EXPONENT INC
Form 10-K405
March 28, 2002

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

FORM 10-K

x **Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 28, 2001.**

OR

¨ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from _____ to _____.**

Commission File Number 0-18655

EXPONENT, INC.
(Exact name of registrant as specified in its charter)

Delaware	**77-0218904**
(State or other jurisdiction of incorporation or organization)	**(IRS employer identification no.)**

149 Commonwealth Drive, Menlo Park, California 94025
(Address of principal executive offices, including zip code)

Registrant s telephone number, including area code: (650) 326-9400

Securities registered pursuant to Section 12(b) of the Act: None

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

Common Stock, $.001 par value
(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

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

The aggregate market value of the voting stock held by non-affiliates of the registrant based on the closing sale price of the Common Stock as reported on the NASDAQ National Market on March 15, 2002, was approximately $72,489,194.

The number of shares of the issuer s Common Stock outstanding as of March 15, 2002 was 6,567,716.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s definitive Proxy Statement for the Registrant s 2002 Annual Meeting of Stockholders to be held on June 13, 2002, are incorporated by reference into Part III of this Form 10-K.

EXPONENT, INC.
FORM 10-K ANNUAL REPORT
FISCAL YEAR ENDED DECEMBER 28, 2001
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FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains, and incorporates by reference, certain forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995, and the rules promulgated pursuant to the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended thereto under) that are based on the beliefs of the Company s management, as well as assumptions made by and information currently available to the Company s management. Such forward-looking statements are subject to the safe harbor created by the Private Securities Litigation Reform Act of 1995. When used in this document and in the documents incorporated herein by reference, the words anticipate, believe, estimate, expect and similar expressions, as they relate to the Company or its management, identify suc forward-looking statements. Such statements reflect the current views of the Company or its management with respect to future events and are subject to certain risks, uncertainties and assumptions. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, the Company s actual results, performance, or achievements could differ materially from those expressed in, or implied by, any such forward-looking statements. Factors that could cause or contribute to such material differences include those discussed in this Report under the heading Factors That May Affect Future Operating Results and Market Price of Stock and elsewhere. The inclusion of such forward-looking information should not be regarded as a representation by the Company or any other person that the future events, plans, or expectations contemplated by the Company will be achieved. The Company undertakes no obligation to release publicly any updates or revisions to any such forward-looking statements that may reflect events or circumstances occurring after the date of this Report.

PART I

Item 1. Business

GENERAL

Exponent, Inc., incorporated in Delaware in 1989 (Exponent , and, together with its operating groups, the Company), is a science and engineering consulting firm that provides solutions to complex problems. Our multidisciplinary team of scientists, physicians, engineers and business consultants brings together more than 70 different disciplines to solve complicated issues facing industry and business today. Our professional staff can perform in-depth scientific research and analysis, or very rapid-response evaluations to provide our clients with the critical information they need.

In December 2000, the Company merged Exponent Failure Analysis Associates, Inc. (FaAA), Exponent Health Group, Inc. (EHG) and Exponent Environmental Group, Inc. (EEG), which previously had been wholly owned subsidiaries, into Exponent, Inc., the parent company. This change has had no effect on the reporting of our operating segments.

CLIENTS

General

Exponent serves clients in automotive, aviation, chemical, construction, energy, government, health, insurance, manufacturing, technology and other sectors of the economy. Many of our engagements are initiated by lawyers or insurance companies, whose clients anticipate or are engaged in, litigation over an alleged failure of their products, equipment or services. We have seen our services in failure prevention and technology evaluation grow as the technological complexity of products has increased over the years. We had gross revenues from continuing operations of approximately $124 million, $132 million and $112 million for fiscal years 2001, 2000 and 1999, respectively. During 2001, 2000 and 1999 approximately 21%, 21% and 20%, respectively, of our gross revenues from continuing operations were derived from professional services provided to clients, organizations and insurers related to the transportation industry. Additionally, during 2001, 2000 and 1999 we derived approximately 14%, 24% and 12%, respectively, of gross revenues from continuing operations from professional services provided to government agencies and contractors.

Pricing and Terms of Engagements

We provide our services on either a fixed-price basis or on a time and expenses basis, charging hourly rates for each staff member involved in a project, based on his or her skills and experience. Our standard rates for professionals range from $80 to $750 per hour. Our engagement agreements typically provide for monthly billing, require payment of our invoices within 30 days of receipt and permit clients to terminate an engagement at any time. Clients normally agree to indemnify our work and our personnel against liabilities arising out of the use or application of the results of our work or recommendations.

SERVICES

Recent events have heightened corporate awareness of the need to protect workers, facilities and operations. In 2001, public health and product safety were featured prominently in the news. Product recalls related to vehicle components, medical devices, food and other consumer products continue to make headlines. We are pleased that over the past year Exponent s consultants have been engaged to provide solutions to many of these emerging and challenging technical issues.

Exponent s service offerings are provided through a practice-focused format. Many projects require support from multiple practice areas. We currently operate 12 practice areas.

Biomechanics

Civil Engineering

Data Analysis

Electrical Engineering

Environmental Science

Health and
Epidemiology

Human
Factors

Human Health Risk
Assessment

Mechanical Engineering & Materials
Science

Technology
Development

Thermal
Sciences

Vehicle
Engineering

Biomechanics

Exponent s Biomechanics staff uses engineering and biomedical science to explore the cause, nature and severity of injuries. The type and distribution of injuries, combined with our extensive experience in human injury tolerance, allows us to determine forces and motions that must have occurred to produce the

injuries. Using medical records, injury analysis can frequently provide information about human dynamics that is not directly available by other means. Through close interaction with our Accident Reconstruction and Human Factors service areas, our consultants analyze the human s overall role in an accident, including likelihood, causation and severity. We are also actively involved in assessing potential injury or medical risk to individuals that utilize medical devices such as cardiac stents or orthopedic implants.

Civil Engineering

Exponent has over 30 years experience investigating all types of structural, hydrological, geotechnical, geological, geomechanical, construction and building problems, from major catastrophes to simple performance failures. The scientific investigation of these events provides our clients with a thorough assessment of damage, as well as expert analysis of causation to be used for purposes of retrofit, repair, claims adjustment or litigation. Furthermore, we use our experience to help clients before failures occur, to determine the vulnerability of their facilities to damage and to develop appropriate mitigation measures.

In 2001, our consultants were called upon to assist in several noteworthy investigations. Dr. John Osteraas, Practice Director for Civil Engineering was a member of one of the Federal Emergency Management Agency (FEMA) urban search and rescue response teams for the World Trade Center rescue and recovery efforts and continues to study the collapses and consult with interested parties. We also provided testimony in a major litigation alleging construction design defects. We have continued to assist clients with the investigation and resolution of damage claims and litigation arising from the 1994 Northridge Earthquake, and worked with the California Earthquake Authority to improve response to future earthquake insurance claims. In addition, we broadened our capabilities in the area of construction management to provide our clients economic analysis of construction delay claims.

Data Analysis

Exponent s expertise in risk analysis helps quantify how machines, vehicles, consumer products and components behave in the real world the direct measurement of risk. We advise our clients on whether design changes may increase or decrease risk, or whether overall safety justifies a particular design. Using the largest collection of accident and incident data in the world, our Data Analysis group reviews real-world performance of consumer products, transportation and other human activity. Recently a pharmaceutical manufacturer retained Exponent to provide statistical consulting and data analysis to help test the accuracy of a drug-delivery program.

Electrical Engineering

In the age of electronics, Exponent continues to be a highly sought-after player for understanding current and potential risks involving electrical and electronic components. Our team of electrical engineers performs a wide array of investigations ranging from electric power systems to semiconductor devices. We operate laboratories for testing both heavy equipment and light electronic equipment. Computers and specialized software are used to analyze electric power systems, circuits and other equipment configurations. In 2001, we were retained by the Delaware Public Service Commission (PSC) to investigate technical issues related to the proposed merger between Potomac Electric Power Company (PEPCO) and Conectiv a power delivery provider to more than one million customers in New Jersey, Delaware, Maryland and Virginia. We are conducting power flow studies, testing for network transfer capability, transmission congestion, voltage support and reactive requirements and making recommendations for improvement to the system. In the electronics and semiconductor area, our consultants continue to work with manufacturers and suppliers to assure product quality.

Environmental Science

Exponent s environmental scientists and engineers provide proven, cost-effective, scientifically defensible and realistic assessments and solutions to complex environmental issues. We offer technical, regulatory and litigation support to industries that include mining and minerals, petrochemicals, forest products, shipbuilding, railroads, aerospace and defense and trade associations. Our consultants have considerable experience in assessing damages and planning cost-effective environmental restoration solutions for corporations. We are currently responding to the increase in mold and indoor air quality issues and have increased our environmental, health and structural staff to meet the needs of our clients. Our consultants also address hydrological issues related to new housing and office complex developments around the country.

Health and Epidemiology

Exponent has one of the foremost health sciences consulting practices in the U.S. Our health practice combines the expertise and experience of MDs and Ph.D.s to provide a comprehensive perspective on

human health issues such as occupational and environmental health, pharmaceuticals, medical devices and the quality of health care. In 2001, we were retained by the California Public Utilities Commission (CPUC) to evaluate and prioritize requests from business customers for exemptions from rotating power outages based on potential impacts to public health and safety. This evaluation provided a risk-prioritized list of business customers for CPUC s consideration to grant exemptions from rotating power.

The practice utilizes consultants expertise in occupational epidemiology to examine possible work related diseases and injuries. In 2001, we undertook studies of the effects of Endocrine Disrupting Chemicals (EDC) on the population, as well as reviews of how certain medical devices, pharmaceuticals and other medical products impact human health.

Human Factors

Our Human Factors practice analyzes human cognition and behavior to guide product design decisions to provide better safety and usability. Working in conjunction with other Exponent practices, our scientists look at ways to improve product design, as well as review safety information and training to help change human behavior and reduce accidents. In 2001, our consultants published an article in the International Journal of Vehicle Design entitled Mobile communications, driver distraction and vehicle accidents. The article discussed and analyzed current research on the physical and cognitive challenges presented by using a cell phone while driving. Exponent concluded that cell phone use contributes to or causes some motor vehicle accidents, but this is also true for a variety of other potential distracters such as radios and passengers thus more research was needed to quantify the potential problem. In addition, we continue to support litigation involving potential use and misuse of consumer products.

Human Health Risk Assessment

Exponent s team of toxicologists study and analyze industry and regulatory issues relating to products and processes and their effect on humans and their environment. We provide solutions for potential environmental liabilities and effectively communicate those results with industry, regulatory personnel and the public. In 2001, we participated in extensive studies of the effect of beryllium on industry workers and convened a panel earlier this year to evaluate a relatively new clinical test that may help in identifying those who have the potential to develop an occupational disease caused by exposure to beryllium metal.

Mechanical Engineering and Materials Science

Our mechanical engineers and materials scientists have both an academic and real-world understanding of all areas of mechanical and materials engineering, including reliability and hazard evaluation, design assessment, fluid and thermal analysis and materials life prediction. We routinely work with manufacturers to assess risks to their products during their design and manufacturing phases of product development. For example, in 2001, we assisted a major consumer product manufacturer in responding to allegations of defective design by the Consumer Product Safety Commission. In addition, we assist with product recall support and provide litigation support when required. In 2001, we continued to expand our work in the biotechnology and medical device arena, providing materials analysis and mechanical design assessment of current devices, as well as products under development. We use our experience to provide our clients with a thorough comprehension of their current or potential designs to determine vulnerabilities before failures occur and to develop appropriate mitigation methods.

Technology Development

Drawing on our multidisciplinary engineering, testing and failure analysis and prevention expertise, our Technology Development practice specializes in harnessing commercial technologies to develop effective military and industrial equipment and systems.

We continue to support the development of the U.S. Army s Soldier Systems Land Warrior Program. As a result of our success leveraging Commercial-off-the-Shelf (COTS) technologies for Land Warrior, we were awarded a contract to provide materials assessment and design analysis for the Advanced Combat Uniform for the U.S. Army. In addition, in 2001, we were awarded a follow-on contract with the Defense Manpower Agency to perform reliability characterization and testing on Smartcards used throughout the Department of Defense.

Thermal Sciences

Exponent has investigated and analyzed thousands of fires and explosions ranging from high loss disasters to small insurance claims. Information gained from these analyses has assisted clients in assessing preventative measures related to the design of their products, as well as evaluating failures when they occur. In 2001, we provided engineering and

visualization consulting support for litigation surrounding the 1999 Kaiser Aluminum plant explosion. Recently the National Law Journal, one of the nation s leading legal newspapers, listed the Kaiser litigation as the top defense verdict of the year. Our Thermal Practice is investigating cause and origin issues surrounding the September 11th tragedy.

Vehicle Engineering

Our Vehicle Engineering practice provides design analysis, vehicle crash testing, component testing and accident reconstruction services to clients when they are developing new automotive products, facing unexpected performance issues, or are seeking information on how an accident occurred. At our 147-acre Test and Engineering Center in Phoenix, we develop unique test protocols using proprietary tests developed by our consulting staff. In 2001, we completed development of one such test that now provides a repeatable test technique for evaluating a roof-to-ground impact in a vehicle rollover event. Exponent developed (in conjunction with Ford Motor Company) a translating and rotating vehicle drop system. The system is well suited to developmental testing of rollover occupant protection systems and investigation of roof strength issues.

COMPETITION

The marketplace for our services is fragmented and we face different sources of competition in providing various services. In addition, the services that we provide to some of our clients can be performed in-house by those clients. However, because of liability and independence concerns, clients that have the capability to perform such services themselves often retain Exponent or other independent consultants.

In each of the foregoing areas, we believe that the principal competitive factors are: technical capability and breadth of services, ability to deliver services on a timely basis, professional reputation, knowledge of the litigation process and the ability to offer fixed fee pricing. Although we believe that we generally compete favorably in each of these areas, some of our competitors may be able to provide services acceptable to our clients at lower prices.

We believe that the barriers to entry in particular areas of engineering expertise are low and that for many of our technical disciplines, competition is increasing. In response to competitive forces in the marketplace, we continue to explore new markets for our various technical disciplines.

EMPLOYEES

As of December 28, 2001, we employed 601 full-time and part-time employees, including 364 engineering and scientific staff, 107 technical support staff and 130 administrative and support staff. Our highly skilled staff includes 305 employees with advanced degrees, of which 172 employees have achieved the level of Ph.D.

EXECUTIVE OFFICERS

The executive officers of Exponent and their ages as of March 28, 2002 are as follows:

Name	Age	Position
Michael R. Gaulke	56	President, Chief Executive Officer and Director
Subbaiah V. Malladi, Ph.D.	55	Chief Technical Officer and Director
Roger L. McCarthy, Ph.D.	53	Chairman of the Board of Directors
Richard L. Schlenker, Jr.	36	Chief Financial Officer and Corporate Secretary

Executive officers of Exponent are appointed by the Board of Directors and serve at the discretion of the Board or until the appointment of their successors. There is no family relationship between any of the directors and officers of the Company.

Michael R. Gaulke joined the Company in September 1992, as Executive Vice President and Chief Financial Officer. He was named President in March 1993 and he was appointed as a member of the Board of Directors of the Company in January 1994. He assumed his current role of President and Chief Executive Officer in June of 1996. From November 1988 to September 1992, Mr. Gaulke served as Executive Vice President and Chief Financial Officer at Raynet Corporation, a subsidiary of Raychem Corporation. Prior to joining Raynet, Mr. Gaulke was Executive Vice President and Chief Financial Officer of Spectra Physics, Inc., where he was employed from 1979 to 1988. From 1972 to 1979, Mr. Gaulke served as a consultant with McKinsey & Company. Mr. Gaulke is a member of the Board of Directors of Cymer, Inc. and serves on the Board of Advisors of the Whitehead Institute. Mr. Gaulke received a MBA (1972) in Marketing and Operations from Stanford University Graduate School of Business and a B.S. (1968) in Electrical Engineering from Oregon State University.

Subbaiah V. Malladi, Ph.D., joined the Company in 1982 as a Senior Engineer, becoming a Senior Vice President in January 1988 and a Corporate Vice President of Exponent Failure Analysis Associates, Inc. in September 1993. In October 1998, Dr. Malladi was appointed Chief Technical Officer of the Company. Dr. Malladi has also served as a director of the Company from March 1991 through September 1993. He was re-appointed as a director in April 1996 and has remained on the Board since this date. He received a Ph.D. (1980) in Mechanical Engineering from the California Institute of Technology, M.Tech (1972) in Mechanical Engineering from the Indian Institute of Technology, B.E. (1970) in Mechanical Engineering from SRI Venkateswara University, India and B.S. (1966) in Physics, Chemistry and Mathematics from Osmania University, India. Dr. Malladi is a Registered Professional Mechanical Engineer in the State of California, and a member of the following professional organizations: American Institute of Aeronautics and Astronautics; American Association for the Advancement of Science; Combustion Institute; and National Fire Protection Association.

Roger L. McCarthy, Ph.D., joined the Company in August 1978. Currently, Dr. McCarthy is Chairman of the Board of Directors and a director of the Company. From June 1996 to October 1998, he served as Chief Technical Officer of the Company and director of the Company. He was Chairman of FaAA from 1986 until its dissolution in December 2000. He has been a director of the Company since 1989 and a director of FaAA since 1980. He was Chief Executive Officer of the Company and FaAA from 1982 to June 1996. He also served as Chairman and President of the Company from 1986 to March 1993. Dr. McCarthy received his Ph.D. (1977), Mech.E. (1975) and S.M. (1973) from Massachusetts Institute of Technology and his B.S.E. (1972) in Mechanical Engineering and A.B. (1972) in Philosophy from the University of Michigan. Dr. McCarthy is a Registered Professional Engineer in the states of California and Arizona and a member of the following professional organizations: American Society of Metals; American Society of Mechanical Engineers (ASME); Safety Engineering and Risk Analysis Division of ASME; Society of Automotive Engineers; American Society for Testing and Materials; Human Factors and Ergonomics Society; National Society of Professional Engineers; American Society of Heating, Refrigeration and Air-

Conditioning Engineers; National Fire Protection Association; American Welding Society; National Safety Council; Society for Risk Analysis; and American Statistical Association.

Richard L. Schlenker, Jr. joined the Company in October 1990. Mr. Schlenker is the Chief Financial Officer and Corporate Secretary for the Company. He was appointed Chief Financial Officer in July 1999 and was appointed Secretary of the Company in November 1997. Mr. Schlenker was the Director of Corporate Development from 1998 until his appointment as CFO. He was the Manager of Corporate Development from 1996 until 1998. From 1993 to 1996, Mr. Schlenker was a Business Manager at Exponent Failure Analysis Associates, Inc. where he managed the business activities for multiple consulting practices within FaAA. Prior to 1993 he held several different positions in finance and accounting within the Company. Mr. Schlenker holds a B.S. in Finance from the University of Southern California.

Item 2. Properties

Exponent s Silicon Valley office facilities consist of a 153,738 square foot building, with office and laboratory space located on a 6.3 acre tract of land owned by us in Menlo Park California and an adjacent 27,000 square feet of leased warehouse storage space.

Our Test and Engineering Center (TEC) occupies 147 acres in Maricopa County, Arizona. We lease this land from the state of Arizona under a 30-year lease agreement that expires in January 2028 and has an option to renew for two fifteen-year periods. In September 1999, we completed construction of a new indoor test facility at the TEC. In October 2000, we completed construction of an engineering and test preparation building at the TEC. In addition, we lease office, warehouse and laboratory space in 23 other locations in 16 states, as well as in Germany.

Leases for these offices, warehouse and laboratory facilities have terms generally ranging between one to ten years. Aggregate lease payments in fiscal 2001 for all leased properties were approximately $3,742,000.

Item 3. Legal Proceedings

Exponent is not engaged in any material legal proceedings.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of security holders during the fourth quarter of fiscal 2001.

PART II

Item 5. Market for the Registrant s Common Equity and Related Stockholder Matters

Exponent s common stock is traded on the NASDAQ National Market under the symbol EXPO. The following table sets forth for the fiscal periods indicated the high and low closing sales prices for our common stock.

Stock prices by quarter	High	Low
Fiscal Year Ended January 3, 2003:		
First Quarter (through March 15, 2002)	$ 14.00	$ 12.32
Fiscal Year Ended December 28, 2001:		
First Quarter	$ 13.50	$ 9.13
Second Quarter	$ 13.00	$ 10.25
Third Quarter	$ 12.00	$ 9.05
Fourth Quarter	$ 13.00	$ 9.25
Fiscal Year Ended December 29, 2000:		
First Quarter	$ 11.00	$ 6.25
Second Quarter	$ 10.25	$ 7.25
Third Quarter	$ 9.75	$ 8.13
Fourth Quarter	$ 10.00	$ 7.13

As of March 15, 2002, there were 372 holders of record of our common stock. Because many of the shares of our common stock are held by brokers and other institutions on behalf of stockholders, we believe that there are considerably more beneficial holders of our common stock than record holders.

We have never paid cash dividends. We currently intend to retain future earnings for reinvestment in our business and, therefore, do not anticipate paying cash dividends in the foreseeable future.

Item 6. Selected Consolidated Financial Data

	Fiscal Years				
	2001	2000	1999	1998	1997
(In thousands, except per share data)					
Consolidated Statements of Operations Data:					
Revenues	$ 104,497	$ 101,598	$ 93,271	$ 80,412	$ 70,935
Operating income	$ 9,617	$ 10,662	$ 7,983	$ 4,029	$ 7,084
Income from continuing operations	$ 6,122	$ 7,428	$ 5,411	$ 3,920	$ 4,817
Net income	$ 6,122	$ 7,782	$ 5,188	$ 4,080	$ 4,262
Income per share from continuing operations:					
Basic	$ 0.94	$ $1.12	$ 0.80	$ 0.53	$ 0.67
Diluted	$ 0.85	$ $1.05	$ 0.78	$ 0.51	$ 0.65
Net income per share:					
Basic	$ 0.94	$ 1.17	$ 0.77	$ 0.55	$ 0.60
Diluted	$ 0.85	$ 1.10	$ 0.75	$ 0.53	$ 0.58
Consolidated Balance Sheet Data:					
Cash and equivalents	$ 7,815	$ 6,379	$	$ 6,082	$ 8,412
Working capital	$ 31,747	$ 24,033	$ 26,672	$ 32,571	$ 33,428
Total assets	$ 91,034	$ 85,626	$ 80,452	$ 86,985	$ 88,251
Long-term liabilities	$ 1,192	$ 886	$ 4,748	$ 16,144	$ 17,742
Total equity	$ 70,531	$ 65,337	$ 60,148	$ 58,315	$ 56,716

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

Forward looking statements

The statements in this report that are not statements of historical fact are forward-looking statements and are based on current expectations and actual results may differ materially. These forward-looking statements involve numerous risks and uncertainties that could cause actual results to differ materially, including but not limited to, the possibility that the demand for Exponent s services may decline as a result of changes in general and industry specific economic conditions and the effects of competitive services and pricing; one or more current or future claims made against us may result in substantial liabilities; and such other risks and uncertainties as are described in reports and other documents filed by us from time to time with the Securities and Exchange Commission.

Overview

Exponent, Inc. is a science and engineering consulting firm that provides solutions to complex problems. Our multidisciplinary team of scientists, physicians, engineers and business consultants brings together more than 70 different disciplines to solve complicated issues facing industry and business today. Our services include analysis of product development or product recall, regulatory compliance, discovery of potential problems related to products, people or property and impending litigation, as well as the development of highly technical new products.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our critical accounting policies are as follows:

revenue recognition;

estimating the allowance for doubtful accounts;

accounting for income taxes; and

valuing long-lived assets, intangible assets and goodwill.

Revenue recognition. We derive our revenue primarily from professional fees earned on consulting engagements and fees earned for the use of our equipment and facilities, as well as third party expenses directly associated with the services that are billed to our client. Third party expenses are included in revenues, net of related costs.The majority of our engagements are performed on time and material or fixed-price billing arrangements. On time and material type projects, revenue is generally recognized as the services are performed. On fixed-fee contracts revenue is recognized based on the estimated percentage of completion of the services rendered.

Significant management judgments and estimates must be made and used in connection with the revenue recognized in any accounting period. Material differences may result in the amount and timing of our revenue for any period, if we made different judgments or utilized different estimates, especially on fixed-price, percentage of completion engagements. The estimate of percentage of completion is evaluated by us, in consultation with our project managers, and is based on the estimated remaining cost to complete and project milestones.

If we determine that the collection of revenue is not reasonably assured, we defer the revenue until its collection becomes reasonably assured. We assess collection based on a number of factors, including past transaction history with the client and project manager, as well as the credit-worthiness of the client.

Allowance for doubtful accounts. The preparation of financial statements requires us to make estimates and assumptions that affect the reported amount of assets and disclosure of contingent liabilities as of the date of the financial statements and the reported amounts of revenue and expense during the period. We must make estimates of our ability to collect accounts receivable and our unbilled work-in-process. Specifically, we analyze billed accounts receivable and unbilled work-in-process based upon historical bad debts, customer concentration, customer credit-worthiness, current economic conditions and changes in customer payment terms when determining the allowance for doubtful accounts. As of December 28, 2001, our accounts receivable balance was $38.6 million, net of an allowance for doubtful accounts of $1.9 million.

Accounting for income taxes. In preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions where we operate. This process involves estimating actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and to the extent that we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance, we must include an expense within the tax provision of the statement of operations in each period, in which the allowance is increased.

Significant judgment is required in determining the provision for income taxes, deferred tax assets and liabilities and any valuation allowance against our deferred tax assets. In the event that actual results differ from these estimates or the estimates are adjusted in future periods, then we may need to establish an additional valuation allowance, which could materially impact our financial position and results of operations. Based on our current financial projections and operating plan for fiscal 2002, we currently believe that we will realize 100% of our deferred tax asset. As of December 28, 2001, we had net deferred tax assets of $2.7 million and net deferred tax liabilities of $905,000 for a net deferred tax asset of $1.8 million and a valuation allowance of $0.

Valuing long-lived assets, intangible assets and goodwill. We assess the impairment of identifiable intangible assets, long-lived assets and goodwill whenever events or changes in circumstances indicate that the carrying amount may be impaired. Factors that we consider when evaluating for possible impairment include the following:

- significant under-performance relative to expected historical or projected future operating results;
- significant changes in the manner of our use of the acquired assets or the strategy for our overall business; and
- significant negative economic trends.

When determining whether the carrying value of intangibles, long-lived assets and goodwill is impaired based upon the existence of one or more of the above factors, we determine the existence of an impairment by comparison of the carrying amount of the asset to future cash flows to be generated by the

asset. If such assets are considered impaired, the impairment is measured as the amount by which the carrying value of the assets exceeds the fair value of the assets. As of December 28, 2001, net intangible assets and goodwill totaled approximately $6.9 million and our long-lived assets, consisting primarily of net property, equipment and improvements totaled $32.6 million.

In 2002, the Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets became effective. As a result, we will cease to amortize approximately $6.6 million of goodwill. We recorded $863,000 of goodwill amortization during fiscal 2001 and would have recorded $903,000 in amortization during fiscal 2002. In place of amortization, this standard requires an annual impairment review beginning in fiscal 2002. We expect to complete our initial review during the second quarter of 2002. We currently do not expect to record an impairment charge upon completion of the initial impairment review; however, we cannot provide assurance that, at the time of the review, a material impairment will not be recorded.

CONSOLIDATED RESULTS OF OPERATIONS

The following table sets forth for the periods indicated, the percentage of revenue of certain items in our consolidated statements of operations and the percentage increase (decrease) in the dollar amount of such items year to year:

	Percentage of Revenues For Fiscal Years			Period to Period Change	
	2001	2000	1999	2001 vs.2000	2000 vs.1999
Revenues	100.0%	100.0%	100.0%	2.9%	8.9%
Operating expenses:					
Compensation and related expenses	65.3	63.5	63.9	5.8	8.1
Other operating expenses	16.6	16.6	17.5	2.7	3.9
General and administrative expenses	8.9	9.4	10.1	(2.5)	2.1
	90.8	89.5	91.5		