amortization of intangible assets (1)	6,390	6,263
Restructuring and acquisition-related		(674)
Total operating expenses	163,326	158,747
Operating income	44,901	44,043
Interest income	3,564	3,066
Interest expense	(2,676)	(2,135)
Other expense, net	(453)	(86)
Income before income taxes	45,336	44,888
Provision for income taxes	14,111	16,431
Net income	$ 31,225	$ 28,457
Earnings per share:		
Basic	$ 0.54	$ 0.44
Diluted	$ 0.52	$ 0.43
Shares used in computing earnings per share:		
Basic	58,057	64,211
Diluted	59,985	66,219

(1) Cost of revenues and selling, general

and administrative expenses exclude the amortization of intangible assets. See Note 2 to the accompanying condensed consolidated financial statements.

See accompanying notes to condensed consolidated financial statements.

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FAIR ISAAC CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME
(In thousands)
(Unaudited)

	Common Stock Shares	Common Stock Par Value	Paid-In-Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income	Total Stockholders Equity	Comprehensive Income
Balance at September 30, 2006	**59,369**	**$ 594**	**$ 1,073,886**	**$ (952,979)**	**$ 644,836**	**$ 3,691**	**$ 770,028**	
Share-based compensation			9,572				9,572	
Exercise of stock options	1,200	12	(12,859)	39,384			26,537	
Tax benefit from exercised stock options			7,896				7,896	
Repurchases of common stock	(3,725)	(37)		(154,453)			(154,490)	
Issuance of ESPP shares from treasury	140	1	(383)	4,677			4,295	
Issuance of restricted stock to employees from treasury	20		(646)	646				
Dividends paid					(1,136)		(1,136)	
Net income					31,225		31,225	$ 31,225
Unrealized gains on investments						76	76	76
Cumulative translation adjustments						5,693	5,693	5,693
Balance at December 31, 2006	**57,004**	**$ 570**	**$ 1,077,466**	**$ (1,062,725)**	**$ 674,925**	**$ 9,460**	**$ 699,696**	**$ 36,994**

See accompanying notes to condensed consolidated financial statements.

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FAIR ISAAC CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Quarter Ended December 31,	
	2006	**2005**
Cash flows from operating activities:		
Net income	$ 31,225	$ 28,457
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,549	12,059
Share-based compensation	9,572	9,514
Deferred income taxes	2,375	(3,041)
Tax benefit from exercised stock options	7,896	6,633
Excess tax benefits from share-based payment arrangements	(2,178)	(3,647)
Net amortization (accretion) of premium (discount) on marketable securities	(365)	35
Provision for doubtful accounts	1,306	368
Changes in operating assets and liabilities, net of acquisition effects:		
Receivables	(10,069)	(810)
Prepaid expenses and other assets	2,181	3,508
Accounts payable	2,845	2,246
Accrued compensation and employee benefits	5,469	2,594
Other liabilities	(2,349)	2,272
Deferred revenue	(1,809)	556
Net cash provided by operating activities	59,648	60,744
Cash flows from investing activities:		
Purchases of property and equipment	(5,125)	(2,545)
Collection of note receivable from sale of product line		249
Purchases of marketable securities	(93,957)	(33,273)
Proceeds from sales of marketable securities	14,250	18,740
Proceeds from maturities of marketable securities	101,099	37,120
Investment in cost-method investee	(213)	
Net cash provided by investing activities	16,054	20,291
Cash flows from financing activities:		
Proceeds from revolving line of credit	70,000	
Debt issuance costs	(408)	
Proceeds from issuances of common stock under employee stock option and purchase plans	30,832	36,154
Dividends paid	(1,136)	(1,295)
Repurchases of common stock	(154,490)	(12,766)
Excess tax benefits from share-based payment arrangements	2,178	3,647

Net cash provided by (used in) financing activities	(53,024)	25,740
Effect of exchange rate changes on cash	1,317	(359)
Increase in cash and cash equivalents	23,995	106,416
Cash and cash equivalents, beginning of period	75,154	82,880
Cash and cash equivalents, end of period	$ 99,149	$ 189,296
Supplemental disclosures of cash flow information:		
Cash paid for income taxes, net	$ 3,003	$ 9,050

See accompanying notes to condensed consolidated financial statements.

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FAIR ISAAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Nature of Business

Fair Isaac Corporation

Incorporated under the laws of the State of Delaware, Fair Isaac Corporation is a provider of analytic, software and data management products and services that enable businesses to automate and improve decisions. Fair Isaac Corporation provides a range of analytical solutions, credit scoring and credit account management products and services to banks, credit reporting agencies, credit card processing agencies, insurers, retailers, telecommunications providers, healthcare organizations and government agencies.

In these condensed consolidated financial statements, Fair Isaac Corporation is referred to as we, us, our, and Fair Isaac.

Principles of Consolidation and Basis of Presentation

We have prepared the accompanying unaudited interim condensed consolidated financial statements in accordance with the instructions to Form 10-Q and the standards of accounting measurement set forth in Accounting Principles Board (APB) Opinion No. 28 and any amendments thereto adopted by the Financial Accounting Standards Board (FASB). Consequently, we have not necessarily included in this Form 10-Q all information and footnotes required for audited financial statements. In our opinion, the accompanying unaudited interim condensed consolidated financial statements in this Form 10-Q reflect all adjustments (consisting only of normal recurring adjustments, except as otherwise indicated) necessary for a fair presentation of our financial position and results of operations. These unaudited condensed consolidated financial statements and notes thereto should be read in conjunction with our audited consolidated financial statements and notes thereto presented in our Annual Report on Form 10-K for the year ended September 30, 2006. The interim financial information contained in this report is not necessarily indicative of the results to be expected for any other interim period or for the entire fiscal year.

The condensed consolidated financial statements include the accounts of Fair Isaac and its subsidiaries. All intercompany accounts and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. These estimates and assumptions include, but are not limited to, assessing the following: the recoverability of accounts receivable, goodwill and other intangible assets, software development costs and deferred tax assets; estimated losses associated with contingencies and litigation; the ability to estimate hours in connection with fixed-fee service contracts, the ability to estimate transactional-based revenues for which actual transaction volumes have not yet been received, the determination of whether fees are fixed or determinable and collection is probable or reasonably assured; and the development of assumptions for use in the Black-Scholes model that estimates the fair value of our share-based awards and assessing forfeiture rates of share-based awards.

2. Amortization of Intangible Assets

Amortization expense associated with our intangible assets, which has been reflected as a separate operating expense caption within the accompanying condensed consolidated statements of income, consisted of the following:

	Quarter Ended December 31,	
	2006	2005
	(In thousands)	
Cost of revenues	$ 3,779	$ 3,714
Selling, general and administrative	2,611	2,549

	$ 6,390	$ 6,263

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FAIR ISAAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Cost of revenues reflects our amortization of completed technology, and selling, general and administrative expenses reflects our amortization of other intangible assets. Intangible assets were $85.5 million and $90.9 million, net of accumulated amortization of $91.3 million and $84.5 million, as of December 31, 2006 and September 30, 2006, respectively.

3. Restructuring and Acquisition-Related Expenses

The following table summarizes our restructuring and acquisition-related accruals associated with our fiscal 2005 Braun Consulting, Inc. acquisition, fiscal 2004 London Bridge Software Holdings plc acquisition, and certain other Fair Isaac facility closures. The current portion and non-current portion is recorded in other accrued current liabilities and other long-term liabilities within the accompanying condensed consolidated balance sheets.

	Accrual at September 30, 2006	Cash Payments	Accrual at December 31, 2006
		(In thousands)	
Facilities charges	$ 15,094	$ (1,005)	$ 14,089
Employee separation	90	(90)	
	15,184	$ (1,095)	14,089
Less: current portion	(6,161)		(5,602)
Non-current	$ 9,023		$ 8,487

4. Share-Based Payment

We maintain the 1992 Long-term Incentive Plan (the 1992 Plan) under which we may grant stock options, stock appreciation rights, restricted stock, restricted stock units and common stock to officers, key employees and non-employee directors. Under the 1992 Plan, a number of shares equal to 4% of the number of shares of Fair Isaac common stock outstanding on the last day of the preceding fiscal year is added to the shares available under this plan each fiscal year, provided that the number of shares for grants of incentive stock options for the remaining term of this plan shall not exceed 5,062,500 shares. The 1992 Plan will terminate in February 2012. In November 2003, our Board of Directors approved the adoption of the 2003 Employment Inducement Award Plan (the 2003 Plan). The 2003 Plan reserves 2,250,000 shares of common stock solely for the granting of inducement stock options and other awards, as defined, that meet the employment inducement award exception to the New York Stock Exchange s listing standards requiring shareholder approval of equity-based inducement incentive plans. Except for the employment inducement award criteria, awards under the 2003 Plan will be generally consistent with those made under our 1992 Plan. The 2003 Plan shall remain in effect until terminated by the Board of Directors. We also maintain individual stock option plans for certain of our executive officers and the chairman of the board. Stock option awards granted during typically have a maximum term of seven years and vest ratably over four years. Stock option awards granted prior to October 1, 2005, typically had a maximum term of ten years and vest ratably over four years.

Under our 1999 Employee Stock Purchase Plan, we are authorized to issue up to 5,062,500 shares of common stock to eligible employees. Employees may have up to 10% of their base salary withheld through payroll deductions to purchase Fair Isaac common stock during semi-annual offering periods. The purchase price of the stock is the lower of 85% of (i) the fair market value of the common stock on the enrollment date (the first day of the offering period), or (ii) the fair market value on the exercise date (the last day of each offering period). Offering period means approximately six-month periods commencing (a) on the first trading day on or after January 1 and terminating on the last trading day in the following June, and (b) on the first trading day on or after July 1 and terminating on the last trading day in the following December.

We estimate the fair value of options granted using the Black-Scholes option valuation model. We estimate the volatility of our common stock at the date of grant based on a combination of the implied volatility of publicly traded options on our common stock and our historical volatility rate, consistent with Statement of Financial Accounting Standards (SFAS) No. 123(R), *Share-Based Payment* and Securities and Exchange Commission Staff Accounting Bulletin No. 107 (SAB 107). Our decision to use implied volatility was based upon the availability of actively traded options on our common stock and our assessment that implied volatility is more representative of future stock price trends than historical volatility. We estimate expected term consistent with the simplified method identified in SAB 107 for share-based awards. We elected to use the simplified method as we changed the contractual life for share-based awards from ten to seven years starting in fiscal 2006. The simplified method calculates the expected term as the average of the vesting and contractual terms of the award. Previously, we estimated expected term based on historical exercise patterns. The

FAIR ISAAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

dividend yield assumption is based on historical dividend payouts. The risk-free interest rate assumption is based on observed interest rates appropriate for the term of our employee options. We use historical data to estimate pre-vesting option forfeitures and record share-based compensation expense only for those awards that are expected to vest. For options granted, we amortize the fair value on a straight-line basis over the vesting period of the options.

The following table summarizes option activity during the quarter ended December 31, 2006:

	Shares (In thousands)	Weighted-average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value (In thousands)
Outstanding at October 1, 2006	13,785	$ 32.25		
Granted	758	41.39		
Exercised	(1,200)	22.12		
Forfeited	(391)	39.20		
Outstanding at December 31, 2006	12,952	33.52	6.06	$ 95,341

The fair value of restricted stock units is based on the fair market value of our common stock on the date of grant. We use historical data to estimate pre-vesting forfeitures and record share-based compensation expense only for those awards that are expected to vest. Share-based compensation expense for restricted stock units is recognized on a straight-line basis over the vesting period. Upon vesting, restricted stock units will convert into an equivalent number of shares of common stock.

The following table summarizes restricted stock unit activity during the quarter ended December 31, 2006:

	Shares (In thousands)	Weighted-average Price
Outstanding at October 1, 2006		$
Granted	231	41.74
Released		
Forfeited		
Outstanding at December 31, 2006	231	41.74

5. Earnings Per Share

The following reconciles the numerators and denominators of basic and diluted earnings per share (EPS):

	Quarter Ended December 31, 2006	2005

	(In thousands, except per share data)	
Numerator for basic earnings per share net income	$ 31,225	$ 28,457
Interest expense on senior convertible notes, net of tax	1	1
Numerator for diluted earnings per share	$ 31,226	$ 28,458
Denominator shares:		
Basic weighted-average shares	58,057	64,211
Effect of dilutive securities	1,928	2,008
Diluted weighted-average shares	59,985	66,219
Earnings per share:		
Basic	$ 0.54	$ 0.44
Diluted	$ 0.52	$ 0.43

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FAIR ISAAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The computation of diluted EPS for the quarters ended December 31, 2006 and 2005, excludes options to purchase approximately 3,419,146 and 648,000 shares of common stock, respectively, because the options exercise prices exceeded the average market price of our common stock in these periods and their inclusion would be antidilutive.

6. Segment Information

We are organized into the following four reportable segments, to align with the internal management of our worldwide business operations based on product and service offerings:

Strategy Machine Solutions. These are pre-configured Enterprise Decision Management (EDM) applications designed for a specific type of business problem or process, such as marketing, account origination, customer management, fraud and medical bill review. This segment also includes our myFICO solutions for consumers.

Scoring Solutions. Our scoring solutions give our clients access to analytics that can be easily integrated into their transaction streams and decision-making processes. Our scoring solutions are distributed through major credit reporting agencies, as well as services through which we provide our scores to lenders directly.

Professional Services. Through our professional services, we tailor our EDM products to our clients environments, and we design more effective decisioning environments for our clients. This segment includes revenues from custom engagements, business solution and technical consulting services, systems integration services, and data management services.

Analytic Software Tools. This segment is composed of software tools that clients can use to create their own custom EDM applications.

Our Chief Executive Officer evaluates segment financial performance based on segment revenues and operating income. Segment operating expenses consist of direct and indirect costs principally related to personnel, facilities, consulting, travel, depreciation and amortization. Indirect costs are allocated to the segments generally based on relative segment revenues, fixed rates established by management based upon estimated expense contribution levels and other assumptions that management considers reasonable. We do not allocate share-based compensation expense, restructuring and acquisition-related expense and certain other income and expense measures to our segments. These income and expense items are not allocated because they are not considered in evaluating the segment s operating performance. Our Chief Executive Officer does not evaluate the financial performance of each segment based on its respective assets or capital expenditures; rather, depreciation and amortization amounts are allocated to the segments from their internal cost centers as described above.

The following tables summarize segment information for the quarters ended December 31, 2006 and 2005:

	Quarter Ended December 31, 2006				
	Strategy Machine Solutions	Scoring Solutions	Professional Services	Analytic Software Tools	Total
			(In thousands)		
Revenues	$ 110,669	$ 44,918	$ 38,417	$ 14,223	$ 208,227
Operating expenses	(90,806)	(16,039)	(34,969)	(11,940)	(153,754)
Segment operating income	$ 19,863	$ 28,879	$ 3,448	$ 2,283	54,473
Unallocated share-based compensation expense					(9,572)

Operating income					44,901
Unallocated interest income					3,564
Unallocated interest expense					(2,676)
Unallocated other expense, net					(453)
Income before income taxes					$ 45,336
Depreciation and amortization	$ 8,410	$ 2,225	$ 1,980	$ 934	$ 13,549

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FAIR ISAAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

	Quarter December 31, 2005				
	Strategy Machine Solutions	Scoring Solutions	Professional Services (In thousands)	Analytic Software Tools	Total
Revenues	$ 111,986	$ 46,156	$ 32,831	$ 11,817	$ 202,790
Operating expenses	(91,366)	(16,622)	(30,913)	(11,006)	(149,907)
Segment operating income	$ 20,620	$ 29,534	$ 1,918	$ 811	52,883
Unallocated share-based compensation expense					(9,514)
Unallocated restructuring and acquisition-related					674
Operating income					44,043
Unallocated interest income					3,066
Unallocated interest expense					(2,135)
Unallocated other expense, net					(86)
Income before income taxes					$ 44,888
Depreciation and amortization	$ 7,909	$ 1,985	$ 1,389	$ 776	$ 12,059

7. Income Taxes

Our effective tax rate was 31.1% and 36.6% during the quarters ended December 31, 2006 and 2005, respectively. The provision for income taxes during interim quarterly reporting periods is based on our estimates of the effective tax rates for the respective full fiscal year. Income tax expense in the quarter ended December 31, 2006, included a benefit of $1.8 million related to a favorable settlement of a state tax examination. In addition, income tax expense was reduced by $0.5 million as a result of the recognition of U.S federal research tax credits related to fiscal 2006. We were unable to recognize these credits during the last nine months of fiscal 2006 as legislation providing for this credit had expired. In December 2006, legislation was enacted that provided for retroactive extension of this credit.

8. Credit Agreement

In October 2006, we entered into a five-year $300 million unsecured revolving credit facility with a syndicate of banks. The credit facility may be increased to $500 million subject to certain terms and conditions. Proceeds from the credit facility can be used for capital requirements and general business purposes and may be used for the refinancing of existing debt, acquisitions and repurchases of our common stock. Interest on amounts borrowed under the credit facility is based on (i) a base rate, which is the greater of (a) the prime rate and (b) the Federal Funds rate plus 0.50% or (ii) LIBOR plus an applicable margin. The margin on LIBOR borrowings ranges from 0.30% to 0.55% and is determined based on our consolidated leverage ratio. In addition, we must pay utilization fees if borrowings and commitments under the credit facility exceed 50% of the total credit facility commitment, as well as facility fees. The credit facility contains certain restrictive covenants, including maintenance of consolidated leverage and fixed charge coverage ratios. The credit facility contains other covenants typical of unsecured facilities. As of December 31, 2006, we had $70.0 million of borrowings outstanding under the credit facility at an average interest rate of 5.675%.

9. Contingencies

We are in disputes with certain customers regarding amounts owed in connection with the sale of certain of our products and services. We also have had claims asserted by former employees relating to compensation and other employment matters. We are also involved in various other claims and legal actions arising in the ordinary course of business. We believe that none of these aforementioned claims or actions will result in a material adverse impact to our consolidated results of operations, liquidity or financial condition. However, the amount or range of any potential liabilities associated with these claims and actions, if any, cannot be determined with certainty. Set forth below is additional detail concerning certain ongoing litigation.

Customer Claims

We are party to two separate lawsuits involving two different customers who have asserted that our performance under professional services contracts with such customers has caused them to incur damages. One customer s lawsuit is pending in the United States District Court for the Central District of California, and the other is pending as a counterclaim to a collection lawsuit that we commenced in the United States District Court for the Southern District of Texas. The customers in these matters have claimed damages in excess of $10 million with one case including a claim for punitive damages. We believe that these claims are without merit, and we intend to contest them vigorously. We also believe that the resolution of these claims will not result in a material adverse impact to our consolidated financial condition.

FAIR ISAAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Putative Consumer Class Action Lawsuits

We are a defendant in a lawsuit captioned as *Robbie Hillis v. Equifax Consumer Services, Inc. and Fair Isaac, Inc.*, which is pending in the U.S. District Court for the Northern District of Georgia. The plaintiff claims that the defendants have jointly sold the Score Power® credit score product in violation of certain procedural requirements under the Credit Repair Organizations Act (CROA), and in violation of the antifraud provisions of that statute. The plaintiff also claims that the defendants are credit repair organizations under CROA. The plaintiff is seeking certification of a class on behalf of all individuals who purchased products containing Score Power from the defendants in the five year period prior to the filing of the Complaint on November 14, 2004. The plaintiff is seeking unspecified damages, attorneys fees and costs. We believe that the claims in this lawsuit are without merit, and we have denied any liability or wrongdoing and have denied that class certification is appropriate. We are vigorously contesting this matter. The plaintiff brought a motion for class certification and a motion for summary judgment in his favor and against the defendants. We opposed, and the Court denied, both of the plaintiff s motions. The plaintiff has brought a motion asking the Court to reconsider its prior ruling. That motion is pending. We believe that the resolution of this claim will not result in a material adverse impact to our consolidated financial condition.

We are a defendant in a lawsuit captioned as *Christy Slack v. Fair Isaac Corporation and MyFICO Consumer Services, Inc.*, which is pending in the United States District Court for the Northern District of California. As in the Hillis matter, the plaintiff is claiming that the defendants violated certain procedural requirements of CROA, and violated the antifraud provisions of CROA, with respect to the sale of credit score products on our myFICO.com website. The plaintiff also claims that the defendants violated the California Credit Services Act (the CSA) and were unjustly enriched. The plaintiff has sought certification of a class on behalf of all individuals who purchased credit score products from us on the myFICO.com website in the five year period prior to the filing of the Complaint on January 18, 2005. Plaintiff seeks unspecified damages, attorneys fees and costs. We believe that the claims in this lawsuit are without merit and we have denied any liability or wrongdoing and have denied that class certification is appropriate. We are vigorously contesting this matter. We brought a motion to dismiss the plaintiff s claims. The Court granted our motion, in part, by dismissing certain of the plaintiff s claims under the CSA. The plaintiff has brought motions for summary judgment and for class certification. We have opposed both motions. The Court has not yet ruled on the plaintiff s motions. We believe that the resolution of this claim will not result in a material adverse impact to our consolidated financial condition.

Braun Consulting, Inc.

Braun (which we acquired in November 2004) was a defendant in a lawsuit filed on November 26, 2001, in the United States District Court for the Southern District of New York (Case No. 01 CV 10629) that alleges violations of federal securities laws in connection with Braun s initial public offering in August 1999. This lawsuit is among approximately 300 coordinated putative class actions against certain issuers, their officers and directors, and underwriters with respect to such issuers initial public offerings. As successor in interest to Braun, we have entered into a Stipulation and Agreement of Settlement, pursuant to a Memorandum of Understanding, along with most of the other defendant issuers in this coordinated litigation, whereby such issuers and their officers and directors will be dismissed with prejudice, subject to the satisfaction of certain conditions, including, among others, approval of the court. Under the terms of this agreement, we will not pay any amount of the settlement.

10. New Accounting Pronouncements Not Yet Adopted

In July 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes,* which prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. Additionally, FIN 48 provides guidance on the derecognition, classification, accounting in interim periods and disclosure requirements for uncertain tax positions. The accounting provisions of FIN 48 will be effective for the Company beginning October 1, 2007. We are in the process of determining what effect, if any, the adoption of FIN 48 will have on our consolidated financial statements.

In September 2006, the SEC released Staff Accounting Bulletin (SAB) No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements*, which provided the Staff s view regarding the process of quantifying financial statement misstatements. SAB 108 requires an entity to quantify misstatements using both a balance sheet and income statement approach to determine if a misstatement is material. The evaluation requirements of SAB No. 108 are effective for fiscal years ending after November 15, 2006. We are in the process of determining what effect, if any, the adoption of SAB No. 108 will have on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measures*, which defines fair value, establishes a framework for measuring fair value and expands disclosures about assets and liabilities measured at fair value. The statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are in the process of determining what effect, if any, the adoption of SFAS No. 157 will have on our consolidated financial statements.

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Item 2. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

FORWARD LOOKING STATEMENTS

Statements contained in this Report that are not statements of historical fact should be considered forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the Act). In addition, certain statements in our future filings with the Securities and Exchange Commission (SEC), in press releases, and in oral and written statements made by us or with our approval that are not statements of historical fact constitute forward-looking statements within the meaning of the Act. Examples of forward-looking statements include, but are not limited to: (i) projections of revenue, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other statements concerning future financial performance; (ii) statements of our plans and objectives by our management or Board of Directors, including those relating to products or services; (iii) statements of assumptions underlying such statements; (iv) statements regarding business relationships with vendors, customers or collaborators; and (v) statements regarding products, their characteristics, performance, sales potential or effect in the hands of customers. Words such as believes, anticipates, expects, intends, targeted, sh potential, goals, strategy, and similar expressions are intended to identify forward-looking statements, but are not the exclusive means of identifying such statements. Forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from those in such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to, those described in Item 1A of Part II, Risk Factors, below. The performance of our business and our securities may be adversely affected by these factors and by other factors common to other businesses and investments, or to the general economy. Forward-looking statements are qualified by some or all of these risk factors. Therefore, you should consider these risk factors with caution and form your own critical and independent conclusions about the likely effect of these risk factors on our future performance. Such forward-looking statements speak only as of the date on which statements are made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made to reflect the occurrence of unanticipated events or circumstances. Readers should carefully review the disclosures and the risk factors described in this and other documents we file from time to time with the SEC, including our reports on Forms 10-Q and 8-K to be filed by the Company in fiscal 2007.

RESULTS OF OPERATIONS

Overview

We are a leader in Enterprise Decision Management (EDM) solutions that enable businesses to automate and improve their decisions across the enterprise. Our predictive analytics and decision management systems power hundreds of billions of customer decisions each year. We help companies acquire customers more efficiently, increase customer value, reduce fraud and credit losses, lower operating expenses and enter new markets more profitably. Most leading banks and credit card issuers rely on our solutions, as do many insurers, retailers, telecommunications providers, healthcare organizations, pharmaceutical and government agencies. We also serve consumers through online services that enable people to purchase and understand their FICO® scores, the standard measure of credit risk in the United States, empowering them to manage their financial health.

Most of our revenues are derived from the sale of products and services within the consumer credit, financial services and insurance industries, and during the quarter ended December 31, 2006, 75% of our revenues were derived from within these industries. A significant portion of our remaining revenues is derived from the telecommunications, healthcare and retail industries, as well as the government sector. Our clients utilize our products and services to facilitate a variety of business processes, including customer marketing and acquisition, account origination, credit and underwriting risk management, fraud loss prevention and control, and client account and policyholder management. A significant portion of our revenues is derived from transactional or unit-based software license fees, annual license fees under long-term software license arrangements, transactional fees derived under scoring, network service or internal hosted software arrangements, and annual software maintenance fees. The recurrence of these revenues is, to a significant degree, dependent upon our clients continued usage of our products and services in their business activities. The more significant activities underlying the use of our products in these areas include: credit and debit card usage or active account levels; lending acquisition, origination and customer management activity; workers compensation and automobile medical injury insurance claims; and wireless and wireline calls and subscriber levels. Approximately 74% and 77% of our revenues during the quarters ended December 31, 2006 and 2005, respectively, were derived from arrangements with transactional or unit-based pricing. We also derive revenues from other sources which generally do not recur and include, but are not limited to, perpetual or time-based licenses with upfront payment terms, non-recurring professional service arrangements and gain-share arrangements where revenue is derived based on percentages of client revenue growth or cost reductions attributable to our products.

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Within a number of our sectors there has been a sizable amount of industry consolidation. In addition, many of our sectors are experiencing increased levels of competition. As a result of these factors, we believe that future revenues in particular sectors may decline. However, due to the long-term customer arrangements we have with many of our customers, the near term impact of these declines may be more limited in certain sectors.

One measure used by management as an indicator of our business performance is the volume of new bookings achieved. We define a new booking as estimated future contractual revenues, including agreements with perpetual, multi-year and annual terms. New bookings values may include: (i) estimates of variable fee components such as hours to be incurred under new professional services arrangements and customer account or transaction activity for agreements with transactional-based fee arrangements, (ii) additional or expanded business from renewals of contracts, and (iii) to a lesser extent, previous customers that have attrited and been re-sold only as a result of a significant sales effort. During the quarter ended December 31, 2006, we achieved new bookings of $72.1 million. There were no deals with bookings values of $3.0 million or more during the quarter ended December 31, 2006. In comparison, new bookings in the prior year quarter ended December 31, 2005 were $127.8 million, including eight deals with bookings values of $3.0 million or more.

Management regards the volume of new bookings achieved, among other factors, as an important indicator of future revenues, but they are not comparable to, nor should they be substituted for, an analysis of our revenues, and they are subject to a number of risks and uncertainties, including those described in Item 1A of Part II, Risk Factors, concerning timing and contingencies affecting product delivery and performance. Although many of our contracts have fixed non-cancelable terms, some of our contracts are terminable by the client on short notice or without notice. Accordingly, we do not believe it is appropriate to characterize all of our new bookings as backlog that will generate future revenue.

Our revenues derived from clients outside the United States continue to grow, and may in the future grow more rapidly than our revenues from domestic clients. International revenues totaled $61.2 million and $51.8 million during the quarters ended December 31, 2006 and 2005, respectively, representing 29% and 26% of total consolidated revenues in each of these periods. In addition to clients acquired via our acquisitions, we believe that our international growth is a product of successful relationships with third parties that assist in international sales efforts and our own increased sales focus internationally, and we expect that the percentage of our revenues derived from international clients will increase in the future.

Our reportable segments are: Strategy Machine Solutions, Scoring Solutions, Professional Services and Analytic Software Tools. Although we sell solutions and services into a large number of end user product and industry markets, our reportable business segments reflect the primary method in which management organizes and evaluates internal financial information to make operating decisions and assess performance. Comparative segment revenues, operating income, and related financial information for the quarters ended December 31, 2006 and 2005 are set forth in Note 6 to the accompanying condensed consolidated financial statements.

Revenues

The following tables set forth certain summary information on a segment basis related to our revenues for the fiscal periods indicated.

Segment	Quarter Ended December 31, 2006	Quarter Ended December 31, 2005	Percentage of Revenues 2006	Percentage of Revenues 2005	Period-to-Period Change	Period-to-Period Percentage Change
	(In thousands)				(In thousands)	
Strategy Machine Solutions	$ 110,669	$ 111,986	53%	55%	$ (1,317)	(1)%
Scoring Solutions	44,918	46,156	22%	23%	(1,238)	(3)%
Professional Services	38,417	32,831	18%	16%	5,586	17%

Analytic Software Tools	14,223	11,817	7%	6%	2,406	20%
	$ 208,227	$ 202,790	100%	100%	5,437	3%

Quarter Ended December 31, 2006 Compared to Quarter Ended December 31, 2005 Revenues

Strategy Machine Solutions segment revenues decreased $1.3 million due to a $1.3 million decrease in revenues from our *mortgage banking solutions,* a $1.3 million decrease in revenues from our *marketing solutions,* a $1.0 million decrease in revenues from our *originations solutions* and a $0.4 million net decrease in revenues from our other strategy machine solutions. The revenue decline was partially offset by a $1.5 million increase in revenues from our *fraud solutions,* and a $1.2 million increase in revenues from our *customer management solutions*. The decrease in *mortgage banking solutions* revenues was attributable to declines in license and transactional revenues. The decrease in *marketing solutions* revenues was attributable primarily to a decline in sales volumes. The decrease in *originations solutions* revenues was the result of a decline in transactional-based revenues due to a volume decline and unfavorable pricing on a renewed customer contract. The increase in *fraud solutions* revenues was attributable primarily to increases in volumes associated with transactional-based agreements. The increase in *customer management solutions* revenues was attributable primarily to an increase in license sales.

Scoring Solutions segment revenues decreased $1.2 million primarily due to a decline in revenues derived from prescreening services that we provided directly to users in financial services. This decrease was due to a difficult comparison to strong revenues for these services that we recorded in the first quarter last year. The decline was partially offset by an increase in revenues derived from risk scoring services at the credit reporting agencies, resulting from increased sales of scores for prescreening activities, and an increase in revenues derived from our FICO expansion score product.

During the quarters ended December 31, 2006 and 2005, revenues generated from our agreements with Equifax, TransUnion and Experian, collectively accounted for approximately 18% of our total revenues, including revenues from these customers that are recorded in our other segments.

Professional Services segment revenues increased $5.6 million from consulting services for our fraud and customer management products. In addition, we had increased revenues for services to develop predictive models for a large customer. The increase in fraud was primarily due to revenues derived from a gain-share provision associated with a large customer. The increase was partially offset by a decline in implementation services for our collection and recovery products.

Analytic Software Tools segment revenues increased $2.4 million primarily due to an increase in sales of Blaze Advisor perpetual and term licenses and increased maintenance revenue. The increase reflects the timing of Blaze Advisor sales, which includes large individual contracts. The increase in maintenance revenues was due to growth in our installed base of Blaze Advisor software applications.

Operating Expenses and Other Income (Expense)

The following table sets forth certain summary information related to our statements of income for the fiscal periods indicated.

	Quarter Ended December 31,		Percentage of Revenues		Period-to-Period Change	Period-to-Period Percentage Change
	2006	2005	2006	2005		
	(In thousands)					
Revenues	$ 208,227	$ 202,790	100%	100%	$ 5,437	3%
Operating expenses:						
Cost of revenues	70,569	67,045	34%	33%	3,524	5%
Research and development	17,719	22,730	8%	11%	(5,011)	(22)%
Selling, general and administrative	68,648	63,383	33%	31%	5,265	8%
Amortization of intangible assets	6,390	6,263	3%	3%	127	2%
Restructuring and acquisition-related		(674)			674	
Total operating expenses	163,326	158,747	78%	78%	4,579	3%

Operating income	44,901	44,043	22%	22%	858	2%
Interest income	3,564	3,066	1%	1%	498	16%
Interest expense	(2,676)	(2,135)	(1)%	(1)%	(541)	(25%)
Other expense, net	(453)	(86)			(367)	
Income before income taxes	45,336	44,888	22%	22%	448	1%
Provision for income taxes	14,111	16,431	7%	8%	(2,320)	(14)%
Net income	$ 31,225	$ 28,457	15%	14%	2,768	10%
Number of employees at quarter end	2,712	2,844			(132)	(5)%

Cost of Revenues

Cost of revenues consists primarily of employee salaries and benefits for personnel directly involved in creating, installing and supporting revenue products; travel and related overhead costs; costs of computer service bureaus; internal network hosting costs; amounts payable to credit reporting agencies for scores; software costs; and expenses related to our consumer score services through myFICO.com.

The quarter over quarter increase of $3.5 million in cost of revenues resulted from a $2.9 million increase in personnel and other labor-related costs and a $1.2 million increase in facilities and infrastructure costs. The increase was partially offset by a $0.6 million decline in other costs. The increase in personnel and other labor-related costs was attributable primarily to an increase in salary and related benefit costs, which included the impact of annual staff salary increases. The increase in facilities and infrastructure costs was attributable primarily to an increase in allocated facility and information system costs associated with the increase in professional services activities.

Over the next several quarters, we expect that cost of revenues as a percentage of revenues will be consistent with that incurred during the quarter ended December 31, 2006.

Research and Development

Research and development expenses include the personnel and related overhead costs incurred in development of new products and services, including primarily the research of mathematical and statistical models and the development of new versions of Strategy Machine Solutions and Analytic Software Tools.

The quarter over quarter decrease of $5.0 million in research and development expenditures was attributable primarily to a $3.9 million decrease in personnel and related costs and a $0.9 million decrease in facilities and infrastructure costs. The decrease in personnel and related costs was the result of lower salary and benefit costs due to the shift of employees to non-U.S. locations and staff reductions slightly offset by costs associated with annual salary adjustments. The decrease in facilities and infrastructure costs was attributable primarily to a decrease in allocated facility and information system costs.

Over the next several quarters, we expect that research and development expenditures as a percentage of revenues will be consistent with or slightly higher than that incurred during the quarter ended December 31, 2006.

Selling, General and Administrative

Selling, general and administrative expenses consist principally of employee salaries and benefits, travel, overhead, advertising and other promotional expenses, corporate facilities expenses, legal expenses, business development expenses, and the cost of operating computer systems.

The quarter over quarter increase of $5.3 million in selling, general and administrative expenses was attributable to a $5.0 million increase in personnel and other labor-related costs and a $0.3 million net increase in other expenses. The increase in personnel and labor-related costs resulted primarily from an increase in salary and benefit costs associated with annual salary adjustments and growth in sales staff. In addition, personnel and other labor-related costs increased on higher commission costs.

Over the next several quarters, we expect that selling, general and administrative expenses as a percentage of revenues will be consistent with that incurred during the quarter ended December 31, 2006.

Amortization of Intangible Assets

Amortization of intangible assets consists of amortization expense related to intangible assets recorded in connection with acquisitions accounted for by the purchase method of accounting. Our definite-lived intangible assets, consisting primarily of completed technology and customer contracts and relationships, are being amortized using the straight-line method or based on forecasted cash flows associated with the assets over periods ranging from two to fifteen years.

Amortization expense for the quarter ended December 31, 2006 was essentially unchanged from the same period last year.

Restructuring and Acquisition-Related

During the quarter ended December 31, 2005, we recorded a $0.7 million gain due to the sublease of office space that we had exited in fiscal 2002. The gain resulted from an adjustment to the liability established for the exit of the lease space and a refund received for past rent paid to the landlord.

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Interest Income

Interest income is derived primarily from the investment of funds in excess of our immediate operating requirements. The quarter over quarter increase in interest income was attributable to interest associated with settlement of a state tax examination that occurred in the quarter ended December 31, 2006.

Interest Expense

Interest expense recorded during the quarter ended December 31, 2006 relates to our $400.0 million of 1.5% Senior Convertible Notes (Senior Notes), including the amortization of debt issuance costs, and interest associated with borrowing under our revolving credit facility. Interest expense recorded during the quarter ended December 31, 2005 was only related to the Senior Notes.

Other Expense, Net

Other expense, net consists primarily of realized investment gains/losses, exchange rate gains/losses resulting from re-measurement of foreign-denominated receivable and cash balances held by our U.S. reporting entities into the U.S. dollar functional currency at period-end market rates, net of the impact of offsetting forward exchange contracts, and other non-operating items.

The increase in other expense, net was primarily due to foreign exchange currency losses of $0.5 million that were recognized in the quarter ended December 31, 2006, compared with foreign exchange currency losses of $0.1 million recorded in the quarter ended December 31, 2005.

Provision for Income Taxes

Our effective tax rate was 31.1% and 36.6% during the quarters ended December 31, 2006 and 2005, respectively. The provision for income taxes during interim quarterly reporting periods is based on our estimates of the effective tax rates for the respective full fiscal year. Income tax expense in the quarter ended December 31, 2006, included a benefit of $1.8 million related to a favorable settlement of a state tax examination. In addition, income tax expense was reduced by $0.5 million as a result of the recognition of U.S federal research tax credits related to fiscal 2006. We were unable to recognize these credits during the last nine months of fiscal 2006 as legislation providing for this credit had expired. In December 2006, legislation was enacted that provided for retroactive extension of this credit.

Operating Income

The following table sets forth certain summary information on a segment basis related to our operating income for the fiscal periods indicated.

Segment	**Quarter Ended December 31, 2006**	**Quarter Ended December 31, 2005**	**Period-to-Period Change**	**Period-to-Period Percentage Change**
		(In thousands)		
Strategy Machine Solutions	$ 19,863	$ 20,620	$ (757)	(4)%
Scoring Solutions	28,879	29,534	(655)	(2)%
Professional Services	3,448	1,918	1,530	80%
Analytic Software Tools	2,283	811	1,472	182%
Segment operating income	54,473	52,883	1,590	3%
Unallocated share-based compensation	(9,572)	(9,514)	(58)	(1)%
Unallocated restructuring and acquisition-related		674	(674)	(100)%
Operating income	$ 44,901	$ 44,043	858	2%

The quarter over quarter increase of $0.9 million in operating income was attributable to an increase in segment revenues. At the segment level, the increase in segment operating income was driven by increases of $1.5 million in segment operating income within both our Analytic Software Tools and Professional Services segments, partially offset by a $0.8 million and $0.7 million decrease in segment operating income within our Strategy Machine Solutions and Scoring Solutions segments, respectively. The increase in

Professional Services segment operating income was the result of the increase in sales, partially offset by higher personnel costs to support increased professional services activities. In our Analytic Software Tools segment, higher segment operating income was due to an increase in sales of perpetual licenses for our EDM products and lower product development costs, partially offset by increased sales costs. The decrease in Strategy Machine Solutions segment operating income was attributable to a decline in sales of *mortgage solutions*, *marketing solutions* and *originations solutions* products. The decrease in Scoring Solutions segment operating income was attributable primarily to a decline in revenues derived from prescreening services that we provided directly to users in financial services. We believe that operating income as a percentage of revenues in our Scoring Solutions segment may decline in the future due to lower operating margins on new products.

Capital Resources and Liquidity

Cash Flows from Operating Activities

Our primary method for funding operations and growth has been through cash flows generated from operating activities. Net cash provided by operating activities decreased slightly from $60.7 million during the quarter ended December 31, 2005 to $59.6 million during the quarter ended December 31, 2006. Operating cash flows were negatively impacted by an increase in trade receivables of $10.1 million, which resulted from longer payment terms on certain customer contracts and slower collections. Operating cash flows were positively impacted by the increase in earnings during the quarter ended December 31, 2006 and a decline in cash paid for income taxes.

Cash Flows from Investing Activities

Net cash provided by investing activities totaled $16.1 million during the quarter ended December 31, 2006, compared to net cash provided by investing activities of $20.3 million in quarter ended December 31, 2005. The decline in cash flows provided by investing activities was primarily attributable to a $1.2 million decrease in proceeds from sales and maturities of marketable securities, net of purchases, and a $2.6 million increase in property and equipment purchases.

Cash Flows from Financing Activities

Net cash used by financing activities totaled $53.0 million in the quarter ended December 31, 2006, compared to net cash provided by financing activities of $25.7 million in quarter ended December 31, 2005. The change in cash flows from financing activities was primarily due to a $141.7 million increase in common stock repurchased and a $70.0 million increase in cash proceeds from borrowings under a revolving credit facility. We used cash provided by operations and borrowings under the revolving credit facility to fund common stock repurchased during the quarter.

Repurchases of Common Stock

From time to time, we repurchase our common stock in the open market pursuant to programs approved by our Board of Directors. In November 2006, our Board of Directors approved a new common stock repurchase program that replaced a previous program. The new program allows us to purchase shares of our common stock up to an aggregate cost of $500.0 million. Through December 31, 2006, we had repurchased 3,725,400 shares of our common stock under this new program for an aggregate cost of $154.5 million.

Dividends

During the quarter ended December 31, 2006, we paid a quarterly dividend of two cents per common share, which is representative of the eight cents per year dividend we have paid in recent years. Our dividend rate is set by the Board of Directors on a quarterly basis taking into account a variety of factors, including among others, our operating results and cash flows, general economic and industry conditions, our obligations, changes in applicable tax laws and other factors deemed relevant by the Board. Although we expect to continue to pay dividends at the current rate, our dividend rate is subject to change from time to time based on the Board s business judgment with respect to these and other relevant factors.

Credit Agreement

In October 2006, we entered into a five-year $300 million unsecured revolving credit facility with a syndicate of banks. The credit facility may be increased to $500 million subject to certain terms and conditions. Proceeds from the credit facility can be used for capital requirements and general business purposes and may be used for the refinancing of existing debt, acquisitions and repurchases of our common stock. Interest on amounts borrowed under the credit facility is based on (i) a base rate, which is the greater of (a) the

prime rate and (b) the Federal Funds rate plus 0.50% or (ii) LIBOR plus an applicable margin. The margin on LIBOR borrowings ranges from 0.30% to 0.55% and is determined based on our consolidated leverage ratio. In addition, we must pay utilization fees if borrowings and commitments under the credit facility exceed 50% of the total credit facility commitment, as well as facility fees. The credit facility contains certain restrictive covenants, including maintenance of consolidated leverage and fixed charge coverage ratios. The credit facility contains other covenants typical of unsecured facilities. As of December 31, 2006, we had $70.0 million of borrowings outstanding under the credit facility at an average interest rate of 5.675%.

Capital Resources and Liquidity Outlook

As of December 31, 2006, we had $269.3 million in cash, cash equivalents and marketable security investments. We believe that these balances, as well as borrowings from our $300 million revolving credit facility and anticipated cash flows from operating activities, will be sufficient to fund our working and other capital requirements and any repayment of existing debt over the course of the next twelve months and for the foreseeable future. In the normal course of business, we evaluate the merits of acquiring technology or businesses, or establishing strategic relationships with or investing in these businesses. We may elect to use available cash and cash equivalents and marketable security investments to fund such activities in the future. In the event additional needs for cash arise, we may raise additional funds from a combination of sources, including the potential issuance of debt or equity securities. Additional financing might not be available on terms favorable to us, or at all. If adequate funds were not available or were not available on acceptable terms, our ability to take advantage of unanticipated opportunities or respond to competitive pressures could be limited.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources.

Critical Accounting Policies and Estimates

We prepare our consolidated financial statements in conformity with U.S. generally accepted accounting principles. These accounting principles require management to make certain judgments and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. We periodically evaluate our estimates including those relating to revenue recognition, the allowance for doubtful accounts, goodwill and other intangible assets resulting from business acquisitions, internal-use software, income taxes and contingencies and litigation. We base our estimates on historical experience and various other assumptions that we believe to be reasonable based on the specific circumstances, the results of which form the basis for making judgments about the carrying value of certain assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

We believe the following critical accounting policies involve the most significant judgments and estimates used in the preparation of our consolidated financial statements:

Revenue Recognition

Software license fee revenue is recognized when persuasive evidence of an arrangement exists, delivery of the product has occurred at our customer s location, the fee is fixed or determinable and collection is probable. We use the residual method to recognize revenue when an arrangement includes one or more elements to be delivered at a future date and vendor-specific objective evidence (VSOE) of the fair value of all undelivered elements exists. VSOE of fair value is based on the normal pricing practices for those products and services when sold separately by us and customer renewal rates for post-contract customer support services. Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is recognized as revenue. If evidence of the fair value of one or more undelivered elements does not exist, the revenue is deferred and recognized when delivery of those elements occurs or when fair value can be established. The determination of whether fees are fixed or determinable and collection is probable involves the use of assumptions. We evaluate contract terms and customer information to ensure that these criteria are met prior to our recognition of license fee revenue. Changes to the elements in a software arrangement, the ability to identify VSOE for those elements, the fair value of the respective elements, and changes to a product s estimated life cycle could materially impact the amount of earned and unearned revenue.

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When software licenses are sold together with implementation or consulting services, license fees are recognized upon delivery provided that the above criteria are met, payment of the license fees is not dependent upon the performance of the services, and the services do not provide significant customization or modification of the software products and are not essential to the functionality of the software that was delivered. For arrangements with services that are essential to the functionality of the software, the license and related service revenues are recognized using contract accounting as described below.

If at the outset of an arrangement we determine that the arrangement fee is not fixed or determinable, revenue is deferred until the arrangement fee becomes due, assuming all other revenue recognition criteria have been met. If at the outset of an arrangement we determine that collectibility is not probable, revenue is deferred until the earlier of when collectibility becomes probable or the receipt of payment. If there is uncertainty as to the customer s acceptance of our deliverables, revenue is not recognized until the earlier of receipt of customer acceptance, expiration of the acceptance period or when we can demonstrate we meet the acceptance criteria.

Revenues from post-contract customer support services, such as software maintenance, are recognized on a straight-line basis over the term of the support period. The majority of our software maintenance agreements provide technical support as well as unspecified software product upgrades and releases when and if made available by us during the term of the support period.

Revenues recognized from our credit scoring, data processing, data management and internet delivery services are recognized as these services are performed, provided persuasive evidence of an arrangement exists, fees are fixed or determinable, and collection is reasonably assured. The determination of certain of our credit scoring and data processing revenues requires the use of estimates, principally related to transaction volumes in instances where these volumes are reported to us by our clients on a monthly or quarterly basis in arrears. In these instances, we estimate transaction volumes based on preliminary customer transaction information, if available, or based on average actual reported volumes for an immediate trailing period. Differences between our estimates and actual final volumes reported are recorded in the period in which actual volumes are reported. We have not experienced significant variances between our estimates and actual reported volumes in the past and anticipate that we will be able to continue to make reasonable estimates in the future. If for some reason we were unable to reasonably estimate transaction volumes in the future, revenue may be deferred until actual customer data was received, and this could have a material impact on our results of operations during the period of time that we changed accounting methods.

Transactional or unit-based license fees under software license arrangements, network service and internally-hosted software agreements are recognized as revenue based on system usage or when fees based on system usage exceed monthly minimum license fees, provided persuasive evidence of an arrangement exists, fees are fixed or determinable and collection is probable. The determination of certain of our transactional or unit-based license fee revenues requires the use of estimates, principally related to transaction usage or active account volumes in instances where this information is reported to us by our clients on a monthly or quarterly basis in arrears. In these instances, we estimate transaction volumes based on preliminary customer transaction information, if available, or based on average actual reported volumes for an immediate trailing period. Differences between our estimates and actual final volumes reported are recorded in the period in which actual volumes are reported. We have not experienced significant variances between our estimates and actual reported volumes in the past and anticipate that we will be able to continue to make reasonable estimates in the future. If for some reason we were unable to reasonably estimate customer account or transaction volumes in the future, revenue would be deferred until actual customer data was received, and this could have a material impact on our consolidated results of operations.

We provide consulting, training, model development and software integration services under both hourly-based time and materials and fixed-priced contracts. Revenues from these services are generally recognized as the services are performed. For fixed-price service contracts, we apply the percentage-of-completion method of contract accounting to determine progress towards completion, which requires the use of estimates. In such instances, management is required to estimate the input measures, generally based on hours incurred to date compared to total estimated hours of the project, with consideration also given to output measures, such as contract milestones, when applicable. Adjustments to estimates are made in the period in which the facts requiring such revisions become known and, accordingly, recognized revenues and profits are subject to revisions as the contract progresses to completion.

Estimated losses, if any, are recorded in the period in which current estimates of total contract revenue and contract costs indicate a loss. If substantive uncertainty related to customer acceptance of services exists, we apply the completed contract method of accounting and defer the associated revenue until the contract is completed. If we are unable to accurately estimate the input measures used for percentage-of-completion accounting, revenue would be deferred until the contract is complete, and this could have a material impact on our consolidated results of operations.

Revenue recognized under the percentage-of-completion method in excess of contract billings is recorded as an unbilled receivable. Such amounts are generally billable upon reaching certain performance milestones as defined by individual contracts. Billings collected in advance of performance and recognition of revenue under contracts are recorded as deferred revenue.

In certain of our non-software arrangements, we enter into contracts that include the delivery of a combination of two or more of our service offerings. Typically, such multiple element arrangements incorporate the design and development of data management tools or systems and an ongoing obligation to manage, host or otherwise run solutions for our customer. Such arrangements are divided into separate units of accounting provided that the delivered item has stand-alone value and there is objective and reliable evidence of the fair value of the undelivered items. The total arrangement fee is allocated to the undelivered elements based on their fair values and to the initial delivered elements using the residual method. Revenue is recognized separately, and in accordance with our revenue recognition policy, for each element.

As described above, sometimes our customer arrangements have multiple deliverables, including service elements. Generally, our multiple element arrangements fall within the scope of specific accounting standards that provide guidance regarding the separation of elements in multiple-deliverable arrangements and the allocation of consideration among those elements (e.g., American Institute of Certified Public Accountants Statement of Position (SOP) No. 97-2, *Software Revenue Recognition*, as amended). If not, we apply the separation provisions of Emerging Issues Task Force (EITF) Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables*. The provisions of EITF Issue No. 00-21 require us to unbundle multiple element arrangements into separate units of accounting when the delivered element(s) has stand-alone value and fair value of the undelivered element(s) exists. When we are able to unbundle the arrangement into separate units of accounting, we apply one of the accounting policies described above to each unit. If we are unable to unbundle the arrangement into separate units of accounting, we apply one of the accounting policies described above to the entire arrangement. Sometimes this results in recognizing the entire arrangement fee when delivery of the last element in a multiple element arrangement occurs. For example, if the last undelivered element is a service, we recognize revenue for the entire arrangement fee as the service is performed, or if no pattern of performance is discernable, we recognize revenue on a straight-line basis over the term of the arrangement.

We record revenue on a net basis for those sales in which we have in substance acted as an agent or broker in the transaction.

Allowance for Doubtful Accounts

We make estimates regarding the collectibility of our accounts receivable. When we evaluate the adequacy of our allowance for doubtful accounts, we analyze specific accounts receivable balances, historical bad debts, customer creditworthiness, current economic trends and changes in our customer payment cycles. Material differences may result in the amount and timing of expense for any period if we were to make different judgments or utilize different estimates. If the financial condition of our customers deteriorates resulting in an impairment of their ability to make payments, additional allowances might be required. We have not experienced significant variances in the past between our estimated and actual doubtful accounts and anticipate that we will be able to continue to make reasonable estimates in the future. If for some reason we did not reasonably estimate the amount of our doubtful accounts in the future, it could have a material impact on our consolidated results of operations.

Business Acquisitions; Valuation of Goodwill and Other Intangible Assets

Our business acquisitions typically result in the recognition of goodwill and other intangible assets, and in certain cases non-recurring charges associated with the write-off of in-process research and development (IPR&D), which affect the amount of current and future period charges and amortization expense. Goodwill represents the excess of the purchase price over the fair value of net assets acquired, including identified intangible assets, in connection with our business combinations accounted for by the purchase method of accounting. We amortize our definite-lived intangible assets using the straight-line method or based on forecasted cash flows associated with the assets over the estimated useful lives, while IPR&D is recorded as a non-recurring charge on the acquisition date. Goodwill is not amortized, but rather is periodically assessed for impairment.

The determination of the value of these components of a business combination, as well as associated asset useful lives, requires management to make various estimates and assumptions. Critical estimates in valuing certain of the intangible assets include but are not limited to: future expected cash flows from product sales and services, maintenance agreements, consulting contracts, customer contracts, and acquired developed technologies and patents or trademarks; expected costs to develop the IPR&D into commercially viable products and estimating cash flows from the projects when completed; the acquired company s brand awareness and market position, as well as assumptions about the period of time the acquired products and services will continue to be used in our product portfolio; and discount rates. Management s estimates of fair value and useful lives are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable. Unanticipated events and circumstances may occur and assumptions may change. Estimates using different assumptions could also produce significantly different results.

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We continually review the events and circumstances related to our financial performance and economic environment for factors that would provide evidence of the impairment of our intangible assets. When impairment indicators are identified with respect to our previously recorded intangible assets, then we test for impairment using undiscounted cash flows. If such tests indicate impairment, then we measure the impairment as the difference between the carrying value of the asset and the fair value of the asset, which is measured using discounted cash flows. Significant management judgment is required in forecasting of future operating results, which are used in the preparation of the projected discounted cash flows and should different conditions prevail, material write downs of net intangible assets and other long-lived assets could occur. We periodically review the estimated remaining useful lives of our acquired intangible assets. A reduction in our estimate of remaining useful lives, if any, could result in increased amortization expense in future periods.

We test goodwill for impairment at the reporting unit level at least annually during the fourth quarter of each fiscal year and more frequently if impairment indicators are identified. We have determined that our reporting units are the same as our reportable segments. The first step of the goodwill impairment test is a comparison of the fair value of a reporting unit to its carrying value. We estimate the fair values of our reporting units using discounted cash flow valuation models and by comparing our reporting units to guideline publicly-traded companies. These methods require estimates of our future revenues, profits, capital expenditures, working capital, and other relevant factors, as well as selecting appropriate guideline publicly-traded companies for each reporting unit. We estimate these amounts by evaluating historical trends, current budgets, operating plans, industry data, and other relevant factors. The estimated fair value of each of our reporting units exceeded its respective carrying value in fiscal 2006, indicating the underlying goodwill of each reporting unit was not impaired as of our most recent testing date. Accordingly, we were not required to complete the second step of the goodwill impairment test. The timing and frequency of our goodwill impairment test is based on an ongoing assessment of events and circumstances that would more than likely reduce the fair value of a reporting unit below its carrying value. We will continue to monitor our goodwill balance and conduct formal tests on at least an annual basis or earlier when impairment indicators are present. There are various assumptions and estimates underlying the determination of an impairment loss, and estimates using different, but each reasonable, assumptions could produce significantly different results. Therefore, the timing and recognition of impairment losses by us in the future, if any, may be highly dependent upon our estimates and assumptions. We believe that the assumptions and estimates utilized were appropriate based on the information available to management.

Share-Based Compensation

Prior to October 1, 2005, we accounted for our share-based employee compensation plans under the measurement and recognition provisions of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations, as permitted by Financial Accounting Standards Board (FASB) SFAS No. 123, *Accounting for Stock-Based Compensation*. We generally recorded no employee compensation expense for options granted prior to October 1, 2005 as options granted generally had exercise prices equal to the fair market value of our common stock on the date of grant. We also recorded no compensation expense in connection with our 1999 Employee Stock Purchase Plan as the purchase price of the stock was not less than 85% of the lower of the fair market value of our common stock at the beginning of each offering period or at the end of each offering period. In accordance with SFAS No. 123, we disclosed our net income and earnings per share as if we had applied the fair value-based method in measuring compensation expense for our share-based incentive awards.

Effective October 1, 2005, we adopted the fair value recognition provisions of SFAS No. 123(R), *Share-Based Payment,* using the modified prospective transition method. Under that transition method, compensation expense that we recognize beginning on that date includes expense associated with the fair value of all awards granted on and after October 1, 2005, and expense for the unvested portion of previously granted awards outstanding on October 1, 2005. Results for prior periods have not been restated.

We estimate the fair value of options granted using the Black-Scholes option valuation model. We estimate the volatility of our common stock at the date of grant based on a combination of the implied volatility of publicly traded options on our common stock and our historical volatility rate, consistent with SFAS No. 123(R) and Securities and Exchange Commission Staff Accounting Bulletin No. 107 (SAB 107). Our decision to use implied volatility was based upon the availability of actively traded options on our common stock and our assessment that implied volatility is more representative of future stock price trends than historical volatility. We estimate expected term consistent with the simplified method identified in SAB 107 for share-based awards. We elected to use the simplified method as we changed the contractual life for share-based awards from ten to seven years starting in fiscal 2006. The simplified method calculates the expected term as the average of the vesting and contractual terms of the award. Previously, we estimated expected term based on historical exercise patterns. The dividend yield assumption is based on historical dividend payouts. The risk-free interest rate assumption is based on observed interest rates appropriate for the term of our employee options. We use historical data to estimate pre-vesting option forfeitures and record share-based compensation expense only for those awards that are expected to vest. For options granted, we amortize the fair value on a straight-line basis. All options are amortized over the requisite service periods of the awards, which are generally the vesting periods. If factors change we may decide to use different assumptions under the Black-Scholes option valuation model in the future, which could materially affect our net income and earnings per share.

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Income Taxes

We use the asset and liability approach to account for income taxes. This methodology recognizes deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax base of assets and liabilities and operating loss and tax credit carryforwards. We then record a valuation allowance to reduce deferred tax assets to an amount that more likely than not will be realized. We consider future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance, which requires the use of estimates. If we determine during any period that we could realize a larger net deferred tax asset than the recorded amount, we would adjust the deferred tax asset to increase income for the period or reduce goodwill if such deferred tax asset relates to an acquisition. Conversely, if we determine that we would be unable to realize a portion of our recorded deferred tax asset, we would adjust the deferred tax asset to record a charge to income for the period or increase goodwill if such deferred tax asset relates to an acquisition. Although we believe that our estimates are reasonable, there is no assurance that our the valuation allowance will not need to be increased to cover additional deferred tax assets that may not be realizable, and such an increase could have a material adverse impact on our income tax provision and results of operations in the period in which such determination is made. In addition, the calculation of tax liabilities also involves significant judgment in estimating the impact of uncertainties in the application of complex tax laws. Resolution of these uncertainties in a manner inconsistent with management s expectations could also have a material impact on our income tax provision and results of operations in the period in which such determination is made.

Contingencies and Litigation

We are subject to various proceedings, lawsuits and claims relating to products and services, technology, labor, shareholder and other matters. We are required to assess the likelihood of any adverse outcomes and the potential range of probable losses in these matters. If the potential loss is considered probable and the amount can be reasonably estimated, we accrue a liability for the estimated loss. If the potential loss is considered less than probable or the amount cannot be reasonably estimated, disclosure of the matter is considered. The amount of loss accrual or disclosure, if any, is determined after analysis of each matter, and is subject to adjustment if warranted by new developments or revised strategies. Due to uncertainties related to these matters, accruals or disclosures are based on the best information available at the time. Significant judgment is required in both the assessment of likelihood and in the determination of a range of potential losses. Revisions in the estimates of the potential liabilities could have a material impact on our consolidated financial position or consolidated results of operations.

New Accounting Pronouncements Not Yet Adopted

In July 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes,* which prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. Additionally, FIN 48 provides guidance on the derecognition, classification, accounting in interim periods and disclosure requirements for uncertain tax positions. The accounting provisions of FIN 48 will be effective for the Company beginning October 1, 2007. We are in the process of determining what effect, if any, the adoption of FIN 48 will have on our consolidated financial statements.

In September 2006, the SEC released Staff Accounting Bulletin (SAB) No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements*, which provided the Staff s view regarding the process of quantifying financial statement misstatements. SAB 108 requires an entity to quantify misstatements using both a balance sheet and income statement approach to determine if a misstatement is material. The evaluation requirements of SAB No. 108 are effective for fiscal years ending after November 15, 2006. We are in the process of determining what effect, if any, the adoption of SAB No. 108 will have on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measures*, which defines fair value, establishes a framework for measuring fair value and expands disclosures about assets and liabilities measured at fair value. The statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are in the process of determining what effect, if any, the adoption of SFAS No. 157 will have on our consolidated financial statements.

Item 3. *Quantitative and Qualitative Disclosures About Market Risk*

Market Risk Disclosures

We are exposed to market risk related to changes in interest rates, equity market prices, and foreign currency exchange rates. We do not use derivative financial instruments for speculative or trading purposes.

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Interest Rate Risk

We maintain an investment portfolio consisting mainly of income securities with an average maturity of three years or less. These available-for-sale securities are subject to interest rate risk and will fall in value if market interest rates increase. We have the ability to hold our fixed income investments until maturity, and therefore we would not expect our operating results or cash flows to be affected to any significant degree by the effect of a sudden change in market interest rates on our securities portfolio. The following table presents the principal amounts and related weighted-average yields for our investments with interest rate risk at December 31, 2006 and September 30, 2006:

	December 31, 2006			September 30, 2006		
	Cost Basis	Carrying Amount	Average Yield	Cost Basis	Carrying Amount	Average Yield
			(In thousands)			
Cash and cash equivalents	$ 99,149	$ 99,149	2.98%	$ 75,178	$ 75,154	2.85%
Short-term investments	122,997	122,812	4.84%	152,446	152,141	4.79%
Long-term investments	41,753	41,679	5.20%	33,306	33,254	5.10%
	$ 263,899	$ 263,640	4.20%	$ 260,930	$ 260,549	4.27%

We are the issuer of 1.5% Senior Convertible Notes (Senior Notes) that mature in August 2023. The fair value of our Senior Notes, as determined based on quoted market prices, may increase or decrease due to various factors, including fluctuations in the market price of our common stock, fluctuations in market interest rates and fluctuations in general economic conditions. The following table presents the principal amounts, carrying amounts, and fair values for our Senior Notes at December 31, 2006 and September 30, 2006:

	December 31, 2006			September 30, 2006		
	Principal	Carrying Amount	Fair Value	Principal	Carrying Amount	Fair Value
			(In thousands)			
Senior Notes	$400,000	$400,000	$424,000	$400,000	$400,000	$407,000

We have interest rate risk with respect to our five-year $300 million unsecured revolving credit facility. Interest rates are applied to amounts outstanding under this facility at variable rates based on Federal Funds rate plus 0.50% or LIBOR plus margins that range from 0.30% to 0.55% based on our consolidated leverage ratio. A change in interest rates on this variable rate debt impacts the interest incurred and cash flows, but does not impact the fair value of the instrument. As of December 31, 2006 we had $70.0 million of borrowings outstanding on this facility and we had no borrowings outstanding as of September 30, 2006.

Forward Foreign Currency Contracts

We maintain a program to manage our foreign currency exchange rate risk on existing foreign currency receivable and bank balances by entering into forward contracts to sell or buy foreign currency. At period end, foreign-denominated receivables and cash balances held by our U.S. reporting entities are remeasured into the U.S. dollar functional currency at current market rates. The change in value from this remeasurement is then reported as a foreign exchange gain or loss for that period in our accompanying consolidated statements of income and the resulting gain or loss on the forward contract mitigates the exchange rate risk of the associated assets. All of our forward foreign currency contracts have maturity periods of less than three months. Such derivative financial instruments are subject to market risk.

The following table summarizes our outstanding forward foreign currency contracts, by currency at December 31, 2006:

	Contract Amount		
	Foreign Currency	US $	Fair Value US $
	(In thousands)		
Sell foreign currency:			
EURO (EUR)	EUR 13,650	$17,969	$
Japanese Yen (YEN)	YEN 110,000	925	
Buy foreign currency:			
British Pound (GBP)	GBP 4,082	$ 8,000	$

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The forward foreign currency contracts were all entered into on December 31, 2006, therefore, the fair value was $0 on that date.

Item 4. ***Controls and Procedures***

Evaluation of Disclosure Controls and Procedures

An evaluation was carried out under the supervision and with the participation of Fair Isaac s management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of Fair Isaac s disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this quarterly report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that Fair Isaac s disclosure controls and procedures are effective to ensure that information required to be disclosed by Fair Isaac in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and (ii) accumulated and communicated to the Chief Executive Officer and Chief Financial Officer to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

No change in Fair Isaac s internal control over financial reporting was identified in connection with the evaluation required by Rule 13a-15(d) of the Exchange Act that occurred during the period covered by this quarterly report and that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. ***Legal Proceedings***

We are a defendant in a lawsuit captioned as *Robbie Hillis v. Equifax Consumer Services, Inc. and Fair Isaac, Inc.,* which is pending in the U.S. District Court for the Northern District of Georgia. The plaintiff claims that the defendants have jointly sold the Score Power® credit score product in violation of certain procedural requirements under the Credit Repair Organizations Act (CROA), and in violation of the antifraud provisions of that statute. The plaintiff also claims that the defendants are credit repair organizations under CROA. The plaintiff is seeking certification of a class on behalf of all individuals who purchased products containing Score Power from the defendants in the five year period prior to the filing of the Complaint on November 14, 2004. The plaintiff is seeking unspecified damages, attorneys fees and costs. We believe that the claims in this lawsuit are without merit, and we have denied any liability or wrongdoing and have denied that class certification is appropriate. We are vigorously contesting this matter. The plaintiff brought a motion for class certification and a motion for summary judgment in his favor and against the defendants. We opposed, and the Court denied, both of the plaintiff s motions. The plaintiff has brought a motion asking the Court to reconsider its prior ruling. That motion is pending.

We are a defendant in a lawsuit captioned as *Christy Slack v. Fair Isaac Corporation and MyFICO Consumer Services, Inc.*, which is pending in the United States District Court for the Northern District of California. As in the Hillis matter, the plaintiff is claiming that the defendants violated certain procedural requirements of CROA, and violated the antifraud provisions of CROA, with respect to the sale of credit score products on our myFICO.com website. The plaintiff also claims that the defendants violated the California Credit Services Act (the CSA) and were unjustly enriched. The plaintiff has sought certification of a class on behalf of all individuals who purchased credit score products from us on the myFICO.com website in the five year period prior to the filing of the Complaint on January 18, 2005. Plaintiff seeks unspecified damages, attorneys fees and costs. We believe that the claims in this lawsuit are without merit and we have denied any liability or wrongdoing and have denied that class certification is appropriate. We are vigorously contesting this matter. We brought a motion to dismiss the plaintiff s claims. The Court granted our motion, in part, by dismissing certain of the plaintiff s claims under the CSA. The plaintiff has brought motions for summary judgment and for class certification. We have opposed both motions. The Court has not yet ruled on the plaintiff s motions.

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Item 1A. ***Risk Factors***

Risks Related to Our Business

We have expanded the pursuit of our EDM strategy, and we may not be successful.

We have expanded the pursuit of our business objective to become a leader in helping businesses automate and improve decisions across their enterprises, an approach that we commonly refer to as Enterprise Decision Management, or EDM. Our EDM strategy is designed to enable us to increase our business by selling multiple products to clients, as well as to enable the development of custom client solutions that may lead to opportunities to develop new proprietary scores or other new proprietary products. The market may be unreceptive to this general EDM business approach, including being unreceptive to purchasing multiple products from us or unreceptive to our customized solutions. If our EDM strategy is not successful, we may not be able to grow our business, growth may occur more slowly than we anticipate or our revenues and profits may decline.

We recently restructured the method by which we sell our products and services and if our new sales strategy is not successful, our business will be harmed.

Previously, we sold our products and services in a product-focused manner. As part of our expanded EDM strategy, we now sell our products and services using a client-centric approach which focuses on delivering complete solutions involving multiple products or suites of products for our customers through various means, including the use of client teams called Integrated Client Networks (or ICNs) that focus on customers by vertical market and geography, and the use of an integrated consulting and sales approach. If our employees are not able to adjust rapidly enough to this ICN approach, then we may be unable to maintain or increase our revenues. Further, there can be no assurance that our customers and potential customers will react positively to EDM or this new selling approach and, as a result, that we will continue to maintain or increase revenues. If revenues eventually increase as a result of this change, there is no assurance that any increase will occur as quickly as we might anticipate.

We derive a substantial portion of our revenues from a small number of products and services, and if the market does not continue to accept these products and services, our revenues will decline.

As we attempt to implement our EDM strategy, we expect that revenues derived from our scoring solutions, account management solutions, fraud solutions, originations, collections, and insurance solutions products and services will continue to account for a substantial portion of our total revenues for the foreseeable future. Our revenues will decline if the market does not continue to accept these products and services. Factors that might affect the market acceptance of these products and services include the following:

- changes in the business analytics industry;
- changes in technology;
- our inability to obtain or use state fee schedule or claims data in our insurance products;
- saturation of market demand;
- loss of key customers;
- industry consolidation;
- failure to execute our client-centric selling approach; and
- inability to successfully sell our products in new vertical markets.

If we are unable to access new markets or develop new distribution channels, our business and growth prospects could suffer.

We expect that part of the growth that we seek to achieve through our EDM strategy will be derived from the sale of EDM products and service solutions in industries and markets we do not currently serve. We also expect to grow our business by delivering our EDM solutions through additional distribution channels. If we fail to penetrate these industries and markets to the degree we anticipate utilizing our EDM strategy, or if we fail to develop additional distribution channels, we may not be able to grow our business, growth may occur more slowly than we anticipate or our revenues and profits may decline.

If we are unable to develop successful new products or if we experience defects, failures and delays associated with the introduction of new products, our business could suffer serious harm.

Our growth and the success of our EDM strategy depends upon our ability to develop and sell new products or suites of products. If we are unable to develop new products, or if we are not successful in introducing new products, we may not be able to grow our business, or growth may occur more slowly than we anticipate. In addition, significant undetected errors or delays in new products or new versions of products may affect market acceptance of our products and could harm our business, financial condition or results of operations. In the past, we have experienced delays while developing and introducing new products and product enhancements, primarily due to difficulties developing models, acquiring data and adapting to particular operating environments. We have also experienced errors or bugs in our software products, despite testing prior to release of the products. Software errors in our products could affect the ability of our products to work with other hardware or software products, could delay the development or release of new products or new versions of products and could adversely affect market acceptance of our products. Errors or defects in our products that are significant, or are perceived to be significant, could result in rejection of our products, damage to our reputation, loss of revenues, diversion of development resources, an increase in product liability claims, and increases in service and support costs and warranty claims.

We rely on relatively few customers, as well as our contracts with the three major credit reporting agencies, for a significant portion of our revenues and profits. If the terms of these relationships change, our revenues and operating results could decline.

Most of our customers are relatively large enterprises, such as banks, credit card processors, insurance companies, healthcare firms, retailers and telecommunications carriers. As a result, many of our customers and potential customers are significantly larger than we are and may have sufficient bargaining power to demand reduced prices and favorable nonstandard terms.

We also derive a substantial portion of our revenues and operating income from our contracts with the three major credit reporting agencies, TransUnion, Equifax and Experian, and other parties that distribute our products to certain markets. We are also currently involved in litigation with TransUnion, Equifax and Experian arising from their development and marketing of a credit scoring product competitive with our products. We have asserted various claims, including claims of unfair competition and antitrust, against each of the credit reporting agencies and their collective joint venture entity, VantageScore, LLC. This litigation could have a material adverse effect on our relationship with one or more of the major credit reporting agencies, or with major customers.

The loss of or a significant change in a relationship with a major customer, the loss of or a significant change in a relationship with one of the major credit reporting agencies with respect to their distribution of our products or with respect to our myFICO offerings, the loss of or a significant change in a relationship with a significant third-party distributor or the delay of significant revenues from these sources, could have a material adverse effect on our revenues and results of operations.

We rely on relationships with third parties for marketing and distribution. If we experience difficulties in these relationships, our future revenues may be adversely affected.

Our Scoring Solutions segment and Strategy Machine Solutions segment rely on distributors, and we intend to continue to market and distribute our products through existing and future distributor relationships. Our Scoring Solutions segment relies on, among others, TransUnion, Equifax and Experian. Failure of our existing and future distributors to generate significant revenues, demands by such distributors to change the terms on which they offer our products or our failure to establish additional distribution or sales and marketing alliances could have a material adverse effect on our business, operating results and financial condition. In addition, certain of our distributors presently compete with us and may compete with us in the future either by developing competitive products themselves or by distributing competitive offerings. For example, TransUnion, Equifax and Experian have developed a credit scoring product to compete directly with our products and are collectively attempting to sell the product. Competition from distributors or other sales and marketing partners could significantly harm sales of our products.

If we do not engage in acquisition activity to the extent we have in the past, we may be unable to increase our revenues at historical growth rates.

Our historical revenue growth has been augmented by numerous acquisitions, and we anticipate that acquisitions will continue to be an important part of our revenue growth. Our future revenue growth rate may decline if we do not make acquisitions of similar size and at a comparable rate as in the past.

If we engage in acquisitions, significant investments in new businesses, or divestitures of existing businesses, we will incur a variety of risks, any of which may adversely affect our business.

We have made in the past, and may make in the future, acquisitions of, or significant investments in, businesses that offer complementary products, services and technologies. Any acquisitions or investments will be accompanied by the risks commonly encountered in acquisitions of businesses, which may include:

failure to achieve the financial and strategic goals for the acquired and combined business;

- overpayment for the acquired companies or assets;
- difficulty assimilating the operations and personnel of the acquired businesses;
- product liability exposure associated with acquired businesses or the sale of their products;
- disruption of our ongoing business;
- dilution of our existing stockholders and earnings per share;
- unanticipated liabilities, legal risks and costs;
- retention of key personnel;
- distraction of management from our ongoing business; and
- impairment of relationships with employees and customers as a result of integration of new management personnel.

We have also divested ourselves of businesses in the past, and may do so again in the future. Any divestitures will be accompanied by the risks commonly encountered in the sale of businesses, which may include:

- disruption of our ongoing business;
- reductions of our revenues or earnings per share;
- unanticipated liabilities, legal risks and costs;
- the potential loss of key personnel;
- distraction of management from our ongoing business; and
- impairment of relationships with employees and customers as a result of migrating a business to new owners.

These risks could harm our business, financial condition or results of operations, particularly if they occur in the context of a significant acquisition. Acquisitions of businesses having a significant presence outside the U.S. will increase our exposure to the risks of conducting operations in international markets.

The occurrence of certain negative events may cause fluctuations in our stock price.

The market price of our common stock may be volatile and could be subject to wide fluctuations due to a number of factors, including variations in our revenues and operating results. We believe that you should not rely on period-to-period comparisons of financial results as an indication of future performance. Because many of our operating expenses are fixed and will not be affected by short-term fluctuations in revenues, short-term fluctuations in revenues may significantly impact operating results. Additional factors that may cause our stock price to fluctuate include the following:

- variability in demand from our existing customers;
- failure to meet the expectations of market analysts;
- changes in recommendations by market analysts;
- the lengthy and variable sales cycle of many products, combined with the relatively large size of orders for our products, increases the likelihood of short-term fluctuation in revenues;

- consumer dissatisfaction with, or problems caused by, the performance of our products;
- the timing of new product announcements and introductions in comparison with our competitors;
- the level of our operating expenses;
- changes in competitive conditions in the consumer credit, financial services and insurance industries;
- fluctuations in domestic and international economic conditions;
- our ability to complete large installations on schedule and within budget;
- acquisition-related expenses and charges; and
- timing of orders for and deliveries of software systems.

In addition, the financial markets have experienced significant price and volume fluctuations that have particularly affected the stock prices of many technology companies, and these fluctuations sometimes have been unrelated to the operating performance of these companies. Broad market fluctuations, as well as industry-specific and general economic conditions may adversely affect the market price of our common stock.

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Our products have long and variable sales cycles. If we do not accurately predict these cycles, we may not forecast our financial results accurately and our stock price could be adversely affected.

We experience difficulty in forecasting our revenues accurately because the length of our sales cycles makes it difficult for us to predict the quarter in which sales will occur. In addition, our ICN selling approach is more complex than our prior sales approach because it emphasizes the sale of complete EDM solutions involving multiple products or services across our customers organizations. This makes forecasting of revenues in any given period more difficult. As a result of our ICN approach and lengthening sales cycles, revenues and operating results may vary significantly from period to period. For example, the sales cycle for licensing our products typically ranges from 60 days to 18 months. Customers are often cautious in making decisions to acquire our products, because purchasing our products typically involves a significant commitment of capital, and may involve shifts by the customer to a new software and/or hardware platform or changes in the customer s operational procedures. Since our EDM strategy contemplates the sale of multiple decision solutions to a customer, expenditures by any given customer are expected to be larger than with our prior sales approach. This may cause customers to make purchasing decisions more cautiously. Delays in completing sales can arise while customers complete their internal procedures to approve large capital expenditures and test and accept our applications. Consequently, we face difficulty predicting the quarter in which sales to expected customers will occur and experience fluctuations in our revenues and operating results. If we are unable to accurately forecast our revenues, our stock price could be adversely affected.

We typically have revenue-generating transactions concentrated in the final weeks of a quarter which may prevent accurate forecasting of our financial results and cause our stock price to decline.

Large portions of our software license agreements are consummated in the weeks immediately preceding quarter end. Before these agreements are consummated we create and rely on forecasted revenues for planning, modeling and earnings guidance. Forecasts, however, are only estimates and actual results may vary for a particular quarter or longer periods of time. Consequently, significant discrepancies between actual and forecasted results could limit our ability to plan, budget or provide accurate guidance, which could adversely affect our stock price. Any publicly-stated revenue or earnings projections are subject to this risk.

The failure to recruit and retain additional qualified personnel could hinder our ability to successfully manage our business.

Our EDM strategy and our future success will depend in large part on our ability to attract and retain experienced sales, consulting, research and development, marketing, technical support and management personnel. The complexity of our products requires highly trained customer service and technical support personnel to assist customers with product installation and deployment. The labor market for these individuals is very competitive due to the limited number of people available with the necessary technical skills and understanding and may become more competitive with general market and economic improvement. We cannot be certain that our compensation strategies will be perceived as competitive by current or prospective employees. This could impair our ability to recruit and retain personnel. We have experienced difficulty in recruiting qualified personnel, especially technical, sales and consulting personnel, and we may need additional staff to support new customers and/or increased customer needs. We may also recruit skilled technical professionals from other countries to work in the United States. Limitations imposed by immigration laws in the United States and abroad and the availability of visas in the countries where we do business could hinder our ability to attract necessary qualified personnel and harm our business and future operating results. There is a risk that even if we invest significant resources in attempting to attract, train and retain qualified personnel, we will not succeed in our efforts, and our business could be harmed. Non-appreciation in the value of our stock may adversely affect our ability to use equity and equity based incentive plans to attract and retain personnel, and may require us to use alternative and more expensive forms of compensation for this purpose.

The failure to obtain certain forms of model construction data from our customers or others could harm our business.

We must develop or obtain a reliable source of sufficient amounts of current and statistically relevant data to analyze transactions and update our products. In most cases, these data must be periodically updated and refreshed to enable our products to continue to work effectively in a changing environment. We do not own or control much of the data that we require, most of which is collected privately and maintained in proprietary databases. Customers and key business alliances provide us the data we require to analyze transactions, report results and build new models. Our EDM strategy depends in part upon our ability to access new forms of data to develop custom and proprietary analytic tools. If we fail to maintain sufficient sourcing relationships with our customers and business alliances, or if they decline to provide such data due to legal privacy concerns, competition concerns, prohibitions or a lack of permission from their customers, we could lose access to required data and our products might become less effective. In addition, certain of our insurance solutions products use data from state workers compensation fee schedules adopted by state regulatory agencies. Third parties have asserted copyright interests in these data, and these assertions, if successful, could prevent us from using these data. Any interruption of our supply of data could seriously harm our business, financial condition or results of operations.

We will continue to rely upon proprietary technology rights, and if we are unable to protect them, our business could be harmed.

Our success depends, in part, upon our proprietary technology and other intellectual property rights. To date, we have relied primarily on a combination of copyright, patent, trade secret, and trademark laws, and nondisclosure and other contractual restrictions on copying and distribution to protect our proprietary technology. This protection of our proprietary technology is limited, and our proprietary technology could be used by others without our consent. In addition, patents may not be issued with respect to our pending or future patent applications, and our patents may not be upheld as valid or may not prevent the development of competitive products. Any disclosure, loss, invalidity of, or failure to protect our intellectual property could negatively impact our competitive position, and ultimately, our business. There can be no assurance that our protection of our intellectual property rights in the United States or abroad will be adequate or that others, including our competitors, will not use our proprietary technology without our consent. Furthermore, litigation may be necessary to enforce our intellectual property rights, to protect our trade secrets, or to determine the validity and scope of the proprietary rights of others. Such litigation could result in substantial costs and diversion of resources and could harm our business, financial condition or results of operations.

Some of our technologies were developed under research projects conducted under agreements with various U.S. government agencies or subcontractors. Although we have commercial rights to these technologies, the U.S. government typically retains ownership of intellectual property rights and licenses in the technologies developed by us under these contracts, and in some cases can terminate our rights in these technologies if we fail to commercialize them on a timely basis. Under these contracts with the U.S. government, the results of research may be made public by the government, limiting our competitive advantage with respect to future products based on our research.

If we are subject to infringement claims, it could harm our business.

With recent developments in the law that permit patenting of business methods, we expect that products in the industry segments in which we compete, including software products, will increasingly be subject to claims of patent infringement as the number of products and competitors in our industry segments grow. We may need to defend claims that our products infringe patent, copyright or other rights, and as a result we may:

- incur significant defense costs or substantial damages;

- be required to cease the use or sale of infringing products;

- expend significant resources to develop or license a substitute non-infringing technology;

- discontinue the use of some technology; or

- be required to obtain a license under the intellectual property rights of the third party claiming infringement, which license may not be available or might require substantial royalties or license fees that would reduce our margins.

Breaches of security, or the perception that e-commerce is not secure, could harm our business.

Our business requires the appropriate and secure utilization of consumer and other sensitive information. Internet-based, electronic commerce requires the secure transmission of confidential information over public networks, and several of our products are accessed through the Internet, including our consumer services accessible through the www.myFICO.com website. Security breaches in connection with the delivery of our products and services, including products and services utilizing the Internet, or well-publicized security breaches, and the trend toward broad consumer and general public notification of such incidents, could significantly harm our business, financial condition or results of operations. We cannot be certain that advances in criminal capabilities, discovery of new vulnerabilities, attempts to exploit vulnerabilities in our systems, data thefts, physical system or network break-ins or inappropriate access, or other developments will not compromise or breach the technology protecting the networks that access our net-sourced products, consumer services and proprietary database information.

Protection from system interruptions is important to our business. If we experience a sustained interruption of our telecommunication systems it could harm our business.

Systems or network interruptions could delay and disrupt our ability to develop, deliver or maintain our products and services, causing harm to our business and reputation and resulting in loss of customers or revenue. These interruptions can include fires, floods, earthquakes, power losses, equipment failures and other events beyond our control.

Risks Related to Our Industry

Our ability to increase our revenues will depend to some extent upon introducing new products and services. If the marketplace does not accept these new products and services, our revenues may decline.

We have a significant share of the available market in portions of our Scoring Solutions segment and for certain services in our Strategy Machine Solutions segment, specifically, the markets for account management services at credit card processors and credit card fraud detection software. To increase our revenues, we must enhance and improve existing products and continue to introduce new products and new versions of existing products that keep pace with technological developments, satisfy increasingly sophisticated customer requirements and achieve market acceptance. We believe much of the future growth of our business and the success of our EDM strategy will rest on our ability to continue to expand into newer markets for our products and services, such as direct marketing, healthcare, insurance, small business lending, retail, telecommunications, personal credit management, the design of business strategies using Strategy Science technology and Internet services. These areas are relatively new to our product development and sales and marketing personnel. Products that we plan to market in the future are in various stages of development. We cannot assure you that the marketplace will accept these products. If our current or potential customers are not willing to switch to or adopt our new products and services, our revenues will decrease.

If we fail to keep up with rapidly changing technologies, our products could become less competitive or obsolete.

In our markets, technology changes rapidly, and there are continuous improvements in computer hardware, network operating systems, programming tools, programming languages, operating systems, database technology and the use of the Internet. If we fail to enhance our current products and develop new products in response to changes in technology or industry standards, or if we fail to bring product enhancements or new product developments to market quickly enough, our products could rapidly become less competitive or obsolete. For example, the rapid growth of the Internet environment creates new opportunities, risks and uncertainties for businesses, such as ours, which develop software that must also be designed to operate in Internet, intranet and other online environments. Our future success will depend, in part, upon our ability to:

- innovate by internally developing new and competitive technologies;
- use leading third-party technologies effectively;
- continue to develop our technical expertise;
- anticipate and effectively respond to changing customer needs;
- initiate new product introductions in a way that minimizes the impact of customers delaying purchases of existing products in anticipation of new product releases; and
- influence and respond to emerging industry standards and other technological changes.

If our competitors introduce new products and pricing strategies, it could decrease our product sales and market share, or could pressure us to reduce our product prices in a manner that reduces our margins.

We may not be able to compete successfully against our competitors, and this inability could impair our capacity to sell our products. The market for business analytics is new, rapidly evolving and highly competitive, and we expect competition in this market to persist and intensify. Our regional and global competitors vary in size and in the scope of the products and services they offer, and include:

- in-house analytic and systems developers;
- scoring model builders;
- enterprise resource planning (ERP) and customer relationship management (CRM) packaged solutions providers;

business intelligence solutions providers;

credit report and credit score providers;

business process management solution providers;

process modeling tools providers;

automated application processing services providers;

data vendors;

neural network developers and artificial intelligence system builders;

third-party professional services and consulting organizations;

account/workflow management software providers;

managed care organizations; and

software tools companies supplying modeling, rules, or analytic development tools.

We expect to experience additional competition from other established and emerging companies, as well as from other technologies. For example, certain of our fraud solutions products compete against other methods of preventing credit card fraud, such as credit cards that contain the cardholder s photograph, smart cards, cardholder verification and authentication solutions and other card authorization techniques. Many of our anticipated competitors have greater financial, technical, marketing, professional services and other resources than we do and industry consolidation is creating even larger competitors in many of our markets. As a result, our competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements. They may also be able to devote greater resources than we can to develop, promote and sell their products. Many of these companies have extensive customer relationships, including relationships with many of our current and potential customers. Furthermore, new competitors or alliances among competitors may emerge and rapidly gain significant market share. For example, TransUnion, Equifax and Experian have formed an alliance that has developed a credit scoring product competitive with our products. If we are unable to respond as quickly or effectively to changes in customer requirements as our competition, our ability to expand our business and sell our products will be negatively affected.

Our competitors may be able to sell products competitive to ours at lower prices individually or as part of integrated suites of several related products. This ability may cause our customers to purchase products that directly compete with our products from our competitors. Price reductions by our competitors could negatively impact our margins, and could also harm our ability to obtain new long-term contracts and renewals of existing long-term contracts on favorable terms.

Government regulations that apply to us or to our customers may expose us to liability, affect our ability to compete in certain markets, limit the profitability of or demand for our products, or render our products obsolete. If these regulations are applied or are further developed in ways adverse to us, it could adversely affect our business and results of operations.

Legislation and governmental regulation affect how our business is conducted and, in some cases, subject us to the possibility of future lawsuits arising from our products and services. Globally, legislation and governmental regulation also influence our current and prospective customers activities, as well as their expectations and needs in relation to our products and services. Both our core businesses and our newer initiatives are affected globally by federal, regional, provincial, state and other jurisdictional regulations, including those in the following significant regulatory areas:

Consumer report data and consumer reporting agencies. Examples in the U.S. include: the Fair Credit Reporting Act (FCRA), the Fair and Accurate Credit Transactions Act (FACTA), which amends FCRA, and certain proposed regulations under FACTA, presently under consideration;

Identity theft and loss of data. Examples include FACTA and other regulations modeled after the current California Security Breach Notification Act, that require consumer notification of security breach incidents and additional federal and state legislative enactments in this area;

Fair and non-discriminatory lending practices, such as the Equal Credit Opportunity Act (ECOA);

Privacy-related laws, including but not limited to the provisions of the Financial Services Modernization Act of 1999, also known as the Gramm Leach Bliley Act (GLBA), the Health Insurance Portability and Accountability Act of 1996 (HIPAA), the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA Patriot Act) and similar state privacy laws;

Extension of credit to consumers through the Electronic Fund Transfers Act, as well as non-governmental VISA and MasterCard electronic payment standards;

Quasi-governmental regulations, such as Fannie Mae and Freddie Mac regulations for our mortgage services products;

Insurance regulations related to our insurance products;

The application or extension of consumer protection laws, including, state and federal laws governing the use of the Internet and telemarketing, and credit repair;

Jurisdictional regulations applicable to international operations, including the European Union s Privacy Directive; and

Sarbanes-Oxley Act (SOX) regulations to verify internal process controls and require material event awareness and notification.

In making credit evaluations of consumers, performing fraud screening or user authentication, our customers are subject to requirements of multiple jurisdictions which may impose contradictory requirements. Privacy legislation such as GLBA or the European Union s Privacy Directive may also affect the nature and extent of the products or services that we can provide to customers, as well as our ability to collect, monitor and disseminate information subject to privacy protection. In addition to existing regulation, changes in legislative, judicial, regulatory or consumer environments could harm our business, financial condition or results of operations. For example, the FACTA amendments to FCRA will result in new regulation. These regulations or the interpretation of these amendments could affect the demand for or profitability of some of our products, including scoring and consumer products. New regulations pertaining to financial institutions could cause them to pursue new strategies, reducing the demand for our products. In addition, legislative reforms of workers compensation laws that aim to simplify this area of regulation and curb abuses could diminish the need for, and the benefits provided by, certain of our insurance solutions products and services.

Our revenues depend, to a great extent, upon conditions in the consumer credit, financial services and insurance industries. If any of our clients industries experiences a downturn, it could harm our business, financial condition or results of operations.

During fiscal 2006, 71% of our revenues were derived from sales of products and services to the consumer credit, financial services and insurance industries. A downturn in the consumer credit, the financial services or the insurance industry, including a downturn caused by increases in interest rates or a tightening of credit, among other factors, could harm our business, financial condition or results of operations. While the rate of account growth in the U.S. bankcard industry has been slowing and many of our large institutional customers have merged and consolidated in recent years, we have generated most of our revenue growth from our bankcard-related scoring and account management businesses by selling and cross-selling our products and services to large banks and other credit issuers. As this industry continues to consolidate, we may have fewer opportunities for revenue growth due to changing demand for our products and services that support customer acquisition programs of our customers. In addition, industry consolidation could affect the base of recurring revenues derived from contracts in which we are paid on a per-transaction basis if consolidated customers combine their operations under one contract. There can be no assurance that we will be able effectively to promote future revenue growth in our businesses.

While we are expanding our sales of consumer credit, financial services and insurance products and services into international markets, the risks are greater as we are less well-known and some of these markets are in their infancy.

Risk Related to External Conditions

If any of a number of material adverse developments occurs in general economic conditions and world events, such developments could affect demand for our products and services and harm our business.

Purchases of technology products and services and decisioning solutions are subject to adverse economic conditions. When an economy is struggling, companies in many industries delay or reduce technology purchases, and we experience softened demand for our decisioning solutions and other products and services. If the current improvement in global economic conditions slows or reverses, or if there is an escalation in regional or continued global conflicts or terrorism, we may experience reductions in capital expenditures by our customers, longer sales cycles, deferral or delay of purchase commitments for our products and increased price competition, which may adversely affect our business and results of operations.

In operations outside the United States, we are subject to unique risks that may harm our business, financial condition or results of operations.

A growing portion of our revenues is derived from international sales. During fiscal 2006, 28% of our revenues were derived from business outside the United States. As part of our growth strategy, we plan to continue to pursue opportunities outside the United States, including opportunities in countries with economic systems that are in early stages of development and that may not mature sufficiently to result in growth for our business. Accordingly, our future operating results could be negatively affected by a variety of factors arising out of international commerce, some of which are beyond our control. These factors include:

- general economic and political conditions in countries where we sell our products and services;
- difficulty in staffing and efficiently managing our operations in multiple geographic locations and in various countries;
- effects of a variety of foreign laws and regulations, including restrictions on access to personal information;
- import and export licensing requirements;

- longer payment cycles;
- reduced protection for intellectual property rights;
- currency fluctuations;
- changes in tariffs and other trade barriers; and
- difficulties and delays in translating products and related documentation into foreign languages.

There can be no assurance that we will be able to successfully address each of these challenges in the near term. Additionally, some of our business will be conducted in currencies other than the U.S. dollar. Foreign currency transaction gains and losses are not currently material to our cash flows, financial position or results of operations. However, an increase in our foreign revenues could subject us to increased foreign currency transaction risks in the future.

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In addition to the risk of depending on international sales, we have risks incurred in having research and development personnel located in various international locations. We currently have a substantial portion of our product development staff in international locations, some of which have political and developmental risks. If such risks materialize, our business could be damaged.

Our anti-takeover defenses could make it difficult for another company to acquire control of Fair Isaac, thereby limiting the demand for our securities by certain types of purchasers or the price investors are willing to pay for our stock.

Certain provisions of our Restated Certificate of Incorporation, as amended, could make a merger, tender offer or proxy contest involving us difficult, even if such events would be beneficial to the interests of our stockholders. These provisions include adopting a Shareholder Rights Agreement, commonly known as a poison pill, and giving our board the ability to issue preferred stock and determine the rights and designations of the preferred stock at any time without stockholder approval. The rights of the holders of our common stock will be subject to, and may be adversely affected by, the rights of the holders of any preferred stock that may be issued in the future. The issuance of preferred stock, while providing flexibility in connection with possible acquisitions and other corporate purposes, could have the effect of making it more difficult for a third party to acquire, or discouraging a third party from acquiring, a majority of our outstanding voting stock. These factors and certain provisions of the Delaware General Corporation Law may have the effect of deterring hostile takeovers or otherwise delaying or preventing changes in control or changes in our management, including transactions in which our stockholders might otherwise receive a premium over the fair market value of our common stock.

If we experience changes in tax laws or adverse outcomes resulting from examination of our income tax returns, it could adversely affect our results of operations.

We are subject to federal and state income taxes in the United States and in certain foreign jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes. Our future effective tax rates could be adversely affected by changes in tax laws, by our ability to generate taxable income in foreign jurisdictions in order to utilize foreign tax losses, and by the valuation of our deferred tax assets. In addition, we are subject to the examination of our income tax returns by the Internal Revenue Service and other tax authorities. We regularly assess the likelihood of adverse outcomes resulting from such examinations to determine the adequacy of our provision for income taxes. There can be no assurance that the outcomes from such examinations will not have an adverse effect on our operating results and financial condition.

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

Issuer Purchases of Equity Securities (1)

Period	**Total Number of Shares Purchased**	**Average Price Paid per Share**	**Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs**	**Maximum Dollar Value of Share that May Yet Be Purchased Under the Plans or Programs**
October 1, 2006 through October 31, 2006				$ 164,665,553
November 1, 2006 through November 30, 2006	3,112,900	$ 41.39	3,112,900	$ 371,157,965
December 1, 2006 through December 31, 2006	612,500	41.87	612,500	$ 345,510,098

	3,725,400	$ 41.47	3,725,400	$ 345,510,098

(1) In November 2006, our Board of Directors canceled the August 2006 repurchase program and approved a new repurchase program that allows us to purchase up to an aggregate of $500 million in shares of our common stock in the open market or though negotiated transactions.

Item 3. ***Defaults Upon Senior Securities***

Not applicable.

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

Not applicable.

Item 5. ***Other Information***

Not applicable.

Item 6. ***Exhibits***

Exhibit Number	Description
10.1	Transition Agreement dated December 8, 2006, by and between Fair Isaac Corporation and Gresham T. Brebach, Jr.
10.2	Form of Restricted Stock Unit agreement
31.1	Rule 13a-14(a)/15d-14(a) Certifications of CEO.
31.2	Rule 13a-14(a)/15d-14(a) Certifications of CFO.
32.1	Section 1350 Certification of CEO.
32.2	Section 1350 Certification of CFO.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

FAIR ISAAC CORPORATION

DATE: February 7, 2007

By /s/ CHARLES M. OSBORNE
Charles M. Osborne
Interim Chief Executive Officer, Vice President
and Chief Financial Officer
(for Registrant as duly authorized officer
and as Principal Financial Officer)

DATE: February 7, 2007

By /s/ MICHAEL J. PUNG
Michael J. Pung
Vice President, Finance
(Principal Accounting Officer)

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EXHIBIT INDEX
To Fair Isaac Corporation Report On Form 10-Q
For The Quarterly Period Ended December 31, 2006

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