

Overview

We generate net revenues by providing business, economic, and information technology consulting services primarily under time and materials, fixed-price or capped-fee billing arrangements. Under time and materials billing arrangements, revenues are recognized as the services are performed. Revenues on fixed-price and capped-fee contracts are recognized using the percentage of completion method of accounting and are adjusted monthly for the cumulative impact of any revision in estimates. We determine the percentage of completion of our contracts by comparing costs incurred to date to total estimated costs. Contract costs include direct labor and expenses related to performance of the contract. We believe that the majority of our work will continue to be performed under time and materials billing arrangements. Net revenues exclude reimbursable expenses charged to clients. We typically bill on a monthly basis to monitor client satisfaction and manage our outstanding accounts receivable balances. Our net revenues are substantially derived from clients located in the United States and Canada.

Gross profit is derived from net revenues less the cost of revenues, which includes salaries, bonuses and benefits paid to consultants. Our financial performance is primarily based upon billing margin (billable daily rate less the consultant's daily cost) and personnel utilization rates (billable days divided by paid days). We monitor our engagements to manage billing and utilization rates. We derive a substantial majority of our net revenues from engagements billed on a time and materials basis. We are generally able to pass increases in our cost of revenues along to our clients to the extent that we bill engagements on a time and materials basis. We generally are unable to pass along increases in our cost of revenues with respect to engagements billed on a fixed-price or capped-fee basis. Generally, clients are billed for expenses incurred by us on the clients' behalf. In addition, we closely monitor and attempt to control expenses that are not passed through to our clients. Incentive compensation expenses paid to consultants have a large variable component relating to net revenues and profit and, therefore, vary based upon our ability to achieve our operating objectives.

Selling, general and administrative expenses consist of salaries and benefits of certain senior management and other administrative personnel and training, marketing and promotional costs. These expenses are associated with our development of new business and with our management, finance, recruiting, marketing and administrative activities. Incentive compensation expenses for certain senior management also have a significant variable component relating to net revenues and profit and, therefore, vary based upon our ability to achieve our operating objectives.

Through December 31, 1998, we and certain of our subsidiaries were treated as partnerships for federal and state income tax purposes and items of income, expense and tax credit were passed through to our respective equity holders. Nextera Business Performance Solutions Group, Inc. (formerly named Symmetrix, Inc.) and Pyramid Imaging, Inc. (subsequently merged into Nextera Business Performance Solutions Group, Inc.), two of our wholly-owned subsidiaries, were subject to federal and state income taxes for periods ended prior to January 1, 1999. Our provision for income taxes for periods ended through December 31, 1998 reflect the accrued tax liabilities of these two subsidiaries and certain items of income and loss from the ownership of Lexecon Inc. Effective December 31, 1998, we changed to corporate form and became subject to federal and state income taxes applicable to "C" corporations. Our tax provisions, both historically and for periods ending after December 31, 1998, did and are expected to vary from the federal statutory rate of 34% predominately due to valuation allowance adjustments, nondeductible goodwill amortization, utilization of post-acquisition net operating losses, state and local taxes and nondeductible meal expenses.

Preferred Stock

On December 14, 2000, the Company entered into a Note Conversion Agreement with Knowledge Universe, Inc. (the Note Conversion Agreement). Under the terms of the Note Conversion Agreement, Knowledge Universe, Inc. converted \$21,000,000 of debentures into 210,000 shares of \$0.001 par value Series A Cumulative Convertible Preferred Stock (Series A Preferred Stock). The Series A Preferred Stock bears dividends at a 10% rate from issuance through June 30, 2001 and at a 7% rate thereafter. Such dividends are payable quarterly in arrears in cash or, at the option of the Company, in additional nonassessable shares of Series A Preferred Stock.

Acquisitions

We were founded in February 1997 and have focused on building our portfolio of practice areas primarily through selective acquisitions through December 31, 1998 and, to a lesser extent, internal growth. The Company has pursued an acquisition strategy resulting in the acquisitions detailed below. Our results of operations have been, and will continue to be, affected by substantial annual non-cash amortization charges for goodwill as a result of these acquisitions being accounted for under the purchase method of accounting. For the foreseeable future, we will be unable to account for future acquisitions under the pooling-of-interests method of accounting because, among other reasons, we are a controlled subsidiary. Accordingly, our historical Consolidated Financial Statements include operating results of the acquired companies only from the effective date of each respective acquisition. We are amortizing intangible assets on a straight-line basis over 5 years for intangibles relating to personnel and principally over 40 years for all other intangibles, including goodwill. We periodically evaluate whether recent events and circumstances have occurred that indicate the acquired goodwill lives or valuation may warrant revision.

2000 Acquisition

Effective January 1, 2000, the Company acquired substantially all of the assets and certain liabilities of Cambridge Economics, Inc. ("Cambridge Economics"), a Massachusetts-based consulting firm that provides strategic, economic and business transformation and other services to a diverse group of domestic and international clients. Cambridge Economics was acquired for \$8.4 million of cash and a \$2.1 million promissory note due January 2002.

1999 Acquisitions

Effective September 30, 1999, the Company, through Sibson AP, LLC, a newly formed acquisition subsidiary of the Company, acquired substantially all of the assets of SCCAP Pty Limited ("SCCAP"), an Australian human resources consulting firm, for \$1.7 million in cash.

Effective June 1, 1999, the Company acquired substantially all of the assets and certain liabilities of The Economics Resource Group, Inc. ("ERG"), a Massachusetts-based consulting firm that provides economic and strategic services primarily to energy and other regulated industries. ERG was acquired for \$9.6 million of cash and a \$2.4 million promissory note payable January 1, 2001.

Effective May 18, 1999, the Company acquired NeoEnterprises, Inc. ("NeoEnterprises"), a Connecticut-based electronic commerce, or "e-commerce," consulting and development company. NeoEnterprises was acquired for 170,000 shares of Class A Common Stock.

Effective January 29, 1999, the Company acquired the stock of The Alexander Corporation Limited ("Alexander"), a United Kingdom-based human resources consulting firm. Alexander was acquired for (pound)360,000 (approximately \$590,000) and 150,000 shares of Class A Common Stock, including the payment of (pound)60,000 (approximately \$100,000) in final satisfaction of amounts payable under an earnout arrangement.

1998 Acquisitions

Effective December 31, 1998, the Company acquired Lexecon Inc. ("Lexecon"), an Illinois-based economic consulting firm. Lexecon was acquired for \$31.1 million in cash and 4,266,240 shares of Class A Common Stock, including 1,450,240 shares of Class A Common Stock which were determined based upon the price per share in the initial public offering of the Company's Class A common stock.

Effective August 31, 1998, Nextera acquired substantially all the assets and assumed certain liabilities of Sibson & Company, L.P. and acquired Sibson Canada, Inc., (collectively "Sibson") human resources consulting firms based in New Jersey and Toronto, Canada, respectively. Sibson was acquired for \$37.4 million in cash, 2,613,087 shares of Class A Common Stock and 197,813 exchangeable shares of Sibson Canada Co., a newly formed wholly-owned subsidiary of Nextera, that may be exchanged at the option of the holders into 197,813 shares of Class A Common Stock. The shares were exchanged in 2000.

Effective March 31, 1998, Nextera acquired substantially all of the assets and assumed certain liabilities of The Planning Technologies Group, Inc. ("PTG"), a Massachusetts-based strategy and management consulting firm. PTG was acquired for \$6.7 million in cash and 214,000 shares of Class A Common Stock.

Effective March 31, 1998, Nextera acquired Pyramid Imaging, Inc. ("Pyramid"), a California-based consulting and technology firm. Pyramid was acquired for \$10.0 million in cash and 640,000 shares of Class A Common Stock, including \$0.8 million in cash and 53,333 shares of Class A Common Stock issued during 1999 as a result of the achievement of certain revenue and pretax earnings targets related to the performance of Pyramid during the twelve months ended March 31, 1999.

Effective January 5, 1998, Nextera acquired substantially all of the assets and assumed certain liabilities of SIGMA Consulting, LLC ("SIGMA"), a New York-based management consulting firm. SIGMA was acquired for \$10.0 million in cash and 669,000 shares of Class A Common Stock.

Results of Operations

The following table sets forth our results of operations for the year ended December 31:

	2000		1999		1998	
	Amount	%	Amount	%	Amount	%
Net revenues	\$161,000	100%	\$155,955	100%	\$ 67,590	100%
Cost of revenues	98,394	61	87,835	56	44,985	67
Gross profit	62,606	39	68,120	44	22,605	33
Selling, general and						
administrative expenses	61,066	38	44,975	29	23,103	34
Amortization expense	5,436	4	4,723	3	1,722	3
Special charges	8,162	5	7,405	5	7,969	12
Income (loss) from operations	(12,058)	(8)	11,017	7	(10,189)	(15)
Other income (expense), net	(13,205)	(8)	(8,836)	(6)	(6,723)	(10)
Income (loss) before income taxes	(25,263)	(16)	2,181	1	(16,912)	(25)
Provision (benefit) for income taxes	(1,291)	(1)	(884)	(1)	243	—
Net income (loss)	\$ (23,972)	(15)%	\$ 3,065	2%	\$ (17,155)	(25)%

The following table sets forth our results of quarterly operations for the periods indicated.

	December 31, September 30,		June 30, March 31,		December 31, September 30,		June 30, March 31,		December 31, September 30,		June 30, March 31,	
	2000	2000	2000	2000	1999	1999	1999	1999	1998	1998	1998	1998
Net revenues	\$ 34,193	\$35,805	\$44,040	\$46,962	\$43,197	\$40,094	\$36,519	\$36,145	\$28,009	\$17,486	\$13,909	\$ 8,186
Cost of revenues	21,694	25,492	24,992	26,216	24,098	22,755	20,470	20,512	17,406	12,641	9,315	5,623
Gross profit	12,499	10,313	19,048	20,746	19,099	17,339	16,049	15,633	10,603	4,845	4,594	2,563
Selling, general and												
administrative expenses	16,170	17,268	14,240	13,388	12,696	11,531	10,594	10,154	8,528	7,279	4,410	2,886
Amortization expense	1,357	1,362	1,365	1,352	1,290	1,243	1,156	1,034	688	466	344	224
Special charges	6,292	—	1,870	—	1,316	—	1,705	4,384	7,002	967	—	—
Income (loss)												
from operations	(11,320)	(8,317)	1,573	6,006	3,797	4,565	2,594	61	(5,615)	(3,867)	(160)	(547)
Other income												
(expense), net	(7,545)	(2,132)	(1,828)	(1,700)	(1,240)	(1,222)	(2,591)	(3,783)	(2,404)	(1,648)	(1,104)	(1,567)
Income (loss) before												
income taxes	(18,865)	(10,449)	(255)	4,306	2,557	3,343	3	(3,722)	(8,019)	(5,515)	(1,264)	(2,114)
Provision (benefit)												
for income taxes	1,206	(4,208)	(110)	1,821	(886)	—	2	—	43	—	75	125
Net income (loss)	\$ (20,071)	\$ (6,241)	\$ (145)	\$ 2,485	\$ 3,443	\$ 3,343	\$ 1	\$ (3,722)	\$ (8,062)	\$ (5,515)	\$ (1,339)	\$ (2,239)

The following table sets forth the percentage relationship to net revenues of our results of operations for the periods indicated.

	December 31, 2000	September 30, 2000	June 30, 2000	March 31, 2000	December 31, 1999	September 30, 1999	June 30, 1999	March 31, 1999	December 31, 1998	September 30, 1998	June 30, 1998	March 31, 1998
Net revenues	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Cost of revenues	63	71	57	56	56	57	56	57	62	72	67	69
Gross profit	37	29	43	44	44	43	44	43	38	28	33	31
Selling, general and												
Administrative expenses	47	48	32	29	29	29	29	28	30	42	32	35
Amortization expense	4	4	3	3	3	3	3	3	2	3	2	3
Special charges	18	—	4	—	3	—	5	12	25	6	—	—
Income (loss)												
from Operations	(33)	(23)	4	12	9	11	7	—	(20)	(22)	(1)	(7)
Interest income												
(expense), Net	(22)	(6)	(4)	(3)	(3)	(3)	(7)	(10)	(9)	(9)	(8)	(19)
Income (loss)												
before Income taxes	(55)	(29)	—	9	6	8	—	(10)	(29)	(32)	(9)	(26)
Provision (benefit)												
for Income taxes	4	(12)	—	4	(2)	—	—	—	—	—	1	1
Net income (loss)	(59)%	(17)%	—%	5%	8%	8%	0%	(10)%	(29)%	(32)%	(10)%	(27)%

Acquisitions completed by Nextera have been accounted for under the purchase method of accounting. Accordingly, the Consolidated Financial Statements of the Company include operating results of the acquired companies only from the effective date of each respective acquisition.

Comparison of the Year Ended December 31, 2000 and the Year Ended December 31, 1999

Net Revenues

Net revenues increased 3.2% to \$161.0 million for the year ended December 31, 2000 from \$156.0 million for the year ended December 31, 1999. This increase was primarily attributable to an increase in economic consulting revenues, due in part to the inclusion of revenues relating to the acquisition of ERG effective June 30, 1999 and Cambridge Economics effective January 1, 2000. Offsetting this increase was a decrease in revenues primarily from the Company's Technology Solutions Group due principally to an industry-wide decrease in demand for such services during the second half of 2000 and, to a lesser extent, a decrease in revenues from our human capital services. The Company expects the decreased demand for technology services to continue to adversely affect its Technology Solutions Group revenues during at least the first half of 2001.

Gross Profit

Gross profit decreased 8.1% to \$62.6 million for the year ended December 31, 2000 from \$68.1 million for the year ended December 31, 1999. Gross margin as a percentage of sales decreased to 38.9% in 2000 from 43.7% in 1999. The decrease in gross margin was due primarily to lower chargeability in the Company's Technology Solutions Group. As a result of the decreased demand for technology services, the Company reduced its workforce by 100 consultants in the fourth quarter of 2000, most of whom work in the Technology Solutions Group. Annualized cost savings resulting from the workforce reduction actions is anticipated to be approximately \$16.5 million. The workforce was further reduced by an additional 67 consultants in the first quarter of 2001 due to the continued weakening demand for technology services.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased 35.8% to \$61.0 million for the year ended December 31, 2000 from \$45.0 million for the year ended December 31, 1999. As a percentage of revenues, such expenses increased to 38.0% in 2000 from 28.8% in 1999. The increase in expense resulted primarily from higher sales and marketing spending and an increase in reserves for bad debts in the Company's Technology Solutions Group. As a result of the decreased demand for technology services, the Company reduced its workforce principally in this sector by 32 administrative personnel in the fourth quarter of 2000. The increase in selling general and administrative expenses also resulted in part from the acquisitions of ERG and Cambridge Economics.

Other Expense, Net

Interest expense, net decreased to \$7.8 million for the year ended December 31, 2000 from \$8.8 million for the year ended December 31, 1999 due principally to the repayment of a portion of the Company's outstanding indebtedness with the proceeds from the Company's initial public offering of Class A Common Stock, which was completed on May 21, 1999. Offsetting this reduction in borrowings and interest expense were borrowings and expense incurred in connection with the acquisitions of ERG and Cambridge Economics and for working capital requirements.

Also included in other expense, net in 2000 was a \$5.4 million non-cash charge associated with the write down to fair market value of certain available for sale investments and other assets for which an other than temporary decline in market value was incurred.

Special Charges

In the fourth quarter 2000, the Company awarded to certain employees special incentive-related compensation awards. Such awards totaled \$6.7 million and are payable in cash and restricted stock during 2001, subject to employees remaining employed by the Company on the dates of the payments. The Company recorded a special charge of \$2.3 million in 2000 associated with the pro rata share of such payments over the associated vesting period and will record a charge for the remainder of the award in 2001.

In October and December 2000, the Company implemented a plan to reduce its consulting and administrative staffs, resulting in severance costs of approximately \$2.4 million. Approximately \$1.8 million of this charge was paid in the fourth quarter of 2000 and the remainder of the accrual is expected to be substantially paid in the first quarter of 2001. In June 2000, the Company recorded a charge of \$1.9 million as a result of severance costs incurred in connection with management changes at the Company's Technology Solutions Group. Approximately \$1.2 million of this charge was paid in 2000 and the remainder is expected to be paid ratably through January of 2002.

As a result primarily of the fourth quarter workforce reduction described above, the Company has identified and made plans to vacate certain portions of leased facilities. The Company recorded a charge of \$1.5 million associated with the cost of exiting these facilities which was included in accounts payable and accrued expenses as of December 31, 2000.

The Company granted to certain non-employee consultants options to purchase 445,245 of its Class A Common Stock at an exercise price of \$14.00 per share in 1999. Such options were fully-vested upon grant. The Company recorded a non-cash compensation expense of \$4.4 million, which represented the estimated fair value of the options calculated using the Black-Scholes model.

The Company recorded a non-cash compensation expense of \$1.7 million, principally representing the difference between the fair value of 197,760 fully-vested options granted in 1999 to certain non-stockholder employees on the date of grant of \$10.00 per share and the \$1.50 exercise price of the options. Such options were granted in final satisfaction of an agreement entered into in December 1998 under which payments totaling \$4.2 million in cash and fully-vested options to purchase 384,000 of Class A Common Stock at a purchase price of \$1.50 per share were granted during 1998.

In November 1999, in connection with a change in senior management, the Company implemented a plan to reduce its administrative staff, resulting in severance costs of approximately \$1.3 million.

Income Tax Benefit

The Company recorded an income tax benefit of \$1.3 million for the year ended December 31, 2000. Valuation allowances have been established during 2000 relating to all net deferred tax assets that must be realized through the generation of taxable income in future periods.

In light of the number and significance of acquisitions completed from January 1, 1998 through December 31, 1999, management has presented below for 1999 and 1998 a comparison of the sequential quarterly results of operations for the periods enumerated below because it believes such comparisons are the most meaningful presentation of the Company's financial results.

Comparison of Three Months Ended December 31, 1999 and Three Months Ended September 30, 1999

Net Revenues

Net revenues increased 7.7% to \$43.2 million for the three months ended December 31, 1999 from \$40.1 million for the three months ended September 30, 1999. This increase was primarily attributable to an increase in human capital revenues, due in part to the inclusion of revenues relating to the acquisition of the assets of SCCAP effective September 30, 1999, and to an increase in e-commerce and e-business revenues.

Gross Profit

Gross profit increased 10.1% to \$19.1 million for the three months ended December 31, 1999 from \$17.3 million for the three months ended September 30, 1999. Gross margin as a percentage of sales increased to 44.2% for the three months ended December 31, 1999 from 43.2% for the three months ended September 30, 1999. The increase in gross margin was due primarily to improved chargeability of our consultants in the quarter.

Consolidated Balance Sheets

(In Thousands, Except Share Data)

As of December 31,	2000	1999
Assets		
Current assets:		
Cash and cash equivalents	\$ 4,322	\$ 7,011
Accounts receivable, net of allowance for doubtful accounts of \$2,551 and \$953 at December 31, 2000 and 1999, respectively	36,890	38,930
Costs and estimated earnings in excess of billings	422	7,092
Due from affiliates	610	156
Due from officers	30	93
Income taxes receivable	4,350	—
Prepaid expenses and other current assets	2,803	2,460
Total current assets	49,427	55,742
Property and equipment, net	14,542	10,587
Intangible assets, net of accumulated amortization of \$12,136 and \$6,700 at December 31, 2000 and 1999, respectively	159,459	155,800
Other assets	10,674	4,633
Total assets	\$234,102	\$226,762
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 22,610	\$ 19,512
Notes payable to bank	187	248
Senior credit facility	8,050	—
Deferred revenue	1,758	1,505
Due to affiliates	2,503	752
Current portion of long-term debt and capital lease obligations	3,222	690
Total current liabilities	38,330	22,707
Long-term debt and capital lease obligations	3,516	4,021
Senior credit facility, net of current portion	37,972	22,946
Debentures due to affiliates, including at December 31, 2000 accrued interest thereon	10,980	29,831
Other long-term liabilities	1,327	1,200
Stockholders' equity:		
Preferred Stock, \$0.001 par value, 10,000,000 shares authorized, 600,000 authorized shares designated Series A, 210,000 Series A and no shares issued and outstanding at December 31, 2000 and 1999	21,098	—
Exchangeable shares, no par value, 2,500,000 shares authorized, no and 197,813 shares issued and outstanding at December 31, 2000 and 1999	—	495
Class A Common Stock, \$0.001 par value, 50,000,000 shares authorized, 31,396,789 and 30,633,049 shares issued at December 31, 2000 and 1999	31	31
Class B Common Stock, \$0.001 par value, zero, 4,300,000 shares authorized, 3,848,560 and 4,274,630 shares issued and outstanding at December 31, 2000 and 1999	4	4
Treasury Stock, 301,400 shares Class A Common Stock at December 31, 2000	(947)	—
Additional paid-in capital	163,263	162,299
Retained earnings (deficit)	(41,077)	(17,105)
Accumulated other comprehensive income (loss)	(395)	333
Total stockholders' equity	141,977	146,057
Total liabilities and stockholders' equity	\$234,102	\$226,762

The accompanying notes are an integral part of these financial statements.

Consolidated Statements of Operations

(In Thousands, Except Per Common Share Data)	For the Year Ended December 31, 2000	For the Year Ended December 31, 1999	For the Year Ended December 31, 1998
Net revenues	\$161,000	\$155,955	\$ 67,590
Cost of revenues	98,394	87,835	44,985
Gross profit	62,606	68,120	22,605
Selling, general and administrative expenses	61,066	44,975	23,103
Amortization expense	5,436	4,723	1,722
Special charges	8,162	7,405	7,969
Income (loss) from operations	(12,058)	11,017	(10,189)
Interest income	—	531	160
Interest expense	(7,773)	(9,367)	(6,883)
Other expense	(5,432)	—	—
Income (loss) before income taxes	(25,263)	2,181	(16,912)
Provision (benefit) for income taxes	(1,291)	(884)	243
Net income (loss)	\$ (23,972)	\$ 3,065	\$(17,155)
Net income (loss) per common share, basic	\$ (0.69)	\$ 0.10	\$ (1.14)
Net income (loss) per common share, diluted	\$ (0.69)	\$ 0.10	\$ (1.14)
Weighted average common shares outstanding,			
Basic	35,121	29,990	14,997
Weighted average common shares outstanding,			
Diluted	35,121	30,441	14,997

The accompanying notes are an integral part of these financial statements.

1. Basis of Presentation

Nextera Enterprises, Inc. (“Nextera” or the “Company”) is a leading global management-consulting firm with deep expertise in strategy, organizational management, economics and technology. Nextera’s unique consultancy combines unusually broad and distinctive experience with thought leadership and hands-on tactics and capabilities to deliver complete solutions. The Company provides companies with collaborative and integrated approaches to address complex business issues involving the relationship of knowledge, people and technology.

Nextera was formed on February 26, 1997 as Education Technology Consulting LLC and renamed Nextera Enterprises L.L.C. on April 11, 1997. Effective December 31, 1998, Nextera Enterprises L.L.C. was dissolved, at which time the Company commenced operating as Nextera Enterprises, Inc. Accordingly, the consolidated financial statements reflect the operations of the predecessor, Nextera Enterprises, L.L.C., for all periods through December 31, 1998. Stockholders’ equity has been restated to give retroactive recognition to the establishment of Nextera Enterprises, Inc. for all periods presented by reclassifying from common stock to additional paid-in capital the proceeds from the issuance of units in excess of the par value of the common stock. In addition, all references in the financial statements and notes to number of shares, per share amounts and stock option data have been restated to reflect the formation of Nextera Enterprises, Inc.

The majority stockholder of the Company is Nextera Enterprises Holdings, Inc., which is controlled by Knowledge Universe, Inc., which, in turn, is controlled by Knowledge Universe, L.L.C.

Acquisitions

The Company has used the purchase method of accounting for its acquisitions. Operating results of acquired companies have been included in the Company’s results of operations only from the effective date of each respective acquisition. Allocation of purchase price for these acquisitions was based upon estimates of the fair value of the net assets. Pro forma data is not presented for the acquisitions completed in 2000 or 1999 since the acquisitions were not material to the Company’s results of operations.

2000

Effective January 1, 2000, the Company acquired substantially all of the assets and certain liabilities of Cambridge Economics, Inc. (“Cambridge Economics”), a Massachusetts-based consulting firm that provides strategic, economic and business transformation and other services to a diverse group of domestic and international clients. Cambridge Economics was acquired for \$8.4 million of cash and a \$2.1 million promissory note due January 2002.

1999

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Effective May 18, 1999, the Company acquired NeoEnterprises, Inc. (“NeoEnterprises”), a Connecticut-based electronic commerce, or “e-commerce,” consulting and development company. NeoEnterprises was acquired for 170,000 shares of Class A Common.

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1998

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Effective January 5, 1998, Nextera acquired substantially all of the assets and assumed certain liabilities of SiGMA Consulting, LLC (“SiGMA”), a New York-based management consulting firm. SiGMA was acquired for \$10.0 million in cash and 669,000 shares of Class A Common Stock.

The following information presents the unaudited pro forma condensed results of operations for the year ended December 31, 1998 as if the acquisitions of SiGMA, PTG, Pyramid, Sibson and Lexecon had occurred on January 1, 1998. The pro forma results are presented for information purposes only and are not necessarily indicative of the future results of operations of the Company or the results of operations of the Company had the acquisitions occurred on January 1, 1998 (in thousands, except per share data).

Net revenues	\$135,167
Net loss	(12,044)
Net loss per common share, basic and diluted	\$ (0.61)

2. Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. Significant intercompany accounts and transactions have been eliminated in consolidation. The Company accounts for its investments in which it owns less than 20% of the voting stock and does not possess significant influence over the operations of the investee under the cost method of accounting.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Revenue Recognition

The Company derives its revenues from consulting services under time and materials, capped-fee and fixed-price billing arrangements. Under time and materials arrangements, revenues are recognized as the services are provided. Revenues on fixed-price and capped-fee contracts are recognized using the percentage of completion method of accounting and are adjusted monthly for the cumulative impact of any revision in estimates. The Company determines the percentage of completion of its contracts by comparing costs incurred to date to total estimated costs. Contract costs include direct labor and expenses related to the contract performance. Costs and estimated earnings in excess of billings represents revenues recognized in excess of amounts billed. Deferred revenue represents billings in excess of revenues recognized. Net revenues exclude reimbursable expenses charged to clients.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand and demand deposits accounts. The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. Cash equivalents are stated at cost, which approximates market value.

Available-for-sale Investments

The Company’s marketable equity securities are considered available-for-sale investments and are carried in “Other assets” in the accompanying consolidated balance sheet at market value, with the difference between cost and market value, net of related tax effects, recorded in the “Accumulated other comprehensive income” component of Consolidated Stockholders’ Equity. As of December 31, 2000 and 1999, the market value of available-for-sale investments was \$7,358,000 and \$1,307,000, respectively, amounts \$134,000 and \$224,000, respectively, more than the adjusted cost basis of such investments. No such investments were outstanding as of December 31, 1998. During 2000, the Company recorded a \$209,000 write down to fair market value of certain available for sale investments that had an other than temporary decline in market value. The unrealized gains (losses) component of accumulated other comprehensive income (loss) was \$70,000 and \$117,000 at December 31, 2000 and 1999, respectively.

Property and Equipment

Property and equipment are stated at cost. Depreciation is provided using the straight-line method over the estimated useful lives of the assets as follows:

Furniture and fixtures	5–7 years
Equipment	3–5 years
Software	3 years

Leasehold improvements are amortized over the lesser of the lease term or the useful life of the property. Amortization of assets under capital leases is included in depreciation.

Intangible and Other Long-lived Assets

Intangible assets consist principally of the cost in excess of assets acquired resulting from acquisitions and are being amortized on a straight-line basis over 5 years for intangibles relating to personnel and principally over 40 years for other intangibles. Other long-lived assets include, among others, investments in affiliates, certain available-for-sale investments and fixed assets. The Company assesses the carrying value and future useful life of these assets whenever events or changes in circumstances indicate that impairment may have occurred or that the future life has diminished. The Company considers the future undiscounted cash flows of the acquired companies in assessing the recoverability of these assets. If impairment is indicated through this review, the carrying amount of the intangible assets will be reduced to their respective estimated fair values as determined based upon the best information available in the circumstances. Such information likely would include a review of comparable market prices of similar assets or businesses, if available, or an estimate of fair value based upon the present value of estimated expected future cash flows. Any impairment is charged to expense in the period in which the impairment is incurred.

Financial Instruments

The carrying value of financial instruments such as cash equivalents, accounts receivable, accounts payable and accrued expenses approximate their fair values based on the short-term maturities of these instruments. The carrying value of long-term debt approximates its fair value based on references to similar instruments.

Concentration of Credit Risk

The Company provides its services to customers in diversified industries, primarily in the United States. The Company performs ongoing credit evaluations of its customers and generally does not require collateral. The Company maintains reserves for potential credit losses and such losses have been within management's expectations. During 2000, 1999 and 1998, no customer accounted for more than 10% of net revenues.

Foreign Currency Translation

Assets and liabilities of the Company's foreign subsidiaries are translated at year-end exchange rates, and revenues and expenses are translated at average exchange rates. The gains and losses resulting from the changes in exchange rates from year to year have been reported in other comprehensive income. Foreign currency transaction gains and losses are included in the accompanying statement of operations and are not material for the periods presented. The foreign currency translation component of accumulated other comprehensive income (loss) was \$(465,000) and \$216,000 at December 31, 2000 and 1999, respectively.

Basic and Diluted Earnings Per Common Share

The Company presents two earnings per share amounts, basic earnings per common share and diluted earnings per common share. Basic earnings per common share includes only the weighted average shares outstanding and excludes any dilutive effects of options, warrants and convertible securities. The dilutive effects of options, warrants and convertible securities are added to the weighted average shares outstanding in computing diluted earnings per common share. For the years ended December 31, 2000 and 1998, basic and diluted earnings per common share are the same due to the antidilutive effect of potential common shares outstanding.

Income Taxes

Deferred income taxes are provided for temporary differences between the financial reporting and the tax bases of assets and liabilities and are measured using enacted income taxes and laws that will be in effect when temporary differences are expected to reverse.

Stock-based Compensation and Other Equity Instruments

The Company has elected to follow Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25") and related Interpretations in accounting for its employee stock options. Under APB 25, because the exercise price of the Company's employee stock options equals or exceeds the market price of the underlying stock on the date of grant, no compensation expense is recognized.

The Company accounts for equity instruments issued to non-employees in exchange for goods or services using the fair value method. Accordingly, warrants issued to Knowledge Universe, Inc. in connection with an acquisition (see Note 8) have been recorded at their fair value on the date of grant.

Recently Issued Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board issued SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities ("SFAS 133"). SFAS 133 requires companies to record derivatives on the balance sheet as assets and liabilities, measured at fair value. Gains or losses resulting from changes in the value of those derivatives would be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. SFAS 133, as amended, is effective beginning in 2001. The adoption of SFAS 133 is not expected to have a material impact on the financial position or results of operations of the Company.

3. Property and Equipment

Property and equipment consists of the following:

(In Thousands)	2000	1999
As of December 31,		
Equipment	\$ 9,230	\$ 7,578
Software	3,201	1,981
Furniture and fixtures	4,208	3,100
Leasehold improvements	4,558	2,343
	21,197	15,002
Less: accumulated depreciation	6,655	4,415
Property and equipment, net	\$14,542	\$10,587

4. Intangible Assets

Intangible assets consist of the following:

(In Thousands)	2000	1999
As of December 31,		
Goodwill	\$165,547	\$156,542
Intangibles related to personnel	6,048	5,958
	171,595	162,500
Less: accumulated amortization	12,136	6,700
Intangible assets, net	\$159,459	\$155,800

5. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consist of the following:

(In Thousands)	2000	1999
As of December 31,		
Trade accounts payable	\$ 4,918	\$ 4,097
Accrued payroll and compensation	11,053	11,165
Accrued income taxes	—	1,601
Other	6,639	2,649
	\$22,610	\$19,512

6. Financing Arrangements

Notes Payable to Bank

The Company has a Canadian line of credit that provides for maximum borrowings of approximately \$300,000. Borrowings under the line are payable on demand and bear interest at Canadian prime plus 1%. As of December 31, 2000, \$187,000 was outstanding under the line.

Effective June 25, 1999, the Company consolidated its domestic notes payable to banks into an interim discretionary demand credit agreement. Borrowings under the discretionary demand credit agreement bore interest at the banks base rate and were available for working capital and acquisition financing purposes, with an aggregate limit of \$30,000,000. All borrowing under the discretionary demand credit facility were repaid on December 30, 1999 when the facility was replaced with a Senior Credit Facility.

Debentures Due to Affiliates—Short Term

On December 15, 2000, the Company entered into a debenture agreement with Knowledge Universe Capital Co. LLC, an affiliate of our majority shareholder, for borrowings of \$10,000,000. The Company borrowed \$2,500,000 on December 15, 2000, with additional funding of \$2,500,000 received on January 15, 2001 and \$5,000,000 received on February 15, 2001. Interest accrues on the debentures at a rate of 10%, compounded monthly, and is payable on the last day of each quarter. Accrued but unpaid interest is added to the outstanding principal balance. Borrowings under the debentures are due and payable on 10 days demand by the lender and interest and principal repayments are subordinated to borrowings under the Senior Credit Facility. Currently, interest is being accrued on the debentures, however, neither interest nor principal payments may be made by the Company until the lenders under the Senior Credit Facility permit such payments to be made.

Bridge Loan Payable

In August 1998, the Company secured a \$40,000,000 credit facility (the "Bridge Loan"), which bore interest during 1998 at the rate of LIBOR plus 450 basis points per annum (10.2% at December 31, 1998). Effective December 31, 1998, the Bridge Loan was amended to increase the credit facility to \$77,500,000, to add Knowledge Universe, Inc. as a lender under the credit facility and to extend the maturity to May 31, 1999. Borrowings under the amended Bridge Loan bore interest at a rate of 12% and were repaid in full during 1999.

Long-Term Debt

Senior Credit Facility

Effective December 30, 1999, the Company entered into a Senior Credit Facility which replaced and expanded the Company's previous discretionary demand credit facility. The Senior Credit Facility, which matures on March 29, 2002, currently provides for a \$25 million revolving credit arrangement, intended for general corporate purposes, and a \$30 million revolving acquisition facility. The revolving credit arrangement further contained a sublimit that provided for the issuance of letters of credit in an

amount that may not exceed \$7.5 million. Interest under the Senior Credit Facility was based, at the Company's election, on the bank's base rate plus 0.25% to 1.50% or LIBOR plus 1.5% to 2.75%, with the spread in either election determined by an overall measurement of total indebtedness to trailing earnings, as defined in the agreement. The agreement also provided for a commitment fee on unused borrowings equal to 0.35% to 0.50%. The Company incurred \$1,050,000 of upfront fees and expenses in connection with the establishment of the Senior Credit Facility, which are being amortized as interest expense over the life of the facility. The Senior Credit Facility contains covenants related to the maintenance of financial ratios, operating restrictions and restrictions on the payment of dividends and disposition of assets.

As a result of operating losses incurred during 2000, the Senior Credit Facility was amended in November and December 2000 to waive compliance with certain of these covenants and to permanently reduce borrowings available under the facility by \$2.4 million. Effective March 2001, the Senior Credit Facility was amended again to waive compliance with certain covenants through January 2002. In connection with this waiver, the Company has agreed to permanently reduce the borrowings outstanding under the facility by \$8.05 million between April 2001 and December 31, 2001. Additionally, no further borrowings or Letters of Credit may be drawn or issued under the facility. Borrowings under the amended facility will bear interest at the bank's base rate plus 3.50%, with payment of 2% of this rate deferred until January 2, 2002 and waived if the facility is fully repaid by December 15, 2001. The waiver requires the Company to pay a fee to the Senior Lenders of \$0.9 million and to issue the senior lenders warrants to purchase 1,418,351 shares of the Company's Class A Common Stock at an exercise price of \$0.86 per share, exercisable at the senior lenders' sole discretion at any time prior to 18 months after payment in full of all of the Company's obligations due under the amended Senior Credit Facility. The Company also agreed that upon the sale or other disposition (or any series of sales or dispositions) by the Company of any of the Company's assets with gross proceeds, in the aggregate, in excess of \$10,000,000, the senior lenders can elect in their sole discretion to require the Company to redeem the warrants for a \$500,000 cash payment by the Company (except to the extent prohibited by a non-waiveable applicable law or regulation). In addition, the Company has the right to call the warrants for a cash payment of \$750,000, which payment may only be made from new financing sources. Additionally, an affiliate of Knowledge Universe is obligated to deliver a guarantee to the senior lenders in the amount of \$2.5 million on or before April 17, 2001. This affiliate was granted a security interest and lien in all of the Company's assets, junior and subordinated to the security interest and lien of the senior lenders. Under the provisions of the amendment, on January 15, 2002 the Company will be required to deliver cash collateral for all outstanding letters of

credit (\$2.9 million as of March 30, 2001). The amended Senior Credit Facility contains covenants related to the maintenance of financial ratios, operating restrictions, partial payment of excess consolidated EBITA to the lenders, and restrictions on the payment of dividends and disposition of assets. The revised covenants were based on the Company's operating plan for 2001. The Company's ability to remain in compliance will be dependent on its ability to successfully execute its operating plan and take appropriate corrective actions if circumstances arise which could cause actual operating results to vary from the plan.

Debentures Due to Affiliates

In 1998, the Company issued two debentures with principal amounts of \$24,970,000 and \$23,000,000, respectively. Both debentures are due on May 1, 2002. The debentures accrue interest at a rate of 10% retroactive to the date the initial capital was funded.

During 1999, the Company repaid \$25,607,000 of principal and interest due under the Debentures. Effective August 31, 1999, in accordance with the terms of the Debenture, unpaid interest then outstanding was converted to principal, with interest accruing thereafter payable on a quarterly basis. Principal and interest amounts due under the Debentures are subordinated to borrowings under the Senior Credit Facility.

In December 2000, \$21,000,000 of the then outstanding debentures was converted into Series A Cumulative Convertible Preferred Stock (see Note 10—Series A Cumulative Convertible Preferred Stock) and dividends accruing thereafter will be added to the outstanding principal balance on a quarterly basis.

7. Income Taxes

The provision for income taxes consists of the following:

(In Thousands)	For the Year Ended December 31, 2000	For the Year Ended December 31, 1999	For the Year Ended December 31, 1998
Current:			
Federal	\$(1,291)	\$ 1,308	\$200
State	—	347	43
Total current tax provision (benefit)	(1,291)	1,655	243
Deferred:			
Federal	—	(2,158)	—
State	—	(381)	—
Total deferred tax provision (benefit)	—	(2,539)	—
Total tax provision (benefit)	\$(1,291)	\$ (884)	\$243

The reconciliation of the consolidated effective tax rate of the Company is as follows:

	For the Year Ended December 31, 2000	For the Year Ended December 31, 1999	For the Year Ended December 31, 1998
Tax (benefit) at statutory rate	(34)%	34%	(34)%
State taxes (benefit), net of federal benefit	0	(1)	0
Permanent differences	4	49	2
Loss treated as partnership flow-through for tax purposes	0	0	11
Valuation allowance adjustments	24	(123)	20
Other	1	0	2
Income tax provision (benefit)	(5)%	(41)%	1%

Other Long-term Debt

Other long-term debt consists of the following:

(In Thousands) As of December 31,	2000	1999
Unsecured note payable to a former stockholder of Symmetrix Issued in connection with a non-compete agreement. Annual payments of \$120,000 are due through May 2010. Interest accrues annually at 8.7%	\$ 780	\$ 828
Promissory note payable to former stockholders of ERG, interest at 5.0%, due January 1, 2001	2,400	2,460
Promissory note payable to former stockholders of Cambridge Economics, interest at 5.88%, due January 10, 2002	2,100	—
Other	—	11
	5,280	3,299
Less: current portion	2,452	48
Long-term debt	\$2,828	\$3,251

Annual maturities of other long-term debt for the years ending after December 31, 2000 are as follows (in thousands):

2001	\$2,452
2002	2,156
2003	62
2004	67
2005	73
2006 and thereafter	470
	\$5,280