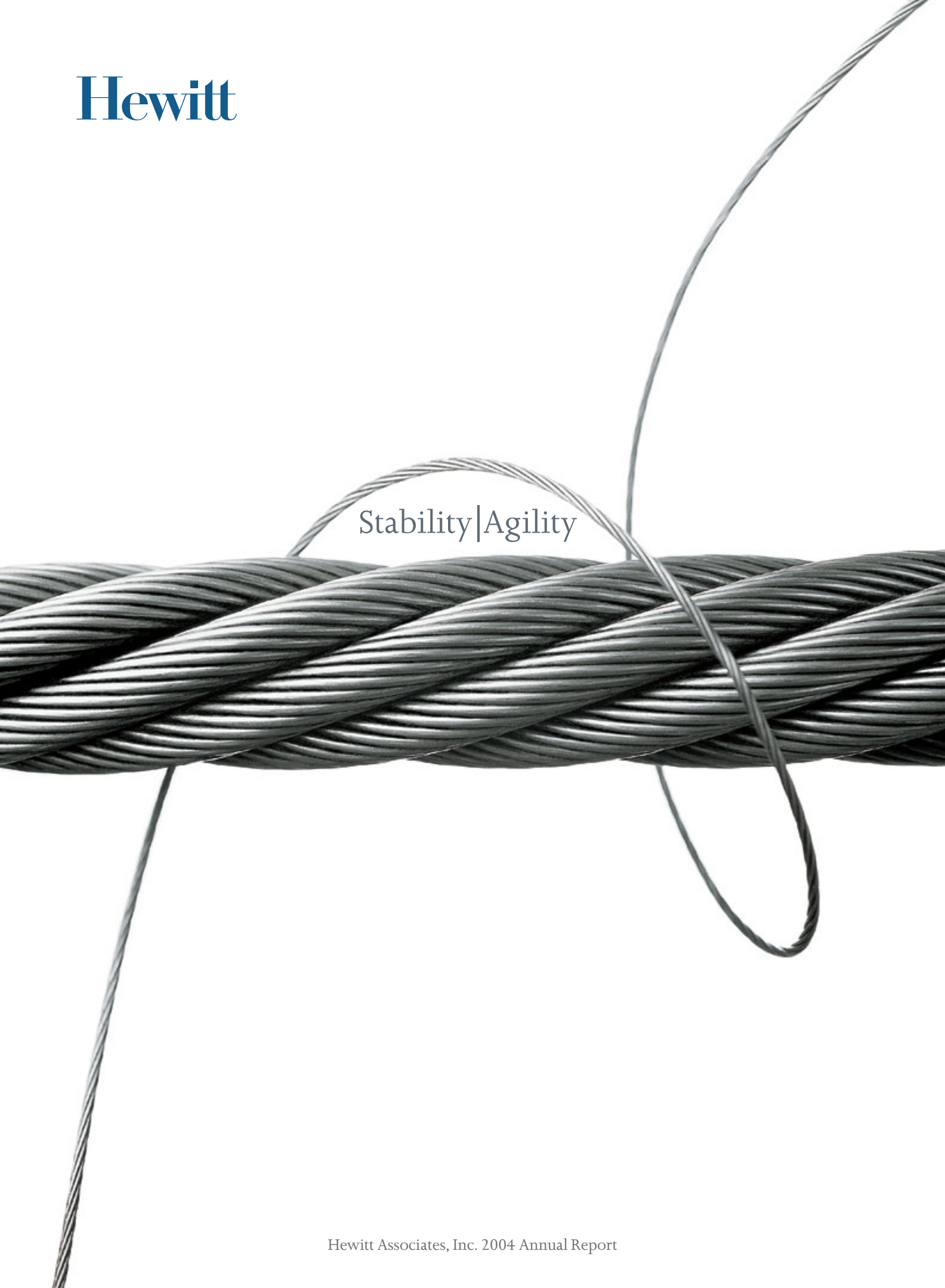


Hewitt



Stability|Agility

stability n:
firmness in position; permanence; constancy,
as of character or purpose; steadiness
syn: soundness, vitality, solidity, strength

agility n:
the state or quality of being agile; quick,
well-coordinated movement; the ability to
think quickly
syn: nimbleness, quickness, adaptability

Hewitt is a world leader in human capital management. We help companies and the people who work for them succeed—together—and by doing so, we help make the world a better place to work.

Much has changed. Much hasn't.

page 2 Stable strategies. Agile responses.
page 14 Letter to Shareholders
page 16 Hewitt at a Glance
page 17 Financial Results

Our longstanding leadership is based on well-established strengths. We provide clients with the greatest depth, breadth, and experience of any human resources organization. We are the first—and only—firm that has integrated human resources outsourcing with human resources consulting, to deliver comprehensive, single-source solutions to large employers.

We're adding to our lead.

People go farther when they all pull together. Hewitt applies that simple truth to the business of people.

Our human resources outsourcing and consulting services help companies manage some of the most important issues they face today—issues that affect their performance and the lives of their employees. We design and deliver health plans that protect both a company's bottom line and its employees. We create and manage retirement programs that extract more value from our clients' benefit investments.

We help companies attract, engage, and reward talent. We enable companies to reduce costs, focus on their core activities, and gain better information. We change the way businesses manage people, and we make those changes work.

We're not resting on our oars. We have added new products, like payroll services. And in 2004, we announced our merger with Exult, a pioneer and leader in full service human resources outsourcing. Now, Hewitt is the only company to integrate the full range of benefits, payroll, human resources information, recruiting, learning, and other services with in-depth human resources consulting expertise. So businesses can find the best—and broadest—solutions from a single source, and keep pulling ahead.





Behind all of our services are processes and technology exclusively dedicated to managing human resources. Our processes have been tested—and proven—in thousands of engagements. Our proprietary technology provides reliable service to more than 18 million employees and retirees, and their families.

We're adding to our strengths.

Our processes reflect all that we have learned over the past 64 years about helping companies work more effectively, achieve their objectives, and grow. We know what works—and what doesn't—and the shortest distance between our clients' needs and their goals.

Our technology includes the world's first integrated database for human resources management. Internet-based delivery systems allow individuals to gain access to information about everything from their health and welfare benefits to training opportunities—and complete regular transactions—at a single site. New capabilities include consumer-based health and retirement programs and health care account administration. Applying predictive analytics to outsourcing and consulting data, new Human Capital Foresight™ services enable businesses to quantify the economic value of human capital.

There's more. Our merger with Exult combines two leaders in human resources business process outsourcing (HR BPO), giving clients the most comprehensive and flexible approach to outsourcing all of their human resource functions. We have gained additional processing capabilities in such areas as staffing, relocation, time and attendance, and learning and development services. New Six Sigma expertise applies a formal, disciplined approach to improving service quality.

Today, our solutions are more flexible than ever. We can make use of all or part of the client's existing information systems to reduce upfront costs, or apply our own technology, right from the start. So each client can gain a solution tailored to its unique—and evolving—requirements.

Hewitt's only business is people. So we give it our undivided attention. We're committed to helping our clients reach their business objectives. Our associates think beyond the conventional answers, to deliver measurable results.

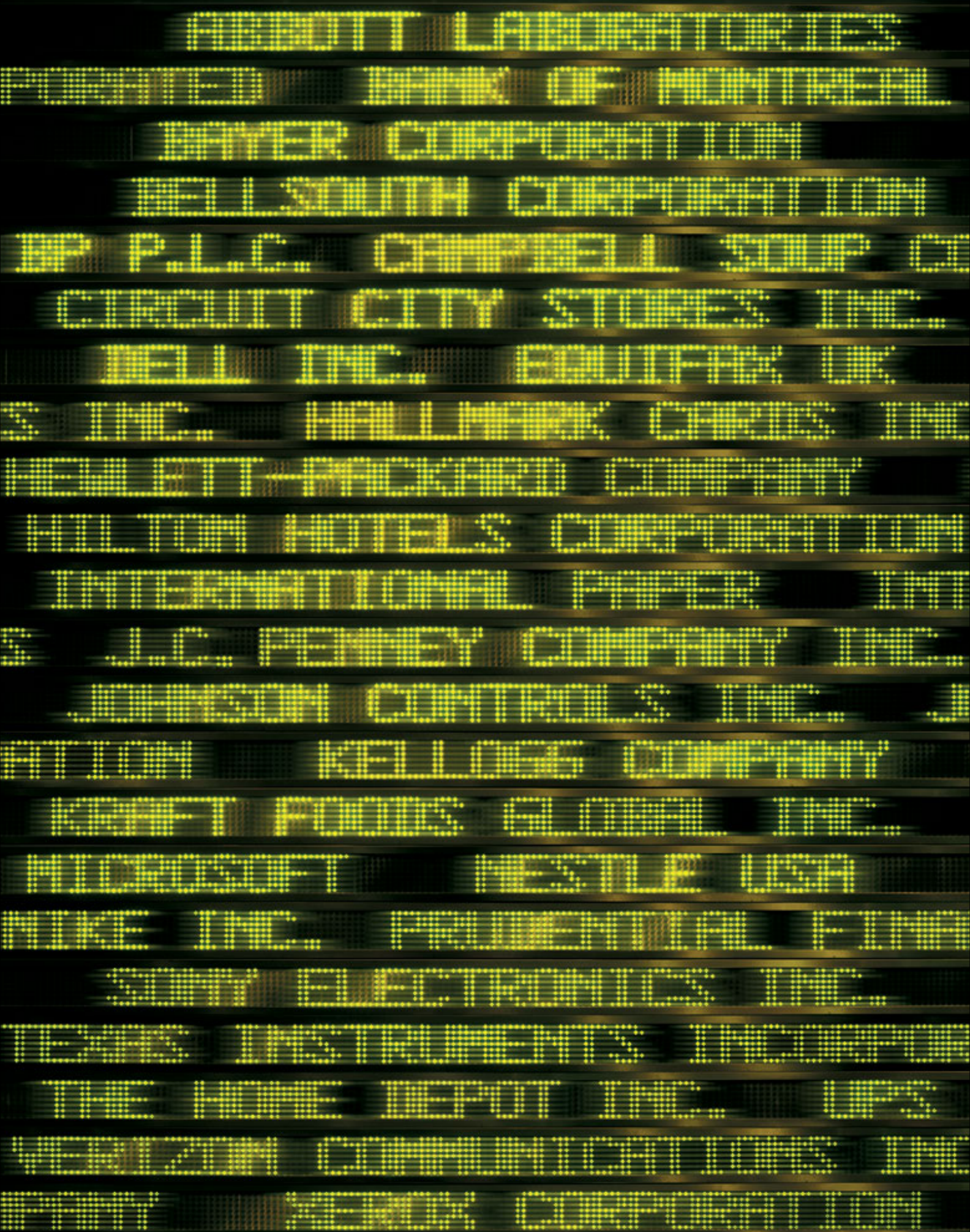
Hewitt people stand out, now more than ever.

Hewitt is one of the world's largest organizations exclusively devoted to human capital management. With nearly 20,000 employees, including Exult, in 35 countries, we have more people, with more experience, and more creative solutions.

Our organization works—because we work together. Our operations are integrated. Consultants apply the vast amounts of data we gain through our outsourcing services to develop solutions that are based on facts, not hunches. Our experience in consulting assures that outsourcing services can be implemented smoothly in the real world. Our “one-firm firm” approach helps us put all of our skills to work, for all of our clients, and creates real teamwork.

Together, we have what it takes to take on complex tasks and deliver results. We have helped companies with hundreds of thousands of employees through mergers and other major changes. We provide a growing number of organizations and their employees with comprehensive HR BPO services that relieve managers of the day-to-day responsibility of administering human resource programs. We administer benefits for organizations with as many as half a million current and former employees. We do the HR work so our clients can concentrate on their core activities and benefit from the outstanding support provided by our human resource professionals.





We've built successful long-term relationships with leaders in virtually every industry. We work with more than 2,600 clients, including more than half of the *Fortune* 500. And nearly 90% of our 100 largest clients have worked with us for five years or more.

Now there's more reason to stay with Hewitt.

When our clients succeed, we do, so we're obsessed with their success. That's one reason why our clients turn to us for critical tasks. We reengineer our clients' human resources activities to transform their effectiveness, reduce costs, and automate processes and transactions. We provide the tools and information that HR managers need to ensure the effectiveness and compliance of their HR programs. Our actuarial valuations of pension plans are part of annual reviews mandated by corporate boards and regulators. We assist clients with the complex human resource issues arising from mergers, acquisitions, divestitures, and other major changes.

Delivering such strategically important services begins with a unique approach to client development. A dedicated group of account professionals, including a team devoted exclusively to business process outsourcing, learns each client's concerns and earns each client's confidence. Outstanding service forges long-term relationships, and new services and capabilities help to expand them. We change along with our clients, so they have no reason to change to anyone else.

At Hewitt, business as usual means innovation. We've been pioneering new human resource ideas, services, and products for more than 64 years.

There's a world of opportunity ahead.

Our innovations include the first personalized benefit and compensation statements and the first communications practice dedicated to educating employees about their benefits. We created the first and most widely used tools for measuring and comparing benefits and total rewards. We wrote the book on flexible compensation and created the first Web-based benefits management tool. We helped companies develop and apply the technology needed to implement managed care plans.

That's only the beginning. We now offer comprehensive and flexible outsourcing services, adapted to each client's specific requirements. We are applying the vast amount of data in our care to deliver more effective information tools and services that help employers and their employees make better decisions. We continue to pioneer new solutions, including payroll, health care account administration, and consumer-based, self-directed health and retirement programs. The first choice is Hewitt.





The world is changing. Our strategies haven't.
They're taking us where we want to go.

Forward.

We've followed the same strategic path for decades. It leads to profitable growth.

We're working hard to *expand relationships* with our current clients. As more clients recognize the value of working exclusively with Hewitt—greater value, lower costs, greater efficiencies, a single Web site, and more—there's plenty of room for additional growth. The addition of Exult enables us to offer uniquely comprehensive solutions to our clients.

More than 18 million employees and retirees, and millions more of their family members, rely on our outsourcing services, but we have only begun to *develop a large, untapped market*. We expect the number of people we serve to grow dramatically, as companies move to concentrate on their core activities and as the technological and regulatory issues associated with managing human resource processes become more challenging.

We have the ability to *broaden our target market*—all over the world. We are well-positioned to meet the growing demand for our services outside of the United States. We will explore alliances that could provide us with expansion opportunities in and beyond our historical target markets. And while our outsourcing business typically serves companies with more than 10,000 employees, many of our services can be adapted for use by companies with a few thousand employees.

We continue to *evolve our service offerings* which supports all of our growth strategies. Our combination with Exult provides additional capacity and capability for delivering outsourcing services.

As expected, investments in new services and the integration of our acquisitions will have a dilutive impact on our short-term results. But over the long term we expect to *improve our margins*. We will leverage our investments in processes, operations, and technology, as well as our infrastructure and people. Combining offices and resources with Exult will bring additional economies and efficiencies of scale.

Much will change.
Much won't.



Hewitt Associates has changed in the past three years. We have become a publicly traded corporation. We have added or developed a number of new services. Acquisitions have increased our presence in major global markets, added to our capabilities, and expanded our client base.

The changes continued in 2004, with the announcement of our merger with Exult—the largest in our history. We are now the leading provider of comprehensive human resources outsourcing services. We are the only organization capable of offering one-stop shopping for virtually all human resource requirements. We have the broadest range of services and the deepest expertise, and we serve more large companies than anyone in our industry.

We are changing for the better. We've gained the resources—and the agility—to meet the changing needs of our clients and their employees and the demands of our marketplace. But we haven't changed our basic beliefs, or the three long-term goals that have always been central to our thinking. We remain focused on serving clients exceptionally well; having engaged and focused associates; and creating a strong and growing business.

Serving clients exceptionally well

Our clients' needs are growing more complex by the day. They don't only want to manage costs, improve the value of their human resources activities, or concentrate on their core businesses—they want to do all three. We are responding by providing more comprehensive, well-integrated, and flexible solutions.

One example is our new relationship with TXU, a Dallas-based energy company. Working under a 10-year agreement, we are providing human resources operations, strategy, design, and administration services to all of TXU's U.S. employees. It is one of our broadest client relationships ever. What's more, we have assumed responsibility for a number of TXU's human resources employees and are leveraging the company's own human resources information systems—the first time that we have adopted such an approach. By selectively utilizing our clients' assets we gain unmatched flexibility in crafting custom-tailored solutions, which enable clients to reduce initial costs and begin outsourcing their processes more quickly.

We're doing more for clients in other ways as well. We're helping them deal with a number of challenges, including health care, retirement, executive compensation, corporate restructuring, and talent management, that are, quite literally, vital to their long-term success. Combining our experience in helping hundreds of companies tackle their health care issues with the data we have collected on millions of people, we are offering cost-effective consumer-driven health care programs that provide the tools that

clients—and their employees—need to make well-informed decisions. The analytical tools now in development, like our Human Capital Foresight analyses, offer companies new ways to measure and manage the overall performance and economic value of their human resource programs and their human capital.

Having engaged and focused associates

Change brings challenges, for everyone. Hewitt and its associates are not immune to the same issues our clients face, but we are demonstrating that we know how to meet them. We work hard to keep people informed and to develop shared goals and expectations. Regular—and frequent—associate engagement surveys identify areas that need improvement. While we can—and will—always do more, our associates remain engaged and focused on delivering the highest quality service to our clients.

And we've just added to the best team in the business. Applying what we have learned in working for our clients and in our previous acquisitions, we are swiftly integrating Exult into our operations. I would like to welcome Exult's 2,700 employee-shareholders, including its senior management team. As we say inside our organization, we will now be "Winning as One."

Creating a strong and growing business

We also have made good progress toward our third core strategic objective. First, we have grown the business by expanding our capabilities and providing more integrated, holistic solutions, which differentiate Hewitt from its competitors. At the same time, however, over the past couple of years we have experienced challenging conditions in our markets. Corporate spending constraints, reduced merger and acquisition activity and a slowdown in restructurings, program design changes, and other major change initiatives all have affected demand for our consulting services. But while our rate of growth has slowed, we've still continued to grow, and our balance sheet and cash flow remain strong. Net revenues for the 2004 fiscal year increased 11%, to \$2.20 billion. Excluding the effects of acquisitions and favorable foreign currency translations, revenues increased by 5%.

We'll continue to grow. After investing to build one of the largest and most resourceful organizations in our industry, we are working to continue to increase our revenues and improve our efficiency. We're systematically streamlining everything we do, so we can serve our clients more effectively.

We're tailoring our operations to the demands of the marketplace. To meet clients' needs for lower-cost service, we've moved selected work to other locations. Established in 2003, our service center in India now employs more than 1,000 associates. In addition to helping us manage costs, it enables us to provide high-quality round-the-clock service and gives us access to an enormous pool of talent.

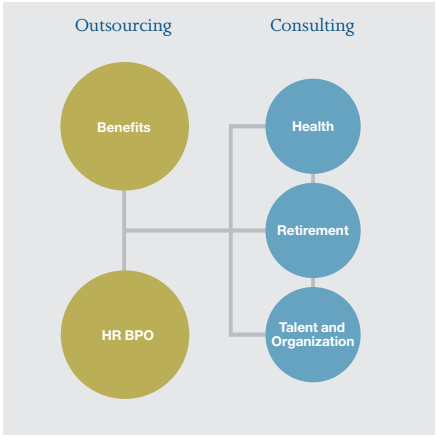
Our to-do list is ambitious. Our clients continue to face extraordinary budget constraints—and major human resource issues and challenges. We are eager to help. We will lead the market for broad-based human resources outsourcing services, today and moving forward. We will work to make our consulting services stand out in the marketplace and make sure our solutions offer real—and distinctive—benefits to clients. We will expand our relationships with existing clients, add new ones, and serve all of them in more ways than ever before. By applying our total resources, we'll ensure that the companies we work with will add to their value by working with us. It is our constant, unchanging commitment. I look forward to continuing to report on our progress.

A handwritten signature in black ink, appearing to read "Dale L. Gifford". The signature is fluid and cursive.

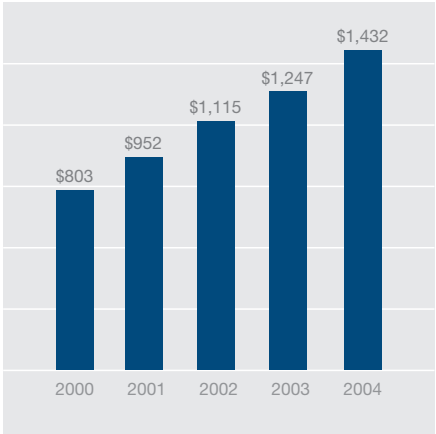
Dale L. Gifford
Chairman and Chief Executive Officer
December 1, 2004

Hewitt at a Glance

Hewitt Service Offerings

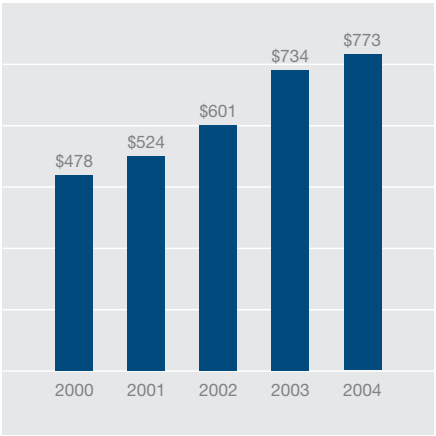


Outsourcing Segment Net Revenues
(dollars in millions)



Number of Clients: nearly 300

Consulting Segment Net Revenues
(dollars in millions)



Number of Clients: nearly 2,400

Hewitt Associates

By continuously extending and expanding our human resource services and solutions, we have achieved more than four decades of consecutive organic revenue growth. In fiscal 2004, our net revenues grew 11% to more than \$2.0 billion. Excluding the effects of acquisitions and favorable foreign currency translations, our revenues increased 5%.

Our human resources expertise is broad and deep. We offer clients a complete range of services, including human resources strategy, design, implementation, administration, communication, and employee customer service. Our success in integrating human resources outsourcing with human resources consulting differentiates us in the marketplace and enables us to find the best and most comprehensive solutions. We help companies manage complex change and the critical issues that they face today.

Outsourcing

Generating the majority of our revenues, our outsourcing business is characterized by long-term contracts, annually recurring revenues, and high client retention rates. In fiscal 2004, our outsourcing business grew 15% to \$1.4 billion. Excluding the effects of acquisitions, outsourcing revenues increased 9%.

We have unmatched scale and outstanding prospects for growth. Our recent combination with Exult has made us the leader in the rapidly growing market for human resources business process outsourcing (HR BPO). We’re now the only organization capable of offering total HR BPO services—benefits, payroll, HR information systems, recruiting, learning, and other HR services—integrated with a full suite of HR consulting services.

Consulting

In an economy increasingly based on knowledge—and service—the effective management of human capital is critical to business success. Our consulting business provides a wide array of services, encompassing the design, implementation, and operation of health and welfare, retirement, and compensation plans, as well as broader human resource programs and actuarial services. Our approaches are unique and differentiated—they are holistic solutions, combined with HR outsourcing—and are tailored to our clients’ individual needs. In 2004, our consulting net revenues increased 5% to \$773 million. Excluding the effects of acquisitions and favorable foreign currency translations, our revenues were approximately even with the prior year.

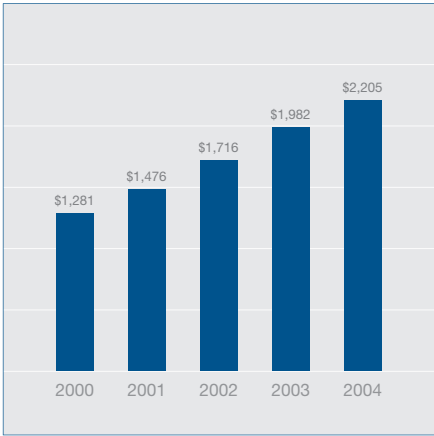
Financial Highlights

Dollars in millions	Fiscal Year Ended September 30,				% Change
	2004		2003		
Net Revenues	\$ 2,205		\$ 1,982		11%
Outsourcing Net Revenues	\$ 1,432		\$ 1,247		15%
Consulting Net Revenues	\$ 773		\$ 734		5%
Operating Income	\$ 223		\$ 178		25%
Core Operating Income*	\$ 240		\$ 217		10%
Approximate Number of Associates	17,000		15,000		13%
Market Price of Stock:†	High	Low	High	Low	
First fiscal quarter	\$ 31.00	\$ 23.50	\$ 36.36	\$ 26.30	
Second fiscal quarter	\$ 35.80	\$ 29.52	\$ 34.60	\$ 24.80	
Third fiscal quarter	\$ 32.85	\$ 27.10	\$ 29.95	\$ 20.70	
Fourth fiscal quarter	\$ 28.18	\$ 24.40	\$ 26.90	\$ 22.95	

*Core operating income and core operating margin are non-GAAP (“GAAP” as defined by accounting principles generally accepted in the United States) financial measures. The Company reported operating income of \$182 million, \$186 million, \$240 million, \$178 million, and \$223 million for fiscal 2000 through 2004, respectively, in accordance with GAAP. In assessing operating performance, the Company also reviews its results on a core basis that: 1) includes estimated owner compensation expenses in the 2000 through 2002 fiscal periods prior to becoming a corporation (approximately \$135 million and \$146 million in fiscal 2000 and fiscal 2001, respectively, and \$108 million for the first eight months of fiscal 2002—prior to incorporation); 2) excludes non-recurring expenses related to the Company’s conversion to a corporate structure (\$26 million in fiscal 2002); 3) excludes charges related to the amortization of the one-time, initial public offering-related grant of restricted stock to employees (\$28 million, \$39 million, and \$17 million in fiscal 2002, 2003, and 2004, respectively); and 4) excludes operating losses related to Sageo (\$21 million and \$73 million in fiscal 2000 and 2001, respectively). The Company believes this measure provides a better understanding of its underlying operating performance. Margin is expressed as a percentage of net revenues.

*Hewitt Associates, Inc. completed its initial public offering on June 27, 2002. The Company’s Class A common stock is listed on the New York Stock Exchange under the symbol “HEW.” As of October 31, 2004, the Company had 879 shareholders of record of its Class A common stock, 38 shareholders of record of its Class B common stock, and 51 shareholders of record of its Class C common stock. The Company has not paid cash dividends on its common stock. The Company’s board of directors reevaluates this policy periodically. Any determination to pay cash dividends will be at the discretion of the board of directors and will be dependent upon the Company’s financial condition, results of operations, capital requirements, terms of financing arrangements, and such other factors as the board of directors deems relevant.

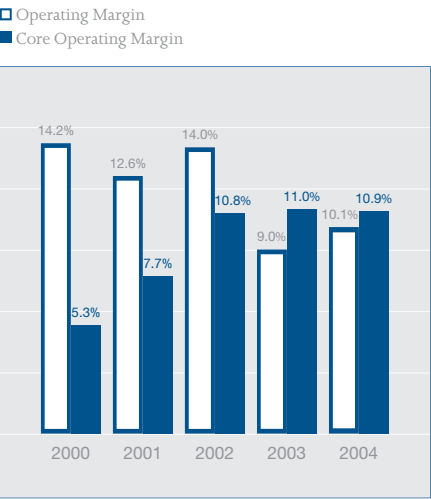
Net Revenues
(dollars in millions)



Operating Income and
Core Operating Income*
(dollars in millions)



Operating Margin and
Core Operating Margin*
(percentages)



Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following information should be read in conjunction with our consolidated and combined financial statements and related notes, included elsewhere in the Company’s Annual Report. In addition to historical information, this discussion and analysis may contain forward-looking statements that involve risks, uncertainties and assumptions, which could cause actual results to differ materially from management’s expectations. Please see additional risks and uncertainties described below and in the “Notes Regarding Forward-Looking Statements” which appears later in this section.

We use the terms “Hewitt,” “the Company,” “we,” “us,” and “our” to refer to the business of Hewitt Associates, Inc. and its subsidiaries and, with respect to the period prior to May 31, 2002, the date of our transition to a corporate structure, the businesses of Hewitt Associates LLC, its subsidiaries and its then affiliates, Hewitt Financial Services LLC and Sageo LLC (“Hewitt Associates and Affiliates”).

We use the term “owner” in this Annual Report to refer to the individuals who are members of FORE Holdings LLC, formerly known as Hewitt Holdings LLC, most of whom are our employees.

Due to integration efforts related to our acquisition of the benefits consulting business of Bacon & Woodrow, standalone results for that business subsequent to the acquisition date were not available. To quantify the effects of the Bacon & Woodrow acquisition in our discussion and analysis of results, we have added the prior-year historical results of the benefits consulting business of Bacon & Woodrow to our prior-period results for comparison with our current-year results.

All references to years, unless otherwise noted, refer to our fiscal years, which end on September 30. For example, a reference to “2004” or “fiscal 2004” means the twelve-month period that ended September 30, 2004. All references to percentages contained in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” refer to calculations based on the amounts in our consolidated and combined financial statements, included elsewhere in this Annual Report. Prior period amounts have been reclassified to conform with the current year presentation.

Overview

Hewitt Associates, Inc., a Delaware corporation, and its subsidiaries provide global human resources outsourcing and consulting services. The Company’s outsourcing business is composed of employee benefit plan, payroll and workforce management administrative services. Hewitt’s consulting business is composed of advisory services in health management, retirement and financial management, talent and organization consulting and other consulting.

In connection with our transition to a corporate structure, which was completed on May 31, 2002, Hewitt Associates, Inc. was formed as a subsidiary of Hewitt Holdings and Hewitt Holdings transferred all of its ownership interests in Hewitt Associates LLC and Affiliates to Hewitt Associates, Inc. In our limited liability company form, Hewitt Holdings’ owners were compensated through distributions of income rather than through salaries, benefits and performance-based bonuses, and we did not incur any corporate income tax. Upon our transition to a corporate structure, (i) Hewitt Holdings’ owners who worked in the business became our employees and we began to include their compensation in our compensation and related expenses, (ii) we became subject to corporate income

taxes and (iii) we began to report net income and earnings per share.

On June 5, 2002, we acquired the actuarial and benefits consulting business of Bacon & Woodrow in the United Kingdom. The purchase price totaled \$259 million and consisted of 9.4 million shares of Hewitt Associates common stock valued at \$219 million, \$39 million of assumed net liabilities and approximately \$1 million of acquisition-related costs. For additional information on the Bacon & Woodrow acquisition, we refer you to Note 6 to our consolidated and combined financial statements. The results of operations for Bacon & Woodrow are included in our historical results from the date of the acquisition, June 5, 2002.

On June 27, 2002, we sold 11,150,000 shares of Class A common stock at \$19.00 per share in our initial public offering. In July 2002, the underwriters exercised their over-allotment option to purchase an additional 1,672,500 shares of our Class A common stock at \$19.00 per share. The combined transactions generated \$219 million in net cash proceeds after offering expenses.

For a pro forma presentation of results had these events occurred at the beginning of the fiscal year 2002, we refer you to our “Pro Forma Results of Operations” which appear later in this section.

On June 5, 2003, we acquired Cyborg Worldwide, Inc., the parent of Cyborg Systems, Inc. (“Cyborg”), a global provider of human resources management software and payroll services. The results of operations for Cyborg are included in the results of the Outsourcing segment from the acquisition date (see Note 6 to the consolidated and combined financial statements).

On June 15, 2003, the Company acquired substantially all of the assets of Northern Trust Retirement Consulting, Northern Trust Corporation’s retirement consulting and administration business (“NTRC”), which provides retirement consulting and actuarial services and defined benefit, defined contribution and retiree health and welfare administration services. The results of NTRC are included in the results of the Outsourcing and Consulting segments from the acquisition date (see Note 6 to our consolidated and combined financial statements).

On July 1, 2003, Hewitt Holdings distributed the shares of Class B common stock of Hewitt Associates it held in beneficial ownership on behalf of its owners, with the exception of certain owners resident outside the United States who will continue to hold their shares through Hewitt Holdings. The distribution reduced Hewitt Holdings’ majority interest in Hewitt Associates of approximately 71% at June 30, 2003, to a minority interest of approximately 2%. The shares continue to be subject to the same restrictions with respect to transfer and book to market phase-in as they were when the shares were held by Hewitt Holdings. Also, with respect to voting, all Class B and Class C shares continue to be voted in accordance with the majority vote of those Class B and Class C stockholders participating in a preliminary vote of such holders. At September 30, 2004, the number of Class B and Class C shares outstanding totaled 66,098,976 or approximately 67% of common stock outstanding.

At the January 29, 2004 Hewitt Associates, Inc. Board Meeting, the make-up of Hewitt’s Board changed so that individuals who have an interest in Hewitt Holdings no longer had a majority position on the Board. On April 29, 2004, Hewitt Holdings formally changed its name from Hewitt Holdings LLC to FORE Holdings LLC (“FORE Holdings”).

Recent Developments

Exult Merger

Exult has been a leading provider of HR business process outsourcing. On June 15, 2004, we entered into an Agreement and Plan of Merger with Exult, Inc. and Eagle Merger Corp., a newly formed wholly owned subsidiary of Hewitt, and on October 1, 2004, after obtaining regulatory and stockholder approvals, the merger was completed. Eagle Merger Corp. was merged with and into Exult, and Exult became the surviving corporation and a wholly owned subsidiary of Hewitt. Under the Agreement, each share of Exult common stock outstanding immediately prior to the effective time of the merger was converted into 0.2 shares of Hewitt Class A common stock. As such, the Exult stockholders received 22,159,921 shares of Hewitt Class A stock in exchange for the 110,799,662 shares of outstanding Exult common stock. The purchase price is estimated to be approximately \$776 million, including assumed debt and acquisition related costs. On October 29, 2004, Exult was merged into Hewitt Associates, Inc. On October 6, 2004, the Company filed a Registration Statement on Form S-3 with the Securities and Exchange Commission to allow the holders of \$110 million of assumed 2.5% convertible senior notes, due on October 1, 2010, to resell their notes and the Hewitt Class A common stock issuable upon conversion of their notes. (See Note 6 to the consolidated and combined financial statements for additional information).

Shelf Registration Statement

On August 27, 2004, we filed an Amended Registration Statement on Form S-3/A with the Securities and Exchange Commission to facilitate possible future underwritten secondary offerings, block trades and other sales by the former owners and the former partners of Bacon & Woodrow. The registration statement became effective on August 31, 2004. Through September 30, 2004, there were no sales of Hewitt stock pursuant to this registration statement.

Release of Transfer Restrictions

Waiver of the transfer restrictions contained in our stockholders’ agreement no longer requires the approval of our Board of Directors. FORE Holdings advised the Company that it will release the transfer restrictions on 2% of the original number of aggregate Class B and Class C shares each month from October through December 2004 (approximately 1.6 million shares per month). Restrictions on 2% of the 0.9 million Class A shares held by certain Exult senior executives after the closing of the merger will also be released each month from October through December 2004 (approximately 20,000 shares per month). The Company is unable to estimate how many of the

related shares will be sold. FORE Holdings stated that liquidity opportunities after December 2004 could include a continuation of the release of transfer restrictions at the same or a different rate, a managed secondary offering, negotiated sales to institutions or a combination of these scenarios. As previously disclosed, sales restrictions on remaining Class B and Class C shares and shares held by certain senior Exult executives are expected to lapse on June 27, 2005.

Stock Repurchase Program

On June 14, 2004, our Board of Directors authorized the Company to repurchase up to an aggregate amount of \$150 million of Hewitt’s Class A, Class B, and Class C common stock, depending on market conditions and other customary factors, in light of the Company’s cash position and expected future cash flows. No repurchases were made through September 30, 2004.

Rule 144 Sales

In addition, during the year, an aggregate of 1,857,325 shares of stock have been converted from Class B and Class C common stock to Class A common stock and sold under Rule 144 by the former owners and the former partners of Bacon & Woodrow pursuant to a Rule 144 sale program previously approved by our Board of Directors.

Segments

Of our \$2.2 billion of consolidated net revenues for fiscal 2004, 65% was generated in our Outsourcing segment and 35% was generated in our Consulting segment.

Outsourcing

Our outsourcing business is composed of benefits, payroll and broader human resource administrative services, and beginning in fiscal 2005, will include a wide range of human resource administrative services from the newly acquired Exult business. With the merger of Exult on October 1, 2004, we expanded the organization’s global presence and brought together existing service capabilities in payroll, workforce administration, rewards management, recruiting and staffing, performance management, learning and development, and talent management, with additional capabilities in recruiting and staffing, learning and development, global mobility, time and attendance, accounts payable, procurement expertise, and vendor management.

Since we first began providing outsourcing services in 1991, we have made significant investments in technology, personnel and office space to build our capabilities and address market opportunity. To maintain our outsourcing leadership position, we remain committed to making significant ongoing investments in technology, infrastructure, and people, in expanding our business and driving greater efficiencies. With the investments that we have made in the benefits administration business to date, our acquisitions of Exult, Cyborg, and NTRC, and our investments in workforce management administration, we expect to be able to continue to improve our outsourcing capabilities and attract new clients.

Consulting

Our consulting services consist of three principal categories: retirement and financial management, talent and organization consulting and health management. In addition to these principal Consulting service lines, we provide tailored communication services to enhance the success of client solutions in all of our service areas. And, to a lesser degree, our client development group also provides consulting services.

We provide a wide array of consulting and actuarial services covering the design, implementation, communication and operation of health and welfare, compensation and retirement plans, and broader human resources programs and processes.

We experience a high level of recurring work because of our clients' annual needs for certain of our services, such as actuarial valuations of defined benefit plans and consultations regarding the processes of compensation review and health plan selection and negotiation. Certain of our consulting services, however, support more discretionary or event-driven client activities, including the re-engineering of a client's human resources policies, corporate restructuring and change (e.g., mergers and acquisitions), and programs and projects designed to improve human resources effectiveness. As we have seen in our business and industry, the demand for these services can be affected by general economic conditions, the financial position of our clients and the particular strategic activities they may be considering, and, therefore, is variable from period to period and more difficult for us to predict.

Following the announcement of investigations by several states into the practices of insurance companies and insurance brokers, we reviewed our business practices relating to our Consulting services. We have received contingent commissions, on an unsolicited basis, which have been less than 0.1% of our Consulting revenues in each of the last three years. We stopped accepting these commissions in May 2004.

Consolidated Financial Highlights

Net revenues increased \$223 million or 11.3% to \$2,205 million in 2004 and increased \$265 million or 15.5% to \$1,982 million in 2003. The net effects of favorable foreign currency translation, principally from the strengthening of European currencies relative to the U.S. dollar, were approximately \$40 million for the year ended September 30, 2004. Revenues from acquisitions of approximately \$79 million for the year ended September 30, 2004 also contributed significantly to the increases. After adjusting for these factors, net revenues increased \$103 million, or 5.2%, for the year ended September 30, 2004. During 2004, we continued to see growth in the number of Outsourcing participants we serve. Outsourcing growth was 8.5% on an organic (i.e., excluding acquisitions), constant currency basis for 2004, including growth in our workforce management business. Consulting revenues declined 0.4% on an organic, constant currency basis for 2004. For the year, declines in demand for our discretionary consulting services, primarily in certain of the other consulting service areas, were offset by growth in health benefit management consulting

while retirement and financial management consulting remained relatively flat.

Operating income increased \$45 million or 25.2% to \$223 million from \$178 million in the prior year. During 2004, operating income as a percentage of net revenue increased to 10.1% compared to 9.0% in the prior year. In 2004 and 2003, the timing of the vesting of the initial public offering restricted stock awards had a significant impact on the comparability of results. Excluding the amortization of the non-cash initial public offering stock awards of \$17 million and \$39 million for years ended September 30, 2004 and 2003, respectively, operating income was \$240 million and \$217 million for these respective periods, an increase of 10.4% year over year. Excluding the initial public offering stock awards, operating income as a percentage of net revenue was 10.9% and 11.0% for the years ended September 30, 2004 and 2003, respectively. On this adjusted basis, operating margins remained relatively flat in 2004 from 2003. Increases in Outsourcing segment margin, related to continued efforts to drive efficiencies in our benefits administration outsourcing business, were offset by decreases in Consulting segment margin, which was the result of declines in our European region, driven by a combination of higher costs due to a previously planned office relocation and compensation costs on lower than planned revenue, which resulted from the delay of certain legislative changes in Europe, as well a decline in revenue for certain discretionary communications and other consulting assignments in North America.

Critical Accounting Policies and Estimates

Conforming with U.S. generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts and disclosures in the consolidated and combined financial statements and this Annual Report. The process of determining significant estimates is fact specific and takes into account factors such as historical experience, known facts, current and expected economic conditions and, in some cases, actuarial techniques. We periodically reevaluate these significant factors and make adjustments when facts and circumstances change, however, actual results may differ from estimates. Certain of our accounting policies require higher degrees of judgment than others in their application. These include certain aspects of accounting for revenue recognition, performance-based compensation, accounts receivable and unbilled work in process and goodwill and other intangible assets.

Revenues

We enter into numerous service contracts through our outsourcing and consulting businesses. Outsourcing contract terms typically range from three to five years, while consulting arrangements are generally of a short-term nature. The Company has contracts for multiple services primarily in the Outsourcing segment. In these contracts, standalone deliverables include core services, such as Defined Benefit, Health & Welfare, or Defined Contribution Benefit Plan Administration, and standalone ancillary services, such as *Your Total Rewards*. These

services are tracked and valued separately and recognized as revenue over the ongoing service period. Consulting services provided in connection with outsourcing engagements are accounted for at the time services are provided and are valued based on prevailing market rates. Most consulting assignments are also very short-term in nature, so that the risks of recognizing revenue in the wrong period or at different values for stand-alone deliverables is significantly reduced.

The Company's clients typically pay for consulting services either on a time-and-materials or on a fixed-fee basis. On fixed-fee engagements, revenues are recognized either as services are provided using the proportional performance method, which utilizes estimates of overall profitability and stages of project completion, or at the completion of a project, based on facts and circumstances of the client arrangement.

Losses on outsourcing or consulting arrangements are recognized during the period in which a loss becomes probable and the amount of the loss is reasonably estimable. Contract or project losses are determined to be the amount by which the estimated direct and a portion of indirect costs exceed the estimated total revenues that will be generated by the arrangement. Estimates are monitored during the term of the arrangement and any changes to estimates are recorded in the current period and can result in either increases or decreases to income.

Performance-Based Compensation

Our compensation program includes a performance-based component that is determined by management. Performance-based compensation is discretionary and is based on individual, team, and total Company performance. The amount of expense for performance-based compensation recognized at interim and annual reporting dates involves judgment, is based on our quarterly and annual results as compared to our internal targets, and takes into account other factors, including industry trends and the general economic environment. Annual performance-based compensation levels may vary from current expectations as a result of changes in the actual performance of the Company, team or individual. As such, accrued amounts are subject to change in future periods if actual future performance varies from performance levels anticipated in prior interim periods.

Client Receivables and Unbilled Work In Process

We periodically evaluate the collectibility of our client receivables and unbilled work in process based on a combination of factors. In circumstances where we become aware of a specific client's difficulty in meeting its financial obligations to us (e.g., bankruptcy, failure to pay amounts due to us or to others), we record an allowance for doubtful accounts to reduce the client receivable to what we reasonably believe will be collected. For all other clients, we recognize an allowance for doubtful accounts based on past write-off history and the length of time the receivables are past due. Facts and circumstances may change, which would require us to alter our estimates of the collectibility of client receivables and unbilled work in process. Factors mitigating this risk include our diverse client base. For the years ended September 30, 2004, 2003, and 2002, no single client accounted for more than 10% of our total revenues.

Goodwill and Other Intangible Assets

We apply the purchase method of accounting for acquisitions. The amounts assigned to the identifiable assets and liabilities acquired in connection with these acquisitions were based on estimated fair values as of the date of the acquisitions, with the remainder recorded as goodwill. Estimates of fair value have been based primarily upon future cash flow projections for the acquired business and net assets, discounted to present value using a risk adjusted discount rate. In connection with these acquisitions, we have recorded significant amounts of intangible assets, including goodwill.

We evaluate our goodwill for impairment whenever indicators of impairment exist, with reviews at least annually. The evaluation is based upon a comparison of the estimated fair value of the reporting unit to which the goodwill has been assigned to the sum of the carrying value of the assets and liabilities for that reporting unit. The fair values used in this evaluation are estimated based upon discounted future cash flow projections for the reporting unit. Our estimate of future cash flows is based on our experience, knowledge and typically third-party advice or market data. However, these estimates can be affected by other factors and economic conditions that can be difficult to predict. Intangible assets with definite lives are amortized over their estimated useful lives and are reviewed for impairment if indicators of impairment arise.

Historical Results of Operations

The following tables set forth our historical results of operations as a percentage of net revenues for the years ended September 30. Operating results for any period are not necessarily indicative of results for any future periods.

	Year ended September 30,							
	2004	2003 ⁽¹⁾	Increase/(Decrease)		2002 ⁽²⁾	% of Net Revenues		
			Amount	%		2004	2003	2002
Revenues:								
Revenues before reimbursements (net revenues)	\$2,204,682	\$1,981,656	\$223,026	11.3%	\$1,716,197	100.0%	100.0%	100.0%
Reimbursements	57,545	49,637	7,908	15.9	33,882	2.6	2.5	2.0
Total revenues	2,262,227	2,031,293	230,934	11.4	1,750,079	102.6	102.5	102.0
Operating expenses:								
Compensation and related expenses, excluding initial public offering restricted stock awards ⁽³⁾	1,412,908	1,266,931	145,977	11.5	1,014,993	64.1	63.9	59.1
Initial public offering restricted stock awards ⁽⁴⁾	16,733	39,010	(22,277)	(57.1)	27,525	0.8	2.0	1.6
Reimbursable expenses	57,545	49,637	7,908	15.9	33,882	2.6	2.5	2.0
Other operating expenses	431,912	396,009	35,903	9.1	357,789	19.6	20.0	20.9
Selling, general and administrative expenses	120,296	101,725	18,571	18.3	75,570	5.4	5.1	4.4
Total operating expenses	2,039,394	1,853,312	186,082	10.0	1,509,759	92.5	93.5	88.0
Operating income	222,833	177,981	44,852	25.2	240,320	10.1	9.0	14.0
Other expenses, net	(14,974)	(17,340)	2,366	(13.6)	(16,894)	(0.6)	(0.9)	(1.0)
Income before income taxes	207,859	160,641	47,218	29.4	223,426	9.5	8.1	13.0
Provision for income taxes	85,015	66,364	18,651	28.1	33,053	3.9	3.3	1.9
Net income ⁽⁵⁾	\$ 122,844	\$ 94,277	\$ 28,567	30.3%	\$ 190,373	5.6%	4.8%	11.1%

⁽¹⁾On June 5, 2003, we acquired Cyborg and on June 15, 2003, we acquired substantially all of the assets of NTRC. As such, their results are included in our results from the respective acquisition dates.

⁽²⁾On June 5, 2002, we acquired the benefits consulting business of Bacon & Woodrow and its results are included in our results from the acquisition date.

⁽³⁾Compensation and related expenses did not include compensation related to the FORE Holdings’ owners who were active in the business prior to our transition to a corporate structure on May 31, 2002.

⁽⁴⁾Compensation expense of \$17 million, \$39 million, and \$28 million for the years ended September 30, 2004, 2003, and 2002, respectively, related to the amortization of initial public offering restricted stock awards.

⁽⁵⁾Prior to our transition to a corporate structure, Hewitt operated as a limited liability company. In such form, owners of the Company were compensated through distributions of income and Hewitt did not incur firm-level income tax. Accordingly, results prior to May 31, 2002 do not include (i) compensation for services rendered by the owners or (ii) firm-level income tax expense.

Fiscal Years Ended September 30, 2004, 2003, and 2002 Revenues

Net revenues were \$2,205 million in 2004, \$1,982 million in 2003, and \$1,716 million in 2002. Net revenues increased by 11.3% in 2004, by 15.5% in 2003, and by 16.3% in 2002. Adjusting for the effects of acquisitions and the favorable effects of foreign currency translation, net revenues grew 5.2% in 2004 and 5.4% in 2003. Outsourcing net revenues increased by 14.8% to \$1,432 million in 2004, by 11.8% to \$1,247 million in 2003, and by 17.2% to \$1,115 million in 2002. Excluding the favorable effects of the acquisitions of Cyborg, NTRC, and the majority interest in our Puerto Rico operations of approximately \$72 million, and the effects of favorable foreign currency translation of approximately \$6 million, Outsourcing net revenues increased 8.5% in 2004. Outsourcing revenue growth was primarily from the addition

of new core benefits services in benefits administration, an increase in one-time projects and the addition of new workforce management clients coming on line. Excluding the favorable effects of the acquisitions of Cyborg and NTRC in 2003 of approximately \$29 million, and the effects of favorable foreign currency translation of approximately \$3 million, Outsourcing net revenues increased 8.9% in 2003. Revenue growth in our outsourcing business in 2003 and 2002, was from increased participant volume in benefits administration through the expansion of services with existing and new clients. Volume growth in 2004 and 2003 was offset in part by lower pricing on new client services and renewals. Consulting net revenues increased by 5.2% to \$773 million in 2004, by 22.3% to \$734 million in 2003, and by 14.7% to \$601 million in 2002. The majority of the growth in 2004 was due to the effect of favorable foreign currency translation of approximately \$34 million

and the effect of acquisitions of approximately \$7 million for NTRC, the majority interest in our Puerto Rico operations and a small acquisition in Ireland. Adjusting for the favorable effects of foreign currency and the acquisitions, Consulting net revenues decreased 0.4% in 2004, from the prior year. Declines in demand for our discretionary consulting services, primarily in certain of our other consulting service areas, were offset by growth in health benefit management consulting while retirement and financial management consulting remained relatively flat. Adjusting for the effects of the Bacon & Woodrow acquisition, the consolidation of our Dutch affiliate upon purchase of the remaining interest in that affiliate in the first quarter of 2003, and favorable foreign currency translation of approximately \$21 million in 2003 and \$5 million in 2002, Consulting net revenues decreased 0.2% in 2003 and increased 6.2% in 2002. Growth in retirement plan and health benefit management consulting in 2003 and 2002 was offset by declines in demand for our more discretionary consulting services in 2003 and to a lesser extent in 2002.

Compensation and Related Expenses

Compensation and related expenses (which include all personnel and outside contractor costs and related expenses) were \$1,413 million in 2004, \$1,267 million in 2003, and \$1,015 million in 2002. These expenses increased by 11.5% in 2004, by 24.8% in 2003, and by 21.2% in 2002. The \$146 million increase in compensation and related expenses in 2004 was due to increases in employee headcount from acquisitions in 2003 and 2004, the effects of foreign currency translation, wage increases, and increases in outsourcing personnel to support the growth of benefits administration outsourcing and workforce management. Excluding compensation expenses related to acquisitions of approximately \$54 million and the unfavorable effects of foreign currency translation of approximately \$21 million, compensation and related expenses grew 5.7% in 2004. Please note that in fiscal 2002, prior to May 31, 2002, compensation and related expenses did not include owners’ compensation as FORE Holdings’ owners were compensated through distributions of income. In connection with our transition to a corporate structure in June 2002, we incurred a non-recurring, non-cash \$18 million compensation expense resulting from certain owners receiving more than their proportional share of total capital, without offset for those owners who received less than their proportional share in the conversion of owners’ capital into common stock, and a non-recurring \$8 million compensation expense related to our establishing an owner vacation liability. The net increase in overall compensation and related expenses in 2003 over 2002 after the inclusion of estimated owner compensation and the exclusion of the non-recurring charges in 2002, was primarily due to the inclusion of Bacon & Woodrow’s compensation and related expenses, cost of living increases, increases in employee headcount from the 2003 acquisitions of Cyborg and NTRC, and increases in Outsourcing personnel to support the growth of benefit administration outsourcing and workforce management. As a percentage of net revenues, compensation

and related expenses were 64.1%, 63.9%, and 59.1% in 2004, 2003, and 2002, respectively. Adjusting for the effects of acquisitions, the incorporation one-time charges of approximately \$26 million, and including estimated owner compensation of approximately \$108 million in 2002, compensation and related expenses as a percentage of net revenues was 63.9% for 2004, 63.7% for 2003, and 64.2% for 2002. Compensation and related expenses as a percentage of net revenues increased slightly in 2004 from 2003 primarily due to lower than expected revenues relative to compensation increases in our retirement plan consulting business in Europe, offset by our continued effort to increase productivity and leverage technology within our benefits administration outsourcing business, increased productivity in certain of our discretionary consulting services and the leveraging of shared services personnel.

Initial Public Offering Restricted Stock Awards

In connection with our initial public offering on June 27, 2002, we granted approximately 5.8 million shares of Class A restricted stock and restricted stock units to our employees. Compensation and related payroll tax expenses of approximately \$83 million were recorded as initial public offering restricted stock award expense from June 27, 2002 through September 30, 2004, of which \$17 million was recorded in 2004, \$39 million in 2003, and \$28 million in 2002. The changes in the initial public offering restricted stock award expense in 2003 and 2004, respectively, relates to the timing of the vesting of the awards. Stock awards that vested over six months were fully expensed in early 2003, while the awards vesting over four years continue to be recognized into expense through June 27, 2006.

Other Operating Expenses

Other operating expenses (which include technology, occupancy and non-compensation related direct client service costs) were \$432 million in 2004, \$396 million in 2003, and \$358 million in 2002. These expenses increased by 9.1% in 2004, by 10.7% in 2003, and by 6.0% in 2002, but as a percentage of revenue declined slightly to 19.6% from 20.0% and 20.9% in 2004, 2003, and 2002, respectively. Adjusting for the effects of the acquisitions in 2004, 2003, and 2002, other operating expenses as a percentage of net revenues were 19.5%, 19.9%, and 20.5%, respectively. The \$36 million increase in other operating expenses in 2004 primarily reflects the inclusion of operating costs from businesses acquired in 2004 and 2003, increased occupancy expenses in connection with a planned office relocation in the United Kingdom and increases in computer equipment repairs and maintenance, partially offset by lower depreciation on computer equipment. The \$38 million increase in other operating expenses in 2003 primarily reflects the inclusion of a full year of Bacon & Woodrow’s results since the June 2002 acquisition as well as the inclusion of acquisitions made by the Company in 2003, increased depreciation and amortization expenses on buildings, computer equipment, and software and increased computer maintenance expenses. These increases were partially offset by lower telecommunications

expenses in our Outsourcing segment as compared to fiscal 2002. There was a \$20 million increase in other operating expenses in 2002, which primarily reflects the inclusion of Bacon & Woodrow since the acquisition, along with increased spending in technology and maintenance expense in Outsourcing, offset in part by lower depreciation expenses on computer equipment and lower software maintenance expenses.

Selling, General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses (which include promotion and marketing costs, corporate professional services, provisions for doubtful accounts and other general office expenses) were \$120 million in 2004, \$102 million in 2003, and \$76 million in 2002. These expenses increased by 18.3% in 2004, by 34.6% in 2003, and decreased by 14.5% in 2002. The \$19 million increase in SG&A expenses in 2004 from 2003 resulted from the inclusion of SG&A costs from businesses acquired in 2004 and 2003, increased insurance costs, and travel expenses. SG&A expenses increased \$26 million in 2003 from 2002, which primarily reflects the inclusion of Bacon & Woodrow since the acquisition as well as the inclusion of the 2003 acquisitions from their respective acquisition dates, and increased travel and insurance expense in 2003. There was a \$1 million increase in SG&A expenses in 2002, after excluding the effects of Sageo in 2001, which primarily reflects the operations of Bacon & Woodrow since the acquisition on June 5, 2002, offset in part by lower client-related and internal travel-related expenses. As a percentage of net revenues, SG&A expenses were 5.5%, 5.1%, and 4.4% in 2004, 2003, and 2002, respectively. Adjusting for the effects of the acquisitions in 2004, 2003, and 2002, SG&A expenses as a percentage of net revenues were 5.3%, 4.9%, and 4.6%, respectively.

Other Expenses, Net

Other expenses, net (which includes interest expense, interest income, and other income or expense, such as equity earnings on unconsolidated ventures) were \$15 million in 2004, \$17 million in 2003, and \$17 million in 2002. As a percentage of net revenues, other expenses, net was 1% or less in all three years. Interest expense was \$19 million in 2004, \$20 million in 2003, and \$16 million in 2002. The decrease in the interest expense in 2004 is primarily due to decreased principal balances on our fixed rate long-term debt. The increase in interest expense in 2003 is primarily due to the addition of a full year of interest expense on two new capital leases for office space executed in the third quarter of 2002. Interest expense remained flat in 2002 from 2001 despite a portion of our short-term debt being repaid with proceeds from the initial public offering because of higher interest expense associated with the two new office capital leases. In 2002, other expenses, net also included a loss of approximately \$4 million from a foreign currency option contract purchased in connection with our acquisition of the benefits consulting business of Bacon & Woodrow which expired in 2002.

Provision for Income Taxes

The provision for income taxes was \$85 million for the year ended September 30, 2004, compared to \$66 million in 2003, and \$33 million in 2002. The increase in the provision for income taxes in 2004 over 2003 is due to increased income before income taxes. The increase in the provision for income taxes in 2003 is primarily due to earnings being taxed for the full year in 2003 as compared to only four months in 2002, as a result of the timing of the Company’s transition to a corporate structure on May 31, 2002 and related one-time charges in June 2002. Approximately \$22 million of the \$33 million tax expense for fiscal 2002 related to tax liabilities arising both from a mandatory change in the Company’s tax accounting method and from the initial recording of deferred tax assets and liabilities related to temporary differences which resulted from the transition to a corporate structure. The remaining \$11 million represents income tax expense arising from earnings between May 31, 2002 and September 30, 2002, while the Company operated as a corporation. The non-recurring, non-cash \$18 million compensation expense resulting from owners receiving more than their proportional share of total capital, without offset for those owners who received less than their proportional share in conversion of owners’ capital into common stock, was not deductible.

Segment Results

We operate many of the administrative and support functions of our business through centralized shared service operations, an arrangement that we believe is the most economical and effective means of supporting the Outsourcing and Consulting segments. These shared services include information systems, human resources, overall corporate management, finance and legal services, general office support, and space management. Additionally, we utilize a client development group that markets the entire spectrum of our services. The compensation and related expenses, other operating expenses, and selling, general and administrative expenses of the administrative and marketing functions are not allocated to the business segments; rather, they are included in unallocated shared costs. The costs of information services, human resources and the direct client delivery activities provided by the client development function are, however, allocated to the Outsourcing and Consulting segments on a specific identification basis or based on usage and headcount. Operating income before unallocated shared costs is referred to as “segment income” throughout this discussion.

Reconciliation of Segment Results to Total Company Results

In thousands	Increase/ (Decrease)				
	2004	2003	Amount	%	2002
Outsourcing⁽¹⁾					
Revenues before reimbursements (net revenues)	\$1,432,091	\$1,247,234	\$184,857	14.8%	\$1,115,462
Segment income ⁽²⁾	297,911	245,905	52,006	21.1%	272,702
Segment income as a percent of segment net revenues	20.8%	19.7%			24.4%
Consulting⁽³⁾					
Revenues before reimbursements (net revenues)	772,591	734,422	38,169	5.2%	600,735
Segment income ⁽²⁾	126,064	136,380	(10,316)	(7.6)%	161,787
Segment income as a percent of segment net revenues	16.3%	18.6%			26.9%
Total Company					
Revenues before reimbursements (net revenues)	\$2,204,682	\$1,981,656	\$223,026	11.3%	\$1,716,197
Reimbursements	57,545	49,637	7,908	15.9%	33,882
Total revenues	\$2,262,227	\$2,031,293	\$230,934	11.4%	\$1,750,079
Segment income ⁽²⁾	\$ 423,975	\$ 382,285	\$ 41,690	10.9%	\$ 434,489
Charges not recorded at the Segment level:					
One-time charges ⁽⁴⁾	—	—	—	—%	26,143
Initial public offering restricted stock awards ⁽⁵⁾	16,733	39,010	(22,277)	(57.1)%	27,525
Unallocated shared costs ⁽²⁾	184,409	165,294	19,115	11.6%	140,501
Operating income ⁽²⁾	\$ 222,833	\$ 177,981	\$ 44,852	25.2%	\$ 240,320

⁽¹⁾On June 5, 2003, we acquired Cyborg and on June 15, 2003, we acquired substantially all of the assets of NTRC. Their results are included in our Outsourcing segment results from the respective acquisition dates.

⁽²⁾Prior to May 31, 2002, FORE Holdings’ owners were compensated through distributions of income. In connection with our transition to a corporate structure on May 31, 2002, FORE Holdings’ owners who worked in the business became employees and we began to record their compensation as compensation and related expenses in arriving at segment income.

⁽³⁾On June 5, 2002, we acquired the benefits consulting business of Bacon & Woodrow. As such, the results of Bacon & Woodrow have been included in our Consulting segment results from the acquisition date.

⁽⁴⁾In connection with our transition to a corporate structure in fiscal 2002, the following one-time charges were incurred: a) \$8 million of non-recurring compensation expense related to the establishment of a vacation liability for FORE Holdings’ owners and b) \$18 million of non-recurring compensation expense resulting from certain FORE Holdings’ owners receiving more common stock than their proportional share of total capital, without offset for those FORE Holdings’ owners who received less than their proportional share.

⁽⁵⁾Compensation expense of \$17 million, \$39 million, and \$28 million for the years ended September 30, 2004, 2003, and 2002, respectively, related to the amortization of initial public offering restricted stock awards.

Outsourcing

Fiscal Years Ended September 30, 2004, 2003, and 2002

Outsourcing net revenues were \$1,432 million in 2004, \$1,247 million in 2003, and \$1,115 million in 2002. Net revenues increased by 14.8% in 2004, 11.8% in 2003, and 17.2% in 2002. Revenue growth in 2004 was due, in part, to the addition of acquisitions such as Cyborg, NTRC, and consolidation of our Puerto Rico operations upon the purchase of the remaining interest in that affiliate, totaling approximately \$72 million, as well as favorable effects of foreign currency translation of approximately \$6 million. Excluding the effects of these acquisitions and favorable foreign currency translation, Outsourcing net revenues increased 8.5% in 2004. This Outsourcing net revenue growth was primarily in the benefits administration business and was due to the addition of new core benefits services, an increase in one-time projects and new workforce management clients coming on line. Revenue growth in 2003 was due, in part, to the acquisitions of Cyborg and NTRC totaling \$29 million, as well as the favorable effects of foreign currency translation of approximately \$3 million. Excluding the effects of these acquisitions and favorable foreign currency translation, Outsourcing net revenues increased 8.9% in 2003. Approximately one-half of this organic net revenue growth was from the addition of new clients and the other half from expanding services with existing clients in benefits administration. In 2002, approximately one-quarter of our net revenue growth was a result of adding new clients with the remainder of the growth from expanding services with existing clients in benefits administration.

Outsourcing segment income as a percentage of outsourcing net revenues was 20.8% in 2004, 19.7% in 2003, and 24.4% in 2002. Excluding the effects of the acquisitions of \$12 million in 2004 and \$3 million in 2003 and including estimated owner compensation of \$22 million prior to the transition to a corporate structure in 2002, segment income as a percentage of Outsourcing net revenues was 21.0%, 20.5%, and 22.4% in 2004, 2003, and 2002, respectively. The increase in margin in 2004 was due to continued efforts to drive efficiencies in our benefits administration outsourcing business by leveraging our technology and scale, which was partially offset by increased personnel to support the development and growth of our workforce management and payroll offerings. The decrease in margin in 2003 from 2002 primarily relates to our continued investment in the development of our workforce management offering.

Consulting

Fiscal Years Ended September 30, 2004, 2003, and 2002

Consulting net revenues were \$773 million in 2004, \$734 million in 2003, and \$601 million in 2002. Net revenues increased 5.2% in 2004, 22.3% in 2003, and 14.7% in 2002. In 2004, the majority of this growth was due to the effect of favorable foreign currency translation of approximately \$34 million, which primarily affected our retirement plan consulting, and the effect of acquisitions of approximately \$7 million for NTRC, the consolidation of our Puerto Rico operations upon the purchase of the remaining interest in that affiliate and a small acquisition in Ireland. Adjusting for the favorable effects of foreign currency and the acquisitions, Consulting net revenues decreased 0.4% in 2004, as compared to the prior year. Declines in demand for our discretionary consulting services, primarily in certain of our other consulting service areas, were offset by growth in health benefit management consulting while retirement and financial management was generally flat year over year. In 2003, Consulting net revenues increased primarily as a result of the June 2002 acquisition of the benefits consulting business of Bacon & Woodrow. A portion of this growth was also due to favorable foreign currency translation from the strengthening of European currencies relative to the U.S. dollar and consolidation of our Dutch affiliate upon purchase of the remaining interest in that affiliate in the first quarter of 2003. Adjusting for the effects of these acquisitions and favorable foreign currency translation of approximately \$21 million in 2003 and \$5 million in 2002, Consulting net revenues decreased 0.2% in 2003 and increased 6.2% in 2002. Growth in retirement plan and health benefit management consulting in 2003 and 2002 was offset by declines in demand for our more discretionary consulting services in 2003 and to a lesser extent in 2002.

Consulting segment income as a percentage of consulting net revenues was 16.3% in 2004, 18.6% in 2003, and 26.9% in 2002. Adjusting for effects of the acquisitions in 2004, 2003, and 2002 and including estimated owner compensation of \$57 million prior to the transition to a corporate structure in 2002, segment income as a percentage of Consulting net revenues was 15.8%, 18.8%, and 16.4% in 2004, 2003, and 2002, respectively. The decrease in margins in 2004 is primarily the result of declines in our European region, driven by a combination of higher costs due to a previously planned office relocation and compensation costs on lower than planned revenue, which resulted from the delay of certain legislative changes in Europe, as well as a decline in revenue for certain discretionary communications and other consulting assignments in North America. The increase in margins in 2003 is primarily due to an increase in margin for retirement plan and health benefit consulting services over our more discretionary consulting services which were down due to continued soft demand for those services in 2003 and 2002.

Quarterly Results

The following tables set forth the unaudited quarterly financial data for the periods indicated. The information for each of these periods has been prepared on the same basis as the audited consolidated and combined financial statements and,

in our opinion, reflects all adjustments consisting only of normal recurring adjustments necessary to present fairly our financial results. Operating results for previous periods do not necessarily indicate results that may be achieved in any future period. Amounts are in millions, except earnings per share information.

	Fiscal 2004 ⁽¹⁾				Fiscal 2003			
	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr	1st Qtr	2nd Qtr	3rd Qtr ⁽¹⁾	4th Qtr ⁽¹⁾
Revenues:								
Revenues before reimbursements (net revenue)	\$532	\$546	\$552	\$575	\$480	\$478	\$495	\$529
Reimbursements	19	13	12	14	14	14	13	9
Total revenues	551	559	564	589	494	492	508	538
Operating expenses:								
Compensation and related expenses, excluding initial public offering restricted stock awards	340	347	359	367	311	310	319	327
Initial public offering restricted stock awards	4	5	4	4	25	5	6	3
Reimbursable expenses	19	13	12	14	14	14	13	9
Other operating expenses	105	111	103	113	94	94	97	111
Selling, general and administrative expenses	27	28	32	33	20	25	25	32
Total operating expenses	495	504	510	531	464	448	460	482
Operating income	56	55	54	58	30	44	48	56
Other expenses, net	(6)	(4)	(4)	(1)	(5)	(4)	(3)	(5)
Income before income taxes	50	51	50	57	25	40	45	51
Provision for income taxes	21	21	20	23	10	16	19	22
Net income	\$ 29	\$ 30	\$ 30	\$ 34	\$ 15	\$ 24	\$ 26	\$ 29
Earnings per share								
—Basic	\$0.31	\$0.32	\$0.31	\$0.34	\$0.16	\$0.25	\$0.28	\$0.31
—Diluted	\$0.30	\$0.31	\$0.30	\$0.34	\$0.15	\$0.24	\$0.27	\$0.31

⁽¹⁾On June 5, 2003, we acquired Cyborg and on June 15, 2003, we acquired substantially all of the assets of NTRC. As such, their results are included in our results from the respective acquisition dates.

Seasonality and Inflation

Revenues and income vary over the fiscal year. Within our Outsourcing segment, we generally experience a seasonal increase in our fiscal fourth and first quarter revenues because our clients’ benefit enrollment processes typically occur during the fall. Within our Consulting segment, we typically experience a seasonal peak in the third and fourth fiscal quarters which reflects our clients’ business needs for these services. We believe inflation has had little effect on our results of operations during the past three years.

Pro Forma Results of Operations

During fiscal 2002, we completed several significant transactions. We completed our transition to a corporate structure in May 2002 and our initial public offering and the acquisition of Bacon & Woodrow in June 2002. The following pro forma results give effect to all three of these transactions as if they had occurred on October 1, 2001, the beginning of fiscal 2002, and exclude any non-recurring adjustments to facilitate comparability across fiscal periods. We believe that pro forma fiscal 2002 results provide meaningful information for comparison with fiscal 2003 and 2004 results.

The Bacon & Woodrow historical results in the following pro forma income statement reflect Bacon & Woodrow’s results prior to the acquisition on June 5, 2002. As such, for the year ended September 30, 2002, the historical results for Bacon & Woodrow include approximately eight months of Bacon & Woodrow’s results prior to the acquisition. The historical results of Hewitt for fiscal 2002 include Bacon & Woodrow’s results since June 5, 2002.

The information presented is not necessarily indicative of the results of operations that might have occurred had the events described above actually taken place as of the dates specified. The pro forma adjustments are based upon available information and assumptions that management believes are reasonable. The Pro Forma Results of Operations and accompanying notes should be read in conjunction with our consolidated and combined financial statements and related notes included elsewhere in this Annual Report.

Pro Forma Income Statement (unaudited)

Dollars in millions, except share and per share data	Year Ended September 30, 2002				
	Hewitt Historical	B&W Historical	Acquisition and Incorporation Adjustments ⁽¹⁾	Adjustments for the Offering ⁽²⁾	Pro Forma
Revenues:					
Revenues before reimbursements (net revenues)	\$1,716	\$91	\$ —	\$ —	\$1,807
Reimbursements	34	3	—	—	37
Total revenues	1,750	94	—	—	1,844
Operating expenses:					
Compensation and related expenses, excluding initial public offering restricted stock awards	1,015	50	93	—	1,158
Initial public offering restricted stock awards	28	—	—	35	63
Reimbursable expenses	34	3	—	—	37
Other operating expenses	358	11	2	—	371
Selling, general and administrative expenses	75	14	(8)	—	81
Total operating expenses	1,510	78	87	35	1,710
Operating income	240	16	(87)	(35)	134
Other expenses, net	(17)	(1)	3	—	(15)
Income before taxes and owner distributions	223	15	(84)	(35)	119
Provision for income taxes	33	—	32	(14)	51
Income before owner distributions		\$15			
Net income	\$ 190		\$(116)	\$(21)	\$ 68
Earnings per share:					
—Basic					\$ 0.73
—Diluted					\$ 0.71
Weighted average shares:					
—Basic					93,250,167
—Diluted					96,330,933

⁽¹⁾Bacon & Woodrow acquisition and Hewitt incorporation adjustments include the following one-time items that are excluded for pro forma purposes: an \$8 million compensation expense for a vacation liability arising from FORE Holdings’ owners becoming employees of the Company; an \$18 million compensation expense resulting from the requirement to recognize the extent to which certain owners’ stock allocation was greater than their proportional share of the capital accounts, without offset for the extent to which certain owners’ stock allocation is less than their proportional share of the capital accounts; a \$22 million non-recurring income tax expense resulting from the mandatory change in our tax accounting method and the establishment of deferred tax assets and liabilities; a \$1 million compensation expense reflecting our assumption of annuity liabilities in connection with the Bacon & Woodrow acquisition; a \$6 million expense related to the former Bacon & Woodrow partners’ purchase of indemnity insurance prior to the acquisition; \$2 million of acquisition-related professional service expenses incurred by Bacon & Woodrow; and \$4 million of losses incurred on a foreign currency purchase option related to the acquisition. Other adjustments include expenses that the Company would have incurred had it been a corporation for the entire period presented: \$120 million of owner compensation expense for both FORE Holdings’ owners and Bacon & Woodrow partners; \$54 million of additional income tax expense as if the Company had been a taxable entity for the entire period; \$2 million of amortization of intangible assets created as part of the acquisition; and \$1 million of interest expense on borrowings to fund distributions of accumulated earnings to Bacon & Woodrow’s partners.

⁽²⁾Initial public offering adjustments include compensation expense of \$35 million reflecting the amortization of the one-time grant of initial public offering restricted stock awards and the related income tax benefit of \$14 million.

On a pro forma basis, the Company’s net revenues were \$1,807 million compared to its actual net revenues of \$1,716 million for the year ended September 30, 2002. The difference in the net revenues is attributable to the inclusion of a full twelve months of the Bacon & Woodrow net revenues on a pro forma basis as compared to the inclusion of the Bacon & Woodrow net revenues from the June 5, 2002, acquisition date forward in the reported historical results for 2002.

On a pro forma basis, the Company’s net income was \$68 million compared to its actual net income of \$190 million for the year ended September 30, 2002. The difference is attributable to: (1) the inclusion of owner salaries, benefits, bonuses, and payroll taxes for the entire year; (2) the inclusion of an

estimated tax expense as if the Company had been subject to income tax for the entire year; (3) the exclusion of non-recurring charges for owner vacation accrual, the disproportionate share compensation charge, and the \$22 million non-recurring income tax expense; (4) the inclusion of compensation expense for the entire year, reflecting the amortization of the one-time grant of initial public offering awards to employees and the estimated tax benefit related to these awards; (5) the inclusion of the Bacon & Woodrow operations for the entire year, adjusted for non-recurring items, on a pro forma basis; (6) the exclusion of losses incurred on a foreign currency purchase option; (7) the inclusion of amortization expense for the amortization of intangible assets acquired as part of the Bacon

& Woodrow business in pro forma net income; (8) the inclusion of estimated interest expense for borrowings to fund the payment of distributions to the former partners of Bacon & Woodrow; and (9) the inclusion of estimated compensation expense for the assumption of annuity liabilities in connection with the Bacon & Woodrow acquisition.

Liquidity and Capital Resources

We have historically funded our growth and working capital requirements with internally generated funds, credit facilities and term notes. Our change to a corporate structure in May 2002 and our initial public offering in June 2002 enhanced our ability to access public market financing to fund new investments and acquisitions, as well as to meet ongoing and future capital resource needs.

Summary of Cash Flows

In thousands	Year Ended September 30,		
	2004	2003	2002
Cash provided by operating activities	\$ 241,089	\$ 278,554	\$ 251,221
Cash used in investing activities	(135,787)	(240,098)	(153,404)
Cash used in financing activities	(44,619)	(51,641)	(81,728)
Effect of exchange rates on cash	1,013	2,210	2,065
Net increase in cash and cash equivalents	61,696	(10,975)	18,154
Cash and cash equivalents at beginning of period	67,785	78,760	60,606
Cash and cash equivalents at end of period	\$ 129,481	\$ 67,785	\$ 78,760

At September 30, 2004, we reclassified the auction rate municipal bonds that were included in cash and cash equivalents to investments. At September 30, 2004, 2003, and 2002, our investments in the auction rate municipal bonds totaled \$183 million, \$160 million, and \$58 million, respectively. Cash and cash equivalents were \$129 million, \$68 million, and \$79 million at September 30, 2004, 2003, and 2002, respectively. Cash and cash equivalents increased by \$62 million or 91.0% in 2004, decreased by \$11 million or 13.9% in 2003, and increased by \$18 million or 30% in 2002. Working capital, defined as current assets less current liabilities, was \$418 million, \$284 million, and \$200 million at September 30, 2004, 2003, and 2002, respectively.

For the years ended September 30, 2004, 2003, and 2002, cash provided by operating activities was \$241 million, \$279 million, and \$251 million, respectively. The decrease in cash provided by operating activities in 2004 was primarily related to a significant increase in advanced billing arrangements in the prior year while current year advance billing levels remained steady. Additionally, the decrease was due in part to the timing of cash collection of receivables and limited deferred billing arrangements, partially offset by increases in

accounts payable and deferred compensation. The increase in cash flows provided by operating activities in 2003 over 2002 was due largely to increases in collections on client receivables. This increase was offset by the inclusion of a full year of compensation expenses related to former owners and a provision for corporate income taxes, stemming from our transition to a corporate structure on May 31, 2002. Prior to May 31, 2002, the distributions to FORE Holdings’ owners were paid out of cash flows from financing activities as capital distributions, and we did not pay corporate income taxes when we operated as a limited liability company. In 2002, cash collections on client receivables were lower as a result of the distribution of \$153 million of client receivables to FORE Holdings in fiscal 2002 as part of our transition to a corporate structure, which reduced our fiscal 2002 cash flows from operating activities.

For the years ended September 30, 2004, 2003, and 2002, cash used in investing activities was \$136 million, \$240 million, and \$153 million, respectively. The decrease in cash used in investing activities in 2004 over 2003 was primarily due to a decrease in net purchases of short-term investments and less net cash paid for acquisitions in the current year than in the prior year. Excluding purchases and sales of short-term investments and cash paid for acquisitions, cash used in investing activities increased by \$28 million due to increased expenditures for property and equipment, offset by slightly lower expenditures for software development than in the prior year. The Company’s property and equipment expenditures were primarily for computer and telecommunications equipment and leasehold improvements and furniture and fixtures related to the relocation to new office space in the United Kingdom and the expansion of operations in India. The increase in cash used in investing activities in 2003 over 2002 was primarily due to cash paid for acquisitions (see Note 6 to the consolidated and combined financial statements) and increased net purchases of short-term investments, offset by decreased spending on computer hardware and software development.

For the year ended September 30, 2004, 2003, and 2002, cash used in financing activities was \$45 million, \$52 million, and \$82 million, respectively. The decrease in cash used in financing activities in 2004 from 2003 was primarily due to reduced spending on capital lease obligations as we have decreased our leasing in favor of purchasing equipment and due to increased proceeds from the exercise of stock options resulting from more options becoming vested. These lower uses of cash were offset by increased payments on our long-term debt as the installments on our unsecured senior term notes have begun to come due. With respect to 2003 and 2002, after our transition to a corporate structure in mid-2002, capital distributions to FORE Holdings’ owners were replaced by compensation and related expenses for those owners who remained active in the business. This change shifted the funds used to pay owner employees from financing to operating activities in mid-2002. Prior to the change, the capital distributions in 2002 were offset in large part by the receipt of the initial public offering proceeds in 2002. Moving into 2003, this change in corporate structure and form of owner

remuneration was one of the primary reasons cash used in financing declined significantly in 2003. Offsetting the decrease in 2003 was an increase in cash used in financing activities to pay down approximately \$8 million of additional debt from internally generated funds from operations than in the prior year.

We incur significant cash outflows for upfront implementation efforts on new outsourcing services. These costs are capitalized as Deferred Contract Costs and amortized over the life of the respective outsourcing arrangements. Similarly, upfront implementation fees are also deferred as Deferred Contract Revenues and amortized over the life of the respective outsourcing arrangements. Historically, for most arrangements, we received upfront implementation fees for those efforts; however, implementation fees may also be received over the ongoing services period. We have seen a shift to more of our implementation fees being recovered over the ongoing services

period. If this shift were to continue, this would reduce our operating cash flows when beginning to implement large new outsourcing agreements than we’ve experienced in the past.

Capital expenditures for property, plant and equipment and software were approximately \$101 million, \$70 million, and \$94 million for the years ended September 30, 2004, 2003, and 2002, respectively. The Company’s significant investments in 2004 were for computer and telecommunications equipment, leasehold improvements and furniture and fixtures.

Commitments

Significant ongoing commitments consist primarily of leases and debt. The following table shows the minimum future debt or non-cancelable rental payments required under existing debt agreements or lease agreements which have initial or remaining non-cancelable lease terms in excess of one year as of September 30, 2004.

Contractual Obligations

In millions	Payments Due in Fiscal Year				
	Total	2005	2006-2007	2008-2009	Thereafter
Operating leases:					
Related party	\$ 438	\$ 33	\$ 67	\$ 67	\$271
Third party	420	65	165	54	136
	858	98	232	121	407
Capital leases:					
Third party	132	11	19	20	82
	132	11	19	20	82
Debt:					
Principal	135	13	51	24	47
Interest	39	10	16	9	4
	174	23	67	33	51
Purchase commitments	54	29	24	1	—
Other long-term liabilities	59	4	15	7	33
Total Contractual Obligations	\$1,277	\$165	\$357	\$182	\$573

Purchase commitments consist of commitments for telecommunications usage, software licenses, consulting contracts and insurance coverage. Other long-term liabilities consist primarily of payments for pension plans, post retirement benefit plans, and other long-term liabilities.

Operating Leases

We have entered into related party operating leases with FORE Holdings and its subsidiaries, Hewitt Properties I LLC, Hewitt Properties II LLC, Hewitt Properties III LLC, Hewitt Properties IV LLC, and Overlook Associates (an equity method investment of

Holdings Property Entity	Location	Commencement Date	Expiration Date
Hewitt Properties I	Lincolnshire, Illinois	November 1998	November 2018
Hewitt Properties II	Lincolnshire, Illinois	December 1999	December 2019
Hewitt Properties III	Lincolnshire, Illinois	May 1999	May 2014
Hewitt Properties IV	Orlando, Florida	March 2000	March 2020
Hewitt Properties IV	The Woodlands, Texas	March 2000	March 2020
Overlook Associates	Lincolnshire, Illinois	*	*

*We have several leases of various terms with Overlook Associates. The first began in 1989 and the last will expire in 2017.

Total lease payments to FORE Holdings and subsidiaries were \$34 million in 2004, \$34 million in 2003, and \$40 million in 2002. The leases were entered into on terms comparable to those which could have been obtained on an arm’s length basis. The underlying real property value owned by FORE Holdings’ property entities aggregated \$360 million and \$357 million in 2004 and 2003, respectively. The investments in the properties owned by these related parties were funded through capital contributions by FORE Holdings and third-party debt. Total outstanding debt owed to third parties by these related parties totaled \$261 million and \$274 million in 2004 and 2003, respectively. The debt is payable over periods that range up to sixteen years, and bears fixed interest rates that range from 5.58% to 7.93%. This debt is not reflected on our balance sheet as the obligation represented by the debt is an obligation of FORE Holdings and its related parties and is not an obligation of the Company. Substantially all of the activities of FORE Holdings’ property entities involve assets that are leased to us. We refer you to Note 15 of our consolidated and combined financial statements for more information regarding these related party leases.

We also have various third-party operating leases for office space, furniture and equipment with terms ranging from one to twenty years. As of September 30, 2004, the minimum aggregate lease payments on these leases totaled \$420 million. We lease office space in approximately 81 locations in 30 countries. As of September 30, 2004, the minimum annual base rent under such office leases totaled \$58 million (non-U.S. lease rental rates converted into U.S. dollars at exchange rates as of September 30, 2004) and aggregate lease payments on the office leases totaled \$407 million. We also have several leases for office furniture used in Hewitt-owned buildings in Lincolnshire, Illinois, The Woodlands, Texas, and Orlando, Florida. The oldest of these leases has a commencement date of July 1, 1998 and expires on June 30, 2006. The most recent of these leases has a commencement date of December 1, 1999 and expires on May 31, 2007. As of September 30, 2004, combined annual lease payments under these leases were \$3 million and the minimum aggregate lease payments on these leases totaled \$9 million. We also lease office equipment such as copiers, servers and disk drives under numerous leases. Annual

FORE Holdings). The minimum aggregate lease payments on these leases totaled \$438 million as of September 30, 2004. The following are real estate lease commitments with FORE Holdings’ Property Entities which were outstanding as of September 30, 2004:

aggregate lease obligations under these leases as of September 30, 2004 were \$3 million and the minimum aggregate lease payments on these leases totaled \$5 million.

Total rental expenses for operating leases were \$116 million in 2004, \$104 million in 2003, and \$104 million in 2002.

Capital Leases

During the third quarter of fiscal 2002, we entered into two 15-year capital leases for office space. At inception of the leases, we recorded \$89 million in buildings and long-term debt to reflect the long-term capital lease obligations. Lease payments are made in monthly installments at 7.33% interest. As of September 30, 2004, the outstanding debt related to these leases was \$83 million. One of the leases, totaling approximately \$23 million at September 30, 2004, was with a related party, The Bayview Trust. However, on March 7, 2003, The Bayview Trust sold the building and our lease was assigned to the third-party purchaser of the building.

Our computer and telecommunications equipment installment notes and capitalized leases are secured by the related equipment. The amounts due are payable over three- to five-year terms and are payable in monthly or quarterly installments and at various interest rates ranging from 2.455% to 7.0%. At September 30, 2004, the outstanding balance on the equipment financing agreements was \$2 million.

Variable Interest Rate Debt

Our debt consists primarily of lines of credit, term notes, and equipment financing arrangements. We currently have one domestic unsecured line of credit facility. The three-year facility provides for borrowings up to \$75 million. Borrowings under the facility accrue interest at LIBOR plus 52.5 to 72.5 basis points or the prime rate, at our option. Borrowings are repayable upon demand or at expiration of the facility on September 27, 2005. Quarterly facility fees ranging from 10 to 15 basis points are charged on the average daily commitment under the facility. If the utilization under the facility exceeds 50% of the commitment, an additional utilization fee is assessed at a rate of 0.125% per annum. At September 30, 2004, there was no outstanding balance on the facility.

Hewitt Bacon & Woodrow Ltd., a U.K. subsidiary, has an unsecured British pound sterling line of credit permitting borrowings up to £5 million until expiration of the facility on July 31, 2005, at a current rate of 5.775%. As of September 30, 2004, there was no outstanding balance on the line of credit. There was other foreign debt outstanding at September 30, 2004 totaling approximately \$0.7 million, pursuant to local banking relationships in over a half-dozen countries.

We have a contract with a lender to guarantee borrowings of our subsidiaries up to \$20 million in multiple currency loans and letters of credit. There is no fixed termination date on this contract. This contract allows Hewitt’s foreign subsidiaries to secure financing at rates based on Hewitt’s creditworthiness. The contract was signed August 31, 2004, and \$1.4 million of the facility is used by Hewitt’s India office to support local letters of credit and bank guarantees. The facility provides for borrowings at LIBOR plus 75 basis points. As of September 30, 2004, there were no borrowings under this contract.

Fixed Interest Rate Debt

We have issued unsecured senior term notes to various financial institutions consisting primarily of insurance companies totaling \$134 million as of September 30, 2004. Of this amount, \$10 million bears interest at 7.65% and is repayable in October 2005; \$15 million bears interest at 7.90% and is repayable in October 2010; \$15 million bears interest at 7.93% and is repayable in June 2007; \$10 million bears interest at 8.11% and is repayable in June 2010; \$9 million bears interest at 7.94% and is repayable in five annual installments which began in March 2003; \$35 million bears interest at 8.08%, and is repayable in five annual installments beginning in March 2008; and \$40 million bears interest at 7.45%, and is repayable in five annual installments which began in May 2004. The unsecured senior term notes include provisions for significant early payment penalties.

A number of our debt agreements contain financial and other covenants including, among others, covenants restricting our ability to incur indebtedness and create liens, to sell the assets or stock of a collateralized subsidiary, and to pay dividends or make distributions to FORE Holdings’ owners, a violation of which would result in a default. Our debt agreements also contain covenants requiring Hewitt Associates LLC and its affiliates to maintain a minimum level of net worth of \$237 million at September 30, 2004, to maintain a maximum ratio of total debt to net worth of 0.45 to 1.00, to maintain interest rate coverage of at least 2.00 to 1.00 and to maintain a leverage ratio not to exceed 2.25 to 1.00. At September 30, 2004, we were in compliance with the terms of our debt agreements.

Self-Insurance

We established a captive insurance subsidiary in fiscal 2003 as a cost-effective way to self-insure against certain business risks and losses. To date, the captive insurance subsidiary has issued policies to cover the deductible portion of various insured exposures including the deductible portions of our workers compensation and professional liability insurance.

We believe the cash on hand, together with funds from operations, other current assets, and existing credit facilities will satisfy our expected working capital, contractual obligations, capital expenditures, and investment requirements for at least the next twelve months and the foreseeable future.

New Accounting Pronouncements

In January 2003, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation No. 46 (“FIN No. 46”), *Consolidation of Variable Interest Entities*, to expand upon existing accounting guidance that addresses when a company should include in its financial statements the assets, liabilities and activities of another entity. In December 2003, the FASB revised FIN No. 46 to provide more clarification. Until now, a company generally has included another entity in its consolidated financial statements only if it controlled the entity through voting interests. FIN No. 46 changes that by requiring a variable interest entity, as defined, to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity’s activities or entitled to receive a majority of the entity’s residual returns or both. FIN No. 46 and FIN No. 46 as revised, did not have a material impact on the Company’s consolidated financial statements.

In September 2004, the FASB’s Emerging Issue Task Force (“EITF”) reached a consensus on EITF Issue No. 04-08, *The Effect of Contingently Convertible Instruments on Diluted Earnings per Share*. The Task Force reached a conclusion that Contingently Convertible Instruments (“Co-Cos”) should be included in diluted earnings per share computations, if dilutive, regardless of whether the market price trigger or other contingent feature has been met. Through September 30, 2004, EITF Issue No. 04-08 had no effect on the Company. In October 2004, with the acquisition of Exult and \$110 million of convertible senior notes, future earnings per share computations will include the convertible notes to the extent that they are determined to be dilutive.

Note Regarding Forward-Looking Statements

This report contains forward-looking statements relating to our operations that are based on our current expectations, estimates and projections. Words such as “anticipates,” “believes,” “continues,” “estimates,” “expects,” “goal,” “intends,” “may,” “opportunity,” “plans,” “potential,” “projects,” “forecasts,” “should,” “will,” and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties, and assumptions that are difficult to predict. Forward-looking statements are based upon assumptions as to future events that may not prove to be accurate. Actual outcomes and results may differ materially from what is expressed or forecasted in these forward-looking statements.

Our actual results may differ from the forward-looking statements for many reasons, including:

- The actions of our competitors could adversely impact our results.
- A prolonged economic downturn could have a material adverse effect on our results.
- Our ability to successfully manage our significant capital investments and acquisitions, including our ability to successfully integrate acquired companies.
- In our outsourcing business, early contract terminations could cause our business to be less profitable than anticipated.
- The demand for human resources business process outsourcing services may not grow at rates we anticipate.
- The loss of a significantly large client or several clients could have a material adverse effect on our revenues.
- If we are not able to anticipate and keep pace with rapid changes in government regulations or if government regulations increase the costs of delivering our services or decrease the need for our services, our business may be negatively affected.
- If we are not able to keep pace with rapid changes in technology or if growth in the use of technology in business is not as rapid as in the past, our business may be negatively affected.
- If our clients are not satisfied with our services, we may face damage to our professional reputation or legal liability.
- The loss of key employees may damage or result in the loss of client relationships.
- Our global operations and expansion strategy entail complex management, foreign currency, legal, tax, and economic risks.
- If we fail to establish and maintain alliances for developing, marketing, and delivering our services, our ability to increase our revenues and profitability may suffer.
- We have only a limited ability to protect the intellectual property rights that are important to our success, and we face the risk that our services or products may infringe upon the intellectual property rights of others.
- We rely on our computing and communications infrastructure and the integrity of these systems, and our revenue growth depends, in part, on our ability to use the Internet as a means for delivering human resources services.
- We rely on third parties to provide certain services and their failure to perform the service could do harm to our business.
- Our profitability will suffer if we are not able to maintain our prices and control our costs, including staffing costs.
- Our ability to recruit, retain, and motivate employees and to compete effectively.
- Insurance market conditions may reduce available coverage and result in increased premium costs and/or higher self retention of risks.
- Our client contracts and vendor relationships may not yield the results we expect.
- Our initial stockholders, many of whom are our employees, continue to hold a significant number of Hewitt shares and their interests may differ from those of our other stockholders.
- Our stock price may decline due to the large number of shares of common stock eligible for future sale.

For a more detailed discussion of our risk factors, see the information under the heading “Risk Factors” in our Registration Statements on Form S-3 (File No. 333-119576) and S-4 (File No. 333-117326) filed with the Securities and Exchange Commission. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or for any other reason.

Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risk primarily from changes in interest rates and foreign currency exchange rates. Historically, we have not entered into hedging transactions, such as foreign currency forward contracts or interest rate swaps, to manage this risk due to our low percentage of foreign debt and restrictions on our fixed rate debt. However, in August 2001, we purchased a £150 million foreign currency option to offset the foreign currency risk associated with the planned purchase of the benefits consulting business of Bacon & Woodrow. This instrument expired in May 2002. We do not hold or issue derivative financial instruments for trading purposes. At September 30, 2004, we were not a party to any hedging transaction or derivative financial instrument.

Interest Rate Risk

We are exposed to interest rate risk primarily through our portfolio of cash and cash equivalents and debt.

Our portfolio of cash and cash equivalents and short-term investments is designed for safety of principal and liquidity. We invest in the highest rated money market investments and regularly monitor the investment ratings. The investments are subject to inherent interest rate risk as investments mature and are reinvested at current market interest rates.

At September 30, 2004, 100% of our unsecured senior term notes were at a fixed rate. At September 30, 2004, a 10% decrease in the levels of interest rates with all other variables held constant would result in an increase in the fair market value of our fixed rate debt of \$1.7 million. At September 30, 2004, a 10% increase in the levels of interest rates with all other variables held constant would result in a decrease in the fair market value of our fixed rate debt of \$1.7 million.

Our short-term debt with a variable rate consists of our unsecured line of credit, which has an interest rate of LIBOR plus 52.5 to 72.5 basis points or the prime rate, at our option. As of September 30, 2004, there was no outstanding balance on this line of credit. In addition, Hewitt Bacon & Woodrow Ltd., our U.K. subsidiary, has an unsecured British pound sterling line of credit permitting borrowings of up to £5 million until expiration of the facility on July 31, 2005, at a current rate of 5.775%. As of September 30, 2004, there was no outstanding balance on the line of credit. There was other foreign debt outstanding at September 30, 2004, totaling approximately \$0.7 million, pursuant to local banking relationships in over a half-dozen countries.

Our foreign subsidiaries maintained debt with an effective interest rate of 6.21% during the year ended September 30, 2004. A one percentage point increase would have increased our interest expense by approximately \$0.15 million for the year ended September 30, 2004. We also maintain an invested cash portfolio which earned interest at an average rate of 1.54% during the year ended September 30, 2004. A one percentage point increase would have increased our interest income by approximately \$2.25 million for the year ended September 30, 2004. Therefore, the net effect of a one percentage point increase in interest rates would have been approximately \$2.10 million (or net decrease in income from a one percentage point decrease in the rate) for the year ended September 30, 2004.

Foreign Exchange Risk

For the year ended September 30, 2004, revenues from U.S. operations as a percent of total revenues were 81%. Unrealized foreign currency translation gains were \$29 million for the year ended September 30, 2004, and were primarily due to the strengthening of the British pound sterling relative to the U.S. dollar over the prior year. We do not enter into any foreign currency forward contracts for speculative or trading purposes.

Operating in international markets means that we are exposed to movements in foreign exchange rates, primarily the British pound sterling and the Euro. Approximately 11% of our net revenues for fiscal 2004 were from the United Kingdom. Approximately 3% of our net revenues for fiscal 2004 were from countries whose currency is the Euro. Changes in these foreign exchange rates could have a significant impact on our translated international results of operations in U.S. dollars. A 10% change in the average exchange rate for the British pound sterling in fiscal 2004, would have impacted our pre-tax net operating income by approximately \$1.4 million. A 10% change in the average exchange rate for the Euro would have impacted our pre-tax net operating income by approximately \$0.1 million for the year ended September 30, 2004.

Report of Independent Registered Public Accounting Firm

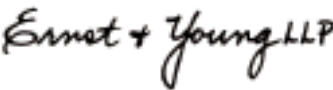
To the Board of Directors and Stockholders of
Hewitt Associates, Inc.:

We have audited the accompanying consolidated balance sheets of Hewitt Associates, Inc. (a Delaware corporation) and subsidiaries and its predecessor (the “Company”) as of September 30, 2004 and 2003, and the related consolidated and combined statements of operations, stockholders’ equity and cash flows for each of the three years ended September 30, 2004. These consolidated and combined financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated and combined financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit

also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated and combined financial statements referred to above present fairly, in all material respects, the financial position of the Company as of September 30, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 2004, in conformity with U.S. generally accepted accounting principles.



Ernst & Young LLP

Chicago, Illinois
October 27, 2004

Consolidated Balance Sheets

Hewitt Associates, Inc.

Dollars in thousands except share and per share amounts	September 30,	
	2004	September 30, 2003
Assets		
Current Assets:		
Cash and cash equivalents	\$ 129,481	\$ 67,785
Short-term investments	183,205	159,720
Client receivables and unbilled work in process, less allowances of \$21,732 and \$15,011 at September 30, 2004 and 2003, respectively	522,882	461,430
Prepaid expenses and other current assets	65,239	46,496
Deferred income taxes, net	246	8,948
Total current assets	901,053	744,379
Non-Current Assets:		
Deferred contract costs	162,602	138,475
Property and equipment, net	236,480	237,476
Capitalized software, net	84,969	95,054
Other intangible assets, net	107,322	107,540
Goodwill, net	285,743	259,294
Other assets, net	29,805	21,937
Total non-current assets	906,921	859,776
Total Assets	\$1,807,974	\$1,604,155
Liabilities		
Current Liabilities:		
Accounts payable	\$ 20,909	\$ 14,508
Accrued expenses	105,470	103,520
Advanced billings to clients	106,934	107,247
Accrued compensation and benefits	181,812	147,821
Short-term debt and current portion of long-term debt	13,445	33,000
Current portion of capital lease obligations	5,373	6,602
Employee deferred compensation and accrued profit sharing	49,450	47,583
Total current liabilities	483,393	460,281
Long-Term Liabilities:		
Deferred contract revenues	118,025	118,167
Debt, less current portion	121,253	135,563
Capital lease obligations, less current portion	79,982	83,191
Other long-term liabilities	75,512	69,468
Deferred income taxes, net	70,456	47,424
Total long-term liabilities	465,228	453,813
Total Liabilities	\$ 948,621	\$ 914,094
Commitments and Contingencies (Notes 14 and 18)		
Stockholders' Equity		
Class A common stock, par value \$0.01 per share, 750,000,000 shares authorized, 32,480,669 and 30,463,187 shares issued and outstanding, as of September 30, 2004 and 2003, respectively	\$ 325	\$ 305
Class B common stock, par value \$0.01 per share, 200,000,000 shares authorized, 61,707,114 and 63,420,466 shares issued and outstanding, as of September 30, 2004 and 2003, respectively	617	634
Class C common stock, par value \$0.01 per share, 50,000,000 shares authorized, 4,391,862 and 4,603,915 shares issued and outstanding as of September 30, 2004 and 2003, respectively	44	46
Restricted stock units, 118,363 and 173,998 units issued and outstanding, as of September 30, 2004 and 2003, respectively	2,166	3,302
Additional paid-in capital	633,934	627,329
Cost of common stock in treasury, 526,518 and 270,294 shares of Class A common stock as of September 30, 2004 and 2003, respectively	(13,414)	(6,164)
Retained earnings	194,430	71,586
Unearned compensation	(27,799)	(45,534)
Accumulated other comprehensive income	69,050	38,557
Total stockholders' equity	859,353	690,061
Total Liabilities and Stockholders' Equity	\$1,807,974	\$1,604,155

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

Consolidated and Combined Statements of Operations⁽¹⁾

Hewitt Associates, Inc.

Dollars in thousands except share and per share amounts	Year Ended September 30,		
	2004	2003	2002 ⁽¹⁾
Revenues:			
Revenues before reimbursements (net revenues)	\$2,204,682	\$1,981,656	\$1,716,197
Reimbursements	57,545	49,637	33,882
Total revenues	2,262,227	2,031,293	1,750,079
Operating expenses:			
Compensation and related expenses, excluding initial public offering restricted stock awards	1,412,908	1,266,931	1,014,993
Initial public offering restricted stock awards	16,733	39,010	27,525
Reimbursable expenses	57,545	49,637	33,882
Other operating expenses	431,912	396,009	357,789
Selling, general and administrative expenses	120,296	101,725	75,570
Total operating expenses	2,039,394	1,853,312	1,509,759
Operating income	222,833	177,981	240,320
Other expenses, net:			
Interest expense	(18,608)	(20,014)	(16,098)
Interest income	3,316	2,638	2,291
Other income (expense), net	318	36	(3,087)
	(14,974)	(17,340)	(16,894)
Income before income taxes	207,859	160,641	223,426
Provision for income taxes	85,015	66,364	33,053
Net income	\$ 122,844	\$ 94,277	\$ 190,373
Earnings (loss) per share ⁽²⁾ :			
–Basic	\$ 1.28	\$ 0.99	\$ (0.27)
–Diluted	\$ 1.25	\$ 0.97	\$ (0.27)
Weighted average shares ⁽²⁾ :			
–Basic	96,031,389	94,783,223	85,301,042
–Diluted	97,950,088	96,832,723	85,301,042

⁽¹⁾In connection with the Company’s transition to a corporate structure on May 31, 2002, owners who worked in the business became employees and the Company began to record their compensation in compensation and related expenses and the Company became subject to corporate income taxes. As such, owner compensation expenses and corporate income taxes were recorded for all of fiscal 2004 and 2003, but only for four months of fiscal 2002. Additionally, on June 5, 2002, the Company acquired the benefits consulting business of Bacon & Woodrow and their results are included in the Company’s results from the acquisition date.

⁽²⁾Loss per share in fiscal 2002 is calculated based on the net loss incurred for the four month period from May 31, 2002, the date on which the Company’s transition to a corporate structure was completed, through September 30, 2002. Similarly, common stock is weighted from May 31, 2002 and not from the beginning of fiscal 2002.

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

Consolidated and Combined Statements of Stockholders’ Equity

Hewitt Associates, Inc.

Dollars in thousands except share and per share amounts	Preferred Shares	Class A Common Shares		Class B Common Shares		Class C Common Shares		Restricted Stock Units		Additional Paid-in Capital	Treasury Stock, at Cost		Retained Earnings (Deficit)	Unearned Compensation	Owners' Capital	Accumulated Other Comprehensive Income (Loss)	Total
		Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount		Shares	Amount					
Balance at September 30, 2001	\$—	—	\$ —	—	\$ —	—	\$ —	—	\$ —	\$ —	—	\$ —	\$ —	\$ —	\$ 260,138	\$ (767)	\$ 259,371
Comprehensive income:																	
Income before taxes and owner distributions for the eight months ended May 31, 2002	—	—	—	—	—	—	—	—	—	—	—	—	—	—	213,064	—	213,064
Net loss for the four months ended September 30, 2002	—	—	—	—	—	—	—	—	—	—	—	—	(22,691)	—	—	—	(22,691)
Other comprehensive income (loss):																	
Minimum pension liability adjustment	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	(690)	(690)
Foreign currency translation adjustments	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	17,648	17,648
Total other comprehensive income (loss)																16,958	
Total comprehensive income (loss)																	207,331
Capital distributions, net	—	—	—	—	—	—	—	—	—	—	—	—	—	—	(415,986)	—	(415,986)
Effect of the transition to corporate structure	—	—	—	70,819,520	708	—	—	—	—	56,508	—	—	—	—	(57,216)	—	—
Disproportionate share allocation adjustment	—	—	—	—	—	—	—	—	—	17,843	—	—	—	—	—	—	17,843
Acquisition of Bacon & Woodrow	—	941,753	9	2,906,904	29	5,568,869	56	—	—	219,146	—	—	—	—	—	—	219,240
Net proceeds from initial public offering	—	12,822,500	128	—	—	—	—	—	—	219,170	—	—	—	—	—	—	219,298
Initial public offering restricted stock grant	—	5,467,216	55	—	—	—	—	322,692	6,131	103,955	—	—	—	(110,141)	—	—	—
Amortization of unearned compensation	—	—	—	—	—	—	—	—	—	—	—	—	—	25,389	—	—	25,389
Issuance of Class A common shares—																	
outside directors	—	3,404	—	—	—	—	—	—	—	79	—	—	—	—	—	—	79
Net forfeiture of restricted common stock pursuant to the global stock plan and other	—	(72,213)	—	—	—	—	—	(2,790)	(53)	(1,324)	—	—	—	1,377	—	—	—
Balance at September 30, 2002	—	19,162,660	192	73,726,424	737	5,568,869	56	319,902	6,078	615,377	—	—	(22,691)	(83,375)	—	16,191	532,565
Comprehensive income (loss):																	
Net income	—	—	—	—	—	—	—	—	—	—	—	—	94,277	—	—	—	94,277
Other comprehensive income (loss):																	
Minimum pension liability adjustment	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	(333)	(333)
Foreign currency translation adjustments	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	22,699	22,699
Total other comprehensive income (loss)																22,366	
Total comprehensive income (loss)																	116,643
Payments for initial public offering costs	—	—	—	—	—	—	—	—	—	(796)	—	—	—	—	—	—	(796)
Amortization of unearned compensation	—	—	—	—	—	—	—	—	—	—	—	—	—	34,834	—	—	34,834
Tax benefits from stock plans	—	—	—	—	—	—	—	—	—	12,122	—	—	—	—	—	—	12,122
Restricted stock unit vesting	—	140,285	1	—	—	—	—	(140,285)	(2,669)	2,668	—	—	—	—	—	—	—
Shares exchanged in secondary offering	—	11,270,912	113	(10,305,958)	(103)	(964,954)	(10)	—	—	—	—	—	—	—	—	—	—
Purchase of Class A common shares for treasury	—	—	—	—	—	—	—	—	—	—	270,294	(6,164)	—	—	—	—	(6,164)
Issuance of Class A common shares:																	
Employee stock options	—	35,808	—	—	—	—	—	—	—	681	—	—	—	—	—	—	681
Outside Directors	—	6,661	—	—	—	—	—	—	—	175	—	—	—	—	—	—	175
Net forfeiture of restricted common stock pursuant to the global stock plan and other	—	(153,139)	(1)	—	—	—	—	(5,619)	(107)	(2,898)	—	—	—	3,007	—	—	1
Balance at September 30, 2003	—	30,463,187	305	63,420,466	634	4,603,915	46	173,998	3,302	627,329	270,294	(6,164)	71,586	(45,534)	—	38,557	690,061
Comprehensive income (loss):																	
Net income	—	—	—	—	—	—	—	—	—	—	—	—	122,844	—	—	—	122,844
Other comprehensive income (loss):																	
Minimum pension liability adjustment	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	1,023	1,023
Foreign currency translation adjustments	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	29,470	29,470
Total other comprehensive income (loss)																30,493	
Total comprehensive income																	153,337
Amortization of unearned compensation	—	—	—	—	—	—	—	—	—	—	—	—	—	15,017	—	—	15,017
Tax benefits from stock plans	—	—	—	—	—	—	—	—	—	4,014	—	—	—	—	—	—	4,014
Restricted stock unit vesting	—	45,982	—	—	—	—	—	(45,393)	(862)	866	—	—	—	—	—	—	4
Purchase of Class A common shares for treasury	—	—	—	—	—	—	—	—	—	—	256,224	(7,250)	—	—	—	—	(7,250)
Issuance of Class A common shares:																	
Employee stock options	—	185,234	2	—	—	—	—	—	—	4,137	—	—	—	(249)	—	—	3,890
Outside Directors	—	9,440	—	—	—	—	—	4,706	10	410	—	—	—	(140)	—	—	280
Rule 144 share conversions and other share conversions	—	1,925,405	19	(1,713,352)	(17)	(212,053)	(2)	—	—	—	—	—	—	—	—	—	—
Net forfeiture of restricted common stock pursuant to the global stock plan and other	—	(148,579)	(1)	—	—	—	—	(14,948)	(284)	(2,822)	—	—	—	3,107	—	—	—
Balance at September 30, 2004	\$—	32,480,669	\$325	61,707,114	\$ 617	4,391,862	\$ 44	118,363	\$ 2,166	\$633,934	526,518	\$(13,414)	\$194,430	\$ (27,799)	\$ —	\$69,050	\$ 859,353

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

Consolidated and Combined Statements of Cash Flows

Hewitt Associates, Inc.

Dollars in thousands	Year Ended September 30,		
	2004	2003	2002
Cash flows from operating activities:			
Net income	\$ 122,844	\$ 94,277	\$ 190,373
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	75,412	76,703	70,575
Amortization	42,806	37,691	26,035
Net unrealized loss on securities	—	—	3,653
Initial public offering restricted stock awards	15,017	34,833	25,389
Owner compensation charge (Note 3)	—	—	17,843
Establishment of owner vacation liability (Note 3)	—	—	8,300
Director stock remuneration	280	175	79
Deferred income taxes	31,590	36,187	2,289
Changes in operating assets and liabilities:			
Client receivables and unbilled work in process	(61,890)	(52,537)	(129,565)
Prepaid expenses and other current assets	(12,620)	(6,696)	(4,139)
Due from related parties	—	3,468	(3,468)
Deferred contract costs	(24,427)	(13,184)	3,689
Accounts payable	6,001	(12,995)	(5,250)
Accrued compensation and benefits	31,524	38,466	59,253
Accrued expenses	7,827	18,849	(31,029)
Advanced billings to clients	(391)	32,811	13,315
Deferred contract revenues	(270)	(9,150)	(3,830)
Employee deferred compensation and accrued profit sharing	1,724	(9,320)	4,200
Other long-term liabilities	5,662	8,976	3,509
Net cash provided by operating activities	241,089	278,554	251,221
Cash flows from investing activities:			
Purchases of short-term investments	(469,330)	(258,975)	(62,690)
Sales of short-term investments	445,845	156,945	5,000
Additions to property and equipment	(69,669)	(43,415)	(58,765)
Cash paid for acquisitions and transaction costs, net of cash acquired	(11,450)	(65,152)	(887)
Increase in other assets	(31,183)	(29,501)	(36,062)
Net cash used in investing activities	(135,787)	(240,098)	(153,404)
Cash flows from financing activities:			
Proceeds from issuance of stock in initial public offering	—	—	226,564
Proceeds from the exercise of stock options	3,890	681	—
Capital distributions to former owners, net	—	—	(263,565)
Short-term borrowings	18,064	7,669	59,661
Repayments of short-term borrowings	(38,639)	(32,624)	(73,765)
Repayments of long-term debt	(13,000)	(9,236)	(6,250)
Repayments of capital lease obligations	(7,684)	(11,171)	(17,007)
Payment of deferred financing fees	—	—	(1,437)
Purchase of Class A common shares for treasury	(7,250)	(6,164)	—
Payment of offering costs	—	(796)	(5,929)
Net cash used in financing activities	(44,619)	(51,641)	(81,728)
Effect of exchange rate changes on cash and cash equivalents	1,013	2,210	2,065
Net increase in cash and cash equivalents	61,696	(10,975)	18,154
Cash and cash equivalents, beginning of period	67,785	78,760	60,606
Cash and cash equivalents, end of period	\$ 129,481	\$ 67,785	\$ 78,760

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

Consolidated and Combined Statements of Cash Flows

Hewitt Associates, Inc.

(continued)

Dollars in thousands	Year Ended September 30,		
	2004	2003	2002
Change in client receivables and unbilled work in process:			
Beginning of year client receivables and unbilled work in process	\$ 461,430	\$ 392,267	\$ 366,493
Beginning of year long-term unbilled work in process	7,143	1,917	—
Non-cash distribution of client receivables to Hewitt Holdings	—	—	(152,500)
Fair value of acquired client receivables and unbilled work in process	2,736	12,481	46,188
Effect of exchange rates on client receivables and unbilled work in process	7,686	9,371	4,438
End of year long-term unbilled work in process	(18,003)	(7,143)	(1,917)
End of year client receivables and unbilled work in process	(522,882)	(461,430)	(392,267)
Change in client receivables and unbilled work in process	\$ (61,890)	\$ (52,537)	\$ (129,565)
Schedule of non-cash investing and financing activities:			
Acquisition, cash paid, net of cash acquired:			
Common stock issued in connection with acquisition	\$ —	\$ —	\$ 219,240
Prepaid transaction costs	(3,708)	—	—
Fair value of assets acquired	(3,530)	(72,932)	(142,406)
Fair value of liabilities assumed	2,966	52,126	100,403
Goodwill	(7,178)	(44,346)	(178,124)
Cash paid, net of cash acquired	(11,450)	(65,152)	(887)
Real estate and equipment purchased under capital leases	2,917	—	88,944
Software licenses purchased under long-term agreements	7,444	8,146	18,148
Client receivables distributed to Hewitt Holdings	—	—	152,500
Conversion of owner capital to common stock	—	—	57,216
Offering costs accrued but not yet paid	—	—	1,347
Supplementary disclosure of cash paid during the year:			
Interest paid	\$ 18,398	\$ 18,390	\$ 16,210
Income taxes paid	56,847	8,486	33,647

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

Notes to the Consolidated and Combined Financial Statements

For the Fiscal Years Ended September 30, 2004, 2003, and 2002

Dollars in thousands except share and per share amounts

Hewitt Associates, Inc.

1. Description of Business

Hewitt Associates, Inc., a Delaware corporation, and its subsidiaries (“Hewitt” or the “Company”) provide global human resources outsourcing and consulting services. The Company’s outsourcing business is composed of employee benefit plan, payroll, and workforce management administration services. Hewitt’s consulting business is composed of advisory services in health management, retirement and financial management, talent and organization consulting, and other consulting.

2. Summary of Significant Accounting Policies

The consolidated and combined financial statements are prepared on the accrual basis of accounting. The significant accounting policies are summarized below:

Principles of Consolidation and Combination

The accompanying consolidated and combined financial statements reflect the operations of the Company and its majority owned subsidiaries after elimination of intercompany accounts and transactions. Combined financial statements are presented for periods prior to the transition to a corporate structure when the combined entities that now make up the Company were under common control. Upon consummation of the transition to a corporate structure, the affiliated companies of Hewitt were transferred into the newly formed corporation, Hewitt Associates, Inc., and their results are presented on a consolidated basis.

Revenue Recognition

Revenues include fees generated from outsourcing contracts and from consulting services provided to the Company’s clients. Revenues from sales or licensing of software are not material. Under the Company’s outsourcing contracts, which typically have a three- to five-year term, clients generally pay an implementation fee and an ongoing service fee. The Company recognizes revenues for non-refundable, upfront implementation fees evenly over the period between the initiation of ongoing services through the end of the contract term (on a straight-line basis). Indirect costs of implementation are expensed as incurred. However, incremental direct costs of implementation are deferred and recognized as expense over the same period that deferred implementation fees are recognized. If a client terminates an outsourcing contract prematurely, both the deferred implementation revenues and related costs are recognized through the period in which the termination occurs.

Revenues related to ongoing service fees and to services provided outside the scope of outsourcing contracts are recognized when persuasive evidence of an arrangement exists, services have been rendered, our fee is determinable and collectibility of our fee is reasonably assured. Ongoing service fees are typically billed and recognized on a monthly basis, typically based on the number of plan participants or services and often with a minimum monthly fee. Ongoing service fees from fixed price contracts are recognized on a straight-line basis. Services provided outside the scope of our outsourcing contracts are billed and recognized on a time-and-material or fixed-fee basis.

The Company’s clients typically pay for consulting services either on a time-and-materials or fixed-fee basis. Revenues are recognized under time-and-material-based arrangements monthly as services are provided. On fixed-fee engagements, revenues are recognized either as services are provided using the proportional performance method or at the completion of a project based on facts and circumstances of the client arrangement.

Losses on outsourcing or consulting arrangements are recognized during the period in which a loss becomes probable and the amount of the loss is reasonably estimable. Contract or project losses are determined to be the amount by which the estimated direct and a portion of indirect costs exceed the estimated total revenues that will be generated by the arrangement. Estimates are monitored during the term of the arrangement and any changes to estimates are recorded in the current period and can result in either increases or decreases to income.

The Company has contracts for multiple services primarily in the Outsourcing segment. In these contracts, standalone deliverables include core services, such as Defined Benefit, Health & Welfare, or Defined Contribution Benefit Plan Administration, and standalone ancillary services, such as Your Total Rewards, which are tracked and valued separately. The upfront, non-refundable implementation fees on outsourcing standalone deliverables are also deferred and recognized over the life of the contract, so that revenues for both implementation services and ongoing services are generally recorded over the same period (e.g., life of the contract). Consulting services provided in connection with outsourcing engagements are accounted for at the time services are provided and are valued based on prevailing market rates.

Revenues earned in excess of billings are recorded as unbilled work in process. Billings in excess of revenues earned are recorded as advanced billings to clients, a deferred revenue liability, until services are rendered.

The Company considers the criteria established by Emerging Issues Task Force (“EITF”) Issue No. 99-19, *Reporting Revenue Gross as a Principal versus Net as an Agent*, in determining whether revenue should be recognized on a gross versus a net basis. In consideration of these criteria, the Company recognizes revenue primarily on a gross basis. Factors considered in determining if gross or net recognition is appropriate include whether the Company is primarily responsible to the client for the services, changes the delivered product, performs part of the service delivered, has discretion on vendor selection, or bears credit risk. In accordance with EITF Issue No. 01-14, *Income Statement Characterization of Reimbursements Received for “Out-of-Pocket” Expenses Incurred*, reimbursements received for out-of-pocket expenses incurred are characterized as revenues and are shown as a separate component of total revenues. Similarly, related reimbursable expenses are also shown separately within operating expenses.

Deferred Contract Costs and Deferred Contract Revenues

For new outsourcing services, upfront implementation efforts are required to set up a client and their human resource or benefit programs on the Company’s systems. The direct implementation

or “set up” costs and any upfront set up fees are deferred and recognized into earnings over the life of the outsourcing agreement. Specific, incremental and direct costs of implementation are deferred and recognized as primarily compensation and related expenses evenly over the period from the initiation of ongoing services through the end of the contract term. Implementation fees may be received either upfront or over the ongoing services period in the fee per participant. By deferring the upfront set up fees over the ongoing services period, all set up revenues are recognized evenly over the contract term along with the corresponding deferred contract costs. Additionally, at September 30, 2004 and 2003, a small portion of the deferred contract revenues includes deferred revenue on payroll software maintenance agreements.

Funds Held for Clients

A small portion of the Company’s outsourcing agreements require the Company to hold client funds. As of September 30, 2004 and 2003, \$14,693 and \$8,292, respectively, were included within prepaid expenses and other current assets and accrued expenses related to the client fund obligations.

Client Receivables and Unbilled Work in Process

The Company periodically evaluates the collectibility of its client receivables and unbilled work in process based on a combination of factors. In circumstances where the Company becomes aware of a specific client’s difficulty in meeting its financial obligations (e.g., bankruptcy filings, failure to pay amounts due to the Company or to others), the Company records an allowance for doubtful accounts to reduce the client receivable to what the Company reasonably believes will be collected. For all other clients, the Company recognizes an allowance for doubtful accounts based on past write-off history and the length of time the receivables are past due. Facts and circumstances may change that would require the Company to alter its estimates of the collectibility of client receivables and unbilled work in process.

Performance-Based Compensation

The Company’s compensation program includes a performance-based component that is determined by management. Performance-based compensation is discretionary and is based on individual, team, and total Company performance. Performance-based compensation is paid once per fiscal year after the Company’s annual operating results are finalized. The amount of expense for performance-based compensation recognized at interim and annual reporting dates involves judgment, is based on our quarterly and annual results as compared to our internal targets, and takes into account other factors, including industry trends and the general economic environment. Annual performance-based compensation levels may vary from current expectations as a result of changes in the actual performance of the Company, team or individual. As such, accrued amounts are subject to change in future periods if actual future performance varies from performance levels anticipated in prior interim periods.

Income Before Income Taxes

Prior to May 31, 2002, the Company operated as a group of affiliated limited liability companies and recorded income before income taxes and owner distributions in accordance with accounting principles generally accepted in the United States of America. Income before income taxes prior to May 31, 2002 is not comparable to fiscal 2003 and 2004 income before income taxes because compensation and related expenses for services rendered by owners have not been reflected as expenses but were reflected as capital distributions to owners. As such, results prior to May 31, 2002, do not reflect the financial position, results of operations, and changes in cash flows that would have been reported had the Company operated as a corporation for all the periods presented.

Income Taxes

On May 31, 2002, the Company became subject to federal and state income taxes and began to apply the asset and liability method described in Statement of Financial Accounting Standards (“SFAS”) No. 109, *Accounting for Income Taxes*. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Prior to May 31, 2002, the Company was not subject to corporate income taxes because it operated as a limited liability company. As a limited liability company, taxes on income earned prior to May 31, 2002 were the responsibility of the former owners of the Company.

Foreign Currency Translation

The Company’s foreign operations use local currency as their functional currency. Accordingly, assets and liabilities of foreign subsidiaries are translated into U.S. dollars at exchange rates in effect at year-end, while revenues and expenses are translated at average exchange rates prevailing during the year. Translation adjustments are reported as a component of accumulated other comprehensive income (loss) in stockholders’ equity. Gains or losses resulting from foreign exchange transactions, which have not been significant, are recorded in earnings within other income (expense), net.

Earnings Per Share

On May 31, 2002, the Company completed its transition to a corporate structure and began to report earnings per share in accordance with SFAS No. 128, *Earnings Per Share*. Under the treasury stock method, unvested restricted stock awards and unexercised stock options with fair market values of the underlying stock greater than the stock options’ exercise prices are considered common stock equivalents for the purposes of calculating diluted earnings per share for periods when there

are positive earnings and the incremental effect would be dilutive. Prior to May 31, 2002, Hewitt was composed of limited liability companies and did not have outstanding common stock from which to calculate earnings per share, nor did the Company’s earnings include owner compensation or income taxes. As such, the Company’s net income prior to May 31, 2002, is not comparable to net income of a corporation or the Company’s net income after May 31, 2002. For the year ended September 30, 2002, earnings per share was calculated based on the net loss incurred in the four-month period from May 31, 2002 through September 30, 2002.

Use of Estimates

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated and combined financial statements and accompanying notes. Estimates are used for, but not limited to, the accounting for contract and project loss reserves, performance-based compensation, the allowance for doubtful accounts, depreciation and amortization, asset impairment, taxes, and any contingencies. Although these estimates are based on management’s best knowledge of current events and actions that the Company may undertake in the future, actual results may be different from the estimates.

Concentrations of Credit Risk

The Company’s financial instruments that are exposed to concentrations of credit risk consist of cash equivalents, client receivables, and unbilled work in process. Hewitt invests its cash equivalents in the highest rated money market and similar investments and continuously monitors the investment ratings. Concentrations of credit risk with respect to unbilled revenues and receivables are limited as no client makes up a significant portion of the Company’s billings. Credit risk itself is limited due to the Company’s large number of Fortune 500 clients, its clients’ strong credit histories, and their dispersion across many different industries and geographic regions. For each of the years ended September 30, 2004, 2003, and 2002, no single client represented ten percent or more of the Company’s total revenues.

Fair Value of Financial Instruments

Cash and cash equivalents, marketable securities, client receivables, and foreign exchange instruments are financial assets with carrying values that approximate fair value. Accounts payable, accrued compensation and benefits, accrued expenses and liabilities, and the Company’s variable rate debt are financial liabilities with carrying values that approximate fair value. The fair value of the Company’s \$134,000 fixed rate senior term notes is estimated to be approximately \$147,000 at September 30, 2004 and was calculated by discounting the future cash flows of the senior term notes at rates currently offered to the Company for similar debt instruments with comparable maturities.

Cash and Cash Equivalents

The Company defines cash and cash equivalents as cash and investments with original maturities of 90 days or less. At September 30, 2004 and 2003, cash and cash equivalents included cash in checking and money market accounts as well as corporate tax-advantaged money market investments maturing in 90 days or less.

Marketable Securities

Marketable securities represent available-for-sale securities and are classified on the balance sheet within short-term investments at their fair market value. Unrealized gains or losses are reported as a component of accumulated other comprehensive income (loss). Realized gains or losses are reported in other expenses, net on the consolidated and combined statements of operations.

Property and Equipment

Property and equipment are recorded at cost. Depreciation and amortization include amounts recorded under capital leases and are computed using the straight-line method over the estimated useful lives of the assets, which are as follows:

Asset Description	Asset Life
Computer equipment	3 to 5 years
Telecommunications equipment	5 years
Furniture and equipment	5 to 15 years
Leasehold improvements	Lesser of estimated useful life or lease term
Buildings	Lesser of estimated useful life or lease term

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of long-lived assets held for use are assessed by a comparison of the carrying amount of the asset to the estimated future undiscounted net cash flows expected to be generated by the asset. If estimated future undiscounted net cash flows are less than the carrying amount of the asset, the asset is considered impaired and expense is recorded in an amount required to reduce the carrying amount of the asset to its fair value.

Software Development Costs

Software development costs for software developed for internal use are accounted for in accordance with the American Institute of Certified Public Accountants’ Statement of Position No. 98-1 (“SOP 98-1”), *Accounting for Costs of Computer Software Developed or Obtained for Internal Use*. SOP 98-1 requires the capitalization of certain costs incurred in connection with developing or obtaining internal use software. The Company amortizes the software costs over periods ranging from three to five years.

Costs associated with the planning and design phase of the development of software products, including coding and testing activities necessary to establish technological feasibility of computer software products to be sold, leased, or otherwise marketed, are expensed as incurred. Once technological feasibility

has been determined, costs incurred in the construction phase of software development, including coding, testing, and product quality assurance are capitalized. Capitalization ceases when the software products are available for release to customers.

Goodwill and Intangible Assets

Goodwill is not amortized but is reviewed for impairment annually or more frequently if indicators arise. The evaluation is based upon a comparison of the estimated fair value of the unit of the Company’s business to which the goodwill has been assigned, to the sum of the carrying value of the assets and liabilities of that unit. The fair values used in this evaluation are estimated based upon discounted future cash flow projections for the unit. These cash flow projections are based upon a number of estimates and assumptions. Intangible assets with definite lives are amortized over their estimated useful lives and are reviewed for impairment if indicators of impairment arise.

Amortization of the Company’s definite lived intangible assets are computed using the straight-line method over the estimated useful lives of the assets, which are as follows:

Asset Description	Asset Life
Capitalized software	3 to 5 years
Trademarks	3 to 5 years
Customer relationships	12 to 30 years

Stock-Based Compensation

The Company accounts for its stock-based compensation plans under SFAS No. 123, *Accounting for Stock-Based Compensation*, as amended by SFAS No. 148, *Accounting for Stock-Based Compensation-Transition and Disclosure*, which allows companies to apply the provisions of Accounting Principles Board (“APB”) Opinion No. 25, *Accounting for Stock Issued to Employees*, and provide pro forma net income and net income per share disclosures for employee stock option grants as if the fair value method defined in SFAS No. 123 had been applied. The Company applies the intrinsic value method for accounting for stock-based compensation as outlined in APB Opinion No. 25.

Restricted stock awards, including restricted stock and restricted stock units, are measured using the fair market value of the stock as of the grant date and are initially recorded as unearned compensation on the balance sheet. As the restricted stock awards vest, the unearned compensation is amortized to compensation expense on a straight-line basis. Employer payroll taxes are also recorded as expense when they become due over the vesting period. The remaining unvested shares are subject to forfeiture and restrictions on sale or transfer for four years from the grant date.

The Company also grants nonqualified stock options at an exercise price equal to the fair market value of the Company’s stock on the grant date. Because the stock options have no intrinsic value on the grant date, no compensation expense is recorded in connection with the stock option grants. Generally, stock options vest 25% on each anniversary of the grant date, are fully vested four years from the grant date, and have a term of ten years.

For purposes of pro forma disclosures, applying the Black-Scholes valuation method, had the estimated fair value of the stock options been amortized to compensation expense over the stock options’ vesting period, the Company’s pro forma net income and earnings per share would have been as follows:

	Year Ended September 30,		
	2004	2003	2002
Net income:			
As reported	\$122,844	\$ 94,277	\$190,373
Less net income through May 31, 2002			213,064
Net loss from June 1, 2002 through September 30, 2002			(22,691)
Stock-based compensation expense included in reported net income, net of tax	9,872	23,016	16,240
Pro forma stock compensation expense, net of tax	(19,807)	(28,459)	(17,370)
Adjusted net income	\$112,909	\$ 88,834	\$ (23,821)

Net income (loss) per share—Basic:						
As reported	\$	1.28	\$	0.99	\$	(0.27)
Adjusted net income (loss) per share	\$	1.18	\$	0.94	\$	(0.28)
Net income (loss) per share—Diluted:						
As reported	\$	1.25	\$	0.97	\$	(0.27)
Adjusted net income (loss) per share	\$	1.15	\$	0.92	\$	(0.28)

The above pro forma information regarding net income and earnings per share has been determined as if the Company had accounted for its employee stock options under the fair value method. The fair value for these stock options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions:

	2004	2003	2002
Expected volatility	35%	35%	35%
Risk-free interest rate	3.36%-3.47%	2.87%-3.37%	3.81%-4.19%
Expected life	5	5	4
Dividend yield	0%	0%	0%

New Accounting Pronouncements

In January 2003, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation No. 46 (“FIN No. 46”), *Consolidation of Variable Interest Entities*, to expand upon existing accounting guidance that addresses when a company should

include in its financial statements the assets, liabilities, and activities of another entity. In December 2003, the FASB revised FIN No. 46 to provide more clarification. Until now, a company generally has included another entity in its consolidated financial statements only if it controlled the entity through voting interests. FIN No. 46 changes that by requiring a variable interest entity, as defined, to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity’s activities or entitled to receive a majority of the entity’s residual returns or both. FIN No. 46 and FIN No. 46 as revised, did not have a material impact on the Company’s consolidated financial statements.

In September 2004, the FASB’s Emerging Issues Task Force (“EITF”) reached a consensus on EITF Issue No. 04-08, *The Effect of Contingently Convertible Instruments on Diluted Earnings per Share*. The Task Force reached a conclusion that Contingently Convertible Instruments (“Co-Cos”) should be included in diluted earnings per share computations, if dilutive, regardless of whether the market price trigger or other contingent feature has been met. Through September 30, 2004, EITF Issue No. 04-08 had no effect on the Company. In October 2004, with the acquisition of Exult and \$110,000 of convertible senior notes, future earnings per share computations will include the convertible notes to the extent that they are determined to be dilutive. See Note 6 for additional information on the acquisition of Exult.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

3. Transition to a Corporate Structure

On May 31, 2002, the Company completed its transition to a corporate structure in connection with its planned initial public offering.

Prior to the transition to a corporate structure, the Company consisted of single-member limited liability companies, which were wholly owned by Hewitt Holdings. As such, owners’ capital represented the ownership interests of Hewitt Holdings in the Company. Historically, distributions to and contributions from Hewitt Holdings were based on the capital requirements of the Company and of Hewitt Holdings, and were subject to the discretion of the owners of Hewitt Holdings.

On March 1, 2002, Hewitt Associates, Inc., a Delaware corporation, was formed as a subsidiary of Hewitt Holdings. Three classes of common stock were authorized. The holders of Class A, Class B, and Class C common stock have one vote per share. All shares of Class B and Class C common stock are voted in accordance with a majority of the votes cast by the holders of Class B and Class C common stock as a group.

In May 2002, Hewitt Associates LLC distributed \$152,500 of accounts receivable and \$55,000 of cash to Hewitt Holdings to fund a distribution to the owners of accumulated earnings in preparation for Hewitt Associates LLC and Affiliates’ transition to a corporate structure. Cash collected on the receivables was first received by the Company and then remitted to Hewitt

Holdings and the Company did not bear any collection risk associated with these receivables.

On May 31, 2002, Hewitt Holdings transferred all of its ownership interests in Hewitt Associates LLC and Affiliates to Hewitt Associates, Inc., thereby making Hewitt Associates LLC and Affiliates a wholly-owned subsidiary of the Company. The capital in the business was converted and Hewitt Holdings received 70,819,520 shares of the Company’s Class B common stock.

In connection with the transition to a corporate structure, the Company incurred a non-recurring compensation expense resulting from certain owners receiving more than their proportional share of total capital, without offset for those owners who received less than their proportional share in the issuance of the Class B common stock. The amount of this one-time charge was \$17,843. As a result of owners becoming employees of the Company, the owners began to receive compensation and the Company incurred an additional non-recurring compensation expense resulting from the establishment of a vacation liability for these owners in the amount of \$8,300. The Company also became subject to income taxes subsequent to its transition to a corporate structure. As a result, the Company incurred a non-recurring income tax expense of \$21,711 to initially record deferred tax assets and liabilities under the provisions of SFAS No. 109.

On July 1, 2003, Hewitt Holdings distributed the shares of Class B common stock of Hewitt Associates to its owners, with the exception of certain owners resident outside the United States who will continue to hold their shares through Hewitt Holdings. The shares continue to be subject to the same restrictions with respect to voting, transfer and book to market phase-in as they were when the shares were held by Hewitt Holdings. The distribution reduced Hewitt Holdings’ majority interest in Hewitt Associates of approximately 71% at June 30, 2003, to a minority interest of approximately 2% at September 30, 2004 and 2003.

On April 29, 2004, Hewitt Holdings LLC changed its name to FORE Holdings LLC (“FORE Holdings”).

4. Initial Public Offering

On June 27, 2002, the Company sold 11,150,000 shares of Class A common stock at \$19.00 per share in its initial public offering. The Company’s gross proceeds from the offering were \$211,850, before the underwriting discount of \$14,829 and offering expenses of \$8,072.

In July 2002, the underwriters exercised their over-allotment option to purchase an additional 1,672,500 shares of the Company’s Class A common stock at \$19.00 per share. The option exercise generated gross proceeds of \$31,778 before the underwriting discount of \$2,225.

Of the \$218,502 in net proceeds received in July 2002, \$52,000 was used to repay the outstanding balance on the Company’s lines of credit, \$8,341 was used to pay income taxes resulting from the Company’s transition to a corporate structure, and the balance was retained for general corporate purposes and working capital.

In connection with the initial public offering, the Company granted to employees restricted stock, restricted stock units, and nonqualified stock options on common stock. (See Note 17, Stock-Based Compensation Plan, for additional information.)

5. Earnings Per Share

Basic earnings per share (“EPS”) is calculated by dividing net income by the weighted-average number of shares of common stock outstanding. Diluted EPS includes the components of basic EPS and also gives effect to dilutive common stock equivalents. For purposes of calculating basic and diluted earnings per share, vested restricted stock awards and exercised stock options are considered outstanding. For diluted EPS, a portion of unvested restricted stock awards and unexercised stock options that are “in-the-money” are also considered common stock equivalents. Restricted stock awards vest 25% on each anniversary of the grant date and are not considered outstanding in basic earnings per share until the vesting date.

For the year ended September 30, 2002, earnings per share was calculated based on the net loss incurred between May 31,

2002 and September 30, 2002, the four-month period during which the Company operated as a corporation. As such, the earnings per share for the year ended September 30, 2002 is not indicative of the amount that would have been computed had the Company been a corporation for the entire year presented. During the period between May 31, 2002 and September 30, 2002, the Company also incurred several one-time charges totaling \$47,854 (see Note 3) related to the Company’s transition to a corporate structure and \$27,525 of compensation expense related to the initial public offering restricted stock award which resulted in a net loss. As such, the effect of incremental shares of common stock equivalents has not been reflected as an adjustment to diluted earnings per share as the impact is antidilutive. Additionally, common stock has been weighted from the time of the Company’s transition to a corporate structure on May 31, 2002 and not from the beginning of fiscal 2002.

The following table presents computations of basic and diluted EPS in accordance with accounting principles generally accepted in the United States of America:

	Year Ended September 30,		
	2004	2003	2002
Net income as reported	\$122,844	\$94,277	\$190,373
Less net income through May 31, 2002			213,064
Net loss from June 1, 2002 through September 30, 2002			\$(22,691)
Weighted-average number of common stock for basic	96,031,389	94,783,223	85,301,042
Incremental effect of dilutive common stock equivalents:			
Unvested restricted stock awards	741,387	1,312,259	—
Unexercised in-the-money stock options	1,177,312	737,241	—
Weighted-average number of common stock for diluted	97,950,088	96,832,723	85,301,042
Earnings (loss) per share—Basic	\$ 1.28	\$ 0.99	\$ (0.27)
Earnings (loss) per share—Diluted	\$ 1.25	\$ 0.97	\$ (0.27)

Stock options to purchase 996,380 weighted-average shares in 2004, 51,782 weighted-average shares in 2003, and 56,223 weighted-average shares in 2002 of Class A common stock were outstanding, but were not included in the computation of diluted earnings per share because the exercise price of the options was greater than the average market price of the Class A common stock and, therefore, the effect would have been antidilutive.

6. Acquisitions

Exult Merger

Exult has been a leading provider of HR business process outsourcing. On June 15, 2004, we entered into an Agreement and Plan of Merger with Exult, Inc. and Eagle Merger Corp., a newly formed wholly owned subsidiary of Hewitt and on October 1, 2004, after obtaining regulatory and stockholder approvals, the merger was completed. Eagle Merger Corp. was merged with and into Exult, and Exult became the surviving corporation and a wholly owned subsidiary of Hewitt. Under the Agreement, each share of Exult common stock outstanding immediately

prior to the effective time of the merger was converted into 0.2 shares of Hewitt Class A common stock. As such, the Exult stockholders received 22,159,921 shares of Hewitt Class A stock in exchange for the 110,799,662 shares of outstanding Exult common stock. The purchase price is estimated to be approximately \$776 million, including assumed debt and acquisition related costs. On October 29, 2004, Exult was merged into Hewitt Associates, Inc. As part of the acquisition, the Company acquired \$110 million of 2.5% convertible senior notes, due on October 1, 2010. On October 6, 2004, the Company filed a Registration Statement on Form S-3 with the Securities and Exchange Commission to allow the holders to resell their notes and the 1,870,748 shares of Hewitt Class A common stock issuable upon conversion of their notes at the current conversion price. In connection with the merger, the Company granted 692,139 shares of Class A restricted stock and restricted stock units to certain Exult employees. These awards were valued at \$18,535 on the October 1, 2004 grant date (a price of \$26.78 per share) and vest ratably through June 27, 2006.

Benefits Administration and Actuarial Business of the Northern Trust Corporation

On June 15, 2003, the Company acquired substantially all of the assets of Northern Trust Retirement Consulting LLC, Northern Trust Corporation’s retirement consulting and administration business (“NTRC”), which provides retirement consulting and actuarial services and defined benefit, defined contribution and retiree health and welfare administration services. The benefit administration business will operate within the Company’s Outsourcing segment and the retirement consulting and actuarial business within the Consulting segment. The purchase price was composed of \$17,600 in cash for the assignment of client, vendor, and third-party contract rights and obligations applicable to the acquired business; computer equipment, furniture and leasehold improvements owned or leased by NTRC in its Atlanta, Georgia facility, and the assumption of NTRC’s real estate lease obligation for its Atlanta, Georgia facility. The allocation of the purchase price resulted in the allocation of \$7,821 to goodwill. The Company expects all of the goodwill to be deductible for U.S. tax purposes. As part of the acquisition agreement, the Company has agreed with the Northern Trust Corporation to, on a non-exclusive basis, recommend Northern Trust Corporation’s custody, trustee, and benefit payment services to the Company’s clients and prospective clients and Northern Trust Corporation has agreed to recommend the Company’s outsourcing services to their clients and prospective clients. NTRC’s results of operations are included within the Company’s historical results from the acquisition date of June 15, 2003. This acquisition is not considered to be material to the Company, and, therefore, pro forma information has not been presented.

Cyborg Worldwide, Inc.

On June 5, 2003, the Company purchased Cyborg Worldwide, Inc., the parent of Cyborg Systems, Inc. (“Cyborg”), a global provider of human resources management software and payroll services. Cyborg will operate within the Company’s Outsourcing segment. The purchase price totaled \$43,645, and was composed of \$43,000 of cash and \$645 of acquisition related costs, plus the potential for additional performance-based consideration of up to \$30,000 payable through 2006. On June 8, 2004, the Company entered an agreement with Cyborg’s selling stockholders to settle the performance-based consideration obligation for \$10,000. The allocation of the \$53,645 adjusted purchase price to acquired net assets resulted in the allocation of \$25,353 to goodwill and \$30,638 to identifiable intangible assets, which includes \$17,823 to customer relationships with an estimated twelve-year useful life, \$12,116 to capitalized software with an estimated five-year life and \$699 to trademarks with an estimated three-year useful life. The preliminary allocation also included allocations of \$9,138 to identifiable assets and \$11,484 to assumed liabilities. The Company expects all of the goodwill to be deductible for U.S. tax purposes. Cyborg’s results of operations are included within the Company’s historical results from the acquisition date of June 5, 2003. This

acquisition is not considered to be material to the Company, and, therefore, pro forma information has not been presented.

Bacon & Woodrow

On June 5, 2002, the Company acquired the actuarial and benefits consulting business of Bacon & Woodrow (“Bacon & Woodrow”) in the United Kingdom. The purchase price totaled \$259,009, and was composed of \$219,240 of common stock, \$38,882 in assumed net liabilities, and \$887 of acquisition related costs. Bacon & Woodrow’s results of operations are included within the Company’s historical results from the acquisition date of June 5, 2002.

Pursuant to the purchase agreement, the former partners and employees of Bacon & Woodrow initially received an aggregate of 1,400,000 shares of the Company’s Series A mandatorily redeemable preferred stock which was redeemable for shares of the Company’s common stock. Effective August 2, 2002, the Bacon & Woodrow former partners and employees elected to exchange their shares of Series A preferred stock for common stock. Of the 9,417,526 shares of common stock issued, the former partners of Bacon & Woodrow received 2,906,904 shares of Class B common stock and 5,568,869 shares of Class C common stock, and a trust for the benefit of the non-partner employees of Bacon & Woodrow received 941,753 shares of Class A common stock.

The allocation of the \$259,009 purchase price to acquired net assets resulted in the allocation of \$178,124 to goodwill, \$65,874 to identifiable intangible assets (primarily customer relationships) with indefinite lives, \$15,011 to identifiable intangible assets with estimated five-year lives, \$61,521 to identifiable assets (which includes \$40,445 of client receivables and unbilled work in process), and \$100,403 to assumed liabilities (which includes \$22,687 of accounts payable and accrued expenses and \$36,071 of short-term borrowings). The Company expects all of the goodwill to be deductible for U.S. tax purposes.

In the quarter ending September 30, 2003, the Company began amortizing the customer relationships intangible asset by taking a charge for the year then ending. The customer relationships intangible asset totaled £45,200, or \$65,874 as of the acquisition date. The Company is amortizing the intangible asset in two classes on a straight-line basis over 15 and 30 years. The allocation between the two classes was based primarily on customer revenue size. The useful life for each class was based primarily on historical customer turnover, the relative difficulty in the ability of customers to switch service providers and the nature and complexity of the customers. The Company estimates that it will record recurring non-cash, pre-tax amortization expense of approximately £408 (\$734 at a September 30, 2004 exchange rate) per quarter for the next 15 years and approximately £345 (\$621 at a September 30, 2004 exchange rate) per quarter thereafter through the end of the 30-year period.

Assuming the acquisition of Bacon & Woodrow occurred at the beginning of fiscal 2002, pro forma net revenues would have been approximately \$1,807,000 in 2002 and pro forma net income would have been approximately \$215,000 in 2002.

These pro forma results, which are unaudited, give effect to the Company’s incorporation and initial public offering on the dates such events actually occurred, on May 31, 2002 and June 27, 2002, respectively. Because the Company was a limited liability company for the first eight months of fiscal 2002, the pro forma effect of the acquisition on earnings per share is not meaningful. The pro forma results are not necessarily indicative of what would have occurred if the acquisition had been consummated at the beginning of 2002, nor are they necessarily indicative of future consolidated operating results.

Other Acquisitions

During 2004, the Company acquired a controlling interest in a joint venture investment in Puerto Rico and the remaining interest in a joint venture investment in India. The Company acquired these entities for cash at an aggregate cost of \$13,249. The preliminary allocations of the purchase price resulted in the aggregate allocation of \$3,569 to goodwill, of which \$2,572 was assigned to the Outsourcing segment, with the remainder of \$997 assigned to the Consulting segment. The Company expects all of the goodwill to be deductible for U.S. tax purposes. These acquisitions are not considered to be material to the Company, and, therefore, pro forma information has not been presented.

During 2003, the Company acquired the controlling interests in joint venture investments in the Netherlands, India, and Singapore, and an actuarial business in Ireland. The Company acquired these entities for cash at an aggregate cost of \$14,617. The allocations of the purchase price resulted in the aggregate allocation of \$17,183 to goodwill, of which \$5,427 was assigned to the Outsourcing segment, with the remainder of \$11,756 assigned to the Consulting segment. The Company expects approximately one-half of the goodwill to be deductible for U.S. tax purposes. These acquisitions are not considered to be material to the Company, and, therefore, pro forma information has not been presented.

7. Short-Term Investments

Short-term investments are composed of available-for-sale securities. Investments classified as available-for-sale securities consist of \$183,205 and \$159,720 of auction rate municipal bonds at September 30, 2004 and 2003, respectively. The Company’s investments in these securities are recorded at cost, which approximates fair market value due to their variable interest rates which typically reset every 28 to 35 days. As a result, at September 30, 2004 and 2003, the Company had no cumulative gross unrealized holding gains (losses) or gross realized gains (losses) from its available-for-sale securities. All income generated from the auction rate municipal bonds was recorded as interest income.

Estimated fair market value of debt securities classified as available-for-sale by contractual maturities consist of the following:

	2004
Amounts included in short-term investments:	
Due in less than one year	\$ 4,855
Due after one year through five years	—
Due after five years through ten years	9,500
Due after ten years	168,850
	\$183,205

8. Client Receivables and Unbilled Work in Process

Client receivables and unbilled work in process, net of allowances, at September 30, 2004 and 2003, consisted of the following:

	2004	2003
Client receivables	\$339,306	\$278,966
Unbilled work in process	183,576	182,464
	\$522,882	\$461,430

As of September 30, 2004 and 2003, \$18,003 and \$7,143, respectively, of long-term unbilled work in process is classified within other assets, net.

The activity in the client receivable and unbilled work in process allowances for the years ended September 30, 2004, 2003, and 2002, consisted of the following:

	2004	2003	2002
Balance at beginning of year	\$ 15,011	\$ 16,160	\$ 14,540
Increase in allowances	23,764	17,661	31,453
Use of allowances	(17,043)	(18,810)	(29,833)
Balance at end of year	\$ 21,732	\$ 15,011	\$ 16,160

9. Financial Instruments

The Company does not enter into derivative transactions except in limited situations when there is a compelling reason to mitigate economic risk. On August 6, 2001, Hewitt purchased a £150 million foreign currency option to offset the foreign currency risk associated with its planned purchase of the benefits consulting business of Bacon & Woodrow for common stock with a value of £140 million. (See Note 6, Acquisitions.) The cost of the foreign currency option was \$2,344, and it expired in May 2002. This instrument did not qualify for the hedge accounting treatment under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, because SFAS No. 133 prohibits hedge accounting for a forecasted business combination. The instrument was marked to the spot rate and resulting gains or losses were recognized currently in other expenses, net. For the year ended September 30, 2002 the loss on the option was \$3,653. The Company had no derivative instruments outstanding at September 30, 2004 and 2003.

10. Property and Equipment

As of September 30, 2004 and 2003, net property and equipment, which includes assets under capital leases, consisted of the following:

	2004	2003
Property and equipment:		
Buildings	\$ 92,057	\$ 90,328
Computer equipment	284,778	255,723
Telecommunications equipment	116,027	110,569
Furniture and equipment	101,493	92,145
Leasehold improvements	92,089	81,912
Total property and equipment	686,444	630,677
Less accumulated depreciation and amortization	(449,964)	(393,201)
Balance at end of year	\$ 236,480	\$ 237,476

11. Goodwill and Other Intangible Assets

The Company adopted SFAS No. 142, *Goodwill and Other Intangible Assets*, on October 1, 2002, which requires that goodwill no longer be amortized but tested for impairment at least annually.

The Company tests goodwill for impairment annually or whenever indicators of impairment arise. During the years ended September 30, 2004, 2003, and 2002, no impairments were recognized.

The following is a summary of net income for the year ended September 30, 2002, adjusted to remove the amortization of goodwill:

	2002
Net income:	
As reported	\$190,373
Goodwill amortization, net of tax	730
As adjusted	\$191,103

The following is a summary of changes in the carrying amount of goodwill for the years ended September 30, 2004 and 2003:

	Outsourcing Segment	Consulting Segment	Total
Balance at September 30, 2002	\$ —	\$201,286	\$201,286
Additions and other adjustments	26,741	17,605	44,346
Effect of changes in foreign exchange rates	—	13,662	13,662
Balance at September 30, 2003	26,741	232,553	259,294
Additions and other adjustments	13,669	(6,495)	7,174
Effect of changes in foreign exchange rates	245	19,030	19,275
Balance at September 30, 2004	\$40,655	\$245,088	\$285,743

Goodwill additions during the year ended September 30, 2004 resulted from the settlement of the Cyborg performance-based consideration obligation and from the acquisitions of the remaining interest in two of the Company’s joint ventures, one in Puerto Rico and one in India. Goodwill adjustments during the year ended September 30, 2004 resulted from purchase price allocation adjustments related to the NTRC acquisition, an acquisition in the Netherlands and Switzerland. Goodwill, customer relationships, and trademark additions during the year ended September 30, 2003, resulted from acquisitions (see Note 6, Acquisitions) and goodwill also increased from an adjustment to the purchase price allocation related to an acquisition in Switzerland.

Intangible assets with definite useful lives are amortized over their estimated useful lives and are tested for impairment whenever indicators of impairment arise. The following is a summary of intangible assets at September 30, 2004 and 2003:

	2004			2003		
Definite useful life	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Capitalized software	\$242,128	\$157,159	\$ 84,969	\$219,220	\$124,166	\$ 95,054
Trademarks	12,478	5,821	6,657	11,517	2,962	8,555
Customer relationships	109,422	8,757	100,665	102,392	3,407	98,985
Total	\$364,028	\$171,737	\$192,291	\$333,129	\$130,535	\$202,594

The increase in the gross carrying amounts of trademarks and customer relationships is primarily the result of the impact of foreign currency exchange rates.

Amortization expense related to definite-lived intangible assets for the years ended September 30, 2004, 2003, and 2002, are as follows:

	2004	2003	2002
Capitalized software	\$35,063	\$32,234	\$24,679
Trademarks	2,617	2,210	509
Customer relationships	5,126	3,247	—
Total	\$42,806	\$37,691	\$25,188

Applying current foreign exchange rates, estimated amortization expense related to intangible assets with definite lives at September 30, 2004, for each of the years in the five-year period ending September 30, 2009 and thereafter is as follows:

	Estimated Intangibles Amortization Expense
Fiscal year ending:	
2005	\$ 38,795
2006	32,669
2007	24,305
2008	13,232
2009	8,335
2010 and thereafter	74,955
Total	\$192,291

12. Other Assets

As of September 30, 2004 and 2003, other assets consisted of the following:

	2004	2003
Other assets:		
Long-term unbilled work in process	\$18,003	\$ 7,143
Prepaid long-term interest and service contracts	9,798	11,667
Investments in affiliated companies	2,004	3,127
Other assets	\$29,805	\$21,937

The Company has several prepaid long-term contracts for maintenance on computer software systems. Benefits related to these long-term prepaid maintenance contracts are received over the contractual period, as designated. The long-term portion of the prepaid interest relates to prepaid lease obligations of the Company.

Investments in less than 50%-owned affiliated companies over which the Company has the ability to exercise significant influence are accounted for using the equity method of accounting. During 2004 and 2003, the Company acquired the controlling interests in joint venture investments in Puerto Rico, the Netherlands, India, and Singapore. See Note 6, Acquisitions, for additional information.

13. Debt

Debt at September 30, 2004 and 2003, consisted of the following:

	2004	2003
Unsecured lines of credit	\$ —	\$ 15,852
Other foreign debt	698	5,711
Unsecured senior term notes	134,000	147,000
	134,698	168,563
Current portion	13,445	33,000
Long-term debt, less current portion	\$121,253	\$135,563

The principal portion of long-term debt becomes due as follows:

Fiscal year ending:	
2005	\$ 13,445
2006	23,136
2007	28,036
2008	17,030
2009	7,051
2010 and thereafter	46,000
Total	\$134,698

On September 27, 2002, the Company obtained two unsecured line of credit facilities. The 364-day facility provided for borrowings up to \$70 million and expired on September 26, 2003. The three-year facility provided for borrowings up to \$50 million. On September 29, 2003, the three-year facility was amended to provide for borrowings up to \$75 million. Borrowings under the facility accrue interest at LIBOR plus 52.5 to 72.5 basis points or the prime rate, at the Company’s option. Borrowings are repayable upon demand or at expiration of the facility on September 27, 2005. Quarterly facility fees ranging from 10 to 15 basis points are charged on the average daily commitment under the facility. If the utilization under the facility exceeds 50% of the commitment, an additional utilization fee based on the utilization is assessed at a rate of 0.125% per annum. At September 30, 2004 and 2003, there was no outstanding balance on the remaining facility.

On March 7, 2003, Hewitt entered into a contract with a lender to guarantee borrowings of its subsidiaries up to \$13 million in multiple currency loans and letters of credit to replace its unsecured multi-currency line of credit, which the Company repaid in February 2003. On August 1, 2003, the contract was amended to increase the guarantee amount to \$20 million. There is no fixed termination date on this contract. This contract allows Hewitt subsidiaries to secure financing at rates based on Hewitt’s creditworthiness. The contract was signed August 31, 2004, and \$1.4 million of the facility is used by Hewitt’s India office to support local letters of credit and bank guarantees. The facility provides for borrowings at LIBOR plus 75 basis points. As of September 30, 2004 and 2003, there were no borrowings under this contract.

On October 16, 2000, the Company issued unsecured senior term notes to various note holders in the amount of \$25,000. Of this amount, \$10,000 bears interest at 7.65%, and is repayable on October 15, 2005; \$15,000 bears interest at 7.90%, and is repayable on October 15, 2010.

On July 7, 2000, the Company issued unsecured senior term notes to various note holders in the amount of \$25,000. Of this amount, \$15,000 bears interest at 7.93%, and is repayable on June 30, 2007; \$10,000 bears interest at 8.11%, and is repayable on June 30, 2010.

On March 30, 2000, the Company issued \$50,000 of unsecured senior term notes to various note holders. Of this amount, \$15,000 bears interest at 7.94% and is repayable in annual installments beginning March 2003 through March 2007. The Company began paying annual installments of \$3,000 in March 2003. At September 30, 2004 and 2003, the outstanding balance was \$9,000 and \$12,000, respectively. The remaining \$35,000 bears interest at 8.08% and is repayable in annual installments beginning March 2008 through March 2012.

On February 23, 1998, the Company obtained an unsecured multi-currency line of credit with banks permitting borrowings up to \$10,000 at a multi-currency interbank interest rate plus 75 basis points. All outstanding balances on the unsecured multi-currency line of credit were repaid in full at the expiration of the facility on February 28, 2003. In addition, Hewitt Bacon & Woodrow Ltd., the Company’s U.K. subsidiary, had an unsecured British pound sterling line of credit permitting borrowings of up to £20 million until July 30, 2003, and £17 million thereafter until expiration of the facility on July 1, 2004. In July 2004, the line of credit was amended and extended to allow for borrowings up to £5,000 until the expiration of the facility on July 31, 2005. As of September 30, 2004, there was no outstanding balance on the line of credit and the current interest rate was 5.775%. At September 30, 2003, the outstanding balance was £9,500, equivalent to \$15,852, with interest at a rate of 4.53%. Other foreign debt outstanding at September 30, 2004 and 2003 totaled \$698 and \$5,711, respectively, pursuant to local banking relationships.

On May 30, 1996, the Company issued unsecured senior term notes to various note holders in the amount of \$50,000, bearing interest at 7.45%. The notes are repayable in annual installments beginning May 2004 through May 2008. The Company began paying installments of \$10,000 in May 2004. At September 30, 2004 and 2003, the outstanding balances were \$40,000 and \$50,000, respectively.

On May 28, 1996, the Company obtained an unsecured seven-year term loan agreement with various banks in the amount of \$30,000, bearing interest at 6.50%. The Company paid interest on a quarterly basis through June 30, 2002. On July 31, 1998, the Company also began to make monthly principal payments which continued through June 30, 2002, at which time, the Company paid the remaining principal balance.

Various debt agreements call for the maintenance of specified financial ratios, among other restrictions. At September 30, 2004 and 2003, the Company was in compliance with all debt covenants.

14. Lease Agreements

The Company has obligations under long-term non-cancelable lease agreements, principally for office space, furniture, and equipment, with terms ranging from one to twenty years. Some of the leases are with related parties (see Note 15, Related Party Transactions).

Capital Leases

Capital lease obligations at September 30, 2004 and 2003, consisted of the following:

	2004	2003
Building capital leases	\$83,023	\$85,813
Computer and telecommunications equipment	2,332	3,980
	85,355	89,793
Current portion	5,373	6,602
Capital lease obligations, less current portion	\$79,982	\$83,191

The Company’s two building capital leases are payable in monthly installments at 7.33% interest and expire in April 2017 and May 2017.

The Company’s computer and telecommunications equipment installment notes and capitalized leases are secured by the related equipment and are payable typically over three to five years in monthly or quarterly installments and at various interest rates ranging from 2.455% to 7.0%.

The following is a schedule of minimum future rental payments required as of September 30, 2004, under capital leases which have an initial or remaining non-cancelable lease term in excess of one year:

Capital Leases:	Principal	Interest	Total
Fiscal year ending:			
2005	\$ 5,373	\$ 6,015	\$ 11,388
2006	3,738	5,695	9,433
2007	4,118	5,416	9,534
2008	4,599	5,102	9,701
2009	5,144	4,750	9,894
2010 and thereafter	62,383	19,617	82,000
Total minimum lease payments	\$85,355	\$46,595	\$131,950

15. Related Party Transactions

The Company entered into real estate transactions as described below with FORE Holdings and its subsidiaries, Hewitt Properties I LLC, Hewitt Properties II LLC, Hewitt Properties III LLC, Hewitt Properties IV LLC, and Hewitt Properties VII LLC, The

Holdings Property Entities	Location	Commencement Date	Expiration Date
FORE Holdings LLC	Rowayton, Connecticut	October 1994	November 2001
Hewitt Properties I	Lincolnshire, Illinois	November 1998	November 2018
Hewitt Properties II	Lincolnshire, Illinois	December 1999	December 2019
Hewitt Properties III	Lincolnshire, Illinois	May 1999	May 2014
Hewitt Properties IV	Orlando, Florida	March 2000	March 2020
Hewitt Properties IV	The Woodlands, Texas	March 2000	March 2020
Hewitt Properties VII*	Norwalk, Connecticut	September 2001	September 2017
The Bayview Trust*	Newport Beach, California	June 2002	May 2017
Overlook Associates	Lincolnshire, Illinois	**	**

*FORE Holdings sold its interest in the Norwalk property in April 2002 and its interest in the Newport Beach property in March 2003, as such, these leases are no longer held by a related party, but remain capital leases of the Company.

**The Company has several leases with Overlook Associates, the first began in 1989 and the last expires in 2017.

Operating Leases

The Company also has various third-party operating leases for office space, furniture, and equipment with terms ranging from one to twenty years. The Company has various office leases that grant a free rent period and have escalating rents. The accompanying consolidated and combined statements of operations reflect rent expense on a straight-line basis recognized over the term of the leases. The difference between straight-line basis rent and the amount paid has been recorded as accrued lease obligations. The Company also has leases that have lease renewal provisions.

The following is a schedule of minimum future rental payments as of September 30, 2004, under operating leases with an initial or remaining non-cancelable lease terms in excess of one year:

Operating Leases:	Third Party	Related Party	Total
Fiscal year ending:			
2005	\$ 64,613	\$ 33,075	\$ 97,688
2006	98,889	33,339	132,228
2007	65,705	33,635	99,340
2008	31,037	33,845	64,882
2009	23,414	33,022	56,436
2010 and thereafter	136,344	270,763	407,107
Total minimum lease payments	\$420,002	\$437,679	\$857,681

Total rental expense for operating leases amounted to \$115,685 in 2004, \$104,094 in 2003, and \$104,228 in 2002.

Bayview Trust, and Overlook Associates (an equity method investment of FORE Holdings). The following related party leases were outstanding during the years ended September 30, 2004, 2003, and 2002:

Total lease payments were \$33,814 in 2004, \$34,105 in 2003, and \$40,053 in 2002. The leases were entered into on terms comparable to those which could have been obtained on an arm’s length basis. The historical cost of the real property owned by the Holdings property entities aggregates to \$360,125 and \$357,114 in 2004 and 2003, respectively. The investment in these properties was funded through capital contributions by FORE Holdings and third-party debt. Total outstanding debt owed to third parties by these related parties totaled \$261,047 and \$273,619 in 2004 and 2003, respectively. The debt is payable over periods that range up to sixteen years, and bears fixed interest rates that range from 5.58% to 7.93%. This debt is not reflected on the Company’s balance sheet as it is an obligation of FORE Holdings and its related parties, and is not an obligation of the Company. Substantially all of the activities of the FORE Holdings property entities involve assets that are leased to the Company. The Company does not guarantee the debt related to these properties.

In April 2002, Hewitt Properties VII sold the Norwalk, Connecticut property and the Company entered into a 15-year capital lease with the purchaser to lease the office space. The Company recorded a \$65,000 increase to both property and long-term debt to record this long-term lease obligation.

In June 2002, the Company entered into a 15-year capital lease with The Bayview Trust to lease office space in Newport Beach, California. The Company recorded a \$23,944 increase to both property and long-term debt to record this long-term lease obligation. On March 7, 2003, The Bayview Trust sold the property in Newport Beach, California, and the Company’s lease was assigned to the third-party purchaser of the building.

From May 31, 2002 through September 30, 2007, Hewitt Associates LLC, a subsidiary of the Company, is providing certain support services to FORE Holdings, primarily in the financial, real estate, and legal departments, as may be requested by FORE Holdings from time to time. FORE Holdings will pay Hewitt Associates LLC an annual fee of \$50 for basic services and an additional fee for additional services on a time-and-materials basis. Fees for services Hewitt Associates LLC provided under the services agreement, totaled \$117, \$425, and \$17 for the years ended September 30, 2004, 2003, and 2002, respectively. All such fees have been paid by FORE Holdings through September 30, 2004.

In fiscal 2002, the consolidated and combined statement of operations includes expenses that have been allocated to the Company on a specific identification basis by Hewitt Holdings at that time. Management believes these allocations and charges were reasonable and that such expenses would not have differed materially had the Company operated on a standalone basis.

16. Retirement Plans

Employee 401(k) and Profit Sharing Plan

The Company has a qualified 401(k) and profit sharing plan for its eligible employees. Under the plan, Hewitt makes annual contributions equal to a percentage of participants’ total cash compensation and may make additional contributions in accordance with the terms of the plan. Additionally, employees may make contributions in accordance with the terms of the plan, with a portion of those contributions matched by the Company. In 2004, 2003, and 2002, profit sharing plan expenses were \$58,035, \$53,980, and \$66,005, respectively.

Defined Benefit Plans

With the acquisition of the actuarial and benefits consulting business of Bacon & Woodrow, the Company acquired a defined benefit pension plan, which was closed to new entrants in 1998 and provides retirement benefits to eligible employees. The Company also has other smaller defined benefit pension plans to provide benefits to eligible employees. It is the Company’s policy to fund in accordance with local practice and legislation.

Healthcare Plans

The Company provides health benefits for retired employees and certain dependents when the employee becomes eligible for these benefits by satisfying plan provisions which include certain age and service requirements. The health benefit plans covering substantially all U.S. and Canadian employees are contributory, with contributions reviewed annually and adjusted as appropriate. These plans contain other cost-sharing features such as deductibles and coinsurance. The Company does not pre-fund these plans and has the right to modify or terminate any of these plans in the future.

The following tables provide a reconciliation of the changes in the defined benefit and healthcare plans’ benefit obligations and fair value of assets for the years ended September 30, 2004

and 2003, and a statement of funded status as of September 30, 2004 and 2003.

	Pension Benefits		Health Benefits	
	2004	2003	2004	2003
Change in Benefit Obligation				
Benefit obligation, beginning of year	\$ 128,633	\$ 63,413	\$ 11,627	\$ 8,553
Acquisitions	726	41,172	—	—
Service cost	8,264	5,784	1,138	803
Interest cost	7,160	4,107	692	597
Plan amendments	—	—	333	404
Actuarial (gains)/losses	(9,056)	9,318	292	1,463
Benefit payments	(3,745)	(1,336)	(598)	(193)
Changes in foreign exchange rates	9,146	6,175	—	—
Benefit obligation end of year	\$ 141,128	\$ 128,633	\$ 13,484	\$ 11,627

Change in Plan Assets

Fair value of plan assets, beginning of year	\$ 87,750	\$ 39,079	\$ —	\$ —
Acquisitions	436	38,118	—	—
Actual return on plan assets	5,049	2,269	—	—
Employer contribution	8,176	5,852	598	193
Benefit payments	(3,745)	(1,336)	(598)	(193)
Changes in foreign exchange rates	5,929	3,768	—	—
Fair value of plan assets, end of year	\$ 103,595	\$ 87,750	\$ —	\$ —

Reconciliation of Accrued Obligation and Total Amount Recognized

Unfunded status	\$ (37,533)	\$ (40,883)	\$ (13,484)	\$ (11,627)
Unrecognized net loss	14,708	21,889	3,875	3,699
Unrecognized prior service cost	—	—	2,953	2,798
Unrecognized transition obligation	—	—	459	492
Minimum pension liability	—	(1,023)	—	—
Net amount recognized, end of year	\$ (22,825)	\$ (20,017)	\$ (6,197)	\$ (4,638)

Amounts recognized in Balance Sheet are as follows:

Accrued benefit cost	\$ 22,825	\$ 19,684	\$ 6,197	\$ 4,638
Accumulated other comprehensive income	—	333	—	—
Net amount recognized	\$ 22,825	\$ 20,017	\$ 6,197	\$ 4,638

Accumulated Benefit Obligation	\$ 118,358	\$ 98,110
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The assumptions used in the measurement of our benefit obligations as of June 30, 2004 and 2003 are as follows:

	Pension Benefits		Health Benefits	
	2004	2003	2004	2003
Weighted-average assumptions:				
Discount rate	5.23%	4.85%	6.00%	6.00%
Expected return on plan assets	5.99%	5.51%	N/A	N/A
Rate of compensation increase	3.73%	3.40%	N/A	N/A

The health plan provides flat dollar credits based on years of service and age at retirement. There is a small group of grandfathered retirees who receive postretirement medical coverage at a percentage of cost. The liabilities for these retirees are

valued assuming an 11.0% health care cost trend rate for 2004. The rate was assumed to decrease gradually to 6.0% in 2014 and remain at that level thereafter.

The effect of a one percentage point increase or decrease in the assumed health care cost trend rates on total service and interest costs and the postretirement benefit obligation are provided in the following table.

	2004	2003
Effect of 1% Change in the Assumed Health Care Cost Trend Rates		
Effect of 1% increase on:		
– Total of service and interest cost components	\$ 4	\$ 4
– Benefit obligations	50	64
Effect of 1% decrease on:		
– Total of service and interest cost components	\$ (4)	\$ (4)
– Benefit obligation	(46)	(59)

The Company’s pension plan weighted-average asset allocations at September 30, 2004 and 2003, by asset category are as follows:

Asset Category	2004	2003
Equity securities	40.47%	37.86%
Debt securities	46.99	48.97
Real estate	4.70	5.61
Other	7.84	7.56
Total	100.00%	100.00%

The investment objectives for the pension plan assets are to generate returns that will enable the plans to meet their future

obligations. The strategies balance the requirement to generate returns through investments such as equity securities, with the need to control risk through less volatile assets such as fixed income securities, while also meeting local regulations. Approximately 90% of the Company’s plan assets relate to the Company’s pension plans in the United Kingdom and Switzerland. In the United Kingdom, the plan assets are managed in two separate portfolios, an equity portfolio and a bond portfolio. The strategy is to invest 56% and 44% of the plan assets in equity securities and debt securities, respectively. The total return is tracked to the relevant market index, within specified tolerances and after allowance for withholding tax where applicable, for each of the funds in which the assets are invested. The plan assets for the Switzerland plan are managed in accordance with the laws in Switzerland. Within the scope of the Swiss laws, the strategy targets equity securities of 35%-45%, debt securities of 35%-65%, real estate investments of 5%-15%, and other investments of 0%-5%.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Pension Benefits	Health Benefits
2005	\$ 2,798	\$ 366
2006	3,004	405
2007	3,084	474
2008	3,318	575
2009	3,291	653
Years 2010 through 2014	23,216	5,050

The components of net periodic benefit costs for the three years ended September 30, 2004 include:

	Pension Benefits			Health Benefits		
	2004	2003	2002	2004	2003	2002
Components of Net Periodic Benefit Cost						
Service cost	\$ 8,264	\$ 5,784	\$ 809	\$1,138	\$ 803	\$ 608
Interest cost	7,160	4,107	1,148	692	597	336
Expected return on plan assets	(5,613)	(3,411)	(1,041)	—	—	—
(Gain) loss recognized in the year	10	—	—	—	—	—
Amortization of:						
– Unrecognized prior service cost	—	—	—	179	160	—
– Unrecognized loss	360	—	—	115	66	68
– Transition obligation	—	—	—	33	33	33
Net periodic benefit cost	\$10,181	\$ 6,480	\$ 916	\$2,157	\$1,659	\$1,045

On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the “Act”) became effective. The Act introduces a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least the actuarial equivalent of Medicare Part D.

In accordance with the FASB Staff Position (“FSP”) 106-2 (“FSP 106-2”), *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of*

2003, the Company evaluated its plan and determined that the plan is not the actuarial equivalent of Medicare Part D. The financial statements and the notes to the financial statements do not include the effect of the Act on the accumulated postretirement benefit obligation or the net periodic postretirement benefit cost.

The Company presently anticipates contributing approximately \$10,000 to fund its pension plans and \$366 to fund its health benefit plans in fiscal 2005.

17. Stock-Based Compensation Plans

In 2002, the Company adopted the Hewitt Associates, Inc. Global Stock and Incentive Compensation Plan (the “Plan”) for employees and directors. The Plan is administered by the Compensation and Leadership Committee of the Board of Directors of the Company (the “Committee”). Under the Plan, employees and directors may receive awards of nonqualified stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units, and cash-based awards, and employees can also receive incentive stock options. As of September 30, 2004, only restricted stock, restricted stock units and nonqualified stock options have been granted. A total of 25,000,000 shares of Class A common stock have been reserved for issuance under the Plan. As of September 30, 2004, there were 8,679,897 shares available for grant under the Plan.

Restricted Stock and Restricted Stock Units

In connection with the initial public offering, the Company granted 5,789,908 shares of Class A restricted stock and restricted stock units to employees. The restricted stock and restricted stock units have substantially the same terms, except the holders of restricted stock units do not have voting rights. The one-time initial public offering-related awards were valued at \$110,141 on the June 27, 2002 grant date (a weighted price of \$19.02 per share) and recognized as unearned compensation

within stockholders’ equity. Over the six-month and four-year vesting periods, the unearned compensation is being recognized as compensation expense. For the years ended September 30, 2004, 2003, and 2002, compensation expense for the initial public offering restricted stock awards was \$16,733, \$39,010, and \$27,525, respectively, including the award compensation expense and applicable payroll taxes for the respective periods.

Stock Options

The Committee may grant both incentive stock options and nonqualified stock options to purchase shares of Class A common stock. Subject to the terms and provisions of the Plan, options may be granted to participants in such number, and upon such terms, as determined by the Committee, provided that incentive stock options may not be granted to non-employee directors. The option price is determined by the Committee, provided that for options issued to participants in the United States, the option price may not be less than 100% of the fair market value of the shares on the date the option is granted and no option may be exercisable later than the tenth anniversary of its grant. The nonqualified stock options granted vest ratably over a period of four years. As of September 30, 2004, the Company has 11,212,831 options outstanding with a weighted-average exercise price of \$23.71. The following table summarizes stock option activity during 2004 and 2003:

	2004		2003		2002	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of fiscal year	7,791,989	\$21.70	4,089,003	\$19.29	—	\$ —
Granted	3,892,029	27.35	3,844,793	24.19	4,106,703	19.29
Exercised	(185,234)	19.57	(35,808)	19.00	—	—
Forfeited	(273,022)	20.19	(105,999)	20.11	(17,700)	19.00
Expired	(12,931)	20.42	—	—	—	—
Outstanding at end of fiscal year	11,212,831	\$23.71	7,791,989	\$21.70	4,089,003	\$19.29

Exercisable options at end of fiscal year	2,926,847	\$20.95	1,106,256	\$19.42	—	\$ —
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The weighted-average estimated fair market value of employee stock options granted during 2004, 2003, and 2002 was \$10.10, \$8.59, and \$6.50 per share, respectively. These stock options were

granted at exercise prices equal to the current fair market value of the underlying stock. The following table summarizes information about stock options outstanding at September 30, 2004.

Reasonable price range groupings:	Outstanding Options			Exercisable Options	
	Number Outstanding	Weighted-Average Exercise Price	Weighted-Average Term (Years)	Number Outstanding	Weighted-Average Exercise Price
\$19.00	3,506,774	\$19.00	7.7	1,817,726	\$19.00
\$23.50–\$29.30	7,649,580	25.75	6.2	1,092,667	24.03
\$32.45–\$34.60	56,477	32.76	8.6	16,454	32.71
	11,212,831	\$23.71	6.7	2,926,847	\$20.95

18. Legal Proceedings

The Company is occasionally subject to lawsuits and claims arising in the normal conduct of business. Management does not expect the outcome of any pending matter to have a material adverse affect on the business, financial condition, or results of operations of the Company.

The Company provides indemnifications of varying scope and size to certain customers against claims of intellectual property infringement made by third parties arising from the use of our products or receipt of our services. The Company evaluates estimated losses for such indemnifications under SFAS No. 5, *Accounting for Contingencies*, as interpreted by FASB Interpretation

No. 45, *Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. Management considers such factors as the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate of the amount of loss. As of September 30, 2004, the Company had no outstanding claims and was not subject to any pending litigation alleging that the Company’s products or services infringe the intellectual property rights of any third parties.

19. Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) consists of the following components:

	Foreign Currency Translation Adjustment	Minimum Pension Liability	Accumulated Other Comprehensive Income (Loss)
As of September 30, 2001	\$ (767)	\$ —	\$ (767)
Other comprehensive income (loss)	17,648	(690)	16,958
As of September 30, 2002	16,881	(690)	16,191
Other comprehensive income (loss)	22,699	(333)	22,366
As of September 30, 2003	39,580	(1,023)	38,557
Other comprehensive income	29,470	1,023	30,493
As of September 30, 2004	\$69,050	\$ —	\$69,050

The increases in foreign currency translation during the years ended September 30, 2004, 2003, and 2002 were primarily related to an increase in the value of the British pound sterling relative to the U.S. dollar.

20. Income Taxes

Prior to the Company’s transition to a corporate structure, no provision for income taxes was made as the liability for such taxes was that of the former owners. As a result of the Company’s transition to a corporate structure on May 31, 2002, a tax expense of \$21,711 was recognized in fiscal 2002 related to deferred tax assets and liabilities recorded in accordance with the provisions of SFAS No. 109, *Accounting for Income Taxes*, arising from temporary differences between the book and tax basis

of the Company’s assets and liabilities at the date of transition.

For the years ended September 30, 2004 and 2003 and for the four-month period subsequent to the transition to a corporate structure in fiscal 2002, the Company’s provision for income taxes aggregated \$85,015, \$66,364, and \$11,342 (\$33,053 income tax expense less the \$21,711 tax expense related to the transition to a corporate structure), respectively, and consisted of the following:

	2004			2003			2002		
	Current	Deferred	Total	Current	Deferred	Total	Current	Deferred	Total
U.S. Federal	\$41,177	\$29,218	\$70,395	\$24,018	\$31,931	\$55,949	\$25,740	\$(16,108)	\$ 9,632
State and local	7,297	3,163	10,460	3,808	4,254	8,062	4,808	(3,314)	1,494
Foreign	4,160	—	4,160	2,353	—	2,353	216	—	216
	\$52,634	\$32,381	\$85,015	\$30,179	\$36,185	\$66,364	\$30,764	\$(19,422)	\$11,342

United States income taxes have not been provided on undistributed earnings of international subsidiaries. Those earnings are considered to be indefinitely reinvested. Upon distribution of those earnings in the form of dividends or otherwise, the Company may be subject to both U.S. income taxes (subject to adjustment for foreign tax credits) and withholding taxes payable to the various foreign countries.

At September 30, 2004 and 2003, the Company had income taxes payable of \$7,505 and \$17,401, respectively. Payments for the current federal income tax liability for 2004 will be reduced by approximately \$4,000, and were reduced by approximately \$12,000 in 2003, for the vesting of restricted stock and restricted stock units and the exercise of nonqualified stock options. The tax benefit resulting from the vesting of the restricted stock and stock units and the exercise of these options has been credited to additional paid-in capital. Income tax expense for the period subsequent to transition differed from the amounts computed by applying the U.S. federal income tax rate of 35% to income before taxes (\$207,859 and \$160,641 for the years ended September 30, 2004 and 2003, respectively, and \$10,361 for the period June 1, 2002 through September 30, 2002) as a result of the following:

	2004	2003	2002
Provision for taxes at U.S. federal statutory rate	\$72,751	\$56,224	\$ 3,626
Increase (reduction) in income taxes resulting from:			
Costs of transition to corporate structure	—	—	4,530
State and local income taxes, net of federal income tax benefits	7,799	5,040	972
Nondeductible expenses	909	839	592
Foreign earnings taxed at varying rates and foreign losses not tax effected	3,909	2,923	1,401
Other	(353)	1,338	221
	\$85,015	\$66,364	\$11,342

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below:

	2004	2003
Deferred tax assets:		
Accrued expenses	\$ 22,157	\$ 20,181
Foreign tax loss carryforwards	38,097	27,579
Other	4,635	12,505
	64,889	60,265
Valuation allowance	(38,097)	(27,579)
	\$ 26,792	\$ 32,686
Deferred tax liabilities:		
Compensation and benefits	\$ 22,804	\$ 12,286
Income deferred for tax purposes	3,340	3,332
Goodwill amortization	31,959	27,633
Depreciation and amortization	10,799	10,273
Other	28,100	17,638
	\$ 97,002	\$ 71,162

Of the \$128,135 net operating loss carryforwards of foreign subsidiaries (representing the \$38,097 of foreign tax loss carryforwards deferred tax asset in the table above), \$107,176 relates to losses that have already provided a tax benefit in the U.S. due to rules permitting flow through of such losses in certain circumstances. Without such losses included, the cumulative net operating loss carryforwards at September 30, 2004 were approximately \$20,959 which are subject to various provisions of each respective country. Approximately \$19,940 of this amount expires between 2005 and 2019 and \$1,019 of the amount has an indefinite life.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities except for goodwill, projected future taxable

income, and tax planning strategies in making this assessment. In order to fully realize the deferred tax asset, the Company will need to generate future taxable income prior to the expiration of the foreign net operating loss carryforwards which expire in 2005 through 2019. Foreign taxable loss for the years ended September 30, 2004 and 2003, and for the four-month period ended September 30, 2002 was \$25,090, \$11,922, and \$21,477, respectively. Consolidated taxable income for the years ended September 30, 2004 and 2003, and for the four-month period ended September 30, 2002 was \$210,396, \$163,263, and \$26,457, respectively. Based upon the level of historical taxable income and projections for future taxable income over the periods during which the deferred tax assets are deductible, management believes it is more likely than not the Company will realize the benefits of these deductible differences, net of the existing valuation allowances at September 30, 2004. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced.

21. Segments and Geographic Data

Under SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, the Company has determined that it has two reportable segments based on similarities among the operating units including homogeneity of services, service delivery methods, and use of technology. The two segments are Outsourcing and Consulting.

• **Outsourcing**—Hewitt applies its human resources expertise and employs its integrated technology solutions to administer its clients’ human resources programs. Hewitt’s benefits outsourcing services include health and welfare (such as medical plans), defined contribution (such as 401(k) plans) and defined benefit (such as pension plans). Hewitt’s payroll services include installed payroll software and fully outsourced processing. Hewitt’s workforce management outsourcing services include workforce administration, rewards management, recruiting and staffing, performance management, learning and development, and talent management.

• **Consulting**—Hewitt provides a wide array of consulting and actuarial services covering the design, implementation, communication and operation of health and welfare, compensation and retirement plans, and broader human resources programs and processes.

While Hewitt reports revenues and direct expenses based on these two segments, Hewitt combines its expertise in human resources outsourcing and consulting to create complete human resources solutions and a full continuum of human resources services.

Hewitt operates many of the administrative and support functions of its business through the use of centralized shared service operations to provide an economical and effective means of supporting the Outsourcing and Consulting segments. These shared services include information systems, human resources, general office support and space management, overall corporate management, finance, and legal services. Additionally, Hewitt utilizes a client development group that markets the entire spectrum of its services. The compensation and related expenses, other operating expenses, and selling, general and administrative expenses of the administrative and marketing functions are not allocated to the business segments, rather, they are included in unallocated shared costs. The costs of information systems, human resources, and the direct client delivery activities provided by the client development function are, however, allocated to the Outsourcing and Consulting segments on a specific identification basis or based on usage or headcount.

The table below presents information about the Company’s reportable segments for the periods presented:

	Year Ended September 30,		
	2004	2003	2002
Outsourcing⁽¹⁾			
Revenues before reimbursements (net revenues)	\$1,432,091	\$1,247,234	\$1,115,462
Segment income ⁽²⁾	297,911	245,905	272,702
Net client receivables and unbilled work in process	294,141	251,672	
Long-term unbilled work in process	18,003	7,143	
Goodwill and certain intangible assets	65,703	53,837	
Deferred contract costs	162,121	138,475	
Consulting⁽³⁾			
Revenues before reimbursements (net revenues)	\$ 772,591	\$ 734,422	\$ 600,735
Segment income ⁽²⁾	126,064	136,380	161,787
Net client receivables and unbilled work in process	228,741	209,758	
Long-term unbilled work in process	—	—	
Goodwill and certain intangible assets	327,362	312,996	
Deferred contract costs	481	—	
Total Company			
Revenues before reimbursements (net revenues)	\$2,204,682	\$1,981,656	\$1,716,197
Reimbursements	57,545	49,637	33,882
Total revenues	\$2,262,227	\$2,031,293	\$1,750,079
Segment income ⁽²⁾	\$ 423,975	\$ 382,285	\$ 434,489
Charges not recorded at the Segment level:			
One-time charges ⁽⁴⁾	—	—	26,143
Initial public offering restricted stock awards ⁽⁵⁾	16,733	39,010	27,525
Unallocated shared costs ⁽²⁾	184,409	165,294	140,501
Operating income ⁽²⁾	\$ 222,833	\$ 177,981	\$ 240,320
Net client receivables and unbilled work in process	\$ 522,882	\$ 461,430	
Long-term unbilled work in process	18,003	7,143	
Goodwill and certain intangible assets	393,065	366,833	
Deferred contract costs	162,602	138,475	
Assets not reported by segment	711,422	630,274	
Total assets	\$1,807,974	\$1,604,155	

⁽¹⁾On June 5, 2003, the Company acquired Cyborg and on June 15, 2003, the Company acquired substantially all of the assets of NTRC. As such, their results are included in the Company’s results from the respective acquisition dates.

⁽²⁾Prior to May 31, 2002, owners were compensated through distributions of income. In connection with the Company’s transition to a corporate structure on May 31, 2002, owners who worked in the business became employees and the Company began to record their compensation as compensation and related expenses in arriving at segment income.

⁽³⁾On June 5, 2002, the Company acquired the benefits consulting business of Bacon & Woodrow. As such, the results of Bacon & Woodrow have been included in the Company’s Consulting segment’s results from the acquisition date.

⁽⁴⁾In connection with the Company’s transition to a corporate structure, the following one-time charges were incurred: a) \$8,300 of non-recurring compensation expense related to the establishment of a vacation liability for its former owners and b) \$17,843 of non-recurring compensation expense resulting from certain owners receiving more common stock than their proportional share of total capital, without offset for those owners who receive less than their proportional share of stock.

⁽⁵⁾Compensation expense of \$16,733, \$39,010, and \$27,525 for the years ended September 30, 2004, 2003, and 2002, respectively, related to the amortization of initial public offering restricted stock awards.

Revenues and long-lived assets by geographic area for the following fiscal years are provided below. Revenues are attributed to geographic areas based on the country where the associates perform the services. Long-lived assets include net property and equipment, deferred contract costs, goodwill and intangible assets, such as capitalized software, but exclude investments in affiliated companies.

	Year Ended September 30,		
	2004	2003	2002
Revenues			
United States	\$1,841,294	\$1,687,861	\$1,571,747
United Kingdom	256,230	212,899	84,313
All Other Countries	164,703	130,533	94,019
Total	\$2,262,227	\$2,031,293	\$1,750,079

Long-Lived Assets		
United States	\$ 514,085	\$ 506,132
United Kingdom	348,912	316,977
All Other Countries	41,920	33,540
Total	\$ 904,917	\$ 856,649

22. Regulated Subsidiary

Hewitt Financial Services LLC (“HFS”), a wholly-owned subsidiary of the Company, is a registered U.S. broker-dealer. HFS is subject to the Securities and Exchange Commission’s “Uniform Net Capital Rule,” and has elected to compute its net capital in accordance with the “Alternative Standard” of that rule. As of September 30, 2004 and 2003, HFS had regulatory net capital, as defined, of \$16,274 and \$2,402, respectively, which exceeded the amounts required by \$16,269 and \$2,397, respectively.

Board of Directors and Senior Management

Hewitt Associates, Inc.

Board of Directors

Dale L. Gifford[†]
Chairman and Chief Executive Officer
Hewitt Associates, Inc.

Steven A. Denning[†]
Executive Managing Member
General Atlantic Partners,
a direct investment firm

Bryan J. Doyle
Outsourcing—Line of Business Leader
Hewitt Associates, Inc.

Cheryl A. Francis^{1*}
Former Executive Vice President and
Chief Financial Officer
R.R. Donnelley & Sons Company,
a print media company

Michael E. Greenlees^{2,3}
Chief Executive Officer
FastChannel Network,
an advertising services company

Julie S. Gordon
Retirement and Financial Management
Market Leader
Hewitt Associates, Inc.

Daniel J. Holland
Chief Operating Officer and
Manager—North America Region
Hewitt Associates, Inc.

Michele M. Hunt²
Founder and President
Vision & Values,
a leadership and organizational
development firm

James P. Kelly^{1,3*}
Former Chairman and
Chief Executive Officer
United Parcel Service,
a package distribution company

Cary D. McMillan^{2*}
Former Chief Executive Officer
Sara Lee Branded Apparel
Former Executive Vice President
Sara Lee Corporation,
leading branded consumer packaged
goods companies

Thomas J. Neff^{2,3}
Chairman of Spencer Stuart, U.S.,
an executive search consulting firm

Steven P. Stanbrook¹
President, Asia
S.C. Johnson & Son,
a manufacturer of consumer products

Board Committees:

¹ Audit

² Compensation and Leadership

³ Nominating and Corporate Governance

* Denotes Committee Chairman

Senior Management

Dale L. Gifford[†]
Chairman and Chief Executive Officer

Sanjiv K. Anand
Chief Technology Applications Officer

John L. Anderson
Talent and Organization Consulting—
Line of Business Leader

Bettye B. Baldwin
Manager—Latin America Region

Michael J. Bennett
Manager—Asia-Pacific Region

Perry O. Brandorff[†]
Manager—Europe Region

Jack E. Bruner
Health Management—
Line of Business Co-Leader

Monica M. Burmeister[†]
Retirement and Financial Management—
Line of Business Leader

Kevin M. Campbell
Outsourcing—Market Strategy and
Development Leader

Perry H. Cliburn
Chief Information Officer

C. Lawrence Connolly, III
General Counsel

Dan A. DeCanniere[†]
Chief Financial Officer

Bryan J. Doyle[†]
Outsourcing—Line of Business Leader

Daniel J. Holland[†]
Chief Operating Officer and
Manager—North America Region

Maureen A. Kincaid
Health Management—
Line of Business Co-Leader

Stephen D. King
Chief Human Resources Officer

James A. Konieczny
Outsourcing—Operations Leader

Michael R. Lee[†]
Client Development Leader

Mark A. Murray
Market Group Leader—
West U.S. Market Group

Christopher S. Palmer
Market Group Leader—
East U.S. Market Group

Roger S. Parkin
Market Group Leader—
U.K. & Ireland Market Group

John M. Ryan[†]
Chief Administrative Officer and
Corporate Development Leader

Alberto Santos, Jr.
Market Group Leader—
Middle Market

Richele A. Soja
Market Group Leader—
Central U.S. Market Group

Stephen M. Unterberger
Outsourcing—Solutions Strategy and
Development

[†] Executive Officer as defined by Securities and Exchange Commission regulations

Corporate Information

Corporate Headquarters

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Trading symbol: HEW

Transfer Agent and Registrar

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Hewitt Associates Employee

OneShares Programs

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Three First National Plaza
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Chicago, IL 60602
(800) 523-2085
www.benefitaccess.com

Annual Meeting of Stockholders

February 2, 2005—9:00 a.m.
The University of Chicago
Gleacher Center
450 North Cityfront Plaza Drive
Chicago, IL 60611

Investor Relations

Securities analysts, investment professionals, and stockholders should direct their questions to:
Investor Relations
(888) 439-6397

Community Relations

For information regarding Hewitt Associates' community relations programs and the Hewitt Associates Foundation, please direct inquiries to:
Community Relations
Hewitt Associates
100 Half Day Road
Lincolnshire, IL 60069

Public Relations

News media and trade publications should direct their inquiries to:
Public Relations
(847) 295-5000

Living our values: Hewitt, Diversity, and the Community

Hewitt's commitment to helping make the world a better place to work extends beyond the doors of our offices to the communities in which we live. It embraces the ideal of diversity.

We are a part of our communities. We serve their businesses and hire their people. And we work to make our communities strong. Hewitt volunteers support a variety of community development efforts. We support education, actively share our skills and expertise, and help prepare young people to take a productive place in society. We stand by those in need.

Our support includes grants, matching gifts, partnerships with community organizations, service on community boards, volunteer activities, and pro-bono human resources consulting. Each year, our associates are eligible for two days off, with pay, to take part in programs that benefit their communities. Run by associates, the Hewitt Associates Foundation supports more than 100 associate-nominated not-for-profit agencies. Our separate Corporate Social Responsibility program partners with nearly a dozen organizations focused on building tomorrow's diverse workforce, with services ranging from one-on-one tutoring and classroom teaching to affordable housing and leadership development, and racial understanding and reconciliation.

Diversity enriches all of us. Diversity of thought, backgrounds, and experiences broadens our perspectives and enables us to see new solutions. We are committed to attracting, hiring, and developing a workforce as diverse as the world markets we serve—and to increasing diversity in middle and upper management. We work closely with community, academic, governmental, and corporate organizations to channel diverse talent into the business. In our consulting and outsourcing work, we take into account the varying needs of our clients' diverse workforces. We sponsor networking opportunities for diverse communities within Hewitt, offer domestic partner benefits, recruit at more than a dozen historically black colleges, and help sponsor a wide range of associations and meetings aimed at building a diverse workforce—and a richer, more rewarding world.

