

DEERE & CO  
Form 10-Q  
February 26, 2009

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

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**FORM 10-Q**

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

**For the quarterly period ended January 31, 2009**

Commission file no: 1-4121

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**DEERE & COMPANY**

**Delaware**  
(State of incorporation)

**36-2382580**  
(IRS employer identification no.)

**One John Deere Place**

**Moline, Illinois 61265**

(Address of principal executive offices)

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Telephone Number: **(309) 765-8000**

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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

Large Accelerated Filer	<input checked="" type="checkbox"/>	Accelerated Filer	<input type="checkbox"/>
Non-Accelerated Filer	<input type="checkbox"/>	Smaller Reporting Company	<input type="checkbox"/>

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

At January 31, 2009, 422,672,599 shares of common stock, \$1 par value, of the registrant were outstanding.

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## PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

## DEERE &amp; COMPANY

## STATEMENT OF CONSOLIDATED INCOME

For the Three Months Ended January 31, 2009 and 2008

(In millions of dollars and shares except per share amounts) Unaudited

	2009	2008
<b>Net Sales and Revenues</b>		
Net sales	\$ 4,560.2	\$ 4,530.6
Finance and interest income	466.6	527.9
Other income	119.1	142.5
<b>Total</b>	<b>5,145.9</b>	<b>5,201.0</b>
<b>Costs and Expenses</b>		
Cost of sales	3,542.5	3,361.8
Research and development expenses	219.4	204.3
Selling, administrative and general expenses	638.9	652.8
Interest expense	274.5	295.1
Other operating expenses	196.9	155.5
<b>Total</b>	<b>4,872.2</b>	<b>4,669.5</b>
<b>Income of Consolidated Group before Income Taxes</b>	<b>273.7</b>	<b>531.5</b>
Provision for income taxes	73.5	170.0
<b>Income of Consolidated Group</b>	<b>200.2</b>	<b>361.5</b>
Equity in income of unconsolidated affiliates	3.7	7.6
<b>Net Income</b>	<b>\$ 203.9</b>	<b>\$ 369.1</b>
<b>Per Share Data</b>		
Net income - basic	\$ .48	\$ .84
Net income - diluted	\$ .48	\$ .83
<b>Average Shares Outstanding</b>		
Basic	422.5	437.7
Diluted	423.7	444.2

See Condensed Notes to Interim Financial Statements.

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DEERE & COMPANY  
CONDENSED CONSOLIDATED BALANCE SHEET  
(In millions of dollars) Unaudited

	January 31 2009	October 31 2008	January 31 2008
<b>Assets</b>			
Cash and cash equivalents	\$ 5,004.1	\$ 2,211.4	\$ 1,496.3
Marketable securities	230.5	977.4	1,153.6
Receivables from unconsolidated affiliates	45.3	44.7	39.2
Trade accounts and notes receivable - net	3,475.4	3,234.6	3,199.3
Financing receivables - net	13,379.3	16,017.0	15,233.1
Restricted financing receivables - net	3,268.9	1,644.8	1,960.6
Other receivables	688.8	664.9	648.7
Equipment on operating leases - net	1,543.7	1,638.6	1,628.4
Inventories	3,836.6	3,041.8	3,288.8
Property and equipment - net	4,149.4	4,127.7	3,651.7
Investments in unconsolidated affiliates	213.7	224.4	157.1
Goodwill	1,241.0	1,224.6	1,248.3
Other intangible assets - net	152.0	161.4	131.2
Retirement benefits	1,131.8	1,106.0	2,016.5
Deferred income taxes	1,419.9	1,440.6	1,451.4
Other assets	1,559.2	974.7	911.1
<b>Total Assets</b>	<b>\$ 41,339.6</b>	<b>\$ 38,734.6</b>	<b>\$ 38,215.3</b>
<b>Liabilities and Stockholders Equity</b>			
Short-term borrowings	\$ 9,333.2	\$ 8,520.5	\$ 9,461.6
Payables to unconsolidated affiliates	118.6	169.2	174.4
Accounts payable and accrued expenses	5,524.5	6,393.6	5,519.3
Deferred income taxes	166.2	171.8	188.4
Long-term borrowings	16,574.7	13,898.5	12,344.4
Retirement benefits and other liabilities	3,067.5	3,048.3	3,488.8
<b>Total liabilities</b>	<b>34,784.7</b>	<b>32,201.9</b>	<b>31,176.9</b>
<b>Commitments and contingencies (Note 5)</b>			
Common stock, \$1 par value (issued shares at January 31, 2009 - 536,431,204)	2,968.2	2,934.0	2,882.4
Common stock in treasury	(5,582.7)	(5,594.6)	(4,449.4)
Retained earnings	10,666.1	10,580.6	9,243.4
Accumulated other comprehensive income (loss)	(1,496.7)	(1,387.3)	(638.0)
Stockholders equity	6,554.9	6,532.7	7,038.4
<b>Total Liabilities and Stockholders Equity</b>	<b>\$ 41,339.6</b>	<b>\$ 38,734.6</b>	<b>\$ 38,215.3</b>

DEERE & COMPANY  
 STATEMENT OF CONSOLIDATED CASH FLOWS  
 For the Three Months Ended January 31, 2009 and 2008  
 (In millions of dollars) Unaudited

	2009	2008
<b>Cash Flows from Operating Activities</b>		
Net income	\$ 203.9	\$ 369.1
Adjustments to reconcile net income to net cash used for operating activities:		
Provision for doubtful receivables	40.0	17.4
Provision for depreciation and amortization	216.9	199.7
Share-based compensation expense	45.7	45.5
Undistributed earnings of unconsolidated affiliates	(3.9)	(5.8)
Provision (credit) for deferred income taxes	29.9	(20.2)
Changes in assets and liabilities:		
Trade, notes and financing receivables related to sales	(283.0)	53.0
Inventories	(874.0)	(1,013.0)
Accounts payable and accrued expenses	(882.4)	(378.8)
Accrued income taxes payable/receivable	(12.9)	183.1
Retirement benefits	6.7	(195.2)
Other	(102.4)	(79.8)
Net cash used for operating activities	(1,615.5)	(825.0)
<b>Cash Flows from Investing Activities</b>		
Collections of receivables	3,381.2	3,118.3
Proceeds from sales of financing receivables	5.7	6.6
Proceeds from maturities and sales of marketable securities	764.4	692.8
Proceeds from sales of equipment on operating leases	117.9	125.2
Proceeds from sales of businesses, net of cash sold		18.4
Cost of receivables acquired	(2,613.8)	(2,723.8)
Purchases of marketable securities	(7.9)	(220.4)
Purchases of property and equipment	(262.1)	(233.1)
Cost of equipment on operating leases acquired	(74.6)	(79.2)
Acquisitions of businesses, net of cash acquired	(40.9)	(34.0)
Other	1.9	(14.0)
Net cash provided by investing activities	1,271.8	656.8
<b>Cash Flows from Financing Activities</b>		
Increase (decrease) in short-term borrowings	1,157.1	(116.2)
Proceeds from long-term borrowings	2,842.2	1,037.7
Payments of long-term borrowings	(653.1)	(1,039.9)
Proceeds from issuance of common stock	3.1	68.7
Repurchases of common stock	(3.2)	(481.5)
Dividends paid	(118.2)	(110.4)
Excess tax benefits from share-based compensation	.5	35.1
Other	(96.0)	(1.2)
Net cash provided by (used for) financing activities	3,132.4	(607.7)
<b>Effect of Exchange Rate Changes on Cash and Cash Equivalents</b>	4.0	(6.4)
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	2,792.7	(782.3)
<b>Cash and Cash Equivalents at Beginning of Period</b>	2,211.4	2,278.6
<b>Cash and Cash Equivalents at End of Period</b>	\$ 5,004.1	\$ 1,496.3

See Condensed Notes to Interim Financial Statements.

Condensed Notes to Interim Financial Statements (Unaudited)

(1) The consolidated financial statements of Deere & Company and consolidated subsidiaries have been prepared by the Company, without audit, pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the U.S. have been condensed or omitted as permitted by such rules and regulations. All adjustments, consisting of normal recurring adjustments, have been included. Management believes that the disclosures are adequate to present fairly the financial position, results of operations and cash flows at the dates and for the periods presented. It is suggested that these interim financial statements be read in conjunction with the financial statements and the notes thereto included in the Company's latest annual report on Form 10-K. Results for interim periods are not necessarily indicative of those to be expected for the fiscal year.

The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts and related disclosures. Actual results could differ from those estimates.

Certain items previously reported in specific financial statement captions in the first quarter of 2008 have been reclassified to conform to the year end 2008 and first quarter of 2009 financial statement presentation. In particular, Accrued taxes previously presented separately has been combined with Accounts payable and accrued expenses on the consolidated balance sheet.

Cash Flow Information

All cash flows from the changes in trade accounts and notes receivable are classified as operating activities in the Statement of Consolidated Cash Flows as these receivables arise from sales to the Company's customers. Cash flows from financing receivables that are related to sales to the Company's customers are also included in operating activities. The remaining financing receivables are related to the financing of equipment sold by independent dealers and are included in investing activities.

The Company had the following non-cash operating and investing activities that were not included in the Statement of Consolidated Cash Flows. The Company transferred inventory to equipment on operating leases of approximately \$34 million and \$57 million in the first three months of 2009 and 2008, respectively. The Company also had non-cash transactions for accounts payable related to purchases of property and equipment of approximately \$118 million and \$83 million at January 31, 2009 and 2008, respectively.

Variable Interest Entities

The Company is the primary beneficiary and consolidates a supplier that is a variable interest entity (VIE). The Company would absorb more than a majority of the VIE's expected losses based on a cost sharing supply contract. No additional support beyond what was previously contractually required has been provided during the first quarter of 2009. The VIE produces blended fertilizer and other lawn care products for the commercial and consumer equipment segment. The assets of the VIE that were consolidated, less the intercompany receivables of \$26

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million eliminated in consolidation, totaled \$88 million and consisted of \$79 million of inventory, \$6 million of property and equipment and \$3 million of other assets. The liabilities of the VIE totaled \$126 million and consisted of \$101 million of accounts payable and accrued expenses and \$25 million of short-term borrowings. The VIE is financed through its own accounts payable and short-term borrowings. The assets of the VIE can only be used to settle the obligations of the VIE. The creditors of the VIE do not have recourse to the general credit of the Company. See Note 6 for VIEs related to securitization of financing receivables.



(2) The information in the notes and related commentary are presented in a format which includes data grouped as follows:

**Equipment Operations** - Includes the Company's agricultural equipment, commercial and consumer equipment and construction and forestry operations with Financial Services reflected on the equity basis.

**Financial Services** - Includes the Company's credit and certain miscellaneous service operations.

**Consolidated** - Represents the consolidation of the Equipment Operations and Financial Services. References to Deere & Company or the Company refer to the entire enterprise.

(3) An analysis of the Company's retained earnings in millions of dollars follows:

	Three Months Ended January 31	
	2009	2008
Balance, beginning of period	\$ 10,580.6	\$ 9,031.7
Net income	203.9	369.1
Dividends declared	(118.3)	(109.3)
Adoption of FIN No. 48 *		(48.0)
Other	(.1)	(.1)
Balance, end of period	\$ 10,666.1	\$ 9,243.4

\* Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes

(4) Most inventories owned by Deere & Company and its U.S. equipment subsidiaries are valued at cost on the last-in, first-out (LIFO) method. If all of the Company's inventories had been valued on a first-in, first-out (FIFO) method, estimated inventories by major classification in millions of dollars would have been as follows:

	January 31 2009	October 31 2008	January 31 2008
Raw materials and supplies	\$ 1,346	\$ 1,170	\$ 1,052
Work-in-process	581	519	543
Finished goods and parts	3,242	2,677	2,941
Total FIFO value	5,169	4,366	4,536
Less adjustment to LIFO basis	1,332	1,324	1,247

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Inventories	\$	3,837	\$	3,042	\$	3,289
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(5) Commitments and contingencies:

The Company generally determines its total warranty liability by applying historical claims rate experience to the estimated amount of equipment that has been sold and is still under warranty based on dealer inventories and retail sales. The historical claims rate is primarily determined by a review of five-year claims costs and current quality developments.

The premiums for extended warranties are primarily recognized in income in proportion to the costs expected to be incurred over the contract period. These unamortized warranty premiums (deferred revenue) included in the following table totaled \$225 million and \$231 million at January 31, 2009 and 2008, respectively.

A reconciliation of the changes in the warranty liability in millions of dollars follows:

	Three Months Ended	
	2009	2008
	January 31	
Balance, beginning of period	\$ 814	\$ 774
Payments	(124)	(125)
Amortization of premiums received	(26)	(19)
Accruals for warranties	117	117
Premiums received	23	27
Foreign exchange	(3)	4
Balance, end of period	\$ 801	\$ 778

At January 31, 2009, the Company had approximately \$150 million of guarantees issued primarily to banks outside the U.S. and Canada related to third-party receivables for the retail financing of John Deere equipment. The Company may recover a portion of any required payments incurred under these agreements from repossession of the equipment collateralizing the receivables. At January 31, 2009, the Company had an accrued liability of approximately \$6 million under these agreements. The maximum remaining term of the receivables guaranteed at January 31, 2009 was approximately six years.

The credit operation's subsidiary, John Deere Risk Protection, Inc., offers crop insurance products through managing general agency agreements (Agreements) with insurance companies (Insurance Carriers) rated Excellent by A.M. Best Company. As a managing general agent, John Deere Risk Protection, Inc. will receive commissions from the Insurance Carriers for selling crop insurance to producers. The credit operations have guaranteed certain obligations under the Agreements, including the obligation to pay the Insurance Carriers for any uncollected premiums. At January 31, 2009, the maximum exposure for uncollected premiums was approximately \$17 million. Substantially all of the credit operations' crop insurance risk under the Agreements has been mitigated by a syndicate of private reinsurance companies. The reinsurance companies are rated Excellent or higher by A.M. Best Company. In the event of a widespread catastrophic crop failure throughout the U.S. and the default of these highly rated private reinsurance companies on their reinsurance obligations, the credit operations would be required to reimburse the Insurance Carriers for exposure under the Agreements of approximately \$20 million at January 31, 2009. The credit operations believe that the likelihood of the occurrence of events that give rise to the exposures under these Agreements is substantially remote and as a result, at January 31, 2009, the credit operations' accrued liability under the Agreements was not material.

At January 31, 2009, the Company had commitments of approximately \$366 million for the construction and acquisition of property and equipment. Also, at January 31, 2009, the Company had pledged or restricted assets of \$189 million, primarily as collateral for borrowings. See Note 6 for additional restricted assets associated with borrowings related to securitizations.

The Company also had other miscellaneous contingent liabilities totaling approximately \$50 million at January 31, 2009, for which it believes the probability of payment is substantially remote. The accrued liability for these contingencies was not material at January 31, 2009.

## (6) Securitization of financing receivables:

The Company, as a part of its overall funding strategy, periodically transfers certain financing receivables (retail notes) into variable interest entities (VIEs) that are special purpose entities (SPEs) as part of its asset-backed securities programs (securitizations). The structure of these transactions is such that the transfer of the retail notes did not meet the criteria of sales in accordance with FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities, and are, therefore, accounted for as secured borrowings. SPEs utilized in securitizations of retail notes differ from other entities included in the Company's consolidated statements because the assets they hold are legally isolated. For bankruptcy analysis purposes, the Company has sold the receivables to the SPEs in a true sale and the SPEs are separate legal entities. Use of the assets held by the SPEs is restricted by terms of the documents governing the securitization transaction.

In securitizations of retail notes related to secured borrowings, the retail notes are transferred to certain SPEs which in turn issue debt to investors. The resulting secured borrowings are included in short-term borrowings on the balance sheet as shown in the following table. The securitized retail notes are recorded as Restricted financing receivables net on the balance sheet. The total restricted assets on the balance sheet related to these securitizations include the restricted financing receivables less an allowance for credit losses, and other assets primarily representing restricted cash as shown in the following table. The SPEs supporting the secured borrowings to which the retail notes are transferred are consolidated unless the Company is not the primary beneficiary in accordance with FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities. No additional support to these SPEs beyond what was previously contractually required has been provided during the first quarter of 2009.

In certain securitizations, the Company is the primary beneficiary of the SPEs and, as such, consolidates the entities. The restricted assets (retail notes, allowance for credit losses and other assets) of the consolidated SPEs totaled \$1,517 million, \$1,303 million and \$1,325 million at January 31, 2009, October 31, 2008 and January 31, 2008, respectively. The liabilities (short-term borrowings and accrued interest) of these SPEs totaled \$1,518 million, \$1,287 million and \$1,352 million at January 31, 2009, October 31, 2008 and January 31, 2008, respectively. The credit holders of these SPEs do not have legal recourse to the Company's general credit.

In other securitizations, the Company transfers retail notes into bank-sponsored, multi-seller, commercial paper conduits, which are SPEs that are not consolidated. The Company is not considered to be the primary beneficiary of these conduits, because the Company's variable interests in the conduits will not absorb a majority of the conduits' expected losses, residual returns, or both. This is primarily due to these interests representing significantly less than a majority of the conduits' total assets and liabilities. These conduits provide a funding source to the Company (as well as other transferors into the conduit) as they fund the retail notes through the issuance of commercial paper. The Company's carrying values and variable interests related to these conduits were restricted assets (retail notes, allowance for credit losses and other assets) of \$1,835 million, \$398 million and \$680 million at January 31, 2009, October 31, 2008 and January 31, 2008, respectively. The liabilities (short-term borrowings and accrued interest) related to these conduits were \$1,778 million, \$398 million and \$701 million at January 31, 2009, October 31, 2008 and January 31, 2008, respectively.

The Company's carrying amount of the liabilities to the unconsolidated conduits, compared to the maximum exposure to loss related to these conduits, which would only be incurred in the event of a complete loss on the restricted assets, was as follows in millions of dollars:

	<b>January 31, 2009</b>	
Carrying value of liabilities	\$	1,778
Maximum exposure to loss		1,835



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The assets of unconsolidated conduits related to securitizations in which the Company's variable interests were considered significant were approximately \$46 billion at January 31, 2009.

The components of consolidated restricted assets related to secured borrowings in securitization transactions follow in millions of dollars:

	January 31 2009		October 31 2008		January 31 2008
Restricted financing receivables (retail notes)	\$ 3,281	\$	1,656	\$	1,972
Allowance for credit losses	(12)		(11)		(11)
Other assets	83		56		44
Total restricted securitized assets	\$ 3,352	\$	1,701	\$	2,005

The components of consolidated secured borrowings and other liabilities related to securitizations follow in millions of dollars:

	January 31 2009		October 31 2008		January 31 2008
Short-term borrowings	\$ 3,292	\$	1,682	\$	2,050
Accrued interest on borrowings	4		3		3
Total liabilities related to restricted securitized assets	\$ 3,296	\$	1,685	\$	2,053

The secured borrowings related to these restricted securitized retail notes are obligations that are payable as the retail notes are liquidated. Repayment of the secured borrowings depends primarily on cash flows generated by the restricted assets. Due to the Company's short-term credit rating, cash collections from these restricted assets are not required to be placed into a restricted collection account until immediately prior to the time payment is required to the secured creditors. At January 31, 2009, the maximum remaining term of all restricted receivables was approximately six years.

(7) Dividends declared and paid on a per share basis were as follows:

	Three Months Ended January 31			
	2009		2008	
Dividends declared	\$	.28	\$	.25
Dividends paid	\$	.28	\$	.25

(8) Worldwide net sales and revenues, operating profit and identifiable assets by segment in millions of dollars follow:

	Three Months Ended January 31			% Change
	2009	2008		
Net sales and revenues:				
Agricultural equipment *	\$ 3,261	\$ 2,758		+18
Commercial and consumer equipment	558	743		-25
Construction and forestry *	741	1,030		-28
Total net sales **	4,560	4,531		+1
Credit revenues *	474	550		-14
Other revenues	112	120		-7
Total net sales and revenues **	\$ 5,146	\$ 5,201		-1
Operating profit (loss): ***				
Agricultural equipment	\$ 348	\$ 332		+5
Commercial and consumer equipment	(59)	8		
Construction and forestry	18	117		-85
Credit	53	133		-60
Other	4	3		+33
Total operating profit **	364	593		-39
Interest, corporate expenses net and income taxes	(160)	(224)		-29
Net income	\$ 204	\$ 369		-45
Identifiable assets:				
Agricultural equipment	\$ 5,947	\$ 4,962		+20
Commercial and consumer equipment	1,801	1,865		-3
Construction and forestry	2,318	2,430		-5
Credit	26,748	23,309		+15
Other	271	210		+29
Corporate	4,255	5,439		-22
Total assets	\$ 41,340	\$ 38,215		+8

\* Additional intersegment sales and revenues

Agricultural equipment sales	\$ 12	\$ 15		-20
Construction and forestry sales	1	2		-50
Credit revenues	68	63		-8

\*\* Includes equipment operations outside the U.S. and Canada as follows:

Net sales	\$ 1,817	\$ 1,808		
Operating profit	79	210		-62

\*\*\* Operating profit (loss) is income from continuing operations before external interest expense, certain foreign exchange gains and losses, income taxes and certain corporate expenses. However, operating profit of the credit segment includes the effect of interest expense and foreign exchange gains or losses.

(9) A reconciliation of basic and diluted net income per share in millions, except per share amounts, follows:

	Three Months Ended January 31	
	2009	2008
Net income	\$ 203.9	\$ 369.1
Average shares outstanding	422.5	437.7
Basic net income per share	\$ .48	\$ .84
Average shares outstanding	422.5	437.7
Effect of dilutive stock options	1.2	6.5
Total potential shares outstanding	423.7	444.2
Diluted net income per share	\$ .48	\$ .83

Out of the total stock options outstanding during the first quarter of 2009 and 2008, options to purchase 9.4 million shares and 2.0 million shares, respectively, were excluded from the above diluted per share computation because the incremental shares under the treasury stock method for the exercise of these options would have caused an antidilutive effect on net income per share.

(10) Comprehensive income, which includes all changes in the Company's equity during the period except transactions with stockholders, was as follows in millions of dollars:

	Three Months Ended January 31	
	2009	2008
Net income	\$ 203.9	\$ 369.1
Other comprehensive income (loss), net of tax:		
Retirement benefits adjustment	10.5	30.5
Cumulative translation adjustment	(93.1)	(.7)
Unrealized gain on investments	5.6	3.2
Unrealized loss on derivatives	(32.4)	(33.5)
Comprehensive income	\$ 94.5	\$ 368.6

(11) The Company is subject to various unresolved legal actions which arise in the normal course of its business, the most prevalent of which relate to product liability (including asbestos related liability), retail credit, software licensing, patent and trademark matters. Although it is not possible to predict with certainty the outcome of these unresolved legal actions or the range of possible loss, the Company believes these unresolved legal actions will not have a material effect on its consolidated financial statements.



(12) The Company has several defined benefit pension plans covering its U.S. employees and employees in certain foreign countries. The Company also has several defined benefit postretirement health care and life insurance plans for employees in the U.S. and Canada.

The worldwide components of net periodic pension cost (income) consisted of the following in millions of dollars:

	Three Months Ended	
	January 31	
	2009	2008
Service cost	\$ 29	\$ 41
Interest cost	139	128
Expected return on plan assets	(184)	(186)
Amortization of actuarial loss	2	11
Amortization of prior service cost	7	7
Early-retirement benefits	2	
Net cost (income)	\$ (5)	\$ 1

The worldwide components of net periodic postretirement benefits cost (health care and life insurance) consisted of the following in millions of dollars:

	Three Months Ended	
	January 31	
	2009	2008
Service cost	\$ 8	\$ 14
Interest cost	83	81
Expected return on plan assets	(30)	(44)
Amortization of actuarial loss	10	23
Amortization of prior service credit	(3)	(4)
Early-retirement benefits	1	
Net cost	\$ 69	\$ 70

During the first quarter of 2009, the Company contributed approximately \$15 million to its pension plans and \$34 million to its other postretirement benefit plans. The Company presently anticipates contributing an additional \$66 million to its pension plans and \$65 million to its other postretirement benefit plans during the remainder of fiscal year 2009. These contributions include payments from Company funds to either increase plan assets or make direct payments to plan participants.

(13) In December 2008, the Company granted options to employees for the purchase of 4.6 million shares of common stock at an exercise price of \$39.67 per share and a binomial lattice model fair value of \$12.66 per share. At January 31, 2009, options for 20.5 million shares were outstanding with a weighted-average exercise price of \$40.45 per share. The Company also granted .3 million of restricted stock units with a weighted-average fair value of \$39.67 per share in the first quarter of 2009. A total of 10.8 million shares remained available for the granting of future options and restricted stock.



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(14) Assets and liabilities measured at fair value on a recurring basis in millions of dollars follow:

	Total	January 31, 2009	
		Level 1	Level 2
Marketable securities	\$ 231	\$ 35	\$ 196
Other assets			
Derivatives:			
Interest rate contracts	746		746
Foreign exchange contracts	69		69
Cross-currency interest rate contracts	14		14
Total assets	\$ 1,060	\$ 35	\$ 1,025

Accounts payable and accrued expenses

Derivatives:

50

a loss of \$3.59 per share. Included in our results for 2005 were a \$166.4 million goodwill impairment charge, \$111.7 million of operating losses related to the HT Contract, \$81.8 million of non-cash compensation expense related to the vesting of Retention RSUs, a \$55.3 million increase in the valuation allowance primarily against our U.S. deferred tax assets, and \$29.6 million of lease and facilities restructuring charges.

### Year Ended December 31, 2005 Compared to Year Ended December 31, 2004

*Revenue.* Our revenue for 2005 was \$3,388.9 million, an increase of \$13.1 million, or 0.4%, over 2004 revenue of \$3,375.8 million. The following tables present certain revenue information and performance metrics for each of our reportable segments during 2005 and 2004. Amounts are in thousands, except percentages. For additional geographical revenue information, please see Note 18, Segment Information, of the Notes to Consolidated Financial Statements.

	Year Ended December 31,		\$ Change	% Change
	2005	2004		
<b>Revenue</b>				
Public Services	\$ 1,293,390	\$ 1,343,670	\$ (50,280)	(3.7%)
Commercial Services	663,797	654,022	9,775	1.5%
Financial Services	379,592	326,452	53,140	16.3%
EMEA	662,020	642,686	19,334	3.0%
Asia Pacific	312,190	328,338	(16,148)	(4.9%)
Latin America	75,664	79,302	(3,638)	(4.6%)
Corporate/Other	2,247	1,312	935	n/m
Total	\$ 3,388,900	\$ 3,375,782	\$ 13,118	0.4%

	Impact of currency fluctuations	Revenue growth (decline), net of currency impact	Total
<b>Revenue</b>			
Public Services	0.0%	(3.7)%	(3.7%)
Commercial Services	0.0%	1.5%	1.5%
Financial Services	0.0%	16.3%	16.3%
EMEA	0.1%	2.9%	3.0%
Asia Pacific	1.1%	(6.0)%	(4.9%)
Latin America	12.9%	(17.5)%	(4.6%)
Corporate/Other	n/m	n/m	n/m
Total	0.4%	0.0%	0.4%

n/m = not meaningful

*Public Services* revenue decreased in 2005, primarily attributable to expected reductions of \$33.8 million in revenue derived from our subcontractors and resales of procured materials (which we must bill our clients, thereby increasing our revenue) and revenue reductions of \$10.0 million associated with two loss contracts, both of which more than offset increases in headcount and chargeable hours resulting from our expanding use of employees at lower average bill rates.

*Commercial Services* revenue increased in 2005, primarily driven by revenue growth with transportation clients and a significant contract with Hawaiian Telcom Communications, Inc., which was partially offset by revenue declines from certain of our clients in the manufacturing and high-tech industries.

*Financial Services* revenue increased in 2005, primarily due to revenue growth in all sectors, with especially strong growth in the Insurance and Global Market sectors. Revenue growth was principally due to an increase in demand for our services. Our average billing rates improved slightly year-over-year, as our ability to obtain higher rates per hour on certain of our market offerings offset the increasing use of lower-priced offshore personnel as a component of our overall pricing model.

*EMEA* revenue increased in 2005, primarily due to combined revenue growth in France and the United Kingdom of \$53.6 million, partially offset by a \$29.8 million revenue decline in Germany. Our business in France experienced a significant shift into systems integration work, while revenue growth in the United Kingdom was driven by our continued expansion in that region. Revenue for Germany declined as a result of decreasing utilization caused by continued deterioration of market conditions in Germany which, consequently, led us to lower billable headcount.

*Asia Pacific* revenue decreased in 2005, driven primarily by decreasing demand for services in Japan and China and the planned elimination of subcontractor usage in the region, which more than offset the improved billing rates achieved across the region in 2005 due to significantly lower revenue write-offs during the year. Limited opportunities in Japan and China led to significant staff reductions and lower utilization rates in those countries.

*Latin America* revenue decreased in 2005, primarily as modest revenue growth in Brazil offset significant declines in revenue in all other countries in which we operate in the region. Revenue was also negative impacted by the weakening of the U.S. dollar against local currencies in Latin America (particularly the Brazilian Real).

*Corporate/Other:* Our Corporate/Other segment does not contribute significantly to our revenue.

*Gross Profit.* During 2005, our revenue increased \$13.1 million and total costs of service increased \$202.7 million when compared to 2004, resulting in a decrease in gross profit of \$189.5 million, or 34.6%. Gross profit as a percentage of revenue decreased to 10.6% for 2005 from 16.2% for 2004. The change in gross profit for 2005 compared to 2004 resulted primarily from the following:

Professional compensation expense increased as a percentage of revenue to 52.2% for 2005, compared to 45.4% for 2004. We experienced a net increase in professional compensation expense of \$238.0 million, or 15.5%, to \$1,770.4 million for 2005 from \$1,532.4 million for 2004. The increase in professional compensation expense was primarily the result of hiring additional billable employees in response to increased demand for our services. In addition, \$74.9 million of this amount was related to the vesting of Retention RSUs.

Other direct contract expenses decreased as a percentage of revenue to 28.7% for 2005 compared to 29.4% for 2004. We experienced a net decrease in other direct contract expenses of \$18.7 million, or 1.9%, to \$972.8 million for 2005 from \$991.5 million for 2004. The change was driven primarily by reduced subcontractor expenses as a result of the increased use of internal resources.

Other costs of service as a percentage of revenue decreased to 7.6% for 2005 from 8.7% for 2004. We experienced a net decrease in other costs of service of \$34.5 million, or 11.8%, to \$258.1 million for 2005 from \$292.6 million for 2004. The decrease in 2005 from 2004 was primarily due to the settlement costs of \$36.9 million involving or related to certain legal actions involving Peregrine Systems, Inc. (see Item 3, Legal Proceedings, ) included in our 2004 results.

In 2005 we recorded, within the Corporate/Other operating segment, a charge of \$29.6 million for lease and facilities restructuring costs, compared to an \$11.7 million charge for lease, facilities and other exist activities in 2004. These costs for 2005 related primarily to the fair value of future lease obligations associated with our previously announced reduction in office space, primarily within the North America, EMEA and Asia Pacific regions, which we no longer use.

*Gross Profit by Segment.* The following tables present certain gross profit and margin information and performance metrics for each of our reportable segments for 2005 and 2004. Amounts are in thousands, except percentages.

	Year Ended December 31,			% Change
	2005	2004	\$ Change	
<b>Gross Profit</b>				
Public Services	\$ 238,904	\$ 290,582	\$ (51,678)	(17.8%)
Commercial Services	(11,142)	129,784	(140,926)	(108.6%)
Financial Services	110,602	101,075	9,527	9.4%
EMEA	87,702	96,236	(8,534)	(8.9%)
Asia Pacific	53,636	31,063	22,573	72.7%
Latin America	4,321	13,454	(9,133)	(67.9%)
Corporate/Other	(126,031)	(114,670)	(11,361)	n/m
Total	\$ 357,992	\$ 547,524	\$ (189,532)	(34.6%)

	Year Ended December 31,	
	2005	2004
<b>Gross Profit as a % of revenue</b>		
Public Services	18.5%	21.6%
Commercial Services	(1.7%)	19.8%
Financial Services	29.1%	31.0%
EMEA	13.2%	15.0%
Asia Pacific	17.2%	9.5%
Latin America	5.7%	17.0%
Corporate/Other	n/m	n/m
Total	10.6%	16.2%

n/m = not meaningful

Changes in gross profit by segment were as follows:

*Public Services* gross profit decreased in 2005, in large measure due to a \$97.9 million increase in compensation expense (including non-cash compensation expense of \$25.5 million relating to the vesting of Retention RSUs) and the \$50.3 million reduction in gross revenue, which on a combined basis, more than offset significant reductions of \$65.7 million in other direct contract expenses and \$30.8 million in other costs of services.

*Commercial Services* gross profit decreased in 2005, as significantly higher gross revenue was eroded by significant cost overruns and loss accruals, most notably \$111.7 million on the previously described HT Contract, which included increases in subcontractor expense accruals and hardware and software purchases



that collectively increased our other direct contract expenses by \$66.6 million which are substantially not recoverable. Significant increases in compensation expense, including non-cash compensation expense relating to the vesting of Retention RSUs, also contributed to the decrease in gross profit.

*Financial Services* gross profit increased in 2005, as higher revenue across all sectors more than offset significant incremental increases in compensation expense related to a substantial increase in headcount, non-cash compensation expense relating to the vesting of Retention RSUs (\$7.5 million) and additional cash bonuses (\$3.0 million).

*EMEA* gross profit decreased in 2005, as incremental increases in compensation expense due to severance costs associated with workforce realignments in Germany, France and Spain (\$27.0 million) and non-cash compensation expense related to the vesting of the Retention RSUs (\$13.8 million) more than offset increases in revenue.

*Asia Pacific* gross profit increased substantially in 2005, despite a decrease in revenue due, in large measure, to significant demonstrated improvements in cost management and realization of contract revenue.

*Latin America* gross profit decreased in 2005, as increases in other direct contract expenses and compensation expense attributable to fringe benefits, non-cash compensation expense related to Retention RSUs and workforce realignments offset modest revenue growth in the region.

*Corporate/Other* consists primarily of rent expense and other facilities related charges, which increased in 2005 primarily due to the lease and facilities restructuring charges discussed above.

*Amortization of Purchased Intangible Assets.* Amortization of purchased intangible assets decreased \$1.2 million to \$2.3 million for 2005 from \$3.5 million for 2004.

*Goodwill Impairment Charges.* In 2005 and 2004, goodwill impairment losses of \$166.4 million and \$397.1 million, respectively, were recognized. For 2005, it was determined that the carrying amount of our EMEA and Commercial Services segments' goodwill exceeded the implied fair value of that goodwill by \$102.2 million and \$64.2 million, respectively. Similarly, in 2004, the EMEA segment's carrying value of goodwill was adjusted downward by \$397.1 million.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses increased \$109.7 million, or 17.1%, to \$750.9 million for 2005 from \$641.2 million for 2004. Selling, general and administrative expenses as a percentage of gross revenue increased to 22.2% for 2005 from 19.0% for 2004. The increase was primarily due to significant costs for sub-contracted labor and other costs directly related to the financial closing process for 2005. We expect to incur expenses in years 2006 and 2007 relating to the preparation of our Consolidated Financial Statements for 2005 and 2006 to remain at this higher than historical level.

*Interest Income.* Interest income was \$9.0 million and \$1.4 million in 2005 and 2004, respectively. Interest income is earned primarily from cash and cash equivalents, including money-market investments. The increase in interest income was due to a higher level of cash available to be invested in money-markets during 2005 as compared to 2004.

*Interest Expense.* Interest expense was \$33.4 million and \$18.7 million in 2005 and 2004, respectively. Interest expense is attributable to our debt obligations, consisting of interest due along with amortization of loan costs and loan discounts. The increase in interest expense was due to higher average debt balances in 2005 as compared to 2004.

*Loss on Early Extinguishment of Debt.* We did not have a loss on early extinguishment of debt during 2005. In December 2004, we recorded a loss on early extinguishment of debt of \$22.6 million related to the make whole premium, unamortized debt issuance costs and fees that were paid in connection with the early extinguishment of \$220.0 million of our senior notes.

*Other Expense, net.* Other expense, net was \$13.6 million and \$0.4 million in 2005 and 2004, respectively. The balances in each period primarily consist of realized foreign currency exchanges losses.

*Income Tax Expense.* We incurred income tax expense of \$122.1 million in 2005 and an income tax expense of \$11.8 million in 2004. The principal reasons for the difference between the effective income tax rate on loss from continuing operations of (20.4)% and (2.2)% for 2005 and 2004, respectively, and the U.S. Federal statutory income tax rate are the nondeductible goodwill impairment charge of \$118.5 million

and \$385.9 million; nondeductible meals and entertainment expense of \$19.6 million and \$19.2 million; increase to deferred tax asset valuation allowance of \$223.0 million and \$24.8 million; state and local income taxes of \$(12.7) million and \$(8.2) million; impact of foreign recapitalization of \$82.0 million and \$54.8 million; foreign taxes of \$13.7 million and \$(1.0) million; income tax reserves of \$18.6 million and \$7.9 million and other nondeductible items of \$8.2 million and \$26.3 million, respectively.

*Net Loss.* For 2005, we incurred a net loss of \$721.6 million, or a loss of \$3.59 per share. Included in our results for 2005 were a \$166.4 million goodwill impairment charge, \$111.7 million of operating losses related to the HT Contract, \$81.8 million of non-cash compensation expense related to the vesting of Retention RSUs, a \$55.3 million increase in the valuation allowance primarily against our U.S. deferred tax assets, and \$29.6 million of lease and facilities restructuring charges. For 2004, we incurred a net loss of \$546.2 million, or a loss of \$2.77 per share. Included in our results for 2004 are a \$397.1 million goodwill impairment charge, \$51.4 million for certain litigation settlement charges and \$11.7 million of lease and facilities restructuring charges.

### ***Obligations and Commitments***

As of December 31, 2006, we had the following obligations and commitments to make future payments under contracts, contractual obligations and commercial commitments (amounts are in thousands):

<b>Contractual Obligations</b>	<b>Total</b>	<b>Payment due by Period</b>			
		<b>Less than 1 year</b>	<b>1-3 years</b>	<b>3-5 years</b>	<b>After 5 years</b>
Long-term debt (1)	\$ 1,101,004	\$ 27,110	\$ 51,325	\$ 72,732	\$ 949,837
Operating leases	349,745	75,472	133,406	75,829	65,038
Unconditional purchase obligations (2)	99,594	51,278	36,126	9,190	3,000
Obligations under the pension and postretirement medical plans	47,558	3,808	7,869	8,433	27,448
Microsoft Collaboration Agreement (3)	4,689	4,689			
<b>Total</b>	<b>\$ 1,602,590</b>	<b>\$ 162,357</b>	<b>\$ 228,726</b>	<b>\$ 166,184</b>	<b>\$ 1,045,323</b>

- (1) Long-term debt includes both principal and interest scheduled payment obligations. Certain of our long-term debt allows the holders the right to convert the debentures into shares of our common stock or cash (at the Company's option) in earlier periods than presented above. For additional information, see Note 6, Notes Payable, of the Notes to Consolidated Financial Statements.
- (2) Unconditional purchase obligations include material agreements to purchase goods or services, principally software and telecommunications services, that are enforceable and legally binding and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Unconditional purchase obligations exclude agreements that are cancelable without penalty.
- (3) For additional information, see Note 10, Collaboration Agreement, of the Notes to Consolidated Financial Statements.



**Liquidity and Capital Resources**

The following table summarizes the cash flow statements for 2006, 2005 and 2004 (amounts are in thousands):

	<b>Year Ended December 31,</b>			<b>2006 to 2005 Change</b>
	<b>2006</b>	<b>2005</b>	<b>2004</b>	
Net cash provided by (used in):				
Operating activities	\$ 58,680	\$ (113,071)	\$ 48,265	\$ 171,751
Investing activities	67,570	(141,043)	(109,387)	208,613
Financing activities	(7,316)	274,152	176,538	(281,468)
Effect of exchange rate changes on cash and cash equivalents	15,297	(9,508)	6,919	24,805
Net increase in cash and cash equivalents	\$ 134,231	\$ 10,530	\$ 122,335	\$ 123,701

*Operating Activities.* Net cash provided by operating activities during 2006 increased \$171.8 million over 2005. This increase was primarily attributable to improved profitability and a decrease in accounts receivable, as our DSOs decreased to 82 days at December 31, 2006 from 94 days at December 31, 2005, providing an additional \$136.3 million. These items were partially offset by the cash outflow to support the professional services and related expenses required under the HT Contract, and, to a lesser extent, payments made for the Peregrine settlement of \$36.9 million.

Net cash used in operating activities during 2005 increased \$161.3 million over 2004. This increase was due to a net loss of \$721.6 million adjusted by impairment of goodwill of \$166.4 million and stock-based compensation expense of \$85.8 million in 2005 as compared to a net loss of \$546.2 million adjusted by impairment of goodwill of \$397.1 million and stock-based compensation expense of \$9.9 million in 2004. These items were partially offset by \$127.5 million in cash generated from working capital, primarily due to a decrease in our DSOs to 94 days at December 31, 2005 from 103 days at December 31, 2004, largely due to more aggressive collections efforts, and \$58.4 million and \$3.2 million in income tax refunds received during 2005 and 2004, respectively.

*Investing Activities.* Net cash provided by investing activities during 2006 increased \$208.6 million over 2005. This increase was predominantly due to the change in the amount of restricted cash posted as collateral for letters of credit and surety bonds. The requirement to deposit and maintain cash collateral terminated as part of the March 31, 2006 amendment to the 2005 Credit Facility, and such cash collateral was released to us. The increase was offset by an increase of \$9.7 million in capital expenditures in 2006 over 2005.

Net cash used in investing activities during 2005 was \$141.0 million, an increase of \$31.7 million over 2004. This increase was due to an increase in restricted cash of \$79.1 million for cash collateral posted in support of bank guarantees for letters of credit and surety bonds, which was partially offset by a decrease in capital expenditures of \$47.5 million. The decline in capital expenditures was due primarily to higher hardware and software costs incurred during 2004 for the implementation of our North America financial reporting systems.

*Financing Activities.* Net cash used in financing activities during 2006 was \$7.3 million, primarily due to repayments of our Japanese term loans. Net cash provided by financing activities for 2005 was \$274.2 million, resulting primarily

from the proceeds on the issuance of debentures with an aggregate principal amount of \$290.0 million, as more fully described in Debt Obligations, below.

In addition, issuances of common stock from our ESPP generated \$0, \$14.9 million and \$26.9 million in cash during 2006, 2005 and 2004, respectively. Because we are not current in our SEC periodic filings, we are unable to issue freely tradable shares of our common stock. Consequently, we were unable to make any public

offerings of our common stock in 2006 or 2005 and have not issued shares under the LTIP or ESPP since early 2005. These sources of financing will remain unavailable to us until we are again current in our SEC periodic filings.

### ***Additional Cash Flow Information***

2007. At March 31, 2007, we had global cash balances of approximately \$249.0 million. Our 2007 Credit Facility consists of (1) term loans in the aggregate principal amount of \$300 million and (2) a letter of credit facility in an aggregate face amount at any time outstanding not to exceed \$200 million. Borrowings under the 2007 Credit Facility will be used for general corporate purposes, including the payment of obligations outstanding under our prior credit facility, and payment of the fees and expenses of the 2007 Credit Facility. For additional information regarding the 2007 Credit Facility, see 2007 Credit Facility.

Our decision to obtain the 2007 Credit Facility was based, in part, on the fact that the North American cash balances have been negatively affected in the first quarter of 2007 by, among other things, cash collection levels not maintaining pace with the levels achieved in the fourth quarter of 2006 and payments made in connection with (1) the uninsured portion of the settlement of the dispute with HT, (2) ongoing costs relating to the design and implementation of the new North American financial reporting systems, (3) ongoing costs relating to production and completion of our financial statements, (4) other additional accrued expenses for 2006 paid in the first quarter of 2007, and (5) our current expectations that operations will not generate cash before the latter part of 2007.

*Outlook.* We currently expect that our operations will continue to use, rather than provide a source of cash through the latter part of 2007. Based on current internal estimates, we nonetheless believe that our cash balances, together with cash generated from operations and borrowings made under our 2007 Credit Facility, will be sufficient to provide adequate funds for our anticipated internal growth and operating needs. Our management may seek alternative strategies, intended to further improve our cash balances and their accessibility, if current internal estimates for cash uses for 2007 prove incorrect. These activities include: initiating further cost reduction efforts, seeking improvements in working capital management, reducing or delaying capital expenditures, seeking additional debt or equity capital and selling assets.

After consultation with a number of our external financial advisors and various credit sources, we continue to believe that our available receivables and expected earnings before interest, tax, depreciation and amortization are, notwithstanding our not being current in our SEC periodic filings, sufficient to provide us with access to the private equity and debt placement markets. However, there can be no assurance that the Company will be able to issue equity or debt with acceptable terms and the proceeds from any such issuances, subject to certain exceptions, must first be used to repay amounts owed under our 2007 Credit Facility.

Based on the foregoing and our current state of knowledge of the outlook for our business, we currently believe that cash provided from operations, existing cash balances and borrowings under our 2007 Credit Facility will be sufficient to meet our working capital needs through the end of 2007. However, actual results may differ from current expectations for many reasons, including losses of business that could result from our continuing failure to timely file periodic reports with the SEC, the occurrence of any event of default that could provide our lenders with a right of acceleration (e.g., non-payment), possible delisting from the NYSE, further downgrades of our credit ratings or unexpected demands on our current cash resources (e.g., to settle lawsuits). For additional information regarding various risk factors that could affect our outlook, see Item 1A, Risk Factors. If cash provided from operations is insufficient and/or our ability to access the capital markets is impeded, our business, operations, results and cash flow could be materially and adversely affected.



**Debt Obligations**

The following tables present a summary of the activity in our debt obligations for 2006 and 2005:

	<b>Balance December 31,</b>				<b>Balance December 31,</b>	
	<b>2005</b>	<b>Borrowings</b>	<b>Repayments</b>	<b>Other (b)</b>	<b>2006</b>	
Convertible debentures	\$ 668,054	\$	\$	\$ 3,436	\$ 671,490	
Yen-denominated term loan (January 31, 2003)	2,803		(2,802)	(1)		
Yen-denominated term loan (June 30, 2003)	1,402		(1,442)	40		
Other	2,501		(2,262)	121	360	
Total notes payable	\$ 674,760	\$	\$ (6,506)	\$ 3,596	\$ 671,850	

	<b>Balance December 31,</b>		<b>Discounts on Senior Debentures</b>		<b>Balance December 31,</b>	
	<b>2004</b>	<b>Borrowings</b>	<b>(a)</b>	<b>Repayments</b>	<b>Other (b)</b>	<b>2005</b>
Convertible debentures	\$ 400,000	\$ 290,000	\$ (23,361)	\$	\$ 1,415	\$ 668,054
Yen-denominated term loan (January 31, 2003)	9,724			(6,089)	(832)	2,803
Yen-denominated term loan (June 30, 2003)	4,863			(2,891)	(570)	1,402
Yen-denominated line of credit(c)	7,795			(6,796)	(999)	
Other	844	2,874		(1,209)	(8)	2,501
Total notes payable	\$ 423,226	\$ 292,874	\$ (23,361)	\$ (16,985)	\$ (994)	\$ 674,760

(a) Amount represents a discount to the \$40,000 principal amount of the July 2005 Senior Debentures.

(b) Other changes in notes payable consist of amortization of notes payable discount and foreign currency translation adjustments.

(c) Yen-denominated line of credit was terminated on December 16, 2005.

At December 31, 2006, we had total outstanding debt of \$671.9 million, compared to total outstanding debt of \$674.8 million at December 31, 2005. The \$2.9 million decrease in total outstanding debt was mainly attributable to the repayment of Yen-denominated term loans as well as other German debt offset by the amortization of notes payable discount related to the convertible debentures.

For information on the Series B Debenture litigation matter that we settled in late 2006, see Item 3, Legal Proceedings Other Matters.

***Debt Ratings***

On February 6, 2007, Standard & Poor's Rating Services ( Standard & Poor's ) withdrew our senior unsecured rating of B- and our subordinated debt rating of CCC+ and removed them from CreditWatch. Separately, on October 6, 2006, Moody's downgraded our corporate family rating to B2 from B1 and the ratings for two of our subordinated convertible bonds series to B3 from B2, and placed our ratings on review for further downgrade.

### **2007 Credit Facility**

On May 18, 2007, we entered into a \$400 million senior secured credit facility and on June 1, 2007, we amended and restated the credit facility to increase the aggregate commitments under the facility from \$400.0 million to \$500.0 million. The 2007 Credit Facility consists of (1) term loans in an aggregate principal amount of \$300.0 million (the *Term Loans*) and (2) a letter of credit facility in an aggregate face amount at any time outstanding not to exceed \$200.0 million (the *LC Facility*). Borrowings under the 2007 Credit Facility will be used for general corporate purposes, including the payment of obligations outstanding under the 2005 Credit Facility, and the payment of fees, commissions and expenses incurred by us in connection with the 2007 Credit Facility. Interest on the Term Loans is calculated, at the Company's option, (1) at a rate equal to 3.5% plus the London Interbank Offered Rate, or LIBOR, or (2) at a rate equal to 2.5% plus the higher of (a) the federal funds rate plus 0.5% and (b) UBS AG, Stamford Branch's prime commercial lending rate. As of June 1, 2007, we have borrowed \$300.0 million under the Term Loans, and an aggregate of approximately \$89.3 million of letters of credit previously outstanding under the 2005 Credit Facility has been assumed under the LC Facility.

Our obligations under the 2007 Credit Facility are secured by liens and security interests in substantially all of our assets and most of our material domestic subsidiaries, as guarantors of such obligations (including a pledge of 65% of the stock of certain of our foreign subsidiaries), subject to certain exceptions.

The 2007 Credit Facility requires us to make prepayments of outstanding Term Loans and cash collateralize outstanding Letters of Credit in an amount equal to (i) 100% of the net proceeds received from property or asset sales (subject to exceptions), (ii) 100% of the net proceeds received from the issuance or incurrence of additional debt (subject to exceptions), (iii) 100% of all casualty and condemnation proceeds (subject to exceptions), (iv) 50% of the net proceeds received from the issuance of equity (subject to exceptions) and (v) for each fiscal year ending on or after December 31, 2008 (and, at our election for the second half of the 2007 fiscal year), the difference between (a) 50% of the Excess Cash Flow (as defined in the 2007 Credit Facility) and (b) any voluntary prepayment of the Term Loan or the LC Facility (as defined in the 2007 Credit Facility) (subject to exceptions). If the Term Loan is prepaid or the LC Facility is reduced prior to May 18, 2008 with other indebtedness or another letter of credit facility, we may be required to pay a prepayment premium of 1% of the principal amount of the Term Loan so prepaid or LC Facility so reduced if the cost of such replacement indebtedness of letter of credit facility is lower than the cost of the 2007 Credit Facility. In addition, we are required to pay \$750,000 in principal plus any accrued and unpaid interest at the end of each quarter, commencing on June 29, 2007 and ending on March 31, 2012.

The 2007 Credit Facility contains affirmative and negative covenants:

The *affirmative covenants* include, among other things: the delivery of unaudited quarterly and audited annual financial statements, all in accordance with generally accepted accounting principles; certain monthly operating metrics and budgets; compliance with applicable laws and regulations (excluding, prior to October 31, 2008, compliance with certain filing requirements under the securities laws); maintenance of existence and insurance; after October 31, 2008, as requested by the Administrative Agent, maintenance of credit ratings; and maintenance of books and records (subject to the material weaknesses previously disclosed in our 2005 Form 10-K).

The *negative covenants*, which (subject to exceptions) restrict certain of our corporate activities, include, among other things, limitations on: disposition of assets; mergers and acquisitions; payment of dividends; stock repurchases and redemptions; incurrence of additional indebtedness; making of loans and investments; creation of liens; prepayment of other indebtedness; and engaging in certain transactions with affiliates.

Events of default under the 2007 Credit Facility include, among other things: defaults based on nonpayment, breach of representations, warranties and covenants, cross-defaults to other debt above \$10 million, loss of lien on collateral, invalidity of certain guarantees, certain bankruptcy and insolvency

events, certain ERISA events, judgments against us in an aggregate amount in excess of \$20 million, and change of control events.

Under the terms of the 2007 Credit Facility, we are not required to become current in our SEC periodic filings until October 31, 2008. Until October 31, 2008, our failure to provide annual audited or quarterly unaudited financial statements, to keep our books and records in accordance with GAAP or to timely file our SEC periodic reports will not be considered an event of default under the 2007 Credit Facility. The timing of the requirement that we become current in our SEC periodic filings is aligned with the timing set forth in the waivers obtained under certain of our indentures. As previously disclosed, the indenture governing the Series A Debentures and Series B Debentures was amended to include a waiver of our SEC reporting requirements under the indenture through October 31, 2008. In addition, the indenture governing the April 2005 Debentures was amended to include a waiver of our SEC reporting requirements under such indenture through October 31, 2007, or through October 31, 2008 if we elect to pay an additional fee to certain holders of such debentures.

### ***Discontinued 2005 Credit Facility***

On July 19, 2005, we entered into a \$150.0 million Senior Secured Credit Facility (the 2005 Credit Facility). Our 2005 Credit Facility provided for up to \$150.0 million in revolving credit and advances. Advances under the revolving credit line were limited by the available borrowing base, which was based upon a percentage of eligible accounts receivable. As of December 31, 2006, we had approximately \$23.7 million available under the borrowing base.

In 2005 and 2006, we entered into five amendments to the 2005 Credit Facility. Among other things, these amendments revised certain covenants contained in the 2005 Credit Facility, including the extensions of the filing deadlines for our 2005, 2006 and 2007 SEC periodic reports and an increase in the amounts of civil litigation payments that we are permitted to pay and in the aggregate amount of investments and indebtedness that we are permitted to make and incur with respect to our foreign subsidiaries. In addition, in 2007 we obtained several limited waivers that, among other things, waived the delivery requirement of our periodic filings to the lenders under the facility.

The 2005 Credit Facility was terminated on May 18, 2007. On that date, all outstanding obligations under the 2005 Credit Facility were paid or assumed under the 2007 Credit Facility, and all liens and security interests under the 2005 Credit Facility were released.

### ***Guarantees and Indemnification Obligations***

In the normal course of business, we have indemnified third parties and have commitments and guarantees under which we may be required to make payments in certain circumstances. These indemnities, commitments and guarantees include: indemnities to third parties in connection with surety bonds; indemnities to various lessors in connection with facility leases; indemnities to customers related to intellectual property and performance of services subcontracted to other providers; and indemnities to directors and officers under the organizational documents and agreements with them. The duration of these indemnities, commitments and guarantees varies, and in certain cases, is indefinite. Certain of these indemnities, commitments and guarantees do not provide for any limitation of the maximum potential future payments we could be obligated to make. We estimate that the fair value of these agreements was minimal. Accordingly, no liabilities have been recorded for these agreements as of December 31, 2006. Information regarding the amounts of our outstanding surety and surety-related bonds and letters of credit can be found above.

We are also required, in the course of business, particularly with certain of our Public Services clients, largely in the state and local markets, to obtain surety bonds, letters of credit or bank guarantees for client engagements. At

December 31, 2006, we had \$101.9 million in outstanding surety bonds and \$89.3 million in letters of credit extended to secure certain of these bonds. The issuers of our outstanding surety bonds may, at any time, require that we post collateral (cash or letters of credit) to fully secure these obligations.

### ***Critical Accounting Policies and Estimates***

The preparation of our Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States requires that management make estimates, assumptions and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenue and expenses during the reporting period. Management's estimates, assumptions and judgments are derived and continually evaluated based on available information, historical experience and various other assumptions that are believed to be reasonable under the circumstances. Because the use of estimates is inherent in the North American financial reporting systems, actual results could differ from those estimates. The areas that we believe are our most critical accounting policies include:

- revenue recognition,
- valuation of accounts receivable,
- valuation of goodwill,
- accounting for income taxes,
- valuation of long-lived assets,
- accounting for leases,
- restructuring charges,
- legal contingencies,
- retirement benefits,
- accounting for stock-based compensation, and
- accounting for intercompany loans.

A critical accounting policy is one that involves making difficult, subjective or complex accounting estimates that could have a material effect on our financial condition and results of operations. Critical accounting policies require us to make assumptions about matters that are highly uncertain at the time of the estimate, and different estimates that we could have used, or changes in the estimate that are reasonably likely to occur, may have a material impact on our financial condition or results of operations.

### ***Revenue Recognition***

We earn revenue from three primary sources: (1) technology integration services where we design, build and implement new or enhanced system applications and related processes, (2) services to provide general business consulting, such as system selection or assessment, feasibility studies, business valuations and corporate strategy services and (3) managed services in which we manage, staff, maintain, host or otherwise run solutions and systems provided to our customers. Contracts for these services have different terms based on the scope, deliverables and complexity of the engagement, which require us to make judgments and estimates in recognizing revenue. Fees for these contracts may be in the form of time-and-materials, cost-plus or fixed price.

Technology integration services represent a significant portion of our business and are generally accounted for under the percentage-of-completion method in accordance with the Statement of Position ( SOP ) 81-1, Accounting for Performance of Construction-Type and Certain Production-Type Contracts ( SOP 81-1 ). Under the percentage-of-completion method, management estimates the percentage-of-completion based upon costs to the client incurred as a percentage of the total estimated costs to the client. When total cost estimates exceed estimated revenue, we accrue for the estimated losses immediately. The use of the percentage-of-completion method requires significant judgment relative to estimating total contract revenue and costs, including assumptions relative to the length of time to complete the project, the nature and complexity of the work to be performed, and anticipated changes in estimated salaries and other costs.



Incentives and award payments are included in estimated revenue using the percentage-of-completion method when the realization of such amounts is deemed probable upon achievement of certain defined goals. Estimates of total contract revenue and costs are continuously monitored during the term of the contract and are subject to revision as the contract progresses. When revisions in estimated contract revenue and costs are determined, such adjustments are recorded in the period in which they are first identified.

Revenue for general business consulting services is recognized as work is performed and amounts are earned in accordance with the Staff Accounting Bulletin ( SAB ) No. 101, Revenue Recognition in Financial Statements, as amended by SAB No. 104, Revenue Recognition ( SAB 104 ). We consider amounts to be earned once evidence of an arrangement has been obtained, services are delivered, fees are fixed or determinable, and collectibility is reasonably assured. For contracts with fees based on time-and-materials or cost-plus, we recognize revenue over the period of performance. Depending on the specific contractual provisions and nature of the deliverable, revenue may be recognized on a proportional performance model based on level of effort, as milestones are achieved or when final deliverables have been provided.

For our managed service arrangements, we typically implement or build system applications for customers that we then manage or run for periods that may span several years. Such arrangements include the delivery of a combination of one or more of our service offerings and are governed by Emerging Issues Task Force ( EITF ) Issue 00-21,

Accounting for Revenue Arrangements with Multiple Deliverables. In managed service arrangements in which the system application implementation or build has standalone value to the customer, and we have evidence of fair value for the managed or run services, we bifurcate the total arrangement into two units of accounting: (i) the system application implementation or build, which is recognized as technology integration services using the percentage-of-completion method under SOP 81-1, and (ii) the managed or run services, which are recognized under SAB 104 ratably over the estimated life of the customer relationship. In instances where we are unable to bifurcate a managed service arrangement into separate units of accounting, the total contract is recognized as one unit of accounting under SAB 104. In such instances, total fees and costs related to the system application implementation or build are deferred and recognized together with managed or run services upon completion of the software application implementation or build ratably over the estimated life of the customer relationship. Certain managed service arrangements may also include transaction-based services in addition to the system application implementation or build and managed services. Fees from transaction-based services are recognized as earned if we have evidence of fair value for such transactions; otherwise, transaction fees are spread ratably over the remaining life of the customer relationship period as received. The determination of fair value requires us to use significant judgment. We determine the fair value of service revenue based upon our recent pricing for those services when sold separately and/or prevailing market rates for similar services.

Revenue includes reimbursements of travel and out-of-pocket expenses with equivalent amounts of expense recorded in other direct contract expenses. In addition, we generally enter into relationships with subcontractors where we maintain a principal relationship with the customer. In such instances, subcontractor costs are included in revenue with offsetting expenses recorded in other direct contract expenses.

Unbilled revenue consists of recognized recoverable costs and accrued profits on contracts for which billings had not been presented to clients as of the balance sheet date. Management anticipates that the collection of these amounts will occur within one year of the balance sheet date. Billings in excess of revenue recognized for which payments have been received are recorded as deferred revenue until the applicable revenue recognition criteria have been met.

#### ***Valuation of Accounts Receivable***

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. Assessing the collectibility of customer receivables requires management judgment. We

determine our allowance for doubtful accounts by specifically analyzing individual accounts receivable, historical bad debts, customer concentrations, customer credit-worthiness, current

economic and accounts receivable aging trends, and changes in our customer payment terms. Our valuation reserves are periodically re-evaluated and adjusted as more information about the ultimate collectibility of accounts receivable becomes available.

### ***Valuation of Goodwill***

Goodwill is the amount by which the cost of acquired net assets in a business acquisition exceeded the fair value of net identifiable assets on the date of purchase. We assess the impairment of goodwill and identifiable intangible assets on at least an annual basis on April 1 and whenever events or changes in circumstances indicate that the carrying value of the asset may not be recoverable, as prescribed in the Statement of Financial Accounting Standards ( SFAS ) No. 142, Goodwill and Other Intangible Assets ( SFAS 142 ).

An impairment review of the carrying amount of goodwill is conducted if events or changes in circumstances indicate that goodwill might be impaired. Factors we consider important that could trigger an impairment review include significant underperformance relative to historically or projected future operating results, identification of other impaired assets within a reporting unit, the more-likely-than-not expectation that a reporting unit or a significant portion of a reporting unit will be sold, significant adverse changes in business climate or regulations, significant changes in senior management, significant changes in the manner of our use of the acquired assets or the strategy for our overall business, significant negative industry or economic trends, a significant decline in our stock price for a sustained period, or a significant unforeseen decline in our credit rating. Determining whether a triggering event has occurred includes significant judgment from management.

The goodwill impairment test prescribed by SFAS 142 requires us to identify reporting units and to determine estimates of the fair value of our reporting units as of the date we test for impairment unless an event occurs or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying amount. As of December 31, 2006, our reporting units consisted of our three North America industry groups and our three international regions. To identify impairment, the fair value of the reporting unit is first compared with its carrying value. If the reporting unit's allocated carrying value exceeds its fair value, we undertake a second evaluation to assess the required impairment loss to the extent that the carrying value of the goodwill exceeds its implied fair value. The fair value of a reporting unit is the amount for which the unit as a whole could be bought or sold in a current transaction between willing parties. We estimate the fair values of our reporting units using a combination of the discounted cash flow valuation model and comparable market transaction models. Those models require estimates of future revenue, profits, capital expenditures and working capital for each unit as well as comparability with recent transactions in the industry. We estimate these amounts by evaluating historical trends, current budgets, operating plans and industry data. Determining the fair value of reporting units and goodwill includes significant judgment by management and different judgments could yield different results.

### ***Accounting for Income Taxes***

Provisions for federal, state and foreign income taxes are calculated on reported pre-tax earnings based on current tax law and also include, in the current period, the cumulative effect of any changes in tax rates from those used previously in determining deferred tax assets and liabilities. Such provisions differ from the amounts currently receivable or payable because certain items of income and expense are recognized in different time periods for financial reporting purposes than for income tax purposes. Significant judgment is required in determining income tax provisions and evaluating tax positions. We establish reserves for income tax when, despite the belief that our tax positions are fully supportable, there remain certain positions that are probable to be challenged and possibly disallowed by various authorities. The consolidated tax provision and related accruals include the impact of such reasonably estimable losses and related interest as deemed appropriate. To the extent that the probable tax outcome of these matters changes, such changes in estimate will impact the income tax provision in the period in which such

determination is made.

The majority of our deferred tax assets at December 31, 2006 consisted of federal, foreign and state net operating loss carryforwards that will expire between 2007 and 2026. During 2006, the valuation allowance against federal, state, and certain foreign net operating loss and foreign tax credit carryforwards increased \$69.4 million over the year ended 2005, due to additional losses.

Since our inception, various foreign, state and local authorities have audited us in the area of income taxes. Those audits included examining the timing and amount of deductions, the allocation of income among various tax jurisdictions and compliance with foreign, state and local tax laws. In evaluating the exposure associated with various tax filing positions we accrue charges for exposures related to uncertain tax positions.

During 2005, the Internal Revenue Service commenced a federal income tax examination for the tax periods ended June 30, 2001, June 30, 2003, December 31, 2003, December 31, 2004 and December 31, 2005. We are unable to determine the ultimate outcome of these examinations, but we believe that we have established appropriate reserves related to apportionment of income between jurisdictions, the impact of the restatement items and certain filing positions. We are also under examination from time to time in foreign, state and local jurisdictions.

At December 31, 2006, we believe we have appropriately accrued for exposures related to uncertain tax positions. To the extent we were to prevail in matters for which accruals have been established or be required to pay amounts in excess of reserves, our effective tax rate in a given financial statement period may be materially impacted.

During 2006, 2005 and 2004, none of the established reserves expired based on the statute of limitations with respect to certain tax examination periods. In addition, an increase to the reserve for tax exposures of \$13.8 million, \$51.6 million, and \$8.0 million, respectively, was recorded as an income tax expense for additional exposures, including interest and penalties.

The carrying value of our net deferred tax assets assumes that we will be able to generate sufficient future taxable income in certain tax jurisdictions to realize the value of these assets. If we are unable to generate sufficient future taxable income in these jurisdictions, a valuation allowance is recorded when it is more likely than not that the value of the deferred tax assets is not realizable. Management evaluates the realizability of the deferred tax assets and assesses the need for any valuation allowance. In 2006, we determined that it was more likely than not that a significant amount of our deferred tax assets primarily in the U.S. may not be realized, therefore we recorded a valuation allowance against those deferred assets.

### ***Valuation of Long-Lived Assets***

Long-lived assets primarily include property and equipment and intangible assets with finite lives (purchased software, internal capitalized software, and customer lists). In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, we periodically review long-lived assets for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable or that the useful lives are no longer appropriate. Each impairment test is based on a comparison of the undiscounted cash flows expected to result from the use and eventual disposition of the asset to the carrying amount of the asset. If an impairment is indicated, the asset is written down to its estimated fair value based on a discounted cash flow analysis. Determining the fair value of long-lived assets includes significant judgment by management, and different judgments could yield different results.

### ***Accounting for Leases***

We lease office facilities under non-cancelable operating leases that expire at various dates through 2017, along with options that permit renewals for additional periods. Rent abatements and escalations are considered in the

determination of straight-line rent expense for operating leases. Leasehold improvements made at the inception of or during the lease are amortized over the shorter of the asset life or the lease term. We receive

incentives to lease office facilities in certain areas which are recorded as a deferred credit and recognized as a reduction to rent expense on a straight-line basis over the lease term.

### ***Restructuring Charges***

We periodically record restructuring charges resulting from restructuring our operations (including consolidation and/or relocation of operations), changes in our strategic plan or management responses to increasing costs or declines in demand. The determination of restructuring charges requires management to utilize significant judgment and estimates related to expenses for employee benefits, such as costs of severance and termination benefits, and costs for future lease commitments on excess facilities, net of estimated future sublease income. In determining the amount of lease and facilities restructuring charges, we are required to estimate such factors as future vacancy rates, the time required to sublet excess facilities and sublease rates. These estimates are reviewed and potentially revised on a quarterly basis based on available information and known market conditions. If our assumptions prove to be inaccurate, we may need to make changes in these estimates that could impact our financial position and results of operations.

### ***Legal Contingencies***

We are currently involved in various claims and legal proceedings. We periodically review the status of each significant matter and assess our potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount can be reasonably estimated, we accrue a liability for the estimated loss. We use significant judgment in both the determination of probability and the determination as to whether an exposure is reasonably estimable. Because of uncertainties related to these matters, accruals are based only on the best information at that time. As additional information becomes available, we reassess the potential liability related to our pending claims and litigation and may revise our estimates. Such revisions in the estimates of potential liabilities could have a material impact on our financial position and results of operations. We expense legal fees as incurred.

### ***Retirement Benefits***

Our pension plans and postretirement benefit plans are accounted for using actuarial valuations required by SFAS No. 87, Employers Accounting for Pensions, SFAS No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions, and SFAS 158, Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans. The pension plans relate to our plans for employees in Germany and Switzerland. Accounting for retirement plans requires management to make significant subjective judgments about a number of actuarial assumptions, including discount rates, salary growth, long-term return on plan assets, retirement, turnover, health care cost trend rates and mortality rates. Depending on the assumptions and estimates used, the pension and postretirement benefit expense could vary within a range of outcomes and have a material effect on our financial position and results of operations. In addition, the assumptions can materially affect accumulated benefit obligations and future cash funding. For 2006, the discount rate to determine the benefit obligation for the pension plans was 4.2%. The discount rate reflects the rate at which the pension benefits could be effectively settled. The rate is based upon comparable high quality corporate bond yields with maturities consistent with expected pension payment periods. A 100 basis point increase in the discount rate would decrease the 2007 pension expense for the plans by approximately \$1.9 million. A 100 basis point decrease in the discount rate would increase the 2007 pension expense for the plans by approximately \$3.7 million. The expected long-term rate of return on assets for the 2006 was 4.5%. This rate represents the average of the long-term rates of return for the defined benefit plan weighted by the plans' assets as of December 31, 2006. To develop this assumption, we considered historical asset returns, the current asset allocation and future expectations of asset returns. The actual long-term rate of return from July 1, 2003 until December 31, 2006 was 4.5%. A 100 basis point increase or decrease in the expected long-term rate of return on the plans' assets would have approximately a \$0.2 million impact on our 2007 pension expense. As of December 31, 2006, the pension plan had an \$6.5 million

unrecognized actuarial loss that will be expensed over the average future working lifetime of active participants.



We also offer a postretirement medical plan to the majority of our full-time U.S. employees and managing directors who meet specific eligibility requirements. For 2006, the discount rate to determine the benefit obligation was 5.8%. The discount rate reflects the rate at which the benefits could be effectively settled. The rate is based upon comparable high quality corporate bond yields with maturities consistent with expected retiree medical payment periods. A 100 basis point increase or decrease in the discount rate would have approximately a \$0.6 million impact on the 2006 retiree medical expense for the plan. As of December 31, 2006, the pension plan had \$2.4 million in unrecognized actuarial losses that will be expensed over the average future working lifetime of active participants.

### *Accounting for Stock-Based Compensation*

We have various stock-based compensation plans under which we have granted stock options, restricted stock awards and stock units to certain officers, employees and non-employee directors. We also have the ESPP and BE an Owner plans that allow for employees to purchase Company stock at a discount. We granted both service-based and performance-based stock units and stock options during 2006. For all awards, the fair value is fixed on the date of grant based on the number of stock units or stock options issued and the fair value of the Company's stock on the date of grant. For the performance-based stock units and stock options, each quarter we compare the actual performance results with the performance conditions to determine the probability of the award fully vesting. The determination of successful compliance with the performance conditions requires significant judgment by management, as differing outcomes may have a significant impact on current and future stock compensation expense.

We adopted SFAS No. 123(R), Share-Based Payment ( SFAS 123(R) ) on January 1, 2006. This standard requires that all share-based payments to employees be recognized in the statements of operations based on their fair values. We have used the Black-Scholes model to determine the fair value of our stock option awards. Under the fair value recognition provisions of SFAS 123(R), share-based compensation is measured at the grant date based on the fair value of the award and is recognized as expense over the vesting period. Determining the fair value of share-based awards at the grant date requires judgment, including estimating stock price volatility and employee stock option exercise behaviors. If actual results differ significantly from these estimates, stock-based compensation expense and our results of operations could be materially impacted. As stock-based compensation expense recognized in the consolidated statements of operations is based on awards that ultimately are expected to vest, the amount of expense has been reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures were estimated based on historical experience. If factors change and we employ different assumptions in the application of SFAS 123(R), the compensation expense that we record in the future periods may differ significantly from what we have recorded in the current period.

We adopted the modified prospective transition method permitted under SFAS 123(R) and consequently have not adjusted results from prior years. Under the modified prospective transition method, the 2006 compensation cost includes expense relating to the remaining unvested awards granted prior to December 31, 2005 along with new grants made during 2006. For grants which vest based on certain specified performance criteria, the grant date fair value of the shares is recognized over the requisite period of performance once achievement of criteria is deemed probable. For grants that vest through the passage of time, the grant date fair value of the award is recognized over the vesting period.

We elected the alternative transition method as outlined in Financial Accounting Standards Board ( FASB ) Staff Position ( FSP ) 123(R)-3, Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards ( FSP 123(R)-3 ), to calculate the historical pool of excess tax benefits available to offset tax shortfalls in periods following the adoption of SFAS 123(R).

The after-tax stock-based compensation expense impact of adopting SFAS 123(R) for the year ended December 31, 2006 was \$25.7 million with a \$0.12 per share reduction to diluted earnings per share. Prior to the adoption of SFAS 123(R), we used the intrinsic value method of accounting prescribed by Accounting Principles Board Opinion ( APB ) No. 25, Accounting for Stock Issued to Employees and related

interpretations, including Financial Interpretation ( FIN ) 44, Accounting for Certain Transactions Involving Stock Compensation , for our plans. Under this accounting method, stock option compensation awards that are granted with an exercise price at the current fair value of our common stock as of the date of the award generally did not require compensation expense to be recognized in the consolidated statement of operations. Stock-based compensation expense recognized for our employee stock option plans, restricted stock units and restricted stock awards was \$85.8 million in 2005, net of tax.

As of December 31, 2006, unrecognized compensation costs and related weighted-average lives over which the costs will be amortized were as follows:

	<b>Unrecognized Compensation Costs</b>	<b>Weighted-Average Life in Years</b>
Stock options	\$ 11,052	1.7
Restricted stock and stock unit awards	41,153	3.1
ESPP	4,713	1.0
Total	\$ 56,918	2.6

#### ***Accounting for Intercompany Loans***

Intercompany loans are classified between long- and short-term based on management's intent regarding repayment. Translation gains and losses on short-term loans are recorded in other income (expense), net, in our Consolidated Financial Statements and similar gains and losses on long-term loans are recorded as other comprehensive income in our Consolidated Statements of Changes in Stockholders' Equity (Deficit). Accordingly, changes in management's intent relative to the expected repayment of these intercompany loans will change the amount of translation gains and losses included in our Consolidated Financial Statements.

#### ***Accounting for Employee Global Mobility and Tax Equalization***

We have a tax equalization policy designed to ensure that our employees on domestic long-term and foreign assignments will be subject to the same level of personal tax, regardless of the tax jurisdiction in which the employee works. We accrue for tax equalization expenses in the period incurred. If the estimated tax equalization liability, including related interest and penalties, is determined to be greater or less than amounts due upon final settlement, the difference is recorded in the current period.

#### ***Recently Issued Accounting Pronouncements***

In June 2006, the FASB issued FIN No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 ( FIN 48 ). This interpretation clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. It prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosures, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We will be required to adopt this interpretation in the first quarter of fiscal year 2007. We are currently evaluating the requirements of FIN 48 and have not yet determined the impact on our Consolidated Financial

Statements.

In September 2006, the SEC staff issued SAB No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* ( SAB 108 ). SAB 108 was issued in order to eliminate the diversity of practice surrounding how public companies quantify financial statement misstatements. SAB 108 requires registrants to quantify the impact of correcting all misstatements using both the *rollover* method, which focuses primarily on the impact of a misstatement on the income statement and is the method we currently use, and the *iron curtain* method, which focuses primarily on the effect of correcting the period-end balance sheet. The use of both of these methods is referred to as the *dual*

approach and should be combined with the evaluation of qualitative elements surrounding the errors in accordance with SAB No. 99, Materiality ( SAB 99 ). The adoption of SAB 108 during 2006 did not have a material impact on our Consolidated Financial Statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements ( SFAS 157 ). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. The provisions of SFAS 157 are effective for the fiscal year beginning January 1, 2008. We are currently evaluating the impact of the provisions of SFAS 157.

In December 2006, the FASB issued FASB Staff Position No. EITF 00-19-2, Accounting for Registration Payment Arrangements ( FSP No. EITF 00-19-2 ). FSP No. EITF 00-19-2 specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision of a financial instrument or other agreement, should be separately recognized and measured in accordance with SFAS No. 5, Accounting for Contingencies. FSP No. EITF 00-19-2 also requires additional disclosure regarding the nature of any registration payment arrangements, alternative settlement methods, the maximum potential amount of consideration and the current carrying amount of the liability, if any. FSP No. EITF 00-19-2 shall be effective immediately for registration payment arrangements and the financial instruments subject to those arrangements that are entered into or modified subsequent to the date of issuance of FSP No. EITF 00-19-2. For registration payment arrangements and financial instruments subject to those arrangements that were entered into prior to the issuance of FSP No. EITF 00-19-2, this guidance shall be effective for financial statements issued for fiscal years beginning after December 15, 2006, and interim periods within those fiscal years. We are currently evaluating the impact FSP No EITF 00-19-2 could have on our financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FAS 115 ( SFAS 159 ). The new statement allows entities to choose, at specific election dates, to measure eligible financial assets and liabilities at fair value that are not otherwise required to be measured at fair value. If a company elects the fair value option for an eligible item, changes in that item's fair value in subsequent reporting periods must be recognized in current earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of the provisions of SFAS 159.

## **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to a number of market risks in the ordinary course of business. These risks, which include interest rate risk and foreign currency exchange risk, arise in the normal course of business rather than from trading activities.

### ***Interest Rate Risk***

Our exposure to potential losses due to changes in interest rates is minimal as our outstanding debt obligations have fixed interest rates. The fair value of our debt obligations may increase or decrease for

various reasons, including fluctuations in the market price of our common stock, fluctuations in market interest rates and fluctuations in general economic conditions.

The table below presents principal cash flows (net of discounts) and related weighted average interest rates by scheduled maturity dates for our debt obligations as of December 31, 2006:

	<b>Expected Maturity Date</b>						<b>Fair Value</b>	
	<b>Year ended December 31,</b>							
	<b>(In thousands of U.S. Dollars, except interest rates)</b>							
	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>Thereafter</b>	<b>Total</b>	
U.S. Dollar Functional Currency Series A Convertible Subordinated Debentures						\$ 250,000	\$ 250,000	\$ 247,825
Average fixed interest rate						3.10%	3.10%	
U.S. Dollar Functional Currency Series B Convertible Subordinated Debentures						\$ 200,000	\$ 200,000	\$ 206,260
Average fixed interest rate						4.10%	4.10%	
U.S. Dollar Functional Currency Series C Convertible Subordinated Debentures						\$ 200,000	\$ 200,000	\$ 273,260
Average fixed interest rate						5.00%	5.00%	
U.S. Dollar Functional Currency Convertible Senior Subordinated Debentures				\$ 40,000			\$ 40,000	\$ 48,536
Average fixed interest rate				0.50%			0.50%	
U.S. Dollar Functional Currency	\$ 360						\$ 360	\$ 360
Average fixed interest rate	5.60%						5.60%	

### ***Foreign Currency Exchange Risk***

We operate internationally and are exposed to potentially adverse movements in foreign currency rate changes. Any foreign currency transaction, defined as a transaction denominated in a currency other than the U.S. dollar, will be

reported in U.S. dollars at the applicable exchange rate. Assets and liabilities are translated into U.S. dollars at exchange rates in effect at the balance sheet date and income and expense items are translated at average rates for the period.

We have foreign exchange exposures related primarily to short-term intercompany loans denominated in non-U.S. dollars to certain of our foreign subsidiaries. The potential gain or loss in the fair value of these intercompany loans that would result from a hypothetical change of 10% in exchange rates would be approximately \$6.9 million and \$9.2 million as of December 31, 2006 and 2005, respectively. For additional information refer to Note 2, Summary of Significant Accounting Policies, of the Notes to Consolidated Financial Statements.

#### **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

See the index included on Page F-1, Index to Consolidated Financial Statements.

#### **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

As previously reported, on February 5, 2007, the Chairman of the Audit Committee of the Board (the Audit Committee ) was notified by our independent registered public accounting firm, PricewaterhouseCoopers LLP ( PwC ), that PwC was declining to stand for re-election and that the client-auditor relationship between the Company and PwC would cease upon PwC 's completion of services related to the audit of our annual financial statements for fiscal 2006 and related 2006 quarterly reviews.

During the Company's years ended December 31, 2005 and December 31, 2006, and through June 28, 2007, there were no disagreements between the Company and PwC on any matter of accounting principle or practice, financial statement disclosure, or auditing scope or procedure that, if not resolved to PwC's satisfaction, would have caused it to make reference to the matter in connection with its report on the Company's consolidated financial statements for the relevant year, and there were no reportable events as defined in Item 304(a)(1)(v) of Regulation S-K, except that the Company disclosed that material weaknesses existed in its internal control over financial reporting for 2006 and 2005. The material weaknesses identified are discussed in Item 9A of the Company's Annual Reports on Form 10-K for the year ended December 31, 2006 and for the year ended December 31, 2005. The Company has authorized PwC to respond fully to any inquiries of its successor concerning the material weaknesses. PwC's audit reports on the Company's consolidated financial statements for the years ended December 31, 2006 and December 31, 2005 did not contain an adverse opinion or disclaimer of opinion, nor were they qualified or modified as to uncertainty, audit scope or accounting principles.

On February 9, 2007, the Audit Committee of the Board of Directors of the Company, as part of its periodic review and corporate governance practices, determined to engage Ernst & Young LLP (Ernst & Young) as the Company's independent registered public accounting firm commencing with the audit for the year ending December 31, 2007. Ernst & Young also has been engaged as the independent registered public accounting firm for the Plan, commencing with the audit for the Plan's year ending December 31, 2007. During the Company's years ended December 31, 2005 and December 31, 2006, and through February 9, 2007, neither the Company, nor anyone on its behalf, consulted with Ernst & Young with respect to either (i) the application of accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on the Company's consolidated financial statements for 2006 or 2005, and no written report or oral advice was provided by Ernst & Young to the Company that Ernst & Young concluded was an important factor considered by the Company in reaching a decision as to the accounting, auditing, or financial reporting issue for 2006 or 2005 or (ii) any matter that was the subject of either a disagreement as defined in Item 304(a)(1)(iv) of Regulation S-K or a reportable event as described in Item 304(a)(1)(v) of Regulation S-K.

## **ITEM 9A. CONTROLS AND PROCEDURES**

### *Evaluation of Disclosure Controls and Procedures*

As of the end of the period covered by this Annual Report, management performed, with the participation of our Chief Executive Officer and our Chief Financial Officer, an evaluation of the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act. Our disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on the evaluation and the identification of the material weaknesses in internal control over financial reporting described below, as well as our inability to file this Annual Report within the statutory time period, our Chief Executive Officer and our Chief Financial Officer concluded that, as of December 31, 2006, the Company's disclosure controls and procedures were not effective.

Because of the material weaknesses identified in our evaluation of internal control over financial reporting, we performed additional procedures so that our consolidated financial statements as of and for the



year ended December 31, 2006, including quarterly periods, are presented in accordance with GAAP. Our additional procedures included, but were not limited to:

- i) recalculating North America revenue and related accounts, such as accounts receivable, unbilled revenue, deferred revenue and costs of service as of and for the year ended December 31, 2006 by validating data to independent source documentation;
- ii) reviewing 100% of all contracts including contract modifications, accruals, and recognition of sub-contractor costs in 2006 in the United States;
- iii) providing GAAP revenue recognition guidance on certain international contracts focusing on those contracts with a value in excess of \$2 million and selected other contracts deemed to be of high risk;
- iv) performing a comprehensive search for unrecorded liabilities at December 31, 2006;
- v) performing a comprehensive global search to identify the complete population of employees deployed on expatriate assignments during 2006 and recalculating related compensation expense classified as costs of service, and employee income tax liabilities as of and for the year ended December 31, 2006;
- vi) performing additional reconciliations of payroll expense to cash payments for payroll including salaries, bonuses, and other wages; as well as agreement of bonus accruals to supporting documentation and subsequent cash disbursements;
- vii) performing additional review of lease and facility charges (performed by our GAAP Technical Accounting Policy Group) to ensure charges complied with GAAP and were complete and accurate;
- viii) performing substantive procedures in areas related to our income taxes in order to provide reasonable assurance as to the related financial statement amounts and disclosures;
- ix) verifying a significant sample of stock-based grants back to supporting documentation and manually agreeing certain assumptions used in the SFAS 123(R) calculations; and
- x) performing additional closing procedures, including detailed reviews of journal entries, re-performance of account reconciliations and analyses of balance sheet accounts.

The completion of these and other procedures resulted in the identification of adjustments related to our consolidated financial statements as of and for the year ended December 31, 2006, which significantly delayed the filing of this Annual Report.

We believe that because we performed the substantial additional procedures described above and made appropriate adjustments, the consolidated financial statements for the periods included in this Annual Report are fairly stated in all material respects in accordance with GAAP.

#### ***Management's Report on Internal Control over Financial Reporting***

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. 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 in accordance with GAAP. Because of its inherent limitations, internal control over financial

reporting may not prevent or detect misstatements. Also, projection of any evaluation of effectiveness to future periods is 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.

Management has conducted, with the participation of our Chief Executive Officer and our Chief Financial Officer, an assessment, including testing of the effectiveness of our internal control over financial reporting as of December 31, 2006. Management's assessment of internal control over financial reporting was conducted

using the criteria in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission ( COSO ).

A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. In connection with management's assessment of our internal control over financial reporting, we identified the following material weaknesses in our internal control over financial reporting as of December 31, 2006.

**1.** We did not maintain an effective control environment over financial reporting. Specifically, we identified the following material weaknesses:

We did not maintain a sufficient complement of personnel in our foreign locations with an appropriate level of knowledge, experience and training in the application of GAAP and in internal control over financial reporting commensurate with our financial reporting requirements.

We did not maintain and communicate sufficient formalized and consistent finance and accounting policies and procedures. We also did not maintain effective controls designed to prevent or detect instances of non-compliance with established policies and procedures specifically with respect to the application of accounting policies at foreign locations.

We did not enforce the consistent performance of manual controls designed to complement system controls over our North American financial accounting system. As a result, transactions and data were not completely and accurately recorded, processed and reported in the financial statements.

We did not maintain adequate controls to ensure that employees could report actual or perceived violations of our policies and procedures. In addition, we did not have sufficient procedures to ensure the appropriate notification, investigation, resolution and remediation procedures were applied to reported violations.

The material weaknesses in our control environment described above contributed to the existence of the material weaknesses discussed in items 2 through 9 below. Additionally, these material weaknesses could result in a misstatement to substantially all our financial statement accounts and disclosures that would result in a material misstatement to the annual or interim consolidated financial statements that would not be prevented or detected.

**2.** We did not maintain effective controls, including monitoring, over our financial close and reporting process. Specifically, we identified the following material weaknesses in the financial close and reporting process:

We did not maintain formal, written policies and procedures governing the financial close and reporting process.

We did not maintain effective controls to ensure that management oversight and review procedures were properly performed over the accounts and disclosures in our financial statements. In addition, we did not maintain effective controls to ensure adequate management reporting information was available to monitor financial statement accounts and disclosures.

We did not maintain effective controls over the recording of recurring and non-recurring journal entries. Specifically, effective controls were not designed and in place to provide reasonable assurance that journal entries were prepared with sufficient supporting documentation and reviewed and approved to ensure the completeness and accuracy of the entries recorded.

We did not maintain effective controls to provide reasonable assurance that accounts were complete and accurate and agreed to detailed support and that reconciliations of accounts were properly performed, reviewed and approved.

We did not maintain effective controls to provide reasonable assurance that foreign currency translation amounts resulting from intercompany loans were accurately recorded and reported in the consolidated financial statements.

These material weaknesses contributed to the material weaknesses identified in items 3 through 9 below and resulted in adjustments to our consolidated financial statements for the year ended December 31, 2006. Additionally, these material weaknesses could result in a misstatement to substantially all of our financial statement accounts and disclosures that would result in a material misstatement of our annual or interim consolidated financial statements that would not be prevented or detected.

**3.** We did not design and maintain effective controls over the completeness, accuracy, existence, valuation and disclosure of revenue, costs of service, accounts receivable, unbilled revenue, deferred contract costs, and deferred revenue. Specifically, we identified the following material weaknesses:

We did not design and maintain effective controls to provide reasonable assurance over the initiation, recording, processing, and reporting of customer contracts, including the existence of and adherence to policies and procedures, adequate segregation of duties and adequate monitoring by management.

We did not design and maintain effective controls to provide reasonable assurance that contract costs, such as engagement subcontractor costs, were completely and accurately accumulated.

We did not design and maintain effective controls to provide reasonable assurance that we adequately evaluated customer contracts to identify and provide reasonable assurance regarding the proper application of the appropriate method of revenue recognition in accordance with GAAP.

We did not design and maintain effective controls to provide reasonable assurance regarding the completeness of information recorded in the financial accounting system. Specifically, we did not design and have in place effective controls to provide reasonable assurance that invoices issued outside of the financial accounting system were appropriately recorded in the general ledger. As a result, we did not ensure that cash received was applied to the correct accounts in the appropriate accounting period.

**4.** We did not design and maintain effective controls over the completeness, accuracy, existence, valuation, and disclosure of our accounts payable, other current liabilities, other long-term liabilities and related expense accounts. Specifically, we did not design and maintain effective controls over the initiation, authorization, processing, recording, and reporting of purchase orders and invoices as well as authorizations for cash disbursement to provide reasonable assurance that liability balances and operating expenses were accurately recorded in the appropriate accounting period and to prevent or detect misappropriation of assets. In addition, we did not have effective controls to: i) provide reasonable assurance regarding the complete identification of subcontractors used in performing services to our customers; or ii) monitor subcontractor activities and accumulation of subcontractor invoices to provide reasonable assurance regarding the complete and accurate recording of contract-related subcontractor costs.

**5.** We did not design and maintain effective controls over the completeness and accuracy of costs related to expatriate compensation expense and related tax liabilities. Specifically, we did not maintain effective controls to identify and monitor employees working away from their home country for extended periods of time. In addition, we did not maintain effective controls to completely and properly calculate the related compensation expense and employee income tax liability attributable to each tax jurisdiction.

**6.** We did not design and maintain effective controls over the completeness, accuracy, valuation, and disclosure of our payroll, employee benefit and other compensation liabilities and related expense accounts. Specifically, we did not

have effective controls designed and in place to provide reasonable assurance of the authorization, initiation, recording, processing, and reporting of employee related costs including bonus, health and welfare, severance, compensation expense, and stock-based compensation amounts in the accounting records. Additionally, we did not design and maintain effective controls over the administration of employee

data or controls to provide reasonable assurance regarding the proper authorization of non-recurring payroll changes.

7. We did not design and maintain effective controls over the completeness, accuracy, existence, valuation and disclosure of property and equipment and related depreciation and amortization expense. Specifically, we did not design and maintain effective controls to provide reasonable assurance that asset additions and disposals were completely and accurately recorded; depreciation and amortization expense was accurately recorded based on appropriate useful lives assigned to the related assets; existence of assets was confirmed through periodic inventories; and the identification and determination of impairment losses were performed in accordance with GAAP. In addition, we did not design and maintain effective controls to provide reasonable assurance of the adherence to our capitalization policy, and we did not design and maintain effective controls to provide reasonable assurance that expenses for internally developed software were completely and accurately capitalized, amortized, and adjusted for impairment in accordance with GAAP.

8. We did not design and maintain effective controls over the completeness, accuracy, valuation, and disclosure of our prepaid lease and long-term lease obligation accounts and the related amortization and lease rental expenses. Specifically, we did not design and maintain effective controls to provide reasonable assurance that new, amended, and terminated leases, and the related assets, liabilities and expenses, including those associated with rent holidays, escalation clauses, landlord/tenant incentives and asset retirement obligations, were reviewed, approved, and accounted for in accordance with GAAP.

9. We did not design and maintain effective controls over the completeness, accuracy, existence, valuation and presentation and disclosure of our income tax payable, deferred income tax assets and liabilities, the related valuation allowance and income tax expense. Specifically, we identified the following material weaknesses:

We did not design and maintain effective controls over the accuracy and completeness of the components of our income tax provision calculations and related reconciliation of our income tax payable and of differences between the tax and financial reporting basis of our assets and liabilities with our deferred income tax assets and liabilities. We also did not maintain effective controls to identify and determine permanent differences between our income for tax and financial reporting income purposes.

We did not maintain effective controls, including monitoring, over the calculation and recording of foreign income taxes, including tax reserves, acquired tax contingencies associated with business combinations and the income tax impact of foreign debt recapitalization. In addition, we did not maintain effective controls over determining the correct foreign jurisdictions or tax treatment of certain foreign subsidiaries for United States tax purposes.

We did not design and maintain effective controls over withholding taxes associated with interest payable on intercompany loans and intercompany trade payables between various tax jurisdictions.

Each of the control deficiencies discussed in items 3 through 9 above resulted in adjustments to our consolidated financial statements for the year ended December 31, 2006. Additionally, these control deficiencies could result in misstatements of the aforementioned financial statement accounts and disclosures that would result in a material misstatement of our annual or interim consolidated financial statements that would not be prevented or detected. Accordingly, management has determined that each of the control deficiencies in items 3 through 9 above constitutes a material weakness.

Because of the material weaknesses described above, management has concluded that we did not maintain effective internal control over financial reporting as of December 31, 2006, based on the *Internal Control - Integrated Framework* issued by COSO.





Our assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2006 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which is included in Item 8 of this Annual Report.

***Remediation of Material Weaknesses in Internal Control over Financial Reporting***

We have engaged in, and continue to engage in, substantial efforts to address the material weaknesses in our internal control over financial reporting and the ineffectiveness of our disclosure controls and procedures.

The Company has remediated its material weakness with respect to senior management setting the proper tone by placing importance on internal control over financial reporting and by placing importance on adherence to the code of business conduct and ethics through the following actions:

Senior management made key hires in specific management positions.

Senior management made strategic replacements of certain country and regional leadership.

Senior management and regional and country leaders consistently communicated the proper tone as to internal control over financial reporting and adherence to the code of business conduct and ethics throughout their respective organizations.

Senior management and regional and country leaders initiated specific efforts to design and implement improvements in internal controls over financial reporting whose primary objective was focused on the completeness and accuracy of financial accounts.

Senior management instituted under the direction of its new Chief Compliance Officer comprehensive training on the Foreign Corrupt Practices Act, delivered in eight different languages, which was monitored to determine completion of the training. This resulted in over 95% of all employees world-wide completing the training and the required test.

We added significant skills and competencies to our corporate finance and accounting function by hiring individuals with strong technical skills and significant experience in areas deemed appropriate to their assigned responsibilities, including the creation of a GAAP Technical Accounting Policy Group, thereby remediating the material weakness with respect to a sufficient complement of personnel in our corporate offices.

The Company has remediated its material weakness with respect to the tracking of its long-term assignment employees ( LTA ) in the United States and the recording of the related expenses and tax liabilities by implementing the following mechanisms:

A comprehensive LTA policy.

Training and testing to measure the comprehension of the LTA policy including tracking of completion of the training and the related test. Completion rates were above 90%.

A comprehensive tracking system that identifies potential LTA personnel and accumulates and records appropriate cost data and related liabilities.

In addition to the foregoing remediation activities, we continued to strengthen the control environment and the accuracy and completeness of the financial accounts. Except as noted above, the following remediation efforts, certain

of which commenced in fiscal 2006 and continue in 2007, were insufficiently mature to fully remediate any additional material weaknesses in fiscal 2006:

We established a global remediation project, under the direction of the Chief Financial Officer, in order to provide oversight and direction in an effort to establish an effective control environment.

We strengthened our Internal Audit function by adding individuals with specialized skills where deemed appropriate.

We continued the implementation of our finance transformation program, the objective of which was to design and develop remediation strategies to address material weaknesses and improve internal controls.

We designed and implemented a global closing process designed to identify and define close tasks for both financial and non-finance functional areas, due dates for close procedures, task completion and ownership, and process integration.

We implemented a financial close management tool which allows us to track progress against approximately 1,500 closing tasks.

We implemented a Program Control initiative, consisting in excess of 250 professionals with requisite skills, designed to support the completeness and accuracy of project accounting details in North America.

We implemented improvements to our billing process, established policies and procedures limiting any invoicing outside of our financial system, and significantly reduced manual billing errors and unapplied cash balances.

In the first quarter of 2007, we deployed a new contract set up process and application to guide the comprehensive review of contract and project set-up data within the accounting system.

In the second quarter of 2007, we deployed and conducted extensive training on an application referred to as the Project Control Workbench. Combined with other process changes, enhanced controls and reporting, this application will improve the accuracy and timeliness of submission of project accounting data needed for accounting for subcontractor accruals, estimate-at-complete, estimate-to-complete, and revenue recognition in North America.

We implemented improved processes to identify, monitor, track and account for employees working outside their home country for extended periods of time including account reconciliations, data reviews, and tax cost projection analyses.

We implemented new processes designed to improve the completeness, accuracy and timing of accounting for expatriate assignments, including the development of a tracking application to assist in the compiling and reporting of employee-related costs.

We deployed an automated tool to assist with the process of requesting time and expense adjustments.

We performed in-depth access reviews in certain regions of the applicable payroll systems to ensure proper access restrictions.

We created an oversight function within the Corporate Controller group to provide additional analyses, review and oversight for fixed assets.

We implemented procedures to include a regular review of asset impairment.

In the first quarter of 2007, we completed a fixed asset inventory in addition to our periodic electronic inventory of laptops and desktops, to validate asset existence.

We centralized all lease administration, enabling us to capture all lease obligations and lease terms, and measure the completeness and accuracy of our lease records.

We implemented a review of certain monthly leasing activity reports to identify lease-related commitments.

We implemented a process to identify real-time lease activity or other lease term changes with respect to our leased facilities.

The foregoing initiatives have enabled us to significantly improve our control environment, the completeness and accuracy of underlying accounting data, and the timeliness with which we are able to close our books. Management is committed to continuing efforts aimed at fully achieving an operationally effective

control environment and timely filing of regulatory required financial information. The remediation efforts noted above are subject to the Company's internal control assessment, testing and evaluation processes. While these efforts continue, we will rely on additional substantive procedures and other measures as needed to assist us with meeting the objectives otherwise fulfilled by an effective control environment.

***Changes in Internal Control over Financial Reporting***

As noted above, senior management implemented and caused to be sustained significant changes to personnel, including finance and accounting personnel in our corporate offices, processes and policies and have communicated the importance of our Standards of Business Conduct and ethics, and the importance of internal control over financial reporting. In addition, senior management caused to be implemented policies and processes and other mechanisms around the identification of our long-term assignment personnel in the United States and the accuracy and completeness of the related financial accounts. These measures matured sufficiently such that in the fourth quarter of 2006, their sustainability and impact were considered sufficient. These changes represent material changes that have occurred in our internal control over financial reporting during the most recently completed fiscal quarter that have materially affected or are reasonably likely to materially affect, our internal control over financial reporting.

**ITEM 9A(T). CONTROLS AND PROCEDURES**

Not applicable.

**ITEM 9B. OTHER INFORMATION**

None.

### PART III.

#### ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Our Board of Directors (the Board) currently consists of nine directors. Our directors are divided into three classes serving staggered three-year terms. Information about our directors as of June 1, 2007, is provided below. For information about our executive officers, please see Executive Officers included in Part I of this Annual Report.

##### *Class I Directors Whose Terms Expire in 2007*

**Douglas C. Allred**, age 56, has been a member of our Board of Directors since January 2000. Mr. Allred is a private investor. Mr. Allred retired from his position as Senior Vice President, Office of the President, of Cisco Systems, Inc. in 2003. Mr. Allred was Senior Vice President, Customer Advocacy, Worldwide Consulting and Technical Services, Customer Services, and Cisco Information Technology of Cisco Systems, Inc. from 1991 to 2002. Mr. Allred is a Governor on the Washington State University Foundation Board of Governors.

**Betsy J. Bernard**, age 52, has been a member of our Board of Directors since March 2004. Ms. Bernard is a private investor. Ms. Bernard was President of AT&T Corporation from 2002 to 2003. From 2001 to 2002, Ms. Bernard was President and Chief Executive Officer of AT&T Consumer. Ms. Bernard is a director of The Principal Financial Group, a global financial institution.

**Spencer C. Fleischer**, age 53, has been a member of our Board of Directors since July 2005. Mr. Fleischer is a senior managing member and Vice Chairman of Friedman Fleischer & Lowe GP II, LLC, a company sponsoring and managing several investment funds that make investments in private and public companies, and has served in such capacity since 1998. Mr. Fleischer was appointed to the Board of Directors in accordance with the terms of the securities purchase agreement, dated July 15, 2005, relating to the July 2005 Senior Debentures among the Company and certain affiliates of Friedman Fleischer & Lowe, LLC. If Mr. Fleischer ceases to be affiliated with the purchasers or ceases to serve on our Board of Directors, so long as the purchasers collectively hold at least 40% of the original principal amount of the July 2005 Senior Debentures, the purchasers or their designee have the right to designate a replacement director to the Board of Directors.

##### *Class II Directors Whose Terms Expire in 2008*

**Wolfgang Kemna**, age 49, has been a member of our Board of Directors since April 2001. Mr. Kemna is Managing Director of Steeb Anwendungssysteme GmbH, a wholly owned subsidiary of SAP AG (SAP). Mr. Kemna was Executive Vice President of Global Initiatives of SAP from 2002 to 2004. He was also a member of SAP's extended executive board from 2000 to 2004.

**Albert L. Lord**, age 61, has been a member of our Board of Directors since February 2003. Mr. Lord is Chairman of the board of directors of SLM Corporation, commonly known as Sallie Mae, and has served in this capacity since 2005. Mr. Lord was Vice Chairman and Chief Executive Officer of Sallie Mae from 1997 to 2005.

**J. Terry Strange**, age 63, has been a member of our Board of Directors since April 2003. Mr. Strange retired from KPMG where he served as Vice Chair and Managing Partner of the U.S. Audit Practice from 1996 to 2002. During this period, Mr. Strange also served as the Global Managing Partner of the Audit Practice of KPMG International and was a member of its International Executive Committee. Mr. Strange is a director of Compass BancShares, Inc., a financial services company, New Jersey Resources Corp., an energy services holding company, Group 1 Automotive,

Inc., a holding company operating in the automotive retailing industry, and Newfield Exploration Company, an independent crude oil and natural gas exploration and production company.

***Class III Directors Whose Terms Expire in 2009***

***Roderick C. McGeary***, age 56, has been a member of our Board of Directors since August 1999 and Chairman of the Board of Directors since November 2004. Since March 2005, Mr. McGeary has served the Company in a full-time capacity, focusing on clients, employees and business partners. From 2004 until 2005, Mr. McGeary served as our Chief Executive Officer. From 2000 to 2002, Mr. McGeary was the Chief Executive Officer of Brience, Inc., a wireless and broadband company. Mr. McGeary is a director of Cisco Systems, Inc., a worldwide leader in networking for the Internet, and Dionex Corporation, a manufacturer and marketer of chromatography systems for chemical analysis.

***Jill S. Kanin-Lovers***, age 55, has been a member of our Board of Directors since May 2007. Ms. Kanin-Lovers served as Senior Vice President of Human Resources & Workplace Management at Avon Products, Inc. from 1998 to 2004. Ms. Kanin-Lovers is a member of the Board of Directors of Dot Foods, Inc., one of the nation's largest food redistributors, Heidrick & Struggles, a leading global search firm, and First Advantage Corporation, a leading provider of risk mitigation and business solutions. Ms. Kanin-Lovers also teaches Corporate Governance for the Rutgers University Mini-MBA program.

***Harry L. You***, age 48, has been a member of our Board of Directors since March 2005. Mr. You has served as Chief Executive Officer of the Company since March 2005. Mr. You also served as the Company's Interim Chief Financial Officer from July 2005 until October 2006. From 2004 to 2005, Mr. You was Executive Vice President and Chief Financial Officer of Oracle Corporation, a large enterprise software company. From 2001 to 2004, Mr. You was the Chief Financial Officer of Accenture Ltd, a global management consulting, technology services and outsourcing company. Mr. You is a director of Korn Ferry International, a leading provider of recruitment and leadership development services.

No family relationships exist between any of the directors or between any director and any executive officer of the Company.

***Presiding Director of Executive Sessions of Non-Management Directors***

Our non-management directors who are not employees of the Company meet separately on a periodic basis. The Board has designated Douglas C. Allred as the Presiding Director for all meetings of the executive sessions of non-management directors.

***Audit Committee***

Our Audit Committee is currently composed of Messrs. Strange (Chair), Kemna and Lord. The Board has affirmatively determined that each member of the Audit Committee has no material relationship with the Company (either directly or as a partner, stockholder or officer of the Company) and is independent of the Company and its management under the listing standards of the NYSE and the applicable regulations of the SEC. Mr. Strange serves on the audit committee of four other publicly registered companies. The Board has determined that such simultaneous service does not impair Mr. Strange's ability to serve on the Company's Audit Committee. In addition, the Board has determined that Mr. Strange is an Audit Committee Financial Expert.

***Compensation Committee Interlocks and Insider Participation***

The members of our Compensation Committee for 2006 were Messrs. Allred (Chair) and Strange and Ms. Bernard. On May 10, 2007, Ms. Kanin-Lovers was appointed to the Compensation Committee, and on June 18, 2007, Mr. Strange stepped down from the committee. No member of the Compensation Committee is a former or current



officer or employee of the Company or any of the Company's subsidiaries. To the Company's knowledge, there were no other relationships involving members of the Compensation Committee requiring disclosure in this section of this Annual Report.

### ***Standards of Business Conduct***

On May 10, 2007, the Board approved our Standards of Business Conduct (the SBC ), which superseded our prior Code of Business Conduct and Ethics as of May 31, 2007. The SBC was developed as part of our commitment to enhancing our culture of integrity and our corporate governance policies. The SBC reflects changes in law and regulation, best practices and updates to the Company's policies. In addition, the SBC contains new or enhanced policies and/or procedures relating to violations of the SBC, conflicts of interest (including those related to the giving and receiving of gifts and entertainment), financial disclosures, the importance of maintaining the confidentiality of Company, client and competitor information, data privacy and protection, Company property, investor and media relations, records management, and lobbying/political activities. The SBC applies to all of our directors and employees, including our principal executive officer, principal financial officer and principal accounting officer. The SBC is posted on our website, at [www.bearingpoint.com](http://www.bearingpoint.com), and is filed as an exhibit to this Annual Report. We intend to satisfy the disclosure requirement regarding any amendment to, or waiver of, a provision of the SBC for our Chief Executive Officer, Chief Financial Officer, Corporate Controller or persons performing similar functions, by posting such amendment or waiver on our within the applicable deadline that may be imposed by government regulation following the amendment or waiver.

### ***Committee Charters***

In addition, our Corporate Governance Guidelines, Audit Committee Charter, Compensation Committee Charter and Nominating and Corporate Governance Committee Charter are posted on the Company's website, at [www.bearingpoint.com](http://www.bearingpoint.com). A printed copy of these documents, as well as our Standards of Business Conduct, will be made available upon request.

### ***Annual Certifications***

The certifications by our Chief Executive Officer and Chief Financial Officer regarding the quality of our public disclosures are filed as Exhibits 31.1 and 31.2, respectively, to this Annual Report. We have also submitted to the NYSE a certificate of our Chief Executive Officer certifying that he is not aware of any violation by the Company of the NYSE corporate governance listing standards.

### ***Communications with Board of Directors***

The Board welcomes your questions and comments. If you would like to communicate directly with our Board, our non-management directors of the Board as a group or Mr. Allred, as the Presiding Director, then you may submit your communication to our General Counsel and Corporate Secretary by writing to them at the following address:

BearingPoint, Inc.  
c/o General Counsel and Corporate Secretary  
8725 W. Higgins Road  
Chicago, IL 60631

All communications and concerns will be forwarded to our Board, our non-management directors as a group or our Presiding Director, as applicable. We also have established a dedicated telephone number for communicating concerns or comments regarding compliance matters to the Company. The phone number is 1-800-206-4081 (or 240-864-0229 for international callers), and is available 24 hours a day, seven days a week. Our Standards of Business Conduct prohibits any retaliation or other adverse action against any person for raising a concern. If you wish to raise your concern in an anonymous manner, then you may do so.



### ***Section 16(a) Beneficial Ownership Reporting Compliance***

Under the U.S. Federal securities laws, directors and executive officers, as well as persons who beneficially own more than ten percent of our outstanding common stock, must report their initial ownership of the common stock and any changes in that ownership to the SEC. The SEC has designated specific due dates for these reports, and we must identify in this Annual Report those persons who did not file these reports when due. Based solely on a review of copies of Forms 3, 4 or 5 filed by us on behalf of our directors and executive officers or otherwise provided to us and copies of Schedule 13Gs, we believe that all of our directors, executive officers and greater than ten percent stockholders complied with their applicable filing requirements for 2006. In 2005, however, Judy Ethell, our Chief Financial Officer, failed to report a Form 4 to report the issuance of RSUs to Robert Glatz, her spouse, in connection with his employment in August 2005. The issuance of RSUs to Mr. Glatz, which was previously described in our Annual Reports on Form 10-K for fiscal years 2004 and 2005 (filed with the SEC on January 31, 2006 and November 22, 2006, respectively), was reported on a Form 4 on June 28, 2007.

## **ITEM 11. EXECUTIVE COMPENSATION**

### ***Compensation Discussion and Analysis***

The success of our business largely depends on our ability to attract, retain and motivate qualified employees, particularly professionals with the advanced information technology skills necessary to perform the services we offer. Our management and the Compensation Committee of our Board of Directors devote a significant amount of time and attention to addressing the compensation of our professionals. Our Compensation Committee has the authority to determine the compensation for our executive officers, including making individual compensation decisions, and reviewing and structuring the compensation programs applicable to our executive officers. Our executive officers are our Chairman of the Board, Chief Executive Officer, Chief Financial Officer, Chief Operating Officer and General Counsel and Secretary. This compensation discussion and analysis provides perspective on our compensation objectives and policies for our Chief Executive Officer, our Chief Financial Officer and our other executive officers. We believe that an understanding of our approach to managing director compensation generally is useful to an understanding of our business model and our particular compensation practices as it relates to our executive officers. For additional information, see Item 1, Business Employees, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations Principal Business Priorities for 2007 and Beyond, and Managing Director Compensation Plan.

### ***Overall Compensation Philosophy and Objectives***

Overall, our compensation philosophy is to enhance corporate performance and stockholder value by aligning the financial interests of our managing directors, including our executive officers, with those of our stockholders. We strive to implement this philosophy by tying a significant portion of our managing directors' compensation to our financial performance.

We design our compensation programs to:

attract and retain the best possible talent;

motivate our people's efforts to achieve long-term positive returns for our stockholders;

increase the use of performance and equity-based awards;

communicate metrics to influence employee performance and accountability;

provide for cash and long-term incentive compensation at levels that are competitive with companies within our industry (targeting to remain around the 50th percentile); and

recognize outstanding individual performance.

### *How Compensation is Determined*

*Mix of Total Compensation.* Our Compensation Committee and management collaborate to determine the mix of compensation for our employees, both among short and long-term compensation and cash and non-cash compensation. Our management team establishes and recommends cash compensation for all of our employees, including our executive officers. Our Compensation Committee reviews management's recommendations of guidelines for salary and cash bonus increases for our employees, determines cash compensation for our executive officers, and establishes guidelines and structures for the issuance of equity-based compensation so as to establish the mix of total compensation for our employees.

In the past, our business model rewarded revenue growth and utilization; however, in 2006, management and our Compensation Committee changed this approach, to emphasize profitability and individual performance in establishing the mix of total compensation to be paid to our executive officers.

*Market Benchmarking.* The Compensation Committee reviews and considers peer benchmarking information in determining the mix or relationship of compensation elements for our executive officers.

We target total compensation for our executive officers to be consistent with peer companies performing at comparable levels. To evaluate the reasonableness and competitiveness of our compensation, we obtain information on market pay levels from various sources, including nationally recognized compensation surveys, SEC filings of selected, publicly-traded benchmark companies and first-hand experience obtained from the marketplace in hiring employees. In addition, we typically engage a consultant to gather information on pay levels and practices for a group of comparable management and technology consulting companies based in the United States. For each comparable company, the Compensation Committee's consultant collects information regarding total compensation levels for executive officers (including base salary, annual bonus, long-term incentives and other compensation) and other related items. The Compensation Committee's consultant summarizes and reviews this information, as well as information from leading published compensation surveys, with the Compensation Committee.

*Role of Compensation Committee and Management in Executive Officer Compensation Decisions.* The Compensation Committee evaluates the performance of our executive officers and approves their annual compensation, including salary, bonus, incentive and equity compensation. The Compensation Committee takes into consideration management's recommendations for the total compensation of our executive officers. For our executive officers, the Compensation Committee generally considers the Company's performance within our industry, the challenges we continue to face in improving our business operations, as well as each individual's current contribution and expected future contribution to our performance. The Chief Executive Officer meets with the Compensation Committee to discuss the performance review for each executive officer (other than himself) and to make compensation recommendations. The Chairman of the Board participates in the review and discussion of the Chief Executive Officer's compensation. The Compensation Committee considers these views when making its compensation determinations, as well as an analysis of short-term and long-term compensation prepared by its outside consultant that compares the individual's compensation for the prior two years, evaluates the compensation recommendations made by management and provides a market analysis comparing these compensation amounts to a group of peer companies. In making compensation decisions, the Compensation Committee also considers the results of the 360 degree performance review process we have implemented, which is intended to broaden the scope of our review process for managing directors and allows peers and direct and indirect reports to review and assess the performance of our managing directors, including our executive officers.

*Management Team Employment Agreements.* Since November 2004, there have been significant changes to our executive management team as a result of the issues related to our North American financial reporting systems, internal controls, various ongoing investigations and related litigation. During the past two years, the Compensation

Committee and management have devoted a significant amount of time to attract highly motivated and experienced individuals to comprise our new executive management team and to provide leadership to the Company. In 2005 and 2006, the Board of Directors appointed a new Chief Executive

Officer, Chief Financial Officer and General Counsel, and, in 2007, the Board appointed a new Chief Operating Officer. We entered into written employment agreements with Mr. You, our Chief Executive Officer, Ms. Ethell, our Chief Financial Officer, Mr. Lutz, our General Counsel and Secretary and Mr. Harbach, our Chief Operating Officer. Prior to agreeing upon the compensation terms of these employment agreements, the Compensation Committee took into consideration competitive market compensation information based upon peer group data and the data of companies with a similar market capitalization. Furthermore, it was necessary to compensate Mr. You, Ms. Ethell and Mr. Lutz with additional equity grants and other signing bonus payments to offset compensation that would have been earned or benefits that would have been received by such individuals had they remained with their previous employers.

### ***Equity Compensation Programs***

In connection with our 2006 Annual Meeting of Stockholders, our Board of Directors included a proposal to amend the LTIP to, among other things, provide for a 25 million share increase in the number of shares authorized for equity awards made under the LTIP. In soliciting proxies from our largest stockholders, we informed our stockholders that the increased share capacity would be used to implement a new equity-based retention strategy for 2007, under which awards would vest over several years and be subject to performance-based vesting criteria. Our management and the Compensation Committee made these recommendation because they realized that (1) approximately 70% of the RSUs we issued in 2005 would vest by January 1, 2007 and (2) the number of shares available under our LTIP would not allow us to issue substantial amounts of equity in the near future. Furthermore, because most of our outstanding stock option awards were granted before 2005, we believed those stock options had limited retentive value since they were granted with exercise prices that were still above our common stock's current stock price. We believe that performance-based equity is viewed more favorably than RSUs by our stockholders because vesting is conditioned upon performance criteria that can be objectively measured rather than mere continuation of employment. Our stockholders approved the LTIP amendments on December 14, 2006.

Generally, we do not expect the Compensation Committee to make any additional grants of RSUs or PSUs to our executive officers through the end of 2009. Until that time, we expect that any bonus compensation earned by our executive officers will be paid in cash.

*PSU Program.* In February 2007, the Compensation Committee adopted a performance share unit ( PSU ) program for the Company's highest-performing managing directors and senior managers, including our executive officers. The PSU program was implemented recognizing that: (i) we had achieved some important milestones in our efforts to become timely in our SEC periodic filings; (ii) we were beginning to achieve a level of operational stability under the direction and guidance of our new executive management team; and (iii) our managing directors had demonstrated their ability to maintain our core business under adverse conditions. As a result, management and the Compensation Committee determined that the PSUs should be structured with a view to promoting longer-term retention. The Compensation Committee concluded that the greatest retentive potential would be achieved if the PSUs were initially granted as large, three-year cliff vesting awards rather than in smaller increments with shorter vesting periods. To ensure that vesting of the PSUs was sufficiently tied to Company performance, the vesting of the PSUs was tied to achievement of performance targets of both minimum growth in consolidated business unit contribution ( CBUC ), defined as (i) consolidated net revenue less (ii) professional compensation, other costs of service and sales, general and administrative expense (excluding stock compensation expense, bonus expense, interest expense and infrastructure expense) and total shareholder return. CBUC was selected as a performance metric that we believe demonstrates the core growth of each of our industry groups. In addition, total shareholder return was selected as a best practice performance metric that we believe is a measure important to our stockholders. In determining the thresholds for these performance targets, the Compensation Committee selected target levels that, in its estimation, would require Company growth, yet also be reasonably achievable to encourage and incent our employees to perform. For additional information on the PSU Program, see Item 7, Management's Discussion and Analysis of Financial Condition and



Results of Operations Principal Business Priorities for 2007 and Beyond.

*Restricted Stock Units ( RSUs ).* We will continue to grant RSUs for various purposes, including as awards granted in connection with promotions and, when we have become current in our SEC periodic reports, as part of developing attractive employment offers for new recruits. The vesting of these RSUs continues to be time-based, either with a three-year cliff vesting provision or vesting ratably over four years. By comparison, we expect that future RSUs granted to our executive officers, if any, will include performance-based vesting requirements. While we may incrementally increase the relative proportion of variable compensation of our executive officers through RSU grants, we currently expect that through 2009, the predominant source of equity awards held by our executive officers will be derived from PSUs.

While we have maintained parity with our major competitors on base cash compensation for our executive officers, relevant market data indicates that we continue to lag behind our competitors in the categories of cash incentive and long-term, equity incentive compensation. We believe the issuance of PSU awards help to balance the mix of fixed and variable compensation of our executive officers, aligning us more closely with the compensation structures offered by our competitors.

### ***Principal Components of Executive Officer Compensation***

The principal elements of our executive officer compensation program consist of base salary, annual incentive cash bonuses and, at appropriate intervals, long-term incentive compensation in the form of grants of stock-based awards. We also provide deferred compensation plans, health and welfare (including medical), retirement and other perquisites and benefits to our executive officers generally available to our other employees.

In determining 2006 compensation, we did not engage an outside consultant to assist the Compensation Committee. Compensation determinations, however, were based in part upon compensation information about executive officers at other systems integration and consulting firms gathered by Watson Wyatt Worldwide. In 2006 and 2007, we engaged Towers Perrin as our compensation consultant to prepare compensation analyses of our executive officers, provide market data information used to determine the payment of 2006 bonuses and 2007 compensation and provide guidance on our long-term compensation strategies, including the structuring of our PSU program.

### ***Fixed Compensation***

*Base Salaries.* Base salaries for our executive officers are determined by evaluating the responsibilities of the position held, the experience and performance of the individual and market information comparing such salaries to the competitive marketplace for executive talent, with emphasis on our primary competitors in the management and technology consulting industry. The Compensation Committee considers salary adjustments based upon the recommendation of the Chief Executive Officer (other than with respect to his salary), the Compensation Committee's evaluation of Company performance and the performance of the executive officer, taking into account any additional or new responsibilities assumed by the individual executive officer in connection with promotions or organizational changes. Salary represents a smaller percentage of total compensation for our executive officers than for our less senior managing directors, with a greater percentage of the executive officers' compensation being tied to performance and our share price.

*Determination of 2006 Base Salaries.* The employment agreements that we entered into with Mr. You, Ms. Ethell and Mr. Lutz provided for their respective base annual salaries during 2006, as reflected in the Summary Compensation Table on page 91. Pursuant to their employment agreements (entered into in 2005), base salary for each of Mr. You and Ms. Ethell was unchanged from 2005 to 2006. Mr. McGeary and Mr. Roberts do not have specific employment agreements with the Company.

For 2006, the Compensation Committee approved a base salary for Mr. McGeary in the range of \$650,000 to \$750,000, and delegated its authority to the Chief Executive Officer to make the final determination of his base salary. Our Chief Executive Officer determined that Mr. McGeary's base salary for

2006 should be \$650,000, based on Mr. McGeary's active involvement with the Board, his contributions as Chief Executive Officer of the Company in 2005, which included the hiring of the new executive management team and his participation in employee roadshows and other communications intended to maintain employee morale and address employee attrition.

In determining Mr. Robert's base salary for 2006, the Compensation Committee considered various factors, such as Mr. Robert's willingness to assume the role of Chief Operating Officer in 2005, the time and effort he spent assisting Mr. You in his new role as Chief Executive Officer, his efforts in addressing morale within the Finance team and helping to abate attrition and his contributions to our Managing Director Compensation Committee.

#### *Variable Compensation*

*Annual Incentive Bonus.* Generally, our executive officers would be eligible to receive annual incentive bonuses pursuant to our MD Compensation Plan, under the same terms and conditions applicable to the Company's managing directors. However, currently, the Compensation Committee determines the target bonus amounts for Mr. You, Ms. Ethell and Mr. Lutz generally in accordance with the terms of their employment agreements. Any such bonuses paid to our executive officers are paid in lieu of MD Compensation Plan amounts. During 2006, we paid the annual bonuses set forth in the Summary Compensation Table on page 91. Bonuses earned for performance during one year are paid in the following year.

*Determination of 2006 Annual Incentive Bonuses.* In 2006, the Compensation Committee determined to award Mr. You, Mr. McGeary and Mr. Roberts cash bonuses equal to 7.8% of their base salaries, which was the percentage applied to determine cash bonuses for each managing director who achieved a "meets expectations" rating for 2006 performance. Although Mr. You was eligible to receive up to 100% of his bonus salary as set forth in his employment agreement, Mr. You and the Compensation Committee agreed that it was appropriate to alter the basis for determining his bonus compensation for 2006. In addition to the cash bonus, the Compensation Committee made conditional RSU awards to Mr. You and Mr. McGeary that would vest based on their achievement of certain performance targets. The stipulated performance targets were not achieved and these awards were not granted. However, for a discussion of a smaller, subsequent award that was made to Mr. You, see *2006 Long-Term Incentive Compensation* below. For 2006, the Compensation Committee determined to award Ms. Ethell and Mr. Lutz cash bonuses equal to 60% and 100%, respectively, of their base salaries (although Mr. Lutz was paid a pro-rated amount, since his employment with the Company started in March 2006).

The Compensation Committee's determinations of cash bonuses awarded to our executive officers in 2006, as well as determinations of 2007 compensation, were based in part on the following considerations:

Harry You	outstanding feedback in the 360 degree peer review process
	successful motivation of the Company's managing directors to drive Company performance
	progress made and left to be achieved with respect to the Company's SEC filing status
	evaluations by Board members

Roderick McGeary	time dedicated to Board of the Directors and effectiveness in fulfilling Chairman role; liaison role between management and the Board management roles and responsibilities, in addition to Board role executive sponsor of the Company's transition to new financial reporting systems executive management role in addressing contractual or engagement relationship issues
Judy Ethell	development of Finance leadership team responsibilities related to development of financial reporting systems oversight of internal audit, internal controls and Sarbanes-Oxley efforts progress achieved and remaining to be achieved with respect to the filing of the Company's SEC periodic reports expanded responsibilities as Chief Financial Officer evaluations by the Audit Committee
Laurent Lutz	restructuring of the Legal department stewardship of key external constituencies e.g., SEC, New York Stock Exchange, insurers creation and implementation of compliance function success in managing and resolving various disputes and lawsuits level of contribution in Board of Directors and committee meetings implementation and oversight of improved disclosure controls
Rich Roberts	individual performance rating among managing directors leadership role within the Public Services business unit

*Long-Term Incentive Compensation*

*2006 Long-Term Incentive Compensation.* In addition to their annual cash incentive bonuses, Mr. You and McGeary received grants of RSUs in connection with their 2006 performance. When the Compensation Committee determined Mr. You's 2006 base compensation, the Compensation Committee also decided that to incent Mr. You's performance, it would make a conditional grant of RSUs to Mr. You at the end of 2006 if Mr. You achieved certain performance milestones. Mr. You was eligible to receive a grant of 187,500 RSUs, to vest 25% on the grant date and 25% annually over the next three years, subject to the achievement of Company performance milestones for 2006. In early 2007, the Compensation Committee determined that these milestones had not been achieved, and as a result, these RSUs were not granted. The Compensation Committee did acknowledge, however, that Mr. You had made substantial contributions to the Company in 2006 (as set forth above) and, as a result, the Compensation Committee decided to make a smaller award of 72,992 RSUs to Mr. You, as bonus compensation for his performance.

In evaluating Mr. McGeary's compensation for 2006, the Compensation Committee considered market data indicating that while Mr. McGeary's cash compensation was commensurate for his position and responsibilities, his long-term incentive compensation was lower than market. Based on the factors set forth above, as well as an analysis of the mix of Mr. McGeary's fixed and variable compensation, the Compensation Committee determined that it would increase Mr. McGeary's long-term compensation. As a result, Mr. McGeary was granted 29,197 RSUs on February 12, 2007.

None of our executive officers received equity grants in 2006 as part of their compensation for 2006. Several of our executive officers, however, received equity grants for reasons other than as part of their 2006 compensation. For an explanation of these grants, please see the Summary Compensation Table on page 91.

On April 20, 2005, pursuant to Regulation BTR, the Company announced there would be a blackout period under the Company's 401(k) plan. Due to existence of the blackout period, the Company was unable to make issuances of equity awards to its executive officers prior to September 14, 2006. The Company's 401(k) Plan was subsequently amended to permanently prohibit participant purchases and Company contributions of its common stock under the 401(k) Plan and as a result of this action, the blackout period under the 401(k) Plan ended, effective as of September 14, 2006 and the Company was again able to make equity-based awards to its executive officers.

To date, we have not instituted any equity ownership requirements for our executive officers. We did not consider any such policy in 2006 due to the BTR blackout mentioned above, as well as the complexities and risks associated with open-market purchases of our common stock by our executive officers while we are not current in our SEC periodic filings. We expect to consider an equity ownership policy once we have become current in our SEC periodic filings.

*2007 Compensation*

*Base Salary.* In determining 2007 compensation, management and the Compensation Committee agreed that the executive officers would receive the standard 4% increase in base compensation provided to all the Company's other managing directors in 2007. The Compensation Committee approved the following 2007 salaries for our executive officers:

<b>Name</b>	<b>Base Salary for 2007</b>
Harry L. You	\$ 780,000
Roderick C. McGearry	676,000
Judy A. Ethell	520,000
Laurent C. Lutz	520,000

In January 2007, Mr. Harbach was appointed as our Chief Operating Officer, replacing Mr. Roberts as an executive officer of the Company. Mr. Harbach's base salary for 2007, set forth in his employment agreement with the Company, is \$700,000.

*PSU Awards.* As part of our 2007 compensation program, the Compensation Committee approved in March 2007 the issuance of PSU awards to our executive officers. The Compensation Committee determined the amount of each PSU award granted to our executive officers by reviewing each executive officer's individual performance and responsibilities and roles within the Company and by assessing and comparing the executive officer's total compensation, including previously granted incentive awards and the balance of fixed and variable compensation, with competitive market data provided by Towers Perrin. PSU awards were granted to the following individuals:

<b>Name</b>	<b>Total Number of PSUs Granted (1)</b>
Harry L. You	959,079

Roderick C. McGear	255,754
Judy A. Ethell	306,905
Laurent C. Lutz	383,632

- (1) The PSUs will vest on December 31, 2009 if two performance-based metrics are achieved for the performance period beginning on February 2, 2007 and ending on December 31, 2009. The Company must first achieve a compounded average annual growth target in consolidated business unit contribution. Then, depending on the Company's total shareholder return relative to those companies that comprise the S&P 500, the percentage of PSU awards that vest will vary from 0% to 250%. The Total Number of PSUs Granted assumes that 100% of the PSU awards vest.

Mr. Harbach did not receive a PSU award since he received a grant of 888,325 RSUs on January 8, 2007 as part of his employment arrangement with the Company.

#### *Other Compensation*

*Deferred Compensation Plans.* We have a Deferred Compensation Plan and a Managing Directors Deferred Compensation Plan. The two plans are substantially identical and permit a select group of management and highly compensated employees to accumulate additional income for retirement and other personal financial goals by making elective deferrals of compensation to which they will become entitled to in the future. Our deferred compensation plans are nonqualified and unfunded, and participants are unsecured general creditors of the Company as to their accounts. Managing directors, including our executive officers, and other highly compensated executives selected by the plans' administrative committee are eligible to participate in the plans. None of our executive officers have participated in our deferred compensation plans.

*Other Benefits.* We offer a variety of health and welfare and retirement programs to all eligible employees. Our executive officers are generally eligible for the same health and welfare programs on the same basis as our other employees. Our retirement program for U.S. employees consists of a 401(k) program, in which executive officers participate on the same terms and conditions as other eligible employees. We match the individual employee's contribution to the program of 25% of the first 6% of pre-tax eligible compensation contributed to the plan, and, at our discretion, may make additional discretionary contributions of up to 25% of the first 6% of pre-tax eligible compensation contributed to the plan. Employee contributions to the 401(k) program for our executive officers, as well as other more highly compensated employees, are limited by federal law. We have not made up for the impact of these statutory limitations on named executives through any type of nonqualified deferred compensation or other program.

*Perquisites and Other Compensation.* In general, we have historically avoided the use of perquisites and other types of non-cash benefits for executive officers and expect this policy to continue. Certain of our executive officers have received perquisites such as reimbursements of moving expenses and legal fees and gross-up payments in connection with the same as set forth in their respective employment agreements.

#### *Regulatory Considerations*

The Internal Revenue Code contains a provision that limits the tax deductibility of certain compensation paid to our executive officers to the extent it is not considered performance-based compensation under the Internal Revenue Code. We have adopted policies and practices to facilitate compliance with Section 162(m) of the Internal Revenue Code. It is intended that awards granted under the LTIP to such persons will qualify as performance-based compensation within the meaning of Section 162(m) and regulations under that section.

In making decisions about executive compensation, we also consider the impact of other regulatory provisions, including the provisions of Section 409A of the Internal Revenue Code regarding non-qualified deferred compensation and the change-in-control provisions of Section 280G of the Internal Revenue Code. In accordance with



recent IRS guidance interpreting Section 409A, the LTIP will be administered in a manner that is in good faith compliance with Section 409A. The Board intends that any awards under the LTIP satisfy the applicable requirements of Section 409A. Generally, Section 409A is inapplicable to incentive stock

options and restricted stock and also to nonqualified stock options so long as the exercise price for the nonqualified option may never be less than the fair market value of the common stock on the date of grant.

In making decisions about executive compensation, we also consider how various elements of compensation will impact our financial results including the impact of SFAS 123(R) which requires us to recognize the cost of employee services received in exchange for awards of equity instruments based upon the grant date fair value of those awards. SFAS 123(R) was a consideration in adopting restricted stock units as a long-term equity incentive.

**REPORT OF THE COMPENSATION COMMITTEE  
OF THE BOARD OF DIRECTORS ON EXECUTIVE COMPENSATION**

The Compensation Committee of the Board of Directors has reviewed and discussed the Compensation Discussion and Analysis section of this Annual Report on Form 10-K with the Company's management and, based on such review and discussion, recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this Annual Report on Form 10-K.

COMPENSATION COMMITTEE

*Douglas C. Allred (Chair)*

*Betsy Bernard*

*Jill S. Kanin-Lovers\**

*J. Terry Strange\*\**

*\*Member of the Compensation Committee since May 10, 2007*

*\*\*Member of the Compensation Committee during 2006 and through June 18, 2007*

**Summary of Cash and Certain Other Compensation**

The Summary Compensation Table below sets forth information concerning all compensation for services in all capacities to the Company for 2006 of those persons who were the Chief Executive Officer, Chief Financial Officer and the three other most highly compensated executive officers of the Company for 2006 ( named executive officers ).

**Summary Compensation Table**

Name and Principal Position	Year	Salary (\$ (1))	Bonus (\$ (1))	Stock Awards (\$ (2))	Option Awards (\$ (2))	Non-Equity Incentive		Total (\$)
						Plan Compensation (\$)	All Other Compensation (\$)	
Harry L. You(3) <i>Chief Executive Officer</i>	2006	750,000	58,500	938,900	2,519,300		331,828	4,598,528
Roderick C. McGeary <i>Chairman of the Board</i>	2006	662,640	50,712	250,000	263,732			1,227,084
Judy A. Ethell(4) <i>Chief Financial Officer</i>	2006	500,000	300,000	690,700	1,131,000		3,797	2,625,497
Laurent C. Lutz(5) <i>General Counsel and Secretary</i>	2006	411,059	1,311,059			525,000	78,431	2,325,549
Richard J. Roberts(6) <i>Chief Operating Officer</i>	2006	650,000	50,700	855,400	332,160		3,977	1,892,237

- (1) Unless otherwise noted, Bonus amounts consist of performance-based cash bonuses accrued in the fiscal year for which the bonus has been earned. We have entered into employment agreements with Mr. You, Ms. Ethell and Mr. Lutz that set forth the terms of their compensation.
- (2) Unless otherwise noted, stock awards, which consist of RSUs, and stock options were granted in accordance with our LTIP. If dividends are declared on our common stock while any RSUs are outstanding, the number of shares to be granted upon settlement of the RSUs will be adjusted to reflect the payment of such dividends. Amounts reflected in the table as 2006 compensation reflect the dollar amount recognized for financial statement reporting purposes in 2006 in accordance with SFAS 123(R) for equity award expense. For additional information about 2006 awards of RSUs, stock options, and other non-equity incentive plan compensation, see Grants of Plan-Based Awards.
- (3) Mr. You's All Other Compensation includes reimbursements of \$259,568 for costs related to the sale of his residences, \$17,117 in commuting expenses, \$51,532 in tax equalization payments with respect to the reimbursement of moving expenses and certain state taxes paid by Mr. You, \$2,361 in personal travel expenses

and \$1,250 in Company matching contributions under our 401(k) Plan.

- (4) On October 3, 2006, we entered into a letter agreement with Ms. Ethell relating to the rescission and replacement of certain grants of nonqualified stock options and RSUs made to her in July 2005 in connection with her employment with the Company. On July 1, 2005, Ms. Ethell received a grant for 292,000 RSUs and a stock option grant to purchase 600,000 shares of common stock (collectively, the 2005 Awards ). The 2005 Awards were intended to be of effect only after the Company had become current in its SEC periodic filings; however, we reconsidered the rationale behind this approach and as a result, we canceled the 2005 Awards and made subsequent replacement grants to Ms. Ethell, effective as of September 19, 2006 (the 2006 Awards ). The 2006 Awards consist of: (a) stock options to purchase up to 600,000 shares of our common stock, of which 25% vested upon grant, and, subject to achievement of certain performance criteria, 25% will vest on July 1 in each of 2007 through 2009, (b) 292,000 RSUs, of which 204,400 vested on date of grant, and, subject, to achievement of certain performance criteria, an additional 29,200 will vest on July 1 in each of 2007 through 2009, and (c) 94,000 RSUs, of which 25% vested on date of grant, and subject to achievement of certain performance criteria, 25% will vest on July 1 in each of 2007 through 2009.
- (5) Mr. Lutz's annual base salary for 2006 was \$500,000. The amount reported as Mr. Lutz's salary is the amount actually paid in 2006. Mr. Lutz's 2006 bonus compensation consists of a \$900,000 signing bonus and \$411,059 of bonus compensation (pro rated, based on an annual performance bonus of \$500,000). Mr. Lutz's 2006 non-equity incentive plan compensation is more fully described under Grants of Plan-Based Awards. Mr. Lutz's All Other Compensation consists of \$41,857 in legal fees paid on Mr. Lutz's behalf in connection with the negotiation of his employment arrangements with the Company, reimbursement of \$36,574 in tax equalization payments with respect to the reimbursement of legal fees and certain state taxes paid by Mr. Lutz.
- (6) Effective as of January 8, 2007, Mr. Roberts no longer serves as our Chief Operating Officer in connection with the appointment of F. Edwin Harbach as our President and Chief Operating Officer.

### Grants of Plan-Based Awards

The following table provides information relating to equity awards made in 2006 to our named executive officers. All of the following awards that relate to our common stock were made pursuant to our LTIP.

Name	Grant Date	Estimated Future Payouts Under Non-Equity Incentive Plan Awards		Estimated Future Payouts Under Equity Incentive Plan Awards		Exercise Price of Option Awards (\$/Sh)	Grant Date Fair Value of Stock and Option Awards
		Target (\$)	Maximum (\$)	Target (#)	Maximum (#)		
Harry You Roderick C. McGeary (1)	9/25/2006			29,411			\$ 249,994
Judy A. Ethell (2)	9/19/2006			600,000		\$ 8.70	2,883,600
	9/19/2006			292,000			2,540,400
	9/19/2006			94,000			817,800
Laurent C. Lutz (3)	2/27/2006	\$ 1,750,000				(3)	
Richard J. Roberts (4)	9/25/2006			77,343			657,416
	9/25/2006			93,177			792,005

(1) Mr. McGeary was granted 29,411 RSUs that vest 25% on January 1 in each of 2007 through 2010.

(2) Ms. Ethell was granted the following awards: (a) stock options to purchase up to 600,000 shares of our common stock, of which 25% vested upon grant, and, subject to achievement of certain performance criteria, 25% will vest on July 1 in each of 2007 through 2009, (b) 292,000 RSUs, of which 204,400 vested on date of grant, and, subject, to achievement of certain performance criteria, an additional 29,200 will vest on July 1 in each of 2007 through 2009, and (c) 94,000 RSUs, of which 25% vested on date of grant, and subject to achievement of certain performance criteria, 25% will vest on July 1 in each of 2007 through 2009. These grants were made pursuant to a letter agreement between the Company and Ms. Ethell, effective as of October 3, 2006, and replaced grants made to Ms. Ethell in 2005 in connection with her employment with the Company. The 2005 Awards were intended to be modified to be of effect only after the Company had become current on its SEC periodic filings, however, the rationale behind this approach was reconsidered by the Company. As a result, the 2005 Awards were canceled and the Compensation Committee approved these subsequent grants to Ms. Ethell, effective as of September 19, 2006.

(3) Mr. Lutz was granted the following: on the earlier of (i) the date an effective registration statement on Form S-8 is filed or is on file and (ii) the date, if any, we cease to be a reporting company under the Exchange Act, a grant of RSUs having an aggregate value of \$1.75 million; provided, however, if RSUs have not yet been granted,

subject to certain conditions, Mr. Lutz will receive cash payments (which will reduce the value of any RSUs to be granted) of \$525,000 on July 1, 2006, \$525,000 on June 30, 2007 and \$175,000 on December 31 in each of 2007 through 2010.

- (4) Mr. Roberts was granted the following awards: (a) 77,343 RSUs, all of which vested on September 25, 2006, and (b) 93,177 RSUs that vest 25% on January 1 in each of 2007 through 2010.

### Outstanding Equity Awards at Fiscal Year-End (December 31, 2006)

The following table provides information regarding the value of all unexercised options and unvested restricted stock units previously awarded to our named executives as of December 31, 2006.

Name	Option Awards				Stock Awards				
	Number of Securities Underlying Unexercised Options (#)	Number of Securities Underlying Unexercised Options (#)	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Options (#)	Option Exercise Price (\$)	Option Expiration Date	Number of Shares or Units of Stock That Have not Vested (#)	Market Value of Shares or Units of Stock That Have not Vested (\$)	Equity Incentive Plan Awards: Number of Shares, Units or Other Rights That Have not Vested (#)	Market Payout Value of Unearned Shares, Units or Other Rights That Have not Vested (\$)
Harry L. You Roderick C. McGeary	500,000(1)	1,500,000(1)		\$ 7.55	3/18/2015	750,000(2)	\$ 5,902,500		
	7,928			55.50	6/30/2010	29,411(3)	231,465		
	15,000			16.38	4/24/2011				
	450,000			9.00	11/19/2014				
Judy A. Ethell	150,000(4)	450,000(4)		8.70	9/19/2016	87,600(4) 70,500(4)	689,412 554,835		
Laurent C. Lutz (5)									
Richard J. Roberts	11,892			18.00	7/31/2010	93,177(6)	733,303		
	53,205			18.00	2/8/2011				
	50,000			13.30	7/24/2011				
	11,611			11.01	9/3/2012				
	70,000			10.01	9/3/2012				

125,000		8.19	8/28/2013
40,000(7)	20,000(7)	9.15	10/4/2014

- (1) Mr. You was granted stock options to purchase up to 2,000,000 shares of our common stock, which options vest 25% on March 18 in each of 2006 through 2009.
- (2) Mr. You was granted 750,000 RSUs, of which 62,500 RSUs vested on March 21, 2007, 125,000 RSUs vest on March 21, 2008, 187,500 RSUs vest on March 21 in each of 2009 and 2010, 125,000 RSUs vest on March 21, 2011 and 62,500 RSUs vest on March 21, 2012.
- (3) Mr. McGeary was granted 29,411 RSUs that vest 25% on January 1 in each of 2007 through 2010.
- (4) Ms. Ethell was granted stock options to purchase up to 600,000 shares of our common stock, of which 25% vested upon grant (September 19, 2006), and, subject to achievement of certain performance criteria, 25% will vest on July 1 in each of 2007 through 2009. In addition, Ms. Ethell was granted (i) 292,000 RSUs, of which 204,400 vested on date of grant (September 19, 2006), and, subject to achievement of certain performance criteria, an additional 29,200 will vest on July 1 in each of 2007 through 2009; and (ii) 94,000 RSUs, of which 25% vested on date of grant (September 19, 2006), and subject to achievement of certain performance criteria, 25% will vest on July 1 in each of 2007 through 2009. These grants were made in connection with the rescission and replacement of the 2005 Awards. For additional information, see footnote 4 of the Summary Compensation Table on page 91.
- (5) From April 20, 2005 through September 14, 2006, pursuant to Regulation BTR, we announced there would be a blackout period under our 401(k) plan. Due to existence of the blackout period, we were unable to make issuances of equity awards to its executive officers. In connection with his employment, Mr. Lutz was granted the following: on the earlier of (i) the date an effective registration statement on Form S-8 is filed or is on file and (ii) the date, if any, we cease to be a reporting company under the Exchange Act, a grant of RSUs having an aggregate value of \$1.75 million; provided, however, if RSUs have not yet been granted, subject to certain conditions, Mr. Lutz will receive cash payments (which will reduce the value of any RSUs to be granted) of \$525,000 on July 1, 2006, \$525,000 on June 30, 2007 and \$175,000 on December 31 in each of 2007 through 2010.
- (6) Mr. Roberts was granted 93,177 RSUs that vest 25% on January 1 in each of 2007 through 2010.
- (7) Mr. Roberts was granted stock options to purchase up to 60,000 shares of our common stock. The stock options vest as follows: 1/3 on October 4 in each of 2005, 2006, and 2007.



### Option Exercises and Stock Vested

The following table provides information with respect to restricted stock units and restricted stock that vested during 2006 with respect to our named executive officers. No options were exercised in 2006.

Name	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting (\$)
Harry L. You				
Roderick C. McGearry				
Judy A. Ethell			227,900	\$ 1,982,730
Laurent C. Lutz				
Richard J. Roberts			149,782	1,226,787

#### *Pension Benefits*

Our only retirement plan for our U.S.-based associates, including our named executive officers, is our 401(k) plan. We do not have a pension plan in which our named executive officers are eligible to participate.

#### *Nonqualified Deferred Compensation Plans*

We have a Deferred Compensation Plan and a Managing Directors Deferred Compensation Plan, which are designed to permit a select group of management and highly compensated employees who contribute materially to our continued growth, development and future business success to accumulate additional income for retirement and other personal financial goals through plans that enable the participants to make elective deferrals of compensation to which they will become entitled to in the future. Our deferred compensation plans are nonqualified and unfunded, and participants are unsecured general creditors of the Company as to their accounts. Our managing directors, including our Named Executive Officers, and other highly compensated executives selected by the plans administrative committee are eligible to participate in the plans. To date, none of our Named Executive Officers have participated in any of our deferred compensation plans.

#### *Employment Agreements*

*Managing Director Agreements.* We have entered into a Managing Director Agreement (a Managing Director Agreement) with each of our approximately 650 managing directors, including our named executive officers. Pursuant to the Managing Director Agreement, we provide up to six months pay for certain terminations of employment by us. In addition, the Managing Director Agreement contains non-competition and non-solicitation provisions for a period of up to two years after such executive's termination of employment or resignation.

Effective as of January 31, 2005, we and certain executive officers of the Company, including Richard J. Roberts, entered into an amendment to their Managing Director Agreements (the Amendment). Each Amendment provides that if within 18 months after the date of the Amendment we hire a new Chief Executive Officer other than Roderick C.

McGeary and terminate, or constructively terminate, such Officer's employment under certain circumstances (the Triggering Event), we will pay to such Officer a lump sum cash amount equal to the sum of such Officer's current annual salary, earned and unused personal days and target incentive compensation pursuant to the terms of the incentive compensation plan then in effect. In addition, any unvested stock options that would have vested from the date of such Triggering Event through the next following anniversary date of the grant of such options will automatically vest. As of July 31, 2006, each of the Amendments had expired.

*Employment Agreement for Harry L. You.* Effective March 21, 2005, we entered into the following arrangements with Harry L. You, our Chief Executive Officer:

*Compensation.* Information regarding Mr. You's annual base and bonus compensation can be found in the Summary Compensation Table above. Information regarding equity awards issued to Mr. You pursuant to his employment arrangements are included under Outstanding Equity Awards at Fiscal Year-End (December 31, 2006), above.

*Benefits/Long-Term Incentives.* Mr. You is entitled to participate in all employee benefit (including long-term incentives), fringe and perquisite plans, practices, programs, policies and arrangements generally provided to senior executives of the Company at a level commensurate with his position.

*Relocation.* Mr. You was reimbursed for reasonable relocation and transitional housing and travel expenses, including a tax gross-up payment to cover all applicable taxes, and the Company provided assistance in connection with the sale of his residences.

*Indemnification.* We agreed to indemnify Mr. You with respect to his activities on behalf of the Company, for any failure of the Company to comply with Section 409A of the Internal Revenue Code of 1986, as amended, and for certain other matters.

*Termination Payments.* Mr. You is entitled to certain termination payments under his employment agreement, which are described below under Potential Payments upon Termination or Change of Control.

*Employment Agreement for Judy A. Ethell.* Effective as of July 1, 2005, we entered into the following arrangements with Judy A. Ethell, our Chief Financial Officer Finance:

*Compensation.* Information regarding Ms. Ethell's annual base and bonus compensation can be found in the Summary Compensation Table above. Information regarding equity awards issued to Ms. Ethell pursuant to her employment arrangements are included under Outstanding Equity Awards at Fiscal Year-End (December 31, 2006), above.

*Benefits/Long-Term Incentives.* Ms. Ethell is entitled to participate in all employee benefit (including long-term incentives), fringe and perquisite plans, practices, programs, policies and arrangements generally provided to senior executives of the Company at a level commensurate with her position.

*Relocation.* Ms. Ethell was reimbursed for reasonable relocation and transitional housing and travel expenses, including a tax gross-up payment to cover all applicable taxes, and the Company provided assistance in connection with the sale of her principal residence.

*Indemnification.* We agreed to indemnify Ms. Ethell with respect to her activities on behalf of the Company, for any failure of the Company to comply with Section 409A of the Internal Revenue Code of 1986, as amended, and for certain other matters.

*Termination Payments.* Ms. Ethell is entitled to certain termination payments under her employment agreement, which are described below under Potential Payments upon Termination or Change of Control.

*Employment Agreement for Laurent C. Lutz.* Effective as of October 17, 2006, the Board determined that Laurent C. Lutz, our General Counsel and Secretary, was an executive officer of the Company. Effective as of February 27, 2006, we had entered into the following arrangements with Mr. Lutz:

*Compensation.* Information regarding Mr. Lutz's annual base and bonus compensation can be found in the Summary Compensation Table above. Information regarding non-equity incentive plan compensation awarded to Mr. Lutz are included under Grants of Plan-Based Awards, above.

*Benefits/Long-Term Incentives.* Mr. Lutz is entitled to participate in all employee benefit (including long-term incentives), fringe and perquisite plans, practices, programs, policies and arrangements generally provided to senior executives of the Company at a level commensurate with his position.

*Legal Fees.* Mr. Lutz was reimbursed for reasonable legal fees in connection with the negotiation and drafting of his employment arrangements.

*Indemnification.* We agreed to indemnify Mr. Lutz in the event that any activity he undertakes on behalf of the Company is challenged as being in violation of any agreement he may have with a prior employer and for certain other matters. In addition, Mr. Lutz is entitled to receive a gross-up for any payment to him under any of his agreements that would be subject to a surtax imposed by Section 409A of the Internal Revenue Code or for any interest or penalties thereon.

*Termination Payments.* Mr. Lutz is entitled to certain termination payments under his employment agreement, which are described below under Potential Payments upon Termination or Change of Control.

***Potential Payments upon Termination or Change of Control***

*Severance Payments under Managing Director Agreements.* Under our Managing Director Agreements, we provide up to six months pay for terminations of employment by us other than for cause, as defined in the agreements. In addition, these agreements contain non-competition and non-solicitation provisions for a period of up to two years after such executive's termination of employment or resignation.

*Severance Payments under Employment Agreements.* Under our employment agreements with Mr. You, Ms. Ethell and Mr. Lutz, we have that upon termination of the individual's employment by us without cause or by the individual for good reason, (as defined in the agreements), within 30 days after our receipt of a fully executed release, we will make a severance payment to the individual.

*Termination Payments under Special Termination Agreements.* We have entered into special termination agreements (each, a Special Termination Agreement) with certain key personnel, including each of our Named Executive Officers (with the exception of Mr. McGeary), as set forth below. The purpose of the Special Termination Agreement is to ensure that these executives are properly protected in the event of a change in control of the Company, thereby enhancing our ability to hire and retain them. The terms of the Special Termination Agreements vary up to a maximum of three years, which terms automatically renew for additional one-year terms unless we give notice that the agreement will not be renewed, or, if later, two years after a change in control. The protective provisions of the Special Termination Agreement become operative only upon a change in control, as defined in the agreement.

All Special Termination Agreements signed on or after August 1, 2006 specify that if, after a change in control and during the term of the agreement, we terminate the executive's employment other than for cause (as defined in the agreements) or the executive terminates his employment because his salary was reduced by at least 20%, the executive is entitled to certain benefits. Generally, Special Termination Agreements signed before August 1, 2006 specify that if, after a change of control and during the term of the agreement, we terminate the executive's employment other than for cause or if the executive terminates his employment for specified reasons (including if his responsibilities have been materially reduced or adversely modified or his compensation has been reduced), the executive is entitled to certain benefits. Under the Special Termination Agreements, these benefits generally include the payment of approximately one year's compensation, based on salary plus bonus as specified in the agreement, continued coverage under our welfare benefit plans (e.g., medical, life insurance and disability insurance) for up to two years at no cost, and outplacement counseling.

**Potential Payments  
Upon Termination of Employment or Change-in-Control  
as of December 31, 2006**

The table below sets forth the potential payments that generally would have been payable to each of our named executive officers as of December 31, 2006 if:

the named executive officer's employment were terminated by us without Cause (as defined in such named executive officer's employment agreement) or by the named executive officer for Good Reason (as defined in such named executive officer's employment agreement); and

the named executive officer's employment (a) were terminated by us within two years after a Change in Control (as defined in such named executive officer's Special Termination Agreement) for any reason other than Cause (as defined in such named executive officer's Special Termination Agreement) or if the executive became permanently disabled or was unable to work for a period of 180 consecutive days, (b) (i) were involuntarily terminated by us (other than for Cause) or (ii) were terminated by the named executive officer following a reduction or adverse change in the named executive officer's duties or compensation, in each case within six months prior to a Change in Control and in anticipation of a Change in Control or (c) were terminated by the named executive officer during the term of the Special Termination Agreement but after a Change in Control if one of the events specified in such named executive officer's Special Termination Agreement has occurred.

Name	Termination of Employment (1) (2)	Change in Control (3)
Harry L. You	\$ 3,724,531(4)	\$ 29,477,602(5)
Roderick C. McGeary	162,500(6)	
Judy A. Ethell	1,488,731(7)	11,627,168(8)
Laurent C. Lutz	4,633,709(9)	12,218,534(10)
Richard J. Roberts	325,000(11)	4,167,168(12)

(1) Amounts set forth in the table for Mr. You, Ms. Ethell and Mr. Lutz reflect the severance payments payable under their respective employment agreements. If Mr. You, Ms. Ethell or Mr. Lutz's employment is not terminated (i) by us without Cause (as defined in such named executive officer's employment agreement) or (ii) by the named executive officer for Good Reason (as defined in such named executive officer's employment agreement), then such named executive officer may still be eligible to receive payments representing earned but unpaid salary and bonuses amounts, any unpaid accrued personal days or unreimbursed business expenses and any other amounts due under the Company's benefit plans. If Mr. You, Ms. Ethell or Mr. Lutz does not qualify for payment under any of the provisions of their respective employment agreements, they may be eligible to receive severance payments under their respective Managing Director Agreements if their employment is terminated for Cause (as defined in the respective Managing Director Agreement) or for no reason. Such payments would generally consist of all earned and unpaid base salary plus a payment equal to three months' pay at such named executive officer's current base salary. Amounts payable under the Managing Director Agreements for Mr. You, Ms. Ethell and Mr. Lutz as of December 31, 2006 would have been \$187,500, \$125,000 and \$125,000, respectively. Amounts set forth in the table for Messrs. McGeary and Roberts reflect the severance payments payable under their respective Managing Director Agreements.

(2)

The values of accelerated stock options and RSUs assume a \$7.87 per share price for our common stock (the closing price on December 29, 2006).

- (3) Amounts set forth in the table for Mr. You, Ms. Ethell, Mr. Lutz and Mr. Roberts reflect the termination payments payable governed under their respective Special Termination Agreements upon a Change of Control (as defined in such agreements). Mr. McGeary is not a party to a Special Termination Agreement. Even if Mr. You, Ms. Ethell or Mr. Lutz is not eligible to receive the payments set forth in the table above upon a change in control (as defined in the Special Termination Agreements), all unvested options and restricted stock held will immediately vest upon the occurrence of a Change of Control (as defined under the LTIP) pursuant to such named executive officer's employment agreement. In addition, the Change of Control provisions under the LTIP generally provide that any unvested portion of stock option grants and RSUs will vest upon the occurrence of a Change of Control (as defined in the LTIP). See Change of Control Provisions Under the LTIP below. Furthermore, if such named executive

officer is not eligible to receive the payments and other benefits specified in his or her Special Termination Agreement upon a change in control, such named executive officer may be eligible to receive the payments payable upon termination of employment under such individual's employment agreement, as specified in this table and the related footnotes.

- (4) Under Mr. You's employment agreement, Mr. You would have been entitled to the following: (i) payment equal to two times the sum of his (A) annual base salary (\$750,000) and (B) target bonus (\$750,000), (ii) payment of accrued and unused personal days (\$51,469), (iii) payment of premiums under the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended for a period of 18 months after termination (\$13,906), and (iv) the vesting of an additional 500,000 options and 62,500 RSUs that would have vested within the first anniversary of the termination date (\$651,875).
- (5) Under Mr. You's Special Termination Agreement, Mr. You would have been entitled to the following: (i) payment equal to 299% of the sum of his (A) annual base salary in 2006 (\$750,000) and (B) bonus payment in 2005 (\$1,000,000), (ii) for a period of 2 years after his termination, continuation of medical, dental, life insurance, disability, accidental death and dismemberment benefits and other welfare benefits, subject to certain exceptions (\$15,307), (iii) if Mr. You's employment is involuntarily terminated by us (other than for Cause) or there is a reduction or adverse change in Mr. You's duties or compensation and Mr. You terminates his employment within six months prior to a Change of Control and in anticipation of a Change of Control, the vesting of all unvested options and RSUs (an additional 1,500,000 options and 750,000 RSUs valued at \$6,382,500), (iv) reimbursement for outplacement services, (v) payment of any earned but unpaid salary, bonus or incentive compensation and (vi) an additional tax gross-up payment of \$18,591,991.
- (6) Under Mr. McGeary's Managing Director Agreement, Mr. McGeary would have been entitled to payment equal to three months of his base salary (\$650,000).
- (7) Under Ms. Ethell's employment agreement, Ms. Ethell would have been entitled to (i) payment equal to the sum of her (A) annual base salary (\$500,000) and (B) target bonus (\$500,000), (ii) payment of accrued and unused personal days (\$59,389), (iii) payment of premiums under the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended for a period of 18 months after termination (\$13,906), and (iv) the vesting of an additional 150,000 options and 52,700 RSUs that would have vested within the first anniversary of the termination date (\$290,249).
- (8) Under Ms. Ethell's Special Termination Agreement, Ms. Ethell would have been entitled to the following: (i) payment equal to 299% of the sum of her (A) annual base salary in 2006 (\$500,000) and (B) target bonus for 2006 (\$500,000), (ii) for a period of 2 years after her termination, continuation of medical, dental, life insurance, disability, accidental death and dismemberment benefits and other welfare benefits, subject to certain exceptions (\$15,307), (iii) if Ms. Ethell's employment is involuntarily terminated by us (other than for Cause) or there is a reduction or adverse change in Ms. Ethell's duties or compensation and Ms. Ethell terminates her employment within six months prior to a Change of Control and in anticipation of a Change of Control, the vesting of all unvested options and RSUs (an additional 450,000 options and 158,100 RSUs valued at \$870,747), (iv) reimbursement for outplacement services, (v) payment of any earned but unpaid salary, bonus or incentive compensation and (vi) an additional tax gross-up payment of \$7,379,986.
- (9) Under Mr. Lutz's employment agreement, Mr. Lutz would have been entitled to (i) payment equal to the sum of his (A) annual base salary (\$500,000) (or, in the event of termination by Good Reason (as defined in his employment agreement), 1 1/2 times annual base salary) and (B) target bonus (\$500,000), (ii) payment of accrued and unused personal days (\$26,375), (iii) payment of premiums under the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended for a period of 18 months after termination (\$14,401),



(iv) vesting of the portion of his RSUs (or corresponding cash award payment) scheduled to vest on the next vesting date following the termination date (or, in the case of a cash award payment related to a termination occurring prior to July 1, 2007, the next 2 vesting dates) (\$700,000) and (v) an additional tax gross-up payment of \$2,886,147.

- (10) Under Mr. Lutz's Special Termination Agreement, Mr. Lutz would have been entitled to the following: (i) payment equal to 299% of the sum of his (A) annual base salary in 2006 (\$500,000) and (B) target bonus for 2006 (\$500,000), (ii) for a period of 2 years after his termination, continuation of medical, dental, life insurance, disability, accidental death and dismemberment benefits and other welfare benefits, subject to certain exceptions (\$12,417), (iii) if Mr. Lutz's employment is involuntarily terminated by us (other than for Cause) or there is a reduction or adverse change in Mr. Lutz's duties or compensation and Mr. Lutz terminates his employment within six months prior to a Change of Control and in anticipation of a Change of Control, the vesting of all unvested RSUs (or corresponding cash award payment, in the amount of \$1,225,000), (iv) reimbursement for outplacement services, (v) payment of any earned but unpaid salary, bonus or incentive compensation and (vi) an additional tax gross-up payment of \$7,610,423. In addition, pursuant to his employment agreement, Mr. Lutz would have been entitled to acceleration of his unpaid retention bonus (\$375,000) upon a Change in Control (as defined in his Special Termination Agreement).
- (11) Under Mr. Roberts' Managing Director Agreement, Mr. Roberts would have been entitled to payment equal to six months of his base salary (\$650,000).

- (12) Under Mr. Roberts' Special Termination Agreement, Mr. Roberts would have been entitled to the following:
- (i) payment equal to the sum of his (A) annual base salary in 2006 (\$650,000) and (B) potential bonus or incentive compensation (20% of base salary or \$130,000),
  - (ii) for a period of 2 years after his termination, continuation of medical, dental, life insurance, disability, accidental death and dismemberment benefits and other welfare benefits, subject to certain exceptions (\$12,759),
  - (iii) if Mr. Roberts' employment is involuntarily terminated by us (other than for Cause) or (ii) there is a reduction or adverse change in Mr. Roberts' duties or compensation and Mr. Roberts terminates his employment within six months prior to a Change of Control and in anticipation of a Change of Control, the vesting of all unvested options and RSUs (an additional 20,000 options and 93,177 RSUs valued at \$707,703),
  - (iv) reimbursement for outplacement services,
  - (v) payment of any earned but unpaid salary, bonus or incentive compensation and
  - (vi) an additional gross-up payment of \$2,640,791.

*Change of Control Provisions Under the LTIP.* In addition to the provisions in the agreements referred to above, in the event of certain Changes of Control of the Company, any non-vested portion of stock option grants and RSUs, and other awards made under the LTIP will generally vest, and any contractual transfer restrictions on restricted stock or other shares issued upon the settlement of RSUs will be released except under the PSU awards. If such a Change of Control were to occur, all stock options not yet exercisable, including those of our Named Executive Officers set forth in the table captioned Outstanding Equity Awards at Fiscal Year-End (December 31, 2006) would vest. In addition, all cash retention awards, including those granted to Mr. Lutz and set forth in the table captioned Grants of Plan-Based Awards would accelerate. Upon a change of control, for PSU awards, the growth target in consolidated business unit contribution will be waived and the acquiring company may (i) substitute the PSUs for the right to receive the acquiring company's stock with the same vesting and settlement schedule, (ii) accelerate and settle in cash the ratable number of PSUs that would vest through the date of change in control and replace the remaining PSUs with a cash incentive bonus program that provides for an opportunity to earn up to the value of the remaining PSUs, or (iii) if neither of the above options is selected, then the PSUs will vest and settle and be payable within 10 days of the change of control.

### ***Managing Director Compensation Plan***

In January 2006, the Compensation Committee of the Board approved and authorized the development of our MD Compensation Plan. The MD Compensation Plan was designed to be a comprehensive cash and equity-based compensation program for the managing directors of the Company and was intended to replace the previous cash-based compensation program for such individuals. Generally, all managing directors, including our Named Executive Officers, are eligible to participate in the MD Compensation Plan. The primary goal of the MD Compensation Plan is to align the compensation of our managing directors with those of our stockholders, and the plan is designed to offer transparency into the Company's executive compensation program, align company performance and individual performance, provide a fair and objective basis for assessing performance, link managing director roles and responsibilities to the Company's business objectives, and enhance the accountability of the Company's executives. Under the MD Compensation Plan, a managing director's compensation may include the following components: (i) RSUs; (ii) target compensation (which may be cash or equity); (iii) performance compensation; and (iv) additional breakthrough awards.

To date, we have been unable to activate the MD Compensation Plan because we are not current with respect to our SEC periodic reports. We were unable to provide for bonuses under the MD Compensation Plan since the plan has not yet been fully activated and the target levels of profitability set forth under the MD Compensation Plan were not achieved due to our ongoing issues related to our financial accounting systems and internal controls and their related impact on our ability to become current in our SEC periodic reports and deliver shares of common stock under equity-based awards.

***Director Compensation***

Non-employee directors, those who are not employed by us on a full-time or other basis, receive compensation for their service on our Board of Directors. The goals for non-employee director compensation are to fairly pay directors for their service, to align directors' interests with the long-term interests of our

stockholders and to have a structure that is transparent. An employee director receives no additional compensation for their service on the Board.

In 2006, non-employee director compensation included the following elements:

an annual fee of \$40,000;

a meeting fee of \$2,000 for attendance in person at any meeting of the Board or a committee of the Board and \$1,000 for attendance by telephone (members of the Audit Committee are paid \$2,000 for attendance at any Audit Committee meeting, whether they attended in person or by telephone);

a grant of stock options to purchase up to 15,000 shares of common stock upon initial election to the Board;

a grant of stock options to purchase up to 5,000 shares of common stock upon initial election as the Chair of the Audit Committee; and

a grant of 8,000 shares of restricted common stock immediately following each annual meeting of stockholders.

#### 2006 Director Compensation Table

Name	Fees Earned or Paid	Stock	Option	Total
	in Cash (\$)	Awards \$(2)	Awards \$(3)(4)	
Douglas C. Allred	70,000	65,760		135,760
Betsy J. Bernard	66,000	65,760		131,760
Spencer C. Fleischer	75,000	65,760	32,376	173,136
Wolfgang Kemna	73,000	65,760		138,760
Albert L. Lord	98,000	65,760		163,760
Alice M. Rivlin (1)	47,000	65,760		112,760
J. Terry Strange	113,000	65,760	5,482	184,242

- (1) Ms. Rivlin did not stand for re-election at our annual meeting of stockholders held on December 14, 2006.
- (2) Reflects the dollar amount recognized for financial statement reporting purposes for the year ended December 31, 2006, in accordance with SFAS 123(R) with respect to grants of restricted stock in 2006. During 2006, each director was granted 8,000 shares of restricted common stock, each with a fair value of \$65,760. In accordance with SFAS 123(R), fair value is calculated using the closing price of our common stock on the date of grant.
- (3) Reflects the dollar amount recognized for financial statement reporting purposes for the year ended December 31, 2006, in accordance with SFAS 123(R) with respect to stock option awards granted prior to 2006. No stock options were awarded to these individuals in 2006. In accordance with SFAS 123(R), fair value was

estimated using the Black-Scholes option-pricing model.

- (4) Outstanding equity awards for each non-employee director is as follows (for a description of the beneficial ownership by our directors, see Item 12, Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters ):

<b>Name</b>	<b>Outstanding Stock Awards at December 31, 2006</b>	<b>Outstanding Option Awards at December 31, 2006</b>
Douglas C. Allred	28,000	15,000
Betsy J. Bernard	16,000	15,000
Spencer C. Fleischer	8,000	15,000
Wolfgang Kemna	28,000	15,000
Albert L. Lord	24,000	15,000
Alice M. Rivlin (1)	28,000	20,000
J. Terry Strange	24,000	20,000

(1) Ms. Rivlin did not stand for re-election at our annual meeting of stockholders held on December 14, 2006.

We also reimburse directors for reasonable travel expenses related to attending a Board, Committee or other Company related business meetings, and provide liability insurance for our directors and officers.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

***Beneficial Ownership of More Than Five Percent***

The following table sets forth the only persons known by us, as of June 1, 2007, to be beneficial owners or more than five percent of our common stock.

Name and Address of 5% Holders of Common Stock	Common Stock	
	Number of Shares	Percentage of Shares Outstanding
Ariel Capital Management, LLC (1) 200 E. Randolph Drive, Suite 2900 Chicago, IL 60601	30,201,218	15.0%
Glenview Capital Management, LLC (2) 767 Fifth Avenue, 44th Floor New York, NY 10153	20,599,345	10.2
Thornburg Investment Management, Inc (3) 119 E. Marcy Street Santa Fe, NM 87501	18,003,408	8.9
Goldman Sachs Asset Management, L.P. (4) 32 Old Slip New York, NY 10005	13,914,809	6.9

- (1) Represents shares beneficially held by Ariel Capital Management, LLC ( Ariel ), as reported on a Schedule 13G filed on February 14, 2007. Ariel has sole voting power with respect to 26,112,088 shares and sole dispositive power with respect to 30,181,188 shares. These shares are beneficially owned by investment advisory clients of Ariel.
- (2) Represents shares beneficially held by Glenview Capital Management, LLC ( Glenview ), Glenview Capital GP, LLC ( Glenview GP ) and Lawrence M. Robbins, as reported on a Schedule 13G filed on February 14, 2007. Glenview serves as investment manager to various entities and as such may be deemed to have voting and dispositive power of such shares. Glenview GP is a general partner of, and serves as the sponsor of, various funds and as such, may be deemed to have voting and dispositive power over such shares. Mr. Robbins is the Chief Executive Officer of Glenview and Glenview GP.
- (3) Represents shares beneficially held by Thornburg Investment Management, Inc ( Thornburg ), as reported on a Schedule 13G filed on April 19, 2007. Thornburg has sole voting power with respect to 11,008,109 shares and sole dispositive power with respect to 18,003,408 shares.
- (4) Represents shares beneficially held by Goldman Sachs Asset Management, L.P. ( Goldman Sachs ), as reported on a Schedule 13G filed on February 12, 2007. Goldman Sachs has sole voting power with respect to 13,766,568 shares and sole dispositive power with respect to 13,914,809 shares.





### Security Ownership of Directors and Executive Officers

The following table sets forth, as of June 1, 2007, information regarding the beneficial ownership of our common stock held by (i) each of our directors and Named Executive Officers and (2) all of our directors and executive officers as a group. To our knowledge, except as otherwise indicated, each of the persons or entities listed below has sole voting and investment power with respect to the shares beneficially owned by him or her. Beneficial ownership is determined in accordance with Rule 13d-3 under the Exchange Act, pursuant to which a person or group of persons is deemed to have beneficial ownership of any shares that he or she has the right to acquire within 60 days of June 1, 2007. Any shares that a person has the right to acquire within 60 days of June 1, 2007 are deemed to be outstanding but are not deemed to be outstanding for the purpose of computing the percentage ownership of any other person.

Name and Address (1)	Common Stock	
	Number of Shares	Percentage of Shares Outstanding
Harry L. You (2)	1,072,500	*
Roderick C. McGear (3)	621,828	*
Douglas C. Allred (4)	51,000	*
Betsy J. Bernard (5)	39,000	*
Judy A. Ethell (6)	790,600	*
Spencer Fleischer (7)	31,000	*
Jill S. Kanin-Lovers		*
Wolfgang Kemna (8)	51,000	*
Albert L. Lord (9)	58,600	*
Laurent C. Lutz		*
Richard J. Roberts (10)(11)	600,468	*
J. Terry Strange (12)	57,000	*
All executive officers and directors as a group (12 persons)	3,372,996	1.6%

\* Less than 1% of our common stock outstanding.

- (1) The address for all persons listed is c/o BearingPoint, Inc., 1676 International Drive, McLean, Virginia 22102 USA.
- (2) Includes 62,500 vested RSUs and 1,000,000 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007. All 62,500 vested RSUs were scheduled for settlement but have not yet settled.
- (3) Includes 7,352 vested RSUs and 472,928 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007. All 7,352 vested RSUs were scheduled for settlement but have not yet settled.
- (4) Includes 15,000 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007.
- (5) Includes 15,000 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007.

- (6) Includes 280,600 vested RSUs, and 300,000 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007 (assumes vesting of 150,000 RSUs and 52,700 options on July 1, 2007 that are subject to Ms. Ethell achieving certain performance criteria). Also includes 210,000 vested RSUs held by Robert R. Glatz, Ms. Ethell's spouse. All 430,600 vested RSUs were scheduled for settlement but have not yet settled.
- (7) Includes 15,000 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007. Mr. Fleischer is a senior managing member of Friedman Fleischer & Lowe GP II, LLC, a Delaware limited liability company ( FFL GP ). FFL GP is the general partner of Friedman Fleischer & Lowe GP II, L.P., which is the general partner of each of Friedman Fleischer & Lowe Capital Partners II, L.P. ( FFL Capital Partners ), FFL Parallel Fund II, L.P. ( FFL Parallel Fund ) and FFL Executive Partners II, L.P. ( FFL Executive Partners, and together with FFL Capital Partners and FFL Parallel Fund, the FFL Funds ). The FFL Funds are the owners of record of \$40 million of initial principal amount of 0.50% Convertible Senior Subordinated Debentures due July 2010

and warrants to purchase up to 3.5 million shares of common stock. Mr. Fleischer disclaims any beneficial ownership of the securities owned by the FFL Funds, except to the extent of his pecuniary interest therein, if any.

- (8) Includes 15,000 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007.
- (9) Includes 15,000 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007.
- (10) Includes 4,301 shares held through a family trust, 173,076 vested RSUs and 361,708 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007. Of the 361,708 vested RSUs, 111,110 RSUs were scheduled for settlement but have not yet settled.
- (11) Effective as of January 8, 2007, Mr. Roberts no longer serves as our Chief Operating Officer in connection with the appointment of F. Edwin Harbach as our President and Chief Operating Officer.
- (12) Includes 20,000 shares of common stock that may be acquired through the exercise of stock options within 60 days of June 1, 2007.

### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

#### ***Friedman Fleischer & Lowe, LLC /Spencer C. Fleischer***

On July 15, 2005, we issued \$40,000,000 aggregate principal amount of our July 2005 Senior Debentures and common stock warrants to purchase up to 3,500,000 shares of our common stock pursuant to a securities purchase agreement, dated July 15, 2005 (the "FF&L Purchase Agreement"), among the Company and certain affiliates of Friedman Fleischer & Lowe, LLC (the "FF&L Purchasers"). In accordance with the terms of the FF&L Purchase Agreement, Mr. Spencer C. Fleischer was appointed to our Board as a Class I Director, effective July 15, 2005. Mr. Fleischer is a senior managing member and Vice Chairman of Friedman Fleischer & Lowe GP II, LLC, the general partner of Friedman Fleischer & Lowe GP II, LP, which is the general partner of several investment funds that make investments in private and public companies in the United States and Bermuda; he has served in this capacity since 1998. If Mr. Fleischer ceases to be affiliated with the FF&L Purchasers or ceases to serve on the Board, so long as the FF&L Purchasers together hold at least 40% of the original principal amount of the July 2005 Senior Debentures, the FF&L Purchasers or their designees have the right to designate a replacement director to our Board.

#### ***Judy Ethell/Robert Glatz***

Effective as of August 22, 2005, Robert Glatz was appointed Executive Vice President Corporate Development, a managing director and a member of our executive team. Robert Glatz is the spouse of Judy Ethell, our Chief Financial Officer. In connection with his employment, Mr. Glatz is entitled to the following: (a) base salary of \$500,000; (b) 300,000 RSUs, with vesting as follows: 180,000 RSUs on December 31, 2005 and 30,000 RSUs on each of August 22, 2006, 2007, 2008 and 2009; (c) eligible to receive an annual bonus with a target amount equal to 100% of his base salary; and (d) sign-on bonus of \$500,000. In addition, we have provided or will provide to Mr. Glatz relocation assistance, indemnification to the fullest extent permitted by law with respect to his activities on behalf of the Company and for other tax related issues, and employee benefit plans generally provided to senior executives of the Company. In addition, as a managing director, Mr. Glatz is a party to the Managing Director Agreement (with certain changes to the defined terms "Good Reason" and "Change of Control") and the Special Termination Agreement. Pursuant to these agreements, upon termination of Mr. Glatz's employment, we will pay to Mr. Glatz: (i) any earned but unpaid base salary through the date of termination; (ii) any earned but unpaid annual bonus for the preceding year, provided that his employment terminates after the payment date for the annual bonus; (iii) any unpaid accrued personal days; (iv) if we terminate his employment without Cause or he terminates for Good Reason, we will pay to him a lump sum cash amount equal to his annual base salary within 30 days after receipt of an executed release and pay his premiums under the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended, for up to 18 months; and (v) any other amounts due under any of our benefit plans.

#### ***Director Independence***

The Board has reviewed each director's independence. As a result of this review, the Board affirmatively determined that each of Messrs. Allred, Fleischer, Kemna, Lord and Strange, and Msses. Bernard and Kanin-Lovers has no material relationship with the Company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the Company). Furthermore, each of these directors is independent of the Company and its management under the listing standards of the NYSE currently in effect and, with respect to members of the Audit Committee, the applicable regulations of the SEC. Messrs. McGeary and You are employees of the Company.

In connection with the Board's determination of Mr. Fleischer's independence, the Board examined Mr. Fleischer's status as a senior managing member of one of the Company's convertible debt holders. After considering all relevant facts and circumstances, the Board determined Mr. Fleischer's relationship was not material and does not impair the independence of Mr. Fleischer. Although Mr. Fleischer attends committee meetings from time to time, he is not a member of our Audit Committee, Compensation Committee or Nominating and Corporate Governance Committee. For more information about Mr. Fleischer's appointment to the Board and his relationship to one of our convertible debt holders, please see "Certain Relationships and Related Transactions, and Director Independence" Friedman, Fleischer & Lowe, LLC /Spencer C. Fleischer.

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES***Audit Committee Pre-Approval Policies*

The Audit Committee has adopted policies and procedures for approving all audit and permissible non-audit services performed by our independent auditors. Consistent with these policies, all engagements of the independent auditor to perform any audit services and non-audit services have been pre-approved by the Audit Committee. No services provided by our independent auditor were approved by the Audit Committee pursuant to the de minimis exception to the pre-approval requirement set forth in paragraph (c)(7)(i)(C) of Rule 2-01 of Regulation S-X.

*Independent Registered Public Accountant's Fees*

During fiscal years 2006 and 2005, our independent registered public accountants, PricewaterhouseCoopers LLP, billed us the fees set forth below in connection with services rendered:

Type of Fee	Fiscal Year Ended,	
	December 31, 2006	December 31, 2005
Audit Fees (1)	\$ 30,979,000	\$ 33,900,000
Audit Related Fees (2)	275,000	159,300
Tax Fees (3)	960,000	1,956,800
All Other Fees (4)	15,000	33,000
Total	\$ 32,229,000	\$ 36,049,100

- (1) Audit fees include audits of consolidated financial statements, reviews of unaudited quarterly financial statements and services that are normally provided by independent auditors in connection with statutory and regulatory filings.
- (2) Audit related fees include assurance and related services provided by our independent auditors that are reasonably related to the performance of the audit or review of our consolidated financial statements and are not included above under Audit Fees. These services principally include audits of employee benefit plans, accounting consultations, and other services in connection with regulatory reporting requirements.
- (3) Tax services principally include consultation in connection with tax compliance, tax consultations and tax planning.
- (4) All other fees include licenses to technical accounting research software.

**PART IV**

**Item 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

(a)(1) The financial statements of the Company required in response to this Item are incorporated by reference from Item 8 of this Report.

(a)(3) See the exhibits listed below under Item 15(b).

(b) Exhibit Index

<b>Exhibit No.</b>	<b>Description</b>
3.1	Amended and Restated Certificate of Incorporation, dated as of February 7, 2001, which is incorporated herein by reference to Exhibit 3.1 from the Company's Form 10-Q for the quarter ended March 31, 2001.
3.2	Amended and Restated Bylaws, amended and restated as of May 5, 2004, which is incorporated herein by reference to Exhibit 3.1 from the Company's Form 10-Q for the quarter ended March 31, 2004.
3.3	Certificate of Ownership and Merger merging Bones Holding into the Company, dated October 2, 2002, which is incorporated herein by reference to Exhibit 3.3 from the Company's Form 10-Q for the quarter ended September 30, 2002.
4.1	Rights Agreement, dated as of October 2, 2001, between the Company and EquiServe Trust Company, N.A., which is incorporated herein by reference to Exhibit 1.1 from the Company's Registration Statement on Form 8-A dated October 3, 2001.
4.2	Certificate of Designation of Series A Junior Participating Preferred Stock, which is incorporated herein by reference to Exhibit 1.2 from the Company's Registration Statement on Form 8-A dated October 3, 2001.
4.3	Amendment No. 1 to the Rights Agreement between the Company and EquiServe Trust Company, N.A., which is incorporated herein by reference to Exhibit 99.1 from the Company's Form 8-K filed on September 6, 2002.
10.1	Amended and Restated Separation Agreement, dated as of February 13, 2001, among KPMG LLP, KPMG Consulting, LLC and the Company, which is incorporated herein by reference to Exhibit 10.1 from the Company's Form 10-Q for the quarter ended March 31, 2001.
10.2	Transition Services Agreement, dated as of February 13, 2001, among KPMG LLP, KPMG Consulting, LLC and the Company, which is incorporated herein by reference to Exhibit 10.3 from the Company's Form 10-Q for the quarter ended March 31, 2001.
10.3	

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Stock Purchase Agreement dated as of December 29, 1999, between Cisco Systems, Inc. and the Company, which is incorporated herein by reference to Exhibit 10.11 from the Company's Form S-1. (Registration No. 333-36328) (referred to below as the Company's Form S-1 )

- 10.4 Investor Rights Agreement dated as of January 31, 2000, among KPMG LLP, Cisco Systems, Inc. and the Company, which is incorporated herein by reference to Exhibit 10.12 from the Company's Form S-1.
- 10.5 Irrevocable Waiver, dated May 17, 2004, by Cisco Systems, Inc. with respect to the Investor Rights Agreement, dated January 31, 2000 and the Stock Purchase Agreement, dated December 29, 1999, which is incorporated herein by reference to Exhibit 10.49 of the Company's Form S-1/A (Registration No. 333-100199).



Exhibit No.	Description
10.6	Credit Agreement dated as of May 18, 2007, as amended and restated on June 1, 2007, among the Company, BearingPoint, LLC, the guarantors party thereto, the lenders party thereto, UBS Securities LLC, Morgan Stanley Senior Funding, Inc., UBS AG, Stamford Branch and Wells Fargo Foothill, LLC.
10.7	Security Agreement dated as of May 18, 2007, among the Company, BearingPoint, LLC, the guarantors party thereto and UBS AG, Stamford Branch, as Collateral Agent.
10.8	Form of Term Note under the Credit Agreement dated as of May 18, 2007.
10.9	Form of 2.50% Series A Convertible Subordinated Debentures due 2024, which is incorporated by reference to Exhibit 10.66 from the Company's Form 10-K for the year ended December 31, 2004.
10.10	Form of 2.75% Series B Convertible Subordinated Debentures due 2024, which is incorporated by reference to Exhibit 10.67 from the Company's Form 10-K for the year ended December 31, 2004.
10.11	Purchase Agreement, dated as of December 16, 2004, among the Company and the Initial Purchasers named therein, which is incorporated by reference to Exhibit 10.68 from the Company's Form 10-K for the year ended December 31, 2004.
10.12	Indenture, dated as of December 22, 2004, by and between the Company and The Bank of New York, as trustee, which is incorporated by reference to Exhibit 99.1 from the Company's Form 8-K filed on March 10, 2006.
10.13	First Supplemental Indenture, dated as of November 7, 2006, between BearingPoint, Inc. and The Bank of New York, as trustee under the Indenture, dated as of December 22, 2004, which is incorporated by reference to Exhibit 99.1 from the Company's Form 8-K filed on November 8, 2006.
10.14	Resale Registration Rights Agreement, dated December 22, 2004, between the Company and the Initial Purchasers, which is incorporated by reference to Exhibit 10.70 from the Company's Form 10-K for the year ended December 31, 2004.
10.15	Form of 5.00% Convertible Senior Subordinated Debentures due 2025, which is incorporated by reference to Exhibit 10.71 from the Company's Form 10-K for the year ended December 31, 2004.
10.16	Form of Securities Purchase Agreement, dated April 21, 2005, among the Company and the purchasers named therein, which is incorporated by reference to Exhibit 10.72 from the Company's Form 10-K for the year ended December 31, 2004.
10.17	Indenture, dated as of April 27, 2005, by and between the Company and the Bank of New York, as trustee, which is incorporated by reference to Exhibit 99.1 from the Company's Form 8-K filed on March 10, 2006.
10.18	First Supplemental Indenture, dated as of November 2, 2006, between BearingPoint, Inc. and The Bank of New York, as trustee under the Indenture, dated as of April 27, 2005, providing for the

issuance of an aggregate principal amount of \$200,000,000 of 5.00% Convertible Senior Subordinated Debentures Due 2025, which is incorporated by reference to Exhibit 99.2 from the Company's Form 8-K filed on November 3, 2006.

- 10.19 Registration Rights Agreement, dated April 27, 2005, between the Company and the placement agents, which is incorporated by reference to Exhibit 10.74 from the Company's Form 10-K for the year ended December 31, 2004.

Exhibit No.	Description
10.20	Securities Purchase Agreement, dated July 15, 2005, among the Company and certain affiliates of Friedman Fleischer & Lowe, LLC, which is incorporated by reference to Exhibit 10.75 from the Company's Form 10-K for the year ended December 31, 2004.
10.21	Form of 0.50% Convertible Senior Subordinated Debentures due July 2010, which is incorporated by reference to Exhibit 10.76 from the Company's Form 10-K for the year ended December 31, 2004.
10.22	Form of Warrant Certificate, dated July 15, 2005, which is incorporated by reference to Exhibit 10.77 from the Company's Form 10-K for the year ended December 31, 2004.
10.23	Registration Rights Agreement, dated July 15, 2005, between the Company and Friedman Fleischer & Lowe, LLC, which is incorporated by reference to Exhibit 10.78 from the Company's Form 10-K for the year ended December 31, 2004.
10.24	Amended and Restated 2000 Long-Term Incentive Plan, effective as of February 2, 2007.
10.25	Employee Stock Purchase Plan, as amended and restated as of February 1, 2007.
10.26	Amended and Restated 401(k) Plan dated August 21, 2003, which is incorporated herein by reference to Exhibit 10.19 from the Company's Form 10-K for the year ended June 30, 2003.
10.27	Amendment No. 1 to Amended and Restated 401(k) Plan dated April 29, 2004, which is incorporated herein by reference to Exhibit 10.20 from the Company's Form S-1/A (Registration No. 333-100199).
10.28	Amendment No. 2 to Amended and Restated 401(k) Plan dated June 24, 2005, which is incorporated by reference to Exhibit 10.24 from the Company's Form 10-K for the year ended December 31, 2004.
10.29	Amendment No. 3 to Amended and Restated 401(k) Plan dated August 22, 2005, which is incorporated by reference to Exhibit 10.25 from the Company's Form 10-K for the year ended December 31, 2004.
10.30	Amendment No. 4 to Amended and Restated 401(k) Plan dated November 1, 2005, which is incorporated by reference to Exhibit 10.26 from the Company's Form 10-K for the year ended December 31, 2004.
10.31	Amendment No. 5 to Amended and Restated 401(k) Plan, effective as of September 14, 2006.
10.32	Amendment No. 6 to Amended and Restated 401(k) Plan, effective as of January 1, 2006.
10.33	Amendment No. 7 to Amended and Restated 401(k) Plan, effective as of May 1, 2007.
10.34	

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Deferred Compensation Plan, as amended and restated as of August 1, 2003, which is incorporated herein by reference to Exhibit 10.20 from the Company's Form 10-K for the year ended June 30, 2003.

- 10.35 Amendment to Deferred Compensation Plan effective as of December 31, 2004, which is incorporated by reference to Exhibit 10.28 from the Company's Form 10-K for the year ended December 31, 2004.
- 10.36 Amended and Restated BearingPoint, Inc. Managing Directors Deferred Compensation Plan dated January 1, 2006, which is incorporated by reference to Exhibit 10.30 from the Company's Form 10-K for the year ended December 31, 2004.
- 10.37 Form of Member Distribution Agreement for KPMG Consulting Qualified Employees, which is incorporated herein by reference to Exhibit 10.6 from the Company's Form S-1 (including for Richard Roberts).

<b>Exhibit No.</b>	<b>Description</b>
10.38	Form of Amendment to the Managing Director Agreement, dated as of January 31, 2005, between the Company and certain executive officers (including for Richard Roberts), which is incorporated by reference to Exhibit 10.8 from the Company's Form 10-K for the year ended December 31, 2004.
10.39	Form of Managing Director Agreement (including for Roderick C. McGeary).
10.40	Form of Managing Director Agreement.
10.41	Form of Special Termination Agreement (including for Richard Roberts), which is incorporated by reference to Exhibit 10.93 from the Company's Form 10-K for the year ended December 31, 2005.
10.42	Form of Restricted Stock Agreement with certain officers of the Company pursuant to the 2000 Long-Term Incentive Plan, which is incorporated herein by reference to Exhibit 10.5 from the Company's Form 10-Q for the quarter ended September 30, 2002.
10.43	Form of Restricted Stock Agreement with non-employee directors of the Company pursuant to the Amended and Restated Long-Term Incentive Plan, which is incorporated herein by reference to Exhibit 10.5 from the Company's Form 10-Q for the quarter ended December 31, 2002.
10.44	Form of Restricted Stock Unit agreement under the Company's 2000 Long-Term Incentive Plan for managing directors and employees, which is incorporated by reference to Exhibit 10.81 from the Company's Form 10-K for the year ended December 31, 2004.
10.45	Form of Performance Share Award Unit Agreement, which is incorporated by reference to Exhibit 99.1 from the Company's Form 8-K filed with the SEC on February 8, 2007.
10.46	Form of Performance Cash Award Agreement, which is incorporated by reference to Exhibit 99.2 from the Company's Form 8-K filed with the SEC on February 8, 2007.
10.47	Employment Letter, effective as of March 21, 2005, between the Company and Harry L. You, which is incorporated by reference to Exhibit 10.86 from the Company's Form 10-K for the year ended December 31, 2004.
10.48	Managing Director Agreement, dated as of March 21, 2005, between the Company and Harry L. You, which is incorporated by reference to Exhibit 10.87 from the Company's Form 10-K for the year ended December 31, 2004.
10.49	Restricted Stock Unit Agreement, dated March 21, 2005, between the Company and Harry L. You, which is incorporated by reference to Exhibit 10.88 from the Company's Form 10-K for the year ended December 31, 2004.
10.50	Special Termination Agreement, dated as of March 21, 2005, between the Company and Harry L. You, which is incorporated by reference to Exhibit 10.89 from the Company's Form 10-K for the year ended December 31, 2004.

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- 10.51 Stock Option Agreement, between the Company and Harry L. You, which is incorporated by reference to Exhibit 10.90 from the Company's Form 10-K for the year ended December 31, 2004.
- 10.52 Form of Restricted Stock Unit Agreement awarded to Harry You and Roderick C. McGeary, which is incorporated by reference to Exhibit 99.2 from the Company's Form 8-K filed with the SEC on February 13, 2007.
- 10.53 Employment Letter, effective as of July 1, 2005, between the Company and Judy A. Ethell, which is incorporated by reference to Exhibit 10.91 from the Company's Form 10-K for the year ended December 31, 2004.
- 10.54 Managing Director Agreement, dated as of July 1, 2005, between the Company and Judy A. Ethell.

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Exhibit No.	Description
10.55	Special Termination Agreement, dated as of July 1, 2005, between the Company and Judy A. Ethell, which is incorporated by reference to Exhibit 10.93 from the Company's Form 10-K for the year ended December 31, 2004.
10.56	Letter Agreement dated October 3, 2006, between the Company and Judy A. Ethell, which is incorporated by reference to Exhibit 10.95 from the Company's Form 10-K for the year ended December 31, 2005.
10.57	Restricted Stock Unit Agreement for 292,000 restricted stock units, dated September 19, 2006, between the Company and Judy A. Ethell, which is incorporated by reference to Exhibit 10.96 from the Company's Form 10-K for the year ended December 31, 2005.
10.58	Restricted Stock Unit Agreement for 94,000 restricted stock units, dated September 19, 2006, between the Company and Judy A. Ethell, which is incorporated by reference to Exhibit 10.97 from the Company's Form 10-K for the year ended December 31, 2005.
10.59	Employment Letter, effective as of February 24, 2006, between the Company and Laurent C. Lutz, which is incorporated by reference to Exhibit 10.91 from the Company's Form 10-K for the year ended December 31, 2005.
10.60	Managing Director Agreement, dated as of February 24, 2006, between the Company and Laurent C. Lutz, which is incorporated by reference to Exhibit 10.92 from the Company's Form 10-K for the year ended December 31, 2005.
10.61	Special Termination Agreement, dated as of February 24, 2006, between the Company and Laurent C. Lutz, which is incorporated by reference to Exhibit 10.94 from the Company's Form 10-K for the year ended December 31, 2005.
10.62	Employment Letter, effective as of January 8, 2007, between the Company and F. Edwin Harbach, which is incorporated by reference to Exhibit 99.2 from the Company's Form 8-K filed with the SEC on January 12, 2007.
10.63	Managing Director Agreement, dated as of January 8, 2007, between the Company and F. Edwin Harbach, which is incorporated by reference to Exhibit 99.3 from the Company's Form 8-K filed with the SEC on January 12, 2007.
10.64	Special Termination Agreement, dated as of January 8, 2007, between the Company and F. Edwin Harbach, which is incorporated by reference to Exhibit 99.4 from the Company's Form 8-K filed with the SEC on January 12, 2007.
10.65	Restricted Stock Unit Agreement, dated January 8, 2007, between the Company and F. Edwin Harbach, which is incorporated by reference to Exhibit 99.5 from the Company's Form 8-K filed with the SEC on January 12, 2007.
14.1	Standards of Business Conduct.

- 16.1 Letter dated June 28, 2007, from PricewaterhouseCoopers LLP to the Securities and Exchange Commission.
- 21.1 List of subsidiaries of the Registrant.
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a).
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a).
- 32.1 Certification of Chief Executive Officer pursuant to Section 1350.
- 32.2 Certification of Chief Financial Officer pursuant to Section 1350.



## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf on June 28, 2007 by the undersigned, thereunto duly authorized.

BEARINGPOINT, INC.

By: /s/ Harry L. You

**Name: Harry L. You**

**Title: Chief Executive Officer**

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on June 28, 2007 by the following persons on behalf of the Registrant and in the capacities indicated.

<b>Signature</b>	<b>Title</b>
/s/ Harry L. You <b>Harry L. You</b>	Director, and Chief Executive Officer (principal executive officer)
/s/ Judy A. Ethell <b>Judy A. Ethell</b>	Chief Financial Officer (principal financial and accounting officer)
/s/ Roderick C. McGeary <b>Roderick C. McGeary</b>	Chairman of the Board of Directors
/s/ Douglas C. Allred <b>Douglas C. Allred</b>	Director
/s/ Betsy J. Bernard <b>Betsy J. Bernard</b>	Director
/s/ Spencer C. Fleischer <b>Spencer C. Fleischer</b>	Director
/s/ Jill S. Kanin-Lovers <b>Jill S. Kanin-Lovers</b>	Director
/s/ Wolfgang Kemna	Director

**Wolfgang Kemna**

/s/ Albert L. Lord

Director

**Albert L. Lord**

/s/ J. Terry Strange

Director

**J. Terry Strange**

**ITEM 8: FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

**BEARINGPOINT, INC.**

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## **REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Stockholders of BearingPoint, Inc.:

We have completed integrated audits of BearingPoint, Inc.'s consolidated financial statements and of its internal control over financial reporting as of December 31, 2006, in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

### Consolidated financial statements

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of BearingPoint, Inc. and its subsidiaries (the Company) at December 31, 2006 and 2005, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 2 to the consolidated financial statements, the Company changed the manner in which it accounts for share-based compensation in 2006 and the manner in which it accounts for defined benefit pension and other postretirement plans effective December 31, 2006.

### Internal control over financial reporting

Also, we have audited management's assessment, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A, that BearingPoint, Inc. did not maintain effective internal control over financial reporting as of December 31, 2006, because (1) the Company did not maintain an effective control environment over financial reporting, (2) the Company did not maintain effective controls, including monitoring, over the financial close and reporting process, (3) the Company did not design and maintain effective controls over the completeness, accuracy, existence, valuation and disclosure of revenue, costs of service, accounts receivable, unbilled revenue, deferred contract costs, and deferred revenue, (4) the Company did not design and maintain effective controls over the completeness, accuracy, existence, valuation, and disclosure of the accounts payable, other current liabilities, other long-term liabilities and related expense accounts, (5) the Company did not design and maintain effective controls over the completeness and accuracy of costs related to expatriate compensation expense and related tax liabilities, (6) the Company did not design and maintain effective controls over the completeness, accuracy, valuation, and disclosure of payroll, employee benefit and other compensation liabilities and related expense accounts, (7) the Company did not design and maintain effective controls over the completeness, accuracy, existence, valuation and disclosure of property and equipment and related depreciation and amortization expense, (8) the Company did not design and maintain effective controls over the completeness, accuracy, valuation, and disclosure of prepaid lease and long-term lease obligation accounts and related amortization and lease rental expenses, and (9) the Company did not design and maintain effective controls over the completeness, accuracy, existence, valuation and presentation and disclosure of income tax payable, deferred income tax assets and liabilities, the related valuation allowance and

income tax expense, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and

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for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit of internal control over financial reporting 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. An audit of internal control over financial reporting includes 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 consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed 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 (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) 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 (iii) 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.

A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. The following material weaknesses have been identified and included in management's assessment as of December 31, 2006:

**1.** The Company did not maintain an effective control environment over financial reporting. Specifically, the Company identified the following material weaknesses:

The Company did not maintain a sufficient complement of personnel in foreign locations with an appropriate level of knowledge, experience and training in the application of generally accepted accounting principles in the United States of America ( GAAP ) and in internal control over financial reporting commensurate with financial reporting requirements.

The Company did not maintain and communicate sufficient formalized and consistent finance and accounting policies and procedures. The Company also did not maintain effective controls designed to prevent or detect instances of non-compliance with established policies and procedures specifically with respect to the application of accounting policies at foreign locations.

The Company did not enforce the consistent performance of manual controls designed to complement system controls over the North American financial accounting system. As a result, transactions and data were not completely and accurately recorded, processed and reported in the financial statements.

The Company did not maintain adequate controls to ensure that employees could report actual or perceived violations of policies and procedures. In addition, the Company did not have sufficient

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procedures to ensure the appropriate notification, investigation, resolution and remediation procedures were applied to reported violations.

The material weaknesses in the Company's control environment described above contributed to the existence of the material weaknesses discussed in items 2 through 9 below. Additionally, these material weaknesses could result in a misstatement to substantially all of the Company's financial statement accounts and disclosures that would result in a material misstatement to the annual or interim consolidated financial statements that would not be prevented or detected.

**2.** The Company did not maintain effective controls, including monitoring, over the financial close and reporting process. Specifically, the Company identified the following material weaknesses in the financial close and reporting process:

The Company did not maintain formal, written policies and procedures governing the financial close and reporting process.

The Company did not maintain effective controls to ensure that management oversight and review procedures were properly performed over the accounts and disclosures in the financial statements. In addition, the Company did not maintain effective controls to ensure adequate management reporting information was available to monitor financial statement accounts and disclosures.

The Company did not maintain effective controls over the recording of recurring and non-recurring journal entries. Specifically, effective controls were not designed and in place to provide reasonable assurance that journal entries were prepared with sufficient supporting documentation and reviewed and approved to ensure the completeness and accuracy of the entries recorded.

The Company did not maintain effective controls to provide reasonable assurance that accounts were complete and accurate and agreed to detailed support and that reconciliations of accounts were properly performed, reviewed and approved.

The Company did not maintain effective controls to provide reasonable assurance that foreign currency translation amounts resulting from intercompany loans were accurately recorded and reported in the consolidated financial statements.

These material weaknesses contributed to the material weaknesses identified in items 3 through 9 below and resulted in adjustments to the Company's consolidated financial statements for the year ended December 31, 2006. Additionally, these material weaknesses could result in a misstatement to substantially all of the Company's financial statement accounts and disclosures that would result in a material misstatement of the Company's annual or interim consolidated financial statements that would not be prevented or detected.

**3.** The Company did not design and maintain effective controls over the completeness, accuracy, existence, valuation and disclosure of revenue, costs of service, accounts receivable, unbilled revenue, deferred contract costs, and deferred revenue. Specifically, the Company identified the following material weaknesses:

The Company did not design and maintain effective controls to provide reasonable assurance over the initiation, recording, processing, and reporting of customer contracts, including the existence of and adherence to policies and procedures, adequate segregation of duties and adequate monitoring by management.



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The Company did not design and maintain effective controls to provide reasonable assurance that contract costs, such as engagement subcontractor costs, were completely and accurately accumulated.

The Company did not design and maintain effective controls to provide reasonable assurance that the Company adequately evaluated customer contracts to identify and provide reasonable assurance regarding the proper application of the appropriate method of revenue recognition in accordance with GAAP.

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The Company did not design and maintain effective controls to provide reasonable assurance regarding the completeness of information recorded in the financial accounting system. Specifically, the Company did not design and have in place effective controls to provide reasonable assurance that invoices issued outside of the financial accounting system were appropriately recorded in the general ledger. As a result, the Company did not ensure that cash received was applied to the correct accounts in the appropriate accounting period.

**4.** The Company did not design and maintain effective controls over the completeness, accuracy, existence, valuation, and disclosure of accounts payable, other current liabilities, other long-term liabilities and related expense accounts. Specifically, the Company did not design and maintain effective controls over the initiation, authorization, processing, recording, and reporting of purchase orders and invoices as well as authorizations for cash disbursement to provide reasonable assurance that liability balances and operating expenses were accurately recorded in the appropriate accounting period and to prevent or detect misappropriation of assets. In addition, the Company did not have effective controls to: i) provide reasonable assurance regarding the complete identification of subcontractors used in performing services to customers; or ii) monitor subcontractor activities and accumulation of subcontractor invoices to provide reasonable assurance regarding the complete and accurate recording of contract-related subcontractor costs.

**5.** The Company did not design and maintain effective controls over the completeness and accuracy of costs related to expatriate compensation expense and related tax liabilities. Specifically, the Company did not maintain effective controls to identify and monitor employees working away from their home country for extended periods of time. In addition, the Company did not maintain effective controls to completely and properly calculate the related compensation expense and employee income tax liability attributable to each tax jurisdiction.

**6.** The Company did not design and maintain effective controls over the completeness, accuracy, valuation, and disclosure of payroll, employee benefit and other compensation liabilities and related expense accounts. Specifically, the Company did not have effective controls designed and in place to provide reasonable assurance of the authorization, initiation, recording, processing, and reporting of employee-related costs including bonus, health and welfare, severance, compensation expense, and stock-based compensation amounts in the accounting records. Additionally, the Company did not design and maintain effective controls over the administration of employee data or controls to provide reasonable assurance regarding the proper authorization of non-recurring payroll changes.

**7.** The Company did not design and maintain effective controls over the completeness, accuracy, existence, valuation and disclosure of property and equipment and related depreciation and amortization expense. Specifically, the Company did not design and maintain effective controls to provide reasonable assurance that asset additions and disposals were completely and accurately recorded; depreciation and amortization expense was accurately recorded based on appropriate useful lives assigned to the related assets; existence of assets was confirmed through periodic inventories; and the identification and determination of impairment losses was performed in accordance with GAAP. In addition, the Company did not design and maintain effective controls to provide reasonable assurance of the adherence to the capitalization policy, and the Company did not design and maintain effective controls to provide reasonable assurance that expenses for internally developed software were completely and accurately capitalized, amortized, and adjusted for impairment in accordance with GAAP.

**8.** The Company did not design and maintain effective controls over the completeness, accuracy, valuation, and disclosure of prepaid lease and long-term lease obligation accounts and related amortization and lease rental expenses. Specifically, the Company did not design and maintain effective controls to provide reasonable assurance that new, amended, and terminated leases, and the related assets, liabilities and expenses, including those associated with rent holidays, escalation clauses, landlord/tenant incentives and asset retirement obligations, were reviewed, approved, and accounted for in accordance with GAAP.



9. The Company did not design and maintain effective controls over the completeness, accuracy, existence, valuation and presentation and disclosure of income tax payable, deferred income tax assets and liabilities, the related valuation allowance and income tax expense. Specifically, the Company identified the following material weaknesses:

The Company did not design and maintain effective controls over the accuracy and completeness of the components of income tax provision calculations and related reconciliation of income tax payable and of differences between the tax and financial reporting basis of assets and liabilities with deferred income tax assets and liabilities. The Company also did not maintain effective controls to identify and determine permanent differences between income for tax and financial reporting income purposes.

The Company did not maintain effective controls, including monitoring, over the calculation and recording of foreign income taxes, including tax reserves, acquired tax contingencies associated with business combinations and the income tax impact of foreign debt recapitalization. In addition, the Company did not maintain effective controls over determining the correct foreign jurisdictions or tax treatment of certain foreign subsidiaries for United States tax purposes.

The Company did not design and maintain effective controls over withholding taxes associated with interest payable on intercompany loans and intercompany trade payables between various tax jurisdictions.

Each of the control deficiencies discussed in items 3 through 9 above resulted in adjustments to the Company's consolidated financial statements for the year ended December 31, 2006. Additionally, these control deficiencies could result in misstatements of the aforementioned financial statement accounts and disclosures that would result in a material misstatement of the Company's annual or interim consolidated financial statements that would not be prevented or detected. Accordingly, management has determined that each of the control deficiencies in items 3 through 9 above constitutes a material weakness. These material weaknesses were considered in determining the nature, timing, and extent of audit tests applied in our audit of the 2006 consolidated financial statements, and our opinion regarding the effectiveness of the Company's internal control over financial reporting does not affect our opinion on those consolidated financial statements.

In our opinion, management's assessment that BearingPoint, Inc. did not maintain effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on criteria established in *Internal Control - Integrated Framework* issued by the COSO. Also, in our opinion, because of the effects of the material weaknesses described above on the achievement of the objectives of the control criteria, BearingPoint, Inc. has not maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control - Integrated Framework* issued by the COSO.

PricewaterhouseCoopers LLP  
Boston, Massachusetts  
June 27, 2007

**BEARINGPOINT, INC.****CONSOLIDATED BALANCE SHEETS****(in thousands, except share amounts)**

	<b>December 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 389,571	\$ 255,340
Restricted cash (note 2)	3,097	121,247
Accounts receivable, net of allowance for doubtful accounts of \$5,927 at December 31, 2006 and \$9,326 at December 31, 2005	361,638	432,415
Unbilled revenue	341,357	355,137
Income tax receivable	1,414	10,867
Deferred income taxes	7,621	18,991
Prepaid expenses	33,677	35,875
Other current assets	65,611	40,345
<b>Total current assets</b>	<b>1,203,986</b>	<b>1,270,217</b>
Property and equipment, net	146,392	170,133
Goodwill	463,446	427,688
Other intangible assets, net		1,545
Deferred income taxes, less current portion	41,663	20,915
Other assets	83,753	81,928
<b>Total assets</b>	<b>\$ 1,939,240</b>	<b>\$ 1,972,426</b>
<b>LIABILITIES AND STOCKHOLDERS DEFICIT</b>		
Current liabilities:		
Current portion of notes payable	\$ 360	\$ 6,393
Accounts payable	295,109	286,273
Accrued payroll and employee benefits	344,715	309,510
Deferred revenue	131,313	166,647
Income tax payable	33,324	41,839
Current portion of accrued lease and facilities charges	17,126	12,515
Deferred income taxes	20,109	10,095
Accrued legal settlements	59,718	38,601
Other current liabilities	135,837	169,624
<b>Total current liabilities</b>	<b>1,037,611</b>	<b>1,041,497</b>
Notes payable, less current portion	671,490	668,367
Accrued employee benefits	116,087	92,338
Accrued lease and facilities charges, less current portion	49,792	38,082
Deferred income taxes, less current portion	7,984	22,876
Income tax reserve	108,499	89,530

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Other liabilities	125,078	65,308
Total liabilities	2,116,541	2,017,998
Commitments and contingencies (notes 9, 10, 11)		
Stockholders' deficit:		
Preferred stock, \$.01 par value 10,000,000 shares authorized		
Common stock, \$.01 par value 1,000,000,000 shares authorized, 205,406,249 shares issued and 201,593,999 shares outstanding on December 31, 2006 and 205,350,249 shares issued and 201,537,999 shares outstanding on December 31, 2005	2,044	2,044
Additional paid-in capital	1,315,190	1,261,797
Accumulated deficit	(1,697,639)	(1,484,199)
Notes receivable from stockholders	(7,466)	(7,578)
Accumulated other comprehensive income	246,297	218,091
Treasury stock, at cost (3,812,250 shares)	(35,727)	(35,727)
Total stockholders' deficit	(177,301)	(45,572)
Total liabilities and stockholders' deficit	\$ 1,939,240	\$ 1,972,426

The accompanying notes are an integral part of these Consolidated Financial Statements.

**BEARINGPOINT, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(in thousands, except share and per share amounts)**

	<b>Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Revenue	\$ 3,444,003	\$ 3,388,900	\$ 3,375,782
Costs of service:			
Professional compensation	1,716,632	1,770,405	1,532,423
Other direct contract expenses	896,999	972,787	991,493
Lease and facilities restructuring charges	29,621	29,581	11,699
Other costs of service	250,225	258,135	292,643
Total costs of service	2,893,477	3,030,908	2,828,258
Gross profit	550,526	357,992	547,524
Amortization of purchased intangible assets	1,545	2,266	3,457
Goodwill impairment charge		166,415	397,065
Selling, general and administrative expenses	748,250	750,867	641,176
Operating loss	(199,269)	(561,556)	(494,174)
Interest income	8,749	9,049	1,441
Interest expense	(37,182)	(33,385)	(18,710)
Loss on early extinguishment of debt			(22,617)
Insurance settlement	38,000		
Other income (expense), net	8,659	(13,630)	(375)
Loss before taxes	(181,043)	(599,522)	(534,435)
Income tax expense	32,397	122,121	11,791
Net loss	\$ (213,440)	\$ (721,643)	\$ (546,226)
Loss per share basic and diluted:			
Net loss	\$ (1.01)	\$ (3.59)	\$ (2.77)
Weighted average shares basic and diluted	212,154,618	201,020,274	197,039,303

The accompanying notes are an integral part of these Consolidated Financial Statements.

**BEARINGPOINT, INC.**

**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (DEFICIT)**  
(in thousands)

	Common Stock		Additional paid-in capital	Accumulated deficit	Notes receivable from stockholders	Accumulated other comprehensive income (loss)	Treasury Stock		Comprehensive loss
	Shares issued	Amount					Shares	Amount	
2003	198,295	\$ 1,973	\$ 1,105,631	\$ (216,330)	\$ (9,114)	\$ 223,562	(3,812)	\$ (35,727)	
Stock									
Incentive									
ing tax									
0	284	3	2,416						
on									
ck									
benefit									
	3,642	36	26,309						
ble									
holders,									
in									
loan					1,059				
ck									
rd of									
	56	1	452						
ck, net									
of \$135			563						
stock									
to									
volving									
business									
t of tax									
	861	9	7,688						
ures	(5)								
e									



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				(546,226)				\$ (546,226)
et of							(616)	(616)
cy ustment						63,009		63,009
ensive								\$ (483,833)
<b>2004</b> ck	203,133	2,022	1,143,059	(762,556)	(8,055)	285,955	(3,812)	(35,727)
centive g tax	164	1	1,200					
on								
ck								
benefit	2,053	21	14,269					
le ders, n								
loan					477			
stock cted nd k units eu of related			82,346					
ersen ulting			(4,929)					
stock to volving iness			3,491					
version g to the ior			14,288					
he July s e loss:			8,073					

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				(721,643)					\$ (721,643)
tion									
						(13,321)			(13,321)
cy									
ustment						(54,543)			(54,543)
ensive									\$ (789,507)
<b>2005</b>	205,350	2,044	1,261,797	(1,484,199)	(7,578)	218,091	(3,812)	(35,727)	

The accompanying notes are an integral part of these Consolidated Financial Statements.

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**BEARINGPOINT, INC.**

**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (DEFICIT) (Continued)**  
**(in thousands)**

Common Stock Shares issued	Amount	Additional paid-in capital	Accumulated deficit	Notes receivable from stockholders	Accumulated other comprehensive income (loss)	Treasury Stock		Comprehensive loss
						Shares	Amount	
205,350	\$ 2,044	\$ 1,261,797	\$ (1,484,199)	\$ (7,578)	\$ 218,091	(3,812)	\$ (35,727)	\$
56		460						
		52,933						
					(11,417)			
			(213,440)					\$ (213,440)
					8,880			8,880
					30,743			30,743
								\$ (173,817)

nsive

t  
31,

205,406	\$ 2,044	\$ 1,315,190	\$ (1,697,639)	\$ (7,466)	\$ 246,297	(3,812)	\$ (35,727)	\$
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The accompanying notes are an integral part of these Consolidated Financial Statements.

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## BEARINGPOINT, INC.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)

	<b>Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Cash flows from operating activities:</b>			
Net loss	\$ (213,440)	\$ (721,643)	\$ (546,226)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Deferred income taxes	(13,406)	49,211	39,332
Provision (benefit) for doubtful accounts	(464)	5,334	(1,057)
Stock-based compensation	53,393	85,837	9,874
Impairment of goodwill		166,415	397,065
Depreciation and amortization of property and equipment	74,023	70,544	78,690
Amortization of purchased intangible assets	1,545	2,266	3,457
Lease and facilities restructuring charges	29,621	29,581	11,699
Amortization of debt issuance costs and debt accretion	8,936	12,396	2,106
Other	(4,780)	11,597	5,389
Changes in assets and liabilities:			
Accounts receivable	84,124	(52,196)	(33,180)
Unbilled revenue	19,814	20,492	(62,323)
Income tax receivable, prepaid expenses and other current assets	(23,702)	26,318	(38,581)
Other assets	(5,710)	(10,025)	(51,975)
Accounts payable, accrued legal settlements and other current liabilities	(14,249)	58,127	20,006
Accrued payroll and employee benefits	23,311	47,018	47,574
Deferred revenue	(38,605)	62,788	101,403
Income tax reserve and other liabilities	78,269	22,869	65,012
Net cash provided by (used in) operating activities	58,680	(113,071)	48,265
<b>Cash flows from investing activities:</b>			
Purchases of property and equipment	(50,581)	(40,849)	(88,334)
Decrease (increase) in restricted cash	118,151	(100,194)	(21,053)
Net cash provided by (used in) investing activities	67,570	(141,043)	(109,387)
<b>Cash flows from financing activities:</b>			
Proceeds from issuance of common stock		14,896	26,904
Proceeds from issuance of notes payable		282,156	1,531,849
Repayments of notes payable	(6,506)	(16,985)	(1,360,288)
Decrease in book overdrafts	(810)	(980)	(22,986)
Payments made in lieu of stock issuance		(4,929)	
(Increase) decrease in notes receivable from stockholders		(6)	1,059

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Net cash provided by (used in) financing activities	(7,316)	274,152	176,538
Effect of exchange rate changes on cash and cash equivalents	15,297	(9,508)	6,919
Net increase in cash and cash equivalents	134,231	10,530	122,335
Cash and cash equivalents beginning of period	255,340	244,810	122,475
Cash and cash equivalents end of period	\$ 389,571	\$ 255,340	\$ 244,810
Supplementary cash flow information:			
Interest paid	\$ 27,582	\$ 17,547	\$ 20,480
Taxes paid, net of refunds	\$ 21,333	\$ (41,741)	\$ 21,397
Supplemental non-cash investing and financing activities:			
Beneficial conversion feature related to the July 2005 Debentures	\$	\$ 14,288	\$
Fair value of July 2005 Warrants	\$	\$ 8,073	\$

The accompanying notes are an integral part of these Consolidated Financial Statements.

**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(in thousands, except share and per share amounts)**

**1. Description of the Business, Liquidity and Basis of Presentation**

*The Company*

BearingPoint, Inc. (the Company) is one of the world's largest management and technology consulting companies, with approximately 17,500 employees at December 31, 2006. The Company provides strategic consulting applications services, technology solutions and managed services to government organizations, Global 2000 companies and medium-sized businesses in the United States and internationally. The Company's services and focused solutions include implementing enterprise systems and business processes, improving supply chain efficiency, performing systems integration due to mergers and acquisitions, and designing and implementing customer management solutions. The Company's service offerings, which involve assisting its clients to capitalize on alternative business and systems strategies in the management and support of key information technology (IT) functions, are designed to help its clients generate revenue, increase cost-effectiveness, implement mergers and acquisitions strategies, manage regulatory compliance, and integrate information and transition clients to next-generation technology.

In North America, the Company provides consulting services through its Public Services, Commercial Services and Financial Services industry groups in which it focuses significant industry-specific knowledge and service offerings to its clients. Outside of North America, the Company is organized on a geographic basis, with operations in Europe, the Middle East and Africa (EMEA), Asia Pacific and Latin America.

*Liquidity*

The Consolidated Financial Statements of the Company are prepared on a going concern basis, which assumes that the Company will continue its operations for the foreseeable future and will realize its assets and discharge its liabilities in the ordinary course of business. The Company has recently experienced a number of factors that have negatively impacted its liquidity, including the following:

The Company has experienced significant recurring net losses. At December 31, 2006, the Company had an accumulated deficit of \$1,697,639 and a total stockholders' deficit of \$177,301.

The Company's business has not generated positive cash from operating activities in certain quarters during 2006, 2005 and 2004.

Due to the material weaknesses in its internal controls, the Company continues to experience significant delays in completing its consolidated financial statements and filing periodic reports with the U.S. Securities and Exchange Commission (the SEC) on a timely basis. Accordingly, the Company continues to devote substantial additional internal and external resources, and experience higher than expected fees for audit services.

Through December 31, 2006, the Company incurred cumulative losses of \$139,882 under a significant contract and a final settlement in 2007 with Hawaiian Telcom Communications, Inc. (HT), which consequently resulted in significantly less cash from operating activities in 2006 and, management believes, 2007.

The Company currently is a party to a number of disputes that involve or may involve litigation or other legal or regulatory proceedings. See Note 11, Commitments and Contingencies.

During 2006 and into 2007, the Company engaged in a number of activities intended to further improve its cash balances and their accessibility. The Company's continued focus during 2006 on reducing DSOs and





**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

improving profitability has improved cash flows from operations. In addition, as discussed in Note 6, Notes Payable, during May 2007, the Company entered into the 2007 Credit Facility, which includes term loans in the aggregate principal amount of \$250,000. In June 2007, the 2007 Credit Facility was amended to, among other things, increase the aggregate principal amount under the term loans by \$50,000. All term loans have been drawn down. Management believes the terms of these term loans have been structured to eliminate the risk of any event of default occurring with respect to the production of financial statements or SEC periodic reports prior to October 2008.

Based on the foregoing and its current state of knowledge of the outlook for its business, the Company currently believes that cash provided from operations, existing cash balances and borrowings under its 2007 Credit Facility will be sufficient to meet its working capital needs through the end of 2007. The Company's management may seek alternative strategies, intended to further improve the Company's cash balances and their accessibility, if current estimates for cash uses for 2007 prove incorrect. These activities include: initiating further cost reduction efforts, seeking improvements in working capital management, reducing or delaying capital expenditures, seeking additional debt or equity capital and selling assets. However, actual results may differ from current expectations for many reasons, including losses of business that could result from the Company's continuing failure to timely file periodic reports with the SEC, the occurrence of any event of default that could provide the Company's lenders with a right of acceleration (e.g., non-payment), possible delisting from the New York Stock Exchange, further downgrades of its credit ratings or unexpected demands on its current cash resources (e.g., to settle lawsuits).

**2. Summary of Significant Accounting Policies**

*Principles of Consolidation*

The Consolidated Financial Statements reflect the operations of the Company and all of its majority-owned subsidiaries. Upon consolidation, all significant intercompany accounts and transactions are eliminated. Certain of the Company's consolidated foreign subsidiaries reported their results on a one-month reporting lag, which allowed additional time to compile results. During 2004, the Company recorded a change in accounting principle resulting from certain Asia Pacific and EMEA regions which changed to reporting on a current period basis. The purpose of the change is to have certain foreign subsidiaries report on a basis that is consistent with the Company's fiscal reporting period. As a result, net loss for the year ended December 31, 2004 includes a cumulative effect of a change in accounting principle of \$529, which represents the December 2003 loss for these entities. This amount is included in other income (expense), net, in the Consolidated Statement of Operations for the year ended December 31, 2004 due to the immateriality of the effect of the change in accounting principle to consolidated net loss. In addition, during the fourth quarter of 2006, the one-month reporting lag in the remaining EMEA entities was eliminated. The elimination of one month of activity increased the Company's 2006 consolidated net loss for the year ended December 31, 2006 by \$1,164.

*Use of Estimates*

The preparation of Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States requires that management make estimates, assumptions and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenue and expenses during the reporting period. Management's estimates, assumptions and judgments are derived and continually evaluated based on available information, historical experience and various other assumptions that are believed to be reasonable



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under the circumstances. Because the use of estimates is inherent in the financial reporting process, actual results could differ from those estimates.

*Reclassifications*

Certain amounts reported in previous years have been reclassified to conform to the current period presentation.

*Revenue Recognition*

The Company earns revenue from three primary sources: (1) technology integration services where it designs, builds and implements new or enhanced system applications and related processes, (2) services to provide general business consulting, such as system selection or assessment, feasibility studies, business valuations and corporate strategy services, and (3) managed services in which it manages, staffs, maintains, hosts or otherwise runs solutions and systems provided to its customers. Contracts for these services have different terms based on the scope, deliverables and complexity of the engagement, which require management to make judgments and estimates in recognizing revenue. Fees for these contracts may be in the form of time-and-materials, cost-plus or fixed price.

Technology integration services represent a significant portion of the Company's business and are generally accounted for under the percentage-of-completion method in accordance with Statement of Position ( SOP ) 81-1, Accounting for Performance of Construction-Type and Certain Production-Type Contracts ( SOP 81-1 ). Under the percentage-of-completion method, management estimates the percentage of completion based upon costs to the client incurred as a percentage of the total estimated costs to the client. When total cost estimates exceed revenue, the Company accrues for the estimated losses immediately. The use of the percentage-of-completion method requires significant judgment relative to estimating total contract revenue and costs, including assumptions relative to the length of time to complete the project, the nature and complexity of the work to be performed, and anticipated changes in estimated salaries and other costs. Incentives and award payments are included in estimated revenue using the percentage-of-completion method when the realization of such amounts are deemed probable upon achievement of certain defined goals. Estimates of total contract revenue and costs are continuously monitored during the term of the contract and are subject to revision as the contract progresses. When revisions in estimated contract revenue and costs are determined, such adjustments are recorded in the period in which they are first identified.

Revenue for general business consulting services is recognized as work is performed and amounts are earned in accordance with Staff Accounting Bulletin ( SAB ) No. 101, Revenue Recognition in Financial Statements, as amended by SAB No. 104, Revenue Recognition ( SAB 104 ). The Company considers amounts to be earned once evidence of an arrangement has been obtained, services are delivered, fees are fixed or determinable, and collectibility is reasonably assured. For contracts with fees based on time-and-materials or cost-plus, the Company recognizes revenue over the period of performance. Depending on the specific contractual provisions and nature of the deliverable, revenue may be recognized on a proportional performance model based on level of effort, as milestones are achieved or when final deliverables have been provided.

For managed service arrangements, the Company typically implements or builds system applications for customers that it then manages or runs for periods that may span several years. Such arrangements include the delivery of a combination of one or more of the Company's service offerings and are governed by Emerging

**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
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Issues Task Force Issue ( EITF ) 00-21, Accounting for Revenue Arrangements with Multiple Deliverables . In managed service arrangements in which the system application implementation or build has standalone value to the customer, and management has evidence of fair value for the managed or run services, the Company bifurcates the total arrangement into two units of accounting: (i) the system application implementation or build which is recognized as technology integration services using the percentage-of-completion method under SOP 81-1, and (ii) the managed or run services, which are recognized under SAB 104 ratably over the estimated life of the customer relationship. In instances where the Company is unable to bifurcate a managed service arrangement into separate units of accounting, the total contract is recognized as one unit of accounting under SAB 104. In such instances, total fees and costs related to the system application implementation or build are deferred and recognized together with managed or run services upon completion of the software application implementation or build ratably over the estimated life of the customer relationship. Certain managed service arrangements may also include transaction-based services in addition to the system application implementation or build and managed services. Fees from transaction-based services are recognized as earned if the Company has evidence of fair value for such transactions; otherwise, transaction fees are spread ratably over the remaining life of the customer relationship period as received. The determination of fair value requires the Company to use significant judgment. Management determines the fair value of service revenue based upon the Company's recent pricing for those services when sold separately and/or prevailing market rates for similar services.

Revenue includes reimbursements of travel and out-of-pocket expenses with equivalent amounts of expense recorded in other direct contract expenses. In addition, the Company generally enters into relationships with subcontractors where it maintains a principal relationship with the customer. In such instances, subcontractor costs are included in revenue with offsetting expenses recorded in other direct contract expenses.

Unbilled revenue consists of recognized recoverable costs and accrued profits on contracts for which billings had not been presented to clients as of the balance sheet date. Management anticipates that the collection of these amounts will occur within one year of the balance sheet date. Billings in excess of revenue recognized for which payments have been received are recorded as deferred revenue until the applicable revenue recognition criteria have been met.

*Costs of Service*

Costs of service include professional compensation and other direct contract expenses, as well as costs attributable to the support of client service professional staff, depreciation and amortization costs related to assets used in revenue-generating activities, bad debt expense relating to accounts receivable, and other costs attributable to serving the Company's client base. Professional compensation consists of payroll costs and related benefits associated with client service professional staff including, stock compensation, tax equalization for employees on foreign and long-term domestic assignments and reductions in workforce. Other direct contract expenses include costs directly attributable to client engagements, such as out-of-pocket costs including travel and subsistence for client service professional staff, costs of hardware and software and costs of subcontractors. Lease and facilities restructuring charges represent the fair value of future lease obligations (net of estimated sublease income), the unamortized cost of fixed assets and other incurred costs associated with the Company's office space reduction efforts. Recurring lease and facilities charges for occupied offices are included in other costs of service.

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*Selling, General and Administrative Expenses*

Selling, general and administrative expenses include expenses related to marketing, information systems, depreciation and amortization, finance and accounting, human resources, sales force and other functions related to managing and growing the Company's business. Advertising costs are expensed when advertisements are first placed or run. Advertising expense was \$21,304, \$20,681 and \$18,709 for the years ended December 31, 2006, 2005 and 2004, respectively.

*Cash, Cash Equivalents and Restricted Cash*

Cash and cash equivalents consist of all cash balances, demand deposits and highly liquid investments with insignificant interest rate risks and original maturity of three months or less. The Company's cash equivalents consisted of money market investments of \$190,409 and \$62,745 at December 31, 2006 and 2005, respectively. Book overdrafts representing outstanding checks in excess of funds on deposit are classified as short-term borrowings and included in other current liabilities on the Consolidated Balance Sheets. As of December 31, 2006 and 2005, cash and cash equivalents included approximately \$21,240 and \$18,000, respectively, of employee contributions to the Employee Stock Purchase Plan (the ESPP) held by the Company, which are payable on demand. As of December 31, 2006 and 2005, the Company classified as restricted cash approximately \$3,097 and \$121,247, respectively, of cash collateral posted to secure reimbursement obligations under letters of credit and surety bonds predominantly related to the Company's previously existing 2005 revolving credit facility.

*Concentrations of Credit Risk and Fair Value of Financial Instruments*

The amounts reflected in the Consolidated Balance Sheets for cash and cash equivalents, accounts receivable and accounts payable approximate their fair value due to their short-term maturities. At December 31, 2006 and 2005, the fair value of the Company's notes payable, including the current portion, was \$776,241 and \$738,092, respectively, compared to their respective carrying values of \$671,850 and \$674,760. Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of notes payable, trade receivables, and unbilled revenue. The Company's cash and cash equivalents are placed with financial institutions with high credit standings. The Company's customer base consists of large numbers of geographically diverse customers dispersed across many countries. Concentration of credit risk with respect to trade accounts receivables is not significant.

U.S. Federal government revenue, inclusive of government sponsored enterprises, accounted for 28.5%, 28.9%, and 29.7%, of the Company's revenue for the years ended December 31, 2006, 2005 and 2004, respectively. At December 31, 2006 and 2005, receivables due from the U.S. Federal government were \$64,605 and \$107,314, respectively. Unbilled revenue due from the U.S. Federal government was \$123,791 and \$129,480 at December 31, 2006 and 2005, respectively. While most of the Company's government agency clients have the ability to unilaterally terminate their contracts, the Company's relationships are generally not with political appointees, and the Company has not historically experienced a loss of Federal government projects with a change in administration.

*Valuation of Accounts Receivable*

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. Assessing the collectibility of customer receivables requires management judgment. The Company determines its allowance for doubtful accounts by specifically analyzing

**BEARINGPOINT, INC.**

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individual accounts receivable, historical bad debts, customer concentrations, customer credit-worthiness, current economic and accounts receivable aging trends, and changes in customer payment terms. Valuation reserves are periodically re-evaluated and adjusted as more information about the ultimate collectibility of accounts receivable becomes available.

*Property and Equipment*

Property and equipment are recorded at cost, less allowances for depreciation and amortization. The cost of software purchased or developed for internal use is capitalized in accordance with SOP 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use. Depreciation is provided for all classes of assets for financial statement purposes using the straight-line method over the estimated useful lives of the assets. Equipment is depreciated over three to five years, software purchased or developed for internal use is depreciated over one to five years, and furniture is depreciated over three to ten years. Leasehold improvements are amortized over the shorter of their useful lives or the remaining term of the respective lease. Maintenance and repairs are charged to expense as incurred. When assets are sold or retired, the asset cost and related accumulated depreciation are relieved from the Consolidated Balance Sheets, and any associated gain or loss is recognized in income from operations.

*Accounting for Leases*

The Company leases all of its office facilities under non-cancelable operating leases that expire at various dates through 2017, along with options that permit renewals for additional periods. Rent abatements and escalations are considered in the determination of straight-line rent expense for operating leases. The Company receives incentives to lease office facilities in certain areas. These incentives are recorded as a deferred credit and recognized as a reduction to rent expense on a straight-line basis over the lease term.

*Asset Retirement Obligations*

The Company leases all of its office facilities under various operating leases, some of which contain clauses that require the Company to restore the leased facility to its original state at the end of the lease term. In accordance with Statement of Financial Accounting Standards ( SFAS ) No. 143, Accounting for Asset Retirement Obligations , these asset retirement obligations are initially measured at fair value and recorded as a liability, and a corresponding increase is recorded in the carrying amount of the underlying property. At December 31, 2006 and 2005, asset retirement obligations were \$2,636 and \$3,674, respectively.

*Goodwill and Other Intangible Assets*

Goodwill is the amount by which the cost of acquired net assets in a business acquisition exceeded the fair value of net identifiable assets on the date of purchase. The Company assesses goodwill for impairment on at least an annual basis on April 1 and whenever events or changes in circumstances indicate that the carrying value of the asset may not be recoverable.

An impairment review of the carrying amount of goodwill is also conducted if events or changes in circumstances indicate that goodwill might be impaired. The Company considers the following to be important factors that could trigger an impairment review: significant underperformance relative to historical or projected future operating results; identification of other impaired assets within a reporting unit; the more-likely-than not expectation that a reporting unit or a significant portion of a reporting unit will be sold;

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significant adverse changes in business climate or regulations; significant changes in senior management; significant changes in the manner of use of the acquired assets or the strategy for the Company's overall business; significant negative industry or economic trends; a significant decline in the Company's stock price for a sustained period or a significant unforeseen decline in the Company's credit rating. In testing goodwill for impairment, the Company aggregates its reporting units with similar economic characteristics as one reporting unit. The resulting reporting units are consistent with the Company's reportable segments as identified in Note 18, Segment Information. To conduct a goodwill impairment test, the fair value of the reporting unit is first compared to its carrying value. If the reporting unit's allocated carrying value exceeds its fair value, the Company undertakes a second evaluation to assess the required impairment loss to the extent that the carrying value of goodwill exceeds its implied fair value. Management estimates the fair value of its reporting units using a combination of the discounted cash flow valuation model and comparable market transaction models.

Other identifiable intangible assets include finite-lived purchased intangible assets, which primarily consist of market rights, order backlog, customer contracts and related customer relationships and trade names. Finite-lived purchased intangible assets are amortized using the straight-line method over their expected period of benefit, which generally ranges from one to five years.

*Valuation of Long-Lived Assets*

Long-lived assets primarily include property and equipment and intangible assets with finite lives (purchased software, capitalized software, and customer lists). In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the Company periodically reviews long-lived assets for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable or that the useful lives are no longer appropriate. Each impairment test is based on a comparison of the undiscounted cash flows to the recorded value of the asset. If an impairment is indicated, the asset is written down to its estimated fair value based on a discounted cash flow analysis. Determining the fair value of long-lived assets includes significant judgment by management, and different judgments could yield different results.

*Foreign Currency*

Assets and liabilities of consolidated foreign subsidiaries, whose functional currency is the local currency, are translated to U.S. dollars at period end exchange rates. Revenue and expense items are translated to U.S. dollars at the average rates of exchange prevailing during the period. The adjustment resulting from translating the financial statements of such foreign subsidiaries to U.S. dollars is reflected as a cumulative translation adjustment and reported as a component of accumulated other comprehensive income in Consolidated Statements of Changes in Stockholders Equity (Deficit). Foreign currency transaction gains and losses related to short-term intercompany loans are recorded in the Consolidated Statements of Operations as incurred. Intercompany loans that are of a long-term nature are accounted for in accordance with SFAS No. 52, Foreign Currency Translation, whereby foreign currency transaction gains and losses are reported in the same manner as translation adjustments.

Cash flows of consolidated foreign subsidiaries, whose functional currency is the local currency, are translated to U.S. dollars using weighted average exchange rates for the period. The Company reports the effect of exchange rate changes on cash balances held in foreign currencies as a separate item in the reconciliation of the changes in cash and cash equivalents during the period.

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Foreign currency gains (losses) are reported as a component of other income (expense) in the Consolidated Statements of Operations. For the years ended December 31, 2006, 2005 and 2004, net foreign currency gains (losses) were \$8,855, \$(13,454), and \$3,135, respectively.

*Accounting for Income Taxes*

In accordance with SFAS No. 109, *Accounting for Income Taxes* ( SFAS 109 ), the Company recognizes deferred income taxes based on the expected future tax consequences of differences between the financial statement basis and the tax basis of assets and liabilities, calculated using enacted tax rates in effect for the year in which the differences are expected to be reflected in the tax return.

The carrying value of the Company's net deferred tax assets assumes that the Company will be able to generate sufficient future taxable income in certain tax jurisdictions to realize the value of these assets. If the Company is unable to generate sufficient future taxable income in these jurisdictions, a valuation allowance is recorded when it is more likely than not that the value of the deferred tax assets is not realizable. Management evaluates the realizability of the deferred tax assets and assesses the need for any valuation allowance adjustment. Management periodically evaluates the need of tax reserves for uncertain tax positions. To the extent that the probable tax outcome of these uncertain tax positions changes, such changes in estimate will impact the income tax provision in the period in which such determination is made.

*Pension and Postretirement Benefits*

The Company's pension expense and obligations are developed from actuarial valuations required by the provisions of SFAS No. 87, *Employers' Accounting for Pensions*, ( SFAS 87 ), SFAS No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*, ( SFAS 106 ) and SFAS No. 158, *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans* an amendment of FASB Statements No. 87, 88, 106, and 132(R) ( SFAS 158 ). SFAS 158 requires recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. Under SFAS 158, gains and losses, prior service costs and credits and any remaining transition amounts under SFAS 87 and SFAS 106 that have not yet been recognized through net periodic benefit cost will be recognized in accumulated other comprehensive income, net of tax effects, until they are amortized as a component of net periodic cost. The measurement date, the date at which the benefit obligation and plan assets are measured, is now required to be the same as the company's fiscal year-end. As required by SFAS 158, the Company adopted the balance sheet recognition provisions at December 31, 2006. The measurement date of the benefit obligation and plan assets is the same as the Company's fiscal year end. In addition, SFAS 87 required the recognition of an additional minimum liability (AML) if the market value of plan assets was less than the accumulated benefit obligation at the end of the measurement date. The AML was eliminated upon the adoption of SFAS 158. See Note 16, *Employee Benefit Plans*, for additional information.

*Accounting for Employee Global Mobility and Tax Equalization*

The Company has a tax equalization policy designed to ensure that its employees on domestic long-term and foreign assignments will be subject to the same level of personal tax, regardless of the tax jurisdiction in which the employee works. The Company records tax equalization expenses in the period incurred. If the estimated tax equalization liability, including related interest and penalties, is determined to be greater or less than amounts due upon final settlement, the difference is recorded in the current period. As of December 31,



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2006 and 2005, the Company's liabilities associated with tax equalization expenses and related interest and penalties associated with failure to timely file and withhold payroll and other taxes were \$87,621 and \$82,482, respectively.

*Stock-Based Compensation*

On January 1, 2006, the Company adopted the provisions of SFAS No. 123(R), Share-Based Payment ( SFAS 123(R) ), to record compensation expense for its employee stock options, restricted stock awards, restricted stock units ( RSUs ) and employee stock purchase plans. This Statement is a revision of SFAS No. 123, Accounting for Stock-Based Compensation ( SFAS 123 ), and supersedes Accounting Principles Board Opinion ( APB ) No. 25, Accounting for Stock Issued to Employees ( APB 25 ), and its related implementation guidance. Prior to the adoption of SFAS 123(R), the Company followed the intrinsic value method in accordance with APB 25, in accounting for its stock options and other equity instruments.

SFAS 123(R) requires that all share-based payments to employees be recognized in the Consolidated Statements of Operations based on their grant date fair values with the expense being recognized over the requisite service period. The Company uses the Black-Scholes model to determine the fair value of its awards at the time of grant. See Note 13, Stock-Based Compensation for additional information.

*Derivative Financial Instruments*

The Company accounts for derivative instruments and debt instruments in accordance with the interpretative guidance of SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities ( SFAS 133 ), EITF 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock, APB No. 14, Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants, EITF 98-5, Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios ( EITF 98-5 ), and EITF 00-27, Application of Issue No. 98-5 to Certain Convertible Instruments ( EITF 00-27 ), and associated pronouncements related to the classification and measurement of warrants and instruments with conversion features. The Company makes certain assumptions and estimates to value its derivatives and debt instruments.

The Company is exposed to changes in foreign currency exchange rates and interest rates that may affect its results of operations and financial position. The Company manages its exposure to changes in foreign currency exchange rates and interest rates through its normal operating and financing activities and, when deemed appropriate, through the use of derivative financial instruments. The Company accounts for its derivative instruments in accordance with SFAS 133, which requires that all derivative instruments be reported on the balance sheet at fair value. If the derivative instrument is a hedge, depending on the nature of the hedge, changes in the fair value of the derivative instrument are either recognized in net income or in other comprehensive income (loss) until the hedged item is recognized in net income. For derivatives that do not qualify as hedges under SFAS 133, the change in fair value is recorded in other income (expense) in the Consolidated Statements of Operations.

The Company may enter into foreign currency forward contracts to offset currency-related changes in its foreign currency denominated assets and liabilities. The fair value of these foreign currency forward contracts is reported in other current assets or other current liabilities in the Consolidated Balance Sheets. The Company did not designate any of its derivatives used to offset currency-related changes in the fair value of foreign currency denominated assets and liabilities as hedges as defined by SFAS 133. Accordingly, changes

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in the fair value of these derivatives were recognized in other income (expense) in the Consolidated Statements of Operations in the period of change. As of December 31, 2006 or 2005, the Company did not have any outstanding foreign currency forward contracts.

*Accumulated Other Comprehensive Income*

Accumulated other comprehensive income consists of the following:

	<b>Foreign currency translation adjustment</b>	<b>Pension and post-retirement benefit</b>	<b>Total</b>
Balance at December 31, 2004	\$ 285,955	\$	\$ 285,955
Change in foreign currency translation	(54,543)		(54,543)
Change in minimum pension liabilities		(13,321)	(13,321)
Balance at December 31, 2005	231,412	(13,321)	218,091
Change in foreign currency translation	30,743		30,743
Change in minimum pension liabilities, net of tax		8,880	8,880
Adoption of SFAS 158, net of tax		(11,417)	(11,417)
Balance at December 31, 2006	\$ 262,155	\$ (15,858)	\$ 246,297

*Recently Issued Accounting Pronouncements*

In June 2006, the FASB issued Financial Interpretation ( FIN ) 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 ( FIN 48 ). This interpretation clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS 109. It prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company will be required to adopt this interpretation in the first quarter of fiscal year 2007. Management is currently evaluating the requirements of FIN 48 and has not yet determined the impact on its Consolidated Financial Statements.

In September 2006, the SEC staff issued SAB No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements ( SAB 108 ). SAB 108 was issued in order to eliminate the diversity of practice surrounding how public companies quantify financial statement misstatements. SAB 108 requires registrants to quantify the impact of correcting all misstatements using both the rollover method, which focuses primarily on the impact of a misstatement on the income statement and is the method the Company currently uses, and the iron curtain method, which focuses primarily on the effect of correcting the period-end balance sheet. The use of both of these methods is referred to as the dual approach and should be combined with the

evaluation of qualitative elements surrounding the errors in accordance with SAB No. 99, Materiality . The adoption of SAB 108 during 2006 did not have a material impact on the Consolidated Financial Statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements ( SFAS 157 ). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. The provisions of SFAS 157 are effective for the fiscal year beginning January 1, 2008. The Company is currently evaluating the impact of the provisions of SFAS 157.

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In December 2006, the FASB issued FASB Staff Position No. EITF 00-19-2, Accounting for Registration Payment Arrangements ( FSP No. EITF 00-19-2 ). FSP No. EITF 00-19-2 specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision of a financial instrument or other agreement, should be separately recognized and measured in accordance with SFAS No. 5, Accounting for Contingencies. FSP No. EITF 00-19-2 also requires additional disclosure regarding the nature of any registration payment arrangements, alternative settlement methods, the maximum potential amount of consideration and the current carrying amount of the liability, if any. FSP No. EITF 00-19-2 shall be effective immediately for registration payment arrangements and the financial instruments subject to those arrangements that are entered into or modified subsequent to the date of issuance of FSP No. EITF 00-19-2. For registration payment arrangements and financial instruments subject to those arrangements that were entered into prior to the issuance of FSP No. EITF 00-19-2, this guidance shall be effective for financial statements issued for fiscal years beginning after December 15, 2006, and interim periods within those fiscal years. The Company is currently evaluating the impact FSP No EITF 00-19-2 could have on its financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FAS 115 ( SFAS 159 ). This new statement allows entities to choose, at specific election dates, to measure eligible financial assets and liabilities at fair value that are not otherwise required to be measured at fair value. If a company elects the fair value option for an eligible item, changes in that item's fair value in subsequent reporting periods must be recognized in current earnings. SFAS 159 is effective for the fiscal year beginning January 1, 2008. The Company is currently evaluating the impact of the provisions of SFAS 159.

**3. Earnings (Loss) per Share**

Basic earnings (loss) per share is computed based on the weighted average number of common shares outstanding and vested RSUs during the period. Diluted earnings (loss) per share is computed using the weighted average number of common shares outstanding during the period plus the dilutive effect of potential future issues of common stock relating to the Company's stock option program, RSUs, convertible debt and other potentially dilutive securities. In calculating diluted earnings (loss) per share, the dilutive effect of stock options is computed using the average market price for the period in accordance with the treasury stock method. The effect of convertible securities on the calculation of diluted net loss per share is calculated using the if converted method.

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The following table sets forth the potentially dilutive securities that were not included in the computation of diluted EPS because to do so would have been anti-dilutive (shares on weighted-average basis):

	<b>Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Employee stock options	39,869,914	44,920,037	38,416,819
Employee stock purchase plan	4,831,754	4,605,505	3,405,662
Restricted stock awards and restricted stock units	4,333,270	4,275,980	758,551
Series A Convertible Subordinated Debentures	23,810,200	23,810,200	892,883
Series B Convertible Subordinated Debentures	19,048,160	19,048,160	694,464
April 2005 Convertible Senior Subordinated Debentures	30,303,020	18,939,388	
July 2005 Convertible Senior Subordinated Debentures	5,925,926	2,716,049	
Warrants issued in connection with the July 2005 Debentures	3,500,000	1,604,167	
Softline acquisition obligation (Note 9)	735,759	713,163	691,079
	132,358,003	120,632,649	44,859,458

**4. Property and Equipment**

Property and equipment, net, consists of the following:

	<b>December 31,</b>	
	<b>2006</b>	<b>2005</b>
Property and equipment:		
Internal-use software	\$ 161,005	\$ 167,621
Equipment	101,026	84,182
Leasehold improvements	72,517	54,706
Furniture	38,063	31,710
Total property and equipment	372,611	338,219
Accumulated depreciation and amortization:		
Internal-use software	(96,798)	(81,815)
Equipment	(72,809)	(49,778)
Leasehold improvements	(37,859)	(24,240)
Furniture	(18,753)	(12,253)
Total accumulated depreciation and amortization	(226,219)	(168,086)

Property and equipment, net	\$ 146,392	\$ 170,133
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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Depreciation and amortization expense related to property and equipment consists of the following:

	<b>Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Amounts included in:			
Other costs of service	\$ 40,502	\$ 39,205	\$ 43,485
Selling, general and administrative expenses	33,521	31,339	35,205
	\$ 74,023	\$ 70,544	\$ 78,690

**5. Business Acquisitions, Goodwill and Other Intangible Assets**

Goodwill balances at December 31, 2006 and 2005 are associated with the acquisition of KPMG Consulting AG (subsequently renamed BearingPoint GmbH) in August 2002 and a series of acquisitions of Andersen Business Consulting practices during 2002.

The changes in the carrying amount of goodwill, at the reporting unit level, for the years ended December 31, 2006 and 2005 are as follows:

	<b>Balance December 31, 2005</b>	<b>Impairment Charge</b>	<b>Foreign Currency Translation Adjustment</b>	<b>Balance December 31, 2006</b>
Public Services	\$ 23,581	\$	\$	\$ 23,581
Financial Services	9,210			9,210
EMEA	325,262		33,871	359,133
Asia Pacific	68,562		1,840	70,402
Latin America	871		47	918
Corporate/Other	202			202
Total	\$ 427,688	\$	\$ 35,758	\$ 463,446

	<b>Balance December 31, 2004</b>	<b>Impairment Charge</b>	<b>Foreign Currency Translation Adjustment</b>	<b>Balance December 31, 2005</b>
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Public Services	\$	23,581	\$		\$		\$	23,581
Commercial Services		64,188		(64,188)				
Financial Services		9,210						9,210
EMEA		485,401		(102,227)		(57,912)		325,262
Asia Pacific		73,459				(4,897)		68,562
Latin America		836				35		871
Corporate/Other		202						202
Total	\$	656,877	\$	(166,415)	\$	(62,774)	\$	427,688

The Company completed its required annual impairment test in April 2006 and determined that the carrying value of goodwill was not impaired.



**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

In the fourth quarter of 2005, the Company determined that a triggering event had occurred, causing the Company to perform a goodwill impairment test on all of its reporting units. The triggering event resulted from a combination of various factors, including lower than previously expected results in the fourth quarter ended December 31, 2005 and a change in management's expectation of future results. As required by SFAS 142, the Company performed a two-step impairment test to identify the potential impairments and, if necessary, to measure the amount of the impairment. Under step one of the impairment test, the Company determined there were potential impairments in its Commercial Services and EMEA reporting units. In determining the fair value of its Commercial Services and EMEA reporting units, the Company revised certain assumptions relative to each reporting unit, which significantly decreased their fair value as compared to the fair value determined during the Company's most recent goodwill impairment test, which had been performed as of April 20, 2005. For the Commercial Services reporting unit, these revisions included the negative impact on future periods from operating losses associated with the Company's contract with Hawaiian Telcom Communications, Inc. For the EMEA reporting unit, these revisions included lowering operating margin growth expectations. In order to quantify the impairment, under step two of the impairment test, the Company completed a hypothetical purchase price allocation of the fair value determined in step one to all of the respective assets and liabilities of its Commercial Services and EMEA reporting units. As a result, goodwill impairment losses of \$64,188 and \$102,227 were recognized in the Commercial Services and the EMEA reporting units, respectively, as the carrying amount of each reporting unit was greater than the revised fair value of that reporting unit (as determined using the expected present value of future cash flows), and the carrying amount of each reporting unit's goodwill exceeded the implied fair value of that goodwill. The goodwill impairment loss of \$64,188 for the Commercial Services reporting unit represented a full impairment of the remaining goodwill in that reporting unit.

On April 20, 2005, the Company determined that a triggering event had occurred, causing the Company to perform a goodwill impairment test on all reporting units. The triggering event resulted from the Company's public announcement of likely restatements of prior period financial statements along with significant delays in filing 2004 annual results and anticipated delays in filing 2005 quarterly results. The Company determined this triggering event may have a significant adverse effect on its business climate and regulatory environment. As required by SFAS 142, the Company applied a two-step impairment test to identify the potential impairment and, if necessary, to measure the amount of the impairment. The Company performed step one of the impairment test to identify the potential impairment and determined there were no impairments to any reporting units. As a result, the step two impairment test was not considered necessary.

During the fourth quarter of the year ended December 31, 2004, the Company determined that a triggering event had occurred, causing the Company to perform a goodwill impairment test on all reporting units. The triggering event resulted from downgrades in the Company's credit rating in December 2004, significant changes in senior management and underperforming foreign legal entities. The Company performed a two-step impairment test to identify the potential impairment and, if necessary, to measure the amount of the impairment. Under step one of the impairment test, the Company determined there was a potential impairment in the EMEA reporting unit. In determining the fair value of its EMEA reporting unit at December 31, 2004, the Company revised certain assumptions relative to EMEA which significantly decreased the fair value of this reporting unit relative to the fair value determined during the Company's annual goodwill impairment test, which was as of April 1, 2004. These revisions included lowering its EMEA segment revenue growth expectations, increasing selling, general and administrative cost projections and factoring in a less than anticipated decline in compensation expense. These changes reflected lower than expected results for the year ended December 31, 2004 and management's current expectations of future results. In order to

quantify the

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

impairment, under step two of the impairment test, the Company completed a hypothetical purchase price allocation of fair value determined in step one to all assets and liabilities of its EMEA reporting unit. As a result, a goodwill impairment loss of \$397,065 was recognized in the EMEA reporting unit as the carrying amount of the reporting unit was greater than the revised fair value of the reporting unit (as determined using the expected present value of future cash flows) and the carrying amount of the reporting unit goodwill exceeded the implied fair value of that goodwill.

Identifiable intangible assets include finite-lived intangible assets, which primarily consist of market rights, order backlog, customer contracts and related customer relationships. Identifiable intangible assets are amortized using the straight-line method over their expected period of benefit, which generally ranges from one to five years. Identifiable intangible assets consist of the following:

	<b>December 31,</b>	
	<b>2006</b>	<b>2005</b>
Other intangible assets:		
Backlog, customer contracts and related customer relationships	\$ 1,309	\$ 1,309
Market rights	10,297	10,297
Total other intangibles	11,606	11,606
Accumulated amortization:		
Backlog, customer contracts and related customer relationships	(1,309)	(1,309)
Market rights	(10,297)	(8,752)
Total accumulated amortization	(11,606)	(10,061)
Other intangible assets, net	\$	\$ 1,545

For the years ended December 31, 2006, 2005 and 2004, amortization expense related to identifiable intangible assets was \$1,545, \$2,266, and \$3,457, respectively. Identifiable intangible assets were fully amortized during 2006.

**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)****6. Notes Payable**

Notes payable consist of the following:

	<b>December 31,</b>	
	<b>2006</b>	<b>2005</b>
Current portion (a):		
Yen-denominated term loan (January 31, 2003)	\$	\$ 2,803
Yen-denominated term loan (June 30, 2003)		1,402
Other	360	2,188
Total current portion	360	6,393
Long-term portion:		
Series A and Series B Convertible Debentures	450,000	450,000
April 2005 Convertible Debentures	200,000	200,000
July 2005 Convertible Debentures (net of discount of \$18,510 and \$21,946, respectively)	21,490	18,054
Other		313
Total long-term portion	671,490	668,367
Total notes payable	\$ 671,850	\$ 674,760

The following is a schedule of annual maturities on notes payable, net of discounts, as of December 31, 2006 for each of the next five calendar years and thereafter:

<b>Year</b>	<b>Amount</b>	
2007	\$	360
2008		
2009		
2010		21,490(b)
2011		
Thereafter		650,000(b)
Total	\$	671,850

(a)

The weighted average interest rate on the current portion of notes payable as of December 31, 2006 and 2005 was 5.6% and 2.4%, respectively.

- (b) As described below, the holders of the Series A and B Convertible Debentures have the right to convert the Debentures into shares of Company common stock only upon occurrence of certain triggering events. The April 2005 Convertible Debentures were convertible upon issuance on April 27, 2005 and the July 2005 Convertible Debentures were convertible starting on July 15, 2006. Upon conversion of these debentures, the Company will have the right to deliver, in lieu of shares of common stock, cash or a combination of cash and shares of common stock. In addition, the holders of the April 2005 Convertible Debentures have the right, at their option, to require the Company to repurchase all or some of their debentures on April 15, 2009, 2013, 2015 and 2020.

**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

*2007 Credit Facility*

On May 18, 2007, the Company entered into a \$400,000 senior secured credit facility and on June 1, 2007, the Company amended and restated the credit facility to increase the aggregate commitments under the facility from \$400,000 to \$500,000 (the 2007 Credit Facility). The 2007 Credit Facility consists of (1) term loans in an aggregate principal amount of \$300,000 (the Term Loans) and (2) a letter of credit facility in an aggregate face amount at any time outstanding not to exceed \$200,000 (the LC Facility). Interest on the Term Loans under the 2007 Credit Facility is calculated, at the Company's option, (1) at a rate equal to 3.5% plus the London Interbank Offered Rate, or LIBOR, or (2) at a rate equal to 2.5% plus the higher of (a) the federal funds rate plus 0.5% and (b) UBS AG, Stamford Branch's prime commercial lending rate. As of June 1, 2007, the Company has borrowed \$300,000 under the Term Loans, and an aggregate of approximately \$89,300 of letters of credit previously outstanding under the 2005 Credit Facility has been assumed under the LC Facility.

The Company's obligations under the 2007 Credit Facility are secured by liens and security interests in substantially all of the Company's assets and most of its material domestic subsidiaries, as guarantors of such obligations (including a pledge of 65% of the stock of certain of its foreign subsidiaries), subject to certain exceptions.

The 2007 Credit Facility requires the Company to make prepayments of outstanding Term Loans and cash collateralize outstanding Letters of Credit in an amount equal to (i) 100% of the net proceeds received from property or asset sales (subject to exceptions), (ii) 100% of the net proceeds received from the issuance or incurrence of additional debt (subject to exceptions), (iii) 100% of all casualty and condemnation proceeds (subject to exceptions), (iv) 50% of the net proceeds received from the issuance of equity (subject to exceptions) and (v) for each fiscal year ending on or after December 31, 2008 (and, at the Company's election for the second half of the 2007 fiscal year), the difference between (a) 50% of the Excess Cash Flow (as defined in the 2007 Credit Facility) and (b) any voluntary prepayment of the Term Loan or the LC Facility (as defined in the 2007 Credit Facility) (subject to exceptions). If the Term Loan is prepaid or the LC Facility is reduced prior to May 18, 2008 with other indebtedness or another letter of credit facility, the Company may be required to pay a prepayment premium of 1% of the principal amount of the Term Loan so prepaid or LC Facility so reduced if the cost of such replacement indebtedness or letter of credit facility is lower than the cost of the 2007 Credit Facility. In addition, the Company is required to pay \$750 in principal plus any accrued and unpaid interest at the end of each quarter, commencing on June 29, 2007 and ending on March 31, 2012.

The 2007 Credit Facility contains affirmative and negative covenants:

The *affirmative covenants* include, among other things: the delivery of unaudited quarterly and audited annual financial statements, all in accordance with generally accepted accounting principles, certain monthly operating metrics and budgets; compliance with applicable laws and regulations (excluding, prior to October 31, 2008, compliance with certain filing requirements under the securities laws); maintenance of existence and insurance; after October 31, 2008, as requested by the Administrative Agent, maintenance of credit ratings; and maintenance of books and records (subject to the material weaknesses previously disclosed in the Company's 2005 Form 10-K).

The *negative covenants*, which (subject to exceptions) restrict certain of the Company's corporate activities, include, among other things, limitations on: disposition of assets; mergers and acquisitions; payment of dividends; stock repurchases and redemptions; incurrence of additional indebtedness; making of loans and

investments; creation of liens; prepayment of other indebtedness; and engaging in certain transactions with affiliates.

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Events of default under the 2007 Credit Facility include, among other things: defaults based on nonpayment, breach of representations, warranties and covenants, cross-defaults to other debt above \$10,000, loss of lien on collateral, invalidity of certain guarantees, certain bankruptcy and insolvency events, certain ERISA events, judgments against the Company in an aggregate amount in excess of \$20,000, and change of control events.

Under the terms of the 2007 Credit Facility, the Company is not required to become current with its SEC periodic filings until October 31, 2008. Until October 31, 2008, the Company's failure to provide annual audited or quarterly unaudited financial statements, to keep its books and records in accordance with GAAP or to timely file its SEC periodic reports will not be considered an event of default under the 2007 Credit Facility.

The 2007 Credit Facility replaced the Company's 2005 Credit Facility, which was terminated on May 18, 2007. For information about the 2005 Credit Facility, see below.

*Series A and Series B Convertible Subordinated Debentures*

On December 22, 2004, the Company completed a \$400,000 offering of Convertible Subordinated Debentures. The offering consisted of \$225,000 aggregate principal amount of 2.50% Series A Convertible Subordinated Debentures due December 15, 2024 (the Series A Debentures) and \$175,000 aggregate principal amount of 2.75% Series B Convertible Subordinated Debentures due December 15, 2024 (the Series B Debentures and together with the Series A Debentures, the Subordinated Debentures). On January 5, 2005, the Company issued an additional \$25,000 aggregate principal amount of its Series A Debentures and an additional \$25,000 aggregate principal amount of its Series B Debentures upon the exercise in full of an option granted to the initial purchasers. Interest is payable on the Subordinated Debentures on June 15 and December 15 of each year, beginning June 15, 2005. The Subordinated Debentures are unsecured and are subordinated to the Company's existing and future senior debt. Due to the delay in the completion of the Company's audited financial statements for the year ended December 31, 2004, the Company was unable to file a timely registration statement with the SEC to register for resale its Subordinated Debentures and underlying common stock. Accordingly, pursuant to the terms of these securities, the applicable interest rate on each series of Subordinated Debentures increased by 0.25% beginning on March 23, 2005 and increased another 0.25% beginning on June 22, 2005. These changes together increased the interest rate on the Series A Debentures and the Series B Debentures to 3.00% and 3.25%, respectively.

On November 2, 2006, the Company entered into the First Supplemental Indenture (the First Supplemental Indenture) with The Bank of New York, as trustee, which amends the subordinated indenture governing the Subordinated Debentures. The First Supplemental Indenture includes: (i) a waiver of the Company's SEC reporting requirements under the Subordinated Indentures through October 31, 2008, (ii) the interest rate payable on all Series A Debentures increased from 3.00% per annum to 3.10% per annum until December 23, 2011, and (iii) adjustment of the interest rate payable on all Series B Debentures from 3.25% per annum to 4.10% per annum until December 23, 2014. In accordance with EITF 96-19, Debtor's Accounting for a Modification or Exchange of Debt Instruments (EITF 96-19), since the change in the terms of the Subordinated Debentures did not result in substantially different cash flows, this change in terms is accounted for as a modification, and therefore additional interest payments will be expensed over the period from November 2, 2006 through December 23, 2011 for Series A, and December 23, 2014 for Series B.





**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

During the period of November 2, 2006 through December 23, 2011, for Series A and December 23, 2014, for Series B, the new effective interest rate on this debt will be 3.60% and 4.50%, respectively. In addition, the Company paid approximately \$1,800 in fees and expenses to third-parties for work performed in connection with all of the modifications to the Company's outstanding debentures, which were expensed as incurred.

The net proceeds from the sale of the Subordinated Debentures were approximately \$435,600, after deducting offering expenses and the initial purchasers' commissions of \$11,400 and other fees and expenses of approximately \$3,000. The Company used approximately \$240,590 of the net proceeds from the sale of the Subordinated Debentures to repay its outstanding \$220,000 Senior Notes and approximately \$135,000 to repay amounts outstanding under its then existing revolving credit facility. The Company also used the proceeds to pay fees and expenses in connection with entering into the \$400,000 Interim Senior Secured Credit Facility, as defined below.

The Subordinated Debentures are initially convertible, under certain circumstances, into shares of the Company's common stock at a conversion rate of 95.2408 shares for each \$1 principal amount of the Subordinated Debentures, subject to anti-dilution and adjustments but not to exceed 129.0 shares, equal to an initial conversion price of approximately \$10.50 per share. Holders of the Subordinated Debentures may exercise the right to convert the Subordinated Debentures prior to their maturity only under certain circumstances, including when the Company's stock price reaches a specified level for a specified period of time, upon notice of redemption, and upon specified corporate transactions. Upon conversion of the Subordinated Debentures, the Company will have the right to deliver, in lieu of shares of common stock, cash or a combination of cash and shares of common stock. The Subordinated Debentures will be entitled to an increase in the conversion rate upon the occurrence of certain change of control transactions or, in lieu of the increase, at the Company's election, in certain circumstances, to an adjustment in the conversion rate and related conversion obligation so that the Subordinated Debentures are convertible into shares of the acquiring or surviving company. The Company will also increase the conversion rate upon occurrence of certain transactions. As of December 31, 2006, none of the circumstances under which the Subordinated Debentures are convertible existed.

On December 15, 2011, December 15, 2014 and December 15, 2019, holders of Series A Debentures, at their option, have the right to require the Company to repurchase any outstanding Series A Debentures. On December 15, 2014 and December 15, 2019, holders of Series B Debentures, at their option, have the right to require the Company to repurchase any outstanding Series B Debentures. In each case, the Company will pay a repurchase price in cash equal to 100% of the principal amount of the Subordinated Debentures, plus accrued and unpaid interest, including liquidated damages, if any, to the repurchase date. In addition, holders of the Subordinated Debentures may require the Company to repurchase all or a portion of the Subordinated Debentures on the occurrence of a designated event, at a repurchase price equal to 100% of the principal amount of the Subordinated Debentures, plus any accrued but unpaid interest and liquidated damages, if any, to, but not including, the repurchase date. A designated event includes certain change of control transactions and a termination of trading, occurring if the Company's common stock is no longer listed for trading on a U.S. national securities exchange.

The Company may redeem some or all of the Series A Debentures beginning on December 23, 2011 and, beginning on December 23, 2014, may redeem the Series B Debentures, in each case at a redemption price in cash equal to 100% of the principal amount of the Subordinated Debentures plus accrued and unpaid interest and liquidated damages, if any, on the Subordinated Debentures to, but not including, the redemption date.



**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Upon a continuing event of default, the trustee or the holders of at least 25% in aggregate principal amount of the Subordinated Debentures may declare the applicable series of Debentures immediately due and payable, which could lead to cross-defaults and possible acceleration of unpaid principal and accrued interest of the April 2005 Convertible Debentures, July 2005 Convertible Debentures (defined below) and the 2007 Credit Facility.

*April 2005 Convertible Senior Subordinated Debentures*

On April 27, 2005, the Company issued \$200,000 aggregate principal amount of its 5.00% Convertible Senior Subordinated Debentures due April 15, 2025 (the April 2005 Convertible Debentures). Interest is payable on the April 2005 Convertible Debentures on April 15 and October 15 of each year, beginning October 15, 2005. The April 2005 Convertible Debentures are unsecured and are subordinated to the Company's existing and future senior debt. The April 2005 Convertible Debentures are senior to the Subordinated Debentures. Since the Company failed to file a registration statement with the SEC to register for resale of its April 2005 Convertible Debentures and the underlying common stock by December 31, 2005, the interest rate on the April 2005 Convertible Debentures increased by 0.25% to 5.25% beginning on January 1, 2006 and will continue to be the applicable interest rate through the date the registration statement is filed. On November 9, 2006, the Company paid to certain consenting holders of April 2005 Convertible Debentures, who provided their consents prior to the expiration of the consent solicitation, a consent fee equal to 1.00% of the outstanding principal amount of the April 2005 Convertible Debentures. The supplemental indenture includes a waiver of the Company's SEC reporting requirements through October 31, 2007, and provides for further extension through October 31, 2008 upon the Company's payment of an additional fee of 0.25% of the principal amount of the debentures. In accordance with EITF 96-19, since the change in the terms of the April 2005 Convertible Debentures did not result in substantially different cash flows, this change in terms is accounted for as a modification, and therefore the consent fees of \$2,000 will be recognized over future periods.

The net proceeds from the sale of the April 2005 Convertible Debentures, after deducting offering expenses and the placement agents' commissions and other fees and expenses, were approximately \$192,800. The Company used the net proceeds from the offering to replace the working capital that was at the time used to cash collateralize letters of credit under the 2004 Interim Credit Facility (see below).

The April 2005 Convertible Debentures are initially convertible into shares of the Company's common stock at a conversion rate of 151.5151 shares for each \$1 principal amount of the April 2005 Convertible Debentures, subject to anti-dilution and adjustments, equal to an initial conversion price of \$6.60 per share at any time prior to the stated maturity. Upon conversion of the April 2005 Convertible Debentures, the Company will have the right to deliver, in lieu of shares of common stock, cash or a combination of cash and shares of common stock. The April 2005 Convertible Debentures will be entitled to an increase in the conversion rate upon the occurrence of certain change of control transactions or, in lieu of the increase, at the Company's election, in certain circumstances, to an adjustment in the conversion rate and related conversion obligation so that the April 2005 Convertible Debentures are convertible into shares of the acquiring or surviving company.

The holders of the April 2005 Convertible Debentures have the right, at their option, to require the Company to repurchase all or some of their debentures on April 15, 2009, 2013, 2015 and 2020. In each case, the Company will pay a repurchase price in cash equal to 100% of the principal amount of the April 2005



**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Convertible Debentures, plus any accrued but unpaid interest, including additional interest, if any, to the repurchase date. In addition, holders of the April 2005 Convertible Debentures may require the Company to repurchase all or a portion of the April 2005 Convertible Debentures on the occurrence of a designated event, at a repurchase price equal to 100% of the principal amount of the April 2005 Convertible Debentures, plus any accrued but unpaid interest and additional interest, if any, to, but not including, the repurchase date. A designated event includes certain change of control transactions and a termination of trading, occurring if the Company's common stock is no longer listed for trading on a U.S. national securities exchange.

The April 2005 Convertible Debentures will be redeemable at the Company's option on or after April 15, 2009 at a redemption price in cash equal to 100% of the principal amount of the April 2005 Convertible Debentures plus accrued and unpaid interest and additional interest, if any, on the April 2005 Convertible Debentures to, but not including, the redemption date.

Upon a continuing event of default, the trustee or the holders of at least 25% in aggregate principal amount of the April 2005 Convertible Debentures may declare the debentures immediately due and payable, which could lead to cross-defaults and possible acceleration of unpaid principal and accrued interest of the Subordinated Debentures, July 2005 Convertible Debentures (defined below) and the 2007 Credit Facility.

*July 2005 Convertible Senior Debentures*

On July 15, 2005, the Company issued \$40,000 aggregate principal amount of its 0.50% Convertible Senior Subordinated Debentures due July 2010 (the July 2005 Convertible Debentures) and common stock warrants (the July 2005 Warrants) to purchase up to 3,500,000 shares of the Company's common stock. The July 2005 Convertible Debentures bear interest at a rate of 0.50% per year and will mature on July 15, 2010. Interest is payable on the July 2005 Convertible Debentures on January 15 and July 15 of each year, beginning January 15, 2006. The July 2005 Convertible Debentures are pari passu to the April 2005 Convertible Debentures and senior to the Subordinated Debentures. Since the Company failed to file a registration statement with the SEC to register for resale its July 2005 Convertible Debentures and the underlying common stock by December 31, 2005, the interest rate on the July 2005 Convertible Debentures increased by 0.25% to 0.75% beginning on January 1, 2006 and will continue to be the applicable interest rate through the date the registration statement is filed. On November 9, 2006, the Company entered into an agreement with the holders of the July 2005 Debentures, pursuant to which the Company paid a consent fee equal to 1.00% of the outstanding principal amount of the July 2005 Debentures, in accordance with the terms of the purchase agreement governing the issuance of the July 2005 Debentures. The agreement includes a waiver of the Company's SEC reporting requirements through October 31, 2007. In accordance with EITF 96-19, since the change in the terms of the July 2005 Convertible Senior Debentures did not result in substantially different cash flows, this change in terms is accounted for as a modification, and therefore the consent fees of \$400 will be recognized over future periods.

The net proceeds from the sale of the July 2005 Convertible Debentures and July 2005 Warrants, after deducting offering expenses and other fees and expenses, were approximately \$38,900.

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In accordance with the terms of the purchase agreement, the holders of the July 2005 Convertible Debentures appointed a designated director to the Company's Board of Directors effective July 15, 2005. If the designated director ceases to be affiliated with the holders of the July 2005 Convertible Debentures or ceases to serve on the Company's Board of Directors, so long as the holders together hold at least 40% of the

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

original principal amount of the July 2005 Convertible Debentures, the holders or their designees have the right to designate a replacement director to the Company's Board of Directors.

The July 2005 Convertible Debentures are initially convertible on or after July 15, 2006 into shares of the Company's common stock at a conversion price of \$6.75 per share, subject to anti-dilution and other adjustments. Upon conversion of the July 2005 Convertible Debentures, the Company will have the right to deliver, in lieu of shares of common stock, cash or a combination of both. The July 2005 Convertible Debentures will be entitled, in certain change of control transactions, to an adjustment in the conversion obligation so that the July 2005 Convertible Debentures are convertible into shares of stock, other securities or other property or assets receivable upon the occurrence of such transaction by a holder of shares of the Company's common stock in such transaction.

The holders of the July 2005 Convertible Debentures may require the Company to repurchase all or a portion of the July 2005 Convertible Debentures on the occurrence of a designated event, at a repurchase price equal to 100% of the principal amount of the July 2005 Convertible Debentures, plus any accrued but unpaid interest and additional interest, if any, to, but not including, the repurchase date. The list of designated events includes certain change of control transactions and a termination of trading occurring if the Company's common stock is no longer listed for trading on a U.S. national securities exchange.

The July 2005 Warrants may be exercised on or after July 15, 2006 and have a five-year term. The initial number of shares issuable upon exercise of the July 2005 Warrants is 3,500,000 shares of common stock, and the initial exercise price per share of common stock is \$8.00. The number of shares and exercise price are subject to certain customary anti-dilution protections and other customary terms. These terms include, in certain change of control transactions, an adjustment in the conversion obligation so that the July 2005 Warrants, upon exercise, will entitle the July 2005 Warrant holders to receive shares of stock, other securities or other property or assets receivable upon the occurrence of such transaction by a holder of shares of the Company's common stock in such transaction.

Upon a continuing event of default, the holders of at least 25% in aggregate principal amount of the July 2005 Convertible Debentures may declare the July 2005 Convertible Debentures immediately due and payable, which could lead to cross-defaults and possible acceleration of unpaid principal and accrued interest of the Subordinated Debentures, April 2005 Convertible Debentures and the 2005 Credit Facility (defined below).

In accordance with the provisions of EITF 98-5 and EITF 00-27, the Company allocated the proceeds received from the July 2005 Convertible Debentures to the elements of the debt instrument based on their relative fair values. The Company allocated fair value to the July 2005 Warrants and conversion option utilizing the Black-Scholes option pricing model, which was consistent with the Company's historical valuation methods. The following assumptions and estimates were used in the Black-Scholes model: volatility of 48.5%; an average risk-free interest rate of 3.98%; dividend yield of 0%; and an expected life of 5 years. The fair value of debt component of the July 2005 Debentures was based on the net present value of the underlying cash flows discounted at a rate derived from the Company's then publicly traded debt, which was 11.4%. Once the relative fair values were established, the Company allocated the proceeds to each component of the contract. Because the conversion price was lower than the then current fair market value of the Company's common stock, the Company determined that a beneficial conversion feature (BCF) existed which required separate accounting.





**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

The accounting conversion value of the BCF calculated was \$14,288 and the fair value allocated to the July 2005 Warrants was \$8,073. The fair value allocated to the warrants and the accounting conversion value of the BCF amounting to \$22,361 were recorded as credits to additional paid in capital. In addition, \$1,000 paid to the holders in connection with this transaction was recorded as a reduction of the net proceeds. The offsetting \$23,361 was treated as a discount to the \$40,000 principal amount of the July 2005 Convertible Debentures. Using the effective interest method with an imputed interest rate of 17.9%, the discount will be accreted as interest expense over the term of the debt contract to bring the value of the debt to its face amount at the time the principal payment is due in July 2010. As of December 31, 2006 and 2005 the Company has amortized \$4,851 and \$1,415, respectively, of the discount as interest expense.

*Discontinued Credit Facilities*  
*Credit Facilities prior to 2005*

On May 29, 2002, the Company entered into a credit agreement with a commercial lender, for a revolving credit facility with a maximum aggregate principal balance of \$250,000. The revolving credit facility expired on May 29, 2005.

On December 17, 2004, the Company entered into a \$400,000 Interim Senior Secured Credit Agreement (the 2004 Interim Credit Facility ), which provided for up to \$400,000 in revolving credit, all of which was to be available for issuance of letters of credit (subject to restrictions), and included up to \$20,000 in a swingline subfacility. The 2004 Interim Credit Facility was terminated by the Company on April 26, 2005.

The 2004 Interim Credit Facility was replaced by the 2005 Credit Facility on July 19, 2005, as described below. Immediately prior to termination of the 2004 Interim Credit Facility, there were no outstanding loans under the 2004 Interim Credit Facility; however, there were outstanding letters of credit of approximately \$87,700, which were issued primarily to meet the Company's obligations to collateralize certain surety bonds issued to support client engagements, mainly in its state and local government business. The \$87,700 in letters of credit remained outstanding after the termination of the 2004 Interim Credit Facility. In order to support the letters of credit that remained outstanding, the Company provided the lenders of the 2004 Interim Credit Facility with the following collateral: (i) \$94,300 of cash which was sourced from cash on hand; and (ii) a security interest in the Company's domestic accounts receivable. Upon entering into the 2005 Credit Facility, the lenders under the 2004 Interim Credit Facility: (i) released all but \$5,000 of the cash collateral (remaining \$5,000, net of expenses, was returned to the Company on April 4, 2006); (ii) released its security interest in the domestic accounts receivable; and (iii) received an \$85,400 letter of credit issued by the lenders under the 2005 Credit Facility.

*2005 Credit Facility*

On July 19, 2005, the Company entered into a \$150,000 Senior Secured Credit Facility (the 2005 Credit Facility ). The 2005 Credit Facility, as amended, provided for up to \$150,000 in revolving credit and advances, all of which was available for issuance of letters of credit. Advances under the revolving credit line were limited by the available borrowing base, which was based upon a percentage of eligible accounts receivable and unbilled receivables. The 2005 Credit Facility was terminated on May 18, 2007. On that date, all outstanding obligations under the 2005 Credit Facility were assumed by the 2007 Credit Facility and liens and security interests were released.



**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

The entire \$150,000 under the 2005 Credit Facility was not always available to the Company because, among other things: (i) certain accounts receivable for government contracts could not be included in the calculation of the borrowing base without obtaining certain consents (this restriction was removed by amendment on March 30, 2006); and (ii) delays in the Company's ability to provide month-end account receivables reports negatively impacted the Company's ability to include such account receivables as part of the borrowing base, which determined the amount the Company could borrow under the 2005 Credit Facility. Borrowings available under the 2005 Credit Facility are used for general corporate purposes. As of December 31, 2006, the Company had approximately \$23,700 available under the borrowing base.

In addition, prior to the March 30, 2006 amendment, the Company was required to cash collateralize 105% of its borrowings, including any outstanding letters of credit, under the 2005 Credit Facility and any accrued and unpaid interest and fees thereon. As of December 31, 2006, the Company had no borrowings under the 2005 Credit Facility but had letters of credit outstanding of approximately \$89,300. The Company was charged an annual rate of 2.75% for the credit spread and other fees for its outstanding letters of credit. The Company fulfilled its obligation to cash collateralize using cash on hand. The requirement to deposit and maintain cash collateral terminated as part of the March 30, 2006 amendment to the 2005 Credit Facility, and such cash collateral was released to the Company.

Interest on loans (other than swingline loans) under the 2005 Credit Facility was calculated, at the Company's option, at a rate equal to LIBOR, or, for dollar-denominated loans, at a rate equal to the higher of the bank's corporate base rate or the Federal funds rate plus 50 basis points ( "Base Rate Loans" ). No matter which rate the Company chose, an applicable margin was added that varied depending upon availability under the revolver and the status of the Company's SEC periodic filings. For Base Rate Loans and LIBOR loans, the applicable margins were 1.00% and 2.00%, respectively, as the Company was not current in its SEC periodic filings during the term of the facility. As of December 31, 2006, the interest rate under the 2005 Credit Facility was 7.36%.

The 2005 Credit Facility contained financial, affirmative, and negative covenants.

The financial covenants included: (i) a minimum U.S. cash collections requirement, (ii) a minimum trailing twelve-month EBITDA covenant, (iii) a maximum leverage ratio and (iv) a maximum trailing twelve-month capital expenditures covenant. The EBITDA and maximum leverage ratio was not tested for a quarterly test period if (i) at all times during the test period that the borrowing base was less than \$120,000, borrowing availability was greater than \$15,000, (ii) at all times during the test period that the borrowing base was greater than or equal to \$120,000 and less than \$130,000, borrowing availability was greater than \$20,000, or (iii) at all times during the test period that the borrowing base was greater than or equal to \$130,000, borrowing availability was greater than \$25,000. These ratios were never tested, since the Company at all times maintained the minimum borrowing base.

The affirmative covenants included the Company becoming current in its SEC periodic filings in accordance to a predetermined schedule, repatriation of a \$65,000 of cash from foreign subsidiaries and the submission to its lender certain weekly and monthly reports providing various financial information.

The negative covenants significantly restricted the Company's corporate activities and ability to dispose of assets without the lenders' consent.

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Standard events of default for a senior secured facility were included, as well as default for payments in respect of judgments against the Company in excess of \$18,000; termination of trading of Company stock; certain indictments, convictions or the commencement of criminal proceedings of or against the Company or any subsidiary.

Upon an event of default under the 2005 Credit Facility, the lenders could require the Company to post cash collateral in an amount equal to 105% of the principal amount of the outstanding letters of credit or declare all borrowings outstanding under the 2005 Credit Facility, together with accrued interest and other fees, immediately due and payable. Any default agreements governing the Company's other significant indebtedness could lead to an acceleration of debt under the 2005 Credit Facility.

The Company's obligations under the 2005 Credit Facility were secured by liens and security interests in substantially all of its present and future tangible and intangible assets and those of certain of its domestic subsidiaries, as guarantors of such obligations (including 65.0% of the stock of its foreign subsidiaries), subject to certain exceptions.

The lenders of the 2005 Credit Facility granted the Company waivers for any default under the 2005 Credit Facility resulting from the Series B debenture lawsuit and the defaults alleged therein, and also consented to the Company's payment of consent fees to the holders of each series of debentures as well as increases in the interest rates payable on all of the debentures.

*Terminated Yen-Denominated Term Loans and Line of Credit*

On January 31, 2003, the Company's Japanese subsidiary entered into a 2.0 billion yen-denominated unsecured term loan. Scheduled principal payments were every six months through July 31, 2005 in the amount of 334.0 million yen and included a final payment of 330.0 million yen on January 31, 2006.

On June 30, 2003, the Company's Japanese subsidiary entered into a 1.0 billion yen-denominated unsecured term loan. Scheduled principal payments were every six months through December 31, 2005 in the amount of 167.0 million yen and included a final payment of 165.0 million yen on June 30, 2006.

On August 30, 2004, the Company's Japanese subsidiary extended its yen-denominated revolving line of credit facility and overdraft line of credit facility dated December 16, 2002. The renewed agreement included a yen-denominated revolving line of credit facility with an aggregate principal balance not to exceed 1.85 billion yen (approximately \$18,026 as of December 31, 2004) and an overdraft line of credit facility with an aggregate principal balance not to exceed 0.5 billion yen (approximately \$4,872 as of December 31, 2004). These facilities, which were scheduled to mature on August 31, 2005 were unsecured, did not contain financial covenants, and were not guaranteed by the Company. These facilities were extended to, and paid in full on, December 16, 2005.

*Early Extinguishment of Senior Notes*

On November 26, 2002, the Company completed a private placement of \$220,000 in aggregate principal of Senior Notes. The offering consisted of \$29,000 of 5.95% Series A Notes due November 2005, \$46,000 of 6.43% Series B Senior Notes due November 2006 and \$145,000 of 6.71% Series C Senior Notes due November 2007. The Senior Notes restricted the Company's ability to incur additional indebtedness and required the Company to maintain certain

levels of fixed charge coverage and net worth, while limiting its

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

leverage ratio to certain levels. The proceeds from the sale of these Senior Notes were used to repay a \$220,000 short-term revolving credit facility entered into for the purpose of funding a portion of the acquisition cost of BE Germany. In December 2004, the entire \$220,000 of Senior Notes was prepaid, using proceeds from the Company's sale of its Subordinated Debentures (see above). Due to the prepayment, the Company recorded in 2004 a loss on the early extinguishment of debt of \$22,617, which represented the make whole premium, unamortized debt issuance costs and fees.

**7. Accrued Payroll and Employee Benefits**

Accrued payroll and employee benefits consist of the following:

	<b>December 31,</b>	
	<b>2006</b>	<b>2005</b>
Accrued compensated absences	\$ 97,123	\$ 91,587
Payroll related taxes	30,482	38,089
Employee mobility and tax equalization	87,621	82,482
Accrued bonus	52,501	32,782
Other	76,988	64,570
Total	\$ 344,715	\$ 309,510

**8. Other Current Liabilities**

Other current liabilities consist of the following:

	<b>December 31,</b>	
	<b>2006</b>	<b>2005</b>
Acquisition obligation (see Note 9)	\$ 16,564	\$ 16,133
Book overdrafts		810
Accrual for loss contracts	24,828	77,920
Other	94,445	74,761
Total	\$ 135,837	\$ 169,624

**9. Acquisition Obligation**

On May 27, 1999, KPMG LLP (the Company's former parent) acquired all of the voting common stock of Softline Consulting & Integrators, Inc. (Softline), a systems integration company, and entered into an agreement to acquire all of the Softline nonvoting common stock for not less than \$65,000. The \$65,000 acquisition obligation for the non-voting common stock of Softline accrued interest at 6% per annum, and was due by its terms at the earlier of a



demand by a majority vote of the nonvoting shareholders, or May 8, 2000. The obligation became due on May 8, 2000 but was not retired at such time. In August 2000, the Company and the counterparties to this agreement entered into an agreement, pursuant to which \$33,980 of this obligation was repaid in cash, \$7,020 was retired through the cancellation of short-term notes due from the counterparties and \$9,000 was settled in November 2000 (\$3,000 in cash and 326,024 shares of the Company's common stock). The remaining obligation of \$15,000 plus interest at 6% per annum, included in other current liabilities, is payable upon the ultimate resolution of specific contingencies relating to the Softline acquisition and will be paid through the issuance of shares of the Company's common stock, valued

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

for such settlement purposes at the IPO price less the underwriting discount or, at the election of the counterparties, through the issuance of cash equal to the current market price of the Company's common stock for up to 30% of the shares otherwise issuable, with the remainder payable in shares valued at the IPO price. The 30% portion of the liability that, at the election of the counterparties, can be settled in either cash or in shares of the Company's common stock represents a derivative feature. Accordingly, the 30% portion of the liability is marked to market each reporting period based on the changes in the intrinsic value of the underlying equity shares. Any change in the value of the underlying shares is recorded as a component of interest expense, amounting to \$430, \$354, and \$909 for the years ended December 31, 2006, 2005 and 2004, respectively.

**10. Collaboration Agreement**

In August 1997, KPMG LLP entered into a collaboration agreement with Microsoft Corporation. Under this agreement, the Company developed a broad portfolio of services and solutions to enable the rapid deployment of Microsoft products. Microsoft paid the Company \$15,000. The agreement requires the Company to train a specified number of consultants to be proficient in Microsoft products, and to participate in joint marketing efforts with Microsoft. Revenue of \$5,000 was recognized as training and other costs associated with the agreement were incurred. Revenue was not recognized for the remaining \$10,000 due to a minimum royalty liability of \$10,000 associated with the agreement. The agreement requires the Company to pay Microsoft royalties on certain net revenue for business relating to Microsoft products. The royalty period ends on the earlier of the date on which the Company makes the minimum aggregate royalty payment of \$10,000 or June 30, 2006. Since the aggregate payments on June 30, 2006 were less than \$10,000, the Company was obligated to make final payment for the difference, of which \$4,689 was paid in July 2006 and the remaining \$4,689 is due on June 30, 2007. No royalty payments were made during the years ended December 31, 2005 and 2004.

**11. Commitments and Contingencies**

The Company currently is a party to a number of disputes which involve or may involve litigation or other legal or regulatory proceedings. Generally, there are three types of legal proceedings to which the Company has been made a party:

Claims and investigations arising from its continuing inability to timely file periodic reports under the Exchange Act (the Exchange Act), and the restatement of its financial statements for certain prior periods to correct accounting errors and departures from generally accepted accounting principles for those years ( SEC Reporting Matters );

Claims and investigations being conducted by agencies or officers of the U.S. Federal government and arising in connection with its provision of services under contracts with agencies of the U.S. Federal government ( Government Contracting Matters ); and

Claims made in the ordinary course of business by clients seeking damages for alleged breaches of contract or failure of performance, by current or former employees seeking damages for alleged acts of wrongful termination or discrimination, and by creditors or other vendors alleging defaults in payment or performance ( Other Matters ).

The Company currently maintains insurance in types and amounts customary in its industry, including coverage for professional liability, general liability and management and director liability. Based on management's current assessment and insurance coverages believed to be available, the Company believes that

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

its financial statements include adequate provision for estimated losses that are likely to be incurred with regard to all matters of the types described above.

**SEC Reporting Matters**

*2005 Class Action Suits*

In and after April 2005, various separate complaints were filed in the U.S. District Court for the Eastern District of Virginia alleging that the Company and certain of its current and former officers and directors violated Section 10(b) of the Exchange Act, Rule 10b-5 promulgated thereunder and Section 20(a) of the Exchange Act by, among other things, making materially misleading statements between August 14, 2003 and April 20, 2005 with respect to its financial results in the Company's SEC filings and press releases. On January 17, 2006, the court certified a class, appointed class counsel and appointed a class representative. The plaintiffs filed an amended complaint on March 10, 2006 and the defendants, including the Company, subsequently filed a motion to dismiss that complaint, which was fully briefed and heard on May 5, 2006. The Company was awaiting a ruling when, on March 23, 2007, the court stayed the case, pending the U.S. Supreme Court's decision in the case of *Makor Issues & Rights, Ltd v. Tellabs*, argued before the Supreme Court on March 28, 2007. On June 21, 2007, the Supreme Court issued its opinion in the *Tellabs* case, holding that to plead a strong inference of a defendant's fraudulent intent under the applicable federal securities laws, a plaintiff must demonstrate that such an inference is not merely reasonable, but cogent and at least as compelling as any opposing inference of non-fraudulent intent. The Supreme Court decision is expected to significantly inform the court's decision regarding the complaint and the Company's motion to dismiss the complaint. It is not possible to predict with certainty whether or not the Company will ultimately be successful in this matter or, if not, what the impact might be. Accordingly, no liability has been recorded.

*2005 Shareholders' Derivative Demand*

On May 21, 2005, the Company received a letter from counsel representing one of its shareholders requesting that the Company initiate a lawsuit against its Board of Directors and certain present and former officers of the Company, alleging breaches of the officers' and directors' duties of care and loyalty to the Company relating to the events disclosed in its report filed on Form 8-K, dated April 20, 2005. On January 21, 2006, the shareholder filed a derivative complaint in the Circuit Court of Fairfax County, Virginia, that was not served on the Company until March 2006. The shareholder's complaint alleged that his demand was not acted upon and alleged the breach of fiduciary duty claims previously stated in his demand. The complaint also included a non-derivative claim seeking the scheduling of an annual meeting in 2006. On May 18, 2006, following an extensive audit committee investigation, the Company's Board of Directors responded to the shareholder's demand by declining at that time to file a suit alleging the claims asserted in the shareholder's demand. The shareholder did not amend the complaint to reflect the refusal of his demand. The Company filed demurrers on August 11, 2006, which effectively sought to dismiss the matter related to the fiduciary duty claims. On November 3, 2006, the court granted the demurrers and dismissed the fiduciary claims, with leave to file amended claims. As a result of the Company's annual meeting of stockholders held on December 14, 2006, the claim seeking the scheduling of an annual meeting became moot. On January 3, 2007, the plaintiff filed an amended derivative complaint re-asserting the previously dismissed derivative claims and alleging that the Board's refusal of his demand was not in good faith. The Company's renewed motion to dismiss all remaining claims was heard on March 23, 2007 and no ruling has yet been entered.



**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

*Series B Debenture Suit*

On September 8, 2005, certain holders of the 2.75% Series B Debentures provided a purported Notice of Default to the Company based upon its failure to timely file certain of its SEC periodic reports due in 2005. Thereafter, these holders asserted that as a result, the principal amount of the Series B Debentures, accrued and unpaid interest and unpaid damages were due and payable immediately.

The indenture trustee for the Series B Debentures then brought suit against the Company and, on September 19, 2006, the Supreme Court of New York ruled on a motion that the Company was in default under the indenture for the Series B Debentures and ordered that the amount of damages be determined subsequently at trial. The Company believed the ruling to be in error and on September 25, 2006, appealed the court's ruling and moved for summary judgment on the matter of determination of damages.

After further negotiations, the Company and the relevant holders of its Series B Debentures entered into a First Supplemental Indenture (the First Supplemental Indenture) with The Bank of New York, as trustee, which amends the subordinated indenture governing the 2.50% Series A Debentures due in 2024 and the Series B Debentures. Concurrently, the Company and the relevant holders of the Series B Debentures lawsuit also agreed to discontinue the lawsuit.

The First Supplemental Indenture modifies the debentures to include: (i) a waiver of the Company's SEC reporting requirements under the subordinated indenture through October 31, 2008, (ii) the interest rate payable on all Series A Debentures increased from 3.00% per annum to 3.10% per annum until December 23, 2011, and (iii) adjustment of the interest rate payable on all Series B Debentures from 3.25% per annum to 4.10% per annum until December 23, 2014.

In order to address any possibility of a claim of cross-default, on November 2, 2006, the Company entered into a First Supplemental Indenture with The Bank of New York, as trustee, which amends the indenture governing the 5.0% Convertible Senior Subordinated Debentures due 2025. The supplemental indenture includes a waiver of the Company's SEC reporting requirements through October 31, 2007 and provides for further extension through October 31, 2008 upon the payment of an additional fee of 0.25% of the principal amount of the debentures. The Company paid to certain consenting holders of these debentures a consent fee equal to 1.00% of the outstanding principal amount of the debentures. In addition, on November 9, 2006, the Company entered into an agreement with the holders of the 0.50% Convertible Senior Subordinated Debentures due July 2010, pursuant to which the Company paid a consent fee equal to 1.00% of the outstanding principal amount of the debentures, in accordance with the terms of the purchase agreement governing the issuance of these debentures.

*SEC Investigation*

On April 13, 2005, pursuant to the same matter number as its inquiry concerning the Company's restatement of certain financial statements issued in 2003, the staff of the SEC's Division of Enforcement requested information and documents relating to the Company's March 18, 2005 Form 8-K. On September 7, 2005, the Company announced that the staff had issued a formal order of investigation in this matter. The Company subsequently has received subpoenas from the staff seeking production of documents and information including certain information and documents related to an investigation conducted by its Audit Committee. The Company continues to provide information and documents to the SEC as requested. The investigation is ongoing and the SEC is in the process of taking the testimony of a

number of its current and former employees, including one of its former directors.

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

In connection with the investigation by its Audit Committee, the Company became aware of incidents of possible non-compliance with the Foreign Corrupt Practices Act and its internal controls in connection with certain of its operations in China and voluntarily reported these matters to the SEC and U.S. Department of Justice in November 2005. Both the SEC and the Department of Justice are investigating these matters in connection with the formal investigation described above. On March 27, 2006, the Company received a subpoena from the SEC regarding information related to these matters. The Company has a reasonable possibility of loss in this matter, although no estimate of such loss can be determined at this time. Accordingly, no liability has been recorded.

**Government Contracting Matters**

*Government Contracts*

A significant portion of the Company's business relates to providing services under contracts with the U.S. Federal government or state and local governments, inclusive of government-sponsored enterprises. During the year ended December 31, 2006, 36.0% of the Company's revenue was earned from contracts with the U.S. Government or state and local governments. These contracts are subject to extensive legal and regulatory requirements and, from time to time, agencies of the U.S. Federal government or state and local governments investigate whether the Company's operations are being conducted in accordance with these requirements and the terms of the relevant contracts. In the ordinary course of business, various government investigations are ongoing. U.S. Federal government investigations of the Company, whether relating to these contracts or conducted for other reasons, could result in administrative, civil or criminal liabilities, including repayments, fines or penalties being imposed upon the Company, or could lead to suspension or debarment from future U.S. Federal government contracting. The Company believes that it has adequately reserved for any losses it may experience from these investigations. Whether such amounts could have a material effect on the results of operations in a particular quarter or fiscal year cannot be determined at this time.

*California Subpoena*

In December 2004, the Company was served with a subpoena by the Grand Jury for the United States District Court for the Central District of California. The subpoena sought records relating to twelve contracts between the Company and the U.S. Federal government, including two General Service Administration (GSA) schedules, as well as other documents and records relating to its U.S. Federal government work. The Company has produced documents in accordance with an agreement with the Assistant U.S. Attorney. The focus of the review is upon its billing and time/expense practices, as well as alliance agreements where referral or commission payments were permitted. In July 2005, the Company received a subpoena by the U.S. Army related to Department of Defense contracts. The Company subsequently was served with subpoenas issued by the inspectors general of the GSA and the Department of Defense. The subpoenas were largely duplicative of the grand jury subpoena. In December 2006, the Company's counsel was informally informed by the Assistant U.S. Attorney involved in this matter that the government has declined to pursue any criminal proceedings arising out of this matter. The government continues to pursue the investigation on the civil side. The Company does not believe that it is either probable that the subpoena will result in a liability to the Company or that the amount or range of a future liability, if any, can be determined. Accordingly, no liability has been recorded.



**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

*Travel Rebate Investigation*

In December 2005, the Company executed a settlement agreement with the Civil Division of the U.S. Department of Justice to settle allegations of potential understatement of travel credits to government contracts. Pursuant to the settlement agreement, in December 2005, the Company paid \$15,500 in the aggregate, including related fees. The settlement payment is included as part of selling, general and administrative expenses in the Consolidated Statement of Operations for the year ended December 31, 2004.

*Department of Interior*

On September 29, 2005, the Company received a Termination for Cause notice (the Notice) directing it to cease work on a task order (Task Order 3) being completed for the Department of Interior (DOI). The Company complied and has properly reserved any outstanding amounts owed to it by the DOI as of December 31, 2004. The underlying Basic Purchase Agreement was subsequently terminated for cause as well, though the only task order that was potentially affected was Task Order 3. In the Notice, the DOI also stated that it may seek to recover excess procurement costs or pursue other legal remedies, but it has taken no action in this regard. The Company believes that it has a strong defense of excusable delay, and believes that where there is a meritorious case of excusable delay, terminations for cause have been overturned. The Company also believes that if the termination for cause is removed, any potential procurement cost liability is also removed. On July 28, 2006, the Company submitted a claim in the amount of approximately \$20,000 to the Government for amounts it believes are owed to it by the DOI. In January 2007, the DOI's contracting officer denied the Company's administrative claim for the payment of its unpaid fees. In addition, in September 2006, the Company filed a lawsuit against the DOI in the U.S. Court of Federal Claims, seeking to overturn the termination for cause. On April 30, 2007, the U.S. Court of Federal Claims granted the Company's motion to dismiss the lawsuit, holding that the DOI's termination for default was procedurally invalid. The DOI may appeal this decision. The only remaining claim in this matter is the Company's claim against the DOI for unpaid project fees, in part for wrongful termination. The Company intends to appeal the contracting officer's denial of its claim for the payment of unpaid fees.

*United States Agency for International Development Contract*

On October 25, 2005, the Company received a letter from *United States Agency for International Development* in which the Contracting Officer stated that she had determined to disallow approximately \$10,746 in subcontractor costs for Kroll, the Company's security subcontractor in Iraq. The Company also received a final decision from the Contracting Officer, dated January 7, 2006, disallowing the Kroll costs. However, on July 10, 2006, based on review and analysis of additional documentation, the Contracting Officer issued a revised final decision that allowed \$10,320 of the costs, while disallowing the remainder, which the Company substantially recovered from Kroll.

*Core Financial Logistics System*

There is an ongoing investigation of the Core Financial Logistics System (CoreFLS) project by the Inspector General's Office of the Department of Veterans Affairs and by the Assistant U.S. Attorney for the Central District of Florida. To date, the Company has been issued three subpoenas, in June 2004, December 2004 and May 2006, seeking the production of documents relating to the CoreFLS project. The Company is cooperating with the investigation and has

produced documents in response to the subpoenas. To date, there have been no specific allegations of criminal or fraudulent conduct on the Company's part or any contractual claims filed against it by the Veterans Administration in connection with the project. The Company continues

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

to believe it has complied with all of its obligations under the CoreFLS contract. It cannot, however, predict the outcome of the inquiry. It is not possible to predict with certainty whether or not the Company will ultimately be successful in this matter or, if not, what the impact might be. As such, no liability has been recorded.

*General Services Administration Audit*

The Office of the Inspector General of the GSA of the United States Government conducted an audit of the Company's GSA Management, Organizational, and Business Improvement Services ( MOBIS ) contract for the period beginning January 1, 2001 through December 31, 2002. The findings from this audit report allege non-compliance, which may have resulted in overcharges to Government customers. Specifically, the report alleges that the Company failed to report and pass on to GSA customers, the reduction it made to its commercial labor rate (Standard Bill Rate) for Administrative Support effective July 1, 2000. On March 6, 2007, the Contracting Officer specified a demand of \$2,318 against the Company, along with certain demand for price reductions.

While the Company continues to believe that it has not overcharged the Government, the Company has entered into settlement discussions with the Government in order to mutually resolve this matter. As part of these discussions, the Company is discussing revisions to the contract with the Contracting Officer to better align its terms, including pricing, to the expectations of both parties. Given the current stage of discussions, the outcome cannot yet be determined and management estimates the probable amount of loss is \$1,200 (accrued as a liability as of December 31, 2006 and 2005).

**Other Matters**

*Peregrine Litigation*

The Company was named as a defendant in several civil lawsuits regarding certain software resale transactions with Peregrine Systems, Inc. during 1999 and 2001, in which purchasers and other individuals who acquired Peregrine stock alleged that the Company participated in or aided and abetted a fraudulent scheme by Peregrine to inflate Peregrine's stock price. The Company was also sued by a trustee succeeding the interests of Peregrine for the same conduct. In December 2005, the Company executed conditional settlement agreements whereby it was released from liability in these matters and in all claims for indemnity by KPMG in each of these cases. The Company issued settlement payments of approximately \$36,900 with respect to these matters in September 2006. In addition, on January 5, 2006, the Company finalized an agreement with KPMG, providing conditional mutual releases to each other from fee advancement and indemnification claims with respect to these matters, with no settlement payment or other exchange of monies between the parties.

The Company did not settle the *In re Peregrine Systems, Inc. Securities Litigation*, and on January 19, 2005, the matter was dismissed by the trial court as it relates to the Company. The plaintiffs have appealed the dismissal and briefing of the appeal has been completed. To the extent that any judgment is entered in favor of the plaintiffs against KPMG, KPMG has notified the Company that it will seek indemnification for any such sums. The Company disputes KPMG's entitlement to any such indemnification.

On November 16, 2004, Larry Rodda, a former employee, pled guilty to one count of criminal conspiracy in connection with the Peregrine software resale transactions that continue to be the subject of the government inquiries.

Mr. Rodda also was named in a civil suit brought by the SEC. The Company was not named in the indictment or civil suit, and are cooperating with the government investigations.

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

*Hawaiian Telcom Communications, Inc.*

The Company had a significant contract (the HT Contract ) with Hawaiian Telcom Communications, Inc., a telecommunications industry client, under which the Company was engaged to design, build and operate various information technology systems for the client. The Company incurred losses of approximately \$28,191 and \$111,690 under this contract in 2006 and 2005, respectively. The HT Contract experienced delays in its build and deployment phases and contractual milestones were missed. The client alleged that the Company was responsible to compensate it for certain costs and other damages incurred as a result of these delays and other alleged failures. The Company believed the client's nonperformance of its responsibilities under the HT Contract caused delays in the project and impacted its ability to perform, thereby causing it to incur significant damages. On February 8, 2007, the Company entered into a Settlement Agreement, and Transition Agreement with the client. Pursuant to the Settlement Agreement, the Company paid \$52,000, \$38,000 of which was paid by certain of its insurers. In addition, the Company waived approximately \$29,600 of invoices and other amounts otherwise payable by the client to the Company. The Transition Agreement governed its transitioning of the remaining work under the HT Contract to a successor provider, which has been completed and accepted by the client.

*Telecommunications Company*

A telecommunications industry client initiated an audit of certain of the Company's time and expense charges, alleging that the Company inappropriately billed the client for days claimed to be non-work days, such as days before and after travel days, travel days, overtime, and other alleged errors. A preliminary audit by the Company of the time and expense records for the project did not reveal the improprieties as alleged. On June 18, 2007, the Company and the client entered into a settlement resolving the client's claims. In connection with the settlement, the Company will make six equal annual payments to the client in an aggregate amount of \$24,000, with the first payment made on the signing date in return for a full release of the client's claims.

*Michael Donahue*

In March 2005, Mr. Donahue filed suit against the Company in connection with the termination of his employment in February 2005. Mr. Donahue alleges he is owed \$3,000 under the terms and conditions of a Special Termination Agreement he executed in November 2001, between \$1,700 and \$2,400 as compensation for the value of stock options he was required to forfeit as the result of his discharge, and an additional \$200 for an unpaid bonus. Mr. Donahue has also argued that a 25% penalty pursuant to Pennsylvania law should be added to each of these sums. In May 2005, the Company removed the matter to Federal court. On October 5, 2005, Mr. Donahue filed his Complaint in Federal Court, under seal. In this Complaint, in response to the Company's motion to compel arbitration, Mr. Donahue dropped his claims for his stock options and performance bonus, although he is free to bring those claims again at a later time. On January 31, 2006, Mr. Donahue filed his Demand for Arbitration, asserting all the claims he originally asserted, including his claims under the Special Termination Agreement, his claims for his stock options, and his claim for his annual bonus payment for 2004, in addition to the statutory penalties sought for these unpaid amounts. The parties have selected arbitrators for the panel, and discovery has commenced. It is reasonably possible that the Company will incur a loss ranging from \$0 to \$7,000, with no amount within this range a better estimate than any other amount. Accordingly, no liability has been recorded.

*Canon Australia*

On June 16, 2006, employees of the Australian subsidiary of Canon presented objections to the

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Company's Australian Country Director related to deficiencies in the Company's work and alleged misrepresentations by the Company in connection with an implementation of an enterprise resource planning and customer relationship management system, which went live in January of 2005. Canon representatives presented arguments supporting their belief that Canon has suffered damages, including damages for lost profits and other consequential damages, as a result of the implementation. Canon has indicated that it may proceed with a claim, although the Company has not received any formal notice of any such claim. This matter is in its very preliminary stages. The contract limits the damages that may be claimed against the Company to no more than approximately \$22,800. It is reasonably possible the Company will incur a loss. Due to the early stage of this matter and the nature of the potential claims, a range of loss cannot be determined at this time. Accordingly, no liability has been recorded.

*Transition Services Provided By KPMG LLP*

KPMG LLP contended that the Company owes approximately \$26,214 in termination costs and unrecovered capital for the termination of information technology services provided under the transition services agreement (see Note 15, Transactions with KPMG LLP). However, in accordance with the terms of the agreement, the Company did not believe that it was liable for termination costs arising upon the expiration of the agreement. In addition, KPMG LLP contended the Company owed an additional \$5,347 in connection with the expiration of the transition services agreement relating to its share of occupancy related assets in subleased offices from KPMG LLP.

In May 2007, the Company and KPMG LLP settled its disputes under the transition services agreement. KPMG LLP released all claims against the Company. In connection with the settlement, the Company amended certain real estate documents relating to a number of properties that it currently sublets from KPMG LLP to either allow it to further sublease these properties to third parties, or to return certain properties the Company no longer utilizes to KPMG LLP, in return for a reduction of the amount of the Company's sublease obligations to KPMG LLP for those properties. The Company also agreed to pay \$5,000 over three years to KPMG LLP as part of the settlement.

**Operating Leases**

The Company leases all of its office facilities under various operating leases, some of which contain escalation clauses. In addition, the Company leases certain of its office facilities under subleases with KPMG LLP. Subleases with KPMG LLP are for periods that coincide with the KPMG LLP lease periods, which run through 2014. The rental cost is based on square footage utilized by the Company.

The following is a schedule of future minimum rental payments required under operating leases that have initial or remaining non-cancelable lease terms in excess of one year as of December 31, 2006. Total minimum rental payments are exclusive of future minimum sublease income of \$19,811.

**Year ending December 31:**

2007	\$ 75,472
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2008	70,789
2009	62,617
2010	44,135
2011	31,694
Thereafter	65,038
Total minimum payments required	\$ 349,745

Total rental expense for all operating leases was \$61,490, \$64,734 and \$66,186 for the years ended December 31, 2006, 2005 and 2004, respectively.

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

**Other Commitments**

In the normal course of business, the Company has indemnified third parties and has commitments and guarantees under which it may be required to make payments in certain circumstances. The Company accounts for these indemnities, commitments and guarantees in accordance with FIN No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. These indemnities, commitments and guarantees include: indemnities to third parties in connection with surety bonds; indemnities to various lessors in connection with facility leases; indemnities to customers related to intellectual property and performance of services subcontracted to other providers; and indemnities to directors and officers under the organizational documents and agreements of the Company. The duration of these indemnities, commitments and guarantees varies, and in certain cases, is indefinite. Certain of these indemnities, commitments and guarantees do not provide for any limitation of the maximum potential future payments the Company could be obligated to make. The Company estimates that the fair value of these agreements was minimal. Accordingly, no liabilities have been recorded for these agreements as of December 31, 2006.

Some clients, largely in the state and local market, require the Company to obtain surety bonds, letters of credit or bank guarantees for client engagements. As of December 31, 2006, the Company had approximately \$101,912 of outstanding surety bonds and \$89,300 of outstanding letters of credit for which the Company may be required to make future payment.

**12. Stockholders' Equity**

*Notes Receivable from Stockholders*

On February 16, 2000, the Company issued stock awards aggregating 297,324 shares to certain employees as part of the separation of KPMG LLP's consulting businesses. In connection with these awards, the Company also provided loans of \$7,433 to the grantees for personal income taxes attributed to the awards. The loans are secured by the shares of common stock issued to the employees and, prior to August 7, 2003, bore interest at 6.2% per annum with respect to \$5,845 of the principal amount and at 4.63% per annum with respect to \$1,588 of the principal amount. Principal and accrued interest on the loans are due no later than August 9, 2007. In the event the value of the Company's common stock is less than the aggregate principal and interest of the loans upon maturity in August 2007, the employees may elect to surrender their shares relating to the stock award. At December 31, 2006, the estimated fair market value of the stock awards was approximately \$2,340.

In October 2001, the Company provided non-recourse loans to individuals who were executive officers at that time of \$1,672, at an interest rate of 4.5%. During 2005, one loan totaling \$483, which included \$62 of accrued interest, was forgiven by the Company. During 2006, the Company forgave the remaining loan that had been fully reserved as of December 31, 2005 and had a balance of \$116, including \$21 of accrued interest.

*Common Stock Repurchase*

In July 2001, the Board of Directors authorized the Company to repurchase up to \$100,000 of its common stock, and in April 2005, the Board of Directors authorized a stock repurchase program for an additional \$100,000 for common

stock repurchases to be made over a twelve-month period beginning on April 11, 2005. The Company did not repurchase shares during this twelve-month period and the April 2005

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

authorization has now expired. As of December 31, 2006, the Company has repurchased 3,812,250 shares of its common stock at an aggregate purchase price of \$35,727 and is authorized to repurchase an additional \$64,273 of its common stock. The Company did not repurchase any of its common stock during the years ended December 31, 2006, 2005 and 2004. The repurchased shares are held in treasury. In addition, the 2007 Credit Facility contains limitations on the Company's ability to repurchase shares of its common stock.

*Preferred Stock*

The Company has 10,000,000 authorized shares of \$0.01 par value preferred stock. An aggregate of 1,000,000 shares of preferred stock have been designated as Series A Junior Participating Preferred Stock for issuance in connection with the Company's shareholder rights plan. As of December 31, 2006, none of the Company's preferred stock was issued or outstanding.

*Shareholder Rights Plan*

On August 29, 2001, the Board of Directors of the Company adopted a shareholder rights plan. Under the plan, a dividend of one preferred share purchase right (a Right) was declared for each share of common stock of the Company that was outstanding on October 2, 2001. Each Right entitles the holder to purchase from the Company one one-thousandth of a share of a new series of Series A Junior Participating Preferred Stock at a purchase price of \$90, subject to adjustment.

The Rights will trade automatically with the common stock and will not be exercisable until a person or group has become an acquiring person by acquiring 15% or more of the Company's outstanding common stock, or a person or group commences a tender offer that will result in such a person or group owning 15% or more of the Company's outstanding common stock. Upon announcement that any person or group has become an acquiring person, each Right will entitle all rightholders (other than the acquiring person) to purchase, for the exercise price of \$90, a number of shares of the Company's common stock having a market value equal to twice the exercise price. Rightholders would also be entitled to purchase common stock of the acquiring person having a value of twice the exercise price if, after a person had become an acquiring person, the Company were to enter into certain mergers or other transactions. If any person becomes an acquiring person, the Board of Directors may, at its option and subject to certain limitations, exchange one share of common stock for each Right.

The Rights have certain anti-takeover effects, in that they would cause substantial dilution to a person or group that attempts to acquire a significant interest in the Company on terms not approved by the Board of Directors. In the event that the Board of Directors determines a transaction to be in the best interests of the Company and its stockholders, the Board of Directors may redeem the Rights for \$0.01 per share at any time prior to a person or group becoming an acquiring person. The Rights will expire on October 2, 2011.

**13. Stock-Based Compensation**

*Long-Term Incentive Plan*

On January 31, 2000, the Company adopted the 2000 Long-Term Incentive Plan (LTIP) pursuant to which the Company is authorized to grant stock options and other awards to its employees and directors.

On December 14, 2006, the plan was amended for certain changes and clarifications. These changes included a 25.0 million share increase in the number of shares authorized for equity awards made under the

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

plan; the elimination of an evergreen formula used to determine the number of shares available under the plan by reference to a certain percentage of the Company's total shares outstanding; revisions that allow awards made to the most senior executives under the plan to qualify as performance-based compensation under Section 162(m) of the Internal Revenue Code (the Code); and revisions to comply with Section 409A of the Code that will minimize the risk of excise taxes being levied on plan participants in connection with changes to the vesting, settlement, or delivery of shares under the awards.

As of December 31, 2006, the LTIP had 92,179,333 shares of common stock that were authorized for grants or awards in the form of stock options, restricted stock awards, RSUs or performance share units (PSUs) (collectively stock units).

Stock options are granted with an exercise price equal to the common stock's fair market value at the date of grant. Generally, stock options granted have 10-year contractual terms and vest over three to four years from the date of grant. Stock-based awards may be issued under the LTIP for consideration as determined by the Compensation Committee of the Board of Directors. As of December 31, 2006, the Company had stock options, restricted stock awards, and RSUs outstanding.

Activity for stock awards and options granted under the LTIP during the year ended December 31, 2006 was as follows:

	<b>Options/Shares</b>	<b>Options Outstanding</b>	
	<b>Available for Grant</b>	<b>Number</b>	<b>Weighted Average Price per Share</b>
Balance at December 31, 2005 (1)	7,609,567	45,676,141	\$ 11.33
Additional shares authorized	25,000,000		
Options granted	(600,400)	600,400	8.70
Options exercised			
Options forfeited	10,239,263	(10,239,263)	11.99
Restricted stock and stock unit awards, net of forfeitures	(7,228,956)	n/a	8.56
Balance at December 31, 2006	35,019,474	36,037,278	\$ 11.10

(1) Options granted during the year ended December 31, 2005 include 2,000,000 non-statutory options issued outside of the LTIP.

The Company adopted the modified prospective transition method permitted under SFAS 123(R) and consequently has not adjusted results from prior years. Under the modified prospective transition method, compensation costs associated with awards for the year ended December 31, 2006 now include the expense relating to the remaining unvested awards granted prior to December 31, 2005 and the expense relating to any awards issued subsequent to December 31, 2005. For grants which vest based on certain specified performance criteria, the grant date fair value of

the shares is recognized over the requisite period of performance once achievement of criteria is deemed probable. For grants that vest through the passage of time, the grant date fair value of the award is recognized over the vesting period. The amount of stock-based compensation recognized during the period is based on the value of the portion of the award that is ultimately expected to vest. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The pre-tax effect of the change in accounting associated with the adoption of SFAS 123(R) was \$26,653 and the application of a forfeiture rate to compensation expense recognized in prior years was not considered significant for disclosure. The Consolidated Statement of Operations for the year ended December 31, 2006 includes stock-

**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

based compensation expense of \$53,393 related to stock option awards, restricted stock awards, RSUs, ESPP and BE an Owner programs.

The Company elected the alternative transition method as outlined in FASB Staff Position 123(R)-3, Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards, to calculate the pool of excess tax benefits available to absorb tax deficiencies recognized subsequent to the adoption of SFAS 123(R). There was no impact to the windfall tax benefit in 2006, as the Company was in a net operating loss carryforward position.

The after-tax stock-based compensation impact of adopting SFAS 123(R) for the year ended December 31, 2006 was \$25,709 and a \$0.12 per share reduction to earnings per share. Prior to the adoption of SFAS 123(R), the Company used the intrinsic value method of accounting prescribed by APB 25 and related interpretations, including FIN 44,

Accounting for Certain Transactions Involving Stock Compensation, for its plans. Under this accounting method, stock option awards that are granted with the exercise price at the current fair value of the Company's common stock as of the date of the award generally did not require compensation expense to be recognized in the Consolidated Statements of Operations.

As of December 31, 2006, unrecognized compensation costs and related weighted-average lives over which the costs will be amortized were as follows:

	<b>Unrecognized Compensation Costs</b>	<b>Weighted-Average Life in Years</b>
Stock options	\$ 11,052	1.7
Restricted stock and stock unit awards	41,153	3.1
ESPP	4,713	1.0
Total	\$ 56,918	2.6

The following table illustrates the proforma effect on net loss and loss per share had the Company applied the fair value recognition provisions of SFAS 123 for the Company's stock-based compensation plans for all of the periods shown:

	<b>Year Ended December 31,</b>	
	<b>2005</b>	<b>2004</b>
Net loss	\$ (721,643)	\$ (546,226)
Add back:	85,837	5,840

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Total stock based compensation expense recorded under intrinsic value method for all stock awards, net of tax effects

Deduct:

Total stock based compensation expense recorded under fair value method for all stock awards, net of tax effects

Pro forma net loss

Loss per share:

Basic and diluted as reported

Basic and diluted pro forma

(173,134) (88,690)

\$ (808,940) \$ (629,076)

\$ (3.59) \$ (2.77)

\$ (4.02) \$ (3.19)

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Certain of the Company's stock-based compensation awards continue to vest and do not accelerate vesting upon retirement or at the attainment of retirement eligibility, therefore, the requisite service period subsequent to attaining such eligibility is considered non-substantive. With the adoption of SFAS 123(R), the Company recognizes compensation expense related to stock-based awards granted on or after January 1, 2006 over the shorter of the requisite service period or the period to attainment of retirement eligibility. Certain awards granted to retirement-eligible employees prior to January 1, 2006 have not been accelerated and will continue to be amortized over their original vesting periods, until employment with the Company has terminated, at which point the compensation expense associated with any remaining unvested awards will be recognized. Had the Company adopted the retirement eligibility provisions of SFAS 123(R) to awards granted prior to January 1, 2006, the cumulative impact of the change in accounting would have been a reduction to expense of \$2,222 and \$2,716 in 2006 and 2005 (pro forma), respectively, and an increase to expense of \$2,703 in 2004 (pro forma).

The fair value of each option award was estimated on the date of grant using the Black-Scholes option pricing model. The expected volatility assumption of all grants issued prior to 2005 was primarily derived from the Company's historical volatility on its publicly traded common stock. Beginning in 2005, the Company determined the expected volatility of the options based on a blended average of the Company's historical volatility and the volatility from its peer group, due to on the limited trading experience of the Company and its current filing status. For 2006 awards, the expected life was approximated by averaging the vesting term and the contractual term in accordance with the simplified method described in SAB No. 107, Share-Based Payment. The risk-free interest rate is the yield currently available on U.S. Treasury zero-coupon issues with a remaining term approximating the expected life used as the input to the Black-Scholes model. The relevant data used to determine the value of the stock option grants, in the respective years, is as follows:

	<b>Stock Price Expected Volatility</b>	<b>Risk-Free Interest Rate</b>	<b>Expected Life</b>	<b>Expected Dividend Yield</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Grant Date Fair Value</b>
Year ended December 31, 2006	50.80%	4.69%	6		\$ 8.70	\$ 4.70
Year ended December 31, 2005	51.08%	4.10%	6		\$ 7.71	\$ 4.57
Year ended December 31, 2004	63.47%	3.65%	6		\$ 8.85	\$ 5.38

The grant date fair value of the Company's common stock purchased or expected to be purchased under the ESPP was estimated for the years ended December 31, 2006, 2005 and 2004 using the Black-Scholes option pricing model with an expected volatility ranging between 30% to 70%, risk free interest rates ranging from 1.03% to 3.29%, an expected life ranging from 6 to 24 months, and an expected dividend yield of zero. For the years ended December 31, 2006, 2005 and 2004, the weighted average grant date fair value of shares purchased under the ESPP was \$0, \$3.21, and \$3.43, respectively.

*Blackout Period*

On April 20, 2005, the Company sent notices to its directors and executive officers notifying them that in connection with the determination that investors should not rely upon certain previously-issued financial statements, and until the Company is current in its SEC periodic filings, the registration statements on Form S-8 covering the issuances of the Company's common stock under its LTIP and ESPP will not be available. ESPP participants would not be permitted to purchase the Company's common stock normally

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## BEARINGPOINT, INC.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

offered pursuant to the ESPP; and stock-based awards under the LTIP would not be settled, as the Company could not provide valid registration of shares delivered for resale. When these restrictions are lifted, the Company will settle the awards from the existing authorized share base.

Furthermore, on April 20, 2005, pursuant to Regulation BTR, the Company announced there would be a blackout period under the Company's 401(k) Plan with respect to purchases of Company stock. Effective as of September 14, 2006, the Company notified its directors, executive officers and employees, that it had amended the 401(k) Plan to permanently prohibit participant purchases and Company contributions of Company stock under the 401(k) Plan. As a result of this action, the blackout period under the 401(k) Plan ended effective as of September 14, 2006.

*Stock Option Plans*

The following table details the weighted-average remaining contractual life of options outstanding at December 31, 2006 by range of exercise prices:

Range of Exercise Price	Outstanding Options			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
	December 31, 2006			December 31, 2006	
\$ 0.00-\$ 5.54	300	5.7	\$ 5.46	300	\$ 5.46
\$ 5.55-\$11.10	25,201,799	6.7	\$ 8.85	21,125,913	\$ 9.02
\$11.11-\$16.64	5,043,219	4.8	\$ 13.26	5,043,219	\$ 13.26
\$16.65-\$27.75	5,647,196	4.0	\$ 18.03	5,647,196	\$ 18.03
\$49.95-\$55.50	144,764	3.0	\$ 55.50	144,764	\$ 55.00
	36,037,278(1)	6.0	\$ 11.10	31,961,392(1)(2)	\$ 11.49
Vested or expected to vest at December 31, 2006	35,718,395(1)	6.0	\$ 11.12		

(1) The aggregate intrinsic values for stock options outstanding, exercisable, and vested or expected to vest as of December 31, 2006 of \$1,885, \$1,333, and \$1,874, respectively, represent the total pre-tax intrinsic values based upon the Company's closing stock price of \$7.87 as of December 31, 2006 which would have been received by the option holders had all the in-the-money options been exercised as of that date.

(2) The weighted average remaining contractual life of stock options exercisable as of December 31, 2006 was 5.7 years.

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Options exercisable at December 31, 2005 and 2004 were 34,900,361 and 32,169,971, respectively, with a weighted average exercise price of \$12.33 and \$14.12, respectively.

The aggregate intrinsic value for stock options exercised during 2006, 2005 and 2004 was \$0, \$185, and \$515, respectively. The cash received in association with these exercises was \$0, \$1,127, and \$2,209, respectively. No stock options were exercised in 2006.

During 2005, 2.0 million stock options were granted with a measurement date market price that was above the grant date exercise price. As a result the Company recognized expense of \$466 for the year ended December 31, 2005.

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

On December 13, 2005, the Company accelerated the vesting of certain unvested and out-of-the-money stock options with exercise prices equal to or greater than \$9.57 per share previously awarded to its employees (excluding executive officers and directors) under the LTIP. The acceleration of vesting was effective for stock options outstanding as of December 13, 2005. Options to purchase approximately 2.9 million shares of common stock, or approximately 21% of the Company's outstanding unvested options, were subject to the acceleration. The weighted average exercise price of the options subject to the acceleration is \$10.39, and the exercise price of these options ranges from \$9.58 to \$21.17 per share, with approximately 93.7% and 99.9% of such options scheduled to vest in 2006 and 2007, respectively. The purpose of the acceleration was to enable the Company to avoid recognizing compensation expense associated with these options in future periods in its Consolidated Statements of Operations, upon adoption of SFAS 123(R). The Company believes that because the accelerated options had exercise prices in excess of the current market value of the Company's common stock, the options had limited economic value and were not achieving their original objective of incentive compensation and employee retention.

Total compensation expense recorded in 2006 for stock options was \$21,097.

*Restricted Stock Units*

On March 25, 2005, the Compensation Committee of the Company's Board of Directors approved the issuance of up to an aggregate of \$165,000 in RSUs under the LTIP to the Company's current managing directors (MDs) and a limited number of key employees, and delegated to the Company's officers the authority to grant these awards. The following table summarizes the RSU activity under this authorization in 2006 and 2005:

	<b>Number of RSUs</b>	<b>Weighted Average Grant Date Fair Value</b>
Outstanding at December 31, 2004		\$
Granted	13,764,793	7.61
Settled		
Forfeited	(496,528)	7.50
Outstanding at December 31, 2005	13,268,265	7.61
Granted	8,048,672	8.48
Settled		
Forfeited	(900,417)	7.80
Outstanding at December 31, 2006	20,416,520	\$ 7.93

The total fair value of RSUs that vested, net of forfeitures, in 2006 and 2005 was approximately \$26,280 and \$81,800, respectively. The vesting and settlement terms for the RSUs granted during 2006 are described below:

5,629,048 RSUs generally vest 25% on each January 1 of calendar years 2007 through 2010 and settle 25% per year starting January 1, 2009;

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

1,615,830 RSUs generally either cliff vest and settle three years from the grant date or vest and settle over two to four years from the grant date; and

803,794 RSUs vest immediately on the grant date, and generally settle on the grant date or settle over one to six years from the grant date.

Certain of these RSU awards have performance vesting criteria, for which the Company has determined achievement to be probable. None of the common stock equivalents underlying these RSUs are considered to be issued or outstanding common stock, as issuance is dependant on various vesting and settlement terms as noted above. In addition, settlement and issuance of any shares underlying these RSUs is delayed until the Company is current with its SEC periodic filings.

As of December 31, 2006, the Company had 20,416,520 RSUs outstanding (excluding approximately 140,934 RSUs awarded to recipients in China where local laws require a cash settlement) with a grant date weighted average fair value of \$7.93.

During the first quarter of 2007, the Company granted approximately 1.4 million (net of forfeitures) RSU awards. These RSUs had a grant date weighted average fair value of \$7.81 and generally either cliff vest and settle three years from the grant date or vest and settle over three to four years from the date of grant. The total compensation expense, net of forfeitures, associated with these RSUs that will be recorded over the vesting period is approximately \$10,957.

Also during the first quarter of 2007, the Compensation Committee of the Board of Directors of the Company, approved a program for the issuance of up to 25.0 million PSUs under the Company's amended and restated LTIP. Under the program, PSU awards were granted to certain managing directors and other high-performing senior-level employees. The PSU awards, each of which initially represents the right to receive at the time of settlement one share of the Company's common stock, will vest on December 31, 2009, subject to the achievement of performance-based metrics. Generally, for any PSU award to vest, two performance-based metrics must be achieved for the performance period beginning on (and including) February 2, 2007 and ending on (and including) December 31, 2009 (the Performance Period):

(i) the Company must first achieve a compounded average annual growth target in consolidated business unit contribution; and

(ii) total shareholder return (TSR) for shares of the Company's common stock must be at least equal to the 25th percentile of TSR of the Standard & Poor's 500 (the S&P 500) in order for any portion of the award to vest. Depending on the Company's TSR performance relative to those companies that comprise the S&P 500, the PSU awards will vest on December 31, 2009 at percentages varying from 0% to 250% of the number of PSU awards originally awarded.

An employee's continuous employment with the Company (except in cases of death, disability or retirement, or certain changes of control as defined in the agreements governing the PSU awards) is also required for vesting of a particular employee's PSU award. The PSU awards will be settled at various dates from 2010 through 2012. As of June 15, 2007,

the Company granted 22.4 million PSUs.

*Restricted Stock Awards*

During fiscal 2002, the Company granted 420,000 shares (unaudited) of restricted common stock, of

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

which 60,000 shares have been forfeited as of December 31, 2006. Holders of restricted stock have all the rights of other stockholders, subject to certain restrictions and forfeiture provisions; such restricted stock is considered to be issued and outstanding. The restrictions on these shares generally expire after three years. The market value of these shares was \$5,586 (unaudited), and was recorded as unearned compensation. These awards were fully vested prior to January 1, 2006. The compensation expense was \$0, \$0 and \$563 during the years ended December 31, 2006, 2005, and 2004, respectively.

Under the LTIP, the Company has the discretion to grant restricted stock to certain of its officers and employees. In connection with the various Andersen Business Consulting acquisitions, the Company committed to the issuance of approximately 3,000,000 shares of common stock (net of forfeitures) to former partners of those practices as a retentive measure. The stock awards have no purchase price and were issued as to one-third of the shares on the first three anniversaries of the acquisition of the relevant consulting practice, so long as the recipient remained employed by the Company. Compensation expense was recorded ratably over the three-year service period beginning in July 2002. Compensation expense was \$3,491 and \$8,723 for the years ended December 31, 2005 and 2004, respectively. In July 2005, the Company settled the third and final settlement of the stock award by paying the recipients \$4,929 in cash. This payment was recorded as a reduction to additional paid in capital. As of December 31, 2006 and 2005, 2,100,998 shares of common stock have been issued.

The Company grants restricted stock to non-employee members of the Board of Directors as annual grants under the LTIP, in connection with the Company's annual meeting of stockholders. The awards are fully vested upon grant, but are subject to transfer restrictions defined in the LTIP until the recipient is no longer a member of the Board of Directors. During each of the years ended December 31, 2006 and 2004, the Company granted 56,000 shares of restricted stock to non-employee directors. Since the Company did not hold its 2005 annual meeting of stockholders, no restricted stock awards were made to the Board of Directors in 2005. Total compensation expense recorded in 2006 and 2004 for these awards was \$460 and \$452, respectively.

In May 2007, the Board of Directors approved grants of an aggregate of 48,000 shares of restricted stock to its non-employee directors. The purpose of these grants was to provide additional compensation to non-employee directors for their service on the Board of Directors during 2005.

*Employee Stock Purchase Plan*

The Company's ESPP was adopted on October 12, 2000 and allows eligible employees to purchase shares of the Company's common stock at a discount, up to a maximum of \$25 at fair value, through accumulated payroll deductions of 1% to 15% of their compensation. Under the ESPP, shares of the Company's common stock were purchased at 85% of the lesser of the fair market value at the beginning of the 24 month offering period (the Look-Back Purchase Price), and the fair market value at the end of each six-month purchase period ending on July 31 and January 31, respectively. In 2005, the Board of Directors amended the ESPP to remove the 24-month Look-Back Purchase Price for all future offering periods under the ESPP. As amended, future offering periods will be a 6-month offering period and the purchase price for the Company's common stock will be calculated at a 15% discount from the closing price on the last day of the 6-month offering period. The purchase price of the Company's common stock for the purchase period in effect at the time of such amendment was grandfathered from this change (i.e., the purchase price was the lower of the Look-Back Purchase Price and the fair market value at the end of the purchase period) (the Grandfathered Offering Period). On April 18, 2007, the Board of Directors amended the ESPP to eliminate the

Look-Back Purchase

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Price for the Grandfathered Offering Period. As amended, the purchase price for the Grandfathered Offering Period will be 85% of the fair market value of the Company's common stock at the end of the Grandfathered Offering Period. During the years ended December 31, 2006, 2005 and 2004, employees purchased a total of 0, 2,053,154 and 3,644,002 shares for \$0, \$13,769 and \$24,707, respectively. As of December 31, 2006, 23,749,276 shares of common stock remained available for issuance under the ESPP. Employee contributions to the ESPP held by the Company were approximately \$21,240 at December 31, 2006. These amounts are included in cash and cash equivalents and are repayable on demand.

In June 2005, the Company announced that certain employees below the managing director level were eligible to participate in its BE an Owner Program. Under this program, as amended, the Company made a cash payment in January 2006 to each eligible employee in an amount equal to 1.5% of that employee's annual salary as of October 3, 2005 (which payment was approximately \$18,456 in the aggregate). The Company intends to make, when it has become current in its SEC periodic filings, a special contribution under the ESPP to each eligible employee in an amount equal to 1.5% of that employee's annual salary as of October 3, 2005 into his or her ESPP account, which contribution will be used to purchase shares of the Company's common stock at a 15% discount.

The 15% discount offered to employees under these plans represents a cost to the Company that must be recognized in the Consolidated Condensed Statements of Operations in accordance with SFAS 123(R). As a result, compensation expense of \$5,557 was recognized for the year ended December 31, 2006. For the years ended December 31, 2005 and 2004, approximately \$11,857 and \$15,976 was included in the pro forma disclosure for compensation expense under SFAS 123.

**14. Income Taxes**

The Company reported a loss before taxes of \$181,043, including net foreign income of \$13,495, for the year ended December 31, 2006. The Company reported a loss before taxes of \$599,522, including net foreign losses of \$173,046, for the year ended December 31, 2005. The Company reported a loss before taxes of \$534,435, including net foreign losses of \$430,180, for the year ended December 31, 2004.

**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

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

	<b>Year Ended December 31, 2006</b>	<b>Year Ended December 31, 2005</b>	<b>Year Ended December 31, 2004</b>
Current:			
Federal	\$ 4,855	\$ 7,437	\$ (33,988)
State and local	1,199	1,400	(11,669)
Foreign	27,648	58,335	14,062
Total current	33,702	67,172	(31,595)
Deferred:			
Federal		40,242	8,930
State and local		15,045	267
Foreign	(1,305)	(338)	34,189
Total deferred	(1,305)	54,949	43,386
Total	\$ 32,397	\$ 122,121	\$ 11,791

The following table presents the principal reasons for the difference between the effective income tax rate on income from continuing operations and the U.S. Federal statutory income tax rate:

	<b>Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
U.S. federal statutory income tax rate	35.0%	35.0%	35.0%
Nondeductible goodwill impairment	0.0%	(6.9%)	(25.3%)
Change in valuation allowance	(40.2%)	(37.2%)	(4.6%)
Foreign taxes	2.1%	(2.3%)	0.2%
Nondeductible meals and entertainment expense	(4.3%)	(1.1%)	(1.3%)
State taxes, net of federal benefit	3.7%	2.1%	1.0%
Impact of foreign recapitalization	(3.0%)	(5.5%)	(3.6%)
Income tax reserve	(4.6%)	(3.1%)	(1.5%)
Non-deductible interest	(2.1%)	(0.5%)	(0.5%)
Foreign dividends	(2.6%)	(0.5%)	0.0%
Other, net	(1.9%)	(0.4%)	(1.6%)

Effective income tax rate	(17.9%)	(20.4%)	(2.2%)
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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

The temporary differences that give rise to a significant portion of deferred income tax assets and liabilities are as follows:

	<b>December 31, 2006</b>	<b>December 31, 2005</b>
Deferred income tax assets:		
Net operating loss carryforwards	\$ 263,531	\$ 196,996
Accrued compensation	33,329	32,297
Reserve for claims	23,323	15,141
Revenue recognition	35,977	37,140
Restricted stock units	41,954	26,821
Other	57,899	68,788
Total gross deferred income taxes	456,013	377,183
Less valuation allowance	(408,149)	(338,792)
Total net deferred income tax assets	47,864	38,391
Deferred income tax liabilities:		
Property and equipment	13,416	23,642
Other	245	313
Foreign currency translation	10,184	5,088
Stock-based compensation	2,828	2,413
Total deferred income tax liabilities	26,673	31,456
Net deferred income tax asset	\$ 21,191	\$ 6,935

These deferred tax assets and liabilities are presented on the Consolidated Balance Sheets as follows:

	<b>December 31, 2006</b>	<b>December 31, 2005</b>
Current deferred tax assets	\$ 7,621	\$ 18,991
Non-current deferred tax assets	41,663	20,915
Current deferred tax liabilities	(20,109)	(10,095)
Non-current deferred tax liabilities	(7,984)	(22,876)

\$	21,191	\$	6,935
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The Company has U.S. net operating loss carryforwards at December 31, 2006 of approximately \$341,209, which expire at various dates beginning in 2010 through 2026. The utilization of these net operating loss carryforwards are subject to limitations. The Company believes that it is more likely than not these net operating loss carryforwards will not be utilized. The Company had U.S. capital loss carryforwards of approximately \$15,296, which expired in 2006. The Company also has foreign net operating loss carryforwards at December 31, 2006 of approximately \$437,981, which expire at various dates between 2007 and 2026 and \$216,106 that carryforward indefinitely as provided by the applicable foreign law. A valuation allowance has been recorded due to the uncertainty of the recognition of certain deferred tax assets, primarily

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**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
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the net operating loss carryforwards of U.S., state, and certain foreign subsidiaries, and the capital loss carryforwards of certain U.S. entities. The net changes in the valuation allowance for the years ended December 31, 2006, 2005 and 2004 were \$69,357, \$224,017, and \$26,738, respectively.

A valuation allowance is provided to offset any deferred tax assets if, based upon the available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. The Company's valuation allowance of \$408,149 and \$338,792 as of December 31, 2006 and 2005, respectively, on its deferred tax asset primarily relates to the uncertainty surrounding the realization of U.S., state and certain foreign net operating loss carryforwards, foreign tax credit carryforwards and domestic capital loss carryforwards on certain investments. Of these amounts, \$2,100 related to amounts recorded in purchase accounting which, if realized, would reduce goodwill in the future.

The Company has not provided for U.S. income taxes on the unremitted earnings of certain foreign subsidiaries as these earnings are considered to be permanently reinvested. These earnings amounted to approximately \$300,315, \$226,030 and \$174,113 for the years ended December 31, 2006, 2005 and 2004, respectively. It is not practicable to compute the estimated deferred tax liability on these earnings.

The Company has also provided reserves for certain tax matters, both domestic and foreign, which could result in additional tax being due. As of December 31, 2006 and 2005, the Company had income tax reserves accrued in the financial statements in the amounts of \$108,499 and \$89,530, respectively. The Company assessed its uncertain foreign, federal and state tax filing positions. This resulted in an increase to its reserve for tax exposures of \$18,969 and \$51,565, in each of the above periods, respectively. The Company believes that the reserves are required as of December 31, 2006 for potential cross-jurisdictional claims, a foreign recapitalization, the characterization of intercompany payments and the timing and the characterization of certain deductions. Interest and penalties have been recorded for these reserve items. The Company also maintains tax reserves related to acquisition contingencies.

In 2006, the Company filed a federal income tax refund claim related to the tax year ended December 31, 2005 in the amount of \$6,300 regarding a net operating loss carryback. The Company received the federal income tax refund before December 31, 2006. In 2005, the Company filed federal refund claims related to December 31, 2004 and prior years in the amount of \$20,400 regarding net operating loss carrybacks, foreign tax credit carrybacks, and corrections of previous amounts reported and other miscellaneous items. In December 2005, the Company received from the Internal Revenue Service tentative refunds amounting to \$15,500 related to the December 31, 2004 net operating loss carryback. The remaining refund claims are under review by the Internal Revenue Service. These refunds are subject to review by the U.S. Congress Joint Committee on Taxation.

During 2005, the Internal Revenue Service commenced a federal income tax examination for the tax years ended June 30, 2001, June 30, 2003, December 31, 2003, December 31, 2004 and December 31, 2005. It is not known at this time whether there will be any adjustments to the refund claims already filed or to taxes paid in any other years as a result of the examination by the Internal Revenue Service. The Company believes that it has adequate reserves for any items that may result in an adjustment as a result of the Internal Revenue Service's income tax examination.

On October 22, 2004, the President signed the American Jobs Creation Act of 2004 (the Act). The Act includes a deduction of 85% for certain foreign earnings that are repatriated, as defined in the Act, resulting in an effective tax cost of 5.25% on any such repatriated foreign earnings. The Company initially elected to





**BEARINGPOINT, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

apply this provision to \$9,000 of earnings repatriation during the fourth quarter of 2005. After further analysis the earnings repatriated do not qualify under the Act.

**15. Transactions with KPMG LLP**

During 2004, KPMG LLP, the Company's former parent, reduced its holdings in Company common stock to less than 5%, and in February 2005, the transaction services agreement (described below) between the Company and KPMG LLP expired. For these reasons, along with certain other factors, as of 2005, KPMG LLP is no longer considered a related party to the Company. There were various arrangements that remained in place during 2005 between the Company and KPMG LLP for infrastructure services (discussed below) and indemnification agreements (see Note 11, Commitments and Contingencies).

*Infrastructure Services.* Effective January 31, 2000, the Company and KPMG LLP entered into an outsourcing agreement whereby the Company received and was charged for services performed by KPMG LLP, which was amended and restated effective July 1, 2000 to eliminate the service related costs that were not required. On February 13, 2001, the Company and KPMG LLP entered into a transition services agreement whereby the Company received and was charged for infrastructure services on substantially the same basis as the amended and restated outsourcing agreement. The allocation of costs to the Company for such services was based on actual costs incurred by KPMG LLP and were allocated among KPMG LLP's assurance and tax businesses and the Company primarily on the basis of full-time equivalent personnel and actual usage (specific identification). With regard to facilities costs, the Company and KPMG LLP have entered into arrangements pursuant to which the Company subleases from KPMG LLP office space that was formally allocated to the Company under the outsourcing agreement. The terms of the arrangements are substantially equivalent to those under the original outsourcing agreement, and will extend over the remaining period covered by the lease agreement between KPMG LLP and the lessor.

Effective October 1, 2002, the Company and KPMG LLP entered into an outsourcing services agreement under which KPMG LLP provides the Company certain services relating to office space. These services covered by the outsourcing services agreement had previously been provided under the transition services agreement. The services were provided for three years at a cost that is less than the cost for comparable services under the transition services agreement.

The transition services agreement and outsourcing services agreement expired on February 13, 2005 and October 1, 2005, respectively. The Company continues to sublease office space from KPMG LLP after the expiration of the transition services agreement under operating lease agreements. In connection with the expiration of the transition services agreement, the Company also agreed to settle a separate arrangement under which it pays KPMG LLP for the use of occupancy-related assets in the office facilities subleased by the Company from KPMG LLP. As such, during July 2005, the Company paid KPMG LLP \$17,356 for its share of the cost of the occupancy-related assets that it believes relates to office locations that it subleased from KPMG LLP. Approximately \$9,660 of the total \$17,356 paid to KPMG LLP related to office locations that were previously abandoned in connection with the Company's office space reduction effort. Accordingly, the Company has reserved for this amount as part of its lease and facilities restructuring charges recorded during the years ended December 31, 2005 and 2004. The Company classified the remaining \$7,696 paid to KPMG LLP as a prepaid service cost, which the Company plans to amortize over the remaining term of its respective sublease agreements with KPMG LLP. As of December 31, 2006, the remaining amount to be expensed was \$3,938. For a discussion regarding the settlement with KPMG LLP, see Note 11, Commitments and Contingencies.



**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Total expenses allocated to the Company under the transition services agreement and outsourcing services agreement with regard to occupancy costs and other infrastructure services are as follows:

	<b>Year Ended December 31,</b>	
	<b>2005(1)</b>	<b>2004</b>
Occupancy costs	\$ 2,760	\$ 23,772
Other infrastructure service costs	3,236	52,391
<b>Total</b>	<b>\$ 5,996</b>	<b>\$ 76,163</b>
Amounts included in:		
Other costs of service	\$ 2,760	\$ 23,772
Selling, general and administrative expenses	3,236	52,391
	<b>\$ 5,996</b>	<b>\$ 76,163</b>

(1) Decline in charges under the KPMG LLP infrastructure agreements from the year ended December 31, 2004 to the year ended December 31, 2005 is due to the expiration of these agreements during 2005.

There were no expenses allocated to the Company relating to the transition services agreement or outsourcing services agreement during the year ended December 31, 2006 as KPMG LLP was not considered a related party during 2006.

*2004 and Prior Periods Related Party Revenue and Costs of Service.* As described above, prior to 2005, KPMG LLP was a related party to the Company and during that time period, the Company periodically provided consulting services directly to KPMG LLP and other affiliates. Additionally, KPMG LLP's assurance and tax businesses utilized the Company's consultants from time to time in servicing their assurance and tax clients. The Company also utilized KPMG LLP's assurance and tax professionals from time to time in servicing their consulting clients and to support internal finance and accounting needs. Management believes that the revenue earned and fees paid between KPMG LLP's assurance and tax businesses, other affiliates and the Company were determined on a basis substantially equivalent to what would have been earned and paid in similar transactions with unrelated parties. For the year ended December 31, 2004 the company earned revenue in the amount of \$1,368, and paid costs in the amount of \$5,727, respectively as a result of these services.

**16. Employee Benefit Plans***401(k) Plan*

The Company sponsors a qualified 401(k) defined contribution plan (the "401(k) Plan") covering substantially all of its employees. Participants are permitted (subject to a maximum permissible contribution under the Internal Revenue

Code for calendar year 2006 of \$15) to contribute up to 50% of their pre-tax earnings to the 401(k) Plan. Employees who make salary reduction contributions during the plan year and who are employed on the last day of the 401 (k) Plan year receive a Company matching contribution of 25% of the first 6% of pre-tax eligible compensation contributed to the 401 (k) Plan, and, at the discretion of the Company, may receive an additional discretionary contribution of up to 25% of the first 6% of pre-tax eligible compensation contributed to the Plan. Matching contributions are calculated once a year on the last day of the plan year (April 30). Effective May 1, 2006, the Plan's year end was changed to December 31. In addition, the

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

Plan does not restrict the ability of employees to dispose of any of the Company's common stock that they hold in their retirement funds (see Note 13, "Stock-Based Compensation"). For the years ended December 31, 2006, 2005 and 2004, Company contributions made, net of forfeitures, were \$7,464, \$7,311, and \$6,484, respectively.

*Pension and Postretirement Benefits*

The Company has both funded and unfunded noncontributory defined benefit pension plans that provide benefits based on years of service and salary. Pension coverage, which is often governed by local statutory requirements, is provided under the various plans.

The Company also offers a postretirement medical plan to the majority of its full-time U.S. employees and managing directors who meet specific eligibility requirements.

For the years ended December 31, 2006, 2005 and 2004, the pension benefit plans and the postretirement medical plan had a measurement date of December 31.

The following schedules provide information concerning the pension and postretirement medical plans held by the Company:

	<b>Pension Plans</b>		
	<b>Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Components of net periodic pension cost</b>			
Service cost	\$ 7,166	\$ 6,362	\$ 5,670
Interest cost	4,429	4,167	4,151
Expected return on plan assets	(1,075)	(1,172)	(1,055)
Amortization of loss	1,026	16	11
Amortization of prior service cost	635	774	776
Curtailement	120	(833)	
Settlement	(365)	(232)	
Net periodic pension cost	\$ 11,936	\$ 9,082	\$ 9,553

	<b>Postretirement Medical Plan</b>		
	<b>Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Components of postretirement medical cost</b>			
Service cost	\$ 1,922	\$ 1,257	\$ 1,082
Interest cost	735	572	414

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Amortization of losses	156	73	
Amortization of prior service cost	478	478	478
Net periodic postretirement medical cost	\$ 3,291	\$ 2,380	\$ 1,974

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## BEARINGPOINT, INC.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

	<b>Pension Plans Year Ended December 31,</b>		<b>Postretirement medical Plan Year Ended December 31,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Change in projected benefit obligation</b>				
Benefit obligation at beginning of year	\$ 112,542	\$ 114,233	\$ 13,204	\$ 9,986
Service cost	7,166	6,362	1,922	1,257
Interest cost	4,428	4,167	736	572
Plan participants' contributions	637	797	188	168
Curtailment (1)	(69)	(1,851)		
Benefits paid	(1,609)	(1,465)	(151)	(207)
Administrative expense	(128)	(146)		
Actuarial (gain) loss	(8,372)	10,381	(826)	1,428
Settlement (1)	(6,986)	(5,300)		
Effect of exchange rate changes	11,550	(14,636)		
Projected benefit obligation at end of year	\$ 119,159	\$ 112,542	\$ 15,073	\$ 13,204
<b>Change in plan assets</b>				
Fair value of plan assets at beginning of year	\$ 24,332	\$ 28,001	\$	\$
Actual return on plan assets	664	2,244		
Employer contributions	3,440	3,888	(37)	39
Employee contributions	637	798	188	168
Benefits paid	(1,609)	(1,465)	(151)	(207)
Administrative expense	(128)	(145)		
Settlement (1)	(6,986)	(5,300)		
Effect of exchange rate changes	1,885	(3,689)		
Fair value of plan assets at end of year	\$ 22,235	\$ 24,332	\$	\$
<b>Reconciliation of funded status</b>				
Funded status	\$ (96,924)	\$ (88,210)	\$ (15,073)	\$ (13,204)
Unrecognized loss	N/A	18,533	N/A	3,408
Unamortized prior service cost	N/A	6,683	N/A	2,504
Net amount recognized	\$ (96,924)	\$ (62,994)	\$ (15,073)	\$ (7,292)
<b>Amounts recognized in Accumulated Other Comprehensive Income</b>				



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Prior service cost	\$ 4,896	\$	\$ 2,026	\$
Net actuarial loss	6,510		2,426	
Total accumulated other comprehensive income	\$ 11,406	\$	\$ 4,452	\$
<b>Amounts recognized in the Consolidated Balance Sheets</b>				
Noncurrent assets	\$ 231	\$ 3,632	\$	\$
Current liabilities	(1,821)		(229)	
Noncurrent liabilities	(95,334)	(66,626)	(14,844)	(7,292)
Net amount recognized	\$ (96,924)	\$ (62,994)	\$ (15,073)	\$ (7,292)
Accumulated benefit obligation	\$ 105,894	\$ 98,087	\$ 15,073	\$ 13,204

(1) The settlement and curtailment related to a decrease in participants in the Switzerland Plan due to a reduction in workforce.

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## BEARINGPOINT, INC.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

As of December 31, 2006, the Switzerland pension plan had a fair value of assets in excess of the projected benefit obligation of \$231. The German pension plan had a projected benefit obligation in excess of the fair value of assets of \$91,881.

	<b>Pension plans Year Ended December 31,</b>		<b>Postretirement medical plan Year Ended December 31,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Weighted-average assumptions used to determine benefit obligations</b>				
Discount rate	4.2%	4.0%	5.8%	5.6%
Rate of compensation increase	3.0%	3.0%		
<b>Weighted-average assumptions used to determine net periodic benefit cost</b>				
Discount rate	3.6%	4.0%	5.6%	5.8%
Expected long-term return on plan assets	4.5%	4.5%		
Rate of compensation increase	3.0%	3.0%		

The Company's target allocation is 30% equities, 14% real estate and 56% bonds. This target allocation is used in conjunction with historical returns on these asset categories, current market conditions, and future expectations in order to determine an appropriate expected long-term return on plan assets. The investment strategy with respect to the pension assets is to achieve a long-term rate of return to satisfy current and future plan liabilities while minimizing risks. The weighted average asset allocations are as follows:

	<b>Pension Plan</b>	
	<b>December 31, 2006</b>	<b>December 31, 2005</b>
<b>Asset category</b>		
Bonds	49.0%	47.0%
Equities	30.0	30.0
Real estate	14.0	13.0
Other	7.0	10.0
Total	100.0%	100.0%

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The benefit payments are expected to be paid from the pension and postretirement medical plans in the following years:

	<b>Pension plans</b>	<b>Postretirement medical plan</b>
2007	\$ 3,579	\$ 229
2008	3,667	267
2009	3,586	349
2010	3,651	445
2011	3,760	577
Years 2012-2016	21,694	5,754
	\$ 39,937	\$ 7,621

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

The assumed health care cost trends for the postretirement medical plan are as follows:

	<b>December 31, 2006</b>	<b>December 31, 2005</b>
Health care cost trend rate assumed for next year	9.0%	10.0%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.0%	5.0%
Year that the rate reaches the ultimate trend rate	2015	2011

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	<b>1%-Point Increase</b>	<b>1%-Point Decrease</b>
Effect on total service and interest cost	\$ 633	\$ (519)
Effect on Postretirement Benefit Obligation	\$ 2,486	\$ (2,071)

The Company expects to contribute \$3,808 to its pension plans and postretirement medical plan in the year ending December 31, 2007. The Company has other employee benefit pension plans outside the U.S. that are not included in the tables above for which the liability was \$5,702 and \$3,105 as of December 31, 2006 and 2005, respectively.

Effective December 31, 2006, the Company adopted the provisions of SFAS 158. SFAS 158 requires the recognition of the funded status of the pension plans and non-pension postretirement benefit plans as an asset or a liability in the Consolidated Balance Sheets. The funded status is measured as the difference between the projected benefit obligation and the fair value of plan assets.

The following table presents the incremental effects on the Company's Consolidated Balance Sheets at December 31, 2006 as a result of adopting this recognition requirement from SFAS 158:

	<b>December 31, 2006</b>		
	<b>Prior to SFAS 158 Adjustments</b>	<b>SFAS 158 Adjustments</b>	<b>Post SFAS 158 Adjustments</b>
Other assets	\$ 89,049	\$ (5,296)	\$ 83,753
Deferred income taxes	37,907	3,756	41,663

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Total assets	1,940,780	(1,540)	1,939,240
Accrued payroll and employee benefits	342,665	2,050	344,715
Total current liabilities	1,035,561	2,050	1,037,611
Accrued employee benefits	108,260	7,827	116,087
Total liabilities	2,106,664	9,877	2,116,541
Accumulated other comprehensive income	257,714	(11,417)	246,297
Total liabilities and stockholders' deficit	\$ 1,940,780	\$ (1,540)	\$ 1,939,240

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**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

The Company expects that \$1,114 of unrecognized prior service cost and \$414 of unrecognized net actuarial loss will be reclassified from accumulated other comprehensive loss and will be recognized as a component of net periodic benefit cost in 2007. The Company does not expect to receive any refunds from the Switzerland pension plan in 2007.

*Deferred Compensation Plan*

The Company maintains a deferred compensation plan in the form of a Rabbi Trust. In accordance with EITF 97-14, *Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested*, the assets of this trust are consolidated within the Company's financial statements. Under this plan, certain members of management and other highly compensated employees may elect to defer receipt of a portion of their annual compensation, subject to maximum and minimum percentage limitations. The amount of compensation deferred under the plan is credited to each participant's deferral account and a deferred compensation liability established by the Company. An amount equaling each participant's compensation deferral is transferred into a grantor trust and invested in various debt and equity securities. The assets of the grantor trust are held by the Company and accounted for under SFAS No. 115, *Accounting for Certain Investments and Equity Securities*, and are recorded as other current assets within the Consolidated Balance Sheets.

Deferred compensation plan investments are classified as trading securities and consist primarily of investments in mutual funds, money market funds and equity securities. In addition, as of December 31, 2006, the Rabbi Trust invested in 179 shares of the Company's common stock. The values of these investments are based on published market quotes at the end of the period. Adjustments to the fair value of these investments are recorded in the Consolidated Statements of Operations. Gross realized and unrealized gains and losses from trading securities have not been material. These investments are specifically designated as available to the Company solely for the purpose of paying benefits under the Company's deferred compensation plan. However, in the event the Company became insolvent, the investments would be available to all unsecured general creditors.

The deferred compensation liability relates to obligations due to participants under the plan. The deferred compensation liability balance represents accumulated participant deferrals, and earnings thereon, since the inception of the plan, net of withdrawals. The deferred compensation liability is recorded within other liabilities on the balance sheet. The Company's liability under the plan is an unsecured general obligation of the Company. At December 31, 2006 and 2005, \$7,352 and \$8,321, respectively, had been deferred under the plan.

**17. Lease and Facilities Restructuring Activities**

In connection with the Company's previously announced office space reduction effort, the Company recorded a \$29,621 restructuring charge during the year ended December 31, 2006 related to lease, facility and other exit activities. The \$29,621 charge, recorded within the Corporate/Other operating segment, included \$27,552 related to the fair value of future lease obligations (net of estimated sublease income) and \$2,069 in other costs associated with exiting facilities. Since July 2003, the Company has incurred a total of \$132,337 in lease and facilities related restructuring charges in connection with its office space reduction effort relating to the following regions: \$31,330 in EMEA, \$863 in Asia Pacific and \$100,144 in North America. As of December 31, 2006, the Company has a remaining lease and facilities accrual of \$17,126 and \$49,792,



**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
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identified as current and non-current portions, respectively. The remaining lease and facilities accrual will be paid over the remaining lease terms which expire in 2014.

During the year ended December 31, 2005, the Company recorded a \$29,581 restructuring charge related to lease, facility and other exit activities. The \$29,581 charge, recorded within the Corporate/Other operating segment, included \$24,837 related to the fair value of future lease obligations (net of estimated sublease income) and \$4,744 in other costs associated with exiting facilities.

During the year ended December 31, 2004, the Company recorded an \$11,699 restructuring charge related to lease, facility and other exit activities. The \$11,699 charge, recorded within the Corporate/Other operating segment, included \$8,173 related to the fair value of future lease obligations (net of estimated sublease income), \$1,305 representing the unamortized cost of fixed assets and \$2,221 in other costs associated with exiting facilities.

The following table summarizes the restructuring activities for the years ended December 31, 2006, 2005 and 2004:

	<b>Lease and Facilities</b>
Balance at December 31, 2003	\$ 55,898
Charges to operations	11,699
Payments	(19,329)
Other (a)	2,074
Balance at December 31, 2004	50,342
Charges to operations	29,581
Payments	(28,315)
Other (a)	(1,011)
Balance at December 31, 2005	50,597
Charges to operations	29,621
Payments	(14,142)
Other (a)	842
Balance at December 31, 2006	\$ 66,918

(a) Other changes in restructuring accrual consist primarily of foreign currency translation adjustments.

**18. Segment Information**

The Company's segment information has been prepared in accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. Operating segments are defined as components of an enterprise engaging in business activities about which separate financial information is available that is evaluated regularly by the Company's chief operating decision-maker, the Chief Executive Officer, in deciding how to allocate resources and



assess performance. The Company's reportable segments consist of its three North America industry groups (Public Services, Financial Services and Commercial Services), its three international regions (EMEA, Asia Pacific and Latin America) and the Corporate/Other category (which

## BEARINGPOINT, INC.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

consists primarily of infrastructure costs). Accounting policies of the segments are the same as those described in Note 2, Summary of Significant Accounting Policies. Upon consolidation all intercompany accounts and transactions are eliminated. Inter-segment revenue is not included in the measure of profit or loss. Performance of the segments is evaluated on operating income excluding the costs of infrastructure and shared service costs (such as facilities, information systems, finance and accounting, human resources, legal and marketing). Beginning in 2005, the Company combined its Communications, Content and Utilities and Consumer, Industrial and Technology industry groups to form the Commercial Services industry group.

Financial data presented by reportable segments is provided below:

	Year ended December 31, 2006							
	Public	Financial	Commercial		Asia	Latin	Corporate/	Total
	Services	Services	Services	EMEA	Pacific	America	Other (1)	
Revenue	\$ 1,339,358	\$ 399,331	\$ 554,806	\$ 703,083	\$ 360,001	\$ 82,319	\$ 5,105	\$ 3,444,003
Operating income	234,309	111,192	57,229	96,180	68,205	4,465	(770,849)	(199,269)
Depreciation and amortization	10,080	852	1,089	10,573	2,795	712	49,467	75,568
Interest expense (2)	25,915	4,715	6,382	3,637	9,717	2,836	(16,020)	37,182
Total assets (3)	418,999	63,342	113,948	573,489	124,068	24,714	620,680	1,939,240

	Year ended December 31, 2005							
	Public	Financial	Commercial		Asia	Latin	Corporate/	Total
	Services	Services	(4)	EMEA (5)	Pacific	America	Other (1)	
Revenue	\$ 1,293,390	\$ 379,592	\$ 663,797	\$ 662,020	\$ 312,190	\$ 75,664	\$ 2,247	\$ 3,388,900
Operating income	195,204	84,926	(117,376)	(47,917)	39,098	(213)	(715,278)	(561,556)
Depreciation and amortization	11,042	1,027	879	6,856	4,328	732	47,946	72,810
Interest expense (2)	27,443	5,610	9,430	1,208	8,107	2,807	(21,220)	33,385
Total assets (3)	469,205	94,781	166,331	515,606	127,757	16,674	582,072	1,972,426

	Year ended December 31, 2004							
	Public	Financial	Commercial		Asia	Latin	Corporate/	Total
	Services	Services	Services	EMEA (5)	Pacific	America	Other (1)	
Revenue	\$ 1,343,670	\$ 326,452	\$ 654,022	\$ 642,686	\$ 328,338	\$ 79,302	\$ 1,312	\$ 3,375,782
Operating income	243,770	79,443	86,142	(317,864)	12,767	10,264	(608,696)	(494,174)

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Depreciation and amortization	10,499	1,636	3,224	10,071	4,238	554	51,925	82,147
Interest expense								
(2)	29,779	4,839	9,927	233	5,698	1,520	(33,286)	18,710
Total assets (3)	462,681	96,186	217,575	701,582	149,627	21,920	533,136	2,182,707

- (1) Corporate/Other operating loss is principally due to infrastructure and shared services costs, such as facilities, information systems, finance and accounting, human resources, legal and marketing.
- (2) Interest expense is allocated to the industry segments based on accounts receivable and unbilled revenue.
- (3) Industry segment assets include accounts receivable, unbilled revenue, certain software and property and equipment directly attributed to the industry segment, purchased intangible assets and goodwill. All other assets are not allocated to industry segments and are classified as corporate assets.
- (4) Commercial Services includes a \$64,188 goodwill impairment charge for the year ended December 31, 2005.
- (5) EMEA includes a \$102,227 and \$397,065 goodwill impairment change for the years ended December 31, 2005 and 2004, respectively.

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## BEARINGPOINT, INC.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

*Geographic Information*

Financial data segmented by geographic area is provided below:

	Year ended December 31,					
	2006		2005		2004	
	Revenue (2)	Property & Equipment, Net (3)	Revenue (2)	Property & Equipment, Net (3)	Revenue (2)	Property & Equipment, Net (3)
North America (1)	\$ 2,293,495	\$ 112,262	\$ 2,336,779	\$ 129,545	\$ 2,324,144	\$ 149,056
EMEA	703,083	26,930	662,020	31,228	642,686	39,220
Asia Pacific	360,001	4,886	312,190	6,832	328,338	12,442
Latin America (4)	82,319	2,314	75,664	2,528	79,302	2,685
Total Outside of North America	1,145,403	34,130	1,049,874	40,588	1,050,326	54,347
Corporate/Other	5,105		2,247		1,312	
Total	\$ 3,444,003	\$ 146,392	\$ 3,388,900	\$ 170,133	\$ 3,375,782	\$ 203,403

- (1) The North America region includes the Public Services, Commercial Services and Financial Services segments. The North America is comprised of operations in the United States and Canada. The Company reports financial information for these two countries as one region. Canadian operations do not contribute materially to the North America region.
- (2) Revenue by geographic region is reported based on where client services are supervised.
- (3) Property and equipment, net of depreciation, related to the geographic region in which the assets reside.
- (4) The Latin America region includes Mexico.

**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)****19. Results by Quarter**

The following tables present unaudited quarterly financial information for each of the last eight quarters:

	<b>Quarterly periods during the year ended</b>			
	<b>December 31, 2006</b>			
	<b>December 31,</b>	<b>September 30,</b>	<b>June 30,</b>	<b>March 31,</b>
	<b>2006</b>	<b>2006</b>	<b>2006</b>	<b>2006</b>
Revenue	\$ 874,331	\$ 843,248	\$ 892,680	\$ 833,744
Costs of service:				
Costs of service	749,437	683,318	698,631	732,470
Lease and facilities restructuring charge	23,372	961	2,488	2,800
Total costs of service	772,809	684,279	701,119	735,270
Gross profit	101,522	158,969	191,561	98,474
Amortization of purchased intangible assets		515	515	515
Selling, general and administrative expenses	209,630	173,323	176,384	188,913
Operating income (loss)	(108,108)	(14,869)	14,662	(90,954)
Insurance settlement, net of legal fees				38,000
Interest/other expense, net	(2,180)	(5,906)	(5,351)	(6,337)
Income (loss) before taxes	(110,288)	(20,775)	9,311	(59,291)
Income tax expense (benefit)	(2,047)	8,858	12,164	13,422
Net loss	\$ (108,241)	\$ (29,633)	\$ (2,853)	\$ (72,713)
Loss per share basic and diluted	\$ (0.51)	\$ (0.14)	\$ (0.01)	\$ (0.34)

	<b>Quarterly periods during the year ended</b>			
	<b>December 31, 2005</b>			
	<b>December 31,</b>	<b>September 30,</b>	<b>June 30,</b>	<b>March 31,</b>
	<b>2005</b>	<b>2005</b>	<b>2005</b>	<b>2005 (1)(2)</b>
Revenue	\$ 790,921	\$ 831,401	\$ 895,245	\$ 871,333
Costs of service:				
Costs of service	762,149	694,458	717,942	826,778

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Lease and facilities restructuring charge	9,094	882		19,605
Total costs of service	771,243	695,340	717,942	846,383
Gross profit	19,678	136,061	177,303	24,950
Amortization of purchased intangible assets	567	567	566	566
Goodwill impairment charge	166,415			
Selling, general and administrative expenses	222,687	200,379	164,360	163,441
Operating income (loss)	(369,991)	(64,885)	12,377	(139,057)
Interest/other expense, net	(7,203)	(6,553)	(12,422)	(11,788)
Income (loss) before taxes	(377,194)	(71,438)	(45)	(150,845)
Income tax expense (benefit)	36,581	(1,014)	4,841	81,713
Net loss	\$ (413,775)	\$ (70,424)	\$ (4,886)	\$ (232,558)
Loss per share basic and diluted	\$ (2.06)	\$ (0.35)	\$ (0.02)	\$ (1.16)

(1) During 2005, the Company identified certain errors in its previously reported financial statements. Because these changes are not material to the Company's financial statements for the periods prior to 2005 or to 2005 taken as a whole, the Company corrected these errors in the first quarter of 2005. These adjustments included entries to correct errors in accounting for certain foreign tax withholdings, income taxes, revenue, and other miscellaneous items. Had

**BEARINGPOINT, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(in thousands, except share and per share amounts)**

these errors been recorded in the proper periods, the impact of the adjustments on the first quarter of 2005 would have been an increase to revenue and gross profit of \$726 and \$4,927, respectively, and a decrease to net loss of \$15,445.

- (2) In the first quarter of 2005, the Company recorded a valuation allowance of approximately \$57,300 primarily against U.S. deferred tax assets to reflect its conclusion that it is more likely than not that these benefits would not be realized.

**20. Supplemental Financial Information**

The following tables present a summary of additions and deductions related to the allowances for doubtful accounts receivable, allowances for income tax valuation and income tax reserve:

	<b>Balance at Beginning of Period</b>	<b>Charge to Costs and Expenses (a)</b>	<b>Deductions- Write Offs</b>	<b>Balance at End of Period</b>
<b>Allowance for Doubtful Accounts</b>				
Year Ended December 31, 2006	\$ 9,326	\$ (464)	\$ (2,935)	\$ 5,927
Year Ended December 31, 2005	11,296	5,334	(7,304)	9,326
Year Ended December 31, 2004	17,240	(1,057)	(4,887)	11,296

(a) Expense reflected in other costs of service in the Consolidated Financial Statements

	<b>Balance at Beginning of Period</b>	<b>Charged to Income Tax Provision</b>	<b>Charged to Other Accounts (b)</b>	<b>Credited to Income Tax Provision</b>	<b>Balance at End of Period</b>
<b>Income Tax Valuation Allowance</b>					
Year Ended December 31, 2006	\$ 338,792	\$ 76,775	\$ (7,418)	\$	\$ 408,149
Year Ended December 31, 2005	114,775	223,031	986		338,792
Year Ended December 31, 2004	88,037	24,757	1,981		114,775

(b) Other accounts include deferred tax accounts.

	<b>Balance at Beginning</b>	<b>Tax Reserve Charged to Income Tax</b>	<b>Charged to Other</b>	<b>Tax Reserve Credited to Income Tax</b>	<b>Balance at End of</b>

<b>Income Tax Reserve</b>	<b>of Period</b>	<b>Provision</b>	<b>Accounts (c)</b>	<b>Provision</b>	<b>Period</b>
Year Ended December 31, 2006	\$ 89,530	\$ 13,795	\$ 5,174	\$	\$ 108,499
Year Ended December 31, 2005	37,965	51,417	148		89,530
Year Ended December 31, 2004	28,403	7,997	1,565		37,965

(c) Other accounts include goodwill and currency translation accounts.

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