

BEARINGPOINT INC
Form 10-Q
June 29, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2006.

OR

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

Commission File Number 001-31451

BEARINGPOINT, INC.
(Exact name of Registrant as specified in its charter)

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

22-3680505
**(IRS Employer
Identification No.)**

1676 International Drive, McLean, VA
(Address of principal executive offices)

22102
(Zip Code)

(703) 747-3000

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The number of shares of common stock of the Registrant outstanding as of June 1, 2007 was 201,641,999.

BEARINGPOINT, INC.
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED SEPTEMBER 30, 2006
EXPLANATORY NOTE

As a result of significant delays in completing our consolidated financial statements for the year ended December 31, 2006 (fiscal 2006), we were unable to timely file with the Securities and Exchange Commission (the SEC) our Annual Report on Form 10-K for the fiscal year ended December 31, 2006 (the 2006 Form 10-K), this Quarterly Report on Form 10-Q for the quarter ended September 30, 2006 and our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2006 and June 30, 2006. In addition, we were unable to timely file with the SEC our Quarterly Report on Form 10-Q for the quarter ended March 31, 2007.

We filed the 2006 Form 10-K on June 28, 2007. Due to the delay in the filing of this Quarterly Report, certain information presented in this Quarterly Report relates to significant events that have occurred subsequent to September 30, 2006.

Contemporaneous with the filing of this Quarterly Report, we are filing our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2006 and June 30, 2006.

BEARINGPOINT, INC.
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED SEPTEMBER 30, 2006
TABLE OF CONTENTS

	Page
PART I FINANCIAL INFORMATION	
Item 1: Financial Statements (unaudited)	1
Consolidated Condensed Statements of Operations for the Three and Nine Months Ended September 30, 2006 and 2005	1
Consolidated Condensed Balance Sheets as of September 30, 2006 and December 31, 2005	2
Consolidated Condensed Statements of Cash Flows for the Nine Months Ended September 30, 2006 and 2005	3
Notes to Consolidated Condensed Financial Statements	4
Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations	24
Item 3: Quantitative and Qualitative Disclosures about Market Risk	40
Item 4: Controls and Procedures	40
PART II OTHER INFORMATION	
Item 1: Legal Proceedings	40
Item 1A: Risk Factors	40
Item 2: Unregistered Sales of Equity Securities and Use of Proceeds	40
Item 3: Defaults Upon Senior Securities	40
Item 4: Submission of Matters to a Vote of Security Holders	40
Item 5: Other Information	40
Item 6: Exhibits	40
SIGNATURES	41

PART I, ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)**BEARINGPOINT, INC.****CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS****(in thousands, except share and per share amounts)****(unaudited)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Revenue	\$ 843,248	\$ 831,401	\$ 2,569,672	\$ 2,597,979
Costs of service:				
Professional compensation	411,130	412,261	1,264,072	1,295,179
Other direct contract expenses	214,282	215,511	670,685	746,492
Lease and facilities restructuring charges	961	882	6,249	20,487
Other costs of service	57,906	66,686	179,662	197,507
Total costs of service	684,279	695,340	2,120,668	2,259,665
Gross profit	158,969	136,061	449,004	338,314
Amortization of purchased intangible assets	515	567	1,545	1,699
Selling, general and administrative expenses	173,323	200,379	538,620	528,180
Operating loss	(14,869)	(64,885)	(91,161)	(191,565)
Interest income	1,554	2,759	6,118	5,792
Interest expense	(8,625)	(8,119)	(26,569)	(25,009)
Insurance settlement			38,000	
Other income (expense), net	1,165	(1,193)	2,857	(11,546)
Loss before taxes	(20,775)	(71,438)	(70,755)	(222,328)
Income tax expense (benefit)	8,858	(1,014)	34,444	85,540
Net loss	\$ (29,633)	\$ (70,424)	\$ (105,199)	\$ (307,868)
Loss per share basic and diluted	\$ (0.14)	\$ (0.35)	\$ (0.50)	\$ (1.53)
Weighted average shares basic and diluted	212,195,647	201,237,326	211,934,766	200,945,176

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

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

	September 30, 2006	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 268,899	\$ 255,340
Restricted cash	3,190	121,247
Accounts receivable, net of allowances of \$5,441 at September 30, 2006 and \$9,326 at December 31, 2005	369,125	432,415
Unbilled revenue	400,466	355,137
Income tax receivable	8,313	10,867
Deferred income taxes	6,653	18,991
Prepaid expenses	49,701	35,875
Other current assets	70,005	40,345
Total current assets	1,176,352	1,270,217
Property and equipment, net	146,500	170,133
Goodwill	448,791	427,688
Other intangible assets, net		1,545
Deferred income taxes, less current portion	28,152	20,915
Other assets	82,728	81,928
Total assets	\$ 1,882,523	\$ 1,972,426
LIABILITIES AND STOCKHOLDERS DEFICIT		
Current liabilities:		
Current portion of notes payable	\$ 355	\$ 6,393
Accounts payable	242,000	286,273
Accrued payroll and employee benefits	316,584	309,510
Deferred revenue	120,655	166,647
Income tax payable	44,290	41,839
Current portion of accrued lease and facilities charges	12,019	12,515
Deferred income taxes	16,515	10,095
Accrued legal settlements	59,863	38,601
Other current liabilities	140,448	169,624
Total current liabilities	952,729	1,041,497
Notes payable, less current portion	670,568	668,367
Accrued employee benefits	107,639	92,338
Accrued lease and facilities charges, less current portion	35,530	38,082
Deferred income taxes, less current portion	9,630	22,876
Income tax reserve	104,233	89,530

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Other liabilities	100,240	65,308
Total liabilities	1,980,569	2,017,998

Commitments and contingencies (note 9)

Stockholders' deficit:

Preferred stock, \$.01 par value 10,000,000 shares authorized

Common stock, \$.01 par value 1,000,000,000 shares authorized,
205,350,249 shares issued and 201,537,999 shares outstanding on

September 30, 2006 and December 31, 2005

	2,044	2,044
Additional paid-in capital	1,295,741	1,261,797
Accumulated deficit	(1,589,398)	(1,484,199)
Notes receivable from stockholders	(7,581)	(7,578)
Accumulated other comprehensive income	236,875	218,091
Treasury stock, at cost (3,812,250 shares)	(35,727)	(35,727)

Total stockholders' deficit	(98,046)	(45,572)
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Total liabilities and stockholders' deficit	\$ 1,882,523	\$ 1,972,426
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The accompanying Notes are an integral part of these Consolidated Condensed Financial Statements

BEARINGPOINT, INC.
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Nine Months Ended September 30,	
	2006	2005
Cash flows from operating activities:		
Net loss	\$ (105,199)	\$ (307,868)
Adjustments to reconcile net loss to net cash used in operating activities:		
Deferred income taxes	3,999	59,402
(Benefit) provision for doubtful accounts	(2,414)	2,202
Stock-based compensation	33,944	25,203
Depreciation and amortization of property and equipment	52,445	52,457
Amortization of purchased intangible assets	1,545	1,699
Lease and facilities restructuring charges	6,249	20,487
Amortization of debt issuance costs and debt accretion	6,420	10,400
Other	(270)	9,335
Changes in assets and liabilities:		
Accounts receivable	72,738	(13,535)
Unbilled revenue	(41,087)	(65,229)
Income tax receivable, prepaid expenses and other current assets	(39,406)	(2,565)
Other assets	(3,674)	(8,892)
Accounts payable, accrued legal settlements and other current liabilities	(59,148)	84,305
Accrued payroll and employee benefits	(414)	14,620
Deferred revenue	(48,191)	23,006
Income tax reserve and other liabilities	47,939	(15,230)
Net cash used in operating activities	(74,524)	(110,203)
Cash flows from investing activities:		
Purchases of property and equipment	(30,259)	(32,373)
Decrease (increase) in restricted cash	118,058	(19,140)
Net cash provided by (used in) investing activities	87,799	(51,513)
Cash flows from financing activities:		
Proceeds from issuance of common stock		14,897
Proceeds from issuance of notes payable		282,153
Repayments of notes payable	(6,506)	(8,787)
(Decrease) increase in book overdrafts	(810)	5,083
Payments made in lieu of stock issuance		(4,929)
Net cash (used in) provided by financing activities	(7,316)	288,417
Effect of exchange rate changes on cash and cash equivalents	7,600	(9,658)
Net increase in cash and cash equivalents	13,559	117,043

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Cash and cash equivalents	beginning of period	255,340	244,810
Cash and cash equivalents	end of period	\$ 268,899	\$ 361,853

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

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

Note 1. Basis of Presentation and Liquidity

Basis of Presentation

The accompanying unaudited interim Consolidated Condensed Financial Statements of BearingPoint, Inc. (the Company) have been prepared pursuant to the rules and regulations of the SEC for Quarterly Reports on Form 10-Q. These statements do not include all of the information and Note disclosures required by accounting principles generally accepted in the United States of America, and should be read in conjunction with our Consolidated Financial Statements and notes thereto for the year ended December 31, 2006, included in the Company's Annual Report on Form 10-K and filed with the SEC on June 28, 2007 (the 2006 Form 10-K). The accompanying Consolidated Condensed Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America and reflect adjustments (consisting solely of normal, recurring adjustments, except as noted below) which are, in the opinion of management, necessary for a fair presentation of results for these interim periods. The results of operations for the three and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for any other interim period or the entire fiscal year.

The interim Consolidated Condensed 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 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 revenue, certain foreign tax withholdings, income taxes, and other miscellaneous items. Had these errors been recorded in the proper periods, the impact of the adjustments on the nine months ended September 30, 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.

Liquidity

The interim Consolidated Condensed 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 September 30, 2006, the Company had an accumulated deficit of \$1,589,398 and a total stockholders' deficit of \$98,046.

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

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 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.

BEARINGPOINT, INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

(in thousands, except share and per share amounts)

(unaudited)

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 regulatory proceedings. See Note 9, 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 days sales outstanding (DSOs) and improving profitability has improved cash flows from operations. In addition, as discussed in Note 3, Notes Payable, during May 2007, the Company entered into the 2007 Credit Facility, as defined herein, 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).

Note 2. Stock-Based Compensation and Employee Stock Purchase Plan

Long-Term Incentive Plan

The Company is authorized to grant stock options and other awards to its employees and directors under its 2000 Long-Term Incentive Plan (the LTIP). On December 14, 2006, the Company amended its LTIP which included the elimination of the formula used to determine the number of shares available for issuance under the LTIP. Previously, the number of shares of common stock authorized for issuance under the LTIP was determined by a formula equal to the greater of (i) 35,084,158 shares of common stock and (ii) 25% of the sum of (x) the number of issued and outstanding shares of the Company's common stock and (y) the authorized shares. The amendment to the LTIP eliminated this formulaic determination of the number of shares of common stock authorized for issuance under the LTIP and replaced this formula with the specified number of authorized shares of 92,179,333, an aggregate increase of 25 million shares available for awards under the LTIP.

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, including shares of restricted stock, restricted stock units (RSUs) and performance share units (PSUs), may be issued under the LTIP for consideration as determined by the Compensation Committee of the Board of Directors and will be settled with the existing authorized share base. As of September 30, 2006, the Company had stock options, restricted stock awards and RSUs outstanding.

Activity for stock awards and options granted under the LTIP during the nine months ended September 30, 2006 was as follows:

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

	Options/Shares Available	Options Outstanding Number	Weighted Average Exercise Price per Share
Balance at December 31, 2005	7,609,567	45,676,141	\$ 11.33
Additional shares authorized			
Options granted	(600,400)	600,400	8.70
Options exercised			
Options forfeited/canceled	9,152,650	(9,152,650)	12.08
Restricted stock awards, net of forfeitures	(6,505,415)	n/a	8.58
Balance at September 30, 2006	9,656,402	37,123,891	\$ 11.10

The Company adopted the modified prospective transition method permitted under Statement of Financial Accounting Standards (SFAS) No. 123(R), Share-Based Payment (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 three and nine months ended September 30, 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 \$7,035 and \$23,025 for the three and nine months ended September 30, 2006, respectively, and the application of a forfeiture rate to compensation expense recognized in prior years was not considered significant for disclosure. The Consolidated Condensed Statements of Operations for the three and nine months ended September 30, 2006 include stock-based compensation expense of \$12,429 and \$33,944, respectively, related to stock option awards, restricted stock awards, RSUs, and the Company's Employee Stock Purchase Plan (ESPP) and BE an Owner programs.

The Company elected the alternative transition method as outlined in Financial Accounting Standards Board (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 quarter ended September 30, 2006 was \$6,772 and a \$0.03 per share reduction to earnings per share. The after-tax stock-based compensation impact of adopting SFAS 123(R) for the nine months ended September 30, 2006 was \$22,159 and a \$0.10 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 Accounting Principles Board Opinion (APB) No. 25, Accounting for Stock Issued to Employees (APB 25), and related interpretations, including FASB Interpretation (FIN) No. 44, Accounting for Certain Transactions Involving Stock Compensation, for its plans. Under this accounting method, stock-option awards that are

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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 September 30, 2006, unrecognized compensation costs and related weighted-average lives over which the costs will be amortized were as follows:

	Unrecognized Compensation Costs	Weighted- Average Life in Years
Stock options	\$ 14,658	2.0
Restricted stock and stock unit awards	48,004	3.5
ESPP	5,421	1.3
Total	\$ 68,083	3.0

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

The following table illustrates the pro forma 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:

	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
Net loss	\$ (70,424)	\$ (307,868)
Add back:		
Total stock-based compensation expense recorded under intrinsic value method for all stock awards, net of tax effects	20,069	25,203
Deduct:		
Total stock-based compensation expense recorded under fair value method for all stock awards, net of tax effects	(36,364)	(87,508)
Pro forma net loss	\$ (86,719)	\$ (370,173)
Loss per share:		
Basic and diluted as reported	\$ (0.35)	\$ (1.53)
Basic and diluted pro forma	\$ (0.43)	\$ (1.84)

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 issued 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 \$501 during the three months ended September 30, 2006 and an increase to expense of \$50 during the three months ended September 30, 2005 (pro forma) and a reduction to expense of \$2,016 and \$1,826 during the nine months ended September 30, 2006 and 2005 (pro forma), respectively.

The fair value of each option award was estimated on the date of grant using the Black-Scholes option pricing model. 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 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 Staff Accounting Bulletin (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 term used as the input to the Black-Scholes model. The relevant

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data used to determine the value of the stock option grants, in the respective periods, is as follows:

	Stock Price Expected Volatility	Risk-Free Interest Rate	Expected Life	Expected Dividend Yield	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value
Three months ended September 30, 2006	50.80%	4.69%	6		\$8.70	\$4.70
Three months ended September 30, 2005	50.32%	4.07%	6		\$7.50	\$3.94
Nine months ended September 30, 2006	50.80%	4.69%	6		\$8.70	\$4.70
Nine months ended September 30, 2005	51.08%	4.00%	6		\$7.71	\$4.57

7

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

The grant date fair value of the Company's common stock purchased and/or expected to be purchased under the ESPP was estimated for the three and nine months ended September 30, 2006 and 2005 using the Black-Scholes option-pricing model with an expected volatility ranging between 30.4% and 70.0%, 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 nine months ended September 30, 2006 and 2005, the weighted average grant date fair value of shares purchased under the ESPP was \$0 and \$3.21, respectively.

Stock Option Plans

The following table details the weighted average remaining contractual life of options outstanding at September 30, 2006 by range of exercise prices:

	Outstanding Options ⁽¹⁾			Options Exercisable ⁽¹⁾	
	Number Outstanding September 30, 2006	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable September 30, 2006	Weighted Average Exercise Price
Range of Exercise Price					
\$0.00 - \$11.10	25,941,284	7.0	\$ 8.86	21,215,905	\$ 9.05
\$11.11- \$16.64	5,243,211	5.0	\$13.25	5,243,211	\$13.25
\$16.65- \$27.75	5,788,899	4.2	\$18.03	5,788,899	\$18.03
\$49.95- \$55.50	150,497	3.3	\$55.50	150,497	\$55.50
	37,123,891	6.3	\$11.10	32,398,512	\$11.55
Vested or Expected to vest at September 30, 2006 ⁽¹⁾	36,415,084	6.2			

(1) The aggregate intrinsic values for stock options outstanding, exercisable and vested or expected to vest as of September 30, 2006 of \$1,891, \$1,096 and \$1,771, respectively, represent the total pre-tax intrinsic values based upon our

closing stock
price of \$7.86 as
of
September 30,
2006 which
would have
been received
by the option
holders had all
the
in-the-money
options been
exercised as of
that date

Options exercisable at September 30, 2006 had a weighted average remaining contractual life of 6.0 years.

Options exercisable at September 30, 2005 were 33,542,827, with a weighted average exercise price of \$12.72.

The aggregate intrinsic value for stock options exercised during the three and nine months ended September 30, 2005 was \$0 and \$185, respectively. The cash received in association with the stock options exercised during the nine months ended September 30, 2005 was \$1,127. No stock options were exercised in the three and nine months ended September 30, 2006.

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 was \$10.39, and the exercise price of these options ranged 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 the three and nine months ended September 30, 2006 for stock options was \$5,425 and \$18,177, respectively.

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

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

number of key employees, and delegated to the Company's officers the authority to grant these awards. The following table summarized the RSU activity under this authorization during the nine months ended September 30, 2006:

	Number of RSUs	Weighted Average Grant Date Fair Value
Outstanding at December 31, 2005	13,268,265	\$7.61
Granted	6,879,594	8.54
Settled		
Forfeited	(399,487)	7.80
Outstanding at September 30, 2006	19,748,372	\$7.93

The total fair value of RSUs that vested, net of forfeitures, in the three months ended September 30, 2006 and 2005 was approximately \$5,394 and \$19,868, respectively. The total fair value of RSUs that vested, net of forfeitures, in the nine months ended September 30, 2006 and 2005 was approximately \$10,919 and \$21,359, respectively. The vesting and settlement terms for the RSUs granted during 2006 are described below:

5,412,756 RSUs generally vest 25% on each January 1 of calendar years 2007 through 2010 and settle 25% per year starting January 1, 2009;

1,287,486 RSUs generally either: (i) cliff vest and settle three years from the grant date; or (ii) vest and settle over two to four years from the grant date; and

179,352 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-based 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 September 30, 2006, the Company had 19,748,372 RSUs outstanding (excluding approximately 141,541 RSUs awarded to recipients in China where local laws require a cash settlement), with a grant date weighted average fair value of \$7.93.

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 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 nine months ended September 30, 2006 and 2005, employees purchased a total of 0 and 2,053,154 shares for \$0 and \$13,769, respectively. As of September 30, 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 \$23,109 at September 30, 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

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

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 \$1,610 and \$4,848 was recognized for the three and nine months ended September 30, 2006, respectively. For the three and nine months ended September 30, 2005, approximately \$2,545 and \$9,818, respectively, were included in the pro forma disclosure for compensation expense under SFAS 123.

Note 3. Notes Payable

Notes payable consist of the following:

	September 30, 2006	December 31, 2005
Current portion:		
Yen-denominated term loan (January 31, 2003)	\$	\$ 2,803
Yen-denominated term loan (June 30, 2003)		1,402
Other	355	2,188
Total current portion	355	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 \$19,432 and \$21,946, respectively)	20,568	18,054
Other		313
Total long-term portion	670,568	668,367
Total notes payable	\$ 670,923	\$ 674,760

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 (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

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

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 of 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.

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 generally accepted accounting principles in the United States of America (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.

Discontinued 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 under the 2005 Credit Facility were released.

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 September 30, 2006, the Company had approximately \$21,810 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 September 30, 2006, the Company had no borrowings under the 2005 Credit Facility but had letters of credit outstanding of approximately \$82,288. 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

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

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 September 30, 2006, the interest rate under the 2005 Credit Facility was 7.37%.

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.

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; and 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.

In addition, the lenders of the 2005 Credit Facility granted the Company waivers for any default under the 2005 Credit Facility 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. The Company accounted for these modifications in accordance with Emerging Issues Task Force Issue No. 96-19, "Debtor's Accounting for a Modification or Exchange of Debt Instruments" (EITF 96-19). In accordance with EITF 96-19, since the change in the terms of outstanding debentures did not result in substantially different cash flows, this change in terms is accounted for as a modification. As such, the 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, and consent fees will be recognized over future periods. 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.

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

Note 4. Earnings (Loss) Per Share

Basic earnings (loss) per share is computed based on the weighted average number of common shares outstanding 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, restricted stock units, 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. During the three months ended September 30, 2006 and 2005, 129,231,298 and 142,195,249 shares, respectively, were not included in the computation of diluted EPS because to do so would have been anti-dilutive. During the nine months ended September 30, 2006 and 2005, 132,080,967 and 118,733,078 shares, respectively, were not included in the computation of diluted EPS because to do so would have been anti-dilutive.

Note 5. Comprehensive Loss

The components of comprehensive loss are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Net loss	\$ (29,633)	\$ (70,424)	\$ (105,199)	\$ (307,868)
Foreign currency translation adjustment, net of tax				
(a)	(6,555)	1,127	13,454	(45,946)
Minimum pension liability			5,329	
Comprehensive loss	\$ (36,188)	\$ (69,297)	\$ (86,416)	\$ (353,814)

(a) Movement in the foreign currency translation adjustment is primarily due to exchange-rate fluctuations of the Euro and Japanese Yen against the U.S. dollar.

Note 6. Segment Reporting

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 consists primarily of infrastructure costs). Accounting policies of the segments are the same as those described in Note 2, Summary of Significant Accounting Policies, of the Company's 2006 Form 10-K. 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), which is represented by the Corporate/Other segment. 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.

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

Three Months Ended September 30,				
	2006			2005
	Revenue	Operating Income (Loss)	Revenue	Operating Income (Loss)
Public Services	\$ 333,825	\$ 61,565	\$ 316,063	\$ 45,892
Commercial Services	133,253	20,572	160,030	17,585
Financial Services	97,161	26,184	103,709	31,108
EMEA	167,089	28,420	152,049	9,259
Asia Pacific	91,609	20,841	77,811	15,477
Latin America	18,758	(125)	21,370	2,779
Corporate/Other	1,553	(172,326)	369	(186,985)
Total	\$ 843,248	\$ (14,869)	\$ 831,401	\$ (64,885)

Nine Months Ended September 30,				
	2006			2005
	Revenue	Operating Income (Loss)	Revenue	Operating Income (Loss)
Public Services	\$ 1,006,022	\$ 184,370	\$ 994,501	\$ 184,987
Commercial Services	409,683	32,433	509,994	(47,034)
Financial Services	319,833	95,919	282,226	72,887
EMEA	501,696	80,754	504,620	56,550
Asia Pacific	271,671	57,054	241,786	40,400
Latin America	56,639	1,984	63,548	9,864
Corporate/Other	4,128	(543,675)	1,304	(509,219)
Total	\$ 2,569,672	\$ (91,161)	\$ 2,597,979	\$ (191,565)

Note 7. Goodwill and Other Intangible Assets

The changes in the carrying amount of goodwill, at the reporting unit level, for the nine months ended September 30, 2006 were as follows:

	Balance December 31, 2005	Impairment Charge	Foreign Currency Translation Adjustment	Balance September 30, 2006
Public Services	\$ 23,581	\$	\$	\$ 23,581
Financial Services	9,210			9,210

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EMEA	325,262		20,650	345,912
Asia Pacific	68,562		415	68,977
Latin America	871		38	909
Corporate/Other	202			202
Total	\$ 427,688	\$	\$ 21,103	\$ 448,791

14

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

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

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:

	September 30, 2006	December 31, 2005
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 three months ended September 30, 2006 and 2005, amortization expense related to identifiable intangible assets was \$515 and \$567, respectively. For the nine months ended September 30, 2006 and 2005, amortization expense related to identifiable intangible assets was \$1,545 and \$1,699, respectively.

Note 8. Restructuring Activities

In connection with the Company's previously announced office space reduction efforts, the Company recorded \$961 and \$6,249 in restructuring charges during the three and nine months ended September 30, 2006, respectively, related to lease, facility and other exit activities. The \$961 charge, recorded within the Corporate/Other operating segment for the three months ended September 30, 2006, included \$961 related to the fair value of future lease obligations (net of estimated sublease income). The \$6,249 charge, recorded within the Corporate/Other operating segment for the nine months ended September 30, 2006, included \$5,656 related to the fair value of future lease obligations (net of estimated sublease income) and \$593 in other costs associated with exiting facilities. Since July 2003, the Company has incurred a total of \$108,965 in lease and facilities related restructuring charges in connection with its office space reduction effort relating to the following regions: \$15,270 in EMEA, \$863 in Asia Pacific and \$92,832 in North America. As of September 30, 2006, the Company has a remaining lease and facilities accrual of \$47,549, of which \$12,019 and \$35,530 have been 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.

Changes in the Company's accrual for restructuring charges for the nine months ended September 30, 2006 were as follows:

Total

Balance at December 31, 2005	\$ 50,597
Charges to operations	6,249
Payments	(9,876)
Other (a)	579
Balance at September 30, 2006	\$ 47,549

(a) Other changes
in the
restructuring
accrual consist
primarily of
foreign currency
translation
adjustments.

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

Note 9. 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 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 periodic 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 CONDENSED FINANCIAL STATEMENTS (Continued)
(in thousands, except share and per share amounts)
(unaudited)

Series B Debenture Suit

On September 8, 2005, certain holders of the 2.75% Series B Convertible Subordinated Debentures (the "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 Convertible Subordinated Debentures due 2024 (the "Series A Debentures") and the Series B Debentures. Concurrently, the Company and the relevant holders of the Series B Debentures lawsuit agreed to discontinue the lawsuit.

The First Supplemental Indenture modifies the debentures to include: (i) a waiver of the Company's SEC periodic 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 the 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 periodic 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 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, as well as one of its former directors.

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. These contracts are subject to extensive legal and regulatory requirements and,

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

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.

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

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

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 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.

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, the Company's former parent, 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.

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

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 \$23,135 and \$111,815 under this contract in the nine months ended September 30, 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 to the client, \$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.

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 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. 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.

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

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 September 30, 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 September 30, 2006, the Company had approximately \$159,358 of outstanding surety bonds and \$82,288 of outstanding letters of credit for which the Company may be required to make future payment.

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

Note 10. Pension and Postretirement Benefits

The components of the Company's net periodic pension cost and post-retirement medical cost for the three and nine months ended September 30, 2006 and 2005 were as follows:

	Three Months Ended September 30, 2006		Nine Months Ended September 30, 2006	
	2006	2005	2006	2005
Components of net periodic pension cost:				
Service cost	\$ 1,792	\$ 1,591	\$ 5,376	\$ 4,773
Interest cost	1,107	1,042	3,321	3,126
Expected return on plan assets	(269)	(293)	(807)	(879)
Amortization of loss	256	4	768	12
Amortization of prior service cost	159	194	477	582
Curtailement	30	(208)	90	(624)
Settlement	(91)	(58)	(273)	(174)
Net periodic pension cost	\$ 2,984	\$ 2,272	\$ 8,952	\$ 6,816
Components of net periodic postretirement medical cost:				
Service cost	\$ 480	\$ 314	\$ 1,440	\$ 942
Interest cost	184	143	552	429
Amortization of losses	39	18	117	54
Amortization of prior service cost	120	120	360	360
Net periodic postretirement medical cost	\$ 823	\$ 595	\$ 2,469	\$ 1,785

Note 11. Income Taxes

For the three and nine months ended September 30, 2006, the Company recognized losses before taxes of \$20,775 and \$70,755, respectively and provided for taxes of \$8,858 and \$34,444, respectively, resulting in an effective tax rate of (42.6%) and (48.7%), respectively. For the three months ended September 30, 2006, the effective tax rate varied from the U.S. Federal statutory tax rate, primarily as a result of a change in valuation allowance, the mix of income attributable to foreign versus domestic tax jurisdictions, non-deductible meals and entertainment, changes in income tax reserves, state and local income taxes, and other items. For the nine months ended September 30, 2006, the effective tax rate varied from the U.S. federal statutory tax rate, primarily as a result of a change in valuation allowance, changes in income tax reserves, non-deductible meals and entertainment, state and local income taxes, other items and the mix of income attributable to foreign versus domestic tax jurisdictions.

For the three and nine months ended September 30, 2005, the Company recognized losses before taxes of \$71,438 and \$222,328, respectively. The Company received an income tax benefit of \$1,014 for the three months ended September 30, 2005 and provided for income taxes of \$85,540 for the nine months ended September 30, 2005, resulting in an effective tax rate of 1.4% and (38.5%), respectively. For the three months ended September 30, 2005, the effective tax rate varied from the U.S. Federal statutory tax rate, primarily as a result of a change in valuation allowance, the mix of income attributable to foreign versus domestic tax jurisdictions, non-deductible meals and entertainment, changes in income tax reserves, state and local income taxes, and other items.

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For the nine months ended September 30, 2005, the effective tax rate varied from the U.S. Federal statutory tax rate, primarily as a result of a change in valuation allowance, changes in income tax reserves, non-deductible meals and entertainment, state and local income taxes, other items and the mix of income attributable to foreign versus domestic tax jurisdictions. In the three months ended September 30, 2005, the Company recorded a U.S. federal income tax benefit in the amount of \$6,100 due to the ability to carryback U.S. Federal net operating losses to prior years. The Company received the federal income tax refund in the three months ended December 31, 2006.

BEARINGPOINT, INC.
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)
(in thousands, except share and per share amounts)
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Note 12. Recently Issued Accounting Pronouncements

In June 2006, the FASB issued 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 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, 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 Company's 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.

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 September 2006, the FASB issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (SFAS 158). SFAS 158 requires employers to fully recognize the obligations associated with single-employer defined benefit pension, retiree healthcare and other postretirement plans in their financial statements. The provisions of SFAS 158 are effective as of the end of the fiscal year ending December 31, 2006. The Company adopted SFAS 158 in the fourth quarter of 2006.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* including an amendment of SFAS 115, (SFAS 159). SFAS 159 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.

PART I, ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) should be read in conjunction with the interim Consolidated Condensed Financial Statements and Notes to the Consolidated Condensed Financial Statements included elsewhere in this Quarterly Report on Form 10-Q.

Disclosure Regarding Forward-Looking Statements

Some of the statements in this Quarterly Report on Form 10-Q constitute forward-looking statements within the meaning of the United States Private Securities Litigation Reform Act of 1995. These statements relate to our operations that are based on our current expectations, estimates and projections. Words such as may, will, could, would, should, anticipate, predict, potential, continue, expects, intends, plans, projects, believes, our view and similar expressions are used to identify these forward-looking statements. The forward-looking statements contained in this Annual Report include statements about our internal control over financial reporting, our results of operations and our financial condition. Forward-looking statements are only predictions and as such are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Forward-looking statements are based upon assumptions as to future events or our future financial performance that may not prove to be accurate. Actual outcomes and results may differ materially from what is expressed or forecast in these forward-looking statements. The reasons for these differences include changes that occur in our continually changing business environment, and the following factors:

Our continuing failure to timely file certain periodic reports with the SEC poses significant risks to our business, each of which could materially and adversely affect our financial condition and results of operations.

In 2004, we identified material weaknesses in our internal control over financial reporting, the remediation of which has materially and adversely affected our business and financial condition, and as of December 31, 2006, these material weaknesses remain.

We face risks related to securities litigation and regulatory actions that could adversely affect our financial condition and business.

Our business may be adversely impacted as a result of changes in demand, both globally and in individual market segments, for our consulting and systems integration services.

Our operating results will suffer if we are not able to maintain our billing and utilization rates or control our costs.

We continue to incur selling, general and administrative (SG&A) expenses at levels significantly higher than those of our competitors. If we are unable to significantly reduce SG&A expenses over the near term, our ability to achieve, and make significant improvements in, net income and profitability will remain in jeopardy.

The systems integration consulting markets are highly competitive, and we may not be able to compete effectively if we are not able to maintain our billing rates or control our costs related to these engagements.

Contracting with the Federal government is inherently risky and exposes us to risks that may materially and adversely affect our business.

Our ability to attract, retain and motivate our managing directors and other key employees is critical to the success of our business. We continue to experience sustained, higher-than-industry average levels of voluntary turnover among our workforce, which has impacted our ability to grow our business.

Our contracts can be terminated by our clients with short notice, or our clients may cancel or delay projects.

If we are not able to keep up with rapid changes in technology or maintain strong relationships with software providers, our business could suffer.

Loss of our joint marketing relationships could reduce our revenue and growth prospects.

We are not likely to be able to significantly grow our business through mergers and acquisitions in the near term.

There will not be a consistent pattern in our financial results from quarter to quarter, which may result in increased volatility of our stock price.

Our profitability may decline due to financial, regulatory and operational risks inherent in worldwide operations.

We may bear the risk of cost overruns relating to our services, thereby adversely affecting our profitability.

We may face legal liabilities and damage to our professional reputation from claims made against our work.

Our services may infringe upon the intellectual property rights of others.

We have only a limited ability to protect our intellectual property rights, which are important to our success.

Our current cash resources might not be sufficient to meet our expected cash needs over time.

We have been unable to issue shares of our common stock under our ESPP since February 1, 2005. The longer we are unable to issue shares of our common stock, the more likely our ESPP participants may elect to withdraw their accumulated cash contributions from the ESPP at rates higher than those we have historically experienced.

Our 2007 Credit Facility imposes a number of restrictions on the way in which we operate our business and may negatively affect our ability to finance future needs, or do so on favorable terms. If we violate these restrictions, we will be in default under the 2007 Credit Facility, which may cross-default to our other indebtedness.

If we cannot generate positive cash flow from our operations, we eventually may not be able to service our indebtedness.

We may be unable to obtain new surety bonds, letters of credit or bank guarantees in support of client engagements on acceptable terms.

Downgrades of our credit ratings may increase our borrowing costs and materially and adversely affect our financial condition.

Our leverage may adversely affect our business and financial performance and may restrict our operating flexibility.

The holders of our debentures have the right, at their option, to require us to purchase some or all of their debentures upon certain dates or upon the occurrence of certain designated events, which could have a material adverse effect on our liquidity.

The price of our common stock may decline due to the number of shares that may be available for sale in the future.

There are significant limitations on the ability of any person or company to acquire the Company without the approval of our Board of Directors.

For a more detailed discussion of these factors, please refer to Item 1A, Risk Factors, included in our 2006 Form 10-K.

Explanatory Note

As a result of significant delays in completing our Consolidated Financial Statements for fiscal 2006, we were unable to timely file with the SEC our 2006 Form 10-K and Quarterly Reports on Form 10-Q for fiscal 2006. In addition, we were unable to timely file with the SEC our Quarterly Report on Form 10-Q for the quarter ended March 31, 2007.

We filed the 2006 Form 10-K on June 28, 2007. Due to the delay in the filing of this Quarterly Report, certain information presented in this Quarterly Report relates to significant events that have occurred subsequent to September 30, 2006.

Overview

We provide 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. In North America, we provide consulting services through our Public Services, Commercial Services and Financial Services industry groups in which we focus significant industry-specific knowledge and service offerings to our clients. Outside of North America, we are organized on a geographic basis, with operations in EMEA, the Asia Pacific region and Latin America.

We have started the transition of our business to a more integrated, global delivery model. In 2007, we created a Global Account Management Program and a Global Solutions Council represented by all of our industry groups that will focus on identifying opportunities for globalized solutions suites. Our Global Delivery Centers continue to grow, both in terms of personnel and the percentage of work they provide to our industry groups.

Economic and Industry Factors

We believe that our clients' spending for consulting services is partially correlated to, among other factors, the performance of the domestic and global economy as measured by a variety of indicators such as gross domestic product, government policies, mergers and acquisitions activity, corporate earnings, U.S. Federal and state government budget levels, inflation and interest rates and client confidence levels, among others. As economic uncertainties increase, clients' interests in

business and technology consulting historically have turned more to improving existing processes and reducing costs rather than investing in new innovations. Demand for our services, as evidenced by new contract bookings, also does not uniformly follow changes in economic cycles. Consequently, we may experience rapid decreases in new contract bookings at the onset of significant economic downturns while the benefits of economic recovery may take longer to realize.

The markets in which we provide services are increasingly competitive and global in nature. While supply and demand in certain lines of business and geographies may support price increases for some of our standard service offerings from time to time, to maintain and improve our profitability we must constantly seek to improve and expand our unique service offerings and deliver our services at increasingly lower cost levels. Our Public Services industry group, which is our largest, also must operate within the U.S. Federal, state and local government markets where unique contracting, budgetary and regulatory regimes control how contracts are awarded, modified and terminated. Budgetary constraints or reductions in government funding may result in the modification or termination of long-term government contracts, which could dramatically affect the outlook of that business.

Revenue and Income Drivers

We derive substantially all of our revenue from professional services activities. Our revenue is driven by our ability to continuously generate new opportunities to serve clients, by the prices we obtain for our service offerings, and by the size and utilization of our professional workforce. Our ability to generate new business is directly influenced by the economic conditions in the industries and regions we serve, our anticipation and response to technological change, the type and level of technology spending by our clients and by our clients' perception of the quality of our work. Our ability to generate new business is also indirectly and increasingly influenced by our clients' perceptions of our ability to manage our ongoing issues surrounding our financial accounting, internal controls and SEC reporting capabilities.

Our gross profit consists of revenue less our costs of service. The primary components of our costs of service include professional compensation and other direct contract expenses. Professional compensation consists of payroll costs and related benefits associated with client service professional staff (including the vesting of various stock awards, tax equalization for employees on foreign and long-term domestic assignments and costs associated with reductions in workforce). Other direct contract expenses include costs directly attributable to client engagements. These costs include out-of-pocket costs such as travel and subsistence for client service professional staff, costs of hardware and software, and costs of subcontractors. If we are unable to adequately control or estimate these costs, or properly anticipate the sizes of our client service and support staff, our profitability will suffer.

Our operating profit reflects our revenue less costs of service and certain additional items that include, primarily, SG&A expenses, which include costs related to marketing, information systems, depreciation and amortization, finance and accounting, human resources, sales force, and other expenses related to managing and growing our business. Write-downs in the carrying value of goodwill and amortization of intangible assets have also reduced our operating profit.

Our operating cash flow is derived predominantly from gross operating profit and how we manage our receivables and payables.

Key Performance Indicators

In evaluating our operating performance and financial condition, we focus on the following key performance indicators: bookings, revenue growth, gross margin (gross profit as a percentage of revenue), utilization, days sales outstanding, free cash flow and attrition.

Bookings. We believe that information regarding our new contract bookings provides useful trend information regarding how the volume of our new business changes over time. Comparing the amount of new contract bookings and revenue provides us with an additional measure of the short-term sustainability of revenue growth. Information regarding our new bookings should not be compared to, or substituted for, an analysis of our revenue over time. There are no third-party standards or requirements governing the calculation of bookings. New contract bookings are recorded using then existing currency exchange rates and are not subsequently adjusted for currency fluctuations. These amounts represent our estimate at contract signing of the net revenue expected over the term of that contract and involve estimates and judgments regarding new

contracts as well as renewals, extensions and additions to existing contracts. Subsequent cancellations, extensions and other matters may affect the amount of bookings previously reported. Bookings do not include potential revenue that could be earned from a client

relationship as a result of future expansion of service offerings to that client, nor does it reflect option years under contracts that are subject to client discretion. In addition, government contracts or work orders are not included in bookings until related appropriations spending has been properly approved and, then, only to the extent of the amount of spending approved. Consequently, there can be significant differences between the times of contract signing and new contract booking recognition. Although our level of bookings provides an indication of how our business is performing, we do not characterize our bookings, or our engagement contracts associated with new bookings, as backlog because our engagements generally can be cancelled or terminated on short notice or without notice.

Revenue Growth. Unlike bookings, which provide only a general sense of future expectations, period-over-period comparisons of revenue provide a meaningful depiction of how successful we have been in growing our business over time.

Gross Margin (gross profit as a percentage of revenue). Gross margin is a meaningful tool for monitoring our ability to control our costs of services. Analysis of the various cost elements, including professional compensation expense, effects of foreign exchange rate changes and the use of subcontractors, as a percentage of revenue over time can provide additional information as to the key challenges we are facing in our business. The cost of subcontractors is generally more expensive than the cost of our own workforce and can negatively impact our gross profit. While the use of subcontractors can help us to win larger, more complex deals, and also may be mandated by our clients, we focus on limiting the use of subcontractors whenever possible in order to minimize our costs. We also utilize certain adjusted gross margin metrics in connection with the vesting and settlement of certain employee incentive awards. For a discussion of these metrics, see Item 11, Executive Compensation Compensation Discussion and Analysis, included in our 2006 Form 10-K.

Utilization. Utilization represents the percentage of time our consultants are performing work, and is defined as total hours charged to client engagement or to non-chargeable client-relationship projects, divided by total available hours for any specific time period, net of holiday and paid vacation hours. In 2006, we changed how we define utilization to make this metric more consistent with how we believe our industry peer group measures this metric. Utilization percentages for fiscal 2005 set forth herein have been adjusted to conform to this new definition.

Days Sales Outstanding (DSO). DSO is an operational metric that approximates the amount of earned revenue that remains unpaid by clients at a given time. DSOs are derived by dividing the sum of our outstanding accounts receivable and unbilled revenue, less deferred revenue, by our average net revenue per day. Average net revenue per day is determined by dividing total net revenue for the most recently ended trailing twelve-month period by 365.

Free Cash Flow. Free cash flow is calculated by subtracting purchases of property and equipment from cash provided by operating activities. We believe free cash flow is a useful measure because it allows better understanding and assessment of our ability to meet debt service requirements and the amount of recurring cash generated from operations after expenditures for fixed assets. Free cash flow does not represent our residual cash flow available for discretionary expenditures as it excludes certain mandatory expenditures such as repayment of maturing debt. We use free cash flow as a measure of recurring operating cash flow. Free cash flow is a non-GAAP financial measure. The most directly comparable financial measure calculated in accordance with generally accepted accounting principles in the United States of America (GAAP) is net cash provided by operating activities.

Attrition. Attrition, or voluntary total employee turnover, is calculated by dividing the number of our employees who have chosen to leave the Company within a certain period by the total average number of all

employees during that same period. Our attrition statistic covers all of our employees, which we believe provides metrics that are more compatible with, and comparable to, those of our competitors.

Readers should understand that each of the performance indicators identified above are utilized by many companies in our industry and by those who follow our industry. There are no uniform standards or requirements for computing these performance indicators, and, consequently, our computations of these amounts may not be comparable to those of our competitors.

Three and Nine Months Ended September 30, 2006 Highlights

In 2006, we were able to sustain our underlying operations and our core business continued to perform, despite the issues we continue to face with respect to our financial accounting systems and efforts to become timely in our SEC periodic reports. We began to see the benefits of restructuring efforts undertaken in previous years, particularly in our Asia Pacific and EMEA industry groups, as well as management actions aimed at improving our profitability. These benefits allowed us to show significant improvements in gross profit and net income (loss) while

maintaining relatively constant year-over-year levels of bookings and revenue. We were also successful in resolving and settling a number of long-running contractual disputes.

We were able to achieve these results despite increasing pricing pressures and competition for the retention of skilled personnel two current industry-wide phenomena that affect us more acutely due to our continuing efforts to timely produce our financial statements and file our periodic reports with the SEC. We continue to be uniquely challenged in these regards and by persisting negative perceptions regarding our financial position that may have been, in our opinion, unjustifiably increased by our settlement of a vigorously contested lawsuit initiated by several holders of our Series B Debentures.

A summary of our financial highlights for the three and nine months ended September 30, 2006 is presented below. For information on additional highlights occurring throughout fiscal 2006, please refer to our 2006 Form 10-K; New contract bookings for the three months ended September 30, 2006 were \$813.3 million, an increase of \$42.3 million, or 5.5%, over new contract bookings of \$771.0 million for the three months ended September 30, 2005. New contract bookings for the nine months ended September 30, 2006 were \$2,431.0 million, an increase of \$2.7 million over new contract bookings of \$2,428.3 million for the nine months ended September 30, 2005. During the three months ended September 30, 2006, new contract bookings increased in our EMEA and Commercial Services industry groups, which were offset by decreased bookings in our Financial Services industry group. For the nine months ended September 30, 2006, new contract bookings in our EMEA, Latin American and Asia Pacific regions increased significantly, while bookings in our Commercial Services and Financial Services industry groups had decreased in the nine months ended September 30, 2005. Bookings in our Public Services industry group were also significantly higher in 2006.

Our revenue for the three months ended September 30, 2006 was \$843.2 million, an increase of \$11.8 million, or 1.4%, over revenue of \$831.4 million for the three months ended September 30, 2005. Our revenue for the nine months ended September 30, 2006 was \$2,569.7 million, a decrease of \$28.3 million, or 1.1%, from revenue for the nine months ended September 30, 2005 of \$2,598.0 million. For the three months ended September 30, 2006, revenue increased in our Public Services industry group and our EMEA and Asia Pacific regions, and was partially offset by a significant revenue decline in our Commercial Services industry group. For the nine months ended September 30, 2006, revenue decreased in our Commercial Services industry group due to revenue declines associated with the settlement of disputes with two significant telecommunications industry clients. These decreases were partially offset by increased revenue in our Financial Services industry group as well as revenue growth in Asia Pacific.

Our gross profit for the three months ended September 30, 2006 was \$159.0 million, compared with \$136.1 million for the three months ended September 30, 2005. Gross profit as a percentage of revenue increased to 18.9% during the three months ended September 30, 2006 from 16.4% during the three months ended September 30, 2005. Increased revenue as well as reductions in professional compensation expense and other direct contract expenses contributed to this improvement. Our gross profit for the nine months ended September 30, 2006 was \$449.0 million, compared with \$338.3 million for the nine months ended September 30, 2005. Gross profit as a percentage of revenue increased to 17.5% during the nine months ended September 30, 2006 from 13.0% during the nine months ended September 30, 2005. The increase was primarily due to significant reductions in professional compensation expense and other direct contract expenses.

We incurred SG&A expenses of \$173.3 million in the third quarter of 2006, representing a decrease of \$27.1 million or 13.5%, from SG&A expenses of \$200.4 million in the third quarter of 2005. We incurred SG&A expenses of \$538.6 million in the nine months ended September 30, 2006, representing an increase of \$10.4 million or 2.0%, over SG&A expenses of \$528.2 million in the nine months ended September 30, 2005. While we achieved cost savings by reducing the size of our sales force and other business development expenses during the nine months ended September 30, 2006, continuing increases in our finance and

accounting costs, primarily for sub-contracted labor and other costs related to the closing of our 2005 financial statements, significantly offset these cost savings.

During the nine months ended September 30, 2006, we realized a net loss of \$105.2 million, or a loss of \$0.50 per share, compared to a net loss of \$307.9 million, or a loss of \$1.53 per share, during the nine months ended September 30, 2005. The decline in net loss in the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005 was attributable to several factors, including:

28

Our gross profit for the nine months ended September 30, 2006 improved Company-wide, compared to our gross profit for the nine months ended September 30, 2005, representing an increase of \$110.7 million;

We recorded \$38.0 million in the nine months ended September 30, 2006 for an insurance settlement in connection with our settlement with Hawaiian Telcom Communications, Inc. (the HT Contract); and

Our income tax provision for the nine months ended September 30, 2006 was lower than our income tax provision for the nine months ended September 30, 2005, as the 2005 amount included a \$57.3 million increase to valuation allowance primarily against our U.S. deferred tax assets.

Contributing to the net loss for the nine months ended September 30, 2006 were \$43.1 million of losses related to the previously mentioned settlements with telecommunication clients, \$39.3 million accrued for bonuses payable to our employees, \$33.9 million of stock-based compensation expense and \$6.2 million of lease and facilities restructuring charges.

Utilization for the three months ended September 30, 2006 was 77.2%, an increase of 250 basis points over the three months ended September 30, 2005. Utilization for the nine months ended September 30, 2006 remained flat at 75.8%, compared to the nine months ended September 30, 2005. Utilization for the three months ended March 31, 2007 was 76.6%.

Free cash flow for nine months ended September 30, 2006 and 2005 was (\$104.8) million and (\$142.6) million, respectively. Net cash used in operating activities in the nine months ended September 30, 2006 and 2005 was (\$74.5) million and (\$110.2) million, respectively. Purchases of property and equipment in the nine months ended September 30, 2006 and 2005 were \$30.3 million and \$32.4 million, respectively. We use free cash flow as a measure of recurring operating cash flow. The change in free cash flow for the nine-month period resulted primarily due to the following:

We experienced higher operating profitability in our business, as evidenced by the sharp decline in operating loss for 2006 as compared 2005. We also lowered our DSOs through enhancements in our cash collections efforts. At September 30, 2006, our DSOs stood at 96 days, representing a decrease of 12 days, or 11%, from our DSOs at September 30, 2005. Our continued focus on this metric during 2006 improved our free cash flow by \$86.3 million for the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005.

We experienced greater cash outflows in 2006 due to payments made for professional services and related expenses accrued under the HT Contract during 2005, and in connection with our settlement with Peregrine Systems, Inc.

As of September 30, 2006, we had approximately 17,400 full-time employees, including approximately 15,300 consulting professionals. This represented a decrease in billable headcount of approximately 0.6% from our headcount at September 30, 2005 of 17,600 and 15,400 respectively. As of March 31, 2007, we had approximately 17,500 full-time employees, including approximately 15,200 consulting professionals.

Our voluntary, annualized attrition rate for the three months ended September 30, 2006 was 28.3%, compared to 27.2% for the three months ended September 30, 2005. The highly competitive industry in which we operate, and our continuing issues related to our North American financial reporting systems and internal controls, have made it particularly critical and challenging for us to attract and retain experienced personnel. Our voluntary, annualized attrition rate for the three months ended March 31, 2007 was 23.9%.

Principal Business Priorities for 2007 and Beyond

In early 2007 our Board of Directors determined our principal business priorities to be to: (1) enhance shareholder value, (2) become timely in our financial and SEC periodic reporting, (3) replace our North American financial reporting systems, (4) reduce employee attrition, (5) increase client awareness, confidence and satisfaction,

and (6) strengthen our balance sheet. For additional information on management's current and planned initiatives to achieve the priorities established by our Board of Directors, please refer to our 2006 Form 10-K.

Segments

Our reportable segments for the three and nine months ended September 30, 2006 consist of our three North America industry groups (Public Services, Commercial Services, and Financial Services), our three international regions (EMEA, Asia Pacific and Latin America) and the Corporate/Other category (which consists primarily of infrastructure costs). Revenue and

gross profit information about our segments are presented below, starting with each of our industry groups and then with each of our three international regions (in order of size).

Our chief operating decision maker, the Chief Executive Officer, evaluates performance and allocates resources among the segments. Upon consolidation, all intercompany accounts and transactions are eliminated. Inter-segment revenue is not included in the measure of profit or loss for each reportable segment. Performance of the segments is evaluated on operating income excluding the costs of infrastructure functions (such as information systems, finance and accounting, human resources, legal and marketing) as described in Note 6, Segment Reporting, of the Notes to Consolidated Condensed Financial Statements. During 2005, we combined our Communications, Content and Utilities and Consumer, Industrial and Technology industry groups to form the Commercial Services industry group.

Three Months Ended September 30, 2006 Compared to Three Months Ended September 30, 2005

Revenue. Our revenue for the third quarter of 2006 was \$843.2 million, an increase of \$11.8 million, or 1.4%, over revenue of \$831.4 million for the third quarter of 2005. The following tables present certain revenue information and performance metrics for each of our reportable segments for the third quarters of years 2006 and 2005. Amounts are in thousands, except percentages.

	Three Months Ended September 30,			%
	2006	2005	\$ Change	Change
Revenue				
Public Services	\$ 333,825	\$ 316,063	\$ 17,762	5.6%
Commercial Services	133,253	160,030	(26,777)	(16.7%)
Financial Services	97,161	103,709	(6,548)	(6.3%)
EMEA	167,089	152,049	15,040	9.9%
Asia Pacific	91,609	77,811	13,798	17.7%
Latin America	18,758	21,370	(2,612)	(12.2%)
Corporate/Other	1,553	369	1,184	n/m
Total	\$ 843,248	\$ 831,401	\$ 11,847	1.4%

	Impact of currency fluctuations	Revenue growth (decline), net of currency impact	Total
Revenue			
Public Services	0.0%	5.6%	5.6%
Commercial Services	0.0%	(16.7%)	(16.7%)
Financial Services	0.0%	(6.3%)	(6.3%)
EMEA	4.7%	5.2%	9.9%
Asia Pacific	(2.1%)	19.8%	17.7%
Latin America	5.4%	(17.6%)	(12.2%)
Corporate/Other	n/m	n/m	n/m
Total	0.8%	0.6%	1.4%

n/m = not
meaningful

Public Services revenue increased during the third quarter of 2006, with strong revenue growth in certain sectors, particularly in our State, Local and Education (SLED) and Healthcare sectors. This increase was partially offset by revenue decline in our Civilian business sector.

Commercial Services revenue decreased during the third quarter of 2006, primarily due to reduced customer demand for our services, particularly within the telecommunications industry.

Financial Services revenue decreased during the third quarter of 2006, primarily due to revenue declines in the Global Markets and Banking sectors, partially offset by revenue growth in the Insurance sector. Global Markets sector revenue declined as we increased the proportion of work derived from lower rate per hour offshore resources in response to client demand, which affected our revenue. The revenue decline in our Banking sector was attributable to a decline in activities in our existing client base, while the revenue increase in our Insurance sector was in response to industry-wide demand for major technology updates and upgrades to operational systems.

EMEA revenue increased during the third quarter of 2006, primarily as a result of the favorable impact of the strengthening of foreign currencies (primarily the Euro) against the U.S. dollar and revenue growth in France, partially offset by significant revenue decline in Germany. Revenue growth in France was driven by an expanding systems integration practice and additional penetration into the French public sector market in 2006. Revenue in Germany declined significantly due to a combination of the impact of reductions in billable headcount precipitated by the restructuring of our business in Germany, increased pressure on pricing and a reduction in the spending levels of German public sector clients.

Asia Pacific revenue increased during the third quarter of 2006, primarily due to significant revenue growth in Australia and Japan. The revenue growth in Australia was primarily due to a significant new client engagement in the telecommunications industry. The revenue increase in Japan was due to revenue growth from system implementation contracts and projects involving compliance with Japan's Financial Instruments and Exchange Law, although a substantial portion of this revenue growth was derived from the use of subcontractors.

Latin America revenue decreased during the third quarter of 2006, due to decreases in local revenue growth in Mexico and Brazil, partially offset by the strengthening of foreign currencies in Latin America against the U.S. Dollar (particularly the Brazilian Real). Revenue in Mexico declined as they continue to restructure the business to position itself for future growth, while revenue in Brazil declined due to the significantly reduced activity of a large client engagement.

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

Gross Profit. During the third quarter of 2006, our revenue increased \$11.8 million and total costs of service decreased \$11.1 million when compared to the third quarter of 2005, resulting in an increase in gross profit of \$22.9 million, or 16.8%. Gross profit as a percentage of revenue increased to 18.9% for the third quarter of 2006 from 16.4% for the third quarter of 2005. The change in gross profit for the third quarter of 2006 compared to the third quarter of 2005 resulted primarily from the following:

Professional compensation expense decreased as a percentage of revenue to 48.8% for the third quarter 2006, compared to 49.6% for the three months ended September 30, 2005. We experienced a net decrease in professional compensation expense of \$1.1 million, or 0.3%, to \$411.1 million for the three months ended September 30, 2006 from \$412.3 million for the three months ended September 30, 2005. The decrease in professional compensation expense from 2005 was primarily related to the vesting of Retention RSUs during the third quarter of 2005.

Other direct contract expenses decreased slightly as a percentage of revenue to 25.4% for the three months ended September 30, 2006 compared to 25.9% for the three months ended September 30, 2005. We experienced a net decrease in other direct contract expenses of \$1.2 million, or 0.6%, to \$214.3 million for the three months ended September 30, 2006 from \$215.5 million for the three months ended September 30, 2005. The increase was driven primarily by increased subcontractor usage during the third quarter of 2006.

Other costs of service as a percentage of revenue decreased to 6.9% for the third quarter of 2006 from 8.0% for the third quarter of 2005. We experienced a net decrease in other costs of service of \$8.8 million, or 13.2%, to \$57.9 million for the third quarter of 2006 from \$66.7 million for the third quarter of 2005. The change was driven primarily by decreases in recruiting charges and bad debt expense.

During the third quarter of 2006 we recorded, within the Corporate/Other operating segment, a charge of \$1.0 million related to lease, facilities and other exit activities, compared with a \$0.9 charge related to lease, facilities and other exit activities in the third quarter of 2005. These charges related primarily to the fair value of future lease obligations associated with office space, primarily within the EMEA and North America regions, which we will no longer be using.

Gross Profit by Segment. The following tables present certain gross profit and margin information and performance metrics for each of our reportable segments for the third quarters of years 2006 and 2005. Amounts are in thousands, except percentages.

	Three Months Ended September 30,			%
	2006	2005	\$ Change	Change
Gross Profit				
Public Services	\$ 69,190	\$ 58,699	\$ 10,491	17.9%
Commercial Services	26,735	26,679	56	0.2%
Financial Services	32,403	37,741	(5,338)	(14.1%)
EMEA	35,005	16,979	18,026	106.2%
Asia Pacific	23,823	19,019	4,804	25.3%
Latin America	1,071	3,649	(2,578)	(70.6%)
Corporate/Other	(29,258)	(26,705)	(2,553)	n/m
Total	\$ 158,969	\$ 136,061	\$ 22,908	16.8%

	Three Months Ended September 30,	
	2006	2005
Gross Profit as a % of revenue		
Public Services	20.7%	18.6%
Commercial Services	20.1%	16.7%
Financial Services	33.3%	36.4%
EMEA	20.9%	11.2%
Asia Pacific	26.0%	24.4%
Latin America	5.7%	17.1%
Corporate/Other	n/m	n/m
Total	18.9%	16.4%

n/m = not
meaningful

Changes in gross profit by segment were as follows:

Public Services gross profit increased in the third quarter of 2006, as higher revenue more than offset significant incremental increases in professional compensation expense related to hiring needs related to demand for our services.

Commercial Services gross profit increased slightly in the third quarter of 2006 despite lower revenue, primarily due to cost savings realized from 2005 workforce realignments and reduced subcontractor expenses as a result of the increased use of internal resources.

Financial Services gross profit decreased in third quarter of 2006, as lower revenue and slight increases in compensation expense more than offset savings in other direct contract expenses, primarily related to a decrease in subcontractor usage.

EMEA gross profit increased in the third quarter of 2006, due primarily to improved profitability in Ireland, France, and Spain as a result of higher utilization and lower costs. Slight declines in other direct contract

expenses also contributed to the increase in gross profit.

Asia Pacific gross profit increased substantially in the third quarter of 2006, primarily due to significant improvements in profitability and staff utilization in the Company's business in Australia and China. Due to the

high demand for resources in the Japanese market and limited availability of qualified personnel, increases in subcontractor expenses served to depress the growth of gross profit in the Company's business in Japan. Significant improvements in compensation expense in 2006 derived from the 2005 workforce reductions in China were more than offset by additional compensation expenses associated with the use of the Company's personnel from outside the region in connection with a significant new telecommunications industry engagement in Australia.

Latin America gross profit decreased in the third quarter of 2006, as lower revenue more than offset savings in other direct contact expenses, primarily resulting from a reduction in subcontractor usage.

Corporate/Other consists primarily of rent expense and other facilities related charges, which increased in the third quarter of 2006 primarily due to the lease and facilities restructuring charges discussed above.

Amortization of Purchased Intangible Assets. Amortization of purchased intangible assets decreased \$0.1 million to \$0.5 million for the three months ended September 30, 2006 from \$0.6 million for the three months ended September 30, 2005.

Selling, General and Administrative Expenses. Selling, general and administrative expenses decreased \$27.1 million, or 13.5%, to \$173.3 million for the three months ended September 30, 2006 from \$200.4 million for the three months ended September 30, 2005. SG&A expenses as a percentage of gross revenue decreased to 20.6% in the three months ended September 30, 2006 from 24.1% for the three months ended September 30, 2005. While we achieved cost savings by reducing the size of our sales force and other business development expenses during the third quarter of 2006, continuing increases in our finance and accounting costs, primarily for sub-contracted labor and other costs related to the closing of our 2005 financial statements, significantly offset these cost savings.

Interest Income. Interest income was \$1.6 million and \$2.8 million in the three months ended September 30, 2006 and 2005, respectively. Interest income is earned primarily from cash and cash equivalents, including money-market investments. The decrease in interest income was due to a lower level of cash available to be invested in money markets during the third quarter of 2006 as compared to the third quarter of 2005.

Interest Expense. Interest expense was \$8.6 million and \$8.1 million in the three months ended September 30, 2006 and 2005, 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 the third quarter of 2006 as compared to the third quarter of 2005.

Other Income (Expense), net. Other income, net was \$1.2 million in the three months ended September 30, 2006 compared to other expense, net of \$1.2 million in the three months ended September 30, 2005. The balances in each period primarily consist of realized foreign currency exchange losses.

Income Tax Expense (Benefit). We incurred income tax expense of \$8.9 million for the three months ended September 30, 2006 and income tax expense of \$1.0 million for the three months ended September 30, 2005. The principal reasons for the difference between the effective income tax rate on loss from continuing operations of (42.6)% and the effective income tax rate on income from continuing operations of 1.4% for the three months ended September 30, 2006 and 2005 were: a change in valuation allowance, the mix of income attributable to foreign versus domestic tax jurisdictions, non-deductible meals and entertainment, changes in income tax reserves, state and local income taxes and other items.

Net Loss. For the three months ended September 30, 2006, we incurred a net loss of \$29.6 million, or a loss of \$0.14 per share. Contributing to the net loss for the three months ended September 30, 2006 were \$25.2 million of losses related to previously mentioned settlements with telecommunication clients, \$12.6 million accrued for bonuses payable to our employees, \$12.4 million of stock-based compensation expense and \$1.0 million of lease and facilities restructuring charges.

For the three months ended September 30, 2005, we incurred a net loss of \$70.4 million, or a loss of \$0.35 per share. Included in our results for the three months ended September 30, 2005 were \$19.9 million of non-cash compensation expense related to retention RSUs, and \$0.9 million of lease and facilities restructuring charges.

Nine Months Ended September 30, 2006 Compared to Nine Months Ended September 30, 2005

Revenue. Our revenue for the nine months ended September 30, 2006 was \$2,569.7 million, a decrease of \$28.3 million, or 1.1%, from revenue of \$2,598.0 million for the nine months ended September 30, 2005. The following tables present certain revenue information and performance metrics for each of our reportable segments for the nine months ended September 30, 2006 and 2005. Amounts are in thousands, except percentages.

	Nine Months Ended September 30,		\$ Change	% Change
	2006	2005		
Revenue				
Public Services	\$ 1,006,022	\$ 994,501	\$ 11,521	1.2%
Commercial Services	409,683	509,994	(100,311)	(19.7%)
Financial Services	319,833	282,226	37,607	13.3%
EMEA	501,696	504,620	(2,924)	(0.6%)
Asia Pacific	271,671	241,786	29,885	12.4%
Latin America	56,639	63,548	(6,909)	(10.9%)
Corporate/Other	4,128	1,304	2,824	n/m
Total	\$ 2,569,672	\$ 2,597,979	\$ (28,307)	(1.1%)

	Impact of currency fluctuations	Revenue growth (decline), net of currency impact	Total
Revenue			
Public Services	0.0%	1.2%	1.2%
Commercial Services	0.0%	(19.7%)	(19.7%)
Financial Services	0.0%	13.3%	13.3%
EMEA	(1.5%)	0.9%	(0.6%)
Asia Pacific	(4.5%)	16.9%	12.4%
Latin America	9.2%	(20.1%)	(10.9%)
Corporate/Other	n/m	n/m	n/m
Total	(0.5%)	(0.6%)	(1.1%)

n/m = not
meaningful

Public Services revenue increased during the nine months ended September 30, 2006, with strong revenue growth in most sectors, particularly in our SLED sector. This increase was partially offset by revenue decline in our Civilian business sector.

Commercial Services revenue decreased during the nine months ended September 30, 2006, primarily due to a \$45.5 million year-over-year decrease in revenue associated with the HT Contract and a reduction of \$20.0 million in revenue related to the resolution of a billings dispute with another large telecommunications client regarding an engagement completed in 2003. Reduced customer demand for our services, particularly within the telecommunications industry also affected our revenue. These decreases were partially offset by the

recognition in the first quarter of 2006 of approximately \$11.0 million in previously deferred revenue.

Financial Services revenue increased during the nine months ended September 30, 2006, primarily due to revenue growth in the Insurance and Banking sectors, partially offset by a decline in our Global Markets sector. Insurance sector revenue increased in response to industry-wide demand for major technology updates and upgrades to operational systems. Banking sector revenue increases were attributable to existing client engagements and the introduction of some new clients into our traditional client base. Global Markets sector

revenue declined as we increased the proportion of work derived from lower rate per hour offshore resources in response to client demand, which affected our revenue.

EMEA revenue slightly decreased during the nine months ended September 30, 2006, primarily due to revenue decline in Germany, partially offset by revenue growth in France. Revenue in Germany declined significantly due to a combination of the impact of reductions in billable headcount precipitated by the restructuring of our business in Germany, increased pressure on pricing and a reduction in the spending levels of German public sector clients. Revenue growth in France was driven by an expanding systems integration practice and additional penetration into the French public sector market in 2006.

Asia Pacific revenue increased during the nine months ended September 30, 2006, primarily due to significant revenue growth in Australia and Japan. Australian revenue increased primarily due to a significant new client engagement in the telecommunications industry. Japanese revenue increased due to revenue growth from system implementation contracts and projects involving compliance with Japan's Financial Instruments and Exchange Law, though a substantial portion of this revenue growth was derived from the use of subcontractors. Asia Pacific revenue was negatively affected in 2006 by the weakening of foreign currencies against the U.S. dollar, primarily the Japanese Yen.

Latin America revenue decreased during the nine months ended September 30, 2006, due to decline in local revenue growth in Mexico and Brazil, partially offset by the strengthening of foreign currencies in Latin America against the U.S. Dollar (particularly the Brazilian Real). Revenue in Mexico declined as the practice continues to restructure the business to position itself for future growth, while revenue in Brazil declined due to the significantly reduced activity of a large client engagement.

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

Gross Profit. During the nine months ended September 30, 2006, our revenue decreased \$28.3 million and total costs of service decreased \$139.0 million when compared to the nine months ended September 30, 2005, resulting in an increase in gross profit of \$110.7 million, or 32.7%. Gross profit as a percentage of revenue increased to 17.5% for the nine months ended September 30, 2006 from 13.0% for the nine months ended September 30, 2005. The change in gross profit for the nine months ended September 30, 2006 compared to the nine months ended September 30, 2005 resulted primarily from the following:

Professional compensation expense decreased as a percentage of revenue to 49.2% for the nine months ended September 30, 2006, compared to 49.9% for the nine months ended September 30, 2005. We experienced a net decrease in professional compensation expense of \$31.1 million, or 2.4%, to \$1,264.1 million for the nine months ended September 30, 2006 from \$1,295.2 million for the nine months ended September 30, 2005. The decrease from the nine months ended September 30, 2005 was primarily due to higher professional compensation expense recorded in 2005 (as compared to 2006) related to the loss accrual for the HT Contract, partially offset by increasing payroll costs attributable to additional billable employees hired in the nine months ended September 30, 2006 in response to increased demand for our services.

Other direct contract expenses decreased as a percentage of revenue to 26.1% for the nine months ended September 30, 2006 compared to 28.7% for the nine months ended September 30, 2005. We experienced a net decrease in other direct contract expenses of \$75.8 million, or 10.2%, to \$670.7 million for the nine months ended September 30, 2006 from \$746.5 million for the nine months ended September 30, 2005. The decrease was primarily due to higher other direct contract expenses recorded in the nine months ended September 30, 2005 related to the loss accrual for the HT Contract. In addition, the decline was driven by reduced subcontractor expenses as a result of the increased use of internal resources and a decrease of resales of procured materials.

Other costs of service as a percentage of revenue decreased to 7.0% for the nine months ended September 30, 2006 from 7.6% for the nine months ended September 30, 2005. We experienced a net decrease in other costs of service of \$17.8 million, or 9.0%, to \$179.7 million for the nine months ended September 30, 2006 from \$197.5 million for the nine months ended September 30, 2005, which was primarily attributable to cost savings realized directly or indirectly from office space reduction efforts taken to date.

During the nine months ended September 30, 2006 we recorded, within the Corporate/Other operating segment, a charge of \$6.2 million related to lease, facilities and other exit activities, compared with a \$20.5 million charge related to lease, facilities and other exit activities in the nine months ended September 30, 2005. These charges

related primarily to the fair value of future lease obligations associated with office space, primarily within the EMEA and North America regions, which we will no longer be using.

Gross Profit by Segment. The following tables present certain gross profit and margin information and performance metrics for each of our reportable segments for the nine months ended September 30, 2006 and 2005. Amounts are in thousands, except percentages.

	Nine Months Ended September 30,		\$ Change	% Change
	2006	2005		
Gross Profit				
Public Services	\$ 206,985	\$ 216,213	\$ (9,228)	(4.3%)
Commercial Services	50,169	(17,852)	68,021	381.0%
Financial Services	113,797	90,927	22,870	25.2%
EMEA	103,114	79,366	23,748	29.9%
Asia Pacific	66,638	50,840	15,798	31.1%
Latin America	5,267	12,854	(7,587)	(59.0%)
Corporate/Other	(96,966)	(94,034)	(2,932)	n/m
Total	\$ 449,004	\$ 338,314	\$ 110,690	32.7%

	Nine Months Ended September 30,	
	2006	2005
Gross Profit as a % of revenue		
Public Services	20.6%	21.7%
Commercial Services	12.2%	(3.5%)
Financial Services	35.6%	32.2%
EMEA	20.6%	15.7%
Asia Pacific	24.5%	21.0%
Latin America	9.3%	20.2%
Corporate/Other	n/m	n/m
Total	17.5%	13.0%

n/m = not
meaningful

Changes in gross profit by segment were as follows:

Public Services gross profit decreased in the nine months ended September 30, 2006, despite higher revenue, due to increases in professional compensation expense related to hiring needs related to demand for our services as well as somewhat higher variable compensation payouts. This increase in compensation was partially offset by declines in subcontractor usage.

Commercial Services gross profit increased in the nine months ended September 30, 2006, despite significantly lower revenue, primarily due to a \$50.7 million year-over-year reduction in losses from the HT Contract. Other factors contributing to the increase in gross profit were the cost savings realized from 2005 workforce realignments and reduced subcontractor expenses as a result of the increased use of internal resources.

Financial Services gross profit increased in the nine months ended September 30, 2006, as higher revenue more than offset increases in compensation expenses related to a substantial increase in billable headcount. Also reducing gross profit was an increase in other direct contract expenses due to additional subcontractor usage driven by higher revenue.

EMEA gross profit increased in the nine months ended September 30, 2006, due primarily to higher revenue and improved profitability in France and Ireland along with significantly improved profitability in Spain as a result of higher utilization and lower costs. Declines in compensation expense and other direct contract expenses also contributed to the increase in gross profit, though compensation expense for 2006 continued to be affected by severance and other costs related to the internal restructuring of the Company's German practice.

Asia Pacific gross profit increased in the nine months ended September 30, 2006, primarily due to significant improvements in profitability and staff utilization in the Company's businesses in Australia and China. Due to the high demand for resources in the Japanese market and limited availability of qualified personnel, increases in subcontractor expenses served to depress the growth of gross profit in the Company's Japanese operations. Significant regional improvements in compensation expense derived from the 2005 workforce reductions in Japan and China were more than offset by additional compensation expenses associated with the use of the Company's personnel from outside the region in connection with a significant new telecommunications industry engagement in Australia.

Latin America gross profit decreased in the nine months ended September 30, 2006, as lower revenue and a slight increase in compensation expenses more than offset a decrease in other direct contract expenses. The increase in compensation expenses was driven by higher billable headcount to meet the growth of our business in the region, predominantly Brazil.

Corporate/Other consists primarily of rent expense and other facilities related charges, which increased in the nine months ended September 30, 2006 primarily due to the lease and facilities restructuring charges discussed above.

Amortization of Purchased Intangible Assets. Amortization of purchased intangible assets decreased \$0.2 million to \$1.5 million for the nine months ended September 30, 2006 from \$1.7 million for the nine months ended September 30, 2005.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased \$10.4 million, or 2.0%, to \$538.6 million for the nine months ended September 30, 2006 from \$528.2 million for the nine months ended September 30, 2005. SG&A expenses as a percentage of gross revenue increased to 21.0% in the nine months ended September 30, 2006 from 20.3% for the nine months ended September 30, 2005. This change was attributable to continuing increases in our finance and accounting costs, primarily for sub-contracted labor and other costs related to the closing of our 2005 financial statements, which were significantly offset by cost savings from the reduction in the size of the Company's sales force and reducing other business development expenses.

Interest Income. Interest income was \$6.1 million and \$5.8 million in the nine months ended September 30, 2006 and 2005, 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 the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005.

Interest Expense. Interest expense was \$26.6 million and \$25.0 million in the nine months ended September 30, 2006 and 2005, 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 the nine months ended September 30, 2006 as compared to the nine months ended September 30, 2005.

Insurance Settlement. During the nine months ended September 30, 2006, we recorded \$38.0 million for an insurance settlement in connection with our settlement with HT. See Note 9, Commitments and Contingencies, of the Notes to Consolidated Condensed Financial Statements for more information.

Other Income (Expense), net. Other income, net was \$2.9 million in the nine months ended September 30, 2006 and other expense, net was \$11.5 million in the nine months ended September 30, 2005. The balances in each period primarily consist of realized foreign currency exchange losses.

Income Tax Expense. We incurred income tax expense of \$34.4 million for the nine months ended September 30, 2006 and income tax expense of \$85.5 million for the nine months ended September 30, 2005. The principal reasons for the difference between the effective income tax rates on loss from continuing operations of (48.7)% and (38.5)% for the nine months ended September 30, 2006 and 2005, respectively, were: a change in valuation allowance, changes in income tax

reserves, non-deductible meals and entertainment, state and local income taxes, other items and the mix of income attributable to foreign versus domestic tax jurisdictions.

Net Loss. For the nine months ended September 30, 2006, we incurred a net loss of \$105.2 million, or a loss of \$0.50 per share. Contributing to the net loss for the nine months ended September 30, 2006 were \$43.1 million of losses related to the previously mentioned settlements with telecommunication clients, \$39.3 million accrued for bonuses payable to our employees, \$33.9 million of stock-based compensation expense and \$6.2 million of lease and facilities restructuring charges.

For the nine months ended September 30, 2005, we incurred a net loss of \$307.9 million, or a loss of \$1.53 per share. Included in our results for the nine months ended September 30, 2005 were \$111.8 million related to the HT Contract, \$21.4 million of non-cash compensation expense related to the vesting of Retention RSUs, a \$57.3 million increase in valuation allowance primarily against our U.S. deferred tax assets and \$20.5 million of lease and facilities restructuring charges.

Liquidity and Capital Resources

The following table summarizes the cash flow statements for the nine months ended September 30, 2006 and 2005 (amounts are in thousands):

	Nine Months Ended September 30,		
	2006	2005	2006 to 2005 Change
Net cash provided by (used in):			
Operating activities	\$ (74,524)	\$ (110,203)	\$ 35,679
Investing activities	87,799	(51,513)	139,312
Financing activities	(7,316)	288,417	(295,733)
Effect of exchange rate changes on cash and cash equivalents	7,600	(9,658)	17,258
Net increase in cash and cash equivalents	\$ 13,559	\$ 117,043	\$ (103,484)

Operating Activities. Net cash used in operating activities during the nine months ended September 30, 2006 decreased \$35.7 million over the nine months ended September 30, 2005. This decrease was primarily attributable to improved profitability and a decrease in accounts receivable of \$72.7 million during the nine months ended September 30, 2006, compared to an increase during the nine months ended September 30, 2005 of \$13.5 million. This was due to a decrease in our DSOs to 96 days at September 30, 2006 from 108 days at September 30, 2005, largely due to more aggressive collection efforts. 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.

Investing Activities. Net cash provided by investing activities during the nine months ended September 30, 2006 increased \$139.3 million over the nine months ended September 30, 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.

Financing Activities. Net cash used in financing activities for the nine months ended September 30, 2006 was \$7.3 million, primarily due to repayments of our Japanese term loans. Net cash provided by financing activities for the nine months ended September 30, 2005 was \$288.4 million, resulting primarily from the proceeds on the issuance of debentures with an aggregate principal amount of \$290.0 million.

In addition, issuances of common stock from our ESPP generated \$0 and \$14.9 million in cash during the nine months ended September 30, 2006 and 2005, 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.

For additional information on our liquidity and capital resources, please refer to Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources, included in our 2006 Form 10-K.

For information on our 2007 Credit Facility and our Discontinued 2005 Credit Facility, please refer to Note 3, Notes Payable.

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.

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 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. 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 September 2006, the FASB issued SFAS No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans (SFAS 158). SFAS 158 requires employers to fully recognize the obligations associated with single-employer defined benefit pension, retiree healthcare and other postretirement plans in their financial

statements. The provisions of SFAS 158 are effective as of the end of the fiscal year ending December 31, 2006. We adopted SFAS 158 in the fourth quarter of 2006.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of SFAS 115, (SFAS 159). SFAS 159 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. We are currently evaluating the impact of the provisions of SFAS 159.

PART I, ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For a discussion of our market risk associated with the Company's market sensitive financial instruments as of December 31, 2006, see "Quantitative and Qualitative Disclosures About Market Risk" in Part II, Item 7A, of our 2006 Form 10-K. There have been no material changes as of September 30, 2006 to our market risk exposure disclosed in our 2006 Form 10-K.

PART I, ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

As of the end of the period covered by this Quarterly 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 as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2006, management concluded that, as of December 31, 2006 and September 30, 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 for the year ended December 31, 2006, we performed additional procedures, as disclosed in Form 10K for the year ended December 31, 2006, so that our consolidated financial statements as of and for the year ended December 31, 2006, including quarterly periods, are presented in accordance with generally accepted accounting principles in the United States of America (GAAP). 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 and our consolidated condensed financial statements for the quarter ended September 30, 2006.

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

Management is committed to continuing efforts aimed at fully achieving an operationally effective control environment and timely filing of information that is required to be filed under the Exchange Act. The remediation efforts, as noted in the Item 9A included in our Annual Report on Form 10-K for the year ended December 31, 2006, will enable 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. These efforts 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

There have been no changes 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.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Please refer to Item 3, "Legal Proceedings," included in our 2006 Form 10-K, which section is incorporated herein by reference and filed as Exhibit 99.1 to this Quarterly Report.

ITEM 1A. RISK FACTORS

For a discussion of potential risks and uncertainties relating to our business, please refer to Item 1A, "Risk Factors," included in our 2006 Form 10-K. There have been no material changes to the risk factors disclosed in our 2006 Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Sales of Securities Not Registered Under the Securities Act

None.

Issuer Purchases of Equity Securities

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5. OTHER INFORMATION

a) None.

b) None.

ITEM 6. EXHIBITS

a) Exhibits

Exhibit

No.	Description
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 ending 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 ending 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	Amendment No. 5 to Amended and Restated 401(k) Plan, effective as of September 14, 2006, which is incorporated by reference to Exhibit 10.31 from the Company's Form 10-K for the year ended December 31, 2006.
10.2	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.
10.3	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.
10.4	

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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.

- 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.
- 99.1 Legal Proceedings section of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BearingPoint, Inc.

DATE: June 28, 2007

By: /s/ Judy A. Ethell
Judy A. Ethell
Chief Financial Officer