

TETRA TECH INC  
Form 10-K  
December 28, 2006

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## FORM 10-K

(Mark One)

**ANNUAL REPORT PURSUANT TO SECTION 13  
OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the Fiscal Year Ended October 1, 2006.

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 0-19655

## TETRA TECH, INC.

(Exact name of registrant as specified in its charter)

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

**95-4148514**  
(I.R.S. Employer  
Identification No.)

**3475 East Foothill Boulevard, Pasadena, California 91107**  
(Address of principal executive offices) (Zip Code)

**(626) 351-4664**  
(Registrant's telephone number, including area code)  
Securities registered pursuant to Section 12(b) of the Act:

**Common Stock, \$.01 par value**  
(Title of class)

**The NASDAQ Stock Market LLC**  
(Name of exchange)

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes  No

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 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.

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

## Edgar Filing: TETRA TECH INC - Form 10-K

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

The aggregate market value of the registrant's common stock held by non-affiliates on March 31, 2006 was \$1.1 billion (based upon the closing price of a share of registrant's common stock as reported by the Nasdaq National Market on that date).

On December 1, 2006, 57,732,712 shares of the registrant's common stock were outstanding.

### **DOCUMENTS INCORPORATED BY REFERENCE**

Portions of registrant's Annual Report to Stockholders for the fiscal year ended October 1, 2006 are incorporated by reference in Part I and Part II of this report where indicated. Portions of registrant's Proxy Statement for its 2007 Annual Meeting of Stockholders are incorporated by reference in Part III of this report where indicated.

---

## TABLE OF CONTENTS

		Page
	<u>PART I</u>	
<u>Item 1</u>	<u>Business</u>	3
	<u>General</u>	3
	<u>Industry Overview</u>	4
	<u>The Tetra Tech Solution</u>	5
	<u>The Tetra Tech Strategy</u>	5
	<u>Project Life Cycle</u>	6
	<u>Reportable Segments</u>	7
	<u>Resource Management</u>	7
	<u>Infrastructure</u>	8
	<u>Communications</u>	9
	<u>Project Examples</u>	9
	<u>Clients</u>	10
	<u>Contracts</u>	12
	<u>Marketing and Business Development</u>	13
	<u>Acquisitions and Divestitures</u>	14
	<u>Competition</u>	14
	<u>Backlog</u>	14
	<u>Regulation</u>	15
	<u>Seasonality</u>	15
	<u>Potential Liability and Insurance</u>	16
	<u>Employees</u>	16
<u>Item 1A</u>	<u>Risk Factors</u>	17
<u>Item 1B</u>	<u>Unresolved Staff Comments</u>	29
<u>Item 2</u>	<u>Properties</u>	29
<u>Item 3</u>	<u>Legal Proceedings</u>	29
<u>Item 4</u>	<u>Submission of Matters to a Vote of Security Holders</u>	30
	<u>PART II</u>	
<u>Item 5</u>	<u>Market for Registrant's Common Equity and Related Stockholder Matters</u>	31
<u>Item 6</u>	<u>Selected Financial Data</u>	31
<u>Item 7</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	31
<u>Item 7A</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	31
<u>Item 8</u>	<u>Financial Statements and Supplementary Data</u>	31
<u>Item 9</u>	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	31
<u>Item 9A</u>	<u>Controls and Procedures</u>	31
<u>Item 9B</u>	<u>Other Information</u>	31
	<u>PART III</u>	
<u>Item 10</u>	<u>Directors and Executive Officers of the Registrant</u>	32
<u>Item 11</u>	<u>Executive Compensation</u>	32
<u>Item 12</u>	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	32
<u>Item 13</u>	<u>Certain Relationships and Related Transactions</u>	32
<u>Item 14</u>	<u>Principal Accountant Fees and Services</u>	32
	<u>PART IV</u>	
<u>Item 15</u>	<u>Exhibits and Financial Statement Schedules</u>	33
	<u>Signatures</u>	37

*This Annual Report on Form 10-K ( Report ), including the Management's Discussion and Analysis of Financial Condition and Results of Operations which is incorporated by reference from our 2006 Annual Report to Stockholders, contains forward-looking statements regarding future events and our future results that are subject to the safe harbors created under the Securities Act of 1933 (the Securities Act ) and the Securities Exchange Act of 1934 (the Exchange Act ). These statements are based on current expectations, estimates, forecasts and projections about the industries in which we operate and the beliefs and assumptions of our management. Words such as expects, anticipates, targets, goals, projects, intends, plans, believes, estimates, seeks, continues, may, variations of such words, and similar expressions are intended to identify such forward-looking statements. In addition, any statement that refers to projections of our future financial performance, our anticipated growth and trends in our businesses, and other characterizations of future events or circumstances, are forward-looking statements. Readers are cautioned that these forward-looking statements are only predictions and are subject to risks, uncertainties and assumptions that are difficult to predict, including those identified below under Risk Factors, and elsewhere herein and in the 2006 Annual Report to Stockholders. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. We undertake no obligation to revise or update publicly any forward-looking statements for any reason.*

## **PART I**

### **Item 1. Business**

#### **General**

We are a leading provider of consulting, engineering and technical services focused on water resource management and civil infrastructure. We serve our clients by defining problems and developing innovative and cost-effective solutions. Our solution usually begins with a scientific evaluation of the problem, one of our differentiating strengths. This solution may span the life cycle of a project. The steps of this life cycle include research and development, applied science and technology, engineering design, program management, construction management, and operations and maintenance.

Since our initial public offering in December 1991, we have increased the size and scope of our business, expanded our service offerings, and diversified our client base and the markets we serve through internal growth and strategic acquisitions. We expect to focus on internal growth, and to continue to pursue complementary acquisitions that expand our geographic reach and increase the breadth and depth of our service offerings to address existing and emerging markets. As of the end of fiscal 2006, we had more than 6,800 full-time equivalent employees worldwide, located primarily in North America in approximately 240 locations.

Our fiscal 2006 operating results reflect the execution of the business plan we initiated in the fourth quarter of fiscal 2004 and continued to implement in fiscal 2005 and 2006 to improve our profitability. In particular, we have been engaged in consolidation and strategic realignment efforts, which focused on exiting from the wireless communications business and the fixed-price civil construction projects. Our operating results for fiscal 2006 reflect the completed wind-down of the fixed-price civil construction business, together with the successful business development efforts in our core business markets.

We were incorporated in Delaware in February 1988 and are headquartered in Pasadena, California. The mailing address of our headquarters is 3475 East Foothill Boulevard, Pasadena, California 91107, and the telephone number at that location is (626) 351-4664. Our corporate website is located at [www.tetrattech.com](http://www.tetrattech.com). Through a link on the Investors section of our website, we make available the following filings as soon as reasonably practicable after they are electronically filed with or furnished to the Securities and Exchange Commission (SEC): our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and any amendments to those reports filed or furnished pursuant to Section 13(d) or 15(d) of the Exchange Act. All such filings are available free of charge.

## Industry Overview

Due to changing threats to human health and the environment, demographic shifts toward sunbelt states, aging infrastructure and new scientific knowledge, many government and commercial organizations face new and complex challenges. These organizations turn to technical service firms for assistance in addressing these challenges. Each organization presents its own unique set of issues and often seeks technical service firms with industry-specific expertise to analyze its problems and develop appropriate solutions. These solutions are then implemented by firms possessing the required engineering and technical service capabilities. Each of the following three business segments provide effective solutions to their clients' unique set of challenges:

*Resource Management.* The world's natural resources (water, air and soil) are inter-dependent and create a delicate balance. Factors such as agricultural and residential development, commercial construction and industrialization often upset this balance. Public concern over environmental issues, especially water quality and availability, has been a driving force behind numerous laws and regulations that are designed to prevent environmental degradation and mandate restorative measures. Government and commercial organizations are focusing on resource management to comply with environmental laws and regulations, respond to public pressure and attain operating efficiencies. Two areas particularly affected by these trends are water management and waste management.

- *Water Management.* Insufficient water supplies, concern over the cost, quality and availability of water and the aging infrastructure used to capture, safeguard and distribute water are critical social and economic concerns. According to the U.S. Environmental Protection Agency (EPA), contamination of groundwater and surface water resulting from agricultural and urban development is one of the most serious environmental problems facing the United States. To address these concerns, government and commercial organizations often seek water management technical services.

- *Waste Management.* In the past, many waste disposal practices caused significant environmental damage. Since the 1970s, more stringent controls on municipal and industrial waste have been adopted by governments around the world to protect the environment. Organizations seek waste management technical services to comply with complex and evolving environmental regulations, minimize the economic and social impact of waste generation and disposal, and realize significant cost savings through increased operating efficiencies.

*Infrastructure.* The continued population growth, the demographic shifts to sunbelt states and increased user expectations have placed significant strains on an overburdened infrastructure, thereby requiring additional development. This development includes water and wastewater treatment plants, transportation, pipelines, and communication and power networks, as well as educational, recreational and correctional facilities. In addition, as existing facilities age, they require upgrading or replacement. Further, the trend toward outsourcing services is causing public and private organizations that develop and maintain these facilities to evaluate their cost structures and establish more efficient alternatives. After September 11, 2001, the need to protect civil infrastructure and provide additional security infrastructure became more significant. The federal government has increasingly turned to technical service firms for advice and assistance, particularly at seaports and airports. These factors have increased the need for planning, engineering design, program management, construction management, and operations and maintenance services.

*Communications.* Technological change and government deregulation have spurred sweeping changes in the communications infrastructure industry. Various service providers are consolidating to offer their subscribers a comprehensive set of services and maintain dominance in their markets. As these trends continue, network service providers have turned to technical service firms for advice and assistance in planning, deploying and maintaining their communications infrastructure.



## **The Tetra Tech Solution**

We provide consulting, engineering and technical services that assist clients in identifying industry-specific problems, defining appropriate solutions and implementing those solutions. The *Engineering News Record* dated July 2006 ranked Tetra Tech as the leader in water technical services. In addition, we were ranked in the top ten in other categories, including dams and reservoirs; hazardous waste; nuclear waste; marine and port facilities; aerospace; transmission lines and cables; water transmission lines and aqueducts; and site assessment and compliance. The following factors distinguish us from our competitors:

*Start With Science.* Our staff has a strong technical foundation in natural and physical science. This strength allows us to effectively evaluate and compare potential solutions to our clients' problems.

*Listen Effectively to Clients.* The ability to listen effectively to our clients' needs is essential to our ability to develop and implement successful solutions. Even before the proposal process begins, we assist our clients by helping them define their strategic objectives and identify issues that are critical to their success. We strive to listen to numerous contacts at various levels within our clients' organizations to help us identify the key issues from a variety of perspectives. We believe that our long history and exposure to a broad client base increases our awareness of the issues being confronted by these organizations, and thereby helps us identify and solve our clients' problems.

*Capitalize on our Extensive Technical Experience.* Since the inception of our predecessor in 1966, we have provided innovative consulting and engineering services, historically focusing on cost-effective solutions to water resource management and environmental problems. We have been successful in leveraging this foundation of scientific and engineering capabilities into other market areas, including transportation and educational facilities. Our services are provided by a wide range of professionals including: archaeologists, biologists, chemical engineers, chemists, civil engineers, computer scientists, economists, electrical engineers, environmental engineers, environmental scientists, geologists, hydrogeologists, mechanical engineers, oceanographers, project managers and toxicologists. Because of the experience that we have gained from thousands of completed projects, we often are able to apply proven solutions to client problems without the time-consuming process of developing new approaches.

*Offer a Broad Range of Services.* Our depth of consulting, engineering and technical skills allows us to respond to our clients' needs at every phase of a project, including initial planning, research and development, applied science and technology, engineering design, program management and construction management. Once a particular project is completed, we also offer our clients additional value-added services such as operations and maintenance. Our expertise across industries and our broad service offerings enable us to be a single-source provider to many of our clients.

*Provide Broad Geographic Coverage and Local Expertise.* We believe that proximity to our clients is instrumental to understanding their needs and delivering comprehensive services. We have significantly broadened our geographic presence in recent years through strategic acquisitions and internal growth. We currently have operations in 49 states. We have also increased our international presence, and currently have limited operations in over 30 countries including Afghanistan, Australia, Canada, Germany, India, Iraq, Japan, the Netherlands, the Philippines, Poland, Thailand and the United Kingdom.

## **The Tetra Tech Strategy**

Our objective is to continue our growth as a leading provider of consulting, engineering and technical services in our chosen business areas. To achieve this objective, we have implemented the following strategy that we believe is integral to our success:

*Leverage Existing Client Base.* Some of our clients engage us to provide limited services. We believe that we can increase our revenue by selling additional services to our existing client base. For example, we





may be able to secure a construction management contract after working with a client on the scientific evaluation and engineering design phases of a project. In addition, we believe that our ability to offer a full spectrum of services allows us to grow our business and compete more effectively for larger projects.

*Identify and Expand into New Business Areas.* We use our consulting services and certain of our technical services as entry points to evaluate new business areas. After our consulting practice is established in a new business area, we can expand our operations by offering additional technical services. For example, based on our work in watershed management consulting services, we identified and expanded into water infrastructure engineering services.

*Focus on Public Sector Projects.* We intend to continue marketing to public sector organizations and bidding for projects to stay on the leading edge of policy development. This experience helps us identify market opportunities and enhances our ability to serve other public and commercial clients. Additionally, public sector contracts often provide more predictable revenue and returns than commercial sector contracts.

*Focus on Cash Generation.* We take a disciplined approach to monitoring, managing and improving our return on investment in each of our business areas through our attempts to negotiate appropriate contract terms, manage our contract performance to minimize schedule delays and cost overruns, and promptly bill and collect accounts receivable.

*Invest in Strategic Acquisitions.* We believe that strategic acquisitions will allow us to continue our growth in selected business areas, broaden our service offerings and extend our geographic presence. We intend to make acquisitions that will enable us to strengthen our position in certain key business areas, or further strengthen our position in our more established service offerings. We believe that our reputation makes us an attractive partner.

#### **Project Life Cycle**

We provide our clients with consulting, engineering and technical services that focus on our clients' specific needs. These needs normally follow a project life cycle that begins with scientific research and concludes with operations and maintenance. We offer these services individually or as part of our full service approach to problem solving.

- *Research and development* to formulate solutions to complex problems and develop advanced computer simulation techniques for modeling problems, ranging in scale from microscopic to global;
- *Applied science and technology* to assess a wide range of problems and develop practical and cost-effective solutions through the application of scientific methods, new technologies and data interpretation;
- *Engineering design* to provide services from concept development and initial planning and design through project completion;
- *Program management* to provide experienced and specialized program managers and project teams to assist clients in managing large and complex projects through completion;
- *Construction management* and related construction services that assist clients in minimizing the risk of cost overruns, schedule delays and contractual conflicts; and
- *Operations and maintenance* to allow clients to outsource routine functions, permitting them to streamline contractor relationships and reduce their operating costs.



## Reportable Segments

We managed our business in three reportable segments in fiscal 2006: resource management, infrastructure and communications. Management established these segments based upon the services provided, the different marketing strategies associated with these services and the specialized needs of their respective clients. During the first quarter of fiscal 2006, we developed and started implementing the initial phase of a plan to combine operating units and re-align our management structure. Through the end of fiscal 2006, we continued to implement the plan by re-aligning the leadership, defining strategic and operating plan objectives, and analyzing management information reporting requirements. We will continue to assess the impact if any, of this plan, and expect to complete this implementation in fiscal 2007.

The following table presents the approximate percentage of revenue, net of subcontractor costs, by reportable segment:

Reportable Segment	Fiscal Year		
	2006	2005	2004
Resource management	62.7 %	63.1 %	61.8 %
Infrastructure	32.7	33.1	33.3
Communications	4.6	3.8	4.9
	100.0 %	100.0 %	100.0 %

Financial information for these segments can be found in Note 15, Reportable Segments, included under the heading Notes to Consolidated Financial Statements in our 2006 Annual Report to Stockholders, which is incorporated by reference.

## Resource Management

One of our major concentrations is water resource management, in which we have a leading position in understanding the inter-relationships of water quality and human activities. We support high priority government programs for water quality improvement, environmental restoration, productive reuse of defense facilities and strategic environmental resource planning. We provide comprehensive services, including research and development, applied science and technology, engineering design, construction management, program management, and operations and maintenance. Our service offerings in the resource management segment are focused on the following project areas:

*Surface Water.* Public concern with the quality of rivers, lakes and streams, as well as coastal and marine waters, and the ensuing legislative and regulatory response, is driving demand for our services. Over the past 40 years, we, together with our predecessor, have developed a specialized set of technical skills that positions us to compete effectively for surface water and watershed management projects. We provide water resource services to federal government clients such as the EPA, the U.S. Department of Defense (DoD) and the U.S. Department of Energy (DOE), and to a broad base of commercial sector clients including those in the chemical, pharmaceutical, utility, aerospace and petroleum industries. We also provide surface water services to state and local government agencies, particularly in the area of watershed management.

*Groundwater.* Groundwater is the source of drinking water for much of the U.S. population and a substantial portion of the water used for residential, industrial and agricultural purposes. Our activities in the groundwater field are diverse and typically include projects such as investigating and identifying sources of chemical contamination, examining the extent of contamination, analyzing the speed and direction of contamination migration, and designing and evaluating remedial alternatives. In addition, we conduct monitoring studies to assess the effectiveness of groundwater treatment and extraction wells.

*Waste Management.* We currently provide a wide range of engineering and consulting services for hazardous waste contamination and remediation projects, from initial site assessment through design and implementation phases of remedial solutions. In addition, we perform risk assessments to determine the probability of adverse health effects that may result from exposure to toxic substances. We also provide waste minimization and pollution prevention services and evaluate the effectiveness of innovative technologies and novel solutions to environmental problems.

*Project Management.* We provide services to our clients relative to environmental remediation and reconstruction activities. The environmental remediation includes unexploded ordnance, both domestically and internationally. Under the Base Realignment and Closure Act, we perform reconstruction services at U.S. military locations and in other locations such as Iraq.

*Regulatory Compliance.* Our regulatory compliance services include advising our clients on the full spectrum of regulatory requirements under the Resource Conservation and Recovery Act, the Comprehensive Environmental Response, Compensation, and Liability Act, the Clean Water Act, the Clean Air Act, the National Environmental Policy Act, and other environmental laws and regulations. Although we provide services to both government and commercial sector clients, our current emphasis is on providing regulatory compliance services to the U.S. Army, Navy and Air Force.

## **Infrastructure**

In our infrastructure segment, we focus on the development of water infrastructure projects; institutional facilities; commercial, recreational, and leisure facilities; transportation projects; and systems and security projects. These facilities and projects are an essential part of everyday life and also sustain economic activity, the security of our infrastructure and the quality of life. Our engineers, architects and planners work in partnership with our clients to provide adequate infrastructure development within their financial constraints. We assist clients with infrastructure projects by providing management consulting, engineering design, program management, construction management, and operations and maintenance. Our service offerings in the infrastructure segment are focused on the following project areas:

*Water Infrastructure.* Our technical services are applied to all aspects of water quantity and quality management ranging from stormwater management through drainage and flood control projects to major water and wastewater treatment plants. Our experience includes planning, design and construction services for drinking water projects, the design of water treatment facilities and reservoirs, and the design of distribution systems including pipelines and pump stations.

*Institutional Facilities.* We provide planning, architectural, engineering and construction management services, including land development and interior building design, for educational, healthcare and research facilities. We have completed engineering and construction management projects for a wide range of clients with specialized needs such as security systems, training and audiovisual facilities, clean rooms, laboratories, medical facilities and emergency preparedness facilities.

*Commercial, Recreational and Leisure Facilities.* We specialize in the planning and design of water-related entertainment and leisure facilities such as theme park attractions and large marine aquariums. Our projects also include high-rise office buildings, museums, hotels, parks, visitor centers



and marinas. We have designed complex aquatic life support systems and provided structural, civil and mechanical engineering and design of interpretive exhibits for a series of large aquarium projects. We have also designed integrated interior building systems for heat, light, security and communications to improve building energy efficiency and cost effectiveness.

*Transportation.* We provide architectural, engineering and construction management services for transportation projects to improve public safety and mobility. Our projects include roadway improvements, commuter railway stations, airport expansions, bridges, major highways, and the repair, replacement and upgrading of older transportation facilities.

*Systems Support and Security.* We provide technology systems integration to improve national security, principally for federal infrastructure. Our projects range from infrastructure vulnerability assessments to security engineering design and project management services. We also provide systems analysis and information management to optimize the U.S. commercial aviation system, and outsourced technical services to improve national security.

### **Communications**

In the communications segment, we focus on the delivery of technical solutions necessary to design and build communications infrastructure projects. Due to our exit from the wireless communications business, the remaining portion of the communications business, known as the wired business, represents a relatively small part of our overall business. Our wired business serves clients and performs services that are similar in nature to those of the infrastructure business. These clients include state and local governments, telecommunications companies and cable operators, and the services include engineering, permitting, site acquisition and construction management.

### **Project Examples**

## Edgar Filing: TETRA TECH INC - Form 10-K

The following table presents brief examples of current projects in our three segments:

### Segment

Resource Management

#### Representative Projects

- Providing engineering services for U.S. Bureau of Reclamation projects throughout the southwestern United States, including water quality modeling, watershed management, public consensus building, and engineering solutions for water supplies.
- Assisting the EPA Office of Wastewater Management in conducting the Clean Water Needs Survey to assess financial needs for constructing wastewater treatment plants and other clean water-related infrastructure.
- Supporting environmental activities at U.S. Air Force installations worldwide to assist the U.S. Air Force in its environmental mission in the areas of environmental conservation and planning, environmental quality, environmental restoration, and design and construction.
- Providing engineering, project management and construction management to help reconstruct Iraq for the U.S. Air Force.
- Supporting environmental activities at U.S. Navy installations primarily throughout the United States to assist the U.S. Navy in protecting the coastal and marine environment.
- Providing environmental operations and maintenance services at Vandenberg Air Force Base in California. Also providing operations and maintenance services for a wastewater treatment plant and a hazardous waste collection plant, air monitoring and other services.

9

---

- Providing program management services for environmental restoration of the Rocky Mountain Arsenal, a former chemical weapons manufacturing plant.
- Providing environmental restoration services at Base Realignment and Closure (BRAC) sites for various agencies within the DoD.
- Serving as prime contractor for National Environmental Policy Act studies at DOE facilities to ensure that the DOE's proposed defense and energy related actions comply with applicable environmental regulations.
- Providing watershed planning and modeling services for the City of Milwaukee to address its combined sewer overflows into Lake Michigan.
- Upgrading information management systems and implementing ISO 14000 compliant environmental management systems for several Fortune 50 industrial clients.
- Providing planning, engineering and systems integration services to support the change from ground-based navigation to satellite navigation for all civil aviation in the United States.
- Providing engineering and technical support services to create a national missile defense system.
- Providing engineering design services for the upgrade of building systems, including air, power and data distribution systems, for several locations of a major luxury hotel chain.
- Providing engineering and construction management services for the upgrade of water distribution and treatment facilities serving Atlanta, Georgia.
- Providing planning and engineering design services for new educational facilities throughout New York.
- Assisting a leading provider of broadband services with deployment and maintenance of a high capacity broadband fiber optic network in the western and midwestern United States.
- Providing engineering design and construction management services for a fiber-to-the-premise network for eleven cities in Utah.

Infrastructure

Communications

### Clients

We provide services to a diverse base of federal, state and local government agencies, as well as commercial and international clients. The following table presents the approximate percentage of our revenue, net of subcontractor costs, by client sector:

Client Sector	Fiscal Year		
	2006	2005	2004
Federal government	46.7 %	46.7 %	46.4 %
State and local government	17.5	17.9	19.1
Commercial	35.1	35.1	33.6
International	0.7	0.3	0.9
	100.0 %	100.0 %	100.0 %



## Edgar Filing: TETRA TECH INC - Form 10-K

Federal government agencies are among our most significant clients. In fiscal 2006, the DoD, EPA and DOE accounted for 26.6%, 6.9% and 5.7% of our revenue, net of subcontractor costs, compared to 25.9%, 7.1% and 4.6% in fiscal 2005, respectively. We often support multiple programs within a single federal agency, both domestically and internationally. We assist state and local government clients in a variety of jurisdictions across the country. Our commercial sector clients include companies in the chemical, mining, pharmaceutical, aerospace, automotive, petroleum, communications and utility industries. No single commercial client accounted for more than 10% of our revenue, net of subcontractor costs, in fiscal 2006.

The following table presents a list of representative clients in our three segments. We have not included international clients because they represent a significantly smaller percentage of our client base.

Reportable Segment	Representative Clients		
	Federal Government	State and Local Governments	Commercial
Resource Management	U.S. Environmental Protection Agency; U.S. Air Force; U.S. Navy; U.S. Army; U.S. Coast Guard; U.S. Forest Service; U.S. Bureau of Reclamation; U.S. Department of Energy; U.S. Agency for International Development; Federal Energy Regulatory Commission; U.S. Postal Service	California Department of Health Services; Washington Department of Ecology; Prince Georges County, Maryland; Clarmont County, Ohio; City of San Jose, California; Salton Sea Authority	Alcoa Inc.; Lockheed Martin Corporation; Conoco Phillips Company; General Electric Company; Exelon Corporation; Hewlett-Packard Company; Unocal Corporation
Infrastructure	U.S. Army Corps of Engineers; U.S. Bureau of Reclamation; U.S. Navy; Federal Emergency Management Agency; U.S. Department of the Interior; U.S. Federal Aviation Administration; U.S. Department of Homeland Security; U.S. National Aeronautics and Space Administration	City of Breckenridge, Colorado; Washington, D.C. Department of Transportation; City of Detroit, Michigan; City of Portland, Oregon; Texas Parks and Wildlife Department; King County, Washington; Delaware Department of Transportation; Delaware Department of Corrections; Boston, Massachusetts Water and Sewer Commission	Boeing Corporation; E.I. DuPont de Nemours and Company; Ford Motor Company; General Motors Corporation; Lowe's Company; Marriott Corporation
Communications		Utah Telecommunications Open Infrastructure Agency (UTOPIA)	Comcast Cable Communications, Inc.; Verizon Communications

## Contracts

Our services are performed under three principal types of contracts with our clients: fixed-price, time-and-materials, and cost-plus. The following table presents the approximate percentage of our revenue, net of subcontractor costs, by contract type:

Contract Type	Fiscal Year		
	2006	2005	2004
Fixed-price	33.5 %	33.8 %	30.5 %
Time-and-materials	43.0	47.7	43.9
Cost-plus	23.5	18.5	25.6
	100.0 %	100.0 %	100.0 %

Our clients select the type of contract we enter into for a particular engagement. Under a fixed-price contract, the client agrees to pay a specified price for our performance of the entire contract or a specified portion of the contract. Fixed-price contracts carry certain inherent risks, including risks of losses from underestimating costs, delays in project completion, problems with new technologies, price increases for materials, and economic and other changes that may occur over the contract period. Consequently, the profitability, if any, of fixed-price contracts may vary substantially. Under our time-and-materials contracts, we are paid for labor at negotiated hourly billing rates and for other expenses. Profitability on these contracts is driven by billable headcount and cost control. Many of our time-and-materials contracts are subject to maximum contract values and, accordingly, revenue related to these contracts is recognized as if these contracts were fixed-price contracts. Under our cost-plus contracts, we are reimbursed for allowable costs and fees, which may be fixed or performance-based. If our costs exceed the contract ceiling or are not allowable, we may not be able to obtain full reimbursement. Further, the amount of the fee received for a cost-plus award fee contract partially depends upon the client's discretionary periodic assessment of our performance on that contract.

Some contracts made with the federal government are subject to annual approval of funding. Federal government agencies may impose spending restrictions that limit the continued funding of our existing contracts and may limit our ability to obtain additional contracts. These limitations, if significant, could have a material adverse effect on us. All contracts made with the federal government may be terminated by the government at any time, with or without cause.

Federal government agencies have formal policies against continuing or awarding contracts that would create actual or potential conflicts of interest with other activities of a contractor. These policies may prevent us in certain cases from bidding for or performing government contracts resulting from or related to certain work we have performed. In addition, services performed for a commercial or government sector client may create conflicts of interest that preclude or limit our ability to obtain work for a private organization. We attempt to identify actual or potential conflicts of interest and to minimize the possibility that such conflicts could affect our work under current contracts or our ability to compete for future contracts. We have, on occasion, declined to bid on a project because of an existing or potential conflict of interest.

Our contracts with the federal government are subject to audit by the government, primarily by the Defense Contract Audit Agency (DCAA). The DCAA generally seeks to: (1) identify and evaluate all activities that either contribute to, or have an impact on, proposed or incurred costs of government contracts; (2) evaluate the contractor's policies, procedures, controls and performance; and (3) prevent or avoid wasteful, careless and inefficient production or service. To accomplish this, the DCAA examines our internal control systems, management policies and financial capability; evaluates the accuracy, reliability and reasonableness of our cost representations and records; and assesses compliance by us with Cost Accounting Standards (CAS) and defective-pricing clauses found within the Federal Acquisition

Regulations (FAR). The DCAA also performs the annual review of our overhead rates and assists in the establishment of our final rates. This review focuses on the allowability of cost items and the applicability of CAS. The DCAA also audits cost-based contracts, including the close-out of those contracts.

The DCAA also reviews all types of federal proposals, including those of award, administration, modification and re-pricing. The DCAA considers our cost accounting system, estimating methods and procedures, and specific proposal requirements. Operational audits are also performed by the DCAA. A review of our operations at every major organizational level is also conducted during the proposal review period. During the course of its audit, the DCAA may disallow costs if it determines that we accounted for such costs in a manner inconsistent with CAS. Under a government contract, only those costs that are reasonable, allocable and allowable are recoverable. A disallowance of costs by the DCAA could have a material adverse effect on us.

We maintain controls to avoid the occurrence of fraud and other unlawful activities due to our corporate policies and the severity of the legal remedies available to the government, including the required payment of damages and/or penalties, criminal and civil sanctions, and debarment. In addition, we maintain preventative audit programs and mitigation measures to ensure that appropriate control systems are in place.

We provide our services under contracts, purchase orders or retainer letters. Our policy provides that all contracts must be in writing. We bill our clients in accordance with the contract terms and periodically based on costs incurred, on either an hourly-fee basis or on a percentage of completion basis, as the project progresses. Most of our agreements permit our clients to terminate the agreements without cause upon payment of fees and expenses through the date of the termination. Generally, our contracts do not require that we provide performance bonds. If required, a performance bond, issued by a surety company, guarantees the contractor's performance under the contract. If the contractor defaults under the contract, the surety will, in its discretion, complete the job or pay the client the amount of the bond. If the contractor does not have a performance bond and defaults in the performance of a contract, the contractor is responsible for all damages resulting from the breach of contract. These damages include the cost of completion, together with possible consequential damages such as lost profits.

#### **Marketing and Business Development**

We utilize both a centralized corporate marketing department and local business development groups within each of our operations. Our corporate marketing department assists management in establishing our business plan, our target markets and an overall marketing strategy. The corporate marketing department also identifies and tracks the development of large federal programs, assesses new business areas, assists in the selection of appropriate co-venturers for new projects and assists in the bid process for new projects. We market throughout the organizations we target, focusing primarily on senior representatives in government organizations and senior management in private companies. In addition, the corporate marketing department supports marketing activities company-wide by coordinating corporate promotional and professional activities, including appearances at trade shows, direct mailings and public relations.

Most business development activities are performed through our local offices by technical or project management staff. We believe that these offices and personnel have a greater understanding of local issues, laws and regulations and, therefore, can better target their marketing activities. These business development activities are coordinated by operations managers located in certain of our offices. These activities include meetings with potential clients and state, county and municipal regulators, presentations to civic and professional organizations and seminars on current technical topics.

### **Acquisitions and Divestitures**

We have historically acquired a significant number of companies and we expect to make future acquisitions. Acquisitions are inherently risky, and no assurance can be given that our previous or future acquisitions will be successful or will not have a material adverse effect on our financial position, results of operations or cash flow. All acquisitions require the approval of our Board of Directors, and those in excess of a certain size require the approval of our lenders and noteholders. Prior acquisitions have resulted in a wide range of outcomes, including some that have not performed as we had anticipated. We acquired two small engineering companies in fiscal 2006. We divested three operating units due to operating and financial performance concerns. We also ceased all revenue producing activities for an operating unit and subsequently abandoned all of its operating activities. The risks associated with acquisitions and divestitures are more fully discussed in the section of this Report entitled "Risk Factors."

### **Competition**

The market for our services is generally highly competitive. We often compete with many other firms ranging from small regional firms to large international firms.

We perform a broad spectrum of consulting, engineering and technical services across the resource management, infrastructure and communications segments. Services within these segments are provided to a client base that includes federal agencies, such as the DoD, the DOE, the U.S. Department of the Interior, the EPA and the U.S. Postal Service, state and local agencies, and the commercial sector. Our competition varies and is a function of the business areas in which, and client sectors for which, we perform our services. The number of competitors for any one procurement can vary widely, depending upon technical qualifications, the relative value of the project, geographic location, the financial terms and risks associated with the work, and any restrictions placed upon competition by the client. Historically, clients have chosen among competing firms by weighing the quality, innovation and timeliness of the firm's service versus its cost to determine which firm offers the best value. When less work becomes available in a given market, price becomes an increasingly important factor.

We believe that our principal competitors include, in alphabetical order: AECOM Technology Corporation; Arcadis NV; Black & Veatch Corporation; Brown & Caldwell; Camp, Dresser & McKee Inc.; CH2M Hill Companies Ltd.; Computer Associates International, Inc.; Earth Tech, Inc., a subsidiary of Tyco International Ltd.; Jacobs Engineering Group, Inc.; MWH Global, Inc.; Science Applications International Corporation; The Shaw Group, Inc.; TRC Companies, Inc.; URS Corporation; and Weston Solutions, Inc.

### **Backlog**

As of October 1, 2006, our backlog was \$1.1 billion, an increase of 17.7% from \$893.8 million as of October 2, 2005. The increase was primarily from our federal government clients such as the DoD, EPA and DOE, particularly with work associated with reconstruction projects in Iraq, unexploded ordnance (UXO) and environmental planning, compliance and remediation work. We include in our backlog only those contracts for which funding has been provided and work authorization have been received. We estimate that approximately \$800 million of the backlog as of October 1, 2006 will be recognized as revenue when we perform the work in fiscal 2007. However, no assurance can be given that all amounts included in the backlog will ultimately be realized, even if evidenced by written contracts. For example, certain of our contracts with the federal government and other clients can be terminated at will. If any of these clients terminate their contracts prior to completion, we may not be able to recognize that revenue.

## Regulation

We engage in various service activities that are subject to government oversight, including environmental laws and regulations, general government procurement laws and regulations, and other regulations and requirements imposed by specific government agencies with which we conduct business.

*Environmental.* A substantial portion of our business involves the planning, design, program management and construction management of pollution control facilities, as well as the assessment and management of remediation activities at hazardous waste or Superfund sites and military bases. In addition, we contract with federal government entities to destroy hazardous materials, including weapons stockpiles. These activities require us to manage, handle, remove, treat, transport and dispose of toxic or hazardous substances.

Some environmental laws, such as the federal Superfund law and similar state statutes, can impose liability upon present and former owners and operators for the entire cost of clean-up for contaminated facilities or sites, as well as generators, transporters and persons arranging for the treatment or disposal of such substances. In addition, while we strive to handle hazardous and toxic substances with care and in accordance with safe methods, the possibility of accidents, leaks, spills and the events of force majeure always exist. Humans exposed to these materials, including workers or subcontractors engaged in the transportation and disposal of hazardous materials and persons in affected areas, may be injured or become ill, resulting in lawsuits that expose us to liability that may result in substantial damage awards. Liabilities for contamination or human exposure to hazardous or toxic materials, or a failure to comply with applicable regulations, could result in substantial costs, including clean-up costs, fines and civil or criminal sanctions, third party claims for property damage or personal injury, or cessation of remediation activities.

Certain of our business operations are covered by Public Law 85-804, which provides for government indemnification against claims and damages arising out of unusually hazardous activities performed at the request of the government. Due to changes in public policies and law, however, government indemnification may not be available in the case of any future claims or liabilities relating to other hazardous activities that we undertake to perform.

*Government Procurement.* The services we provide to the federal government are subject to FAR and other rules and regulations applicable to government contracts. These rules and regulations, among other things:

- Require certification and disclosure of all cost and pricing data in connection with the contract negotiations under certain contract types;
- Impose accounting rules that define allowable and unallowable costs and otherwise govern our right to reimbursement under certain cost-based government contracts; and
- Restrict the use and dissemination of information classified for national security purposes and the exportation of certain products and technical data.

In addition, services provided to the DoD are monitored by the Defense Contract Management Agency and audited by the DCAA. Our government clients can also terminate any of their contracts, and many of our government contracts are subject to renewal or extension annually. For additional information on risks associated with our government-related business, please refer to the section entitled Risk Factors.

## Seasonality

We experience seasonal trends in our business. Our revenue is typically lower in the first quarter of our fiscal year, due primarily to the Thanksgiving, Christmas and, in certain years, New Year's holidays

that fall within the first quarter. Many of our clients' employees, as well as our own employees, take vacations during these holidays. This results in fewer billable hours worked on projects, and correspondingly, less revenue recognized. Our revenue is typically higher in the second half of the fiscal year, due to favorable weather conditions during spring and summer that result in higher billable hours. In addition, our revenue is typically higher in the fourth quarter of the fiscal year due to the federal government's fiscal year-end spending.

### **Potential Liability and Insurance**

Our business activities could expose us to potential liability under various environmental laws and under workplace health and safety regulations. In addition, we occasionally assume liability by contract under indemnification agreements. We cannot predict the magnitude of such potential liabilities.

We maintain a comprehensive general liability policy with an umbrella policy that covers losses beyond the general liability limits. We also maintain professional errors and omissions liability and contractor's pollution liability insurance policies. Currently, we have \$26.0 million of coverage per occurrence on our general liability policy, which includes a deductible of \$250,000. The errors and omissions and contractor's pollution liability insurance policies have limits of \$30.0 million per loss and in the aggregate. They include a per claim self-insured retention in the amount of \$250,000. As we expand our services into additional markets, such as fixed-price remediation with insurance and UXO services, we obtain the necessary types of insurance coverages for such activities, as required by our clients.

We obtain insurance coverage through a broker that is experienced in the professional liability field. The broker and our risk manager regularly review the adequacy of our insurance coverage. However, because there are various exclusions and retentions under our insurance policies, or an insurance carrier may become insolvent, there can be no assurance that all potential liabilities will be covered by our insurance or paid by our carrier.

We evaluate the risk associated with claims. If we determine that a loss is probable and reasonably estimable, we establish an appropriate reserve. A reserve is not established if we determine that the claim has no merit. Our historic levels of insurance coverage and reserves have been adequate. However, partially or completely uninsured claims, if successful and of significant magnitude, could have a material adverse effect on our business.

### **Employees**

As of October 1, 2006, we had more than 7,300 total employees, including more than 6,800 full-time equivalent employees. Our professional staff includes archaeologists, biologists, chemical engineers, chemists, civil engineers, computer scientists, economists, electrical engineers, environmental engineers, environmental scientists, geologists, hydrogeologists, mechanical engineers, oceanographers, project managers and toxicologists. As of October 1, 2006, we had 338 employees represented by 24 labor organizations. We consider the relationships with our employees to be good. We believe that our ability to retain and expand our staff of qualified professionals will be an important factor in determining our future growth and success. To date, we believe that we have been successful in recruiting qualified employees, but there is no assurance that we will continue to be successful in the future. On certain engagements, we supplement our consultants with independent contractors. We believe that the practice of retaining independent contractors on an engagement basis provides us with significant flexibility in adjusting professional personnel levels in response to changes in demand for our services.

**Item 1A. Risk Factors**

*Set forth below and elsewhere in this Report and in other documents we file with the SEC are risks and uncertainties that could cause actual results to differ materially from the results contemplated by the forward-looking statements contained in the Report.*

**Our quarterly and annual operating results may fluctuate significantly, which could have a negative effect on the price of our common stock**

Our quarterly and annual revenue, expenses and operating results may fluctuate significantly because of a number of factors, including:

- Unanticipated changes in contract performance that may affect profitability, particularly with contracts that are fixed-price or have funding limits;
- The seasonality of the spending cycle of our public sector clients, notably the federal government, and the spending patterns of our commercial sector clients;
- Budget constraints experienced by our federal, state and local government clients;
- Acquisitions or the integration of acquired companies;
- Divestiture or discontinuance of operating units;
- Employee hiring, utilization and turnover rates;
- The number and significance of client contracts commenced and completed during the period;
- Creditworthiness and solvency of clients;
- The ability of our clients to terminate contracts without penalties;
- Delays incurred in connection with a contract;
- The size, scope and payment terms of contracts;
- Contract negotiations on change orders and collections of related accounts receivable;
- The timing of expenses incurred for corporate initiatives;
- Reductions in the prices of services offered by our competitors;
- Threatened or pending litigation;
- The impairment of our goodwill;
- Changes in accounting rules; and
- General economic or political conditions.

Variations in any of these factors could cause significant fluctuations in our operating results from quarter to quarter and could result in net losses.

**Our failure to properly manage projects may result in additional costs or claims**

Our engagements often involve large-scale, complex projects. The quality of our performance on such projects depends in large part upon our ability to manage the relationship with our clients, and to effectively manage the project and deploy appropriate resources, including third-party contractors and our own personnel, in a timely manner. If we miscalculate the resources or time we need to complete a project with capped or fixed fees, or the resources or time we need to meet contractual milestones, our operating

17

---



results could be adversely affected. Further, any defects or errors, or failures to meet our clients' expectations, could result in claims for damages against us. Our contracts generally limit our liability for damages that arise from negligent acts, errors, mistakes or omissions in rendering services to our clients. However, we cannot be sure that these contractual provisions will protect us from liability for damages in the event we are sued.

Prior to fiscal 2006, we experienced significant project cost overruns on the performance of fixed-price construction work, other than that associated with our federal government projects. We have bid on and accepted contracts with unfavorable terms and conditions; performed on projects without properly defined scopes; maintained low levels of productivity and entered into projects that were outside our normal scope of services. Although we have implemented procedures intended to address these issues, including the exit from fixed-price civil infrastructure construction projects, no assurance can be given that we will not experience project management issues in the future.

**Demand for our services is cyclical and vulnerable to economic downturns. If the economy weakens, then our revenues, profits and our financial condition may deteriorate**

Demand for our services is cyclical and vulnerable to economic downturns, which may result in clients delaying, curtailing or canceling proposed and existing projects. Our business traditionally lags the overall recovery in the economy; therefore, our business may not recover immediately when the economy improves. If the economy weakens, then our revenues, profits and overall financial condition may deteriorate. Our state and local government clients may face budget deficits that prohibit them from funding new or existing projects. In addition, our existing and potential clients may either postpone entering into new contracts or request price concessions. Difficult financing and economic conditions may cause some of our clients to demand better pricing terms or delay payments for services we perform, thereby increasing the average number of days our receivables are outstanding. Further, these conditions may result in the inability of some of our clients to pay us for services that we have already performed. If we are not able to reduce our costs quickly enough to respond to the revenue decline from these clients, our operating results may be adversely affected. Accordingly, these factors affect our ability to forecast our future revenue and earnings from business areas that may be adversely impacted by market conditions.

**We derive the majority of our revenue from government agencies, and any disruption in government funding or in our relationship with those agencies could adversely affect our business**

In fiscal 2006, we derived approximately 64.2% of our revenue, net of subcontractor costs, from contracts with federal, state and local government agencies. Federal government agencies are among our most significant clients. These agencies generated 46.7% of our revenue, net of subcontractor costs, in fiscal 2006 as follows: 26.6% from the DoD, 6.9% from the EPA, 5.7% from the DOE, and 7.5% from various other federal agencies. A significant amount of this revenue is derived under multi-year contracts, many of which are appropriated on an annual basis. As a result, at the beginning of a project, the related contract may be only partially funded, and additional funding is normally committed only as appropriations are made in each subsequent year. Our backlog includes only the projects that have funding appropriated.

The demand for our government-related services is generally related to the level of government program funding. Accordingly, the success and further development of our business depends, in large part, upon the continued funding of these government programs and upon our ability to obtain contracts under these programs. There are several factors that could materially affect our government contracting business, including the following:

- Changes in and delays or cancellations of government programs, requirements or appropriations;
- Budget constraints or policy changes resulting in delay or curtailment of expenditures relating to the services we provide;

- Re-competes of government contracts;
- The timing and amount of tax revenue received by federal, state and local governments;
- Curtailment of the use of government contracting firms;
- The increasing preference by government agencies for contracting with small and disadvantaged businesses;
- Competing political priorities and changes in the political climate with regard to the funding or operation of the services we provide;
- The adoption of new laws or regulations affecting our contracting relationships with the federal, state or local governments;
- Unsatisfactory performance on government contracts by us or one of our subcontractors, negative government audits, or other events that may impair our relationship with the federal, state or local governments;
- A dispute with or improper activity by any of our subcontractors; and
- General economic or political conditions.

These and other factors could cause government agencies to delay or cancel programs, to reduce their orders under existing contracts, to exercise their rights to terminate contracts or not to exercise contract options for renewals or extensions. Any of these actions could have a material adverse effect on our revenue or timing of contract payments from these agencies.

**A significant shift in U.S. defense spending could harm our operations and significantly reduce our future revenues**

Revenue under contracts with the DoD represented approximately 26.6% of our revenue, net of subcontractor costs, in fiscal 2006, as noted above. While spending authorization for defense-related programs has increased significantly in recent years due to greater homeland security and foreign military commitments, as well as the trend to outsource federal government jobs to the private sector, these spending levels may decrease, remain constant or shift to programs in areas in which we do not currently provide services. In addition, we have experienced an increase in revenue for project management reconstruction services in Iraq in fiscal 2006 compared to prior years. As a result, a significant shift in U.S. defense spending could harm our operations and significantly reduce our future revenues.

**The loss of key personnel or our inability to attract and retain qualified personnel could significantly disrupt our business**

As a professional and technical services company, we are labor-intensive and therefore our ability to attract, retain and expand our senior management and our professional and technical staff is an important factor in determining our future success. With limited exceptions, we do not have employment agreements with any of these individuals. The loss of the services of any of these key personnel could adversely affect our business. Although we have obtained non-compete agreements from certain principals and stockholders of companies we have acquired, we generally do not have non-compete or employment agreements with key employees who were once equity holders of these companies. Further, many of our non-compete agreements have expired. We do not maintain key-man life insurance policies on any of our executive officers or senior managers. In addition, our consolidation efforts within our infrastructure business and our shift to a more centralized structure for the operation of our overall business have resulted, and could result further, in the loss of key employees.

The market for the qualified scientists and engineers is competitive and we may not be able to attract and retain such professionals. In addition, it may be difficult to attract and retain qualified individuals with the expertise and in the timeframe demanded by our clients. For example, some of our government contracts may require us to employ only individuals who have particular government security clearance levels. In an effort to attract key employees, we often grant them stock options, and a reduction in our stock price could impact our ability to retain these professionals.

**Our actual results could differ from the estimates and assumptions that we use to prepare our financial statements, which may significantly reduce our profits**

To prepare financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions as of the date of the financial statements, which affect the reported values of assets and liabilities and revenues and expenses and disclosures of contingent assets and liabilities. Areas requiring significant estimates by our management include:

- The application of the percentage-of-completion method of accounting, and revenue recognition on contracts, changes orders and contract claims;
- Provisions for uncollectible receivables and customer claims and recoveries of costs from subcontractors, vendors and others;
- Provisions for income taxes and related valuation allowances;
- Value of goodwill and recoverability of other intangible assets;
- Valuations of assets acquired and liabilities assumed in connection with business combinations;
- Valuation of employee benefit plans; and
- Accruals for estimated liabilities, including litigation and insurance reserves.

Our actual results could differ from those estimates, which may significantly reduce our profits.

**Our use of the percentage-of-completion method of accounting could result in reduction or reversal of previously recorded revenue and profits**

We account for most of our contracts on the percentage-of-completion method of accounting. Generally, our use of this method results in recognition of revenue and profit ratably over the life of the contract, based on the proportion of costs incurred to date to total costs expected to be incurred. The effect of revisions to revenue and estimated costs, including the achievement of award and other fees, is recorded when the amounts are known and can be reasonably estimated. Such revisions could occur in any period and their effects could be material. The uncertainties inherent in the estimating process make it possible for actual costs to vary from estimates, including reductions or reversals of previously recorded revenue and profit, and such differences could be material.

**The value of our common stock could be volatile**

Our common stock has previously experienced substantial price volatility. In addition, the stock market has experienced extreme price and volume fluctuations that have affected the market price of many companies and that have often been unrelated to the operating performance of these companies. The overall market and the price of our common stock may fluctuate greatly. The trading price of our common stock may be significantly affected by various factors, including:

- Quarter-to-quarter variations in our financial results, including revenue, profits, days sales outstanding, backlog, and other measures of financial performance or financial condition;



- Our announcements or our competitors' announcements of significant events, including acquisitions;
- Resolution of threatened or pending litigation;
- Changes in investors' and analysts' perceptions of our business or any of our competitors' businesses;
- Investors' and analysts' assessments of reports prepared or conclusions reached by third parties;
- Changes in environmental legislation;
- Investors' perceptions of our performance of services in countries in which the U.S. military is engaged, including Iraq and Afghanistan;
- Broader market fluctuations; and
- General economic or political conditions.

Additionally, volatility or a lack of positive performance in our stock price may adversely affect our ability to retain key employees, many of whom are granted stock options, the value of which is dependent on the performance of our stock price.

**There are risks associated with our acquisition strategy that could adversely impact our business and operating results**

A key part of our growth strategy is to acquire other companies that complement our lines of business or that broaden our technical capabilities and geographic presence. We expect to continue to acquire companies as an element of our growth strategy; however, our ability to make acquisitions is more restricted under the May 2005 amendments to our Credit Agreement and Note Purchase Agreement. Acquisitions involve certain known and unknown risks that could cause our actual growth or operating results to differ from our expectations or the expectations of securities analysts. For example:

- We may not be able to identify suitable acquisition candidates or to acquire additional companies on acceptable terms;
- We compete with others to acquire companies which may result in decreased availability of, or increased price for, suitable acquisition candidates;
- We may not be able to obtain the necessary financing, on favorable terms or at all, to finance any of our potential acquisitions;
- We may ultimately fail to consummate an acquisition even if we announce that we plan to acquire a company;
- We may not be able to retain key employees of an acquired company which could negatively impact that company's future performance;
- We may fail to successfully integrate or manage these acquired companies due to differences in business backgrounds or corporate cultures;
- If we fail to successfully integrate any acquired company, our reputation could be damaged. This could make it more difficult to market our services or to acquire additional companies in the future; and
- These acquired companies may not perform as we expect and we may fail to realize anticipated revenue and profits.



In addition, our acquisition strategy may divert management's attention away from our existing businesses, result in the loss of key clients or key employees, and expose us to unanticipated problems or legal liabilities, including responsibility as a successor-in-interest for undisclosed or contingent liabilities of acquired businesses or assets.

Further, acquisitions may also cause us to:

- Issue common stock that would dilute our current stockholders' ownership percentage;
- Assume liabilities, including environmental liabilities;
- Record goodwill that will be subject to impairment testing and potential impairment charges;
- Incur amortization expenses related to certain intangible assets;
- Lose existing or potential contracts as a result of conflict of interest issues;
- Incur large and immediate write-offs; or
- Become subject to litigation.

Finally, acquired companies that derive a significant portion of their revenue from the federal government and that do not follow the same cost accounting policies and billing practices as we do may be subject to larger cost disallowances for greater periods than we typically encounter. If we fail to determine the existence of unallowable costs and establish appropriate reserves in advance of an acquisition, we may be exposed to material unanticipated liabilities, which could have a material adverse effect on our business.

**If we are not able to successfully manage our growth strategy, our business and results of operations may be adversely affected**

Our expected future growth presents numerous managerial, administrative, operational and other challenges. Our ability to manage the growth of our operations will require us to continue to improve our management information systems and our other internal systems and controls. In addition, our growth will increase our need to attract, develop, motivate and retain both our management and professional employees. The inability of our management to effectively manage our growth or the inability of our employees to achieve anticipated performance could have a material adverse effect on our business.

**Adverse resolution of an Internal Revenue Service examination process may harm our financial results**

We are currently under examination by the Internal Revenue Service (IRS) for fiscal years 1997 through 2004. During the third quarter of fiscal 2006, we received a 30-day letter from IRS related to fiscal years 1997 through 2001. We are protesting the position on the letter and expect these issues to go to IRS appeals. One major issue raised by the IRS relates to the research and experimentation (R&E) credits that we claimed during the years under examination. The amount of credits recognized for financial statement purposes represents the amount that we estimate will be ultimately realizable. Should the IRS determine that the amount of R&E credits to which we are entitled is more or less than the amount recognized, we will recognize an adjustment to the income tax accounts in the period in which the determination is made. This may have a material adverse effect on our financial results. Another issue raised by the IRS relates to our tax accounting method for revenue recognition. While resolution of this matter may shift the timing of tax payment, as this is a temporary difference, there should be no material impact on our financial results upon resolution of this issue.

**If we do not successfully implement our new enterprise resource planning system, our cash flows may be impaired and we may incur further costs to integrate or upgrade our systems**

In fiscal 2004, we began implementation of a new company-wide enterprise resource planning (ERP) system, principally for accounting and project management. During fiscal 2007, we plan to convert several





of our large operating units to our ERP system. In the event we do not complete the project successfully, we may experience difficulty in accurately and timely reporting certain revenue and cost data. During the ERP implementation process, we have experienced reduced cash flows due to temporary delays in issuing invoices to our clients, which has adversely affected the timely collection of cash. Further, it is possible that the cost of completing this project could exceed our current projections and negatively impact future operating results.

**As a government contractor, we are subject to a number of procurement rules and regulations and other public sector liabilities, any deemed violation of which could lead to fines or penalties or lost business**

We must comply with and are affected by laws and regulations related to the formation, administration and performance of government contracts. For example, we must comply with the FAR, the Truth in Negotiations Act, CAS and DoD security regulations, as well as many other rules and regulations. These laws and regulations affect how we do business with our clients and, in some instances, impose added costs on our business. A violation of these laws and regulations could result in the imposition of fines and penalties against us or the termination of our contracts. Moreover, as a federal government contractor, we must maintain our status as a responsible contractor. Failure to do so could lead to suspension or debarment, making us ineligible for federal government contracts and potentially ineligible for state and local government contracts.

**Most of our government contracts are awarded through a regulated competitive bidding process, and the inability to complete existing government contracts or win new government contracts over an extended period could harm our operations and adversely affect our future revenue**

Most of our government contracts are awarded through a regulated competitive bidding process. Some government contracts are awarded to multiple competitors, which increases overall competition and pricing pressure and may require us to make sustained post-award efforts to realize revenue under the government contracts. In addition, government clients can generally terminate or modify their contracts at their convenience. Moreover, even if we are qualified to work on a new government contract, we might not be awarded the contract because of existing government policies designed to protect small businesses and underrepresented minority contractors. The inability to complete existing government contracts or win new government contracts over an extended period could harm our operations and adversely affect our future revenue.

**A negative government audit could result in an adverse adjustment of our revenue and costs, could impair our reputation, and could result in civil and criminal penalties**

Government agencies, such as the DCAA, routinely audit and investigate government contractors. These agencies review a contractor's performance under its contracts, cost structure and compliance with applicable laws, regulations and standards. If the agencies determine through these audits or reviews that we improperly allocated costs to specific contracts, they will not reimburse us for these costs. Therefore, an audit could result in substantial adjustments to our revenue and costs.

Further, although we have internal controls in place to oversee our government contracts, no assurance can be given that these controls are sufficient to prevent isolated violations of applicable laws, regulations and standards. If the agencies determine that we or one of our subcontractors engaged in improper conduct, we may be subject to civil or criminal penalties and administrative sanctions, payments, fines and suspension or prohibition from doing business with the government, any of which could materially affect our financial condition, results of operations or cash flows. In addition, we could suffer serious harm to our reputation.

**Our business and operating results could be adversely affected by our inability to accurately estimate the overall risks, revenue or costs on a contract**

We generally enter into three principal types of contracts with our clients: fixed-price, time-and-materials, and cost-plus. Under our fixed-price contracts, we receive a fixed price irrespective of the actual costs we incur and, consequently, we are exposed to a number of risks. These risks include underestimation of costs, problems with new technologies, unforeseen costs or difficulties, delays beyond our control, price increases for materials, and economic and other changes that may occur during the contract period. Under our time-and-materials contracts, we are paid for labor at negotiated hourly billing rates and for other expenses. Profitability on these contracts is driven by billable headcount and cost control. Many of our time-and-materials contracts are subject to maximum contract values and, accordingly, revenue relating to these contracts is recognized as if these contracts were fixed-price contracts. Under our cost-plus contracts, some of which are subject to contract ceiling amounts, we are reimbursed for allowable costs and fees, which may be fixed or performance-based. If our costs exceed the contract ceiling or are not allowable under the provisions of the contract or any applicable regulations, we may not be able to obtain reimbursement for all such costs.

Accounting for a contract requires judgments relative to assessing the contract's estimated risks, revenue and costs, and on making judgments on other technical issues. Due to the size and nature of many of our contracts, the estimation of overall risk, revenue and cost at completion is complicated and subject to many variables. Changes in underlying assumptions, circumstances or estimates may also adversely affect future period financial performance. If we are unable to accurately estimate the overall revenue or costs on a contract, then we may experience a lower profit or incur a loss on the contract.

**Our backlog is subject to cancellation and unexpected adjustments, and is an uncertain indicator of future operating results**

Our backlog as of October 1, 2006 was approximately \$1.1 billion. We include in backlog only those contracts for which funding has been provided and work authorizations have been received. We cannot guarantee that the revenue projected in our backlog will be realized or, if realized, will result in profits. In addition, project cancellations or scope adjustments may occur, from time to time, with respect to contracts reflected in our backlog. For example, certain of our contracts with the federal government and other clients are terminable at the discretion of the client with or without cause. These types of backlog reductions could adversely affect our revenue and margins. Accordingly, our backlog as of any particular date is an uncertain indicator of our future earnings.

**Our international operations expose us to risks such as foreign currency fluctuations and different business cultures, laws and regulations**

During fiscal 2006, we derived approximately 0.7% of our revenue, net of subcontractor costs, from international clients. Some contracts with our international clients are denominated in foreign currencies. As such, these contracts contain inherent risks including foreign currency exchange risk and the risk associated with expatriating funds from foreign countries. In addition, certain expenses are also denominated in foreign currencies. If our revenue and expenses denominated in foreign currencies increases, our exposure to foreign currency fluctuations may also increase. We periodically enter into forward exchange contracts to mitigate such foreign currency exposures.

In addition, the different business cultures associated with international operations may not be fully appreciated before we sign an agreement, and thereby expose us to risk. Likewise, we need to understand prior to signing a contract international laws and regulations, such as foreign tax and labor laws, and U.S. laws and regulations applicable to companies engaging in business outside of the United States, such as the Foreign Corrupt Practices Act. For these reasons, pricing and executing international contracts is more difficult and carries more risk than pricing and executing domestic contracts. Our experience has also shown that it is typically more difficult to collect on international work that has been performed and billed.

**If our co-venturers fail to perform their contractual obligations on a project, we could be exposed to legal liability, loss of reputation and profit reduction or loss on the project**

We occasionally enter into subcontracts, joint teaming ventures and other contractual arrangements so that we can jointly bid and perform on a particular project. Success on these joint projects depends in large part on whether our co-venturers fulfill their contractual obligations satisfactorily. If any of our co-venturers fails to satisfactorily perform their contractual obligations as a result of financial or other difficulties, we may be required to make additional investments and provide additional services in order to make up for our co-venturers' shortfall. If we are unable to adequately address our co-venturers' performance issues, then our client could terminate the joint project, exposing us to legal liability, loss of reputation and reduced profit or loss on the project. We guaranteed performance for these projects on behalf of a third-party company under a U.S. Small Business Administration program, and that company was unable to complete the projects on schedule and budget. As a result, we recorded loss reserves for the completion of certain fixed-price projects in the second quarter of fiscal 2006.

**Our future revenues depend on our ability to consistently bid and win new contracts and renew existing contracts and, therefore, our failure to effectively obtain future contracts could adversely affect our profitability**

Our future revenues and overall results of operations require us to successfully bid on new contracts and renew existing contracts. Contract proposals and negotiations are complex and frequently involve a lengthy bidding and selection process, which is affected by a number of factors including market conditions, financing arrangements and required governmental approvals. For example, a client may require us to provide a bond or letter of credit to protect the client should we fail to perform under the terms of the contract. If negative market conditions arise, or if we fail to secure adequate financial arrangements or the required governmental approval, we may not be able to pursue particular projects, which could adversely affect our profitability.

**Our inability to find qualified subcontractors could adversely affect the quality of our service and our ability to perform under certain contracts**

Under some of our contracts, we depend on the efforts and skills of subcontractors for the performance of certain tasks. Our reliance on subcontractors varies from project to project. In fiscal 2006, subcontractor costs comprised 32.2% of our revenue. The absence of qualified subcontractors with whom we have a satisfactory relationship could adversely affect the quality of our service and our ability to perform under some of our contracts.

**Changes in existing environmental laws, regulations and programs could reduce demand for our environmental services, which could cause our revenue to decline**

A significant amount of our resource management business is generated either directly or indirectly as a result of existing federal and state laws, regulations and programs related to pollution and environmental protection. Accordingly, a relaxation or repeal of these laws and regulations, or changes in governmental policies regarding the funding, implementation or enforcement of these programs, could result in a decline in demand for environmental services that may have a material adverse effect on our revenue.

**The consolidation of our client base could adversely impact our business**

Recently, there has been consolidation within our current and potential commercial client base, particularly in the telecommunications industry. Future consolidation activity could have the effect of reducing the number of our current or potential clients, and lead to an increase in the bargaining power of our remaining clients. This potential increase in bargaining power could create greater competitive pressures and effectively limit the rates we charge for our services. As a result, our revenue and margins could be adversely affected.

**Our revenue from commercial clients is significant, and the credit risks associated with certain of these clients could adversely affect our operating results**

In fiscal 2006, we derived approximately 35.1% of our revenue, net of subcontractor costs, from commercial clients. We rely upon the financial stability and creditworthiness of these clients. To the extent the credit quality of these clients deteriorates or these clients seek bankruptcy protection, our ability to collect our receivables, and ultimately our operating results, may be adversely affected. Periodically, we have experienced bad debt losses.

**Our industry is highly competitive and we may be unable to compete effectively**

Our industry is highly fragmented and intensely competitive. Our competitors are numerous, ranging from small private firms to multi-billion dollar public companies. In addition, the technical and professional aspects of our services generally do not require large upfront capital expenditures and provide limited barriers against new competitors. Some of our competitors have achieved greater market penetration in some of the markets in which we compete, and have substantially more financial resources and/or financial flexibility than we do. As a result of the number of competitors in our industry, our clients may select one of our competitors on a project due to competitive pricing or a specific skill set. These competitive forces could force us to make price concessions or otherwise reduce prices for our services, thereby causing a material adverse effect on our business, financial condition and results of operations.

**Restrictive covenants in our Credit Agreement and Note Purchase Agreement relating to our senior secured notes may restrict our ability to pursue certain business strategies**

Our Credit Agreement and Note Purchase Agreement relating to our senior secured notes restrict our ability to, among other things:

- Incur additional indebtedness;
- Create liens securing debt or other encumbrances on our assets;
- Make loans or advances;
- Pay dividends or make distributions to our stockholders;
- Purchase or redeem our stock;
- Repay indebtedness that is junior to indebtedness under our Credit Agreement and Note Purchase Agreement;
- Acquire the assets of, or merge or consolidate with, other companies; and
- Sell, lease or otherwise dispose of assets.

Our Credit Agreement and Note Purchase Agreement also require that we maintain certain financial ratios, which we may not be able to achieve. We failed to meet these required financial ratios at the end of the second quarter of fiscal 2005. We obtained waivers of the technical defaults caused by these failures and amendments to these agreements in May 2005. The covenants in these agreements may impair our ability to finance future operations or capital needs or to engage in certain business activities. Refer to Note 7, Long-Term Obligations, included under the heading Notes to Consolidated Financial Statements in our 2006 Annual Report to Stockholders, which is incorporated by reference.

**Our services expose us to significant risks of liability and it may be difficult to obtain or maintain adequate insurance coverage**

Our services involve significant risks of professional and other liabilities that may substantially exceed the fees we derive from our services. Our business activities could expose us to potential liability under various environmental laws and under workplace health and safety regulations. In addition, we sometimes



assume liability by contract under indemnification agreements. We cannot predict the magnitude of such potential liabilities.

We obtain insurance from third parties to cover our potential risks and liabilities. It is possible that we may not be able to obtain adequate insurance to meet our needs, may have to pay an excessive amount for the insurance coverage we want, or may not be able to acquire any insurance for certain types of business risks.

**Our liability for damages due to legal proceedings may harm our operating results or financial condition**

We are a party to lawsuits in the normal course of business. Various legal proceedings are currently pending against us and certain of our subsidiaries alleging, among other things, breach of contract or tort in connection with the performance of professional services. We cannot predict the outcome of these proceedings with certainty. In some actions, parties are seeking damages that exceed our insurance coverage or for which we are not insured. If we sustain damages that exceed our insurance coverage or that are not covered by insurance, there could be a material adverse effect on our business, operating results or financial condition.

**Our business activities may require our employees to travel to and work in high security risk countries, which may result in employee death or injury, repatriation costs or other unforeseen costs.**

Certain of our contracts may require our employees travel to and work in high security risk countries that are undergoing political, social and economic upheavals resulting in war, civil unrest, criminal activity or acts of terrorism. For example, we currently have employees working in Afghanistan and Iraq. As a result, we may be subject to costs related to employee death or injury, repatriation or other unforeseen circumstances.

**Our failure to implement and comply with our safety program could adversely affect our operating results or financial condition**

Our safety program is a fundamental element of our overall approach to risk management, and the implementation of the safety program is a significant issue in our dealings with our clients. We maintain an enterprise-wide group of health and safety professionals to help ensure that the services we provide are delivered safely and in accordance with standard work processes. Unsafe job sites and office environments have the potential to increase employee turnover, increase the cost of a project to our clients, expose us to types and levels of risk that are fundamentally unacceptable, and raise our operating costs. The implementation of our safety processes and procedures are monitored by various agencies and rating bureaus, and may be evaluated by certain clients in cases in which safety requirements have been established in our contracts. If we fail to meet these requirements, or to properly implement and comply with our safety program, there could be a material adverse effect on our business, operating results or financial condition.

**Our inability to obtain adequate bonding could have a material adverse effect on our future revenues and business prospects**

Many of our clients require bid and performance and surety bonds. These bonds indemnify the client should we fail to perform our obligations under the contract. If a bond is required for a particular project and we are unable to obtain an appropriate bond, we cannot pursue that project. In some instances, we are required to co-venture with a small or disadvantaged business to pursue certain federal or state contracts. In connection with these ventures, we are sometimes required to utilize our bonding capacity to cover all of the payment and performance obligations under the contract with the client. We have a bonding facility but, as is typically the case, the issuance of bonds under that facility is at the surety's sole discretion. Moreover, due to events that can negatively affect the insurance and bonding markets, bonding may be more difficult to obtain or may only be available at significant additional cost. There can be no assurance

that bonds will continue to be available to us on reasonable terms. Our inability to obtain adequate bonding and, as a result, to bid on new work could have a material adverse effect on our future revenues and business prospects.

**We may be precluded from providing certain services due to conflict of interest issues**

Many of our clients are concerned about potential or actual conflicts of interest in retaining management consultants. Federal government agencies have formal policies against continuing or awarding contracts that would create actual or potential conflicts of interest with other activities of a contractor. These policies, among other things, may prevent us from bidding for or performing government contracts resulting from or relating to certain work we have performed. In addition, services performed for a commercial or government client may create a conflict of interest that precludes or limits our ability to obtain work from other public or private organizations. We have, on occasion, declined to bid on projects due to the conflict of interest issues.

**Changes in accounting for equity-related compensation affects the way we use stock-based compensation to attract and retain employees**

On October 3, 2005, we adopted Statement of Financial Account Standards (SFAS) No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R), which requires the measurement and recognition of compensation expense for all stock-based compensation based on estimated fair values. As a result, our operating results for the fiscal 2006 contain, and our operating results for future periods will contain, a charge for stock-based compensation related to employee stock options, restricted stock and our Employee Stock Purchase Plan. The application of SFAS 123R requires the use of an option-pricing model to determine the fair value of share-based payment awards. This determination of fair value is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, our expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors. Option-pricing models were developed for use in estimating the value of traded options that have no vesting or hedging restrictions and are fully transferable. Because our employee stock options have certain characteristics that are significantly different from traded options, and because changes in the subjective assumptions can materially affect the estimated value, in management's opinion the existing valuation models may not provide an accurate measure of the fair value of our employee stock options. As a result of the adoption of SFAS 123R, our earnings for fiscal 2006 were lower than they would have been if we were not required to adopt SFAS 123R. The adoption of SFAS 123R had a pre-tax amount of \$4.8 million impact on our results of operations in fiscal 2006.

**Compliance with changing regulation of corporate governance and public disclosure will result in additional expenses**

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, new SEC regulations, and the NASDAQ Stock Market LLC rules, are creating additional disclosure and other compliance requirements for us. We are committed to maintaining high standards of corporate governance and public disclosure. As a result, we intend to invest appropriate resources to comply with evolving standards, and this investment may result in increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities.

**Force majeure events, including natural disasters and terrorists' actions could negatively impact the economies in which we operate or disrupt our operations, which may affect our financial condition, results of operations or cash flows**

Force majeure events, including natural disasters, such as Hurricane Katrina that affected the Gulf Coast in August 2005, and terrorist attacks, such as those that occurred in New York and Washington

D.C. on September 11, 2001, could negatively impact the economies in which we operate by causing the closure of offices, interrupting active client projects and forcing the relocation of employees. Further, despite our implementation of network security measures, our servers are vulnerable to computer viruses, break-ins and similar disruptions from unauthorized tampering with our computer systems. We typically remain obligated to perform our services after a terrorist action or natural disaster unless the contract contains a force majeure clause that relieves us of our contractual obligations in such an extraordinary event. If we are not able to react quickly to force majeure, our operations may be affected significantly, which would have a negative impact on our financial condition, results of operations or cash flows.

**Item 1B. Unresolved Staff Comments**

None.

**Item 2. Properties**

Our corporate headquarters is located in Pasadena, California. This facility contains approximately 68,000 square feet of office space. In addition, we lease office space in approximately 240 locations in the United States. In total, our facilities contain approximately 2.2 million square feet of office space and are subject to leases that expire beyond fiscal year 2006. We also rent additional office space on a month-to-month basis.

We believe that our existing facilities are adequate to meet current requirements and that suitable additional or substitute space will be available as needed to accommodate any expansion of operations and for additional offices.

For additional information concerning our obligations under leases, see Note 11, Leases, included under the heading Notes to Consolidated Financial Statements in our 2006 Annual Report to Stockholders, which is incorporated by reference.

**Item 3. Legal Proceedings**

We are subject to certain claims and lawsuits typically filed against the engineering, consulting and construction profession, alleging primarily professional errors or omissions. We carry professional liability insurance, subject to certain deductibles and policy limits, against such claims. However, in some actions, parties are seeking damages that exceed our insurance coverage or for which we are not insured. Management is of the opinion that the resolution of these claims will not have a material adverse effect on our financial position, results of operations or cash flows.

We continue to be involved in the contract dispute with Horsehead Industries, Inc., doing business as Zinc Corporation of America (ZCA). In April 2002, a Washington County Court in Bartlesville, Oklahoma dismissed with prejudice our counter-claims relating to receivables due from ZCA and other costs. In December 2002, the Court rendered a judgment for \$4.1 million and unquantified legal fees against us in this dispute. In February 2004, the Court quantified the previous award and ordered us to pay approximately \$2.6 million in ZCA's attorneys' and consultants' fees and expenses, together with post-judgment interest.

We posted bonds and filed appeals with respect to the earlier judgments. On December 27, 2004, the Court of Civil Appeals of the State of Oklahoma rendered a decision relating to certain aspects of our appeals. In its decision, the Court vacated the \$4.1 million verdict against us. In addition, the Court upheld the dismissal of our counter-claims. On January 18, 2005, both we and ZCA filed petitions for rehearing with the Oklahoma Court of Civil Appeals. On May 24, 2006, the Court of Appeals denied ZCA's petition outright and granted our petition in part. The decision effectively limited ZCA's damages to \$150,000 and gave us the right to contest this amount at a retrial. On June 9, 2006, the Court of Appeals vacated the award to ZCA of its attorneys' and consultants' fees and expenses and remanded this matter to the trial.



court. On June 13, 2006, both we and ZCA filed petitions for Writ of Certiorari with the Oklahoma Supreme Court. On October 23, 2006, the Oklahoma Supreme Court denied both such petitions.

As of October 1, 2006, we maintained \$4.1 million in accrued liabilities relating to the original judgment, and a \$2.6 million accrual for ZCA's attorneys' and consultants' fees and expenses. As a result of the Oklahoma Supreme Court decision in October 2006 and further guidance from our legal counsel, we will reverse \$4.0 million of the accrued liabilities relating to the original judgment in the first quarter of fiscal 2007. Upon further definitive legal developments, the remaining accruals relating to this matter will be adjusted accordingly.

On November 21, 2006, a stockholder filed a putative shareholder derivative complaint in the United States District Court, Central District of California, against certain current and former members of our Board of Directors and certain current and former executive officers, alleging proxy fraud, breach of fiduciary duty, abuse of control, constructive fraud, corporate waste, unjust enrichment and gross mismanagement in connection with the grant of certain stock options to our executive officers. We were also named as a nominal defendant in the action. The complaint seeks damages on our behalf in an unspecified amount, disgorgement of the options which are the subject of the action, any proceeds from the exercise of those options or from any subsequent sale of the underlying stock and equitable relief. The allegations of the complaint appear to relate to options transactions that we disclosed in our Form 10-Q for the third quarter of fiscal 2006. As reported in that Form 10-Q, we recorded additional pre-tax non-cash stock-based compensation charges totaling \$2.3 million relating to continuing operations, and \$0.9 million relating to discontinued operations, net of tax of \$1.3 million (\$0.9 million relating to continuing operations and \$0.4 million relating to discontinued operations) in our consolidated financial statements for the three and nine month periods ended July 2, 2006 as a result of misdated option grants. We are reviewing the complaint in light of our previous investigation and adjustments concerning this matter and will respond appropriately.

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

None.

30

---

## **PART II**

### **Item 5. Market for Registrant's Common Equity and Related Stockholder Matters**

The information required by this Item is incorporated by reference to the information appearing under the heading "Securities Information" in our 2006 Annual Report to Stockholders.

### **Item 6. Selected Financial Data**

The information required by this Item is incorporated by reference to the information appearing under the heading "Selected Consolidated Financial Data" in our 2006 Annual Report to Stockholders.

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

The information required by this Item is incorporated by reference to the information appearing under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our 2006 Annual Report to Stockholders.

### **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

The information required by this Item is incorporated by reference to the information appearing under the heading "Financial Market Risks" in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of our 2006 Annual Report to Stockholders.

### **Item 8. Financial Statements and Supplementary Data**

The information required by this Item is incorporated by reference to the information appearing under the headings "Report of Independent Registered Public Accounting Firm," "Consolidated Balance Sheets," "Consolidated Statements of Operations," "Consolidated Statements of Stockholders' Equity," "Consolidated Statements of Cash Flows," and "Notes to Consolidated Financial Statements" in our 2006 Annual Report to Stockholders.

### **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

### **Item 9A. Controls and Procedures**

#### **Evaluation of disclosure controls and procedures and changes in internal control over financial reporting**

As of October 1, 2006, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures. Based on our management's evaluation (with the participation of our principal executive officer and principal financial officer), our principal executive officer and principal financial officer have concluded that, as of the end of the period covered by this Report, our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act), were effective.

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

The information required by this item is included in our 2006 Annual Report to Stockholders, which is incorporated by reference.

### **Item 9B. Other Information**

None.

### **PART III**

#### **Item 10. Directors and Executive Officers of the Registrant**

The information required by this item relating to our directors and nominees, and compliance with Section 16(a) of the Exchange Act is included under the captions "Proposal No. 1 Election of Directors" and "Ownership of Securities Section 16(a) Beneficial Ownership Reporting Compliance" in our Proxy Statement related to the 2007 Annual Meeting of Stockholders and is incorporated by reference.

The information required by this item relating to our executive officers is included under the caption "Executive Compensation and Related Information Information Concerning Executive Officers" in our Proxy Statement related to the 2007 Annual Meeting of Stockholders and is incorporated by reference.

We have adopted a code of ethics that applies to our principal executive officer and all members of our finance department, including our principal financial officer and principal accounting officer. This code of ethics, entitled "Finance Code of Professional Conduct," is posted on our website. The Internet address for our website is [www.tetratech.com](http://www.tetratech.com), and the code of ethics may be found through a link to the Investors section of our website.

We intend to satisfy the disclosure requirement under Item 5.05 of Form 8-K for any amendment to, or waiver from, a provision of this code of ethics by posting any such information on our website, at the address and location specified above.

#### **Item 11. Executive Compensation**

The information required by this item is included under the captions "Proposal No. 1 Election of Directors Director Compensation" and "Executive Compensation and Related Information" in our Proxy Statement related to the 2007 Annual Meeting of Stockholders and is incorporated by reference.

#### **Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information required by this item relating to security ownership of certain beneficial owners and management, and securities authorized for issuance under equity compensation plans, is included under the caption "Ownership of Securities" in our Proxy Statement related to the 2007 Annual Meeting of Stockholders and is incorporated by reference.

#### **Item 13. Certain Relationships and Related Transactions**

The information required by this item is included under the caption "Executive Compensation and Related Information" in our Proxy Statement related to the 2007 Annual Meeting of Stockholders and is incorporated by reference.

#### **Item 14. Principal Accountant Fees and Services**

The information required by this item is included under the captions "Proposal No. 3 Ratification of Independent Registered Public Accounting Firm" and "Policy on Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of Independent Registered Public Accounting Firm" in our Proxy Statement related to the 2007 Annual Meeting of Stockholders and is incorporated by reference.

**PART IV**

**Item 15.** Exhibits and Financial Statement Schedules

- (a.) 1. **Financial Statements**  
The Index to Financial Statements and Financial Statement Schedule on page 34 is incorporated by reference as the list of financial statements required as part of this Report.
- 2. **Financial Statement Schedule**  
The Index to Financial Statements and Financial Statement Schedule on page 34 is incorporated by reference as the list of financial statement schedules required as part of this Report.
- 3. **Exhibits**  
The exhibit list in the Index to Exhibits on pages 38-40 is incorporated by reference as the list of exhibits required as part of this Report.

**INDEX TO FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULE**

**Item 15(a)**

	<b>Page Number in Form 10-K</b>	<b>Heading in 2006 Annual Report to Stockholders</b>
Management's Report on Internal Control Over Financial Reporting	*	Management's Report on Internal Control Over Financial Reporting
Report of Independent Registered Public Accounting Firm	*	Report of Independent Registered Public Accounting Firms
Consolidated Balance Sheets at October 1, 2006 and October 2, 2005	*	Consolidated Balance Sheets
Consolidated Statements of Operations for each of the three years in the period ended October 1, 2006	*	Consolidated Statements of Operations
Consolidated Statements of Stockholders Equity for each of the three years in the period ended October 1, 2006	*	Consolidated Statements of Stockholders' Equity
Consolidated Statements of Cash Flows for each of the three years in the period ended October 1, 2006	*	Consolidated Statements of Cash Flows
Notes to Consolidated Financial Statements	*	Notes to Consolidated Financial Statements
<u>Report of Independent Registered Public Accounting Firm on Financial Statement Schedule</u>	35	
<u>Schedule II Valuation and Qualifying Accounts and Reserves</u>	36	

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON FINANCIAL STATEMENT SCHEDULE**

To the Stockholders of Tetra Tech, Inc.:

Our audits of the consolidated financial statements, of management's assessment of the effectiveness of internal control over financial reporting and of the effectiveness of internal control over financial reporting referred to in our report dated December 27, 2006 appearing in the 2006 Annual Report to Stockholders of Tetra Tech, Inc. (which report, consolidated financial statements and assessment are incorporated by reference in this Annual Report on Form 10-K) also included an audit of the financial statement schedule listed in Item 15(a)(2) of this Form 10-K. In our opinion, this financial statement schedule presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

/s/ PRICEWATERHOUSECOOPERS LLP

Los Angeles, California

December 27, 2006

**TETRA TECH, INC.**  
**SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS AND RESERVES**

**For the Fiscal Years Ended**  
**October 3, 2004, October 2, 2005 and October 1, 2006**  
**(in thousands)**

	<b>Balance at Beginning of Period</b>	<b>Additions through Acquisitions</b>	<b>Charges to Costs and Earnings</b>	<b>Deductions, Net of Recoveries</b>	<b>Balance at End of Period</b>
<b>Fiscal year ended October 3, 2004:</b>					
Allowance for uncollectible accounts receivable	\$ 12,650	\$ 1,105	\$ 9,153	\$ (1,344 )	\$ 21,564
<b>Fiscal year ended October 2, 2005:</b>					
Allowance for uncollectible accounts receivable(1)	\$ 21,564	\$	\$ 30,061	\$ (9,740 )	\$ 41,885
<b>Fiscal year ended October 1, 2006:</b>					
Allowance for uncollectible accounts receivable	\$ 41,885	\$	\$ 2,682	\$ (15,460 )	\$ 29,107

(1) The charges to costs and earnings increased \$20.9 million in fiscal 2005, compared to fiscal 2004. The increase was primarily related to an operating unit in our resource management segment that incurred contract losses.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: December 28, 2006

TETRA TECH, INC.  
By: /s/ DAN L. BATRACK  
Dan L. Batrack,  
Chief Executive Officer

**POWER OF ATTORNEY**

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Dan L. Batrack and David W. King, jointly and severally, his attorney-in-fact, each with the full power of substitution, for such person, in any and all capacities, to sign any and all amendments to this Annual Report on Form 10-K, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as he might do or could do in person, hereby ratifying and confirming all that each of said attorneys-in-fact and agents, or his substitute, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report on Form 10-K has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ DAN L. BATRACK Dan L. Batrack	Chief Executive Officer and Director (Principal Executive Officer)	December 28, 2006
/s/ DAVID W. KING David W. King	Executive Vice President, Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer)	December 28, 2006
/s/ ALBERT E. SMITH Albert E. Smith	Chairman of the Board	December 28, 2006
/s/ J. CHRISTOPHER LEWIS J. Christopher Lewis	Director	December 28, 2006
/s/ PATRICK C. HADEN Patrick C. Haden	Director	December 28, 2006
/s/ HUGH M. GRANT Hugh M. Grant	Director	December 28, 2006
/s/ RICHARD H. TRULY Richard H. Truly	Director	December 28, 2006



**INDEX TO EXHIBITS**

- 3.1 Restated Certificate of Incorporation of the Company (incorporated by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K for the fiscal year ended October 1, 1995).
- 3.2 Certificate of Amendment of Certificate of Incorporation of the Company (incorporated by reference to Exhibit 3.4 to the Company's Quarterly Report on Form 10-Q as amended for the fiscal quarter ended April 1, 2001).
- 3.3 Amended and Restated Bylaws of the Company (as of November 17, 2003) (incorporated by reference to Exhibit 3.4 to the Company's Annual Report on Form 10-K for the fiscal year ended September 28, 2003).
- 10.1 Amended and Restated Credit Agreement dated as of July 21, 2004 among the Company and the financial institutions named therein (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended June 27, 2004).
- 10.2 First Amendment as of December 14, 2004 to the Amended and Restated Credit Agreement dated as of July 21, 2004 among the Company and the financial institutions named therein (incorporated by reference to Exhibit 10.2 to the Company's Annual Report on Form 10-K for the fiscal year ended October 3, 2004).
- 10.3 Second Amendment dated as of May 12, 2005 to the Amended and Restated Credit Agreement dated as of July 21, 2004 among the Company and the financial institutions named therein (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended April 3, 2005).
- 10.4 Third Amendment dated as of March 24, 2006 to the Amended and Restated Credit Agreement dated as of July 21, 2004 among the Company and the financial institutions named therein (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended April 2, 2006).
- 10.5 Note Purchase Agreement dated as of May 15, 2001 among the Company and the purchasers named therein (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended July 1, 2001).
- 10.6 First Amendment dated as of September 30, 2001 to the Note Purchase Agreement dated as of May 15, 2001 among the Company and the purchasers named therein (incorporated by reference to Exhibit 10.5 to the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2001).
- 10.7 Second Amendment dated as of April 22, 2003 to the Note Purchase Agreement dated as of May 15, 2001 among the Company and the purchasers named therein (incorporated by reference to Exhibit 10.9 to the Company's Annual Report on Form 10-K for the fiscal year ended September 28, 2003).
- 10.8 Third Amendment dated as of December 14, 2004 to the Note Purchase Agreement dated as of May 15, 2001 among the Company and the purchasers named therein (incorporated by reference to Exhibit 10.6 to the Company's Annual Report on Form 10-K for the fiscal year ended October 3, 2004).
- 10.9 Fourth Amendment dated as of May 12, 2005 to the Note Purchase Agreement dated as of May 15, 2001 among the Company and the purchasers named therein (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended April 3, 2005).

38

---

## Edgar Filing: TETRA TECH INC - Form 10-K

- 10.10 Fifth Amendment dated as of March 24, 2006 to the Note Purchase Agreement dated as of May 15, 2001 among the Company and the purchasers named therein (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended April 2, 2006).
- 10.11 1989 Stock Option Plan dated as of February 1, 1989 (incorporated by reference to Exhibit 10.13 to the Company's Registration Statement on Form S-1, No. 33-43723).\*
- 10.12 Form of Incentive Stock Option Agreement executed by the Company and certain individuals in connection with the Company's 1989 Stock Option Plan (incorporated by reference to Exhibit 10.14 to the Company's Registration Statement on Form S-1, No. 33-43723).\*
- 10.13 1992 Incentive Stock Plan (incorporated by reference to Exhibit 10.18 to the Company's Annual Report on Form 10-K for the fiscal year ended October 3, 1993).\*
- 10.14 Form of Incentive Stock Option Agreement used by the Company in connection with the Company's 1992 Incentive Stock Plan (incorporated by reference to Exhibit 10.19 to the Company's Annual Report on Form 10-K for the fiscal year ended October 3, 1993).\*
- 10.15 1992 Stock Option Plan for Nonemployee Directors (incorporated by reference to Exhibit 10.20 to the Company's Annual Report on Form 10-K for the fiscal year ended October 3, 1993).\*
- 10.16 Form of Nonqualified Stock Option Agreement used by the Company in connection with the Company's 1992 Stock Option Plan for Nonemployee Directors (incorporated by reference to Exhibit 10.21 to the Company's Annual Report on Form 10-K for the fiscal year ended October 3, 1993).\*
- 10.17 Employee Stock Purchase Plan (as amended through November 17, 2003) (incorporated by reference to Exhibit 10.17 to the Company's Annual Report on Form 10-K for the fiscal year ended September 28, 2003).
- 10.18 Form of Stock Purchase Agreement used by the Company in connection with the Company's Employee Stock Purchase Plan (incorporated by reference to Exhibit 10.23 to the Company's Annual Report on Form 10-K for the fiscal year ended October 2, 1994).
- 10.19 2005 Equity Incentive Plan (incorporated by reference to Exhibit 10.18 to the Company's Annual Report on Form 10-K for the fiscal year ended October 2, 2005).\*
- 10.20 Form of Stock Option Agreement to be used by the Company in connection with the 2005 Equity Incentive Plan (incorporated by reference to Exhibit 10.19 to the Company's Annual Report on Form 10-K for the fiscal year ended October 2, 2005).\*
- 10.21 Form of Restricted Stock Agreement to be used by the Company in connection with the 2005 Equity Incentive Plan (incorporated by reference to Exhibit 10.20 to the Company's Annual Report on Form 10-K for the fiscal year ended October 2, 2005).\*
- 10.22 Form of Stock Appreciation Rights Agreement to be used by the Company in connection with the 2005 Equity Incentive Plan (incorporated by reference to Exhibit 10.21 to the Company's Annual Report on Form 10-K for the fiscal year ended October 2, 2005).\*
- 10.23 Form of Restricted Stock Unit Agreement to be used by the Company in connection with the 2005 Equity Incentive Plan (incorporated by reference to Exhibit 10.22 to the Company's Annual Report on Form 10-K for the fiscal year ended October 2, 2005).
- 10.24 2003 Outside Director Stock Option Plan (incorporated by reference to Exhibit 10.20 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended March 30, 2003).\*
- 10.25 Form of Option Agreement used by the Company in connection with the 2003 Outside Director Stock Option Plan (incorporated by reference to Exhibit 10.21 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended March 30, 2003).\*

Edgar Filing: TETRA TECH INC - Form 10-K

- 10.26 Form of Indemnity Agreement entered into between the Company and each of its directors and executive officers. (incorporated by reference to Exhibit 10.20 to the Company's Annual Report on Form 10-K for the fiscal year ended October 3, 2004).\*
- 10.27 Executive Compensation Policy (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated November 16, 2006).\*
- 10.28 Separation Agreement and Release between the Company and James M. Jaska dated October 7, 2004 (incorporated by reference to Exhibit 10.1 to the Company's Current Report on 8-K dated October 6, 2004).\*
- 10.29 Letter agreement dated August 5, 2005 between the Company and Albert E. Smith (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated August 5, 2005).\*
- 10.30 Letter agreement dated November 14, 2005 between the Company and Li-San Hwang (incorporated by reference to Exhibit 10.29 to the Company's Annual Report on Form 10-K for the fiscal year ended October 2, 2005).\*
- 10.31 Letter agreement dated November 14, 2005 between the Company and Sam W. Box (incorporated by reference to Exhibit 10.30 to the Company's Annual Report on Form 10-K for the fiscal year ended October 2, 2005).\*
- 13 Annual Report to Stockholders for the fiscal year ended October 1, 2006, portions of which are incorporated by reference in this report as set forth in Part I and Part II hereof. With the exception of these portions, such Annual Report is not deemed filed as part of this report.+
- 21 Subsidiaries of the Company.+
- 23 Consent of Independent Registered Public Accounting Firm (PricewaterhouseCoopers LLP).+
- 24 Power of Attorney (included on page 37 of this Annual Report on Form 10-K).
- 31.1 Chief Executive Officer Certification pursuant to Rule 13a-14(a)/15d-14(a).+
- 31.2 Chief Financial Officer Certification pursuant to Rule 13a-14(a)/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.+

---

\* Indicates a management contract or compensatory arrangement.

+ Filed herewith.

40

---