HARTE-HANKS 2005
MULTI-FACETED

At the intersection of communications and technology, there's a source of solutions for companies with a wide variety of marketing challenges.

- ▶ A multinational pharmaceutical company needs to tell patients with a specific chronic condition about therapeutic advances made possible by a new medication.
- ▶ A regional restaurant chain needs to drive traffic to 96 individual franchises using distinct messages sent to neighborhood households.
- ▶ A national mortgage brokerage firm needs to persuade potential customers to turn to them for quotes.

Despite their contrasting business needs, these three companies share a single goal: to optimize the return on their marketing investment. Each company turned to Harte-Hanks for marketing solutions customized for their unique challenges. The seasoned professionals of Harte-Hanks helped them get the results they needed for their products and services…and their bottom lines. These firms are just three of the hundreds of clients we help every day to surpass their marketing goals.

The people of Harte-Hanks provide unmatched insight, skill, cutting-edge technology, institutional knowledge and fresh perspectives to help our clients succeed. Whether we design and implement data-based programs that help our clients maximize customer loyalty and prospect conversion, or produce our widely read, cost-effective shopper publications with direct mail circulation in excess of 12 million in California and Florida each week, Harte-Hanks offers knowledge and expertise that translate into bottom-line success.

This annual report is a summary of the many ways we created success for our clients in 2005. And in the process, we achieved record results for our shareholders and stakeholders.

3 A DIRECT AND TARGETED MARKETING LEADER

4 FACETS OF OUR REGIONAL AND GLOBAL SUCCESS

7 A SINGLE CORPORATE MISSION

8 ACHIEVEMENTS

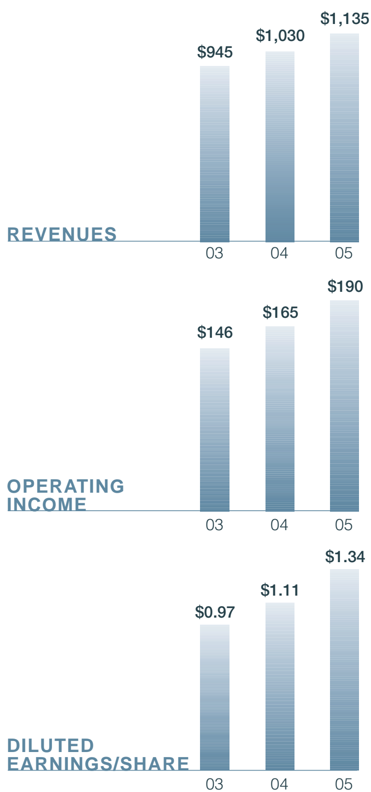
11 2005 FINANCIAL INFORMATION

A DIRECT AND TARGETED MARKETING LEADER

Originally a West Texas newspaper company founded in the 1920s, Harte-Hanks has transformed itself into a leading worldwide direct and targeted marketing company that offers multi-faceted direct marketing solutions and shopper advertising opportunities to a wide range of local, regional, national and international consumer and business-to-business marketers. Our success, and that of our clients, is based on our mastery of marketing and our continual adaptation of new technologies to expand and to refine data-based marketing.

We are well positioned and excel in both of our business lines, shopper publications and direct marketing. These two divisions respond to the targeting needs of our global, national, regional and local clients.

From our more than 40 locations worldwide, Harte-Hanks has built partnerships with clients ranging from small and mid-sized businesses to *Fortune* 1000 companies throughout North America, Europe, South America and the Pacific Rim. How does Harte-Hanks earn clients' trust? With transparency, expertise, efficiency, honesty, strategic intelligence, creativity, and *demonstrable results*.



(In millions, except per share amounts)

FACETS OF OUR REGIONAL AND GLOBAL SUCCESS

Harte-Hanks Shoppers

Two of the nation's largest and most cost-effective shopper publications are Harte-Hanks assets. The *PennySaver* and *The Flyer* are the best-read shopper publications in California and in Florida respectively. Harte-Hanks is North America's largest owner, operator and distributor of shoppers. These weekly publications deliver marketing communications to a circulation of more than 12 million in editions that are targeted geographically, demographically, by lifestyle and even by language.

Our professionals at Harte-Hanks Shoppers sell shopper advertising, produce it, and see it through to delivery. Clients can choose their approach — in the book, front cover, back cover, color, inserts, Web sites or detached cards. There are more than 1,000 separate editions, with average circulation of 12,000. Advertisers can even target neighborhoods within a single edition's area with sub-zone inserts. Advertisements can be submitted as late as three business days before the date they appear in the publication.

In 2005 we launched our new common order entry system which, when completed, will enable advertisers to place an ad in any zone throughout all of our shopper publications with a single entry.

Our shoppers are delivered online with capabilities beyond the print product. Our digital strategy, which emphasizes Web traffic, e-commerce, e-mail, and synergy with the print product, is an exciting approach to linking buyers and sellers.

The *PennySaver* and *The Flyer* are powerful titles. Their respected brand environments are ideal for residential advertisers as well as local, regional and national businesses. They provide successful marketing channels that enable individuals and businesses to reach prospects in their homes in a cost-effective way, because households are highly targeted.

Harte-Hanks Direct Marketing

Harte-Hanks Direct Marketing is in the solutions business. We tailor marketing solutions for the unique challenges faced by each of our clients. We're intimate with the regulatory and industry standards and the benchmarks of our clients' different vertical

FINANCIAL HIGHLIGHTS (in thousands, except per share amount)

	2005	2004	2003
Revenues	$ 1,134,993	$ 1,030,461	$ 944,576
Operating income	$ 190,013	$ 165,295	$ 146,487
Depreciation and amortization	$ 31,345	$ 28,769	$ 30,033
Interest expense	$ 1,957	$ 1,020	$ 855
Net income	$ 114,458	$ 97,568	$ 87,362
Diluted earnings per share	$ 1.34	$ 1.11	$ 0.97
Capital expenditures	$ 28,215	$ 35,146	$ 31,915
Average common and common equivalent shares outstanding — diluted	85,406	87,806	89,982

industries. The depth and range of our expertise ensures that each client is served by a team that's thoroughly familiar with that vertical market. A single client team may include marketing strategists, systems analysts, logistics managers, Web site designers, copywriters and account managers, each experienced in providing solutions for the client's marketing environment. For instance, the specialized knowledge and skills needed to meet the following challenges can be acquired only by horizontal and vertical experience:

- ▶ A retailer wants to generate leads for an online, permission-based marketing program that can grow into a loyalty program.

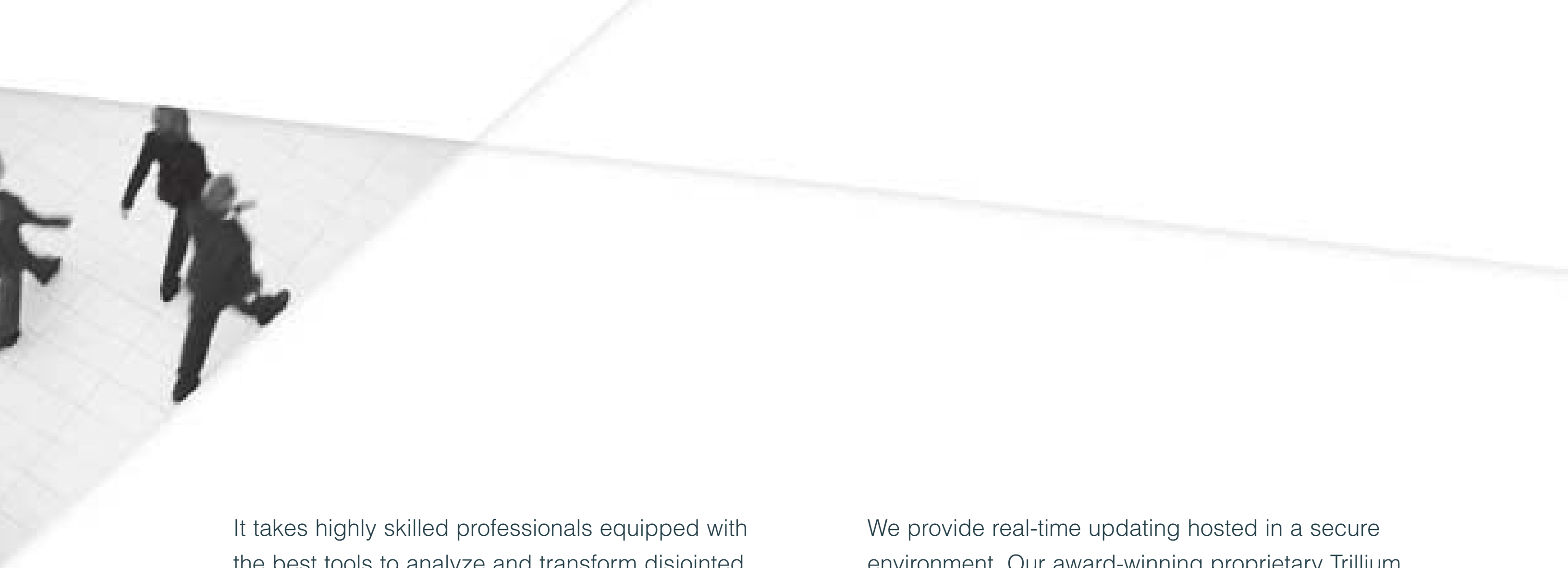
- ▶ A health insurer wants to enroll Medicare recipients in a drug plan by explaining it simply and clearly.

- ▶ An automaker wants to offer multichannel direct marketing programs that its dealers, linking to a single Web site, can customize for delivery to their local target audiences.

- ▶ A technology provider wants to standardize and accelerate its lead generation processes across channels, systems and sources worldwide.

Our professionals who meet these challenges have winning records in marketing for a wide range of verticals. Based throughout the world, they're the brains and muscles of a diverse group of knowledge-intensive operations that mesh to deliver a single outcome: the marketing successes of our clients. We conceptualize what we do with a graphic of five fundamental solution points: ▶ Construct and update the database ▶ Access the data ▶ Analyze the data ▶ Apply the knowledge ▶ Execute the programs.

Across each of these, we tailor solutions specific to the client's evolving market. Once the strategic, data-driven program has been designed and executed, its results are read, analyzed and applied to update the database and refine subsequent marketing programs. The new knowledge enables the cycle to continue more effectively, achieving its goal — increasing the client's return on marketing investment. A true partnership with the client makes this kind of end-to-end relationship possible. Teamwork and expertise are necessary to create strategies that succeed in today's challenging, ever more sophisticated marketplaces.



It takes highly skilled professionals equipped with the best tools to analyze and transform disjointed customer data into patterns that make direct marketing intelligent — and cost-effective for our clients. We can see this when we view the five integrated solution points of direct marketing in more detail: Each involves teams of individuals with different skills who work together for quantifiable results that exceed our clients' expectations.

Constructing and updating the database

To influence future purchase behavior and the customer experience, marketers must understand previous purchase behavior — and clients who need to know partner with Harte-Hanks. We provide our clients with a wealth of customer information by uniquely combining technology, marketing know-how and an understanding of our clients' businesses into tailored database solutions.

Whether a company needs an integrated enterprise-wide view of its customers or wants to improve its multichannel customer communication strategy, Harte-Hanks sets the standard for expertise and strategic execution. We offer thought leadership in marketing and technology, and vertically tailored, pre-built and customized solutions.

We provide real-time updating hosted in a secure environment. Our award-winning proprietary Trillium Software System® and Advanced Data Quality are premier solutions for cleansing and optimizing customer data, and our CI Technology Database™ of business-to-business enterprise and technology data is the world's largest repository of its kind.

Accessing the data

No matter how well-constructed and flexible a database is, the information it contains has value only to the extent that it can be used to solve business problems and improve marketing. Our Allink® solutions, customized for a range of vertical markets such as pharmaceutical, financial, retail and automotive, excel at integrating diverse data-based marketing efforts. Centralizing data from many channels and using best-of-breed access software, Allink enables Harte-Hanks clients to see their customers with a 360-degree view, to facilitate multichannel marketing and to inform all aspects of their business.

Analyzing the data

Our researchers, modelers and analysts provide consultation, campaign support, segmentation and prediction. These professionals improve marketing effectiveness by extracting conclusions from the information generated from data. The insight into behavior patterns that emerges results in smarter targeting and higher return on investment.

Applying the knowledge

This data-based knowledge is put to work in acquiring customers, keeping them loyal, cross-selling, up-selling, extending customer-care services, facilitating merger and acquisition communications, perfecting sales and lead-management systems, and devising promotional campaigns. Harte-Hanks uses the knowledge to conceptualize and design award-winning multichannel initiatives and to refine them in accordance with new insights gained through this interactive process.

Executing the programs

Our front-line teams deliver personalized mail and e-mail campaigns, on-demand production, fulfillment, telemarketing programs, logistics — the full spectrum of direct and interactive marketing services. We are one of the most focused suppliers in each of these areas.

One example of leadership is our highly praised e-mail marketing system, Postfuture. Postfuture offers customized list targeting, scheduling, execution and reporting. It is designed to help facilitate CAN-SPAM and e-mail authentication adherence, assure delivery, and even automate e-marketing programs based on customer transactions.

A SINGLE CORPORATE MISSION

The value of Harte-Hanks is created by our more than 7,000 people. Each of us puts our individual talents and experiences to work every day, responding proactively and flexibly to opportunities and challenges for our clients. Like individual facets that together create a structure of great value, we each play our role in producing results that surpass the client's expectations. That's how Harte-Hanks defines success — as the success of our clients.

To our shareholders

Harte-Hanks delivered strong results in 2005, with record revenue and profits in each quarter. We achieved new heights of performance, in both our Shoppers and Direct Marketing businesses, and a multi-faceted approach was a key to our success — as it will be for years to come. This letter describes the multiple facets, the wins and the groundwork for future success.

First the facets. We are in two dynamic growth businesses. Each of these businesses has a range of competitive advantages that sustains us and provides the fuel for our growth. In Shoppers, we have powerful brands (*PennySaver* and *The Flyer*), a strong readership, a fully vertically integrated operation, many products and therefore many ways to meet customer needs, and a circulation growth strategy that was enhanced in 2005 by the acquisition of *The Flyer,* in Tampa, Florida. In Direct Marketing, Harte-Hanks is a brand that matters — a resource that clients seek for a wide range of direct marketing solutions. Each of our five solution points is best of breed; each has its growth strategy; and together the offerings are even more powerful with even greater potential than the sum of the individual parts. And in both businesses, our people are special.

Our company's employees are terrific all the time. In 2005, we were tested by hurricanes in some unusual ways that did not get a lot of media attention, but affected our business in southern Florida. Our company and individual employees showed generosity in helping people in need during the hurricane season. And they supported each other in a business environment that forced our people to work in compromised space, to relocate to different Harte-Hanks facilities for weeks away from family, and to spend numerous weekends dealing with business challenges. When hurricanes struck our Direct Marketing and Shoppers operations directly, our people worked tirelessly to maintain business continuity — to solve our client challenges. These efforts reflect dedication, commitment and those intangibles that serve to define our unique culture.

For all of 2005, our diluted earnings per share increased to $1.34 on revenues of $1,135.0 million — reflecting increases of 20.7% and 10.1%, respectively. Direct Marketing, comprising 61% of total revenue, experienced revenue gains across-the-board — for the year, each of the vertical markets we track posted growth, including the addition of new logos (clients), a key metric we had set for ourselves. Revenues in Direct Marketing grew by 8.3%, while operating income grew a robust 19.0%. Our Shoppers performance included revenue growth of 13.2% and operating income growth of 9.8%.

The wins in 2005 were widespread. In Shoppers, we extended our growth streak to nine consecutive years. While our circulation increase was smaller than in 2004, we laid the groundwork for significant

expansion in 2006. Our digital strategy was completed in both businesses and we started executing — we are excited about the potential in both businesses. In our Direct Marketing business segment, independent research and ratings of our database service provider (Allink®), data quality software (Trillium Software®) and e-mail service provider (Postfuture®) businesses improved in 2005 (we are among the top providers), and we are well positioned for 2006.

We also integrated the operations of Australia-based Communiqué Direct, which now supports our marketing expansion in Asia-Pacific. To that same end, we also announced our opening of a marketing services outsourcing facility in Manila, the Philippines — with operations there beginning in early 2006. Harte-Hanks has been working, and continues to work, with offshore marketing partners for the past five years — on five continents. This is our first foray in direct ownership of such a facility in Asia. Our Tampa acquisition has been a success both strategically and operationally. We have already expanded circulation in that area and have plans for more in 2006.

We continued to use capital to repurchase shares, a program initiated in 1997. During 2005, we repurchased 4.3 million shares, bringing our total during the past nine years to 43.5 million shares repurchased. Our total capital projects spending in 2005 was $28.2 million, led by spending in product development and enhancement, additional computer and color capacity, common systems and software, and equipment upgrades.

Among corporate directors, Dr. Peter Flawn, who had served our board with dedication and commitment for 20 years, retired. Joining our ranks as an officer was Sloane Levy, who serves as vice president, general counsel and secretary. Two other officers were promoted during the year: Peter Gorman was named executive vice president, and Bill Carman was named senior vice president — both of these appointments reflect their performance leading our Shoppers organizations as well as their corporate service.

Looking forward, the strategy for 2006 includes expanding our international presence in Direct Marketing, growing shopper circulation in both Florida and California, growing our digital offerings, continuing to innovate in both businesses, and continuing to support the most important asset we have — our people.

Specifically, in our two businesses we have many successes and milestones. In Shoppers, here are two:

- New distribution that pushed weekly circulation to more than 12 million in California and Florida, including more than 1 million from *The Flyer* publication in Tampa

- Inclusion of glossy-like pages in our *PennySaver* in San Diego, in a bid to innovate by offering new print advertising formats

In Direct Marketing, we attained:

- New solutions in our Allink database offerings, as well as new means to deliver our Advanced Data Quality data management service to clients
- New industry accolades for a variety of client advertising and marketing campaigns, among them the Hoke Award for the "most courageous solution to a difficult sales/marketing challenge" (an award of the Direct Marketing Association) and the "best practices" award for outsourcing (awarded by the Technology Managers Forum)
- An increased commitment to serve the Asia-Pacific region, to meet client demands and to pursue growth there

Across our company, Harte-Hanks focused on employee training in many important areas, among them management, privacy, security, and integrated products and services. We also initiated a program to cultivate future company leaders, using both recruitment from leading business schools and identification of internal skilled and talented candidates.

Corporate governance and financial integrity remain at our forefront. Pursuant to Section 404 of the Sarbanes-Oxley Act, the Harte-Hanks management team again has certified that our internal controls over financial reporting are adequate, and our external auditor, KPMG LLP, has concurred with this assessment. The Board of Directors and management remain committed to ensure that Harte-Hanks maintains its well-established control-oriented environment as we continue to pursue growth in shareholder value.

2005 provided challenges and opportunities that show how our chief asset — our people — innovate, dedicate and deliver success. They reflect our business, our markets, our clients — they are multi-faceted and resourceful — to help Harte-Hanks make it happen.

RICHARD HOCHHAUSER
President & Chief Executive Officer

FINANCIAL CONTENTS

11 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

21 CONSOLIDATED BALANCE SHEETS

22 CONSOLIDATED STATEMENTS OF OPERATIONS

23 CONSOLIDATED STATEMENTS OF CASH FLOWS

24 CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME

25 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

38 REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

39 MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

40 REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

41 FIVE-YEAR FINANCIAL SUMMARY

42 CORPORATE INFORMATION

43 DIRECTORS, OFFICERS AND HARTE-HANKS OFFICES

OVERVIEW

Management's Discussion and Analysis of Financial Condition and Results of Operations

Harte-Hanks is a worldwide direct and targeted marketing company that provides direct marketing services and shopper advertising opportunities to a wide range of local, regional, national and international consumer and business-to-business marketers. We manage our operations through two operating segments: Direct Marketing and Shoppers.

In 2005, Harte-Hanks Direct Marketing had revenues of $694.6 million, which accounted for approximately 61% of our total revenues. Direct marketing services are targeted to specific industries or markets with services and software products tailored to each industry or market. Currently, our Direct Marketing business services various vertical markets including retail, high-tech/telecom, financial services, pharmaceutical/healthcare, and a wide range of selected markets. We believe that we have the ability to provide services to new industries and markets by modifying our services and applications as opportunities are presented. Depending on the needs of our clients, our Direct Marketing capabilities are provided in an integrated approach through 37 facilities worldwide, 11 of which are located outside of the United States. These centers each possess some specialization and are linked together to support the needs of our clients. We utilize various capabilities and technologies to enable our clients to identify, reach, influence and nurture their customers.

Harte-Hanks Direct Marketing improves the return on our clients' marketing investment with a range of services organized around five solution points:

- Construct and update the database;
- Access the data;
- Analyze the data;
- Apply the knowledge; and
- Execute the programs.

We execute these solution points by providing a range of products and services including:

- Database design and development;
- Data processing and service bureau;
- Software;
- Data enhancements and list brokerage;
- Analytics, modeling, research and strategy;
- E-care, including online technical support and inbound e-mail management;
- Events management, including registration and promotion;
- Website design, management and hosting services;
- Loyalty program management;
- Sales lead management;
- Web-based database marketing;
- Technology databases;
- Creative services;
- Traditional and interactive media planning, placement and buying;
- Strategic planning;

continued ➤

- Fulfillment and distribution;
- Graphics and printing solutions;
- Inbound and outbound telemarketing including telesales and order processing;
- Lettershop services including laser personalization;
- Logistics; and
- E-mail marketing.

Harte-Hanks Shoppers is North America's largest owner, operator and distributor of shopper publications, based on weekly circulation and revenues. Shoppers are weekly advertising publications delivered free by Standard Mail to households and businesses in a particular geographic area. Shoppers offer advertisers a targeted, cost-effective local advertising system, with virtually 100% penetration in their area of distribution. Shoppers are particularly effective in large markets with high media fragmentation in which major metropolitan newspapers generally have low penetration. As of December 31, 2005, our shoppers are zoned into 1,047 separate editions with total circulation in excess of 12 million in California and Florida each week. We plan to cover an additional circulation of at least one million over the next several years in Northern California, Southern California, South Florida and the Tampa area. We believe that expansions provide increased revenues and, ultimately, increased operating income as the publications in these new areas mature. In 2005, our Shoppers segment had revenues of $440.4 million, which represented 39% of our total revenue.

We derive revenues from the sale of direct marketing services and shopper advertising services. As a worldwide business, direct marketing is affected by general national and international economic trends. Our shoppers operate in local markets and are largely affected by the strength of the local economies. Our principal expense items are payroll, postage and transportation.

Our strategy is based on seven key elements: being a market leader in each of our businesses; increasing revenues through growing our base businesses; introducing new services and products; entering new markets and making acquisitions; using technology to create competitive advantages; employing people who understand our clients' business and markets; and creating shareholder value.

RESULTS OF OPERATIONS

Operating results were as follows:

In thousands, except per share amounts	2005	% Change	2004	% Change	2003
Revenues	$ 1,134,993	10.1	$ 1,030,461	9.1	$ 944,576
Operating expenses	944,980	9.2	865,166	8.4	798,089
Operating income	$ 190,013	15.0	$ 165,295	12.8	$ 146,487
Net income	$ 114,458	17.3	$ 97,568	11.7	$ 87,362
Diluted earnings per share	$ 1.34	20.7	$ 1.11	14.4	$ 0.97

Year ended December 31, 2005 vs. Year ended December 31, 2004

Consolidated revenues increased 10.1%, to $1,135.0 million and operating income increased 15.0%, to $190.0 million, in 2005 compared to 2004. Our overall results reflect revenue increases in both the Direct Marketing and Shoppers segments. Direct Marketing results reflect increased revenues in all of that segment's vertical markets including a large, complex, world-wide project that was launched and substantially completed in the first quarter of 2005. Shoppers results were influenced by the acquisition of *The Flyer*, located in Tampa, Florida in April 2005, which contributed about half of the revenue growth for the year. Shoppers results also reflect improved sales in established markets and new year-over-year geographic expansions and household growth in California and Florida. Overall operating expenses increased 9.2%, to $945.0 million, in 2005 compared to 2004. The increase in consolidated operating expenses was a result of increased operating expenses from both the Shoppers and Direct Marketing segments, as well as an increase in general corporate expense. The primary drivers of the increase in operating expenses were increased labor costs due to pay increases and higher production volumes, higher

fuel costs in our direct marketing logistics business, higher postage costs due to higher shoppers volumes and higher paper costs due to higher rates and higher shoppers volumes.

Net income increased 17.3%, to $114.5 million, and diluted earnings per share grew 20.7%, to $1.34 per share, in 2005 when compared to 2004. The increase in net income was a result of increased operating income combined with a lower tax rate, partially offset by higher interest expense, in 2005 when compared to 2004. In 2006 we will begin expensing stock options and other equity compensation, which we estimate will impact 2006 diluted earnings per share by $0.06 to $0.07 cents per share.

Year ended December 31, 2004 vs. Year ended December 31, 2003

Consolidated revenues increased 9.1%, to $1,030.5 million, while operating income increased 12.8%, to $165.3 million, in 2004 compared to 2003. Overall operating expenses increased 8.4%, to $865.2 million. The Company's overall results reflect revenue increases in both its Direct Marketing and Shoppers segments. Increases in operating income in the Company's Direct Marketing and Shoppers segments were partially offset by increased general corporate operating expenses.

Direct Marketing

Direct Marketing operating results were as follows:

In thousands	2005	% Change	2004	% Change	2003
Revenues	$ 694,558	8.3	$ 641,214	9.6	$ 584,804
Operating expenses	586,463	6.6	550,358	8.3	508,163
Operating income	$ 108,095	19.0	$ 90,856	18.5	$ 76,641

Year ended December 31, 2005 vs. Year ended December 31, 2004

Revenue

Direct Marketing revenues increased $53.3 million, or 8.3%, in 2005 compared to 2004. These results reflect increased revenues in all of Direct Marketing's vertical markets. Direct Marketing revenues benefited from a large, complex, worldwide project that was launched and substantially completed in the first quarter of 2005. This one-time project was performed for a client in the high-tech vertical market and accounted for approximately 20% of the revenue growth in 2005 compared to 2004. Revenues from the pharmaceutical/healthcare vertical market had double-digit growth in 2005 compared to 2004. The increased revenues from this vertical were a result of regulatory changes to Medicare, but were partially offset by the effects of drug recalls. Revenues from Direct Marketing's select vertical markets group were also up double digits in 2005 compared to 2004, with most of the growth coming from the manufacturing vertical market. Revenues from the retail vertical market, Direct Marketing's largest vertical market in terms of annual revenue, increased near double digits. Revenues from the high-tech and financial services vertical markets were up in the mid-single digits in 2005 compared to 2004. All of the growth in the high-tech vertical was attributable to the one-time project discussed above. Absent this one-time project, revenues from the high-tech vertical would have been down in the low single digits in 2005 compared to 2004.

From a service offering perspective, Direct Marketing experienced increased revenues from logistics, data processing, telemarketing, personalized mail, database processing and agency-related work. Partially offsetting these increases were declines in revenues from customer care and fulfillment.

The acquisitions of Avellino Technologies Ltd. at the end of February 2004, Postfuture, Inc. in December 2004 and Communiqué Direct in February 2005 also positively affected our revenues in 2005 compared to 2004.

We have not seen any material change in the competitive landscape during 2005. We believe that our capabilities and breadth of services, combined with our national production capability, industry focus and ability to offer a full range of integrated services, enable us to compete effectively.

Revenues from our vertical markets in 2005 were impacted by the economic fundamentals of each industry, various market factors, including the demand for services by our clients, and the financial condition of and budgets available to specific clients. In general, revenues for Direct Marketing are affected by general national and international economic trends.

2006 revenues will depend on how successful we are at growing business with existing clients, acquiring new clients, meeting client demands, and the strength of the national and international economy. We believe that we will continue to benefit from marketing and advertising expenditures being moved from other advertising media to the targeted media space, the results of which can be more effectively tracked, enabling measurement of the return on marketing investment.

Operating Expense

Operating expenses increased $36.1 million, or 6.6%, in 2005 compared to 2004 as a result of increased labor costs, production and distribution costs, general and administrative

expenses and depreciation and amortization expense. Labor costs increased $9.1 million, or 3.3%, in 2005 compared to 2004 as a result of higher payroll costs due to higher volumes in certain offerings and salary increases, and higher healthcare costs. Production and distribution costs increased $22.8 million, or 11.2%, primarily due to higher logistics-related transportation costs, including increased fuel prices, higher outsourcing costs and increased repairs and maintenance expense, partially offset by decreased lease expense. General and administrative expense increased $3.0 million, or 6.8%, due to increased employee expense, general business expenses and facilities-related fees and services, partially offset by decreased insurance expense. Depreciation and amortization expense increased $1.2 million, or 5.3%, due to capital expenditures to support revenue growth. The acquisitions of Avellino Technologies Ltd. at the end of February 2004, Postfuture, Inc. in December 2004 and Communiqué Direct in February 2005 also contributed to the increase in operating expenses in 2005 compared to 2004.

Direct Marketing's largest cost component is labor, and these costs are primarily variable and tend to fluctuate with revenues and the demand for our Direct Marketing services. Total healthcare costs increased in 2005, and healthcare costs in general are expected to continue to increase. This increase is likely to impact Direct Marketing's total labor costs and total operating expenses. Fuel costs also increased significantly in 2005 and are expected to remain at high levels for the foreseeable future. These fuel costs are expected to continue to impact Direct Marketing's total production costs and total operating expenses.

Year ended December 31, 2004 vs. Year ended December 31, 2003

Revenue

Direct Marketing revenues increased $56.4 million, or 9.6%, in 2004 compared to 2003. These results reflect increased revenues in all of Direct Marketing's vertical markets. Revenues from the high-tech/telecom and pharmaceutical/healthcare vertical markets had double-digit growth in 2004 compared to 2003. Revenues from the financial services vertical market increased near double digits in 2004 compared to 2003. Revenues from the retail vertical market, Direct Marketing's largest vertical market in terms of annual revenue, were up in the mid-single digits. Direct Marketing's select markets group also experienced mid-single-digit growth in 2004 over 2003, with the majority of the growth coming from the manufacturing and business services industries.

From a service offering perspective, Direct Marketing experienced increased revenues from customer care, analytics, software, fulfillment, logistics, targeted mail, telesales and agency-related business.

Operating Expense

Operating expenses increased $42.2 million, or 8.3%, in 2004 compared to 2003. Labor costs increased $28.7 million, or 11.4%, as a result of increased incentive compensation due to Direct Marketing's financial performance, higher payroll costs due to higher volumes and increased headcount, and higher unemployment taxes. Labor costs were partially offset by lower healthcare costs and pension expense. Production and distribution costs increased $13.1 million, or 6.9%, primarily due to higher logistics-related transportation costs, outsourcing costs, and production services expense, which were partially offset by decreased lease expense. General and administrative expenses increased $1.8 million, or 4.3%, due to increased insurance expense, employee expense, and bad debt expense, partially offset by decreased royalties and professional services. Depreciation and amortization expense decreased $1.4 million, or 5.7%, due to lower capital expenditures starting in 2001 and continuing into 2002 and assets becoming fully depreciated.

Shoppers

Shoppers operating results were as follows:

In thousands	2005	% Change	2004	% Change	2003
Revenues	$ 440,435	13.2	$ 389,247	8.2	$ 359,772
Operating expenses	346,204	14.1	303,390	7.7	281,765
Operating income	$ 94,231	9.8	$ 85,857	10.1	$ 78,007

Year ended December 31, 2005 vs. Year ended December 31, 2004

Revenue

Shopper revenues increased $51.2 million, or 13.2%, in 2005 compared to 2004. The acquisition of *The Flyer*, located in Tampa, Florida, in April 2005 contributed about half of this revenue growth. The remaining revenue increases primarily were the result of improved sales in established markets and new year-over-year geographic expansions and household growth in California and Florida. Total Shoppers circulation increased by almost 1.3 million during 2005, including the circulation in Tampa at the date of acquisition of approximately 955,000. During the year the Harte-Hanks Shoppers *PennySaver* publication in Southern California expanded circulation by 176,500. The Harte-Hanks Shoppers *PennySaver* publication in Northern California increased geographic coverage by adding 69,500 circulation. The Harte-Hanks Shoppers publication *The Flyer*, located in South Florida, expanded geographically by 6,500 circulation. The Harte-Hanks Shoppers publication *The Flyer*, located in the Tampa, Florida area expanded circulation by 92,000 from the date of the acquisition in April 2005 to the end of 2005. At December 31, 2005, Shoppers circulation reached more than 12 million (including 240,000 in South Orange County California, where

Shoppers publishes two editions each week). We believe that expansions provide increased revenue opportunities, and plan to cover an additional circulation of at least one million over the next several years in Northern California, Southern California, South Florida and the Tampa area. Newer areas initially tend to contribute less from a revenue-per-thousand perspective than existing areas, and in fact are typically expected to be less profitable or even unprofitable until the publications in those areas mature.

From a product-line perspective, Shoppers had strong growth from run-of-press (ROP, or in-book) advertising, primarily core sales, employment and real estate-related advertising. Revenues from distribution products were up slightly compared to 2004.

Operating Expense

Operating expenses increased $42.8 million, or 14.1%, in 2005 compared to 2004 as a result of increased labor costs, production and distribution costs, general and administrative costs and depreciation and amortization expense, as well as the acquisition of *The Flyer* located in Tampa, Florida. Total labor costs increased $14.2 million, or 13.1%. Excluding the Tampa acquisition, labor costs increased $5.4 million, or 5.0%, due to higher payroll costs as a result of higher circulation volumes and expansions, and higher healthcare costs. Total production costs increased $23.5 million, or 14.9%. Excluding the Tampa acquisition, production costs increased $12.0 million, or 7.6%, including increased postage due to increased volumes and circulation growth, increased offload printing expense due to increased print-and-deliver volumes and higher printing rates, and increased paper costs due to increased rates. Total general and administrative costs increased $3.8 million, or 12.0%. Excluding the Tampa acquisition, general and administrative costs increased $1.9 million, or 6.0%, primarily due to increased promotion costs, general business services and bad debt expense, partially offset by decreased insurance costs. Total depreciation and amortization expense was up $1.4 million or 24.2%, with the majority of the increase attributable to the Tampa acquisition. Intangible amortization related to the Tampa acquisition was $0.8 million during 2005.

Shopper revenue and operating results were also impacted in the fourth quarter by Hurricane Wilma, which moved across South Florida causing extensive wind and water damage and loss of electrical power to millions of homes and businesses. This resulted in the loss of one week's publication and delay of another week's publication in our South Florida Shopper, as well as expense associated with property damage to our facility. Our South Florida Shopper represents less than 10% of total Shoppers revenues and less than 3.5% of our total revenues.

Shoppers' largest cost components are labor, postage and paper. Shoppers' labor costs are variable and tend to fluctuate with the number of zones, circulation, volumes and revenues. Total healthcare costs increased in 2005 and healthcare costs in general are expected to continue to increase, and this increase is likely to impact Shoppers' total labor costs and total operating expenses. Standard postage rates had been unchanged since the beginning of the third quarter of 2002, but did increase in the first quarter of 2006, and likely will increase again in the future. Increased postage rates will impact Shoppers total production costs; however, we expect to partially offset this impact on operating results through advertising price increases. Newsprint prices increased throughout 2004 and 2005 and are expected to continue to increase in 2006. This increase impacted Shoppers production costs in 2005, and rising newsprint prices are expected to impact Shoppers production costs into 2006.

Year ended December 31, 2004 vs. Year ended December 31, 2003

Revenue

Shoppers revenues increased $29.5 million, or 8.2%, in 2004 compared to 2003. Revenue increases were the result of improved sales in established markets and geographic expansions into new neighborhoods in California and Florida. Total Shoppers circulation increased by approximately 600,000 during 2004 and at December 31, 2004, Shoppers circulation reached more than 11 million (including 240,000 in South Orange County California, where Shoppers publish two editions each week). During the year, Harte-Hanks Shoppers *PennySaver* publication in Northern California expanded circulation by 323,500. The Harte-Hanks Shoppers *PennySaver* publication in Southern California increased geographic coverage by adding 150,000 circulation. The Harte-Hanks Shoppers publication *The Flyer*, located in South Florida, expanded geographically by 129,500 circulation.

From a product-line perspective, Shoppers had growth in both run-of-press (ROP, or in-book) advertising and its distribution products. These increases were partially offset by decreased coupon book revenues.

Operating Expense

Shoppers operating expenses rose $21.6 million, or 7.7%, in 2004 compared to 2003. Labor costs increased $6.3 million, or 6.2%, due to higher payroll costs as a result of higher volumes and circulation expansions, and higher unemployment taxes, partially offset by lower pension and health care expense. Production costs increased $13.8 million, or 9.6%, including additional postage of $6.6 million due to increased volumes, and increased paper costs due to increased volumes and rates. General and administrative costs increased $1.4 million, or 4.4%, due to increased general business services and bad debt expense, partially offset by decreased promotion expense. Depreciation expense increased $0.1 million, or 2.3%, due to new capital investments to support future growth.

GENERAL CORPORATE EXPENSE

Year ended December 31, 2005 vs. Year ended December 31, 2004

General corporate expense increased $0.9 million, or 7.8%, during 2005 compared to 2004. The increase in general corporate expense was primarily a result of increased professional services, primarily consulting related to a state tax refund and Sarbanes-Oxley related costs, and increased labor, primarily payroll due to higher pension expense.

Year ended December 31, 2004 vs. Year ended December 31, 2003

General corporate operating expense increased $3.3 million, or 39.9%, to $11.4 million in 2004 compared to 2003. The increase in general corporate expense in 2004 was primarily a result of increased incentive compensation due to the Company's financial performance and increased professional services.

INTEREST EXPENSE

Interest expense increased $0.9 million in 2005 over 2004, due primarily to higher outstanding debt levels and higher interest rates. Interest expense increased $0.2 million in 2004 over 2003, due primarily to higher interest rates. Our debt at December 31, 2005 and 2004 is described in Note C of the "Notes to Consolidated Financial Statements," included herein.

INTEREST INCOME

Interest income decreased $0.1 million in 2005 compared to 2004, primarily due to interest related to a tax refund we received in the first quarter of 2004. Interest income increased $0.2 million in 2004 compared to 2003, primarily due to interest related to a tax refund we received in the first quarter of 2004.

OTHER INCOME AND EXPENSE

Other net expense for 2005 and 2004 primarily consists of balance-based bank charges and stockholders expenses.

INCOME TAXES

Year ended December 31, 2005 vs. Year ended December 31, 2004

Income taxes increased $6.6 million in 2005, primarily due to higher pretax income levels, partially offset by $1.2 million and $1.3 million favorable resolutions of tax issues in the second and fourth quarters, respectively, of 2005. These favorable tax resolutions reduced our effective income tax rate from 40.1% in 2004 to 38.6% in 2005. The effective income tax rate calculated is higher than the federal statutory rate of 35% due to the addition of state taxes.

Year ended December 31, 2004 vs. Year ended December 31, 2003

Income taxes increased $8.9 million in 2004, primarily due to higher pretax income levels. The effective income tax rate was 40.1% and 39.3% in 2004 and 2003, respectively.

ACQUISITIONS

We made several acquisitions in 2005 and 2004.

In April 2005, we acquired substantially all of the assets of Flyer Printing Company, Inc. related to *The Flyer*, located in Tampa, Florida. *The Flyer* is a weekly shopper publication delivered by mail with circulation of 955,000 in the Tampa, Florida metropolitan area. The combination of *The Flyer* with our existing shopper operations increased total shopper circulation to approximately 12 million weekly. The total cost of the transaction was approximately $61.7 million and was paid in cash. The total amount of goodwill recognized in this transaction was $41.6 million. Intangible assets recognized in this transaction that are subject to amortization, relating to client relationships and non-compete agreements, totaled $8.3 million. Intangible assets recognized in this transaction that are not subject to amortization, relating to trademarks and trade names, totaled $7.6 million. All goodwill and intangibles recognized as part of this acquisition were assigned to the Shoppers segment. The operating results of the acquired assets have been included in the accompanying Consolidated Financial Statements from the date of acquisition.

In February 2005, we acquired long-standing Australian partner Communiqué Direct pursuant to a purchase option we acquired in June 2003. Founded in 1992, Communiqué Direct, located in a north suburb of Sydney, Australia, was a privately held firm that provided a range of marketing and information services for the business-to-business sector across the Asia-Pacific region. Since 1998, Harte-Hanks and Communiqué Direct had worked with each other on many Pacific Rim marketing applications, focusing on our high-tech clients. The total cost of the transaction was approximately $1.6 million, which was paid in cash.

In December 2004, we acquired Postfuture, Inc., an e-mail service provider located in Richardson, Texas, that provides both e-mail technology and services, among them a platform that automates campaign and transactional e-mail delivery to support e-commerce, customer service, event communication, and lead nurturing. Postfuture's offerings are being integrated into several existing Harte-Hanks solution offerings, including Allink on Demand®, CI Technology Database, and Allink Agent®, among others.

In April 2004, we acquired *Dollar Saver*, a local shopper publication in the fast-growing Hemet area in Southern California — and converted it to the PennySaver brand.

In February 2004, we acquired Avellino Technologies Ltd., a leading provider of data profiling technology. We have integrated Trillium Software System® and the Avellino Discovery software solution. Joining these two solutions allows organizations, for the first time with one solution provider, to define, assess, improve and monitor how well data meet the needs of enterprise business processes. We still offer Trillium Software and Avellino Discovery as stand-alone products as well as an integrated solution within the Trillium Software System. Founded in 1997, Avellino Technologies Ltd. is located in Aldermaston, UK.

We did not make any acquisitions in 2003.

LIQUIDITY AND CAPITAL RESOURCES

Cash provided by operating activities for 2005 was $145.4 million, a $7.9 million decrease compared to 2004. The decrease in 2005 primarily relates to a $4.9 million decrease in other accrued expenses in 2005 versus a $26.2 million increase, which related to increased taxes payable and accrued payroll and bonuses, in 2004. This decrease was partially offset by a $16.9 million increase in net income in 2005 compared to 2004.

Net cash outflows from investing activities were $91.3 million for 2005, compared to net cash outflows of $64.6 million in 2004. The increase in 2005 primarily relates to a higher amount spent on acquisitions, partially offset by a decrease in capital investments in 2005 compared to 2004.

Net cash used in investing activities for 2005 included $63.3 million for acquisitions and $28.2 million for capital expenditures. The Direct Marketing segment's capital expenditures consisted primarily of product development and enhancement, additional computer capacity, computer and communication systems, and equipment upgrades. The Shoppers segment's capital expenditures were primarily related to the Southern California color capacity expansion, common system software, additional computers and other production equipment. $61.7 million of the acquisition-related payments was made in the Shoppers segment, and the remaining $1.5 million was made in the Direct Marketing segment.

Net cash used in investing activities for 2004 included $35.1 million for capital expenditures and $29.7 million for acquisitions. The Direct Marketing segment's capital expenditures consisted primarily of product development and enhancement, additional computer capacity, computer and communication systems, and equipment upgrades. The Shoppers segment's capital expenditures were primarily related to the Southern California color capacity expansion, common system software, additional computers and other production equipment. $28.0 million of the acquisition-related payments was made in the Direct Marketing segment, and the remaining $1.7 million was made in the Shoppers segment.

Net cash outflows from financing activities in 2005 were $68.3 million, compared to $82.1 million in 2004. The decrease in 2005 primarily relates to $52.0 million net borrowings of debt in 2005 compared to $5.0 million net borrowings of debt in 2004. This was partially offset by $28.5 million more spent repurchasing stock in 2005 than in 2004.

Management considers such factors as current assets, current liabilities, total debt, revenues, operating income and cash flows from operations, investing activities and financing activities when assessing our liquidity.

Capital resources are also available from and provided through our unsecured credit facility. On August 12, 2005, Harte-Hanks entered into a five-year $125 million revolving credit facility (the "Credit Facility") with JPMorgan Chase Bank, N.A., as administrative agent. The Credit Facility replaced the existing revolving credit facility with JPMorgan Chase Bank, N.A., as administrative agent, which was scheduled to mature on October 18, 2005. The Credit Facility allows us to obtain revolving credit loans and provides for the issuance of letters of credit. For each borrowing under the Credit Facility, we can generally choose to have the interest rate for that borrowing calculated based on either JPMorgan Chase Bank's publicly announced New York prime rate or on a Eurodollar (as defined in our new Five-Year Credit Agreement) rate plus a spread. The spread is determined based on our total debt-to-EBITDA (as defined in our new Five-Year Credit Agreement) ratio then in effect, and ranges from .315% to .6%. There is a facility fee that we are also required to pay under the Credit Facility that is based on a rate applied to the total commitment amount under the Credit Facility (which is $125 million), regardless of how much of that commitment we have actually drawn upon. The facility fee rate ranges from .085% to .15%, depending on our total debt-to-EBITDA ratio then in effect. In addition, we will also be charged a letter of credit fee with respect to any outstanding letters of credit issued under this credit facility. That fee is calculated by applying a rate equal to the spread applicable to Eurodollar-based loans plus a fronting fee of .125% per annum to the average daily undrawn amount of the outstanding letters of credit.

Under the Credit Facility, we are required to maintain an interest coverage ratio of not less than 2.75 to 1 and a total debt-to-EBITDA ratio of not more than 3.0 to 1. The Credit Facility also contains covenants restricting our and our subsidiaries' ability to grant liens, enter into certain transactions and allow the total amount of indebtedness of our subsidiaries to exceed $20 million.

The Credit Facility also includes customary covenants regarding reporting obligations, delivery of notices regarding certain events, maintaining our corporate existence, payment of obligations, maintenance of our properties and insurance thereon at customary levels with financially sound and reputable insurance companies, maintaining books and records and compliance with applicable laws. The Credit Facility provides for customary events of default including nonpayment of principal or interest, breach of representations and warranties, violations of covenants, failure to pay certain other indebtedness, bankruptcy and material judgments and liabilities, certain violations of environmental laws or ERISA or the occurrence of a change of control. As of December 31, 2005, we were in compliance with all of the covenants of our Credit Facility.

Management believes that its Credit Facility, together with cash provided by operating activities, will be sufficient to fund operations and anticipated acquisitions, stock repurchases, capital expenditures and dividends for the foreseeable future. As of December 31, 2005, we had $63.0 million of unused borrowing capacity under our Credit Facility.

Contractual obligations at December 31, 2005 are as follows:

In thousands	Total	2006	2007	2008	2009	2010	Thereafter
Debt	$ 62,000	$ –	$ –	$ –	$ –	$ 62,000	$ –
Operating leases	93,721	23,556	20,201	15,554	12,174	8,987	13,249
Deferred compensation liability	6,672	702	702	702	702	702	3,162
Other long-term obligations	3,940	2,330	1,528	80	2	–	–
Total contractual cash obligations	$ 166,333	$ 26,588	$ 22,431	$ 16,336	$ 12,878	$ 71,689	$ 16,411

At December 31, 2005, we had letters of credit in the amount of $25.0 million. No amounts were drawn against these letters of credit at December 31, 2005. These letters of credit renew annually and exist to support insurance programs relating to workers' compensation, automobile and general liability, and leases. We had no other off-balance sheet arrangements at December 31, 2005.

We paid a quarterly dividend of $0.05 per common share and $0.04 per common share in each of the quarters in the years ended December 31, 2005 and 2004, respectively. In January 2006, we announced an increase in the regular quarterly dividend from 5.0 cents per share to 6.0 cents per share, payable March 15, 2006 to holders of record on March 1, 2006.

During 2005 we repurchased approximately 4.3 million shares of our common stock for $114.2 million under our stock repurchase program. As of December 31, 2005 we have repurchased 43.5 million shares since the beginning of the stock repurchase program in January 1997. In November 2005 our Board of Directors authorized an additional 5 million shares under our stock repurchase program. Under this program, we had authorization to repurchase approximately 6.4 million additional shares at December 31, 2005.

During 2005 we received 0.2 million shares of our common stock, with an estimated market value of $4.7 million, in connection with stock option exercises. Since January 1997 we have received 1.5 million shares in connection with stock option exercises.

CRITICAL ACCOUNTING POLICIES

Financial Reporting Release No. 60, released by the Securities and Exchange Commission, requires all companies to include a discussion of critical accounting policies or methods used in the preparation of financial statements. Note A of the "Notes to Consolidated Financial Statements" includes a summary of the significant accounting policies and methods used in the preparation of our Consolidated Financial Statements. The following is a discussion of the more significant accounting policies and methods.

Revenue Recognition

We recognize revenue at the time the service is rendered or the product is delivered. Payments received in advance of the performance of services or delivery of the product are recorded as deferred revenue until such time as the services are performed or the product is delivered.

For all sales, we require either a purchase order, a statement of work signed by the client, a written contract, or some other form of written authorization from the client.

Our accounting policy for revenue recognition has an impact on our reported results and relies on certain estimates that require judgments on the part of management. The portion of our revenue that is most subject to estimates and judgments is revenue recognized using the percentage-of-completion method, as discussed below.

Specifically, Direct Marketing revenue from certain projects and certain services such as database build services, internet web design, market research and analytical services may be billed at hourly rates or a set price. If billed at a set price, the revenue is recognized over the contractual period, using the percentage-of-completion method. Management estimates and judgments are used in connection with the revenue recognized in these instances. Should actual costs differ significantly from the original estimated costs, the timing of revenues and overall profitability of the contract could be impacted. Contracts accounted for under the percentage-of-completion method constituted less than 7.5% of total Direct Marketing revenue and less than 4.5% of our revenue for the years ended December 31, 2005, 2004 and 2003.

Direct Marketing revenue is derived from a variety of services and products. Revenue from services such as creative and graphics, printing, personalization of communication pieces using laser and inkjet printing, targeted mail, fulfillment, agency services and transportation logistics are recognized as the work is performed. Revenue is typically based on a set price or rate given to the client.

Revenue from the ongoing production and delivery of data is recognized upon completion and delivery of the work and is typically based on a set price or rate. Revenue from database subscriptions is based on a set price and is recognized ratably over the term of the subscription.

Revenue from database build services may be billed based on hourly rates or at a set price. If billed at a set price, the database build revenue is recognized using the percentage-of-completion method based on individual costs incurred to date compared with total estimated contract costs.

Revenue from market research and analytical services may be billed based on hourly rates or a set price. If billed at a set price, the revenue is recognized using the percentage-of-completion method based on individual costs incurred to date compared with total estimated contract costs. In other instances, progress toward completion is based on performance milestones specified in the contract where such milestones fairly reflect progress toward contract completion.

Revenue related to e-marketing, lead management, multi-channel customer care, inbound and outbound teleservices and technical support is typically billed based on a set price per transaction or service provided. Revenue from these services is recognized as the service or activity is performed.

Revenue from software is recognized in accordance with the American Institute of Certified Public Accountants' (AICPA) Statement of Position (SOP) 97-2 "Software Revenue Recognition," as amended by SOP 98-9 "Modification of SOP 97-2, Software Revenue Recognition." SOP 97-2 generally requires revenue earned on software arrangements involving multiple elements to be allocated to each element based on the vendor-specific objective evidence of fair values of the respective elements. For software sales with multiple elements (for example, software licenses with undelivered post-contract customer support or "PCS"), we allocate revenue to each component of the arrangement using the residual value method based on the fair value of the undelivered elements. This means we defer revenue from the software sale equal to the fair value of the undelivered elements. The fair value of PCS is based upon separate sales of renewals to other clients or upon

renewal rates quoted in the contracts. The fair value of services, such as training and consulting, is based upon separate sales of these services to other clients.

The revenue allocated to PCS is recognized ratably over the term of the support period. Revenue allocated to professional services is recognized as the services are performed. The revenue allocated to software products, including time-based software licenses, is recognized, if collection is probable, upon execution of a licensing agreement and shipment of the software or ratably over the term of the license, depending on the structure and terms of the arrangement. If the licensing agreement is for a term of one year or less and includes PCS, we recognize the software and the PCS revenue ratably over the term of the license.

We apply the provisions of Emerging Issues Task Force Issue No. 00-03 "Application of AICPA Statement of Position 97-2 to Arrangements that Include the Right to Use Software Stored on Another Entity's Hardware" to our hosted software service transactions.

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

As described above, sometimes our customer arrangements have multiple deliverables, including service elements. Generally, our multiple-element arrangements fall within the scope of specific accounting standards that provide guidance regarding the separation of elements in multiple-deliverable arrangements and the allocation of consideration among those elements (e.g., AICPA SOP 97-2 "Software Revenue Recognition"). If not, we apply the provisions of Emerging Issues Task Force Issue No. 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables" ("EITF 00-21"). The provisions of EITF 00-21 require us to unbundle multiple-element arrangements into separate units of accounting when the delivered element(s) has stand-alone value and fair value of the undelivered element(s) exist. When we are able to unbundle the arrangement into separate units of accounting, we apply one of the accounting policies described above to each unit. If we are unable to unbundle the arrangement into separate units of accounting, we apply one of the accounting policies described above to the entire arrangement. This might impact the timing of revenue recognition, but would not change the total revenue recognized from the arrangement.

Shoppers services are considered rendered, and the revenue recognized, when all printing, sorting, labeling and ancillary services have been provided and the mailing material has been received by the United States Postal Service.

Allowance for Doubtful Accounts

We maintain our allowance for doubtful accounts at a balance adequate to reduce accounts receivable to the amount of cash expected to be realized upon collection. The methodology used to determine the minimum allowance balance is based on our prior collection experience and is generally related to the accounts receivable balance in various aging categories. The balance is also influenced by specific clients' financial strength and circumstance. Accounts that are determined to be uncollectible are written off in the period in which they are determined to be uncollectible. Periodic changes to the allowance balance are recorded as increases or decreases to bad debt expense, which is included in the "Advertising, selling, general and administrative" line of our Consolidated Statements of Operations. We recorded bad debt expense of $4.2 million, $3.0 million and $1.6 million for the years ended December 31, 2005, 2004 and 2003, respectively. While we believe our reserve estimate to be appropriate, we may find it necessary to adjust the allowance for doubtful accounts if future bad debt expense exceeds the estimated reserve. Given the significance of accounts receivable to the consolidated financial statements, the determination of net realizable values is considered to be a critical accounting estimate.

Reserve for Healthcare, Workers' Compensation, Automobile and General Liability

We increased our deductible for individual healthcare claims from $150,000 to $175,000 and eliminated our aggregate annual claims deductible in 2005. We have a $250,000 deductible for automobile and general liability claims. Our deductible for workers' compensation decreased from $1.0 million to $500,000 in October 2003. Management makes various subjective judgments about a number of factors in determining our reserve for healthcare, workers' compensation, automobile and general liability insurance, and the related expense. If ultimate losses were 10% higher than our estimate at December 31, 2005, earnings would be impacted by up to $925,000, net of taxes. The amount that earnings would be impacted is dependent on the claim year and our deductible levels for that plan year. Periodic changes to the reserve for workers' compensation, automobile and general liability are recorded as increases or decreases to insurance expense, which is included in the "Advertising, selling, general and administrative" line of our Consolidated Statement of Operations. Periodic changes to the reserve for healthcare are recorded as increases or decreases to employee benefits expense, which is included in the "Payroll" line of our Consolidated Statement of Operations.

Goodwill

Goodwill is recorded to the extent that the purchase price exceeds the fair value of the assets acquired in accordance with Statement of Financial Accounting Standards (SFAS) No. 142. Prior to the adoption of SFAS No. 142 on January 1, 2002, goodwill was being amortized on a straight-line basis over

15- to 40-year periods. Beginning January 1, 2002, goodwill is no longer being amortized, but instead is tested for impairment as discussed below.

We assess the impairment of our goodwill in accordance with SFAS No. 142, by determining the fair value of each of our reporting units and comparing the fair value to the carrying value for each reporting unit. We have identified our reporting units as Direct Marketing and Shoppers. Fair value is determined using projected discounted future cash flows and cash flow multiple models, based on historical performance and management's estimate of future performance, giving consideration to existing and anticipated competitive and economic conditions. If a reporting unit's carrying amount exceeds its fair value, we must calculate the implied fair value of the reporting unit's goodwill by allocating the reporting unit's fair value to all of its assets and liabilities (recognized and unrecognized) in a manner similar to a purchase price allocation, and then compare this implied fair value to its carrying amount. To the extent that the carrying amount of goodwill exceeds its implied fair value, an impairment loss is recorded.

Both the Direct Marketing and Shoppers segments are tested for impairment as of November 30 of each year, after the annual forecasting process for the upcoming fiscal year has been completed. We have not recorded an impairment loss in any of the three years ended December 31, 2005. Significant estimates utilized in our discounted cash flow model include weighted average cost of capital and the long-term rate of growth for each of our reporting segments. These estimates require management's judgment. Any significant changes in key assumptions about our businesses and their prospects, or changes in market conditions, could have an impact on this annual analysis.

At December 31, 2005 and 2004, our goodwill balance was $502.8 million, net of $82.0 million of accumulated amortization, and $458.2 million, net of $82.0 million of accumulated amortization, respectively. Based upon our analysis, the estimated fair values of our reporting units as of December 31, 2005 were well in excess of the reporting units' carrying values.

New Accounting Pronouncements

As discussed in Note A of the Notes to Consolidated Financial Statements, certain new financial accounting pronouncements have been issued which either have already been reflected in the accompanying consolidated financial statements, or will become effective for our financial statements at various dates in the future. The adoption of these pronouncements has not had, or is not expected to have, a material effect on our consolidated financial statements. The adoption of SFAS 123R in 2006 will require us to begin expensing stock options and other equity compensation which will decrease operating income, net income and earnings per share. We estimate the adoption of SFAS 123R will impact 2006 diluted earnings per share by $0.06 to $0.07 per share.

HARTE-HANKS, INC. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

In thousands, except per share and share amounts	December 31, 2005	December 31, 2004
ASSETS		
Current assets		
Cash and cash equivalents	$ 24,561	$ 38,807
Accounts receivable *(less allowance for doubtful accounts of $3,832 in 2005 and $1,892 in 2004)*	184,537	168,755
Inventory	7,947	6,086
Prepaid expenses	14,783	16,664
Deferred income tax asset	14,158	13,812
Other current assets	7,718	6,373
Total current assets	253,704	250,497
Property, plant and equipment		
Land	3,385	3,463
Buildings and improvements	37,483	37,312
Software	85,927	76,347
Equipment and furniture	197,671	190,522
	324,466	307,644
Less accumulated depreciation and amortization	(214,873)	(204,669)
	109,593	102,975
Software development and equipment installations in progress	3,318	10,795
Net property, plant and equipment	112,911	113,770
Intangible and other assets		
Goodwill *(less accumulated amortization of $81,973 in 2005 and 2004)*	502,750	458,171
Other intangible assets *(less accumulated amortization of $4,360 in 2005 and $2,933 in 2004)*	16,669	2,067
Other assets	3,629	3,848
Total intangible and other assets	523,048	464,086
Total assets	$ 889,663	$ 828,353
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Current maturities of long-term debt	$ –	$ 10,000
Accounts payable	62,978	55,632
Accrued payroll and related expenses	35,735	36,539
Customer deposits and unearned revenue	54,143	53,707
Income taxes payable	12,710	17,239
Other current liabilities	9,781	9,075
Total current liabilities	175,347	182,192
Long-term debt	62,000	—
Other long-term liabilities *(including deferred income taxes of $53,270 in 2005 and $48,201 in 2004)*	90,970	74,362
Total liabilities	328,317	256,554
Stockholders' equity		
Common stock, $1 par value, authorized: 250,000,000 shares Issued 2005: 115,453,416; Issued 2004: 114,505,329 shares	115,453	114,505
Additional paid-in capital	269,865	253,515
Retained earnings	980,505	882,750
Less treasury stock, 2005: 33,965,335; 2004: 29,524,064 shares at cost	(782,495)	(663,779)
Accumulated other comprehensive loss	(21,982)	(15,192)
Total stockholders' equity	561,346	571,799
Total liabilities and stockholders' equity	$ 889,663	$ 828,353

See Notes to Consolidated Financial Statements.

HARTE-HANKS, INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF OPERATIONS

In thousands, except per share and share amounts	Year Ended December 31,		
	2005	2004	2003
Revenues	$ 1,134,993	$ 1,030,461	$ 944,576
Operating expenses			
Payroll	418,056	394,417	357,811
Production and distribution	407,512	361,298	334,359
Advertising, selling, general and administrative	88,067	80,682	75,886
Depreciation	29,918	28,169	29,433
Intangible amortization	1,427	600	600
Total operating expenses	944,980	865,166	798,089
Operating income	190,013	165,295	146,487
Other expenses (income)			
Interest expense	1,957	1,020	855
Interest income	(197)	(341)	(168)
Other, net	1,774	1,648	1,895
	3,534	2,327	2,582
Income before income taxes	186,479	162,968	143,905
Income tax expense	72,021	65,400	56,543
Net income	$ 114,458	$ 97,568	$ 87,362
Basic earnings per common share	$ 1.37	$ 1.13	$ 0.99
Weighted-average common shares outstanding	83,734	86,169	88,541
Diluted earnings per common share	$ 1.34	$ 1.11	$ 0.97
Weighted-average common and common equivalent shares outstanding	85,406	87,806	89,982

See Notes to Consolidated Financial Statements.

HARTE-HANKS, INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS

In thousands	Year Ended December 31, 2005	2004	2003
Cash Flows from Operating Activities			
Net income	$ 114,458	$ 97,568	$ 87,362
Adjustments to reconcile net income to net cash provided by operations:			
Depreciation	29,918	28,169	29,433
Intangible amortization	1,427	600	600
Amortization of option-related compensation	161	101	100
Deferred income taxes	6,555	6,963	12,047
Other, net	459	534	379
Changes in operating assets and liabilities, net of effects from acquisitions:			
Increase in accounts receivable, net	(14,250)	(14,215)	(15,024)
(Increase) decrease in inventory	(1,083)	(873)	86
Decrease (increase) in prepaid expenses and other current assets	829	(3,233)	2,931
Increase in accounts payable	6,171	7,442	7,145
(Decrease) increase in other accrued expenses and other liabilities	(4,938)	26,232	7,186
Other, net	5,707	4,029	(8,181)
Net cash provided by operating activities	145,414	153,317	124,064
Cash Flows from Investing Activities			
Acquisitions	(63,274)	(29,705)	(343)
Purchases of property, plant and equipment	(28,215)	(35,146)	(31,915)
Proceeds from the sale of property, plant and equipment	165	268	621
Net cash used in investing activities	(91,324)	(64,583)	(31,637)
Cash Flows from Financing Activities			
Long-term borrowings	112,000	55,000	45,000
Payments on debt	(60,000)	(50,000)	(56,300)
Issuance of common stock	10,397	12,287	12,885
Issuance of treasury stock	183	165	125
Purchase of treasury stock	(114,213)	(85,738)	(76,393)
Dividends paid	(16,703)	(13,792)	(10,619)
Net cash used in financing activities	(68,336)	(82,078)	(85,302)
Net (decrease) increase in cash and cash equivalents	(14,246)	6,656	7,125
Cash and cash equivalents at beginning of year	38,807	32,151	25,026
Cash and cash equivalents at end of year	$ 24,561	$ 38,807	$ 32,151

See Notes to Consolidated Financial Statements.

HARTE-HANKS, INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME

In thousands	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance at January 1, 2003	$111,535	$216,149	$722,231	$(491,793)	$(25,589)	$532,533
Common stock issued — employee benefit plans	213	3,199	–	–	–	3,412
Exercise of stock options for cash and by surrender of shares	1,533	10,392	–	(5,828)	–	6,097
Tax benefit of options exercised	–	6,282	–	–	–	6,282
Dividends paid ($0.12 per share)	–	–	(10,619)	–	–	(10,619)
Treasury stock issued	–	(26)	–	151	–	125
Treasury stock repurchased	–	–	–	(76,393)	–	(76,393)
Comprehensive income, net of tax:						
Net income	–	–	87,362	–	–	87,362
Adjustment for minimum pension liability (net of tax of $2,652)	–	–	–	–	4,053	4,053
Foreign currency translation adjustment	–	–	–	–	2,746	2,746
Total comprehensive income						94,161
Balance at December 31, 2003	$113,281	$235,996	$798,974	$(573,863)	$(18,790)	$555,598
Common stock issued — employee benefit plans	175	3,347	–	–	–	3,522
Exercise of stock options for cash and by surrender of shares	1,049	10,345	–	(4,334)	–	7,060
Tax benefit of options exercised	–	3,818	–	–	–	3,818
Dividends paid ($0.16 per share)	–	–	(13,792)	–	–	(13,792)
Treasury stock issued	–	9	–	156	–	165
Treasury stock repurchased	–	–	–	(85,738)	–	(85,738)
Comprehensive income, net of tax:						
Net income	–	–	97,568	–	–	97,568
Adjustment for minimum pension liability (net of tax of $1,519)	–	–	–	–	2,322	2,322
Foreign currency translation adjustment	–	–	–	–	1,276	1,276
Total comprehensive income						101,166
Balance at December 31, 2004	$114,505	$253,515	$882,750	$(663,779)	$(15,192)	$571,799
Common stock issued — employee benefit plans	174	3,874	–	–	–	4,048
Exercise of stock options for cash and by surrender of shares	774	7,311	–	(4,654)	–	3,431
Tax benefit of options exercised	–	5,133	–	–	–	5,133
Dividends paid ($0.20 per share)	–	–	(16,703)	–	–	(16,703)
Treasury stock issued	–	32	–	151	–	183
Treasury stock repurchased	–	–	–	(114,213)	–	(114,213)
Comprehensive income, net of tax:						
Net income	–	–	114,458	–	–	114,458
Adjustment for minimum pension liability (net of tax of $3,567)	–	–	–	–	(5,450)	(5,450)
Foreign currency translation adjustment	–	–	–	–	(1,340)	(1,340)
Total comprehensive income						107,668
Balance at December 31, 2005	$115,453	$269,865	$980,505	$(782,495)	$(21,982)	$561,346

See Notes to Consolidated Financial Statements.

Note A – Significant Accounting Policies

Consolidation

The accompanying consolidated financial statements present the financial position and the results of operations and cash flows of Harte-Hanks, Inc. and subsidiaries. The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods.

All intercompany accounts and transactions have been eliminated in consolidation. Certain prior year amounts have been reclassified for comparative purposes.

Cash Equivalents

All highly liquid investments with an original maturity of 90 days or less at the time of purchase are considered to be cash equivalents. Cash equivalents are carried at cost, which approximates fair value.

Allowance for Doubtful Accounts

We maintain our allowance for doubtful accounts at a balance adequate to reduce accounts receivable to the amount of cash expected to be realized upon collection. The methodology used to determine the minimum allowance balance is based on our prior collection experience and is generally related to the accounts receivable balance in various aging categories. The balance is also influenced by specific clients' financial strength and circumstance. Accounts that are determined to be uncollectible are written off in the period in which they are determined to be uncollectible. Periodic changes to the allowance balance are recorded as increases or decreases to bad debt expense, which is included in the "Advertising, selling, general and administrative" line of our Consolidated Statements of Operations. We recorded bad debt expense of $4.2 million, $3.0 million and $1.6 million for the years ended December 31, 2005, 2004 and 2003, respectively.

Inventory

Inventory, consisting primarily of newsprint and operating supplies, is stated at the lower of cost (first-in, first-out method) or market.

Property, Plant and Equipment

Property, plant and equipment are stated on the basis of cost. Depreciation of buildings and equipment is computed generally on the straight-line method at rates calculated to amortize the cost of the assets over their useful lives. The general ranges of estimated useful lives are:

Buildings and improvements	10 to 40 years
Equipment and furniture	3 to 20 years
Software	3 to 10 years

Goodwill and Other Intangibles

Goodwill is recorded to the extent that the purchase price exceeds the fair value of the assets acquired in accordance with Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets." Prior to the adoption of SFAS No. 142 on January 1, 2002, goodwill was being amortized on a straight-line basis over 15- to 40-year periods. Beginning January 1, 2002, goodwill is no longer being amortized, but instead is tested for impairment as discussed below.

Other intangibles with indefinite useful lives all relate to trademarks and trade names associated with the Tampa *Flyer* acquisition in April 2005, and were recorded at fair value in accordance with SFAS No. 142.

We assess the impairment of goodwill and other intangibles with indefinite lives in accordance with SFAS No. 142, by determining the fair value of each of our reporting units and comparing the fair value to the carrying value for each reporting unit. We have identified our reporting units as Direct Marketing and Shoppers. Fair value is determined using projected discounted future cash flows and cash flow multiple models, based on historical performance and management's estimate of future performance, giving consideration to existing and anticipated competitive and economic conditions. If a reporting unit's carrying amount exceeds its fair value, we must calculate the implied fair value of the reporting unit's goodwill and other intangibles with indefinite lives by allocating the reporting unit's fair value to all of its assets and liabilities (recognized and unrecognized) in a manner similar to a purchase price allocation, and then compare this implied fair value to its carrying amount. To the extent that the carrying amount of goodwill and other intangibles with indefinite lives exceeds its implied fair value, an impairment loss is recorded.

Both the Direct Marketing and Shoppers segments are tested for impairment as of November 30 of each year, after the annual forecasting process for the upcoming fiscal year has been completed. Based on the results of our impairment test, we have not recorded an impairment loss in any of the three years ended December 31, 2005.

The changes in the carrying amount of goodwill for the years ended December 31, 2005 and 2004, are as follows:

In thousands	Direct Marketing	Shoppers	Total
Balance at January 1, 2004	$312,810	$124,346	$437,156
Additional purchase consideration	19,430	1,585	21,015
Balance at December 31, 2004	$332,240	$125,931	$458,171
Additional purchase consideration	3,023	41,556	44,579
Balance at December 31, 2005	$335,263	$167,487	$502,750

As of December 31, 2005, the balance of other intangibles with indefinite lives was $7.6 million and was all related to the Shoppers segment. As of December 31, 2004, we did not have any intangibles with indefinite useful lives other than goodwill.

Other intangibles with definite useful lives are recorded on the basis of cost in accordance with SFAS No. 142 and are amortized on a straight-line basis over a period of 5 to 10 years. We assess the recoverability of other intangibles with definite lives by determining whether the amortization of the intangible balance over its remaining life can be recovered through projected undiscounted future cash flows over the remaining amortization period. If projected undiscounted future cash flows indicate that an unamortized intangible will not be recovered, an impairment loss is recognized based on projected discounted future cash flows. Cash flow projections are based on trends of historical performance and management's estimate of future performance, giving consideration to existing and anticipated competitive and economic conditions.

At December 31, 2005 the balance of other intangibles with definite useful lives was $9.1 million, net of $4.4 million of accumulated amortization and related to contact databases, client relationships and non-compete agreements. At December 31, 2004 the balance of other intangibles with definite useful lives was $2.1 million, net of $2.9 million of accumulated amortization. Amortization expense related to other intangibles with definite useful lives was $1.4 million, $0.6 million and $0.6 million for each of the years ended December 31, 2005, 2004 and 2003, respectively. Expected amortization expense is $1.6 million for the years ending December 31, 2006, 2007 and 2008, $1.5 million for the year ending December 31, 2009, and $1.2 million for the year ending December 31, 2010.

The changes in the carrying amount of other intangibles with definite useful lives for the years ended December 31, 2005 and 2004 are as follows:

In thousands	Direct Marketing	Shoppers	Total
Balance at January 1, 2004	$2,667	$ –	$2,667
Amortization expense	(600)	–	(600)
Balance at December 31, 2004	$2,067	$ –	$2,067
Additional purchase consideration	100	8,329	8,429
Amortization expense	(620)	(807)	(1,427)
Balance at December 31, 2005	$1,547	$7,522	$9,069

Income Taxes

Income taxes are calculated using the asset and liability method required by SFAS No. 109, "Accounting for Income Taxes." Deferred income taxes are recognized for the tax consequences resulting from timing differences by applying enacted statutory tax rates applicable to future years. These timing differences are associated with differences between the financial and the tax basis of existing assets and liabilities. Under SFAS No. 109, a statutory change in tax rates will be recognized immediately in deferred taxes and income.

Earnings per Share

Basic earnings per common share are based upon the weighted-average number of common shares outstanding. Diluted earnings per common share are based upon the weighted-average number of common shares outstanding and dilutive common stock equivalents from the assumed exercise of stock options using the treasury stock method.

Stock-Based Compensation

We have adopted the disclosure-only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation." Accordingly, no compensation expense has been recognized for options granted where the exercise price is equal to the market price of the underlying stock at the date of grant. For options issued with an exercise price below the market price of the underlying stock on the date of grant, compensation expense is recognized under the provisions of Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees," as permitted under SFAS No. 123.

Had compensation expense for options been determined based on the fair value at the grant date for awards since January 1, 1995, consistent with the provisions of SFAS No. 123, our net income and diluted earnings per share would have been reduced to the pro-forma amounts indicated below:

In thousands, except per share amounts	Year Ended December 31, 2005	2004	2003
Net income — as reported	$114,458	$97,568	$87,362
Stock-based employee compensation expense, included in reported net income, net of related tax effects	99	61	61
Stock-based employee compensation expense determined under fair-value based methods for all awards, net of related tax effects	(4,291)	(3,798)	(3,899)
Net income — pro forma	$110,266	$93,831	$83,524
Basic earnings per share — as reported	$ 1.37	$ 1.13	$ 0.99
Basic earnings per share — pro forma	$ 1.32	$ 1.09	$ 0.94
Diluted earnings per share — as reported	$ 1.34	$ 1.11	$ 0.97
Diluted earnings per share — pro forma	$ 1.29	$ 1.07	$ 0.93

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in 2005, 2004 and 2003:

	Year Ended December 31, 2005	2004	2003
Expected dividend yield	0.7%	0.7%	0.6%
Expected stock price volatility	25.6%	26.3%	27.2%
Risk-free interest rate	4.0%	3.8%	3.6%
Expected life of options	3-10 years	3-10 years	3-10 years

Revenue Recognition

We recognize revenue at the time the service is rendered or the product is delivered. Payments received in advance of the performance of services or delivery of the product are recorded as deferred revenue until such time as the services are performed or the product is delivered.

For all sales, we require either a purchase order, a statement of work signed by the client, a written contract, or some other form of written authorization from the client.

Our accounting policy for revenue recognition has an impact on our reported results and relies on certain estimates that require judgments on the part of management. The portion of our revenue that is most subject to estimates and judgments is revenue recognized using the percentage-of-completion method, as discussed below.

Specifically, Direct Marketing revenue from certain projects and certain services such as database build services, internet web design, market research and analytical services may be billed at hourly rates or a set price. If billed at a set price, the revenue is recognized over the contractual period, using the percentage-of-completion method. Management estimates and judgments are used in connection with the revenue recognized in these instances. Should actual costs differ significantly from the original estimated costs, the timing of revenues and overall profitability of the contract could be impacted. Contracts accounted for under the percentage-of-completion method constituted less than 7.5% of total Direct Marketing revenue and less than 4.5% of our total revenue for the years ended December 31, 2005, 2004 and 2003.

Direct Marketing revenue is derived from a variety of services and products. Revenue from services such as creative and graphics, printing, personalization of communication pieces using laser and inkjet printing, targeted mail, fulfillment, agency services and transportation logistics are recognized as the work is performed. Revenue is typically based on a set price or rate given to the client.

Revenue from the ongoing production and delivery of data is recognized upon completion and delivery of the work and is typically based on a set price or rate. Revenue from database subscriptions is based on a set price and is recognized ratably over the term of the subscription.

Revenue from database build services may be billed based on hourly rates or at a set price. If billed at a set price, the database build revenue is recognized using the percentage-of-completion method based on individual costs incurred to date compared with total estimated contract costs.

Revenue from market research and analytical services may be billed based on hourly rates or a set price. If billed at a set price, the revenue is recognized using the percentage-of-completion method based on individual costs incurred to date compared with total estimated contract costs. In other instances, progress toward completion is based on performance milestones specified in the contract where such milestones fairly reflect progress toward contract completion.

Revenue related to e-marketing, lead management, multi-channel customer care, inbound and outbound teleservices and technical support is typically billed based on a set price per transaction or service provided. Revenue from these services is recognized as the service or activity is performed.

Revenue from software is recognized in accordance with the American Institute of Certified Public Accountants' (AICPA) Statement of Position (SOP) 97-2 "Software Revenue Recognition," as amended by SOP 98-9 "Modification of SOP 97-2, Software Revenue Recognition." SOP 97-2 generally requires revenue earned on software arrangements involving multiple elements to be allocated to each element based on the vendor-specific objective evidence of fair values of the respective elements. For software sales with multiple elements (for example, software licenses with undelivered post-contract customer support or "PCS"), we allocate revenue to each component of the arrangement using the residual value method based on the fair value of the undelivered elements. This means we defer revenue from the software sale equal to the fair value of the undelivered elements. The fair value of PCS is based upon separate sales of renewals to other clients or upon renewal rates quoted in the contracts. The fair value of services, such as training and consulting, is based upon separate sales of these services to other clients.

The revenue allocated to PCS is recognized ratably over the term of the support period. Revenue allocated to professional services is recognized as the services are performed. The revenue allocated to software products, including time-based software licenses, is recognized, if collection is probable, upon execution of a licensing agreement and shipment of the software or ratably over the term of the license, depending on the structure and terms of the arrangement. If the licensing agreement is for a term of one year or less and includes PCS, we recognize the software and the PCS revenue ratably over the term of the license.

We apply the provisions of Emerging Issues Task Force Issue No. 00-03 "Application of AICPA Statement of Position 97-2 to Arrangements that Include the Right to Use Software Stored on Another Entity's Hardware" to our hosted software service transactions.

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

As described above, sometimes our customer arrangements have multiple deliverables, including service elements. Generally, our multiple-element arrangements fall within the scope of specific accounting standards that provide guidance regarding the separation of elements in multiple-deliverable arrangements and the allocation of consideration among those elements (e.g., AICPA SOP 97-2 "Software Revenue Recognition"). If not, we apply the provisions of Emerging Issues Task Force Issue No. 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables" (EITF 00-21). The provisions of EITF 00-21 require us to unbundle multiple element arrangements into separate units of accounting when the delivered element(s) has stand-alone value and fair value of the undelivered element(s) exist. When we are able to unbundle the arrangement into separate units of accounting, we apply one of the accounting policies described above to each unit. If we are unable to unbundle the arrangement into separate units of accounting, we apply one of the accounting policies described above to the entire arrangement. This might impact the timing of revenue recognition, but would not change the total revenue recognized from the arrangement.

Shoppers services are considered rendered, and the revenue recognized, when all printing, sorting, labeling and ancillary services have been provided and the mailing material has been received by the United States Postal Service.

Reserve for Healthcare, Workers' Compensation, Automobile and General Liability

We increased our deductible for individual healthcare claims from $150,000 to $175,000 and eliminated our aggregate annual claims deductible in 2005. We have a $250,000 deductible for automobile and general liability claims. Our deductible for workers' compensation decreased from $1.0 million to $500,000 in October 2003. Our insurance administrator provides us with estimated loss reserves, based upon its experience dealing with similar types of claims, as well as amounts paid to date against these claims. We apply actuarial factors to both insurance estimated loss reserves and to paid claims and then determine reserve levels, taking into account these calculations. Periodic changes to the reserve for workers' compensation, automobile and general liability are recorded as increases or decreases to insurance expense, which is included in the "Advertising, selling, general and administrative" line of our Consolidated Statement of Operations. Periodic changes to the reserve for healthcare are recorded as increases or decreases to employee benefits expense, which is included in the "Payroll" line of our Consolidated Statement of Operations.

Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (FASB) revised Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation" (SFAS No. 123). The revised SFAS No. 123, titled "Share-Based Payment" (SFAS No. 123R), focuses primarily on accounting for transactions in which an entity obtains employee services in exchange for share-based payment transactions. This revised Statement requires public entities to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost is then recognized over the period during which an employee is required to provide service in exchange for the award — the requisite service period (typically the vesting period). No compensation cost is recognized for equity instruments for which employees do not render the requisite service. The grant-date fair value of employee share options and similar instruments is to be estimated using option-pricing models adjusted for the unique characteristics of those instruments. This revised Statement supersedes APB Opinion No. 25 "Accounting for Stock Issued to Employees," and eliminates the alternative to use the intrinsic value method of accounting prescribed by APB No. 25. Under APB No. 25, issuing stock options to employees with an exercise price equal to the market price on the date of grant generally resulted in recognition of no compensation cost. SFAS No. 123R is effective for annual periods beginning after June 15, 2005. We currently follow the disclosure-only provisions of SFAS No. 123 as originally issued, and accordingly no compensation expense has been recognized in the financial statements for options granted where the exercise price is equal to the market price of the underlying stock at the date of grant. The adoption of SFAS No. 123R in our first fiscal quarter of 2006 will reduce our results of operation, but will not have a material impact on our overall financial position. The magnitude of the impact of adoption of SFAS No. 123R cannot be predicted at this time as it will depend on levels of share-based incentive awards granted in the future. However, had we adopted SFAS No. 123R in prior periods, the impact of that standard would have approximated the impact of SFAS No. 123 as described in the "Stock-Based Compensation" section of Note A. SFAS No. 123R also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under prior literature. This requirement will reduce cash flows from operating activities and increase cash flows from financing activities in periods after adoption. While we cannot estimate the magnitude of such amounts in the future because they depend on, among other things, when employees exercise stock options, the amounts of operating cash flows recognized for such excess tax deductions were $5.1 million, $3.8 million and $6.3 million for the years ended December 31, 2005, 2004 and 2003, respectively.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets," which addresses the measurement of exchanges of nonmonetary assets. SFAS No. 153 eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets, which was previously provided by APB Opinion No. 29, "Accounting for Nonmonetary Transactions," and replaces it with an exception for exchanges that do not have commercial substance. SFAS No. 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. SFAS No. 153 was effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. The adoption of SFAS

No. 153 did not affect our financial position or results of operations.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections." SFAS No. 154 replaces APB Opinion No. 20, "Accounting Changes" and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements." SFAS No. 154 changes the requirements for the accounting for and reporting of a change in accounting principle and applies to all voluntary changes and changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. This Statement requires retrospective application to prior periods' financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. This Statement will be effective for any accounting changes and corrections of errors made by us starting January 1, 2006. We do not believe the adoption of SFAS No. 154 will have a material impact on our financial position or results of operations.

In December 2004, the FASB issued Staff Position No. 109-2, "Accounting and Disclosure Guidance for the Foreign Repatriation Provision Within the American Jobs Creation Act of 2004" (2004 Act), which allows an enterprise time beyond the end of the financial reporting period covering the date of enactment to evaluate the effect of the 2004 Act on its plan for reinvestment or repatriation of foreign earnings for purposes of applying SFAS No. 109. There was no impact to our 2004 or 2005 consolidated financial statements as a result of adoption of Staff Position No. 109-2. We currently have no plans to repatriate funds under the provisions of the 2004 Act.

Note B – Acquisitions

In April 2005, we acquired substantially all of the assets of Flyer Printing Company, Inc. related to *The Flyer* located in Tampa, Florida. *The Flyer* is a weekly shopper publication delivered by mail with circulation of 955,000 in the Tampa, Florida metropolitan area. The combination of *The Flyer* with our existing shopper operations increased total shopper circulation to approximately 12 million weekly. The total cost of the transaction was approximately $61.7 million and was paid in cash. The total amount of goodwill recognized in this transaction was $41.6 million. Intangible assets recognized in this transaction that have definite useful lives and are subject to amortization, relating to client relationships and non-compete agreements, totaled $8.3 million. Intangible assets recognized in this transaction that are not subject to amortization, relating to trademarks and trade names, totaled $7.6 million. All goodwill and intangibles recognized as part of this acquisition were assigned to the Shoppers segment. The operating results of the acquired assets have been included in the accompanying Consolidated Financial Statements from the date of acquisition.

In February 2005, we acquired long-standing Australian partner Communiqué Direct, pursuant to a purchase option that we acquired in June 2003. Founded in 1992, Communiqué Direct, located in a north suburb of Sydney, Australia, was a privately held firm that provided a range of marketing and information services for the business-to-business sector across the Asia-Pacific region. The total cost of the transaction was approximately $1.6 million, which was paid in cash.

In December 2004, we acquired Postfuture, Inc., an e-mail service provider located in Richardson, Texas, that provides both e-mail technology and services, among them a platform that automates campaign and transactional e-mail delivery to support e-commerce, customer service, event communication, and lead nurturing. Postfuture's offerings are being integrated into several existing Harte-Hanks solution offerings, including Allink on Demand®, CI Technology Database, and Allink Agent®, among others.

In April 2004, we acquired *Dollar Saver*, a local shopper publication in the fast-growing Hemet area in Southern California — and converted it to the *PennySaver* brand.

In February 2004, we acquired Avellino Technologies Ltd., a leading provider of data profiling technology. We have integrated Trillium Software System® and the Avellino Discovery software solution. Joining these two solutions allows organizations, for the first time with one solution provider, to define, assess, improve and monitor how well data meets the needs of enterprise business processes. We still offer Trillium Software and Avellino Discovery as stand-alone products as well as an integrated solution within the Trillium Software System. Founded in 1997, Avellino Technologies Ltd. is located in Aldermaston, UK.

We did not make any acquisitions in 2003.

The total cash outlay in 2005 related to acquisitions was $63.3 million. The total cash outlay in 2004 for acquisitions was $29.7 million. The total cash outlay in 2003 for acquisitions, which related to acquisitions prior to 2003, was $0.3 million.

The operating results of the acquired companies have been included in the accompanying consolidated financial statements from the date of acquisition under the purchase method of accounting. We have not disclosed pro-forma amounts, including the operating results of prior years' acquisitions, as they are not considered material.

Note C – Long-Term Debt

Cash payments for interest were $1.7 million, $1.0 million, and $0.9 million for the years ended December 31, 2005, 2004 and 2003, respectively.

In thousands	December 31, 2005	2004
Revolving loan commitment, various interest rates based on Eurodollar (effective rate of 4.69% at December 31, 2005), due August 12, 2010	$62,000	$ –
Revolving loan commitment, various interest rates based on Eurodollar, due October 17, 2005	–	10,000
Less current maturities	–	(10,000)
	$62,000	$ –

Credit Facilities

On August 12, 2005, we entered into a five-year $125 million revolving credit facility (the "Credit Facility") with JPMorgan Chase Bank, N.A., as administrative agent. The Credit Facility replaced the existing revolving credit facility with JPMorgan Chase Bank, N.A., as administrative agent, which was scheduled to mature on October 18, 2005. The Credit Facility allows us to obtain revolving credit loans and provides for the issuance of letters of credit. For each borrowing under the Credit Facility, we can generally choose to have the interest rate for that borrowing calculated based on either JPMorgan Chase Bank's publicly announced New York prime rate or on a Eurodollar (as defined in our new Five-Year Credit Agreement) rate plus a spread. The spread is determined based on our total debt-to-EBITDA (as defined in our new Five-Year Credit Agreement) ratio then in effect, and ranges from .315% to .6%. There is a facility fee that we are also required to pay under the Credit Facility that is based on a rate applied to the total commitment amount under the Credit Facility (which is $125 million), regardless of how much of that commitment we have actually drawn upon. The facility fee rate ranges from .085% to .15%, depending on our total debt-to-EBITDA ratio then in effect. In addition, we will also be charged a letter-of-credit fee with respect to any outstanding letters of credit issued under this Credit Facility. That fee is calculated by applying a rate equal to the spread applicable to Eurodollar-based loans plus a fronting fee of .125% per annum to the average daily undrawn amount of the outstanding letters of credit.

Under the Credit Facility, we are required to maintain an interest coverage ratio of not less than 2.75 to 1 and a total debt-to-EBITDA ratio of not more than 3.0 to 1. The Credit Facility also contains covenants restricting our and our subsidiaries' ability to grant liens, enter into certain transactions and allow the total amount of indebtedness of our subsidiaries to exceed $20 million.

The Credit Facility also includes customary covenants regarding reporting obligations, delivery of notices regarding certain events, maintaining our corporate existence, payment of obligations, maintenance of our properties and insurance thereon at customary levels with financially sound and reputable insurance companies, maintaining books and records and compliance with applicable laws. The Credit Facility provides for customary events of default including nonpayment of principal or interest, breach of representations and warranties, violations of covenants, failure to pay certain other indebtedness, bankruptcy and material judgments and liabilities, certain violations of environmental laws or ERISA or the occurrence of a change of control. If we were not in compliance with any of these affirmative or negative covenants a default would occur and the lenders could terminate their commitments under the Credit Facility and declare all outstanding borrowings, interest and fees due. We have been in compliance with all covenants since obtaining the Credit Facility.

The Credit Facility does not contain any cross-default provisions.

Note D – Income Taxes

The components of income tax expense (benefit) are as follows:

In thousands	Year Ended December 31, 2005	2004	2003
Current			
Federal	$56,593	$47,081	$37,820
State and local	8,609	10,539	6,376
Foreign	264	818	300
Total current	$65,466	$58,438	$44,496
Deferred			
Federal	$ 5,130	$ 7,498	$10,825
State and local	471	801	2,435
Foreign	954	(1,337)	(1,213)
Total deferred	$ 6,555	$ 6,962	$12,047
Total income tax expense	$72,021	$65,400	$56,543

The differences between total income tax expense and the amount computed by applying the statutory federal income tax rate to income before income taxes were as follows:

In thousands	Year Ended December 31, 2005	%	2004	%	2003	%
Computed expected income tax expense	$65,269	35%	$57,039	35%	$50,367	35%
Net effect of state income taxes	5,960	3%	7,371	5%	5,717	4%
Change in the beginning of the year balance of the valuation allowance	(58)	0%	39	0%	10	0%
Other, net	850	1%	951	1%	449	0%
Income tax expense for the period	$72,021	39%	$65,400	40%	$56,543	39%

Total income tax expense (benefit) was allocated as follows:

In thousands	Year Ended December 31, 2005	2004	2003
Results of operations	$72,021	$65,400	$56,543
Stockholders' equity	(8,700)	(2,299)	(3,630)
Total	$63,321	$63,101	$52,913

The tax effects of temporary differences that gave rise to significant portions of the deferred tax assets and deferred tax liabilities were as follows:

In thousands	December 31, 2005	2004
Deferred tax assets		
Deferred compensation and retirement plan	$ 13,737	$ 10,291
Accrued expenses not deductible until paid	5,527	5,114
Accounts receivable, net	1,300	662
Other, net	219	211
State income tax	2,772	3,236
Foreign net operating loss carryforwards	1,185	2,201
State net operating loss carryforwards	251	682
Capital loss carryforward	492	492
Total gross deferred tax assets	25,483	22,889
Less valuation allowance	(743)	(1,174)
Net deferred tax assets	24,740	21,715
Deferred tax liabilities		
Property, plant and equipment	(16,051)	(16,830)
Goodwill	(47,802)	(39,274)
Total gross deferred tax liabilities	(63,853)	(56,104)
Net deferred tax liabilities	$(39,113)	$(34,389)

Net deferred taxes are recorded both as a current deferred income tax asset and as other long-term liabilities based upon the classification of the related timing difference. There are approximately $10.6 million and $7.9 million of deferred tax assets related to non-current items that are netted with long-term deferred tax liabilities at December 31, 2005 and 2004, respectively.

As of December 31, 2005 and 2004 we had net operating loss and capital loss carryforwards that are available to reduce future taxable income and that will begin to expire in 2006.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Based on the expectation of future taxable income and that the deductible temporary differences will offset existing taxable temporary differences, management believes it is more likely than not that we will realize the benefits of these deductible differences, net of the existing valuation allowances, at December 31, 2005 and December 31, 2004.

The valuation allowance for deferred tax assets as of January 1, 2004 was $1,089,000. The valuation allowance at December 31, 2005 and December 31, 2004 relates to federal capital loss and state net operating loss carryforwards which are not expected to be realized.

Deferred income taxes have not been provided on the undistributed earnings of our foreign subsidiaries as these earnings have been, and under current plans will continue to be, permanently reinvested in these subsidiaries. If those earnings were not considered permanently reinvested, U.S. federal deferred income taxes would have been recorded. However, it is not practicable to estimate the amount of additional taxes which may be payable upon distributions.

Cash payments for income taxes were $64.9 million, $50.1 million and $39.9 million in 2005, 2004 and 2003, respectively.

Note E – Employee Benefit Plans

Prior to January 1, 1999, we maintained a defined benefit pension plan for which most of our employees were eligible. In conjunction with significant enhancements to the 401(k) plan, we elected to freeze benefits under this defined benefit pension plan as of December 31, 1998.

In 1994, we adopted a non-qualified, supplemental pension plan covering certain employees, which provides for incremental pension payments so that total pension payments equal those amounts that would have been payable from the principal pension plan were it not for limitations imposed by income tax regulation. The benefits under this supplemental pension plan, which is an unfunded plan, will continue to accrue as if the principal pension plan had not been frozen.

The status of the defined benefit pension plans at year-end was as follows:

In thousands	Year Ended December 31, 2005	2004
Change in benefit obligation		
Benefit obligation at beginning of year	$113,532	$109,171
Service cost	738	561
Interest cost	7,024	6,568
Actuarial loss	10,106	1,973
Benefits paid	(4,833)	(4,741)
Benefit obligation at end of year	126,567	113,532
Change in plan assets		
Fair value of plan assets at beginning of year	95,438	89,210
Actual return on plan assets	5,956	10,918
Contributions	51	51
Benefits paid	(4,833)	(4,741)
Fair value of plan assets at end of year	96,612	95,438
Funded status	(29,955)	(18,094)
Unrecognized actuarial loss	44,656	35,062
Unrecognized prior service cost	365	426
Net amount recognized	$ 15,066	$ 17,394

The following amounts have been recognized in the Consolidated Balance Sheets:

In thousands	December 31, 2005	2004
Accrued benefit liability	$(27,363)	$(16,175)
Intangible asset	667	824
Accumulated other comprehensive loss	41,762	32,745
Net amount recognized	$ 15,066	$ 17,394

The minimum pension liability included in other comprehensive income increased $9.0 million during the year ended December 31, 2005, and decreased $3.8 million during the year ended December 31, 2004.

We are not required to make and do not intend to make a contribution to either pension plan in 2006 other than to the extent needed to cover benefit payments related to the unfunded plan.

The following information is presented for pension plans with an accumulated benefit obligation in excess of plan assets:

In thousands	December 31, 2005	2004
Projected benefit obligation	$126,567	$113,532
Accumulated benefit obligation	123,975	111,613
Fair value of plan assets	$ 96,612	$ 95,438

The non-qualified, unfunded pension plan had an accumulated benefit obligation of $14.2 million and $10.8 million at December 31, 2005 and 2004, respectively, and is included in the "Other long-term liabilities" line in the Consolidated Balance Sheets.

Net pension cost for both plans included the following components:

In thousands	Year Ended December 31,		
	2005	2004	2003
Service cost	$ 738	$ 561	$ 523
Interest cost	7,024	6,568	6,561
Expected return on plan assets	(7,917)	(7,396)	(5,964)
Amortization of prior service cost	61	64	65
Recognized actuarial loss	2,473	2,060	2,477
Net periodic benefit cost	$2,379	$1,857	$3,662

The weighted-average assumptions used for measurement of the defined pension plans were as follows:

	Year Ended December 31,		
	2005	2004	2003
Weighted-average assumptions used to determine net periodic benefit cost			
Discount rate	6.00%	6.25%	6.85%
Expected return on plan assets	8.50%	8.50%	9.00%
Rate of compensation increase	4.00%	4.00%	4.00%

	December 31, 2005	2004
Weighted-average assumptions used to determine benefit obligations		
Discount rate	5.75%	6.00%
Rate of compensation increase	4.00%	4.00%

The discount rate assumptions are based on current yields of investment-grade corporate long-term bonds. The expected long-term return on plan assets is based on the expected future average annual return for each major asset class within the plan's portfolio (which is principally comprised of equity investments) over a long-term horizon. In determining the expected long-term rate of return on plan assets, we evaluated input from its investment consultants, actuaries, and investment management firms including their review of asset class return expectations, as well as long-term historical asset class returns. Projected returns by such consultants and economists are based on broad equity and bond indices. Additionally, we considered our historical 15-year compounded returns, which have been in excess of the forward-looking return expectations.

The funded pension plan assets as of December 31, 2005 and 2004 by asset category are as follows:

In thousands	Year Ended December 31,			
	2005	%	2004	%
Equity securities	$73,735	76%	$67,815	71%
Debt securities	21,149	22%	26,516	28%
Other	1,728	2%	1,107	1%
Total plan assets	$96,612	100%	$95,438	100%

The expected future pension benefit payments as of December 31, 2005 are as follows:

In thousands	
2006	$ 4,948
2007	5,204
2008	5,731
2009	6,129
2010	6,744
2011 - 2015	38,944
	$67,699

The investment policy for the Harte-Hanks, Inc. Pension Plan focuses on the preservation and enhancement of the plan's assets through prudent asset allocation, quarterly monitoring and evaluation of investment results, and periodic meetings with investment managers.

The investment policy's goals and objectives are to meet or exceed the representative indices over a full market cycle (3-5 years). The policy establishes the following investment mix,

which is intended to subject the principal to an acceptable level of volatility while still meeting the desired return objectives:

	Target	Acceptable Range	Benchmark Index
Domestic equities	59.5%	35% - 75%	S&P 500
Large cap growth	30.0%	15% - 30%	Russell 1000 Growth
Large cap value	22.5%	15% - 30%	Russell 1000 Value
Mid cap value	7.0%	5% - 15%	Russell Mid Cap Value
Domestic fixed income	25.5%	20% - 50%	LB Aggregate
International equities	15.0%	10% - 25%	MSC1 EAFE

To address the issue of risk, the investment policy places high priority on the preservation of the value of capital (in real terms) over a market cycle. Investments are made in companies with a minimum five-year operating history and sufficient trading volume to facilitate, under most market conditions, prompt sale without severe market effect. Investments are diversified; reasonable concentration in any one issue, issuer, industry or geographic area is allowed if the potential reward is worth the risk.

Investment managers are evaluated by the performance of the representative indices over a full market cycle for each class of assets. The Pension Plan Committee reviews, on a quarterly basis, the investment portfolio of each manager, which includes rates of return, performance comparisons with the most appropriate indices, and comparisons of each manager's performance with a universe of other portfolio managers who employ the same investment style.

Prior to January 1, 1999, we also sponsored several 401(k) plans to provide employees with additional income upon retirement. We generally matched a portion of employees' voluntary before-tax contributions. Employees were fully vested in their own contributions and generally vested in matching contributions upon three years of service. Effective January 1, 1999, changes were made that combined all 401(k) plans and allowed for immediate vesting of enhanced matching contributions. Total 401(k) expense recognized in 2005, 2004 and 2003 was $6.6 million, $6.3 million and $6.1 million, respectively.

The 1994 Employee Stock Purchase Plan provides for a total of 6,000,000 shares to be sold to participating employees at 85% of the fair market value at specified quarterly investment dates. Shares available for sale totaled 2,652,103 at December 31, 2005.

Note F – Stockholders' Equity

In January 2006, we announced an increase in the regular quarterly dividend from 5.0 cents per share to 6.0 cents per share, payable March 15, 2006 to holders of record on March 1, 2006.

During 2005 we repurchased 4.3 million shares of our common stock for $114.2 million under our stock repurchase program. As of December 31, 2005 we have repurchased 43.5 million shares since the beginning of the stock repurchase program in January 1997. In November 2005 our Board of Directors authorized an additional 5 million shares under our stock repurchase program. Under this program, we had authorization to repurchase approximately 6.4 million additional shares at December 31, 2005.

During 2005 we received 0.2 million shares of our common stock, with an estimated market value of $4.7 million, in connection with stock option exercises. Since January 1997 we have received 1.5 million shares in exchange for proceeds related to stock option exercises.

On the following dates we purchased the following amounts of our common stock from Mr. Houston H. Harte: April 29, 2005, 100,000 shares for $28.44 per share; August 15, 2005, 100,000 shares for $27.33 per share; and October 31, 2005, 100,000 shares for $25.60 per share. All of these purchases were made at the closing price per share of our common stock on the date of purchase. Mr. Harte is a member of our Board of Directors.

Note G – Equity-Based Plans

In 1991 we adopted the 1991 Stock Option Plan (1991 Plan) pursuant to which we issued to officers and key employees options to purchase shares of common stock. Under the 1991 Plan, options were granted at exercise prices equal to the market price of the common stock on the grant date (1991 Plan market price options) and at exercise prices below market price of the common stock (1991 Plan performance options). In May 2005 we adopted the 2005 Omnibus Incentive Plan (2005 Plan) pursuant to which we may issue to officers and key employees up to 4,570,000 equity securities. No additional options will be granted under the 1991 Plan. Through December 31, 2005, all options granted under the 2005 Plan have been granted at exercise prices equal to the market price of the common stock on the grant date (2005 Plan market price options).

As of December 31, 2005, 2005 Plan market price options to purchase 111,000 shares were outstanding with exercise prices ranging from $25.76 to $29.05 per share. 2005 Plan market price options become exercisable in 25% increments on the second, third, fourth and fifth anniversaries of their date of grant. The weighted-average exercise price for outstanding 2005 Plan market price options at December 31, 2005 was $27.98. There were no exercisable 2005 Plan market price options at December 31, 2005. The weighted-average remaining life for outstanding 2005 Plan market price options was 9.52 years.

As of December 31, 2005, 2004 and 2003, 1991 Plan market price options to purchase 7,228,684 shares, 7,099,685 shares and 7,216,659 shares, respectively, were outstanding with exercise prices ranging from $8.54 to $26.88 per share at December 31, 2005. 1991 Plan market price options granted prior to January 1998 became exercisable after the fifth anniversary of their date of grant. Beginning January 1998, 1991 Plan market price options generally become exercisable in 25% increments on the second, third, fourth and fifth anniversaries of their date of grant. The weighted-average exercise price for outstanding 1991 Plan market price options and exercisable 1991 Plan market price options at December 31, 2005 was $18.13 and $14.83, respectively. The weighted-average remaining life for outstanding 1991 Plan market price options was 5.78 years.

At December 31, 2005, 2004 and 2003, 1991 Plan performance options to purchase 88,500 shares, 129,000 shares and

161,325 shares, respectively, were outstanding with exercise prices ranging from $0.67 to $1.33 per share at December 31, 2005. No 1991 Plan performance options have been granted since January 1999. The 1991 Plan performance options became exercisable in whole or in part after three years, and the extent to which they became exercisable at that time depended upon the extent to which we achieved certain goals established at the time the options were granted. Prior to December 2005, that portion of the 1991 Plan performance options that did not become exercisable at an earlier date became exercisable after the ninth anniversary of the date of grant. In December 2005 the remaining unvested 1991 Plan performance options, representing 51,000 shares of the Company's common stock at exercise prices of either $0.67 or $1.33 per share, were amended to comply with Section 409A of the Internal Revenue Code of 1986, as amended. Under this option amendment, these unvested 1991 Plan performance options will only be exercisable on the business day following the vesting date of each option. Compensation expense of $0.2 million, $0.1 million and $0.1 million was recognized for the 1991 Plan performance options during the years ended December 31, 2005, 2004 and 2003, respectively. The weighted-average exercise price for outstanding 1991 Plan performance options and exercisable 1991 Plan performance options at December 31, 2005, was $0.84 and $0.82, respectively. The weighted-average remaining life for outstanding 1991 Plan performance options was 1.8 years.

The following summarizes all stock option activity during 2005, 2004 and 2003:

	Number of Shares	Weighted Average Option Price
Options outstanding at January 1, 2003	9,018,752	$12.92
Granted	318,300	$18.04
Exercised	(1,533,296)	6.87
Cancelled	(425,772)	16.15
Options outstanding at December 31, 2003	7,377,984	$14.21
Granted	1,269,750	22.46
Exercised	(1,051,038)	10.68
Cancelled	(368,011)	17.35
Options outstanding at December 31, 2004	7,228,685	$16.01
Granted	1,220,050	25.88
Exercised	(773,890)	9.98
Cancelled	(246,661)	21.82
Options outstanding at December 31, 2005	7,428,184	$18.07
Exercisable at December 31, 2005	3,893,118	$14.70

The following table summarizes information about stock options outstanding at December 31, 2005:

	Outstanding			Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Life (Years)	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$ 0.67 – 11.92	971,677	1.59	$ 9.69	920,677	$10.18
$13.04 – 14.63	798,605	4.03	$ 13.86	784,170	$13.86
$14.67 – 15.63	790,355	4.86	$ 14.83	607,568	$14.85
$15.75 – 17.45	922,527	4.39	$ 16.58	808,871	$16.48
$17.98 – 18.61	969,695	6.11	$ 18.21	448,007	$18.22
$18.79 – 21.23	692,125	6.76	$ 19.87	319,625	$19.91
$22.03 – 25.48	1,130,000	8.16	$ 22.50	4,200	$23.10
$25.63 – 29.05	1,153,200	9.12	$ 25.90	–	–
	7,428,184	5.79	$ 18.07	3,893,118	$14.70

The weighted-average fair value of market price options granted during 2005, 2004 and 2003 was $8.30, $7.26 and $5.96, respectively. No performance options were granted during the three-year period ended December 31, 2005.

Note H – Fair Value of Financial Instruments

Because of their maturities and/or variable interest rates, certain financial instruments have fair values approximating their carrying values. These instruments include revolving credit agreements, accounts receivable and trade payables.

Note I – Commitments and Contingencies

At December 31, 2005, we had letters of credit in the amount of $25.0 million. No amounts were drawn against these letters of credit at December 31, 2005. These letters of credit exist to support insurance programs relating to workers' compensation, automobile and general liability, and leases.

From time to time we become involved in various claims and lawsuits incidental to our businesses. In the opinion of management, after consultation with counsel, any ultimate liability arising out of currently pending claims and lawsuits is not expected to have a material effect on our financial condition or operations.

Note J – Leases

We lease certain real estate and equipment under various operating leases. Most of the leases contain renewal options for varying periods of time. The total rent expense applicable to operating leases was $27.5 million, $27.5 million and $29.2 million for the years ended December 31, 2005, 2004 and 2003, respectively.

Step rent provisions and escalation clauses, capital improvement funding, and other lease concessions are taken into account in computing minimum lease payments. We recognize the minimum lease payments on a straight-line basis over the minimum lease term.

Note K – Selected Quarterly Data (Unaudited)

In thousands, except per share amounts	2005 Quarter Ended December 31	September 30	June 30	March 31	2004 Quarter Ended December 31	September 30	June 30	March 31
Revenues	$300,955	$281,735	$284,010	$268,293	$277,491	$262,566	$254,152	$236,252
Operating income	51,269	48,605	47,820	42,319	47,333	43,506	42,898	31,558
Net income	31,433	28,825	29,127	25,073	27,580	25,653	25,546	18,789
Basic earnings per share	$ 0.38	$ 0.34	$ 0.34	$ 0.30	$ 0.32	$ 0.30	$ 0.30	$ 0.21
Diluted earnings per share	$ 0.38	$ 0.34	$ 0.34	$ 0.29	$ 0.32	$ 0.29	$ 0.29	$ 0.21

The future minimum rental commitments for all non-cancelable operating leases with terms in excess of one year as of December 31, 2005 are as follows:

In thousands	
2006	$23,556
2007	20,201
2008	15,554
2009	12,174
2010	8,987
After 2010	13,249
	$93,721

Note L – Earnings Per Share

A reconciliation of basic and diluted earnings per share (EPS) is as follows:

In thousands except per share amounts	Year Ended December 31, 2005	2004	2003
Basic EPS Net income	$114,458	$97,568	$87,362
Weighted-average common shares outstanding used in earnings-per-share computations	83,734	86,169	88,541
Earnings per share	$ 1.37	$ 1.13	$ 0.99
Diluted EPS Net income	$114,458	$97,568	$87,362
Shares used in diluted earnings-per-share computations	85,406	87,806	89,982
Earnings per share	$ 1.34	$ 1.11	$ 0.97
Computation of Shares Used in Earnings-per-Share Computations			
Average outstanding common shares	83,734	86,169	88,541
Average common equivalent shares — dilutive effect of option shares	1,672	1,637	1,441
Shares used in diluted earnings-per-share computations	85,406	87,806	89,982

For the purpose of calculating the shares used in the diluted EPS calculations, 42,000, 109,000 and 56,000 anti-dilutive market price options have been excluded from the EPS calculations for the years ended December 31, 2005, 2004 and 2003, respectively.

Note M – Business Segments

We are a worldwide direct and targeted marketing company, with operations in two segments — Direct Marketing and Shoppers.

Direct marketing services are targeted to specific industries or markets, with services and software products tailored to each industry or market. Currently, our Direct Marketing business serves various vertical markets including retail, high-tech/telecom, financial services, pharmaceutical/healthcare, and a wide range of selected markets. Depending on the needs of our clients, our Direct Marketing capabilities are provided in an integrated approach through 37 facilities worldwide, 11 of which are located outside of the United States. These centers each possess some specialization and are linked together to support the needs of our clients. We utilize various capabilities and technologies to enable our clients to identify, reach, influence and nurture their customers. Harte-Hanks Direct Marketing provides a range of services organized around five solution points: Construct and update the database — Access the data — Analyze the data — Apply the knowledge — Execute the programs.

Harte-Hanks Shoppers is North America's largest owner, operator and distributor of shopper publications, based on weekly circulation and revenues. Shoppers are weekly advertising publications delivered free by Standard Mail to households and businesses in a particular geographic area. Shoppers offer advertisers a targeted, cost-effective local advertising system, with high penetration in their area of distribution. As of December 31, 2005, our shoppers are zoned into 1,047 separate editions with total circulation in excess of 12 million in California and Florida each week. Shoppers are particularly effective in large markets with high media fragmentation in which major metropolitan newspapers generally have low penetration. Our Shoppers clients range from large national companies to local neighborhood businesses to individuals with a single item for sale.

In thousands	Year Ended December 31, 2005	2004	2003
Revenues			
Direct Marketing	$ 694,558	$ 641,214	$ 584,804
Shoppers	440,435	389,247	359,772
Total revenues	$ 1,134,993	$ 1,030,461	$ 944,576
Operating income			
Direct Marketing	$ 108,095	$ 90,856	$ 76,641
Shoppers	94,231	85,857	78,007
Corporate Activities	(12,313)	(11,418)	(8,161)
Total operating income	$ 190,013	$ 165,295	$ 146,487
Income before income taxes			
Operating income	$ 190,013	$ 165,295	$ 146,487
Interest expense	(1,957)	(1,020)	(855)
Interest income	197	341	168
Other, net	(1,774)	(1,648)	(1,895)
Total income before income taxes	$ 186,479	$ 162,968	$ 143,905
Depreciation			
Direct Marketing	$ 23,721	$ 22,518	$ 23,908
Shoppers	6,174	5,621	5,493
Corporate Activities	23	30	32
Total depreciation	$ 29,918	$ 28,169	$ 29,433
Goodwill and intangible amortization			
Direct Marketing	$ 620	$ 600	$ 600
Shoppers	807	–	–
Total goodwill and intangible amortization	$ 1,427	$ 600	$ 600
Capital expenditures			
Direct Marketing	$ 18,264	$ 22,587	$ 18,526
Shoppers	9,914	12,556	13,365
Corporate Activities	37	3	24
Total capital expenditures	$ 28,215	$ 35,146	$ 31,915
Total assets			
Direct Marketing	$ 567,512	$ 574,033	
Shoppers	279,241	203,587	
Corporate Activities	42,910	50,733	
Total assets	$ 889,663	$ 828,353	
Goodwill			
Direct Marketing	$ 335,263	$ 332,240	
Shoppers	167,487	125,931	
Total goodwill	$ 502,750	$ 458,171	
Other intangible assets			
Direct Marketing	$ 1,547	$ 2,067	
Shoppers	15,122	–	
Total other intangible assets	$ 16,669	$ 2,067	

The segment's core clients are local service businesses and small retailers. Shoppers' client base is entirely domestic.

Included in Corporate Activities are general corporate expenses. Assets of Corporate Activities include unallocated cash, investments and deferred income taxes.

Information about our operations in different business segments is set forth below based on the nature of the products and services offered. We evaluate performance based on several factors, of which the primary financial measures are segment revenues and operating income. The accounting policies of the business segments are the same as those described in the summary of significant accounting policies (Note A).

Information about the operations in different geographic areas:

	Year Ended December 31,		
In thousands	2005	2004	2003
Revenues[a]			
United States	$1,068,981	$ 974,258	$ 896,788
Other countries	66,012	56,203	47,788
Total revenues	$1,134,993	$1,030,461	$ 944,576
Long-lived net assets[b]			
United States	$ 101,366	$ 104,877	
Other countries	11,545	8,893	
Total long-lived assets	$ 112,911	$ 113,770	

[a] Geographic revenues are based on the location of the client.
[b] Long-lived assets are based on physical location.

The Board of Directors and Stockholders

Harte-Hanks, Inc.:

We have audited the accompanying consolidated balance sheets of Harte-Hanks, Inc. and subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of operations, cash flows, and the stockholders' equity and comprehensive income for each of the years in the three-year period ended December 31, 2005. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Harte-Hanks, Inc. and subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2005, in conformity with accounting principles generally accepted in the United States.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 16, 2006, expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

KPMG LLP

San Antonio, Texas
March 16, 2006

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

We are responsible for the preparation and integrity of the consolidated financial statements appearing in our Annual Report. The consolidated financial statements were prepared in conformity with accounting principles generally accepted in the United States and include amounts based on management's estimates and judgments. All other financial information in this report has been presented on a basis consistent with the information included in the financial statements.

We are also responsible for establishing and maintaining adequate internal controls over financial reporting. We maintain a system of internal controls that is designed to provide reasonable assurance as to the fair and reliable preparation and presentation of the consolidated financial statements, as well as to safeguard assets from unauthorized use or disposition.

Our control environment is the foundation for our system of internal controls over financial reporting. It sets the tone of our organization and includes factors such as integrity and ethical values. Our internal controls over financial reporting are supported by formal policies and procedures that are reviewed, modified and improved as changes occur in business conditions and operations.

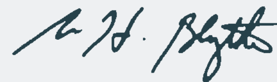
The Audit Committee of the Board of Directors, which is composed solely of outside directors, meets periodically with members of management, the internal auditors and the independent auditors to review and discuss internal controls over financial reporting and accounting and financial reporting matters. Our independent registered public accounting firm and internal auditors report to the Audit Committee and accordingly have full and free access to the Audit Committee at any time.

We conducted an evaluation of the effectiveness of our internal controls over financial reporting based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). This evaluation included review of the documentation of controls, evaluation of the design effectiveness of controls, testing of the operating effectiveness of controls and a conclusion on this evaluation. Based on our evaluation, we concluded that internal control over financial reporting was effective as of December 31, 2005.

KPMG LLP, an independent registered public accounting firm, has issued an attestation report on management's assessment of internal control over financial reporting, which is included herein.

March 16, 2006

Richard Hochhauser
President and Chief Executive Officer



Dean Blythe
Senior Vice President and
Chief Financial Officer

Jessica Huff
Vice President, Finance and
Chief Accounting Officer

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders

Harte-Hanks, Inc.:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control Over Financial Reporting, that Harte-Hanks, Inc. and subsidiaries maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The management of Harte-Hanks is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

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

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

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

In our opinion, management's assessment that Harte-Hanks, Inc. and subsidiaries maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in Internal Control — Integrated Framework issued by COSO. Also, in our opinion, Harte-Hanks, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on the criteria established in Internal Control — Integrated Framework issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Harte-Hanks, Inc. and subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of operations, cash flows, and stockholders' equity and comprehensive income for each of the years in the three-year period ended December 31, 2005 and our report dated March 16, 2006 expressed an unqualified opinion on those consolidated financial statements.

KPMG LLP

San Antonio, Texas
March 16, 2006

FIVE-YEAR FINANCIAL SUMMARY

In thousands, except per share amounts	2005	2004	2003	2002	2001
Statement of Operations Data					
Revenues	$1,134,993	$1,030,461	$944,576	$908,777	$917,928
Operating expenses					
Payroll, production and distribution	825,568	755,715	692,170	652,243	653,002
Advertising, selling, general and administrative	88,067	80,682	75,886	73,518	76,376
Depreciation	29,918	28,169	29,433	32,128	32,079
Goodwill and intangible amortization	1,427	600	600	600	16,841
Total operating expenses	944,980	865,166	798,089	758,489	778,298
Operating income	190,013	165,295	146,487	150,288	139,630
Interest expense, net	1,760	679	687	934	2,578
Net Income	114,458	97,568	87,362	90,745	79,684
Earnings per common share—diluted	1.34	1.11	0.97	0.96	0.82
Cash dividends per common share	0.20	0.16	0.12	0.10	0.08
Weighted-average common and common equivalent shares outstanding—diluted	85,406	87,806	89,982	94,872	97,174
Adjusted data to exclude amortization of goodwill, net of tax effect[a]					
Net Income	114,458	97,568	87,362	90,745	91,700
Earnings per common share—diluted	1.34	1.11	0.97	0.96	0.94
Segment Data					
Revenues					
Direct Marketing	694,558	641,214	584,804	573,826	601,901
Shoppers	440,435	389,247	359,772	334,951	316,027
Total revenues	$1,134,993	$1,030,461	$944,576	$908,777	$917,928
Operating income					
Direct Marketing	$ 108,095	$ 90,856	$ 76,641	$ 83,872	$ 85,020
Shoppers	94,231	85,857	78,007	74,564	63,398
General corporate	(12,313)	(11,418)	(8,161)	(8,148)	(8,788)
Total operating income	$ 190,013	$ 165,295	$146,487	$150,288	$139,630
Operating income excluding amortization of goodwill[a]					
Direct Marketing	$ 108,095	$ 90,856	$ 76,641	$ 83,872	$ 97,171
Shoppers	94,231	85,857	78,007	74,564	67,470
General corporate	(12,313)	(11,418)	(8,161)	(8,148)	(8,788)
Total operating income	$ 190,013	$ 165,295	$146,487	$150,288	$155,853
Capital expenditures	$ 28,215	$ 35,146	$ 31,915	$ 17,358	$ 26,445
Balance sheet data (at end of period)					
Property, plant and equipment, net	$ 112,911	$ 113,770	$ 97,747	$ 94,154	$109,428
Goodwill and other intangibles, net	519,419	460,238	439,823	440,067	438,325
Total assets	889,663	828,353	759,130	736,732	771,049
Total long term debt	62,000	–	5,000	16,300	48,312
Total stockholders' equity	$ 561,346	$ 571,799	$555,598	$532,533	$552,366

[a] Effective January 1, 2002, we adopted the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets," which established new accounting and reporting requirements for goodwill and other intangible assets and eliminated the amortization of goodwill. See Note A of the "Notes to Consolidated Financial Statements" for further discussion of SFAS No. 142.

Common Stock

Our common stock is listed on the New York Stock Exchange (symbol: HHS). The reported high and low quarterly sales price ranges for 2005 and 2004 were as follows:

	2005		2004	
	High	Low	High	Low
First Quarter	27.62	25.24	23.42	21.38
Second Quarter	30.98	26.11	24.88	22.51
Third Quarter	30.18	25.62	25.68	23.56
Fourth Quarter	26.82	25.39	27.00	24.13

In 2005, quarterly dividends were paid at the rate of 5.0 cents per share. In 2004, quarterly dividends were paid at the rate of 4.0 cents per share.

In January 2006, we announced an increase in the regular quarterly dividend from 5.0 cents per share to 6.0 cents per share, payable March 15, 2006 to holders of record on March 1, 2006.

As of March 1, 2006, there are approximately 2,900 holders of record.

Transfer Agent and Registrar

Computershare Trust Company, N.A.
P.O. Box 43078
Providence, RI 02940-3078
Shareholder Inquiries: (781) 575-4593
www.computershare.com

Annual Meeting of Stockholders

The annual meeting of stockholders will be held at 10:00 a.m. on May 16, 2006, at 200 Concord Plaza Drive, First Floor, San Antonio, Texas.

Form 10-K Annual Report

A copy of the Company's annual report on Form 10K as filed with the Securities and Exchange Commission ("SEC") may be accessed free of charge on our website at *http://www.harte-hanks.com* or on the SEC's website at *http://www.sec.gov*. Additionally, you can obtain a copy of this document, free of charge, upon written request to:

Sloane Levy, Secretary
Harte-Hanks, Inc.
P.O. Box 269
San Antonio, Texas 78291-0269

DIRECTORS

David L. Copeland
President, SIPCO, Inc.

William F. Farley
Founder & Owner, Livingston Capital

Larry Franklin
Chairman

William K. Gayden
Chairman & Chief Executive Officer, Merit Energy Company

Christopher M. Harte
Private Investor

Houston H. Harte
Vice Chairman

Richard Hochhauser
President & Chief Executive Officer

Judy C. Odom
Private Investor
Co-Founder, Former Chairman & Chief Executive Officer, Software Spectrum, Inc.

OFFICERS

Richard Hochhauser
President & Chief Executive Officer

Peter Gorman
Executive Vice President, Shoppers

Dean Blythe
Senior Vice President & Chief Financial Officer

Kathy Calta
Senior Vice President, Direct Marketing

Bill Carman
Senior Vice President, Shoppers

James Davis
Senior Vice President, Direct Marketing

Bill Goldberg
Senior Vice President, Direct Marketing

Gary Skidmore
Senior Vice President, Direct Marketing

Robert J. Colucci
Vice President, Direct Marketing

Loren Dalton
Vice President, Shoppers

Carlos Guzman
Vice President, Shoppers

Frank Harvey
Vice President, Direct Marketing

Jessica Huff
Vice President, Finance & Chief Accounting Officer

Spencer Joyner, Jr.
Vice President, Direct Marketing

Dave LaGreca
Vice President, Direct Marketing

Sloane Levy
Vice President, General Counsel & Secretary

Federico Ortiz
Vice President, Tax

Michael Paulsin
Vice President, Shoppers

Tann Tueller
Vice President, Direct Marketing

CORPORATE OFFICE

San Antonio, Texas
http://www.harte-hanks.com

DIRECT MARKETING

Austin, Texas
Baltimore, Maryland
Billerica, Massachusetts
Bloomfield, Connecticut
Cincinnati, Ohio
Clearwater, Florida
Deerfield Beach, Florida
East Bridgewater, Massachusetts
Fort Worth, Texas
Fullerton, California
Glen Burnie, Maryland
Grand Prairie, Texas
Jacksonville, Florida
Lake Mary, Florida
Langhorne, Pennsylvania
Monroe Township, New Jersey
New York, New York
Ontario, California
Pennsauken, New Jersey
Richardson, Texas
River Edge, New Jersey
San Diego, California
Shawnee, Kansas
Sterling Heights, Michigan
Westville, New Jersey
Wilkes-Barre, Pennsylvania

NATIONAL MARKETS HEADQUARTERS

Cincinnati, Ohio

INTERNATIONAL OFFICES

Aldermaston, United Kingdom
Dublin, Ireland
Frenchs Forest, Australia
Hasselt, Belgium
Madrid, Spain
Manila, Philippines
Melbourne, Australia
São Paulo, Brazil
Sèvres, France
Stuttgart, Germany
Uxbridge, United Kingdom

SHOPPERS

The Flyer
South Florida
Central-West Florida
http://www.theflyer.com

PennySaver
Northern California
Southern California — Greater Los Angeles Area
Southern California — Greater San Diego Area
http://www.pennysaverusa.com

We make it happen.

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(210) 829-9000 • www.harte-hanks.com

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