TALK AMERICA HOLDINGS INC
Form 10-K/A
March 28, 2005

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

FORM 10-K/A
(AMENDMENT NO. 2)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2003
Commission File No. 000-26728

TALK AMERICA HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**23-2827736** (I.R.S. Employer Identification Number)
12020 Sunrise Valley Drive, Suite 250 **Reston, Virginia** (Address of principal executive offices)	**20191** (zip code)

(703) 391-7500
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
None	Not applicable

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, Par Value $.01 Per Share
Rights to Purchase Series A Junior Participating Preferred Stock
(Title of class)

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 [X] No [ ]

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).
Yes [X] No [ ]

As of June 30, 2003, the aggregate market value of the voting stock held by non-affiliates of the registrant, based on the average of the high and low prices of the common stock on June 30, 2003 of $10.79 per share as reported on the Nasdaq National Market, was approximately $280,519,337.15 (calculated by excluding solely for purposes of this form outstanding shares owned by directors and executive officers).

As of March 9, 2004, the registrant had issued and outstanding 26,670,050 shares of common stock, par value $.01 per share.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2004 Annual Meeting of Stockholders.	Part III

Explanatory Note

Talk America Holdings, Inc. is filing this Amendment No. 2 on Form 10-K/A ("Amendment No. 2") to our Annual Report on Form 10-K originally filed with the Securities and Exchange Commission on March 12, 2004, as previously amended by Amendment No. 1 on Form 10-K/A filed with the Securities and Exchange Commission on May 7, 2004 (as so amended, the "Original 10-K"), for the purpose of restating our consolidated financial statements (as previously restated) for the year ended December 31, 2003 (including the quarters thereof) to reflect corrections of the following errors:

Item #:

1. Revenue for each of the four quarters of 2003 and the year ended December 31, 2003 was increased to recognize certain customer fees previously recorded in sales, use and excise tax liabilities, with corresponding increases in operating income, net income, net income per share-basic and net income per share-diluted, along with corresponding reductions of sales, use and excise tax liabilities;

2. The number of diluted weighted average common and common equivalent shares outstanding for each of the third and fourth quarters 2003 and year ended December 31, 2003 was decreased to reflect the inclusion of assumed tax benefits in the proceeds used to repurchase shares in the application of the treasury stock method of accounting for outstanding options, with a corresponding increase in diluted net income per share for each of these periods;

3. Income tax expense for each of the third and fourth quarters 2003 and year ended December 31, 2003 was reduced to reflect additional deferred tax assets relating to net operating loss carryforwards due to (a) a correction in the calculation of net operating losses utilized in 2003 to reflect the deductibility of state income taxes and (b) a correction to the calculation of state deferred tax assets, with corresponding increases in net income, net income per share-basic and net income per share-diluted for each of these periods; and

4. Deferred tax assets were increased by $6.5 million and goodwill was decreased by a corresponding amount beginning in the third quarter 2003 and for the year ended December 31, 2003 to record the deferred tax asset associated with acquired net operating loss carryforwards.

The effect of these items is reflected in our consolidated financial statements contained in Item 8 of this Amendment No. 2, with corresponding changes reflected in Item 6, Selected Consolidated Financial Data, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations and Item 9A, Controls and Procedures. The effect of these items on our consolidated statement of operations for the year ended December 31, 2003 is summarized in the following table. Each of the adjustments shown in the table includes a bracketed reference, by the item numbers set forth above, to the financial item or items described above giving rise to such adjustment.

(in 000s, except per share data)				2003						
		Q1 (Unaudited)		Q2 (Unaudited)		Q3 (Unaudited)		Q4 (Unaudited)		Year
Revenues:										
Reported	$	87,843	$	93,748	$	99,929	$	101,143	$	382,663
Adjustments [1]		359		158		249		264		1,030
As Restated	$	88,202	$	93,906	$	100,178	$	101,407	$	383,693
Operating Income:										
Reported	$	15,179	$	19,027	$	17,620	$	13,432	$	65,258
Adjustments [1]		359		158		249		264		1,030
As Restated	$	15,538	$	19,185	$	17,869	$	13,696	$	66,288
Pre-Tax Income:										
Reported	$	14,961	$	17,500	$	16,106	$	12,197	$	60,763
Adjustments [1]		359		158		249		264		1,030
As Restated	$	15,320	$	17,658	$	16,355	$	12,461	$	61,793
Income Tax Expense (Benefit):										
Reported	$	5,835	$	6,825	$	(35,460)	$	5,103	$	(17,697)
Adjustments [1] [3]		141		62		(2,287)		(243)		(2,327)
As Restated	$	5,976	$	6,887	$	(37,747)	$	4,860	$	(20,024)
Net Income:										
Reported	$	9,126	$	10,675	$	51,566	$	7,094	$	78,461
Adjustments [1] [3]		217		96		2,536		507		3,356
As Restated	$	9,343	$	10,771	$	54,102	$	7,601	$	81,817
Basic EPS:										
Reported	$	0.35	$	0.41	$	1.96	$	0.27	$	2.99
Adjustments [1] [2] [3]		--		--		0.09		0.02		0.11
As Restated	$	0.35	$	0.41	$	2.05	$	0.29	$	3.10
Fully Diluted EPS:										
Reported	$	0.32	$	0.37	$	1.74	$	0.25	$	2.75
Adjustments [1] [2] [3]		--		--		0.14		0.02		0.19
As Restated	$	0.32	$	0.37	$	1.88	$	0.27	$	2.94
Fully Diluted Shares:										
Reported		29,940		29,563		29,761		28,884		28,514
Adjustments [2]		--		--		(884)		(777)		(708)
As Restated		29,940		29,563		28,877		28,107		27,806

Unless otherwise expressly stated (including the restatement reflected in the Amendment No. 1 on Form 10-K/A filed with the Securities and Exchange Commission on May 7, 2004), this Amendment No. 2 does not reflect events occurring after the filing on March 12, 2004 of our Annual Report on Form 10-K for the year ended December 31, 2003, nor does it modify or update in any way disclosures contained in the Original 10-K other than to reflect the restatement discussed above.

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ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The selected consolidated financial data should be read in conjunction with, and are qualified in their entirety by, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our Consolidated Financial Statements included elsewhere in this Form 10-K.

	Year Ended December 31,				
	2003 (Restated)(1)	2002	2001	2000	1999
	(In Thousands, Except For Per Share Amounts)				
Consolidated Statements of Operations Data:					
Revenue	$ 383,693	$ 317,507	$ 488,158	$ 525,712	$ 516,548
Costs and expenses:					
Network and line costs	181,682	155,567	235,153	292,931	289,029
General and administrative expenses	57,503	53,510	82,202	65,360	39,954
Provision for doubtful accounts	11,599	9,365	92,778	53,772	28,250
Sales and marketing expenses	48,277	27,148	73,973	152,028	96,264
Depreciation and amortization	18,344	17,318	34,390	19,257	6,214
Impairment and restructuring charges	--	--	170,571	--	--
Significant other charges (income)	--	--	--	--	(2,718)
Total costs and expenses	317,405	262,908	689,067	583,348	456,993
Operating income (loss)	66,288	54,599	(200,909)	(57,636)	59,555
Other income (expense):					
Interest income	388	802	1,220	4,859	3,875
Interest expense	(7,353)	(9,087)	(6,091)	(5,297)	(4,616)
Other income (expense), net	2,470	28,448	17,950	(3,822)	20,115
Income (loss) before provision for income taxes	61,793	74,762	(187,830)	(61,896)	78,929
Provision (benefit) for income taxes	(20,024)	(22,300)	--	--	--
Income (loss) before cumulative effect of an accounting change	81,817	97,062	(187,830)	(61,896)	78,929
Cumulative effect of an accounting change	--	--	(36,837)	--	--
Net income (loss)	$ 81,817	$ 97,062	$ (224,667)	$ (61,896)	$ 78,929
Income (loss) per share - Basic:					
Income (loss) before cumulative effect of an accounting change per share	$ 3.10	$ 3.56	$ (7.11)	$ (2.63)	$ 3.87
Cumulative effect of an accounting change per share	--	--	(1.40)	--	--
Net income (loss) per share	$ 3.10	$ 3.56	$ (8.51)	$ (2.63)	$ 3.87
Weighted average common shares outstanding	26,376	27,253	26,414	23,509	20,395

Income (loss) per share - Diluted:					
Income (loss) before cumulative effect of an accounting change per share	$ 2.94	$ 3.15	$ (7.11)	$ (2.63)	$ 3.68
Cumulative effect of an accounting change per share	--	--	(1.40)	--	--
Net income (loss) per share	$ 2.94	$ 3.15	$ (8.51)	$ (2.63)	$ 3.68
Weighted average common and common equivalent shares outstanding	27,806	30,798	26,414	23,509	21,471

	At December 31,				
	2003 (Restated) (1)	**2002**	**2001**	**2000**	**1999**
			(In Thousands)		
Consolidated Balance Sheet Data:					
Cash and cash equivalents	$ 35,242	$ 33,588	$ 22,100	$ 40,604	$ 78,937
Total current assets	105,595	82,825	51,214	97,203	150,893
Goodwill and intangibles, net	17,769	26,882	29,672	218,639	1,068
Total assets	247,178	189,075	165,737	407,749	215,008
Current portion of long-term debt	16,806	61	14,454	2,822	--
Total current liabilities	93,235	64,754	87,789	100,271	71,168
Contingent obligations	--	--	--	114,630	114,630
Long-term debt	31,791	100,855	152,370	103,695	84,985
Stockholders' equity (deficit)	103,143	23,466	(74,422)	82,700	(69,375)

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(1) The Selected Consolidated Financial Data for 2003 (as previously restated on May 7, 2004) has been restated for matters related to (a) the recognition in revenue in the four quarters of 2003 and year ended December 31, 2003 of certain customer fees previously recorded in those periods as increases in sales, use and excise tax liabilities; (b) the calculation of outstanding diluted weighted average common and common equivalent shares in the third and fourth quarters 2003 and the year ended December 31, 2003 to reflect the inclusion of tax benefits in the proceeds used to repurchase shares in the application of the treasury method of accounting for outstanding options; (c) for the third and fourth quarters 2003 and the year ended December 31, 2003, a correction in the calculation of net operating losses utilized in 2003 and in the calculation of state deferred tax assets; and (d) the recording, beginning in the third quarter 2003 and for the year ended December 31, 2003, of a deferred tax asset associated with acquired net operating loss carryforwards. See Note 16 to the Consolidated Financial Statements.

See “Management’s Discussion and Analysis of Financial Condition and Results of Operations” for a discussion of items affecting the results of 2001, 2002 and 2003.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Restatements of Previously Issued Consolidated Financial Statements

Amendment No. 1

As discussed in Note 16 to our Consolidated Financial Statements, we revised our previously issued consolidated sheet as of December 31, 2003 and related disclosures in Note 5 to reflect the change in classification of $15 million of our 12% Senior Subordinated Notes from long-term debt to current portion of long-term debt. Refer to Note 16 to our Consolidated Financial Statements for further information regarding this restatement.

Amendment No. 2

As discussed in Note 16 to our Consolidated Financial Statements, we further restated our previously issued Consolidated Financial Statements for the year ended December 31, 2003 and the four quarters of 2003 for matters related to: (a) the recognition in revenue in the four quarters 2003 and year ended December 31, 2003 of certain customer fees previously recorded in those periods as increases in sales, use and excise tax liabilities; (b) the calculation of outstanding diluted weighted average common and common equivalent shares in the third and fourth quarters of 2003 and the year ended December 31, 2003 to reflect the inclusion of assumed tax benefits in the proceeds used to repurchase shares in the application of the treasury stock method of accounting for outstanding options; (c) a correction in the calculation of net operating losses utilized in 2003 and in the calculation of state deferred tax assets for the third and fourth quarters 2003 and the year ended December 31, 2003; and (d) the recording, beginning in the third quarter of 2003 and for the year ended December 31, 2003, of a deferred tax asset associated with acquired net operating loss carryforwards. Refer to Notes 15 and 16 to the Consolidated Financial Statements for further information regarding this restatement, including the effect of the restatement for each of the four quarters 2003 and the year ended December 31, 2003.

The information in the following discussion reflects these restatements, but is not otherwise updated.

The following discussion should be read in conjunction with the Consolidated Financial Statements included elsewhere in this Form 10-K.

Cautionary Note Concerning Forward-Looking Statements

Certain of the statements contained in this Form 10-K Report may be considered “forward-looking statements” for purposes of the securities laws. From time to time, oral or written forward-looking statements may also be included in other materials released to the public. These forward-looking statements are intended to provide our management’s current expectations or plans for our future operating and financial performance, based on our current expectations and assumptions currently believed to be valid. For these statements, we claim protection of the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995. These forward-looking statements can be identified by the use of forward-looking words or phrases, including, but not limited to, “believes,” "estimates," "expects," "expected," "anticipates," "anticipated," “plans,” “strategy,” “target,” “prospects” and other words of similar meaning in connection with a discussion of future operating or financial performance. Although we believe that the expectations reflected in such forward-looking statements are reasonable, there can be no assurance that such expectations will prove to have been correct.

All forward-looking statements involve risks and uncertainties that may cause our actual results to differ materially from those expressed or implied in the forward-looking statements. This Form 10-K Report includes important information as to risk factors in the “Business” section under the headings “Business Operations,” “Competition” and “Regulation” and in “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” In addition to those factors discussed in this Form 10-K Report, you should see our other reports on Forms 10-K, 10-Q and 8-K filed with the Securities and Exchange Commission from time to time for information identifying factors that may cause actual results to differ materially from those expressed or implied in the forward-looking statements.

OVERVIEW

Talk America Holdings, Inc., through its subsidiaries, offers a bundle of local and long distance phone services to residential and small business customers in the United States. Our business strategy is to build a large, profitable base of bundled phone service customers using the wholesale operating platforms of the incumbent local exchange companies and then to migrate customers to our own networking platform and further increase our revenues and profitability by offering new products and services to these customers. We refer to this strategy as our “customer first” strategy.

In 2000, we decided to expand beyond our historical long distance service offerings and utilize the unbundled network element platform to enter the large local telecommunications market and diversify our product portfolio through the bundling of local service with our core long distance service offerings. We encountered a number of operational and business difficulties during the rollout of our bundled service offering in 2000 and worked to address the operational issues that we encountered. We focused on improving the overall efficiency of the bundled business model in 2001. During 2002, our top operating priorities were to lower bad debt expense, reduce customer turnover, or “churn,” and lower our customer acquisition costs. During 2003, our primary focus was increasing sales of our bundled services within the targets established by management for acquisition costs, customer turnover and bad debt expense. We ended 2003 with 557,000 billed bundled lines. We expect our existing base of long distance customers to continue to decline in 2004 through attrition due to our decision to focus our marketing efforts on the sale of our bundled product.

An integral element of our business strategy is our development of our own local networking capacity. This development, if successful, will enhance our operating flexibility and provide us with an alternative to the wholesale operating platforms of the incumbent local exchange companies. As the first step in enabling us to implement this stage of our business strategy, during 2003, we deployed networking assets in Michigan and have begun to carry test calls over our own switching platform. We are in the process of automating the business processes required to provide local network-based services and to support the proposed deployment of our own local network. Our objective is to develop a viable networking opportunity as an alternative to the wholesale operating platforms of the incumbent local exchange companies to provide us with operating flexibility. In addition, we will add new services and enhance our existing service and product offerings, as available, to increase our revenues and profitability from our customers.

RESULTS OF OPERATIONS

The following table sets forth for the periods indicated certain of our financial data as a percentage of revenue:

	Year Ended December 31,		
	2003 (Restated)	**2002**	**2001**
Revenue	100.0%	100.0%	100.0%
Costs and expenses:			
Network and line costs	47.5	49.0	48.2
General and administrative expenses	15.0	16.8	16.8

Provision for doubtful accounts	3.0	2.9	19.0
Sales and marketing expenses	12.6	8.6	15.2
Depreciation and amortization	4.8	5.5	7.0
Impairment and restructuring charges	--	--	34.9
Total costs and expenses	82.9	82.8	141.2
Operating income	17.1	17.2	(41.2)
Other income (expense):			
Interest income	0.1	0.3	0.3
Interest expense	(1.9)	(2.9)	(1.2)
Other, net	0.6	9.0	3.6
Income (loss) before income taxes	15.9	23.6	(38.5)
Provision (benefit) for income taxes	(5.2)	(7.0)	--
Income (loss) before cumulative effect of an accounting change	21.3	30.6	(38.5)
Cumulative effect of an accounting change	--	--	(7.5)
Net income (loss)	21.3%	30.6%	(46.0)%

The following table sets forth for certain items of our financial data for each year the percentage increase or (decrease) in such item from the preceding fiscal year:

	Year Ended December 31,	
	2003 (Restated)	**2002**
Revenue	20.8%	(35.0)%
Costs and expenses:		
Network and line costs	16.8	(33.8)
General and administrative expenses	7.5	(34.9)
Provision for doubtful accounts	23.9	(89.9)
Sales and marketing expenses	77.8	(63.3)
Depreciation and amortization	5.9	(49.6)
Impairment and restructuring charges	--	(100.0)
Total costs and expenses	(20.7)	(61.8)
Operating income	21.4	127.2
Other income (expense):		
Interest income	(51.6)	(34.3)
Interest expense	(19.1)	49.2
Other, net	(91.3)	58.5
Income before income taxes	(17.3)	139.8
Benefit for income taxes	(10.2)	--
Income before cumulative effect of an accounting change	(15.7)	151.7
Cumulative effect of an accounting change	--	(100.0)
Net income (loss)	(15.7)%	143.2%

Revenue. The increase in revenue in 2003 from 2002 was due to the increase in bundled revenue offset by a decline in long distance revenue. In 2002 both long distance and bundled revenue decreased. In 2000, we decided to shift our focus to the bundled product and no longer actively market the long distance product. During 2003 and 2004, we increased certain fees and rates related to our long distance and bundled products and such changes in rates may adversely impact customer turnover.

The increase in bundled revenue to $282.3 million in 2003 from $171.2 million in 2002 was due to higher average bundled lines in 2003 as compared to 2002, partially offset by lower average monthly revenue per customer. We

ended 2003 with 557,000 billed bundled lines. Approximately 58.6% of the bundled lines in December 2003 were in Michigan. While we have expanded our marketing efforts in additional states during 2003, including Georgia, Illinois, New York, New Jersey, Indiana, Wisconsin, Ohio and Maryland, continued growth in revenues will depend upon our ability to develop and scale various marketing programs in additional states or areas and to maintain or reduce the current level of customer turnover.

The decrease in bundled revenue to $171.2 million in 2002 from $196.5 million in 2001 was due to lower average revenue per bundled line in 2002 as compared to 2001. Such decrease resulted from our strategy to market lower priced products to be more competitive with incumbent and other competitive local exchange carriers. We ended 2002 with 333,000 billed bundled lines compared with approximately 179,000 billed bundled lines in 2001. Approximately 61.1% of the bundled lines in December 2002 were in Michigan.

Our long distance revenue decreased in 2003 to $101.4 million from $146.3 million in 2002, and from $291.7 million in 2001. Our decision in 2000 to invest in building a bundled customer base, together with customer turnover, contributed to the decline in long distance customers and revenue, although the effect on revenue of the decline in customers was offset partially by an increase in average monthly revenue per customer due to price increases. We expect this decline in long distance customers and revenues to continue. Long distance revenues for 2002 and 2001 included non-cash amortization of deferred revenue of $6.2 million and $7.4 million, respectively, related to a telecommunications service agreement entered into in 1997. Deferred revenue relating to this agreement had been amortized over a five-year period. The agreement and related amortization terminated in October 2002.

Network and Line Costs. The increase of network and line costs in 2003 from 2002 is primarily due to the increase in bundled customers, partially offset by the decrease in long distance customers. The lower total network and line costs as a percentage of revenue were due primarily to lower network costs as a percentage of revenue for both the bundled and long distance products. This decrease was partially offset by a shift in our customer base to the higher cost bundled product from the lower cost long distance product.

Bundled network and line costs were $141.9 million for 2003, as compared to $96.1 million for 2002 and $107.7 million for 2001. Long distance network and line costs were $39.8 million for 2003, as compared to $59.5 million for 2002 and $127.5 million for 2001. As a percentage of bundled revenue, bundled and network line costs were 50.4% for 2003, as compared to 56.1% for 2002 and 54.8% for 2001. Long distance network and line costs as a percentage of long distance revenue were 39.2% for 2003, as compared to 40.6% for 2002 and 43.7% for 2001.

The decrease of network and line costs in 2002 from 2001 was primarily due to the decrease in long distance customers and a reduction in access and usage rates. Network and line costs for 2002 benefited from a credit of $1.7 million in connection with a New York Public Service Commission mandated refund from Verizon New York of certain unbundled network element platform switching costs. The growth in 2002 of local bundled service as a percentage of total revenue from 2001 and product mix has contributed to the increase in overall network and line cost as a percentage of revenues.

We structure and price our products in order to maintain network and line costs as a percentage of revenue at certain targeted levels. While the control of the structure and pricing of our products assists us in mitigating risks of increases in network and line costs, the telecommunications industry is highly competitive and there can be no assurances that we will be able to effectively market these higher priced products. There are several factors that could cause our network and line costs as a percentage of revenue to increase in the future, including without limitation:

· determinations by the FCC, courts, or state commission(s) that make unbundled local switching and/or combinations of unbundled network elements effectively unavailable to us in some or all of our geographic service areas, requiring us to provide services in these areas through total service resale agreements with incumbent local exchange companies, through network elements purchased from the Regional Bell Operating Companies at "just and reasonable" rates under Section 271 of the Act or through the switching facilities of other non-incumbent carriers, in any case at significantly increased costs, or to provide services over our own switching facilities, if they have been deployed. The Court of Appeals, on March 2, 2004, issued an order that reversed the FCC's Triennial Review Order in part and remanded to the FCC with instructions to revise the Order in material ways that may make unbundled local switching and/or combinations of unbundled network elements effectively unavailable to us in some or all of our geographic service areas (see Item 1, "Regulation," above and "Liquidity and Capital Resources, Other Matters," below);

· adverse changes to the current pricing methodology mandated by the FCC for use in establishing the prices charged to us by incumbent local telephone companies for the use of their unbundled network elements. The FCC's 2003 Triennial Review Order, which was reversed in part and remanded to the FCC with instructions to revise the Order in material ways, (see Item 1, "Regulation," above and "Liquidity and Capital Resources, Other Matters," below)

clarified several aspects of these pricing principles related to depreciation, fill factors (i.e. network utilization) and cost of capital, which could enable incumbent local telephone companies to increase the prices for unbundled network elements. In addition, the FCC released a Notice of Proposed Rulemaking on December 15, 2003, which initiated a proceeding to consider making additional changes to its unbundled network element pricing methodology, including reforms that would base prices more on the actual network costs incurred by incumbent local exchange companies than on the hypothetical network costs that would be incurred when the most efficient technology is used. These changes could result in material increases in prices charged to us for unbundled network elements; and

· determinations by state commissions to increase prices for unbundled network elements in ongoing state cost dockets.

Changes in the pricing of our service plans could also cause network and line costs as a percentage of revenue to change in the future. See our discussion under "Liquidity and Capital Resources, Other Matters," below.

General and Administrative Expenses. General and administrative expenses increased in 2003 from 2002. In 2002, general and administrative expenses were reduced by a settlement of litigation relating to an obligation with a third party of $1.7 million. The increase was also due to an increase in the number of employees for customer service and information technology to support our expanding base of bundled customers. As of December 31, 2003, we had 270 and 53 employees within customer service and information technology, respectively, as compared to 225 and 43 as of December 31, 2002. The decrease in general and administrative expenses in 2002 from 2001 was due primarily to significant reductions in workforce and other cost cutting efforts by us as we pursued improvements in operating efficiencies of our bundled business model and the litigation settlement.

While we expect general and administrative expense as a percentage of revenue to continue to decline as the customer base grows, realization of such efficiencies will be dependent on the ability of management to continue to control personnel costs in areas such as customer service and collections. There can be no assurances that we will be able to realize these efficiencies.

Provision for Doubtful Accounts. The provision for doubtful accounts increased in 2003 from 2002. In 2002, the provision for doubtful accounts was reduced by a reversal of the reserve for doubtful accounts of $1.9 million due to better than expected collections experience on accounts receivable outstanding at year end 2001. The benefits of our actions taken during the third and fourth quarters of 2001 to reduce bad debt expense and improve the overall credit quality of our customer base were reflected in the lower bad debt expense for 2002. In general, bad debt expense as a percentage of revenue of our long distance customers is lower than that of our bundled customers because of the relatively greater maturity of the long distance customer base, however, the impact of this lower bad debt expense is decreasing as our base of long distance customers continues to decline.

Sales and Marketing Expenses. The increase in sales and marketing expenses in 2003 from 2002 is primarily attributable to increased levels of sales and marketing activity to continue our bundled sales growth. The decrease in sales and marketing costs in 2002 from 2001 was primarily attributable to the reduction in marketing fees paid to AOL due to the termination of the marketing relationship with AOL effective September 30, 2001. Currently, substantially all of our sales and marketing expenses relate to the bundled product. Included in sales and marketing expenses are advertising expenses of $6.8 million for 2003, $1.5 million for 2002, and $0.2 million for 2001. We expect sales and marketing expenses to increase in 2004 as we continue to target growth in the bundled product and invest in the development of our marketing programs.

Impairment and Restructuring Charges. Included in impairment and restructuring charges for 2001 was an impairment charge of $168.7 million primarily related to the write-down of goodwill associated with the August 2000 acquisition of Access One Communications Corp. In September 2001, we approved a plan to close one of our call center operations. We incurred expenses of $1.9 million during 2001 to reflect the elimination of approximately 225 positions and lease exit costs in connection with the call center closure. There were no impairment or restructuring charges in 2002.

Interest Expense. The decrease in interest expense in 2003 from 2002 is primarily due to lower outstanding debt balances. As a result of the restructuring agreement with AOL on December 23, 2002, we recorded interest expense associated with the 8% Secured Convertible Notes on our consolidated statement of operations for 2003, partially offsetting the decrease due to lower outstanding debt. The increase in interest expense in 2002 from 2001 was primarily due to the higher yielding debt instruments delivered in the exchange of our 4-1/2% and 5% Convertible Subordinated Notes for 8% Convertible Senior Subordinated Notes and 12% Senior Subordinated Notes and the restructuring of our senior credit facility. The issuance in 2001 of the 8% Secured Convertible Notes was initially accounted for as a troubled debt restructuring. As such, the aggregate interest expense for these notes was recorded as

a liability at such time and the subsequent interest expense associated with these notes of $2.7 million and $0.8 million for 2002 and 2001, respectively, were not reflected in the statement of operations.

Depreciation and Amortization. Amortization expense decreased significantly in 2002 from 2001 due to the write-down in 2001 of goodwill associated with the acquisition of Access One. Additionally, we adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," which established the impairment approach rather than amortization for goodwill, resulting in reduced amortization as a result of the elimination of goodwill amortization in 2002.

Other Income, Net. Other income for 2003 consists of gains from our repurchase of a portion of our 12% Senior Subordinated Notes at a discount to par. Other income in 2002 included $28.9 million attributed to the restructuring and repurchase of a portion of our 8% Secured Convertible Notes and $1.6 million attributed to the repurchase of a portion of our 12% Senior Subordinated Notes, partially offset by a loss of $1.1 million related to the retirement of our senior credit facility.

Other income for 2001 of $20.6 million include a $16.9 million gain on the restructuring of the AOL contingent redemptions in accordance with SFAS No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructurings." In addition, we reacquired $5.0 million of our 4-1/2% Convertible Subordinated Notes due 2002 at a $3.8 million discount from the face amount. The amount for 2001 also consisted of a $2.4 million unrealized loss on the increase in fair value of the AOL contingent redemptions in accordance with the fair value accounting treatment under EITF Abstract No. 00-19. This amount did not recur, as the AOL contingent redemptions had been restructured effective December 2001.

On January 1, 2003, we adopted Statement of Financial Accounting Standards No. 145, “Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statements No. 13, and Technical Corrections as of April 2002”, issued in May 2002, by the Financial Accounting Standards Board, which eliminates the requirement to report gains and losses from extinguishment of debt as extraordinary items. The adoption of SFAS 145 resulted in a reclassification from extraordinary gains (losses) from the extinguishment of debt of $29.3 million and $20.7 million to other income (expense) for 2002 and 2001, respectively.

Provision for Income Taxes. In both 2003 and 2002, management evaluated the deferred tax asset valuation allowance and determined that a portion of the allowance should be reversed. The evaluation considered profitability of the business, the ability to utilize the deferred tax assets in the future and possible restrictions on use due to provisions of the Internal Revenue Code Section 382 "Change in Ownership." After consideration of each of these factors, we concluded certain deferred tax assets will more likely than not be utilized, and reversed deferred tax asset valuation allowances of $50.6 million and $22.3 million for 2003 and 2002, respectively, recognized non-cash deferred income tax benefits of $44.1 million and $22.3 million for 2003 and 2002, respectively, and reduced the amount of goodwill related to the August 2000 acquisition of Access One Communications, Inc. by $6.5 million in 2003. In 2003, the tax benefit was partially offset by an income tax expense of $24.1 million.

As a result of the application of net operating loss carryforwards, or NOLs, we currently need only pay accrued alternative minimum taxes and certain state income taxes. As of December 31, 2003, we had approximately $174.4 million of NOLs of which approximately $151.4 million are estimated to be available to offset taxable income. A valuation allowance has been recorded to reduce the carrying amounts of certain state NOLs, which we believe may not be realized. We will continue to assess the valuation allowance of these deferred tax assets, and will reverse such allowance if we conclude that it is more likely than not these deferred tax assets will be utilized. We expect that our NOLs will be fully utilized by 2007 with the exception of $2.3 million in NOLs generated by Access One Communications, Inc. and its subsidiaries, which will be fully utilized by 2018.

Cumulative Effect of an Accounting Change. We adopted Emerging Issues Task Force (EITF) Abstract No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock," in the quarter ended June 30, 2001. The cumulative effect of the adoption of this change in accounting principle resulted in a non-cash charge to operations of $36.8 million in the second quarter of 2001, representing the change in fair value

of contingent redemption features of warrants and common stock held by AOL from issuance on January 5, 1999 through June 30, 2001. The requirements under EITF 00-19 will not apply to future changes in the value of these instruments, as the AOL contingent redemptions have been restructured effective December 2001.

LIQUIDITY AND CAPITAL RESOURCES

Our management assesses our liquidity in terms of our ability to generate cash to fund our operations, our capital expenditures and our debt service obligations. In 2003 and 2002, our operating activities provided net cash flow of $73.2 million and $51.9 million, respectively, more than half of which in each year was used by us to reduce our outstanding debt obligations and a significant portion of the balance of which was used to fund capital expenditures and capitalized software development costs. As of December 31, 2003, we had $35.2 million in cash and cash equivalents and long-term debt (including current maturities) of $48.6 million, compared to $33.6 million and $100.9 million, respectively, at December 31, 2002.

Our contractual obligations as of December 31, 2003 are summarized by years to maturity as follows (in thousands):

Contractual Obligations		Total		1 year or less (as restated)		2 - 3 Years		4 - 5 Years (as restated)		Thereafter
Talk America Holdings, Inc.:										
12% Senior Subordinated Notes due 2007 (1)	$	40,730	$	15,000	$	--	$	25,730	$	--
8% Convertible Senior Subordinated Notes due 2007 (2)		3,778				--		3,778		--
5% Convertible Subordinated Notes due 2004		670		670		--		--		--
Talk America Inc. and other subsidiaries:										
Capital lease obligations		3,419		1,136		2,283		--		--
	$	48,597	$	16,806	$	2,283	$	29,508	$	--
Operating leases	$	8,248	$	2,960	$	4,306	$	501	$	481
Carrier commitments (3)		81,650		19,250		41,600		20,800		--
Total Contractual Obligations	$	138,495	$	39,016	$	48,189	$	50,809	$	481

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(1) Reflects our November 5, 2003 notice and commitment to redeem $15 million principal amount of these 12% Senior Subordinated Notes on January 5, 2004 and resulting change in the maturity of such principal amount to the noticed redemption date. Since the end of 2003 and through February 27, 2004, we have redeemed the $15 million of these 12% Senior Subordinated Notes that we so noticed for redemption and we have noticed for redemption and committed to redeem on April 20, 2004 a further $15.0 million principal amount of these 12% Senior Subordinated Notes.

(2) The amount of the 8% Convertible Senior Subordinated Notes include $2.8 million of principal and $1.0 million of future accrued interest.

(3) In December 2003, we entered into a new four-year master carrier agreement with AT&T. The agreement provides us with a variety of services, including transmission facilities to connect our network switches as well as services for international calls, local traffic, international calling cards, overflow traffic and operator assisted calls. The agreement also provides that, subject to certain terms and conditions, we will purchase these services exclusively from AT&T during the term of the agreement, provided, however, that we are not obligated to purchase exclusively in certain cases, including if such purchases would result in a breach of any contract with another carrier that was in place when we entered into the AT&T agreement, or if vendor diversity is required. Certain of our network service agreements,

including the AT&T agreement, contain certain minimum usage commitments. Our contract with AT&T establishes pricing and provides for annual minimum revenue commitments based upon usage as follows: 2004 - $25 million, 2005 - $32 million, 2006 - $32 million and 2007 - $32 million and obligates us to pay 65 percent of the revenue shortfall, if any. A separate contract with a different vendor establishes pricing and provides for annual minimum payments for 2004 of $3.0 million. While we believe we will meet these annual minimum revenue commitments, and that we will not have to pay the shortfalls, there can be no assurances of this, and, if we are required to pay any of the shortfall amounts under one of these agreements, our costs of purchasing the services under the agreement will correspondingly increase.

Cash Provided By Operating Activities. Net cash provided by operating activities was $73.2 million in 2003 and $51.9 million in 2002. In 2003, the major contributors to the net cash provided by operating activities were:
· Net income of $81.8 million;
· Increases in accounts payable and accrued expenses of $3.1 million, primarily due to increased levels of sales and marketing activity to continue our bundled sales growth, and an increase in network and line costs primarily due to the increase in bundled customers;
· A decrease in other assets of $1.5 million, primarily from repayment of a related party loan;
· An increase in deferred revenue of $4.4 million for advance customer billings, primarily due to the growth in bundled customers.

Partially offsetting these contributors to the net cash provided by operating activities were:
· Non-cash benefits of $25.9 million, primarily consisting of a net deferred tax asset of $23.4 million and gain from debt extinguishments of $2.5 million. We recognized non-cash deferred income tax benefits of $50.6 million because of our outlook for continued profitability and our ability to more likely than not utilize the deferred tax assets. The tax benefit was partially offset by income tax expense of $24.1 million. The application of NOL carryforwards have limited our current payment of income taxes to cash taxes for alternative minimum taxes and state income taxes. We expect that our NOLs will be fully utilized by 2007;
· An increase in accounts receivable of $24.1 million due to the continued shift in our customer base from long distance customers to local bundled customers with higher average monthly revenue per customer. We generally do not have a significant concentration of credit risk with respect to net trade accounts receivable, due to the large number of end-users comprising our customer base.

In 2002, the major contributors to the net cash provided by operating activities were:
· Net income of $97.1 million; and
· An increase in other liabilities of $2.6 million, primarily consisting of an increase in interest payable due to higher yielding debt instruments delivered in the exchange for our 4-1/2% and 5% Convertible Subordinated Notes for 8% Convertible Senior Subordinated Notes and 12% Senior Subordinated Notes, and the restructuring of our senior credit facility.

Partially offsetting these contributors to the net cash provided by operating activities were:
· An increase in accounts receivable of $10.6 million, primarily due to the continued shift in our customer base from long distance customers to local bundled customers with higher average monthly revenue per customer;
· A decrease in accounts payable and accrued expenses of $11.5 million, primarily due to decreases in 2002 of network and line costs, sales and marketing expenses and general and administrative expenses from 2001 and due to prompter payment of vendors; and
· Non-cash items of $53.3 million, primarily consisting of a gain from restructuring and redemption of convertible debt of $28.9 million and the deferred income tax valuation reserve reversal of $22.3 million. On December 23, 2002, we restructured our 8% Secured Convertible Notes and, accordingly, these notes were no longer accounted for as a troubled debt restructuring. The $28.9 million gain from the restructuring and repurchase of these notes was related to the decrease in future accrued interest, which was reflected as a $28.9 million reduction in long-term debt. We recognized non-cash deferred income tax benefits because of our outlook for continued profitability and our ability to utilize the deferred tax assets.

Net Cash Used in Investing Activities. In 2003, approximately 42% of our $11.8 million in capital expenditures consisted of costs related to our deployment of networking assets (local switch and colocation equipment) in Michigan. Also in 2003, to support our customer growth, we opened a new customer service call center. Costs associated with our call center initiatives were approximately 12% of total capital expenditures. The remaining 2003 capital expenditures consisted primarily of upgrades to our information technology capabilities to support our customer growth. In addition, during 2003, we entered into a capital lease valued at $3.4 million for upgrades to our customer data storage equipment. In 2004, we plan to add two more colocations and to start migrating local bundled customers over to our network, and expect to incur capital expenditures of approximately $12 to $15 million for both

network and non-network assets. As we pursue our "customer first" strategy of building a large, profitable base of bundled service customers using the wholesale operating platforms of the incumbent local exchange companies and then migrate those customers to our own networking platform and offer new products and services to these customers, our capital expenditures are expected to increase significantly.

Capitalized software development costs consist of direct development costs associated with internal-use computer software including external direct costs of material and services and payroll costs for employees devoting time to the software projects. In 2003, capitalized software development costs totaled $2.7 million and were primarily related to the development of customer relations management software. In 2004, we expect software development costs to increase moderately as we continue to develop the integrated information systems required to provide local switch-based service.

Net cash used in investing activities was $7.3 million during 2002, consisting of capitalized software development costs of $2.5 million and capital expenditures primarily for the purchase of equipment of $4.8 million.

Net Cash Used in Financing Activities. Net cash used in financing activities for 2003 and 2002 was primarily attributable to debt repayment and purchases of $52.9 and $32.7 million, respectively. For 2002, $2.8 million of interest was recorded as additional principal on the 12% Senior Subordinated Notes and 8% Secured Convertible Notes for payment of interest in kind rather than in cash. Since December 31, 2003 and through February 27, 2004, we have purchased $15.0 million principal amount of our 12% Senior Subordinated Notes at par and committed to redeem an additional $15 million principal amount in April 2004.

In addition, in 2003, pursuant to our share buyback program announced in January 2003, we purchased 1,315,789 shares for a purchase price of $5.0 million. Under the buyback program, we are authorized to spend up to $10.0 million for share purchases, with a cap of 2.5 million shares.

In 2004, we will continue to evaluate opportunities to purchase our debt prior to maturity, as well as to consider acquiring shares under the balance of our share buyback program. The remaining shares authorized under the program may be purchased, from time to time, in the open market and/or in private transactions.

Note Obligations

8% Secured Convertible Notes

In September 2001, we restructured our financial obligations with America Online, Inc. that arose under our 1999 investment agreement and, effective September 30, 2001, also ended our marketing relationship with AOL. In connection with the restructuring, we entered into a Restructuring and Note Agreement with AOL, pursuant to which we had outstanding as of December 31, 2002, $30.2 million principal amount of our 8% Secured Convertible Notes. On December 23, 2002, we restructured these 8% Secured Convertible Notes to provide for: a new maturity date of September 19, 2006, the elimination of a pay-in-kind interest option and additional flexibility to purchase subordinated debt and common stock through September 30, 2003. During 2003, we purchased all of these 8% Secured Convertible Notes. In addition, we concurrently purchased from AOL the 1,315,789 shares of our common stock held by AOL for an aggregate price of $5 million.

Convertible Subordinated Notes and Exchange Offers

Effective April 4, 2002, we completed the exchange of $57.9 million of the $61.8 million outstanding principal balance of our 4-1/2% Convertible Subordinated Notes that matured on September 15, 2002 for $53.2 million principal amount of new 12% Senior Subordinated PIK Notes due August 2007 and $2.8 million principal amount of new 8% Convertible Senior Subordinated Notes due August 2007 and cash paid of $0.5 million. In addition, we exchanged $17.4 million of the $18.1 million outstanding principal balance of our 5% Convertible Subordinated Notes that mature on December 15, 2004 for $17.4 million principal amount of the new 12% Senior Subordinated Notes. In 2003 and 2002, we acquired $25.2 million and $5.7 million principal amount of our 12% Senior Subordinated Notes, respectively, at respective discounts from face amount of $2.5 million and $1.6 million, which discounts are reported as other income in our consolidated statement of operations. We paid at maturity the remaining $3.9 million principal balance of our outstanding 4-1/2% Convertible Subordinated Notes due September 2002. Since December 31, 2003

and through February 27, 2004, we have purchased an additional $15.0 million principal amount of our 12% Senior Subordinated Notes at face amount and have committed to redeem an additional $15.0 million principal amount in April 2004.

Other Matters

Our provision of telecommunication services is subject to government regulation. See Item 1, "Regulation," above. Changes in existing regulations could have a material adverse effect on us. Our local telecommunication services are provided almost exclusively through the use of unbundled network elements purchased from incumbent local telephone companies, and it is primarily the availability of cost-based unbundled network element rates that enables us to price our local telecommunications services competitively. The FCC currently requires incumbent local telephone companies to provide an unbundled network element platform, that includes all of the network elements required by a competitor to provide a retail telecommunications service, in most geographic areas. Through the use of such unbundled network element platforms we are able to provide retail local services entirely through the use of the incumbent local telephone company's facilities at lower prices than those available for local resale through total resale service agreements. In its UNE Triennial Review proceeding, the FCC sought to identify, among other issues, which if any network elements the incumbent local telephone companies should no longer be required to offer on an unbundled basis. The FCC also analyzed the issue of which elements must be unbundled in response to a remand of its previous rules by the U.S. Court of Appeals for the District of Columbia Circuit. In the FCC's UNE Triennial Review Order, released August 21, 2003 and effective as of October 2, 2003, the Commission determined that certain network elements will no longer be subject to unbundling, while other elements must continue to be offered subject to further, more detailed review by the state public utility commissions. The Order was subject to numerous federal judicial appeals, which were consolidated in the U.S. Court of Appeals for the District of Columbia Circuit. The Court, on March 2, 2004, issued an order that reversed the FCC's Order in part and remanded to the FCC with instructions to revise the Order in material ways. The Court stayed its decision until the denial of any petitions for rehearing or for a 60-day period (i.e., until May 1, 2004), whichever is later.

Should the local circuit switching unbundled network element become effectively unavailable due to this adverse decision or otherwise, we would be unable to offer services on an unbundled network element platform basis and would instead have to serve customers through total service resale agreements with the incumbent local exchange companies, through network elements purchased from the Regional Bell Operating Companies at "just and reasonable" rates under Section 271 of the Act or through our own facilities or the switching facilities of other non-incumbent carriers. Our transition from providing telecommunications services on an unbundled network element platform basis could delay our service roll-out in some markets, increase our costs and negatively impact our business, prospects, operating margins, results of operations, cash flows and financial condition. See Item 1, "Regulation."

We are party to a number of legal actions and proceedings arising from our provision and marketing of telecommunications services, as well as certain legal actions and regulatory matters arising in the ordinary course of business. During the second quarter 2003, we were made aware that AOL agreed to settle a class action case for approximately $10 million; the claims in the case allegedly relate to marketing activities conducted pursuant to a former telecommunications marketing agreement, between us and AOL. At the time of the settlement agreement, AOL asserted that we are required to indemnify AOL in this matter under the terms of the marketing agreement and advised that it will seek such indemnification from us. We believe that we do not have an obligation to indemnify AOL in this matter and that any claim by AOL for this indemnification would be without merit. We have received no further information regarding this matter and it is our intention, if AOL initiates a claim for indemnification under the marketing agreement, to defend against the claim vigorously. We believe that the ultimate outcome of the foregoing actions will not result in liability that would have a material adverse effect on our financial condition or results of operations.

While we believe that we have access to new capital in the public or private markets to fund our ongoing cash requirements, there can be no assurance as to the timing, amounts, terms or conditions of any such new capital or whether it could be obtained on terms acceptable to us. We anticipate that our cash requirements will generally be met from our cash-on-hand and from cash generated from operations. Based on our current projections for operations, we believe that our cash-on-hand and our cash flow from operations will be sufficient to fund our currently contemplated capital expenditures, our debt service obligations, and the expenses of conducting our operations for at least the next

twelve months. However, there can be no assurance that we will be able to realize our projected cash flows from operations, which is subject to the risks and uncertainties discussed above, or that we will not be required to consider capital expenditures in excess of those currently contemplated, as discussed above.

Our business involves risks and uncertainties and our actual results could differ materially from our expectations. In addition to those factors discussed elsewhere in this Form 10-K, important factors that could impact our business include, among others:

· changes in government policy, regulation and enforcement and/or adverse judicial or administrative interpretations and rulings relating to regulations and enforcement, including, but not limited to, those that affect the continued availability to us, on acceptable economic terms, of the unbundled network element platform of the local exchange carriers network, on which our business, as now conducted, is substantially dependent;
· our ability successfully to implement our business strategy, including the development and deployment of our own local services networking platform and the migration of our customer base to the new platform, and our ability to finance the costs of such implementation;
· the success of such business strategy if and when implemented;
· increased price competition for long distance and local services;
· our ability to continue to manage the nonpayment of amounts due us from our customers from bundled and long distance services;
· attrition in the number of our customers;
· our ability to continue to manage our operations, including attracting and retaining qualified personnel;
· our ability to continue to expand our active offering of local bundled services to a greater number of states;
· our ability to continue to manage our collection management systems and credit controls for customers;
· interruptions in our network and information systems; and
· our ability to continue to provide adequate customer service.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to bad debt, goodwill and intangible assets, income taxes, contingencies and litigation. We base our estimates and judgments on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Allowance for Doubtful Accounts

Allowances for doubtful accounts are maintained for estimated losses resulting from the failure of customers to make required payments on their accounts. We review accounts receivable aging trends, historical bad debt trends, and customer credit-worthiness through customer credit scores, current economic trends and changes in customer payment history when evaluating the adequacy of the allowance for doubtful accounts. In addition, we review the financial condition of the carriers that pay us access charges to assess their ability to make payments.

Valuation of Long-Lived Assets and Intangible Assets with a Definite Life

We review the recoverability of the carrying value of long-lived assets, including intangibles with a definite life, for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. When such events occur, we compare the carrying amount of the assets to the undiscounted expected future cash flows from them. Factors we consider important that could trigger an impairment review include the following:

· Significant underperformance relative to historical or projected future operating results
· Significant changes in the manner of our use of the acquired assets or the strategy for our overall business
· Significant negative industry or economic trends
· Significant decline in our stock price for a sustained period and market capitalization relative to net book value

If this comparison indicates there is impairment, the amount of the impairment loss to be recorded is calculated by the excess of the net assets' carrying value over its fair value and is typically calculated using discounted expected future cash flows.

Goodwill

Goodwill represents the cost in excess of net assets of acquired companies. Effective January 1, 2002, with the adoption of SFAS No. 142, goodwill (comprised of goodwill acquired in the Access One acquisition in August 2000) will not be amortized, but rather will be tested for impairment annually, and will be tested for impairment between annual tests if an event occurs or circumstances change that would indicate the carrying amount may be impaired. Prior to January 1, 2002, goodwill and intangibles were amortized on a straight-line basis over periods ranging from 5 years to 15 years. Impairment testing for goodwill is performed at a reporting unit level; we determined that we have one reporting unit under the guidance of SFAS No. 142. An impairment loss would generally be recognized when the carrying amount of the reporting unit’s net assets exceeds the estimated fair value of the reporting unit. Prior to January 1, 2002, goodwill was tested for impairment in a manner consistent with long-lived assets and intangible assets with a definite life.

Income Taxes

Income taxes are accounted for under the asset and liability method. During 2003, we recorded income taxes at a rate equal to our combined federal and state effective rates. Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to the differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled.

We consider all available evidence, both positive and negative, to determine whether, based on the weight of that evidence, a valuation allowance is needed for some portion or all of a net deferred tax asset. Judgment is used in considering the relative impact of negative and positive evidence. In arriving at these judgments, the weight given to the potential effect of negative and positive evidence is commensurate with the extent to which it can be objectively verified. We record a valuation allowance to reduce our deferred tax assets and review the amount of such allowance annually. When we determine certain deferred tax assets are more likely than not to be utilized, we will reduce our valuation allowance accordingly.

New Accounting Pronouncements

Effective January 1, 2002, we adopted Emerging Issues Task Force (EITF) 01-09, "Accounting for Consideration Given by a Vendor to a Customer or a Reseller of the Vendor's Products." This issue presumes that consideration from a vendor to a customer or reseller of the vendor's products is a reduction of the selling prices of the vendor's products and, therefore, should be characterized as a reduction of revenue when recognized in the vendor's statement of operations and could lead to negative revenue under certain circumstances. Revenue reduction is required unless the consideration relates to a separate, identifiable benefit and the benefit's fair value can be established. The adoption of this issue resulted in a reclassification from sales and marketing expenses of $7.3 million to a reduction of net sales for the year ended December 31, 2001 attributable to direct marketing promotion check campaigns. The adoption of EITF 01-09 did not have a material effect on our consolidated financial statements for the years ended December 31, 2003 and 2002, as we did not have any direct marketing promotion check campaigns during this period.

In May 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 145, “Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statements No. 13, and Technical Corrections as of April 2002.” SFAS 145 eliminates the requirement to report gains and losses from extinguishment of debt as extraordinary items. Gains and losses from extinguishment of debt will now be classified as extraordinary items only if they meet the criteria of APB Opinion No. 30. We adopted SFAS 145 effective January 1, 2003. The adoption of SFAS 145 resulted in a reclassification from extraordinary gains (losses) from the extinguishment of debt of $29.3 million and $20.7 million, respectively, to other income (expense) for the years ended December 31, 2002 and 2001.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

TALK AMERICA HOLDINGS, INC. AND SUBSIDIARIES
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Consolidated balance sheets as of December 31, 2003 (restated) and 2002	18
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Report of Independent Registered Public Accounting Firm

To the Board of Directors and
Shareholders of Talk America Holdings, Inc.:

In our opinion, the consolidated financial statements listed in the index appearing under Item 15(a) (1) present fairly, in all material respects, the financial position of Talk America Holdings, Inc. and its subsidiaries at December 31, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 15(a)(2) presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13 and Technical Corrections as of April 2002", effective January 1, 2003 and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets", effective January 1, 2002.

As discussed in Note 16 to the consolidated financial statements, the December 31, 2003 consolidated financial statements have been restated.

PricewaterhouseCoopers LLP
Philadelphia, Pennsylvania
February 3, 2004, except for
Note 14, as to which date is
February 27, 2004, and Note
16, as to which date is
March 25, 2005

TALK AMERICA HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except for per share data)

	Year Ended December 31,		
	2003 (Restated)	2002	2001
Revenue	$ 383,693	$ 317,507	$ 488,158
Costs and expenses:			
Network and line costs	181,682	155,567	235,153
General and administrative expenses	57,503	53,510	82,202
Provision for doubtful accounts	11,599	9,365	92,778
Sales and marketing expenses	48,277	27,148	73,973
Depreciation and amortization	18,344	17,318	34,390
Impairment and restructuring charges	--	--	170,571
Total costs and expenses	317,405	262,908	689,067
Operating income (loss)	66,288	54,599	(200,909)
Other income (expense):			
Interest income	388	802	1,220
Interest expense	(7,353)	(9,087)	(6,091)
Other income (expense), net	2,470	28,448	17,950
Income (loss) before provision for income taxes	61,793	74,762	(187,830)
Provision (benefit) for income taxes	(20,024)	(22,300)	--
Income (loss) before cumulative effect of an accounting change	81,817	97,062	(187,830)
Cumulative effect of an accounting change	--	--	(36,837)
Net income (loss)	$ 81,817	$ 97,062	$ (224,667)
Income (loss) per share - Basic:			
Income (loss) before cumulative effect of an accounting change per share	$ 3.10	$ 3.56	$ (7.11)
Cumulative effect of an accounting change per share	--	--	(1.40)
Net income (loss) per share	$ 3.10	$ 3.56	$ (8.51)
Weighted average common shares outstanding	26,376	27,253	26,414
Income (loss) per share - Diluted:			
Income (loss) before cumulative effect of an accounting change per share	$ 2.94	$ 3.15	$ (7.11)
Cumulative effect of an accounting change per share	--	--	(1.40)
Net income (loss) per share	$ 2.94	$ 3.15	$ (8.51)
Weighted average common and common equivalent shares outstanding	27,806	30,798	26,414

See accompanying notes to consolidated financial statements.

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TALK AMERICA HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except for share and per share data)

		December 31, 2003 (Restated)		December 31, 2002
Assets				
Current assets:				
Cash and cash equivalents	$	35,242	$	33,588
Accounts receivable, trade (net of allowance for uncollectible accounts of $9,414 and $7,821 at December 31, 2003 and 2002, respectively)		40,321		27,843
Deferred income taxes		24,605		17,500
Prepaid expenses and other current assets		5,427		3,894
Total current assets		105,595		82,825
Property and equipment, net		68,069		66,915
Goodwill		13,013		19,503
Intangibles, net		4,666		7,379
Deferred income taxes		48,288		4,800
Other assets		7,547		7,653
	$	247,178	$	189,075
Liabilities and Stockholders' Equity				
Current liabilities:				
Accounts payable	$	35,296	$	32,152
Sales, use and excise taxes		13,521		11,439
Deferred revenue Legal settlements		10,873		6,480
Current portion of long-term debt		16,806		61
Accrued compensation		9,888		5,609
Other current liabilities		6,851		9,013
Total current liabilities		93,235		64,754
Long-term debt		31,791		100,855
Deferred income taxes		19,009		--
Commitments and contingencies				
Stockholders' equity:				
Preferred stock - $.01 par value, 5,000,000 shares authorized; no shares outstanding		--		--
Common stock - $.01 par value, 100,000,000 shares authorized; 26,662,952 and 27,469,593 shares issued and outstanding at December 31, 2003 and 2002, respectively		280		275
Additional paid-in capital		354,847		351,992
Accumulated deficit		(246,984)		(328,801)
Treasury stock - $.01 par value, 1,315,789 shares at December 31, 2003		(5,000)		--
Total stockholders' equity		103,143		23,466

	$	247,178	$	189,075

See accompanying notes to consolidated financial statements.

TALK AMERICA HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Year Ended December 31,		
	2003 (Restated)	2002	2001
Cash flows from operating activities:			
Net income (loss)	$ 81,817	$ 97,062	$ (224,667)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Provision for doubtful accounts	11,599	9,365	92,778
Depreciation and amortization	18,344	17,318	34,390
Non-cash compensation	--	194	--
Non-cash interest and amortization of accrued interest liabilities	(260)	832	--
Provision for uncollectible note	--	--	77
Loss on sale and retirement of assets	23	205	116
Impairment of goodwill and intangibles	--	--	168,684
Cumulative effect of accounting change of contingent redemptions	--	--	36,837
Gain from restructuring of convertible debt	--	(28,909)	--
Gain from restructuring of contingent redemptions	--	--	(16,867)
Gain from extinguishment of debt	(2,475)	(431)	(3,781)
Unrealized loss on increase in fair value of contingent redemptions	--	--	2,372
Deferred income taxes	(23,409)	(22,300)	--
Gain on legal settlement	--	(1,681)	--
Changes in assets and liabilities:			
Accounts receivable, trade	(24,078)	(10,560)	(65,788)
Prepaid expenses and other current assets	(1,605)	(1,902)	(527)
Other assets	1,475	2,211	1,142
Accounts payable	3,144	(11,462)	(27,181)
Deferred revenue	4,393	(3,713)	(9,004)
Sales, use and excise taxes	2,082	3,101	404
Other current liabilities and accrued compensation	2,116	2,568	5,418
Net cash provided by (used in) operating activities	73,166	51,898	(5,597)
Cash flows from investing activities:			
Acquisition of intangibles	(133)	(50)	(154)
Capital expenditures	(11,842)	(4,781)	(2,949)
Capitalized software development costs	(2,739)	(2,501)	(1,406)
Net cash used in investing activities	(14,714)	(7,332)	(4,509)
Cash flows from financing activities:			
Payments of borrowings	(52,914)	(17,983)	(2,624)
Payments of capital lease obligations	(61)	(1,036)	(1,022)
Acquisition of convertible debt and senior notes	--	(14,691)	(1,227)
Proceeds from exercise of options and warrants	1,177	632	--
	--	--	(3,525)

Payments in connection with restructuring contingent redemptions						
Purchase of treasury stock		(5,000)		--		--
Net cash used in financing activities		(56,798)		(33,078)		(8,398)
Net increase (decrease) in cash and cash equivalents		1,654		11,488		(18,504)
Cash and cash equivalents, beginning of year		33,588		22,100		40,604
Cash and cash equivalents, end of year	$	35,242	$	33,588	$	22,100

See accompanying notes to consolidated financial statements.

TALK AMERICA HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)
(In thousands)

	Common Stock				Treasury Stock		
	Shares	Amount	Additional Paid-In Capital	Accumulated Deficit	Shares	Amount	Total
lance, December 31, 00	26,148	$ 261	$ 287,486	$ (201,196)	(91)	$ (3,851)	$ 82,7
t (loss)	--	--	--	(224,667)	--	--	(224,66
uance of common stock for compensation	--	--	(2,451)	--	68	2,858	4
mulative effect of an accounting change	--	--	65,617	--	--	--	65,6
uance of common stock in connection with AOL tructuring	1,003	11	440	--	24	993	1,4
quisition of treasury stock	--	--	--	--	(1)	--	
uance of warrants for services	--	--	77	--	--	--	
lance, December 31, 2001	27,151	272	351,169	(425,863)	--	--	(74,42
t income	--	--	--	97,062	--	--	97,0
uance of common stock for services	67	1	82	--	--	--	
ercise of common stock options	252	2	741	--	--	--	7
lance, December 31, 2002	27,470	275	351,992	(328,801)	--	--	23,4
t income, restated	--	--	--	81,817	--	--	81,8
quisition of treasury stock	--	--	--	--	1,316	(5,000)	(5,00
ercise of common stock options	509	5	1,172	--	--	--	1,17
come tax benefit related to exercise of common ck options	--	--	1,683	--	--	--	1,68
ance, December 31, 2003 (restated)	27,979						

$

280

$

354,847

$

(246,984)

1,316

$

(5,000)

$103,143

See accompanying notes to consolidated financial statements.

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TALK AMERICA HOLDINGS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF ACCOUNTING POLICIES

(a) Business

Talk America Holdings, Inc., through its subsidiaries, offers a bundle of local and long distance phone services to residential and small business customers in the United States. We operate our own nationwide long distance network and deliver local services through wholesale operating agreements with the incumbent local exchange companies. We have developed integrated order processing, provisioning, billing, payment, collection, customer service and information systems that enable us to offer and deliver high-quality service, savings through competitively priced telecommunication products, and simplicity through consolidated billing and responsive customer service. We operate our own sales and customer service centers. We manage our business as one reportable operating segment.

(b) Basis of Financial Statements Presentation

The consolidated financial statements include the accounts of Talk America Holdings, Inc. and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated.

(c) Use of Estimates

In preparing financial statements in conformity with generally accepted accounting principles in the United States, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from those estimates.

(d) Reclassifications

Certain amounts for 2002 and 2001 have been reclassified to conform to the current year presentation.

(e) Risks and Uncertainties

Future results of operations involve a number of risks and uncertainties. Factors that could affect future operating results and cash flows and cause actual results to vary materially from historical results include, but are not limited to:

- Changes in government policy, regulation and enforcement or adverse judicial or administrative interpretations and rulings or legislative action relating to regulations, enforcement and pricing, including, but not limited to, changes that affect the continued availability of the unbundled network element platform of the local exchange carriers network and the costs associated therewith
- Dependence on the availability and functionality of the networks of the incumbent local exchange carriers as they relate to the unbundled network element platform
- Increased price competition in local and long distance services, including bundled services, and overall competition within the telecommunications industry, including, but not limited to, in the State of Michigan
- Adverse determinations in certain litigation matters

Negative developments in these areas could have a material effect on our business, financial condition and results of operations.

(f) Concentration of Credit Risk

We maintain our cash and cash equivalents in bank deposit accounts, which at times may exceed federally insured limits. We generally do not have a significant concentration of credit risk with respect to net trade accounts receivable, due to the large number of end users comprising our customer base.

(g) Recognition of Revenue

We derive our revenues from local and long distance phone services, primarily local services bundled with long distance services. We recognize revenue from voice, data and other telecommunications-related services in the period in which subscribers use the related service. Deferred revenue represents the unearned portion of local service and features that are billed a month in advance.

Revenue for 2002 and 2001 included amortization of a non-refundable prepayment received in 1997 in connection with an amended telecommunications services agreement with Shared Technologies Fairchild, Inc. The prepayment was amortized over the five-year term of the agreement, which expired October 2002. The amount included in revenue was $6.2 million in 2002 and $7.4 million in 2001.

(h) Allowance for Doubtful Accounts

Allowances for doubtful accounts are maintained for estimated losses resulting from the failure of customers to make required payments on their accounts. We review accounts receivable aging trends, historical bad debt trends, and customer credit-worthiness through customer credit scores, current economic trends and changes in customer payment history when evaluating the adequacy of the allowance for doubtful accounts. In addition, we review the financial condition of the carriers that pay us access charges to assess their ability to make payments.

(i) Cash and Cash Equivalents

We consider all temporary cash investments purchased with an initial maturity of three months or less to be cash equivalents.

(j) Property and Equipment and Depreciation

Property and equipment are recorded at historical cost. Depreciation and amortization are calculated using the straight-line method over the estimated useful lives of the assets from 3 to 39 years. Leasehold improvements are depreciated over the life of the related lease or asset, if shorter. Amortization of assets acquired under capital leases is included in depreciation and amortization expense.

Repair and maintenance costs are expensed as incurred. Significant improvements extending the useful life of property are capitalized. When property is retired or otherwise disposed of, the cost of the property and the related accumulated depreciation are removed from the accounts, and any resulting gains or losses are reflected in the consolidated statement of operations.

(k) Computer Software Development Costs

Direct development costs associated with internal-use computer software are accounted for under Statement of Position 98-1 "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" and are capitalized including external direct costs of material and services and payroll costs for employees devoting time to the software projects. Costs incurred during the preliminary project stage, as well as for maintenance and training are expensed as incurred. Amortization is provided on a straight-line basis over the shorter of 3 years or the estimated useful life of the software.

Computer software developed or obtained for internal use are included in other assets at December 31, 2003 and 2002 were $6.6 million and $3.9 million, respectively, net of accumulated amortization of $2.1 million and $0.6 million at December 31, 2003 and 2002. Amortization expense was $1.5 million and $0.6 million, respectively, for the years ended December 31, 2003 and 2002.

(l) Goodwill and Intangibles

Effective January 1, 2002, we adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," which establishes the impairment approach rather than amortization for goodwill. Effective January 1, 2002, we are not required to record amortization expense on goodwill, but instead are required to evaluate these assets for potential impairment at least annually and test for impairment between annual tests if an event occurs or circumstances change that would indicate the carrying amount may be impaired.

In order to complete the transitional assessment of goodwill as required by SFAS 142, we determined the fair value of the reporting unit associated with the goodwill and compared it to the reporting unit's carrying amount, including goodwill. We determined that we have one reporting unit. The fair value of the reporting unit was determined primarily using a discounted cash flow approach and quoted market price of our stock. The amount of goodwill reflected in the balance sheet as of December 31, 2002 and 2001 was $13.0 and $19.5 million, respectively. We completed the transitional assessment of goodwill and determined that the fair value of the reporting unit exceeds its carrying amount, thus goodwill was not considered impaired at the date of adoption. We tested for impairment during the second quarter 2003 and determined goodwill is not impaired.

The following unaudited pro forma summary presents the adoption of SFAS 142 as of the beginning of the periods presented to eliminate the amortization expense recognized in those periods related to goodwill that are no longer required to be amortized. The pro forma amounts for the year ended December 31, 2001 does not include any write-downs of goodwill that could have resulted had we adopted SFAS 142 as of the beginning of that year and performed the required impairment test under this standard.

(In thousands, except for per share data)	Year Ended December 31,					
		2003 (Restated)		**2002**		**2001**
Net income (loss) as reported	$	81,817	$	97,062	$	(224,667)
Add back: Goodwill amortization		--		--		17,271
Adjusted net income (loss)	$	81,817	$	97,062	$	(207,396)
Basic income (loss) per share:						
Net income (loss) as reported per share	$	3.10	$	3.56	$	(8.51)
Goodwill amortization per share		--		--		0.66
Adjusted net income (loss) per share	$	3.10	$	3.56	$	(7.85)
Diluted income (loss) per share:						
Net income (loss) as reported per share	$	2.94	$	3.15	$	(8.51)
Goodwill amortization per share		--		--		0.66
Adjusted net income (loss) per share	$	2.94	$	3.15	$	(7.85)

Intangible assets consisted primarily of purchased customer accounts with a definite life and are being amortized on a straight-line basis over 5 years. We incurred amortization expense on intangible assets with a definite life of $2.8 million, $2.8 million, and $3.2 million for the years ended December 31, 2003, 2002 and 2001, respectively. Our balance of intangible assets with a definite life was $4.4 million at December 31, 2003, net of accumulated amortization of $9.0 million. Amortization expense on intangible assets with a definite life for the next 5 years as of December 31, is as follows: 2004 - $2.8 million, and 2005 - $1.7 million.

(m) Valuation of Long-Lived Assets

Effective January 1, 2002, we adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS 144 establishes a single accounting model for the impairment or disposal of long-lived assets, including discontinued operations.

We review the recoverability of the carrying value of long-lived assets, including intangibles with a definite life, for impairment using the methodology prescribed in SFAS 144 whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable.

(n) Income Taxes

Income taxes are accounted for under the asset and liability method. Accordingly, deferred tax assets and liabilities are recognized currently for the future tax consequences attributable to the temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. A valuation allowance is recorded to reduce the carrying amounts of deferred tax assets if it is more likely than not that such assets will not be realized.

(o) Net Income (Loss) Per Share

Basic earnings per share is computed by dividing income (loss) available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the effect of common shares issuable upon exercise of stock options, warrants and conversion of convertible debt, when such effect is not antidilutive.

(p) Financial Instruments

The carrying values of accounts receivable, prepaid expenses and other current assets, accounts payable and accrued expenses approximate their fair values. Convertible debt is recorded at face amount but such debt has traded in the open market at discounts to face amount. The market value of our public debt securities was approximately 100% and 75% of face amount at December 31, 2003 and 2002, respectively.

(q) Stock-Based Compensation

We account for our stock option awards under the intrinsic value based method of accounting prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations, including FASB Interpretation No. 44 "Accounting for Certain Transactions Including Stock Compensation," an interpretation of APB Opinion No. 25. Under the intrinsic value based method, compensation cost is the excess, if any, of the quoted market price of the stock at grant date or other measurement date over the amount an employee must pay to acquire the stock. We make pro forma disclosures of net income and earnings per share as if the fair value based method of accounting had been applied as required by SFAS No. 123, "Accounting for Stock-Based Compensation" and SFAS 148, “Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of SFAS 123”. The following disclosure complies with the adoption of this statement and includes pro forma net loss as if the fair value based method of accounting had been applied:

(In thousands)	Year Ended December 31,		
	2003 (Restated)	**2002**	**2001**
Net income (loss) as reported	$ 81,817	$ 97,062	$ (224,667)
Add: Stock-based employee compensation expense included in reported net income (loss)	--	110	--
Deduct: Total stock-based employee compensation expense determined under fair value based method for all options	(1,348)	(5,208)	(1,380)
Pro forma net income (loss)	$ 80,469	$ 91,964	$ (226,047)

	Year Ended December 31,		
	2003 (Restated)	**2002**	**2001**
Basic earnings (loss) per share:			
As reported	$ 3.10	$ 3.56	$ (8.51)
Pro forma	$ 3.05	$ 3.38	$ (8.56)
Diluted earnings (loss) per share:			
As reported	$ 2.94	$ 3.15	$ (8.51)
Pro forma	$ 2.94	$ 2.96	$ (8.56)

For purposes of pro forma disclosures under SFAS 123, the estimated fair value of the options is assumed to be amortized to expense over the options' vesting period. The fair value of the options granted has been estimated at the various dates of the grants using the Black-Scholes option-pricing model with the following assumptions:

- Fair market value based on our closing common stock price on the date the option is granted;
- Risk-free interest rate based on the weighted averaged 5 year U.S. treasury note strip rates;
- Volatility based on the historical stock price over the expected term (5 years);
- No expected dividend yield based on future dividend payment plans.

(r) Comprehensive Income

We have no items of comprehensive income or expense. Accordingly, our comprehensive income (loss) and net income (loss) are equal for all periods presented.

(s) New Accounting Pronouncements

Effective January 1, 2002, we adopted Emerging Issues Task Force (EITF) 01-09, "Accounting for Consideration Given by a Vendor to a Customer or a Reseller of the Vendor's Products." This issue presumes that consideration from a vendor to a customer or reseller of the vendor's products is a reduction of the selling prices of the vendor's products and, therefore, should be characterized as a reduction of revenue when recognized in the vendor's statement of operations and could lead to negative revenue under certain circumstances. Revenue reduction is required unless the consideration relates to a separate, identifiable benefit and the benefit's fair value can be established. The adoption of this issue resulted in a reclassification from sales and marketing expenses of $7.3 million to a reduction of net sales for the year ended December 31, 2001 attributable to direct marketing promotion check campaigns. The adoption of EITF 01-09 did not have a material effect on our consolidated financial statements for the years ended December 31, 2003 and 2002, as we did not have any direct marketing promotion check campaigns during this period.

In May 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 145, “Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statements No. 13, and Technical Corrections as of April 2002.” SFAS 145 eliminates the requirement to report gains and losses from extinguishment of debt as extraordinary items. Gains and losses from extinguishment of debt will now be classified as extraordinary items only if they meet the criteria of APB Opinion No. 30. We have adopted SFAS 145 effective January 1, 2003. The adoption of SFAS 145 resulted in a reclassification from extraordinary gains (losses) from the extinguishment of debt of $29.3 million and $20.7 million, respectively, to other income (expense) for the years ended December 31, 2002 and 2001.

(t) Advertising

We expense advertising costs as they are incurred. Advertising expenses totaled approximately $6.8 million, $1.5 million and $0.2 million for the years ended December 31, 2003, 2002 and 2001, respectively.

NOTE 2. IMPAIRMENT AND RESTRUCTURING CHARGES

In 2001, we recorded an impairment charge of $168.7 million primarily related to the write-down of goodwill associated with the acquisition of Access One Communications Corp. in August 2000. SFAS 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of," required the evaluation of impairment of long-lived assets and identifiable intangibles whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Management determined that goodwill should be evaluated for impairment in accordance with the provisions of SFAS 121 due to the increased bad debt rate and increased customer turnover, as well as the restructuring of our financial obligations with America Online, Inc. and the concurrent termination of our marketing relationship with AOL that occurred in the year ended December 30, 2001. The write-down of goodwill was based on an analysis of projected discounted cash flows using a discount rate of 18%, which results determined that the fair value of the goodwill was substantially less than the carrying value.

In September 2001, we approved a plan to close one of our call center operations and recorded a charge of $2.5 million to reflect the elimination of approximately 225 positions amounting to $1.0 million and lease exit costs amounting to $1.5 million in connection with the call center closure. Actual restructuring costs were $1.9 million, comprised of $1.2 million of employee severance costs and $0.7 million of lease termination and other call center closure costs.

NOTE 3. COMMITMENTS AND CONTINGENCIES

(a) Lease Agreements

We lease office space and equipment under operating and capital lease agreements. Certain leases contain renewal options and purchase options, and generally provide that we shall pay for insurance, taxes and maintenance. Total rent expense for all operating leases for the years ended December 31, 2003, 2002 and 2001 was $1.9 million, $2.4 million, and $2.5 million, respectively. As of December 31, 2003, we had future minimum annual lease obligations under noncancellable leases with terms in excess of one year as follows (in thousands):

Year Ended December 31,	Operating Leases	Capital Lease	Total
2004	$ 2,960	$ 1,191	$ 4,151
2005	2,495	1,164	3,659
2006	1,811	1,164	2,975
2007	363	--	363
2008	138	--	138
Thereafter	481	--	481
Total minimum lease payments	$ 8,248	$ 3,519	$ 11,767
Less: interest		100	
Present value of minimum lease payments		$ 3,419	
Less: current installments		1,136	
Long-term obligations		$ 2,283	

(b) Legal Proceedings

In the third quarter of 2002, we paid $140,000 in connection with the settlement of litigation relating to an obligation with a third party that had previously been reflected as a liability, and recorded a non-cash reduction of expense in the amount of $1.7 million.

On November 12, 2001, Traffix, Inc. was awarded approximately $6.2 million in an arbitration concerning the termination of a marketing agreement between us and Traffix, which the parties agreed would be paid in two installments - $3.7 million paid in November 2001 and the remaining $2.5 million paid in April 2002.

We are party to a number of legal actions and proceedings arising from our provision and marketing of telecommunications services, as well as certain legal actions and regulatory matters arising in the ordinary course of business. During the second quarter of 2003, we were made aware that AOL agreed to settle a class action case for approximately $10 million; the claims in the case allegedly relate to marketing activities conducted pursuant to the former telecommunications marketing agreement, between us and AOL. At the time of the settlement agreement, AOL asserted that we are required to indemnify AOL in this matter under the terms of the marketing agreement and advised that it will seek such indemnification from us. We believe that we do not have an obligation to indemnify AOL in this matter and that any claim by AOL for this indemnification would be without merit. We have received no further information regarding this matter and it is our intention, if AOL initiates a claim for indemnification under the marketing agreement, to defend against the claim vigorously. We believe that the ultimate outcome of the foregoing actions will not result in a liability that would have a material adverse effect on our financial condition or results of operations.

(c) Network Commitments

We are party to various network service agreements, which contain certain minimum usage commitments. In December 2003, we entered into a new four-year master carrier agreement with AT&T. The agreement provides us with a variety of services, including transmission facilities to connect our network switches as well as services for international calls, local traffic, international calling cards, overflow traffic and operator assisted calls. The agreement also provides that, subject to certain terms and conditions, we will purchase these services exclusively from AT&T during the term of the agreement, provided, however, that we are not obligated to purchase exclusively in certain cases, including if such purchases would result in a breach of any contract with another carrier that was in place when we entered into the AT&T agreement or if vendor diversity is required. Certain of our network service agreements, including the AT&T agreement contain certain minimum usage commitments. Our contract with AT&T establishes pricing and provides for annual minimum revenue commitments based upon usage as follows: 2004 - $25 million, 2005 - $32 million, 2006 - $32 million, 2007 - $32 million, and obligates us to pay 65 percent of the revenue shortfall, if any. A separate contract with a different vendor establishes pricing and provides for annual minimum payments for 2004 of $3.0 million. While we believe we will meet these annual minimum revenue commitments and that we will not have to pay any shortfalls, there can be no assurances of this, and, if we are required to pay any of the shortfall amounts under one of these agreements, our costs of purchasing the services under the agreement will correspondingly increase.

NOTE 4. PROPERTY AND EQUIPMENT

The following is a summary of property and equipment, at cost, less accumulated depreciation (in thousands):

	Lives	December 31, 2003	December 31, 2002
Land		$ 330	$ 330
Buildings and building improvements	39 years	6,987	6,782
Leasehold improvements	3-10 years	1,757	397
Switching equipment	10-15 years	64,161	59,289
Software	3 years	7,877	6,366
Equipment and other	3-10 years	50,830	44,770
		131,942	117,934
Less: Accumulated depreciation		(63,873)	(51,019)
		$ 68,069	$ 66,915

The following is a summary of property and equipment, at cost, recorded under capital leases (in thousands):

	Lives	December 31, 2003	December 31, 2002
Equipment and other	3 years	$ 3,627	$ 235
Less: Accumulated depreciation		(196)	(117)
		$ 3,431	$ 118

For the years ended December 31, 2003, 2002 and 2001, depreciation expense amounted to $14.1 million, $13.3 million and $13.6 million, respectively.

NOTE 5. DEBT AND CAPITAL LEASE OBLIGATIONS

The following is a summary of our debt and capital lease obligations (in thousands):

	December 31, 2003	December 31, 2002
12% Senior Subordinated Notes Due 2007	$ 40,730	$ 65,970
8% Secured Convertible Notes Due 2006	--	30,150
8% Convertible Senior Subordinated Notes Due 2007 (1)	3,778	4,038
5% Convertible Subordinated Notes Due 2004	670	670
Capital lease obligations	3,419	88
Total long-term debt and capital lease obligations	$ 48,597	$ 100,916
Less: current maturities (2)	16,806	61
Total long-term debt and capital lease obligations, excluding current maturities	$ 31,791	$ 100,855

(1) Includes future accrued interest or $1.0 million and $1.2 million in 2003 and 2002, respectively.

(2) Reflects our November 5, 2003 notice and commitment to redeem $15 million principal amount of these 12% Senior Subordinated Notes on January 5, 2004 and resulting change in the maturity of such principal amount to the noticed redemption date.

(a) 12% Senior Subordinated Notes Due 2007 and 8% Convertible Senior Subordinated Notes Due 2007

Effective April 4, 2002, we completed the exchange of $57.9 million of the $61.8 million outstanding principal balance of our 4-1/2% Convertible Subordinated Notes due December 15, 2002 ("4-1/2% Convertible Subordinated Notes") for $53.2 million principal amount of our new 12% Senior Subordinated PIK Notes due August 2007 ("12% Senior Subordinated Notes") and $2.8 million principal amount of our new 8% Convertible Senior Subordinated Notes due August 2007 ("8% Convertible Senior Subordinated Notes") and cash paid of $0.5 million. In addition, we exchanged $17.4 million of the $18.1 million outstanding principal balance of our 5% Convertible Subordinated Notes ("5% Convertible Subordinated Notes") that mature on December 15, 2004 for $17.4 million principal amount of the 12% Senior Subordinated Notes.

The 12% Senior Subordinated Notes accrue interest at a rate of 12% per year on the principal amount, payable semiannually on February 15 and August 15, beginning on August 15, 2002. Interest is payable in cash, except that we may, at our option, pay up to one-third of the interest due on any interest payment date through and including the August 15, 2004 interest payment date in additional 12% Senior Subordinated Notes. The 8% Convertible Senior Subordinated Notes accrue interest at a rate of 8% per year on the principal amount, also payable semiannually on February 15 and August 15, and are convertible, at the option of the holder, into common stock at $15.00 per share. The 12% Senior Subordinated Notes and 8% Convertible Senior Subordinated Notes are redeemable at any time at our option at par value plus accrued interest to the redemption date.

In accordance with SFAS No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructurings," we accounted for the exchange of the 4-1/2% Convertible Subordinated Notes for $53.2 million of the 12% Senior Subordinated Notes and $2.8 million of the 8% Convertible Senior Subordinated Notes as a troubled debt restructuring. Since the total liability of $57.4 million ($57.9 million of principal as of the exchange date, less cash payments of $0.5 million) was less than the future cash flows to holders of 8% Convertible Senior Subordinated Notes and 12% Senior Subordinated Notes of $91.5 million (representing the $56.0 million of principal and $35.5 million of future interest expense), the liability remained on our balance sheet at $57.4 million as long-term debt. We recognized the difference of $1.4 million between principal and the carrying amount as a reduction of interest expense over the life of the new notes.

In 2003, we acquired $25.2 million principal amount of 12% Senior Subordinated Notes during 2003 at a $2.5 million discount from face amount. In 2002, we acquired $5.7 million principal amount of 12% Senior Subordinated Notes at a $1.6 million discount from face amount. In accordance with SFAS No. 145, “Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statements No. 13, and Technical Corrections as of April 2002,” in 2003 we reported the amount of the discount as other income in our consolidated statement of operations and its adoption resulted in a reclassification of this discount from extraordinary gains (losses) from the extinguishment of debt to other income (expense) in our consolidated statement of operations for the year ended December 31, 2002.

(b) 5% Convertible Subordinated Notes Due 2004

As of December 31, 2003, we had $0.7 million principal amount outstanding of our 5% Convertible Subordinated Notes that mature on December 15, 2004. Interest on these notes is due and payable semiannually on June 15 and December 15. The notes are convertible, at the option of the holder, at a conversion price of $76.14 per share. The 5% Convertible Subordinated Notes are redeemable, in whole or in part at our option, at 100.71% of par.

(c) 8% Secured Convertible Notes Due 2006

During 2003, we purchased $30.2 million of the 8% Secured Convertible Notes due 2006 ("8% Secured Convertible Notes"), representing the entire outstanding principal amount.

The 8% Secured Convertible Notes were convertible into shares of our common stock at the rate of $15.00 per share and were guaranteed by our principal operating subsidiaries and were secured by a pledge of our assets. Interest on these notes was due and payable semiannually.

On December 23, 2002, we amended certain provisions of the September 2001 restructuring agreement with AOL. As a consequence of the amendment and our purchase of $4.1 million of the 8% Secured Convertible Notes in the fourth quarter of 2002, we recorded a gain of $28.9 million from the decrease in the future accrued interest relating to the 8% Secured Convertible Notes. This gain was reflected as a $28.9 million reduction in long-term debt. The adoption of SFAS 145 resulted in a reclassification of this gain from extraordinary gains (losses) from the extinguishment of debt to other income (expense) in our consolidated statement of operations for the year ended December 31, 2002. As a further consequence, we began recording the interest expense associated with the 8% Secured Convertible Notes in our consolidated statement of operations.

(d) Senior Credit Facility

On October 4, 2002, our principal operating subsidiaries retired, prior to maturity, all of the debt outstanding under the Senior Credit Facility Agreement between the subsidiaries and MCG Finance Corporation. As a result of the retirement of the debt under the Senior Credit Facility Agreement, the pledge of assets and the restrictions and covenants under the Senior Credit Facility Agreement were terminated and we incurred a non-cash charge to earnings of $1.1 million, reflecting the acceleration of the amortization of certain deferred finance charges and fees. The adoption of SFAS 145 resulted in a reclassification of this charge from extraordinary gains (losses) from the extinguishment of debt to other income (expense) in our consolidated statement of operations for the year ended December 31, 2002.

(e) Capital Leases

During 2003, we entered into a non-cancelable capital lease agreement for upgrades to our customer data storage equipment. Approximately $3.4 million was outstanding under this agreement at December 31, 2003. Total assets under this lease agreement are approximately $3.4 million as of December 31, 2003. The lease is repayable in 36 monthly installments, which includes interest based on an annual percentage rate of approximately 2%.

(f) Minimum Annual Payments

As of December 31, 2003, the required minimum annual principal payments of long-term debt obligations, including capital leases, for each of the next five fiscal years is as follows (in thousands):

Year Ended December 31,	
2004	$ 16,806
2005	1,131
2006	1,152
2007	29,508
2008	--
	$48,597

NOTE 6. RELATED PARTY TRANSACTION

We had a note receivable with one of our officers with a balance of $1.0 million as of December 31, 2002 for relocation and construction of a new residence in Florida. The note receivable bore interest at 6.25% and the principal balance together with unpaid accrued interest was payable to us in November 2004. The note was collateralized by the new residence. In 2003, the note was paid in full.

NOTE 7. STOCKHOLDERS' EQUITY

(a) Reverse Stock Split

Our stockholders approved a one-for-three reverse stock split of our common stock, effective October 15, 2002, decreasing the number of common shares authorized from 300 million to 100 million. All applicable references to the number of shares of common stock and per share information, stock option data and market prices have been restated to reflect this reverse stock split.

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(b) Stockholders Rights Plan

On August 19, 1999, we adopted a Stockholders Rights Plan designed to deter coercive takeover tactics and prevent an acquirer from gaining control of us without offering a fair price to all of our stockholders. Under the terms of the plan, preferred stock purchase rights were distributed as a dividend at the rate of one right for each of our shares of Common Stock held as of the close of business on August 30, 1999. Until the rights become exercisable, Common Stock issued by us will also have one right attached. Each right will entitle holders to buy one three-hundredth of a share of our Series A Junior Participating Preferred Stock at an exercise price of $165. Each right will thereafter entitle the holder to receive upon exercise Common Stock (or, in certain circumstances, cash, property or other securities of us) having a value equal to two times the exercise price of the right. The rights will be exercisable only if a person or group acquires beneficial ownership of 20% or more of Common Stock or announces a tender or exchange offer which would result in such person or group owning 20% or more of Common Stock, or if the Board of Directors declares that a 15% or more stockholder has become an "adverse person" as defined in the plan.

We, except as otherwise provided in the plan, will generally be able to redeem the rights at $0.001 per right at any time during a ten-day period following public announcement that a 20% position in us has been acquired or after our Board of Directors declares that a 15% or more stockholder has become an "adverse person." The rights are not exercisable until the expiration of the redemption period. The rights will expire on August 19, 2009, subject to extension by the Board of Directors.

(c) Treasury Stock

In 2003, we purchased 1,315,789 of our common shares from America Online, Inc. at an aggregate price of $5.0 million.

NOTE 8. STOCK OPTIONS, WARRANTS AND RIGHTS

(a) Stock Based Compensation Plan

Incentive stock options, non-qualified stock options and other stock based awards may be granted by us to employees, directors and consultants under the 2003 Long Term Incentive Plan (“2003 Plan”), 2000 Long Term Incentive Plan ("2000 Plan"), 1998 Long Term Incentive Plan ("1998 Plan") and otherwise in connection with employment and to employees under the 2001 Non-Officer Long Term Incentive Plan ("2001 Plan"). Generally, the options vest over a three-year period and expire ten years from the date of grant. At December 31, 2003: 405,000; 14,232; 541; and 15,556 shares of common stock were available under the 2003 Plan, 2001 Plan, 2000 Plan, and 1998 Plan, respectively, for possible future issuances. The exercise price of the options is 100% of the market value of the common stock on the grant date.

Stock options granted in 2003 generally have contractual terms of 10 years. The options granted to employees have an exercise price equal to the fair market value of the stock at grant date. The vast majority of options granted in 2003 vest one-third each year, beginning on the first anniversary of the date of grant.

Information with respect to options under our plans is as follows:

	Options Shares	Exercise Price Range Per Share	Weighted Average Exercise Price
Outstanding, December 31, 2000	5,023,106	$2.64-$51.75	$ 25.80
Granted	365,733	$0.99-$5.94	$ 2.58
Exercised	--	--	--

Cancelled	(2,912,700)	$4.02-$51.75	$34.02
Outstanding, December 31, 2001	2,476,139	$0.99-$47.64	$12.72
Granted	2,248,686	$1.11-$11.91	$1.78
Exercised	(250,906)	$0.99-$7.88	$2.50
Cancelled	(288,218)	$1.26-$47.64	$21.66
Outstanding, December 31, 2002	4,185,701	$1.11-$48.54	$6.84
Granted	1,873,171	$3.70-$14.35	$10.33
Exercised	(509,149)	$0.99-$15.75	$2.34
Cancelled	(112,616)	$1.38-$30.18	$12.48
Outstanding, December 31, 2003	5,437,107	$0.99-$47.63	$8.35

The following table summarizes options exercisable at December 31, 2003, 2002 and 2001:

	Option Shares	Exercise Price Range Per Share	Weighted Average Exercise Price
2001	1,285,508	$2.64-$47.64	$16.74
2002	2,942,999	$0.99-$48.54	$6.84
2003	2,939,893	$0.99-$47.63	$7.99

The following table summarizes the status of stock options outstanding at December 31, 2003:

Range of Exercise Prices	Number Outstanding at December 31, 2003	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (years)	Number Exercisable at December 31, 2003	Weighted Average Exercise Price
$0.99 to $10.31	2,701,243	$3.12	6.5	1,874,437	$2.20
$10.32 to $14.35	2,355,699	$11.57	9.0	685,291	$14.11
$14.36 to $21.00	150,058	$19.70	5.2	150,058	$19.70
$21.01 to $30.00	134,998	$28.16	2.8	134,998	$28.16
$30.01 to $47.63	95,109	$30.94	5.4	95,109	$30.94

The weighted average estimated fair values of the stock options granted during the years ended December 31 2003, 2002 and 2001 based on the Black-Scholes option pricing model were $7.79, $2.34, and $1.71, respectively. The fair value of stock options used to compute pro forma net income (loss) and basic and diluted earnings (loss) per share disclosures is the estimated fair value at grant date using the Black-Scholes option-pricing model with the following assumptions:

Assumption	2003	2002	2001
Expected Term	5 years	5 years	5 years
Expected Volatility	98.63%	98.13%	78.95%
Expected Dividend Yield	--%	--%	--%
Risk-Free Interest Rate	3.15%	4.33%	5.92%

(b) Warrants

Warrants to purchase an aggregate of 290,472 shares of our common stock at an exercise price of $6.30 per share and expiring August 2005 were outstanding at December 31, 2003. In connection with a credit facility agreement with a lender and certain consulting services that the lender was to provide to us, we issued warrants to the lender as follows: in August 2000, a warrant for 100,000 shares of our common stock, at an exercisable price of $14.19 per share and expiring August 2007; in October 2000 a warrant for 50,000 shares of our common stock, at an exercise price of $13.08 per share and expiring October 20, 2005; in August 2001, a warrant for 50,000 shares of our common stock, at an exercise price of $2.04 per share and expiring August 16, 2006.

NOTE 9. INCOME TAXES

A reconciliation of the Federal statutory rate to the (benefit) for income taxes is as follows:

	Year Ended December 31,		
	2003 (Restated)	2002	2001
Current income tax expense:			
Federal	$ 1,032	$ --	$ --
State	2,355	--	--
	3,387	--	--
Deferred income tax expense (benefit):			
Federal	(17,206)	(22,300)	--
State	(6,205)	--	--
	(23,411)	(22,300)	--
Total (benefit) for income taxes	$ (20,024)	$ (22,300)	$ --

Deferred tax assets and liabilities at December 31, 2003 and 2002 are comprised of the following elements:

	Year Ended December 31,	
	2003 (Restated)	2002
Deferred Tax Assets		
Net operating loss carry-forwards	$ 77,908	$ 104,032
Amortization	--	1,558
Allowance for uncollectible accounts	3,809	3,250
Warrants issued for compensation	1,051	1,070
Accruals not currently deductible	562	1,317
Net capital loss carry-forwards	3,119	8,875
Alternative minimum tax credit carryforward	1,204	--
Deferred tax assets	87,653	120,102
Less valuation allowance	(14,760)	77,591
Net deferred tax assets	$ 72,893	$ 42,511
Deferred Tax Liabilities		
Depreciation and amortization	$ 16,881	$ 17,386
Deductions not currently expensed	1,731	2,825
Revenues not currently taxed	397	--
Deferred tax liabilities	$ 19,009	$ 20,211

A reconciliation of the Federal statutory rate to our effective tax rate is as follows:

	Year Ended December 31,		
	2003 (Restated)	2002	2001
Federal income taxes (benefit) computed at the statutory rate	35.0%	35.0%	(35.0)%
Increase (decrease) in income taxes resulting from:			
State income taxes less Federal benefit	4.0	0.0	0.0
Valuation allowance changes affecting the provision for income taxes	(71.4)	(64.8)	35.0
Total provision (benefit) for income taxes	(32.4)%	(29.8)%	--%

At December 31, 2003 and 2002, management evaluated the deferred tax asset valuation allowance and determined that portions of the allowance should be reversed. The 2003 and 2002 evaluations considered profitability of the business, the ability to utilize these deferred tax assets against future profitable amounts and possible restrictions on use due to provisions of the Internal Revenue Code Section 382. Based on information currently available to us, the change of ownership percentage subject to Section 382 was approximately 25% for the applicable three-year testing period.

We have not reversed the deferred tax valuation allowance for a $22.9 million deduction claimed in the 1996 year, which is currently contested by the Internal Revenue Service, $8.9 million in capital loss carryforwards that are expected to expire, and $60.2 million in state net operating loss carryforwards that are expected to expire before realization.

After consideration of each of these factors, we reversed deferred tax asset valuation allowances of $50.6 million and $22.3 million for 2003 and 2002, respectively.

In 2003, we had federal net operating loss carryforwards which are scheduled to expire as follows:

2011	$ --
2012	--
2018	91,954
2019	43,161
2020 and thereafter	55,892
	$ 191,007

NOTE 10. AOL AGREEMENTS

In September 2001, we restructured our financial obligations with America Online, Inc., or AOL, that arose under the Investment Agreement entered into on January 5, 1999 and, effective September 30, 2001, also ended our marketing relationship with AOL. In connection with the AOL restructuring, we entered into with AOL a restructuring and note agreement pursuant to which we issued to AOL $54.0 million principal amount of our 8% Secured Convertible Notes and 1,026,209 additional shares of our common stock, after which AOL held a total of 2,400,000 shares of common

stock. We agreed to provide certain registration rights to AOL in connection with the shares of common stock issued to it by us.

In addition to the restructuring of the financial obligations discussed above, we agreed with AOL, in a further amendment to our marketing agreement in September 2001, to discontinue, effective as of September 30, 2001, our marketing relationship under the marketing agreement. AOL, in lieu of any other payment for the early discontinuance of the marketing relationship, paid us $20 million by surrender and cancellation of $20 million principal amount of our 8% Secured Convertible Notes delivered to AOL as discussed above, thereby reducing the outstanding principal amount of our 8% Secured Convertible Notes to $34 million.

In accordance with SFAS No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructurings," the AOL restructuring transaction was accounted for as a troubled debt restructuring. We combined all liabilities due AOL at the time of the restructuring agreement, including the contingent redemption feature of the warrants with a value of $34.2 million and the contingent redemption feature of the common stock with a value of $54.0 million. The total liability of $88.2 million was reduced by the fair value of the 1,026,209 incremental shares provided to AOL of $1.4 million and cash paid in connection with the AOL restructuring of $3.5 million. Since the remaining value of $83.3 million was greater than the future cash flows to AOL of $66.4 million, the liability was written down to the value of the future cash flows due to AOL and an extraordinary gain of $16.9 million was recorded in the third quarter of 2001. As a result of this accounting treatment, we recorded no interest expense associated with these convertible notes during 2001 and 2002 in our statements of operations.

Under the terms of the investment agreement, we agreed to reimburse AOL for losses AOL may incur on the sale of certain shares of our common stock. In addition, AOL also had the right to require us to repurchase warrants held by AOL. Upon the occurrence of certain events, including material defaults by us under our AOL agreements and our "change of control", we could have been required to repurchase for cash all of the shares held by AOL for $78.3 million ($57 per share), and the warrants for $36.3 million. We originally recorded the contingent redemption value of the common stock and warrants at $78.3 and $36.3 million, respectively, with a corresponding reduction in additional paid-in capital. In connection with the implementation of EITF 00-19, the contingent redemption feature of the common stock and warrants were recorded as a liability at their fair values of $53.5 and $32.3 million, respectively, as of June 30, 2001. The increase in the fair value of these contingent redemption instruments from issuance on January 5, 1999 to June 30, 2001 was $36.8 million, which has been presented as a cumulative effect of a change in accounting principle in the statement of operations for the year ended December 31, 2001. For 2001, we recorded an unrealized loss of $2.4 million on the increase in the fair value of the contingent redemption instruments, which was reflected in other (income) expense on the statement of operations. As discussed above, these contingent redemption instruments were satisfied through the restructuring agreement entered into with AOL in September 2001.

In February 2002, by letter agreement, AOL agreed, subject to certain conditions, to waive certain rights that it had under the restructuring agreement with respect to the restructuring of our existing 4-1/2% and 5% Convertible Subordinated Notes. Under the letter agreement, we paid AOL approximately $1.2 million as a prepayment on the 8% Secured Convertible Notes, approximately $0.7 million of which was credited against amounts we owed AOL under the letter agreement for cash payments in the restructuring of these other notes. We complied with the various conditions of the letter agreement and did not owe AOL any additional payments related to this restructuring of its other notes.

In December 2002, by letter agreement, we amended certain provisions of the restructuring agreement with AOL. Pursuant to this amendment, the maturity date for the 8% Secured Convertible Notes issued under the restructuring agreement was advanced to September 19, 2006 from 2011, and our right to elect to pay a portion of the interest on the 8% Secured Convertible Notes in kind rather than in cash was eliminated. This amendment also provided that certain limitations on the purchase of our outstanding subordinated indebtedness and common stock were amended, to permit us, through September 30, 2003, to: (i) repurchase outstanding subordinated indebtedness provided we do not pay more than 80% of the face amount and, for every dollar used to repurchase subordinated indebtedness, we repurchase $0.50 of principal amount of 8% Secured Convertible Notes from AOL; and (ii) purchase shares of our common stock, provided we purchase the shares at or below market value and we concurrently purchase an equal number of shares of the common stock from AOL. The aggregate amount that we may utilize with respect to both the repurchase of subordinated indebtedness and of common stock cannot exceed $10 million.

As a consequence of this amendment in December 2002 and the repurchase of $4.1 million of our 8% Secured Convertible Notes in the fourth quarter of 2002, we recorded a non-cash gain of $28.9 million from the decrease in the future accrued interest relating to our 8% Secured Convertible Notes, which was reflected as a $28.9 million reduction in long-term debt. As a further consequence, we began recording the interest expense associated with the 8% Secured Convertible Notes on our statements of operations.

The restructuring agreement provided that the investment agreement, the security agreement securing our obligations under the investment agreement and the existing registration rights agreement with AOL were terminated in their entirety and the parties were released from any further obligation under these agreements.

In 2003, we repurchased $30.2 million of the 8% Secured Convertible Notes due 2006. In addition, we concurrently purchased from AOL the 1,315,789 shares of our common stock held by AOL for an aggregate price of $5 million.

NOTE 11. SUPPLEMENTAL CASH FLOW INFORMATION

	2003	2002	2001
Supplemental disclosure of cash flow information:			
Cash paid during the year for interest	$ 9,930	$ 6,252	$ 5,620
Cash paid during the year for taxes	1,980	--	--
Supplemental schedule of non-cash investing and financing activities:			
Acquisition of equipment under capital lease obligations	3,392	--	2,145
Interest expense paid in additional principal	--	2,824	--
Issuance of warrants for services	--	--	77
Contingent redemptions exchanged for convertible debt	--	--	32,400
Acquisitions:			
Fair value of assets acquired	--	--	835
Goodwill	--	--	54
Less: liabilities assumed	--	--	(889)
Acquisitions, net cash acquired	--	--	--
Cumulative effect of accounting change attributed to implementation of EITF 00-19 for the contingent redemption feature of common stock and warrants:			
Increase in additional paid-in capital	--	--	65,617
Net change in contingent redemption value of warrants and common stock	--	--	(28,780)
Cumulative effect of accounting change	$ --	$ --	$ 36,837

NOTE 12. EMPLOYEE BENEFIT PLANS

We sponsor a defined contribution pension plan (the “Plan”). The Plan qualifies as a deferred salary arrangement under Section 401(k) of the Internal Revenue Code. Eligible employees may contribute up to 15% of their compensation (subject to Internal Revenue Code limitations). The Plan allows employees to choose among a variety of investment alternatives. We are not required to contribute to the Plan. During the years ended December 31, 2003, 2002 and 2001, we elected to contribute $125,000, $131,000 and $108,000 to the Plan, respectively.

NOTE 13. PER SHARE DATA

Basic earnings per common share is calculated by dividing net income by the average number of common shares outstanding during the year. Diluted earnings per common share is calculated by adjusting outstanding shares, assuming conversion of all potentially dilutive stock options, warrants and convertible bonds. Earnings per share are computed as follows (in thousands):

	Year Ended December 31,		
	2003 (Restated)	2002	2001
Income (loss) before cumulative effect of an accounting change	$ 81,817	$ 97,062	$ (187,830)
Cumulative effect of an accounting change	--	--	(36,837)
Income available to common stockholders used to compute basic income (loss) per share	$ 81,817	$ 97,062	$ (224,667)
Interest expense on convertible bonds	(1)	18	--
Income available for common stockholders after assumed conversion of dilutive securities used to compute diluted income (loss) per share	$ 81,816	$ 97,080	$ (224,667)
Weighted average number of common shares outstanding used to compute basic income (loss) per share	26,376	27,253	26,414
Effect of dilutive securities*:			
Stock options and warrants	1,233	1,347	--
8% Secured convertible bonds due 2006	--	2,010	--
5% Convertible subordinated notes due 2004	9	--	--
8% Senior convertible subordinated notes due 2007	188	188	--
Weighted average number of common and common equivalent shares outstanding used to compute diluted income (loss) per share	27,806	30,798	26,414
Income (loss) per share - Basic:			
Income (loss) before cumulative effect of an accounting change per share	$ 3.10	$ 3.56	$ (7.11)
Cumulative effect of an accounting change per share	--	--	(1.40)
Net income (loss) per share	$ 3.10	$ 3.56	$ (8.51)
Weighted average common shares outstanding	26,376	27,253	26,414
Income (loss) per share - Diluted:			
Income (loss) before cumulative effect of an accounting change per share	$ 2.94	$ 3.15	$ (7.11)
Cumulative effect of an accounting change per share	--	--	(1.40)
Net income (loss) per share	$ 2.94	$ 3.15	$ (8.51)
Weighted average common and common equivalent shares outstanding	27,806	30,798	26,414

* The diluted share basis for the years ended December 31, 2003, 2002 and 2001 excludes options and warrants to purchase 1.3 million, 1.7 million and 3.0 million shares of common stock, respectively. The diluted share basis for the years ended December 31, 2002 and 2001 excludes convertible bonds that are convertible into 9 thousand and 3.3 million shares of common stock, respectively, due to their antidilutive effect.

NOTE 14. SUBSEQUENT EVENTS

In 2004, through February 27, 2004, we have (i) acquired an additional $15 million of our 12% Senior Subordinated Notes, leaving $25.7 million principal amount of our 12% Senior Subordinated Notes outstanding, and (ii) committed to redeem on April 20, 2004, an additional $15 million of our 12% Senior Subordinated Notes.

NOTE 15. QUARTERLY FINANCIAL DATA (UNAUDITED)

The consolidated statements of operations for the year ended December 31, 2003 and each quarter have been restated as follows to reflect these items discussed in Note 16.

	Quarter Ended			
(In thousands, except per share data)	**March 31,**	**March 31,**	**June 30,**	**June 30,**
2003 (1)	As Originally Reported	As Restated	As Originally Reported	As Restated
Revenues	$ 87,843	$ 88,202	$ 93,748	$ 93,906
Operating income	15,179	15,538	19,027	19,185
Net income	9,126	9,343	10,675	10,771
Net income per share - Basic	0.35	0.35	0.41	0.41
Net income per share - Diluted	0.32	0.32	0.37	0.37

	Quarter Ended			
(In thousands, except per share data)	**September 30,**	**September 30,**	**December 31,**	**December 31,**
2003 (1)	As Originally Reported	As Restated	As Originally Reported	As Restated
Revenues	$ 99,929	$ 100,178	$ 101,143	$ 101,407
Operating income	17,620	$ 17,869	13,432	13,696
Net income	51,566	54,102	7,094	7,601
Net income per share - Basic	1.96	2.05	0.27	0.29
Net income per share - Diluted	1.74	1.88	0.25	0.27

	Quarter Ended			
(In thousands, except per share data) **2002**	**March 31,**	**June 30,**	**September 30,**	**December 31,**
Revenues	$ 79,447	$ 77,673	$ 79,133	$ 81,254
Operating income	10,322	12,231	15,753	16,293
Net income	8,130	9,417	13,378	66,137
Net income per share - Basic	0.30	0.35	0.49	2.42
Net income per share - Diluted	0.28	0.30	0.42	2.10

The consolidated balance sheet at December 31, 2003 and at the end of each quarter 2003 have been restated as follows to reflect these items discussed in Note 16.

	Quarter E		
(In thousands)			
2003	March 31, As Originally Reported	March 31, As Restated	June 30, As Originally Reported
Deferred tax assets			
Current	$ 16,765	$ 16,623	$ 10,653
Long-term	--	--	--
Goodwill	19,503	19,503	19,503
Total assets	178,051	180,053	169,318
Sales, use and excise tax	11,772	11,412	12,794
Total liabilities	150,448	152,233	130,554
Total stockholders' equity	27,603	27,820	38,764

(1) Restated as discussed in Note 16.

NOTE 16. RESTATEMENTS

May 7, 2004 Restatement

On May 7, 2004, we revised our consolidated balance sheet as of December 31, 2003 and related disclosures in Note 5 to reflect the change in classification of $15 million of our 12% Senior Subordinated Notes from long-term debt to current portion of long-term debt. The restatement is the result of our commitment pursuant to a notice to holders on November 5, 2003 (see Note 5) to redeem $15 million principal amount of our 12% Senior Subordinated Notes on January 5, 2004, which resulted in a change of maturity of such principal amount to the noticed redemption date.

March 28, 2005 Restatement

On March 28, 2005, we further revised our consolidated financial statements to correct for the following errors:

(a) Due to a classification error in our general ledger, we incorrectly recorded certain customer fee revenues to the consolidated balance sheets for the four quarters of 2003 and for the year ended December 31, 2003 as sales, use and excise tax liabilities. These customer fee revenues aggregated $1.0 million for the full year 2003. These customer fees have now been appropriately recorded to revenues in the consolidated statement of operations for the year ended December 31, 2003 and in the unaudited quarterly periods for 2003.
(b) In connection with the preparation of the financial statements for 2004, we determined that in our calculations since the third quarter of 2003 we had not incorporated the tax benefits associated with the assumed exercise of employee stock options. As a result, fully diluted shares outstanding were over-reported and income per fully diluted share was understated in those periods.
(c) In connection with the preparation of the financial statements for the first and second quarters of 2004, we identified errors in the computation of the deferred tax assets recognized in the third quarter of 2003 as follows: (i) failure to deduct state income tax expense from federal taxable income resulted in the deferred tax benefit as originally reported for the year ended December 31, 2003 and the unaudited third quarter of 2003 being understated by $0.9 million and (ii) failure to complete the appropriately detailed analysis of our deferred tax assets relating to state net operating loss carryforwards resulted in the deferred tax benefit as originally reported for the year ended December 31, 2003 and the unaudited third quarter of 2003 being understated by $1.7 million. In February 2005, we determined that we improperly corrected for the errors in the deferred tax computations through an adjustment to the effective tax rate for 2004 rather than through the restatement of our prior period financial statements.
(d) In connection with the release of the valuation allowance in the third quarter 2003, $6.5 million of deferred tax assets associated with acquired net operating loss carryforwards were realizable and should have been, recorded as a deferred tax asset. Originally, we believed this deferred tax asset was limited due to provisions of the Internal Revenue Code Section 382. This error resulted in deferred tax assets being understated and goodwill being overstated in each of the periods beginning in the third quarter 2003.

As a result of these restatements, certain originally reported amounts in the consolidated statements of operations for the year ended December 31, 2003 have been restated as follows (in thousands, except per share data):

Year Ended December 31, 2003	As Originally Reported	Adjustments	As Restated
Revenues	$ 382,663	$ 1,030	$ 383,693
Operating income	65,258	1,030	66,288
Provision (benefit) for income taxes	(17,697)	(2,327)	(20,024)
Net income	78,461	3,356	81,817

Net income per share - Basic	2.97	0.13	3.10
Net income per share - Diluted	2.75	0.19	2.94
Weighted average common and common equivalent shares outstanding - Diluted	28,514	(708)	27,806

As a result of these restatements, certain originally reported amounts in the consolidated balance sheet at December 31, 2003 has been restated as follows (in thousands):

At December 31, 2003	**As Originally Reported**	**Adjustments**	**As Restated**
Deferred tax assets			
Current	$ 24,605	$ --	$ 24,605
Long-term	40,543	7,745	48,288
Goodwill	19,503	(6,490)	13,013
Total assets	245,923	1,255	247,178
Sales, use and excise tax	14,551	(1,030)	13,521
Total liabilities	146,136	(2,101)	144,035
Total stockholders' equity	99,787	3,356	103,143

As a result of these restatements, certain originally reported amounts for cash flows from operating activities in the consolidated statement of cash flows have been adjusted as follows (in thousands):

At December 31, 2003	**As Originally Reported**	**Adjustments**	**As Restated**
Cash flows from operating activities:			
Net Income	$ 78,461	$ 3,356	$ 81,817
Deferred income taxes	(19,740)	(3,669)	(23,409)
Changes in assets and liabilities:			
Sales, use and excise taxes	3,112	(1,030)	2,082
Other current liabilities and accrued compensation	773	1,343	2,116
Net cash provided by operating activities	73,166	--	73,166

ITEM 9A. CONTROLS AND PROCEDURES.

Disclosure Controls and Procedures—We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), as appropriate, to allow timely decisions regarding required disclosure.

We carried out an evaluation under the supervision and with the participation of our management, including the CEO and CFO, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of December 31, 2003. Based upon this evaluation, our CEO and the CFO

concluded that, for the reasons described below, our disclosure controls and procedures were not effective as of December 31, 2003.

We have restated our previously issued consolidated financial statements for the year ended December 31, 2003 and the four quarters of 2003 and will restate the first three quarters of 2004. This restatement was primarily the result of the following material weaknesses:

1. We did not maintain effective controls over the application of generally accepted accounting principles related to the financial reporting process for complex transactions. Specifically, we did not have personnel who possess sufficient depth, skills and experience in accounting for and review of complex transactions in the financial reporting process to ensure that complex transactions were accounted for in accordance with generally accepted accounting principles. This control deficiency resulted in the restatement of our revenues and sales, use and excise tax liability for each of the quarters in 2003 and year ended December 31, 2003.

2. We did not maintain effective controls over sales, use and excise tax liabilities. Specifically, our reconciliation and review procedures with respect to sales, use and excise tax liability that we collect and remit did not identify that certain customer fee revenue had been incorrectly recorded in the sales, use and excise tax general ledger account. This control deficiency resulted in the restatement of our revenues and sales, use and excise tax liability for each of the quarters in 2003 and the year ended December 31, 2003.

The restatements, described above, were for matters related to (a) the recognition in revenue in the four quarters 2003 and year ended December 31, 2003 of certain customer fees previously recorded in those periods as increases in current liabilities; (b) the calculation of outstanding diluted weighted average common and common equivalent shares in the third and fourth quarters 2003 and the year ended December 31, 2003 to reflect the inclusion of assumed tax benefits in the proceeds used to repurchase shares in the application of the treasury stock method of accounting for outstanding options; (c) for the third and fourth quarters 2003 and the year ended December 31, 2003, a correction in the calculation of net operating losses utilized in 2003 and in the calculation of state deferred tax assets; and (d) the recording, beginning in the third quarter 2003 and for the year ended December 31, 2003, of a deferred tax asset associated with acquired net operating loss carryforwards. Refer to Notes 15 and 16 to the Consolidated Financial Statements for further information regarding this restatement, including the effect of the restatement for each of the four quarters of 2003 and the year ended December 31, 2003.

To address these material weaknesses, subsequent to December 31, 2003, we have taken the following actions:

1. Engaging outside contractors with technical and accounting related expertise to assist in the preparation of the income tax provision and related work papers. We are also implementing controls to assure accurate data is provided to, and that we review and agree with the conclusions of, outside contractors.

2. Outside contractors with technical accounting capabilities have been and will be retained to the extent an issue is sufficiently complex and outside the technical accounting capabilities of our personnel.

3. We have redesigned the account reconciliation process for sales, use and excise tax liabilities. Our Controller will increase the depth of review of the account reconciliation and our Chief Accounting Officer will confirm that established review processes are being adhered to.

We are in the process of developing procedures for the testing of these controls to determine if the material weaknesses have been remediated. We will continue the implementation of policies, processes and procedures regarding the review of complex transactions. Management belives that our controls and procedures will continue to improve as a result of the further implementation of these measures.

The changes to internal control over financial reporting were implemented subsequent to the quarter ended December 31, 2003. There were no changes in our internal control over financial reporting that occurred during the quarter ended December 31, 2003 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K.

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

1. Consolidated Financial Statements:

The Consolidated Financial Statements filed as part of this report are listed in the "Index to Consolidated Financial Statements" in Item 8.

2. Consolidated Financial Statement Schedule:

The Consolidated Financial Statement Schedule filed as part of this report is listed in the "Index to S-X Schedule."

Schedules other than those listed in the accompanying Index to S-X Schedule are omitted for the reason that they are either not required, not applicable or the required information is included in the Consolidated Financial Statements or notes thereto.

TALK AMERICA HOLDINGS, INC. AND SUBSIDIARIES

INDEX TO S-X SCHEDULE

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SCHEDULE II -- VALUATION AND QUALIFYING ACCOUNTS
(In Thousands)

DESCRIPTION DEDUCTIONS	BALANCE AT BEGINNING OF PERIOD	ADDITIONS CHARGED TO COSTS AND EXPENSES	DEDUCTIONS FOR WRITE-OFFS	BALANCE AT END OF PERIOD
Year Ended December 31, 2003:				
Reserve and allowances deducted from asset accounts:				
Allowance for uncollectible accounts	$ 7,821	$ 11,599	$ (10,006)	$ 9,414
Year Ended December 31, 2002:				
Reserve and allowances deducted from asset accounts:				
Allowance for uncollectible accounts	$ 46,404	$ 9,365	$ (47,948)	$ 7,821
Year Ended December 31, 2001:				
Reserve and allowances deducted from asset accounts:				
Allowance for uncollectible accounts	$ 29,429	$ 92,778	$ (75,803)	$ 46,404

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EXHIBIT NUMBER	DESCRIPTION
3.1	Our composite form of Amended and Restated Certificate of Incorporation, as amended through October 15, 2002 (incorporated by reference to Exhibit 3.2 to our Current Report on Form 8-K, dated October 16, 2002).
3.2	Our Bylaws (incorporated by reference to Exhibit 3.2 to our registration statement on Form S-1 (File No. 33-94940)).
3.3	Certificate of Designation of Series A Junior Participating Preferred Stock dated August 27, 1999 (incorporated by reference to Exhibit A to Exhibit 1 to our registration statement on Form 8-A (File No. 000-26728)).
4.1	Specimen of Talk America Holdings, Inc. common stock certificate (incorporated by reference to Exhibit 4.1 to our Annual Report on Form 10-K for the year ended December 31, 2002).
4.2	Form of Warrant Agreement for Elec Communications, Kenneth Baritz, Joel Dupre, Keith Minella, Rafael Scolari, and William Rogers dated August 9, 2000 (incorporated by reference to Exhibit 4.2 to our Annual Report on Form 10-K for the year ended December 31, 2000).
4.3	Form of Warrant Agreement for MCG Credit Corporation dated August 9, 2000 (incorporated by reference to Exhibit 4.3 to our Annual Report on Form 10-K for the year ended December 31, 2000).
4.4	Form of Warrant Agreement for MCG Credit Corporation dated October 20, 2000 (incorporated by reference to Exhibit 4.4 to our Annual Report on Form 10-K for the year ended December 31, 2000).
4.5	Form of Warrant Agreement for MCG Finance Corporation dated October 20, 2000 (incorporated by reference to Exhibit 4.5 to our Annual Report on Form 10-K for the year ended December 31, 2000).
4.6	Indenture dated as of December 10, 1997 between Tel-Save Holdings, Inc. and First Trust of New York, N.A. (incorporated by reference to Exhibit 10.34 to our Annual Report on Form 10-K for the year ended December 31, 1997).
4.7	Indenture dated as of April 2, 2002, between Talk America Holdings, Inc. and Wilmington Trust Company (incorporated by reference to Exhibit 10.69 to our Annual Report on Form 10-K for the year ended December 31, 2001).
4.8	Supplemental Indenture No. 1 dated as of April 2, 2002, between Talk America Holdings, Inc. and Wilmington Trust Company, to the Indenture dated as of April 2, 2002, between Talk America Holdings, Inc. and Wilmington Trust Company (incorporated by reference to Exhibit 10.70 to our Annual Report on Form 10-K for the year ended December 31, 2001).
4.9	Supplemental Indenture No. 2 dated as of April 2, 2002, between Talk America Holdings, Inc. and Wilmington Trust Company, to the Indenture dated as of April 2, 2002 (incorporated by reference to Exhibit 10.71 to our Annual Report on Form 10-K for the year ended December 31, 2001).
4.10	First Supplemental Indenture dated as of April 2, 2002, between Talk America Holdings, Inc. and U.S. Bank Trust National Association, to the Indenture dated as of September 9, 1997 (incorporated by reference to Exhibit 10.72 to our Annual Report on Form 10-K for the year ended December 31, 2001).

4.11 First Supplemental Indenture dated as of April 2, 2002, between Talk America Holdings, Inc. and U.S. Bank Trust National Association, to the Indenture dated as of December 10, 1997 (incorporated by reference to Exhibit 10.73 to our Annual Report on Form 10-K for the year ended December 31, 2001).

10.1 Employment Agreement with Aloysius T. Lawn, IV dated March 28, 2001 (incorporated by reference to Exhibit 10.1 to our Annual Report on Form 10-K for the year ended December 31, 2000).*

10.2 Employment Agreement with Edward B. Meyercord, III dated January 1, 2004 (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).*

10.3 Indemnification Agreement with Aloysius T. Lawn, IV dated March 28, 2001(incorporated by reference to Exhibit 10.3 to our Annual Report on Form 10-K for the year ended December 31, 2000). *

10.4 Indemnification Agreement with Edward B. Meyercord, III (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003). *

10.5 Tel-Save Holdings, Inc. 1995 Employee Stock Option Plan (incorporated by reference to Exhibit 10.15 to our registration statement on Form S-1 (File No. 33-94940)).*

10.6 Employment Agreement with Gabriel Battista dated January 1, 2004 (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).*

10.7 Indemnification Agreement with Gabriel Battista dated as of December 28, 1998 (incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated January 20, 1999). *

10.8 Stock Option Agreement, dated as of November 13, 1998, with Gabriel Battista (incorporated by reference to Exhibit 10.4 to our Current Report on Form 8-K dated January 20, 1999).*

10.9 Our 1998 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.14 to our Current Report on Form 8-K dated January 20, 1999).*

10.10 2000 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.31 to our Registration Statement on Form S-4 (No. 333-40980)). *

10.11 Form of Non-Qualified Stock Option Agreement, dated December 12, 2000, for each of Gabriel Battista, Aloysius T. Lawn IV and Edward B. Meyercord, III (incorporated by reference to Exhibit 10.40 to our Annual Report on Form 10-K for the year ended December 31, 2000).*

10.12 Rights Agreement dated as of August 19, 1999 by and between the Talk.com Inc. and First City Transfer Company, as Rights Agent (incorporated by reference to Exhibit 1 to our registration statement on Form 8-A (File No. 000-26728)).

10.13 Employment Agreement with Thomas M. Walsh dated as of August 7, 2000 (incorporated by reference to Exhibit 10.1 to our Quarterly Report on Form 10-Q dated November 14, 2000).*

10.14 Indemnification Agreement with Thomas M. Walsh dated as of August 7, 2000 (incorporated by reference to Exhibit 10.2 to our Quarterly Report on Form 10-Q dated November 14, 2000).*

10.15 Non-Qualified Stock Option Agreement with Thomas M. Walsh dated as of August 7, 2000 (incorporated by reference to Exhibit 10.3 to our Quarterly Report on Form 10-Q dated November 14, 2000).*

10.16 Lease by and between Talk.com Holding Corp. and University Science Center, Inc. dated April 10, 2000 (incorporated by reference to Exhibit 10.54 to our Annual Report on Form 10-K for the year ended December 31, 2000).

10.17 Lease by and between The Other Phone Company, dba Access One Communications and University Science Center, Inc. dated December 8, 1999 (incorporated by reference to Exhibit 10.55 to our Annual Report on Form 10-K for the year ended December 31, 2000).

10.18 Restated Access One Communications Corp. 1997 Stock Option Plan (incorporated by reference to Exhibit 4.2 to our registration statement on Form S-8 (File No. 333-52166).*

10.19 Restated Access One Communications Corp. 1999 Stock Option Plan (incorporated by reference to Exhibit 4.3 to our registration statement on Form S-8 (File No. 333-52166).*

10.20 Employment Agreement with Jeffrey Earhart dated October 2, 2001 (incorporated by reference to Exhibit 10.1 to our Quarterly Report on Form 10-Q dated November 14, 2001).*

10.21 Employment Agreement with Warren Brasselle dated March 8, 2000 (incorporated by reference to Exhibit 10.48 to our Annual Report on Form 10-K for the year ended December 31, 2001).*

10.22 Employment Agreement with Timothy Leonard dated March 29, 2002 (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).*

10.23

Sublease Agreement by and between Talk America Inc. and Food Lion, LLC, dated as of November 26, 2003 (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).

10.24 Lease by and between Talk America Inc. and BTS Owners LLC, dated as of July 1, 2003 (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).

10.25 First Amendment, dated as of September 19, 2001, to the Rights Agreement dated as of August 19, 1999, by and between Talk America Holdings, Inc. and First City Transfer Company, as Rights Agent (incorporated by reference to Exhibit 10.9 to our Current Report on Form 8-K filed on September 24, 2001).

10.26 Amendment to Employment Agreement for Warren Brasselle dated May 14, 2002 (incorporated by reference to Exhibit 10.4 to our Quarterly Report on Form 10-Q dated November 14, 2001).*

10.27 Our 2001 Non-Officer Long Term Incentive Plan (incorporated by reference to Exhibit 4.1 to our registration statement on Form S-8 (File No. 333-74820).*

10.28 Indenture of Lease by and between Woodruff Properties and Omnicall, Inc. dated August 1, 1998 (incorporated by reference to Exhibit 10.64 to our Annual Report on Form 10-K for the year ended December 31, 2001).

10.29 Amendment dated February 9, 2001 to the Indenture of Lease by and between Woodruff Properties and Omnicall, Inc. dated August 1, 1998 (incorporated by reference to Exhibit 10.65 to our Annual Report on Form 10-K for the year ended December 31, 2001).

10.30 Lease Agreement by and between Bridge Plaza Partnership and The Furst Group, Inc. dated as of November 4, 1998 (incorporated by reference to Exhibit 10.66 to our Annual Report on Form 10-K for the year ended December 31, 2001).

10.31 Option dated July __, 2001 to Renew the Lease Agreement by and between Bridge Plaza Partnership and The Furst Group, Inc. dates as of November 4, 1998 (incorporated by reference to Exhibit 10.67 to our Annual Report on Form 10-K for the year ended December 31, 2001).

10.32 Office Lease by and between Reston Plaza I and II, LLC and Talk.com, Inc. dated as of April 28, 2000 (incorporated by reference to Exhibit 10.68 to our Annual Report on Form 10-K for the year ended December 31, 2001).

10.33 Our 2003 Long Term Incentive Plan (incorporated by reference to Exhibit B of our Definitive Proxy Statement filed on May 6, 2003).

10.34 Second Amendment to Rights Agreement, dated as of December 13, 2002, to the Rights Agreement dated as of August 19, 1999, by and between Talk America Holdings, Inc., First City Transfer Company and Stocktrans, Inc. (incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on December 13, 2002).

10.35 Lease Agreement by and between Jeffrey M. Baumrucker and Monique M. Baumrucker and Talk America Inc. dated as of July 7, 2003 (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).

10.36 Amendment dated March 10, 2003 to the Indenture of Lease by and between Woodruff Properties and Omnicall, Inc. dated August 1, 1998 (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).

14.1 Code of Ethics (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).

21.1 Our Subsidiaries (previously filed as an Exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003).

23.1 Consent of PricewaterhouseCoopers LLP (filed herewith).

31.1 Certification of Edward B. Meyercord, III Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

31.2 Certification of David G. Zahka Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

32.1 Certification of Edward B. Meyercord, III Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished to the Commission herewith).

32.2 Certification of David G. Zahka Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished to the Commission herewith).

SIGNATURES

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

Date: March 28, 2005

TALK AMERICA HOLDINGS, INC.

By: /s/ Edward B. Meyercord, III
Edward B. Meyercord, III
Chief Executive Officer