

ELOYALTY CORP
Form S-3
November 08, 2006

Table of Contents

As filed with the Securities and Exchange Commission on November 8, 2006

No. 333-

**SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

**Form S-3
REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

eLoyalty Corporation
(Exact name of registrant as specified in its charter)

Delaware
*(State or other jurisdiction of incorporation or
organization)*

36-4304577
(I.R.S. Employer Identification No.)

**150 Field Drive, Suite 250
Lake Forest, Illinois 60045
(847) 582-7000**
(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Steven H. Shapiro
Vice President, General Counsel and Corporate Secretary
**150 Field Drive, Suite 250
Lake Forest, Illinois 60045
(847) 582-7000**
(Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies of all communications, including communications sent to agent for service, should be sent to:

Bruce F. Perce
Mayer, Brown, Rowe & Maw LLP
**71 South Wacker Drive
Chicago, Illinois 60606
(312) 782-0600**

Approximate date of commencement of proposed sale to the public: From time to time on or after the effective date of this Registration Statement.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box.

CALCULATION OF REGISTRATION FEE

| Title of Each Class of Securities to be Registered(1) | Proposed Maximum Aggregate Offering Price(2) | Amount of Registration Fee(1) |
|---|--|-------------------------------|
| Non-transferable Common Stock Subscription Rights | N/A | \$0(3) |
| Common Stock, par value \$0.01 per share | \$18,000,000(4) | \$1,926 |

- (1) This registration statement relates to (a) non-transferable subscription rights to purchase common stock of the Registrant, which subscription rights are to be issued to holders of the Registrant’s common stock and Series B preferred stock, (b) the shares of common stock deliverable upon the exercise of the non-transferable subscription rights pursuant to the rights offering, and (c) the preferred stock purchase rights associated with such shares of common stock. This registration statement also covers any additional shares of common stock of the Registrant that may become issuable due to adjustments for changes resulting from stock dividends, stock splits, recapitalizations, mergers, reorganizations, combinations or exchanges or other similar events.
- (2) Estimated pursuant to Rule 457(o) solely for purposes of calculating the registration fee.
- (3) The non-transferable subscription rights are being issued without consideration. Pursuant to Rule 457(g), no separate registration fee is payable with respect to the rights being offered hereby since the rights are being registered in the same registration statement as the securities to be offered pursuant thereto.
- (4) Represents the gross proceeds from the assumed exercise of all non-transferable subscription rights to be issued.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to Completion, dated November 8, 2006

PROSPECTUS

**Common Stock
Rights to Purchase up to
Shares of Common Stock**

We are distributing at no charge to holders of our common stock and Series B preferred stock non-transferable subscription rights to purchase shares of our common stock. You will receive _____ of a subscription right for each share of common stock and each share of Series B preferred stock held of record at the close of business on _____, 2006. We will not issue fractional rights and will round all of the subscription rights down to the nearest whole number. We are distributing subscription rights exercisable for up to _____ shares of our common stock.

Each whole subscription right will entitle you to purchase one share of our common stock at a subscription price equal to \$ _____ per share.

The subscription rights will expire if they are not exercised by 5:00 p.m., New York City time, on _____, 2006, unless we extend the offering period. You should carefully consider whether to exercise your subscription rights before the expiration of the rights offering. All exercises of subscription rights are irrevocable. Our board of directors is making no recommendation regarding your exercise of the subscription rights. The subscription rights may not be sold or transferred.

If you exercise all of the rights distributed to you, you will also be entitled to purchase additional shares not purchased by other stockholders pursuant to the over-subscription rights described in this prospectus.

We may cancel or terminate the rights offering at any time prior to its expiration. If we terminate or cancel this offering, we will return your subscription price, but without any payment of interest.

The shares are being offered directly by us without the services of an underwriter or selling agent.

Shares of our common stock are traded on the Nasdaq Global Market under the symbol ELOY. On November 7, 2006, the closing sale price for our common stock was \$19.05 per share. The shares of common stock issued in the rights offering will also be listed on the Nasdaq Global Market under the same symbol.

The exercise of your subscription rights for shares of our common stock involves risks. You should carefully consider the risk factors beginning on page 9 of this prospectus before exercising your subscription rights.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is , 2006

TABLE OF CONTENTS

| | |
|--|----|
| <u>Questions And Answers Relating To The Rights Offering</u> | 1 |
| <u>Prospectus Summary</u> | 5 |
| <u>Risk Factors</u> | 9 |
| <u>Special Note Regarding Forward-Looking Statements</u> | 17 |
| <u>Use Of Proceeds</u> | 19 |
| <u>Price Range Of Common Stock And Dividend Policy</u> | 19 |
| <u>Capitalization</u> | 20 |
| <u>Dilution</u> | 20 |
| <u>The Rights Offering</u> | 21 |
| <u>Description Of Capital Stock</u> | 30 |
| <u>Certain Material U.S. Federal Income Tax Considerations</u> | 41 |
| <u>Plan Of Distribution</u> | 42 |
| <u>Legal Matters</u> | 42 |
| <u>Experts</u> | 42 |
| <u>Incorporation By Reference</u> | 43 |
| <u>Where You Can Find More Information</u> | 43 |
| <u>Consent of PricewatersCoopers LLP</u> | |

You should rely only on the information contained or incorporated by reference in this prospectus. We have not authorized anyone to provide you with additional or different information from that contained or incorporated by reference in this prospectus. The information contained in this prospectus is accurate only as of the date on the front cover of this prospectus and any information we have incorporated by reference is accurate only as of the date of the document incorporated by reference, regardless of the time of delivery of this prospectus or any exercise of the rights.

Table of Contents

QUESTIONS AND ANSWERS RELATING TO THE RIGHTS OFFERING

What is a rights offering?

We are distributing to holders of our common stock and Series B preferred stock as of 5:00 p.m., New York City time, on , 2006, which is the record date for this rights offering, at no charge, non-transferable subscription rights to purchase shares of our common stock. You will receive of a subscription right for each share of common stock and each share of Series B preferred stock you owned at the close of business on the record date. The subscription rights will be evidenced by rights certificates. We will not issue fractional rights and will round all of the subscription rights down to the nearest whole number.

What is a right?

Each whole subscription right will entitle you to purchase one share of our common stock at a subscription price equal to \$ per share. You may exercise any number of whole subscription rights, or you may choose not to exercise any subscription rights.

Why are we conducting the rights offering?

We are making the rights offering in order to raise capital and strengthen our financial position. Our board of directors considered a number of financing alternatives and considered, among other things, the relative costs of the various alternatives, the potential dilution to our current stockholders of various alternatives, the market price of our common stock and general conditions of the securities markets.

Will holders of the Series B preferred stock receive rights?

Yes. The terms of our outstanding Series B preferred stock give the holders of the Series B preferred stock the right to participate in the rights offering on the same basis as the holders of our common stock without having to convert their shares of Series B preferred stock into common stock.

Am I required to exercise the rights I receive in the rights offering?

No. You may exercise any number of your whole rights, or you may choose not to exercise any rights. However, if you choose not to fully exercise your rights, the relative percentage of our common stock that you own will decrease and your voting and other rights will be diluted.

What is the basic subscription privilege?

For each whole right that you own, you will have a basic subscription privilege to buy from us one share of our common stock at the subscription price. You may exercise your basic subscription privilege for some or all of your rights.

What is the over-subscription privilege?

If you exercise all of the basic subscription rights distributed to you, you will also be entitled to purchase additional shares not purchased by other stockholders pursuant to their basic subscription rights at the same subscription price per share that applies to the basic subscription rights.

What are the limitations on the over-subscription rights?

We will be able to satisfy your exercise of the over-subscription rights only if other stockholders do not elect to purchase all of the shares offered under their basic subscription rights. We will honor over-subscription requests in full to the extent sufficient shares are available following the exercise of rights under the basic subscription rights. If over-subscription requests exceed shares available, we will allocate the available shares pro rata based on the number of shares each oversubscribing stockholder purchased under the basic subscription rights. Any excess subscription payments will be returned, without interest, promptly after the completion of the rights offering.

Table of Contents

How soon must I act to exercise my rights?

The rights may be exercised beginning on the date of this prospectus through the expiration date, which is 5:00 p.m., New York City time, on , 2006. If you elect to exercise any rights, the subscription agent must actually receive all required documents and payments from you at or before the expiration date. Although we have the option of extending the expiration date of the subscription period, we currently do not intend to do so.

May I transfer my rights?

No. You may not sell or transfer your rights.

Are we requiring a minimum subscription to complete the rights offering?

No. We may decide to consummate the rights offering even if less than all of the shares we are offering are purchased.

How was the subscription price determined?

The subscription price was established by our board of directors. The subscription price is not necessarily related to our book value, results of operations, cash flows, financial condition, the future market value of our common stock or any other established criteria of value. We cannot assure you that you will be able to sell shares purchased in this offering at a price equal to or greater than the subscription price. We do not intend to change the subscription price in response to changes in the trading price of our common stock prior to the closing of the rights offering.

Have any stockholders indicated they will exercise their rights?

Several of our directors who are also stockholders have individually advised us that they currently intend to participate in the rights offering. In addition, two of our largest stockholders, entities affiliated with TCV IV, L.P. and TCV III (Q), L.P., which we refer to as Technology Crossover Ventures or TCV, and Sutter Hill Ventures, have individually advised us that they currently intend to participate in the rights offering. However, we do not have any formal commitments from any of the foregoing stockholders to participate in the rights offering and we cannot assure you that any of them will exercise all or any part of their basic subscription privilege or their over-subscription privilege.

If Technology Crossover Ventures and Sutter Hill Ventures exercise their basic subscription privileges in full and no other stockholders do so, the percentage of the outstanding common stock owned by Technology Crossover Ventures would increase from % to %, and the percentage of the outstanding common stock owned by Sutter Hill Ventures would increase from % to %. In addition, the percentage of the outstanding voting stock (which includes our Series B preferred stock) owned by Technology Crossover Ventures would increase from % to %, and the percentage of the outstanding voting stock owned by Sutter Hill Ventures would increase from % to %. Their percentage ownership could increase further if they exercised their over-subscription privileges.

Are there any other conditions to the completion of the rights offering?

Yes. The completion of the rights offering is subject to the conditions described under The Rights Offering Conditions, Withdrawal and Termination.

Can the rights offering be canceled?

Yes. We may cancel the rights offering at any time prior to the expiration date and for any reason, in which event all funds received in the rights offering will be returned without interest to those persons who subscribed for shares in the

rights offering.

Table of Contents

How do I exercise my rights?

You must properly complete the enclosed rights certificate and deliver it, along with the full subscription price (including any amounts in respect of your over-subscription privilege), to the subscription agent before 5:00 p.m., New York City time, on , 2006. If you use the mail, we recommend that you use insured, registered mail, return receipt requested. If you cannot deliver your subscription rights certificate to the subscription agent on time, you may follow the guaranteed delivery procedures described under The Rights Offering Guaranteed Delivery Procedure.

If you send a payment that is insufficient to purchase the number of shares you requested, or if the number of shares you requested is not specified in the forms, the payment received will be applied to exercise the subscription privilege to the extent of the payment. If the payment exceeds the subscription price for the full exercise of the subscription privilege, or if you subscribe for more shares than you are eligible to purchase pursuant to the over-subscription privilege, the excess will be returned to you as soon as practicable. You will not receive interest on any payments refunded to you under the rights offering.

If the rights offering is not completed, will my subscription payment be refunded to me?

Yes. The subscription agent will hold all funds it receives in a segregated bank account until completion of the rights offering. If the rights offering is not completed, the subscription agent will return promptly, without interest, all subscription payments.

Must I pay the subscription price in cash?

Yes. You must timely pay the full subscription price for the basic subscription privileges and the over-subscription privileges you wish to exercise by wire transfer, certified or cashier's check drawn on a U.S. bank, U.S. postal money order or personal check that clears before the expiration date of the rights offering.

What if a bank, broker or other nominee is the record holder of my shares?

If you wish to exercise your rights, please promptly contact the bank, broker or other nominee holding your shares. Your bank, broker or other nominee holder is the holder of the shares you own and must exercise the rights on your behalf for shares you wish to purchase. The bank, broker or other nominee has been requested to contact you for instructions on exercising your rights.

After I exercise my rights, can I change my mind?

No. Once you send in your rights certificate and payment, you cannot revoke the exercise of your rights, even if you later learn information about us that you consider to be unfavorable. You should not exercise your rights unless you are certain that you wish to purchase the shares of common stock offered pursuant to this rights offering.

Is exercising my rights risky?

The exercise of your rights involves risks. Exercising your rights means buying shares of our common stock, and should be considered as carefully as you would consider other equity investment. Among other things, you should carefully consider the risks described under the heading Risk Factors.

Has eLoyalty's board of directors made a recommendation regarding the rights offering?

The decision whether to exercise your rights must be made by you based on your evaluation of our business and the terms of the offering. Our board of directors does not make any recommendation to you about whether you should exercise your rights.

Table of Contents

What fees or charges apply if I exercise my rights?

We are not charging any fees or sales commissions to issue rights to you or to issue shares to you if you exercise your rights. If you exercise your rights through a broker or other holder of your shares, you are responsible for paying any fees that person may charge.

When will I receive my new shares of common stock?

If you purchase shares of common stock through the rights offering, we will issue certificates representing those shares to you or DTC on your behalf, as the case may be, as soon as practicable after the completion of the rights offering. Subject to state securities laws and regulations, we have the discretion to delay distribution of any shares you may have elected to purchase by exercise of your rights in order to comply with state securities laws.

Will the rights be listed on a stock exchange or national market?

The rights will not be listed on the Nasdaq Global Market or any other stock exchange or national market. Our common stock trades on the Nasdaq Global Market under the symbol ELOY and the shares to be issued in connection with the rights offering will be eligible for trading on the Nasdaq Global Market.

What are the U.S. federal income tax consequences of exercising my rights?

The receipt and exercise of your rights will not be taxable under U.S. federal income tax laws. You should, however, seek specific tax advice from your personal tax advisor in light of your personal tax situation and as to the applicability and effect of any other tax laws. See Material U.S. Federal Income Tax Consequences.

What happens if I choose not to exercise my rights?

You are not required to exercise your rights or otherwise take any action in response to this rights offering. If you do not exercise your rights and the rights offering is completed, the number of shares of our common stock or Series B preferred stock you own will not change but your percentage ownership of our total outstanding voting stock will decrease. Your percentage ownership of our voting stock may also decrease if you do not exercise your basic subscription privilege in full.

How many shares of common stock will be outstanding after the rights offering?

As of October 31, 2006, there were shares of our common stock and shares of our Series B preferred stock outstanding. We will issue up to shares of common stock in the rights offering, depending on the number of rights that are exercised. Based on the number of shares outstanding as of October 31, 2006, if we issue all shares of common stock available in this rights offering, we would have shares of common stock and shares of Series B preferred stock outstanding.

How much money will eLoyalty receive from the rights offering?

The total proceeds to us from the rights offering will depend on the number of rights that are exercised. If we issue all shares available in the rights offering, the total proceeds to us, before expenses, will be \$18.0 million.

What if I have more questions?

If you have more questions about the rights offering or need additional copies of the rights offering documents, please contact the subscription agent, Mellon Bank, N.A., at .

Table of Contents

PROSPECTUS SUMMARY

*This summary highlights the information contained elsewhere in or incorporated by reference into this prospectus. Because this is only a summary, it does not contain all of the information that you should consider before deciding whether to exercise your rights. For a more complete understanding of this rights offering, the common stock and our company, we encourage you to read this entire prospectus, including the information under the heading *Risk Factors*, and the documents to which we refer you under the heading *Documents Incorporated by Reference*.*

We are a leading management consulting, systems integration, and managed services company focused on optimizing customer interactions. With professionals throughout North America and an additional presence in Europe, we offer a broad range of enterprise customer resource management, or CRM, services and solutions that include creating customer strategies; defining technical architectures; improving sales, service and marketing processes; and selecting, implementing, integrating, supporting and hosting best-of-breed CRM and analytics software applications. We derive revenue from three primary sources: consulting services, managed services and the sale of product, which are frequently sold and delivered together.

We are focused on growing and developing our business through two primary service lines: Behavioral Analytics™ and Converged Internet Protocol Contact Center Solutions. In recent years, we have invested heavily to develop the following differentiated capabilities in these service lines:

Behavioral Analytics™ (BA)

eLoyalty pioneered this solution, which applies human behavioral modeling to analyze and improve customer interactions. Using our BA applications, eLoyalty can help clients:

- automatically measure customer satisfaction and agent performance on every call;
- identify and understand customer personality;
- improve rapport between agent and customer;
- reduce call handle times while improving customer satisfaction;
- identify opportunities to improve self-service applications; and
- improve cross-sell and up-sell success rates.

We have designed a scalable application platform to enable us to rapidly implement BA applications for its clients. The BA solution is delivered as a subscription service, primarily in a remote-hosted model.

Converged Internet Protocol Contact Center (CIPCC) Solutions

Our CIPCC service line focuses on helping clients realize the benefits of transitioning their contact centers to a single network infrastructure from the traditional two-network (voice network and separate data network) model. These benefits include cost savings, remote agent flexibility and application enhancements. eLoyalty has developed a set of tools and methodologies to help clients financially model, plan migration paths, and configure, integrate and support converged Internet Protocol (IP) network solutions within their contact center environments.

We derive revenue from three primary sources: consulting services, managed services and the sale of product, which are frequently sold and delivered together. It is not uncommon for a consulting services engagement surrounding the design and implementation of customer service or marketing solutions to lead to the sale of both product and a long-term maintenance and support or hosting relationship. These services and products are packaged and marketed through a common business development team.

Our consulting services and managed services delivery teams often work together and leverage common tools and methodologies to deliver this spectrum of solutions to our clients. In addition to consulting services revenue driven by our BA and CIPCC engagements, we derive a majority of our revenue from a broad range of CRM consulting work with long-standing accounts, as well as non-service line follow-on consulting relating

Table of Contents

to BA and CIPCC engagements. New managed services revenue is primarily driven by BA and CIPCC engagements. We also generate revenue from the resale of product, which consists of software and hardware primarily sold through our CIPCC service line. The vast majority of this revenue relates to reselling products from Cisco Systems, Inc.

Recent Developments

On November 8, 2006, we issued a press release announcing our results for the third quarter of 2006. We reported total revenue of \$25.9 million and \$66.1 million for the three and nine months ended September 30, 2006, respectively, and net loss per common share of \$0.05 and \$1.45 for the three and nine months ended September 30, 2006, respectively. The following is a summary of revenue by major component:

| | Three Months Ended | | Nine Months Ended | |
|-------------------------|---------------------------|-------------------|--------------------------|-------------------|
| | 09/30/2006 | 10/01/2005 | 09/30/2006 | 10/01/2005 |
| | (000 s) | | | |
| Revenue: | | | | |
| Consulting services | \$ 11,137 | \$ 12,176 | \$ 32,517 | \$ 35,195 |
| Managed services | 8,348 | 4,109 | 19,470 | 14,556 |
| Services revenue | 19,485 | 16,285 | 51,987 | 49,751 |
| Product | 5,165 | 4,092 | 11,002 | 7,814 |
| Reimbursed expenses | 1,266 | 930 | 3,104 | 2,845 |
| Total revenue | \$ 25,916 | \$ 21,307 | \$ 66,093 | \$ 60,410 |

We deferred revenue of \$2.7 million during the third quarter of 2006 related to Behavioral Analytics™ contracts and CIPCC multi-element contracts. We recognized \$2.0 million of previously deferred revenue during the quarter. Of this amount, \$1.2 million reflected a cumulative adjustment for Behavioral Analytics™ subscription and deployment revenue that had been previously deferred until a specific project deliverable had been provided to the client.

As of September 30, 2006, we had deferred revenue of \$7.3 million related to Behavioral Analytics™ contracts and CIPCC multi-element contracts. It is anticipated that \$2.5 million of this deferred revenue will be recognized over the next twelve months.

We earn marketing incentives from Cisco related to sales of certain Cisco products. We recorded \$1.9 million of these incentives as a reduction to cost of product in the third quarter of 2006. Of this amount, \$1.7 million is related to product sales made during the period of February 2006 through July 2006, for which payment is expected to be received in the fourth quarter of 2006. The remaining amount is related to product sales made in August and September of 2006, for which payment is expected in the second quarter of 2007. The future amount of these incentives may fluctuate significantly based on a number of factors, including the volume of product sales and the nature of Cisco's incentive program.

We were incorporated in Delaware in May, 1999. Our executive offices are located at 150 Field Drive, Suite 250, Lake Forest, Illinois 60045 (telephone number 847-582-7000).

Table of Contents

The Rights Offering

| | |
|---------------------------------|---|
| Rights Granted | We have granted to each person who was a record holder of our common stock or Series B preferred stock on the record date of a right for each share of common stock or Series B preferred stock held of record as of the record date. |
| Basic Subscription Privilege | For each whole right that you own, you will have a basic subscription privilege to buy from us one share of our common stock at the subscription price. You may exercise your basic subscription privilege for some or all of your rights, or you may chose not to exercise your rights. |
| Over-Subscription Privilege | <p>If you exercise your basic subscription privilege in full, you will also have an over-subscription privilege to subscribe for any shares that our other rights holders do not purchase under their basic subscription privilege. The subscription price for shares purchased pursuant the over-subscription privilege will be the same as the subscription price for the basic subscription privilege.</p> <p>If holders exercise their over-subscription privileges for more shares than are available to be purchased pursuant to the over-subscription privileges, we will allocate the shares of our common stock to be issued pursuant to the exercise of over-subscription privileges pro rata among those over-subscribing rights holders. Pro rata means in proportion to the number of shares of our common stock that you and the other subscription rights holders have agreed to purchased by exercising your basic subscription privileges. If you are not allocated the full amount of shares for which you oversubscribe, you will receive a refund of the subscription price, without interest, that you delivered for those shares of our common stock that are not allocated to you. The subscription agent will mail such refunds after the completion of the offering.</p> |
| Subscription Price | The subscription price per share of common stock shall be equal to \$. |
| Record Date | , 2006 |
| Expiration Date | The rights will expire at 5:00 p.m., New York City time, on , 2006, unless we extend it. |
| Procedure for Exercising Rights | <p>You must properly complete the enclosed rights certificate and deliver it, along with the full subscription price (including any amounts in respect of your over-subscription privilege), to the subscription agent before 5:00 p.m., New York City time, on , 2006, unless the expiration date is extended.</p> <p>If you use the mail, we recommend that you use insured, registered mail, return receipt requested. If you cannot deliver your subscription rights certificate to the subscription agent on time, you may follow the guaranteed delivery procedures described under The Rights Offering</p> |

Guaranteed Delivery Procedures.

Use of Proceeds

The total proceeds to us from the rights offering will depend on the number of rights that are exercised. If we issue all shares available in the rights offering, the total proceeds to us, before expenses, will be \$18.0 million.

Table of Contents

| | |
|-----------------------------------|---|
| | <p>We intend to use for working capital, capital expenditures and general corporate purposes.</p> |
| Non-Transferability of Rights | <p>The rights may not be sold, transferable or assigned and will not be listed for trading on any securities exchange or the Nasdaq Global Market.</p> |
| No revocation | <p>If you exercise your rights, you may not revoke that exercise.</p> |
| Conditions to the Rights Offering | <p>The completion of the rights offering is subject to the conditions described under The Rights Offering Conditions, Withdrawal and Termination.</p> |
| Amendment; Termination | <p>We may amend the terms of the rights offering or extend the subscription period of the rights offering. We also reserve the right to withdraw the rights offering at any time prior to the expiration date and for any reason, in which event all funds received in the rights offering will be returned without interest to those persons who subscribed for shares in the rights offering.</p> |
| No Board Recommendation | <p>The decision whether to exercise your rights must be made by you based on your evaluation of our business and the terms of the offering. Our board of directors does not make any recommendation to you about whether you should exercise your rights.</p> |
| Issuance of Common Stock | <p>If you purchase shares of common stock through the rights offering, we will issue certificates representing those shares to you or DTC on your behalf, as the case may be, as soon as practicable after the completion of the rights offering.</p> |
| Listing of Common Stock | <p>Our common stock trades on the Nasdaq Global Market under the symbol ELOY and the shares to be issued in connection with the rights offering will be eligible for trading on the Nasdaq Global Market.</p> |
| Federal Income Tax Consequences | <p>The receipt and exercise of your rights will not be taxable under U.S. federal income tax laws. You should, however, seek specific tax advice from your personal tax advisor in light of your personal tax situation and as to the applicability and effect of any other tax laws. See Material U.S. Federal Income Tax Consequences.</p> |
| Subscription Agent | <p>Mellon Bank, N.A.</p> |

Table of Contents

RISK FACTORS

An investment in our common stock involves a high degree of risk. You should carefully consider the risks described below, together with the other information contained or incorporated by reference in this prospectus, before making a decision to invest in our common stock. The risks described below are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also materially and adversely affect our business operations. If any of the following risks actually occurs, our business, results of operations and financial condition could suffer. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment.

Risks Related to Our Business

We depend on a limited number of clients for a significant portion of our revenue, and the loss of a significant customer or a substantial decline in the number or scope of projects we do for a significant customer would have a material adverse effect on our business.

While our overall levels of client concentration have declined in recent periods, we derive and expect to continue to derive for the foreseeable future a significant portion of our revenue from a limited number of clients. For example, our top customer accounted for % of our revenue in the nine months ended September 30, 2006, 13% of our revenue in fiscal year 2005, 14% of our revenue in fiscal year 2004 and 24% of our revenue for our top customer in fiscal year 2003. Our top 5 and top 10 customers accounted for % and % of revenue, respectively, for the nine months ended September 30, 2006, 37% and 56% of revenue, respectively, in fiscal year 2005, 52% and 66% of revenue, respectively in fiscal year 2004 and 57% and 73% of revenue, respectively, in fiscal year 2003. The volume of services that we provide for a specific client is likely to vary from year to year, and a major client in one year might not use our services in a subsequent year. To the extent that any significant client uses less of our services or terminates its relationship with us, as may occur as clients respond to conditions affecting their own business, our revenue could decline substantially, which could seriously harm our business.

We depend on good relations with our major clients and any harm to these good relations may materially and adversely harm our business or our ability to compete effectively.

To attract and retain clients, we depend to a large extent on our relationships with our customers and our reputation for high quality consulting services and managed services. We design, create, implement, host, maintain and support applications and solutions that are often critical to our clients' businesses. While we believe that we generally enjoy good relations with our clients, if a client is not satisfied with our services, products or solutions, including those of subcontractors we employ, it may be damaging to our reputation and business. Any defects or errors in our services or solutions or failure to meet our clients' expectations could result in:

delayed or lost revenue due to adverse client reaction;

requirements to provide additional services to a client at a reduced or no charge;

negative publicity, which could damage our reputation and adversely affect our ability to attract or retain clients; and

claims for damages against us, regardless of our responsibility for such failure.

If we fail to meet our contractual obligations with our clients, we could be subject to legal liabilities or loss of clients. Although our contracts typically include provisions to limit our exposure to legal claims for the services and solutions we provide and the applications and systems we develop or integrate, these provisions may not protect us in all cases.

Table of Contents

If we do not effectively manage the risks associated with increasingly complex client projects and new services offerings, our profit margins and our financial results may suffer.

We may fail to accurately estimate the time and resources necessary for the performance of our services. It can be difficult to judge the time and resources necessary to complete consulting projects, to deploy, support and operate hosted solutions, or to support and maintain complex contact center architectures. A number of different risks must be accounted for, including, without limitation, the variability and predictability of the number, size, scope, cost and duration of, and revenue from, client engagements, unanticipated cancellations or deferrals of client contracts or follow-on phases of engagements in process, collection of revenue, variable employee utilization rates, project personnel costs and engagement requirements. Accurate estimates as to the costs and timing of completion of engagements is particularly important for the limited number that are performed on a fixed-price or not-to-exceed basis. Our failure to accurately estimate these risks could reduce the profitability of, or result in a loss on, our engagements and could damage our client relationships and our reputation.

Our ability to retain our existing professionals, and our ability to recruit additional talented professionals, are critical to the success of our business.

We believe that our success will depend substantially on our ability to attract, train, motivate and retain highly skilled management, strategic, technical, product development and other key professional employees. The information technology services industry continues to be people-intensive and faces a shortage of qualified personnel, especially those with specialized skills or experience. We compete with other companies to recruit and hire from this limited pool. If we cannot hire and retain qualified personnel, or if a significant number of our current employees leave, we may be unable to complete or retain existing engagements or bid for new engagements of similar scope and revenue.

If one or more of our key personnel were unable or unwilling to continue in their present positions, they could be difficult to replace and our business could be seriously harmed. This would result not only in the loss of key employees, but also potentially in the loss of client relationships or new business opportunities. In addition, there is no guarantee that the employee and customer non-solicitation and non-competition agreements we have entered into with our senior professionals would deter them from departing us for our competitors or that such agreements would be upheld and enforced by a court or other arbiter across all jurisdictions where we engage in business.

We rely heavily on our senior management team for the success of our business.

We rely heavily on our senior management team to manage our practices. Given the highly specialized nature of our services, these people must have a thorough understanding of our service offerings as well as the skills and experience necessary to manage the organization. If one or more members of our senior management team leave and we cannot replace them with a suitable candidate quickly, we could experience difficulty in managing our business properly, and this could harm our business prospects, client relationships, employee morale and results of operations.

Our industry is very competitive and, if we fail to compete successfully, our market share and business will be adversely affected.

We operate in a highly competitive and rapidly changing market and compete with a variety of organizations that offer services similar to those we offer. The market includes a variety of participants that compete with us at various levels of our business, including strategic consulting firms, systems integrators, general information technology services providers, web consulting firms, application service providers, and other firms that provide both consulting and systems integration services and solutions. New market entrants also pose a threat to our business.

Many of our competitors have longer operating histories, more clients, and longer relationships with their clients, greater brand or name recognition and significantly greater financial, technical, marketing and public relations resources than we do. As a result, our competitors may have enhanced abilities to compete for

Table of Contents

specific clients and market share generally, including through substantial economic incentives to clients to secure contracts. Existing or future competitors may develop or offer solutions that are comparable or superior to ours at a lower price. In addition, our competitors may be in a better position to respond quickly to new or emerging technologies and changes in client requirements or expectations. They may also develop and promote their products and services more effectively than we do and be better able to compete for skilled professionals by offering substantial compensation incentives.

We must keep pace with the rapid rate of technological innovation and change, as well as evolving industry standards, in order to build our business.

Our industry is characterized by rapid and continually changing technologies, the introduction of many new products and services and evolving industry standards and client preferences. Our solutions must meet the requirements of and achieve significant acceptance among our current and prospective clients within this environment. Our future business will depend on our continuing ability to adapt to and incorporate changing technologies and emerging industry standards and to remain knowledgeable with respect to emerging CRM technology, customer loyalty research and applied CRM solutions.

In addition, our future business depends upon continued growth in the acceptance and use of CRM methodologies and technologies by our current and prospective clients and their customers and suppliers. Their acceptance and usage in turn may depend upon factors such as:

- the actual or perceived benefits of adoption and implementation of CRM methodologies and technologies, including the predictability of a meaningful return on investment, cost efficiencies or other measurable economic benefits;

- their actual or perceived ease of use and access to such new technologies and methodologies; and

- their willingness to adopt new business methods incorporating a customer-centric approach.

We cannot assure you that we will be successful in anticipating or responding to these developments and challenges on a timely or competitive basis or at all, or that our ideas and solutions will be successful in the marketplace. In addition, new or disruptive technologies and methodologies by our competitors may make our service or solution offerings uncompetitive. Any of these circumstances could adversely affect our ability to obtain and successfully complete substantial new client engagements that are important to maintain and grow our business. The recent