TIER TECHNOLOGIES INC
Form 10-Q
August 10, 2001

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

FORM 10-Q

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2001

OR

[_] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 000-23195

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

California	94-3145844
(State or other jurisdiction of incorporation or organization	(I.R.S. Employer Identification No.)

1350 Treat Boulevard, Suite 250
Walnut Creek, California 94596
(Address of principal executive offices)
(Zip Code)

(925) 937-3950
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

(1) Yes [X] No [_] (2) Yes [X] No [_]

As of August 6, 2001, the number of shares outstanding of the Registrant's Class A Common Stock was 967,754 and the number of shares outstanding of the Registrant's Class B Common Stock was 12,110,394.

This report contains a total of 27 pages of which this page is number 1.

TIER TECHNOLOGIES, INC.

FORM 10-Q

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Certain statements contained in this report, including statements regarding the development of the Company's services, markets and future demand for the Company's services, and other statements regarding matters that are not historical facts, are "forward-looking statements" within the meaning of federal securities laws. When used in this report, the words "believes", "expects", "anticipates", "intends", "estimates", "shows", "will likely" and similar expressions are intended to identify such forward-looking statements. Such forward-looking statements include risks and uncertainties; consequently, actual results may differ materially from those expressed or implied thereby. Factors that could cause actual results to differ materially from those set forth herein include, but are not limited to, those factors listed in ''Factors that May Affect Future Results'' section, as set forth beginning on page 18 of this report. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this report. The Company undertakes no obligation to publicly release the result of any revisions to these forward-looking statements or factors to reflect events or circumstances after the date of this report or to reflect the occurrence of unanticipated events.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

TIER TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(unaudited)
(in thousands)

ASSETS
Current assets:
Cash and cash equivalents
Short-term investments
Accounts receivable, net
Prepaid expenses and other current assets
Total current assets
Equipment and software, net
Notes and accrued interest receivable from related parties
Acquired intangible assets, net
Other assets
Total assets
LIABILITIES AND SHAREHOLDERS' EQUITY
Current liabilities:
Accounts payable
Accrued liabilities
Accrued subcontractor expenses
Accrued compensation and related liabilities
Purchase price payable
Other current liabilities
Total current liabilities
Borrowings and capital lease obligations, less current portion
Purchase price payable
Total liabilities
Commitments and contingent liabilities
Shareholders' equity:
Common stock, no par value
Notes receivable from shareholders
Deferred compensation
Accumulated other comprehensive loss
Retained earnings
Total shareholders' equity
Total liabilities and shareholders' equity

See Notes to Condensed Consolidated Financial Statements

TIER TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)
(in thousands, except per share data)

	Three Months Ended June 30,	
	2001	2000
Revenues	$26,956	$27,657
Cost of revenues	15,642	16,976
Gross profit	11,314	10,681
Costs and expenses:		
Selling and marketing	2,220	2,003
General and administrative	5,520	5,599
Other nonrecurring charges	--	644
Depreciation and amortization	1,786	1,665
Income from operations	1,788	770
Interest income (expense), net	179	206
Income before income taxes	1,967	976
Provision for income taxes	747	405
Net income	$ 1,220	$ 571
Basic net income per share	$ 0.10	$ 0.05
Shares used in computing basic net income per share	12,701	12,374
Diluted net income per share	$ 0.09	$ 0.05
Shares used in computing diluted net income per share	13,603	12,527

See Notes to Condensed Consolidated Financial Statements

TIER TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(in thousands)

	Nine M Ended June 2001
Net cash provided by operating activities	$ 6,243
Investing activities:	
Purchases of equipment and software	(1,993)
Notes and accrued interest receivable from related parties	(410)
Repayment on notes and accrued interest receivable from related parties	276
Business combinations, net of cash acquired	(9,867)
Subsidiary disposal, net of cash	--
Restricted cash	--
Purchases of available-for-sale securities	(7,947)
Sales of available-for-sale securities	3,696
Maturities of available-for-sale securities	5,678
Other assets	(2)
Net cash used in investing activities	(10,569)
Financing activities:	
Borrowings under bank lines of credit	7,500
Payments on borrowings	--
Repurchase of common stock	--
Net proceeds from issuance of common stock	1,332
Payments on capital lease obligations and notes payable to shareholders	(186)
Net cash provided by financing activities	8,646
Effect of exchange rate changes on cash	(233)
Net increase in cash and cash equivalents	4,087
Cash and cash equivalents at beginning of period	10,256
Cash and cash equivalents at end of period	$ 14,343
Supplemental disclosures of cash flow information:	
Cash paid during the period for:	
Interest	$ 414
Income taxes paid (refunded), net	$ 2,119
Supplemental disclosures of non-cash transactions:	
Equipment acquired under capital lease obligations	$ --
Assumed liabilities related to business combinations	$ --
Class B common stock issued in business combinations	$ 1,184
Conversion of Class A common stock to Class B common stock	$ 286
Class B common stock returned in disposal of business	$ --

See Notes to Condensed Consolidated Financial Statements

TIER TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1 -- BASIS OF PRESENTATION

The accompanying condensed consolidated financial statements of Tier Technologies, Inc. ("Tier" or the "Company") include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation. In the opinion of management, the condensed consolidated financial statements reflect all normal and recurring adjustments which are necessary for a fair presentation of the Company's financial position, results of operations and cash flows as of the dates and for the periods presented. The condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information. Consequently, these statements do not include all the disclosures normally required by generally accepted accounting principles for annual financial statements nor those normally made in the Company's Annual Report on Form 10-K. Accordingly, reference should be made to the Company's Form 10-K filed on December 7, 2000 and other reports the Company filed with the Securities and Exchange Commission for additional disclosures, including a summary of the Company's accounting policies, which have not materially changed. The consolidated results of operations for the three months and nine months ended June 30, 2001 are not necessarily indicative of results that may be expected for the fiscal year ending September 30, 2001 or any future period, and the Company makes no representations related thereto.

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

Certain reclassifications have been made to the prior period financial statements to conform to the current period presentation.

NOTE 2 -- REVENUE RECOGNITION

The majority of the Company's revenues are derived from professional consulting and processing services billed to clients on either a time and materials basis, a fixed price basis or a per-transaction basis. Time and materials revenues are recognized as services are performed. Revenues from fixed price contracts are recognized using the percentage-of-completion method of contract accounting based on the ratio of incurred costs to total estimated costs. Losses on contracts are recognized when they become known and reasonably estimable. Actual results of contracts may differ from management's estimates and such differences could be material to the consolidated financial statements. Revenues from performance-based contracts are recognized based on fees charged on a per-transaction basis. Most of the Company's contracts are terminable by the client following limited notice and without significant penalty to the client. The completion, cancellation or significant reduction in the scope of a large project would have a material adverse effect on the Company's business, financial condition and results of operations. For the three months ended June 30, 2001, revenues from two clients totaled approximately $3,296,000 and $2,860,000, which represented 12.2% and 10.6% of total revenues, respectively. For the nine months ended June 30, 2001, revenues from another client totaled

approximately $13,517,000 which represented 15.2% of total revenues.

Unbilled receivables represent revenue recognized in excess of amounts billed in accordance with contractual billing terms. Unbilled receivables at June 30, 2001 and September 30, 2000 were $10,420,000 and $9,567,000, respectively, of which $1,371,000 and $2,145,000, respectively, were included in non-current other assets as these amounts were not billable for more than one year under the terms of the contracts. Unbilled receivable for one client accounted for 21.3% of total net accounts receivable at June 30, 2001.

NOTE 2 - REVENUE RECOGNITION (continued)

Worldwide revenues derived from sales to governmental agencies were $16,019,000 and $16,415,000 for the three months ended June 30, 2001 and 2000, respectively and $54,378,000 and $47,394,000 for the nine months ended June 30, 2001 and 2000, respectively.

NOTE 3 -- ACQUISITIONS

ADC Consultants Pty ("ADC")

During the quarter ended June 30, 2001, the Company paid approximately $395,000 (based on an exchange rate of AU $2.03 to US $1.00) for the achievement of certain performance targets in accordance with the purchase agreement for ADC.

Service Design Associates ("SDA")

During the quarter ended June 30, 2001, the Company issued approximately 134,000 shares of Class B common stock valued at approximately $1,184,000 as payment for the achievement of certain performance targets in accordance with the purchase agreement for certain assets and liabilities of SDA. The Company also accrued approximately $1,416,000 as a result of the achievement of certain performance targets in accordance with the purchase agreement for certain assets and liabilities of SDA.

The SCA Group, Inc. and Harris Chapman (collectively "SCA")

During the quarter ended June 30, 2001, the Company paid $1,833,000 for the achievement of certain performance targets in accordance with the purchase agreement for certain assets and liabilities of SCA.

NOTE 4 -- BANK LINES OF CREDIT

At June 30, 2001, the Company had a $10 million revolving credit facility, of which $2.5 million may be used for letters of credit. The credit facility has a maturity date of August 26, 2002. The total commitment amount is limited to 85% of eligible accounts receivable plus 50% of up to $6 million of eligible unbilled receivables. The credit facility is secured by first priority liens and security interests in the Company's assets (excluding assets owned by Tier

Technologies (Australia) Pty Ltd., Simsion Bowles & Associates ("SBA") and ADC Consultants Pty Ltd.), including a pledge of 65% of the stock of the Company's subsidiaries excluding SBA. Interest is based on either the adjusted LIBOR rate plus 2.5% or the lender's announced prime rate plus 0.25%, at the Company's option and is payable monthly. As of June 30, 2001, the interest rate was approximately 6.6% and the outstanding borrowings were $7.5 million. In addition, standby letters of credit totaling approximately $346,000 were outstanding at June 30, 2001. Among other provisions, the credit facility requires the Company to maintain certain minimum financial ratios. As of June 30, 2001, the Company was in compliance with all financial ratios.

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TIER TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS--(Continued)
(unaudited)

NOTE 4 -- BANK LINES OF CREDIT (continued)

At June 30, 2001, the Company (through one of its Australian subsidiaries) had a credit facility that included a $1.3 million revolving line of credit with St. George Bank Limited of Australia (based on a June 30, 2001 exchange rate of AU $1.95 to US $1.00). Under the terms of the amended credit facility, the principal balance of the credit line will reduce during the quarter ending September 30, 2001 to a maximum line of approximately $1.0 million. The line of credit bears interest at fixed rates that are set at the time of each drawdown on the line. In December 1999, the balance of the line of credit was converted to a variable rate loan ("Loan"). The variable rate is based upon the bank's prime rate less 1.25% and interest is payable monthly. As of June 30, 2001, the interest rate was 8.0% and the outstanding balance of the Loan was approximately $1.3 million. The credit facility also provides for the issuance of letters of credit up to $148,000. Letters of credit totaling $141,000 were outstanding as of June 30, 2001. Among other provisions, the credit facility requires the Company's Australian subsidiary to maintain certain minimum financial ratios. As of June 30, 2001, the Company's Australian subsidiary was not in compliance with certain provisions of this credit facility; however, the bank waived such noncompliance.

NOTE 5 -- NET INCOME PER SHARE

The following table sets forth the computation of basic and diluted net income per share:

	Three Month Ended June 30,	
	2001	2
	(in thousand	
Numerator:		
Net income	$ 1,220	$
Denominator for basic net income per share-weighted average common shares outstanding shares outstanding	12,701	
Effects of dilutive securities:		
Common stock options	902	

Common stock contingently issuable	--	
Denominator for diluted net income per share-adjusted weighted average common shares and assumed conversions	13,603	
Basic net income per share	$ 0.10	$
Diluted net income per share	$ 0.09	$

Options to purchase approximately 958,000 and 1,441,000 shares of Class B common stock at exercise prices ranging from $10.88 to $17.81 per share and $8.63 to $17.81 per share, respectively, were not included in the computation of diluted net income per share for the three months and nine months ended June 30, 2001, respectively, because the options' exercise prices were greater than the average market price of the shares for these periods. Options to purchase approximately 3,371,000 and 2,313,000 shares of Class B common stock at exercise prices ranging from $5.78 to $17.81 per share and $6.81 to $17.81 per share, respectively, were not included in the computation of diluted net income per share for the three and nine months ended June 30, 2000, respectively, because the options' exercise prices were greater than the average market price of the shares for these periods.

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TIER TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS--(Continued)
(unaudited)

NOTE 6 -- COMPREHENSIVE INCOME (LOSS)

The Company's comprehensive income (loss) was as follows:

	Three Months End June 30,	
	2001	2000 (
Net income	$ 1,220	$
Foreign currency translation adjustment	793	
Total comprehensive income (loss)	$ 2,013	$

NOTE 7--OTHER NONRECURRING CHARGES

In April 2000, the Company recorded $644,000 of expense for severance costs related to a former officer.

In March 2000, the Company completed the sale of its U.K. subsidiary, Midas Computer Software Limited ("Midas"). The gross proceeds, including repayment of intercompany debt of approximately $1.4 million, amounted to approximately $2.6 million in cash and $1.3 million attributable to a release of 51,074 shares of the Company's Class B common stock and a share guarantee on the original acquisition. The Company recorded a nonrecurring loss of approximately $1.3

million as a result of the sale of Midas.

In December 1999, the Company recorded $263,000 of expense for severance costs related to a former officer.

NOTE 8--ALLIANCE AGREEMENT

In September 1999, the Company entered into a long-term strategic alliance ("Alliance Agreement"), with Siemens Business Services Limited ("SBS"). Under this Alliance Agreement, the Company has two existing contracts - the Application Service Center ("ASC") contract and the Consulting contract. Under the amended ASC contract, effective August 31, 2001, the Company has committed to utilizing a minimum amount of resources that SBS is obligated to mobilize pursuant to the ASC contract. The Company will market the ASC's services worldwide in exchange for fees based on the utilization of ASC resources by third parties. To the extent there is a shortfall in utilization, the Company's maximum obligation under the ASC contract for under-utilization shall not exceed $15.3 million (based on the June 30, 2001 exchange rate of GBP 0.71 to US $1.00) over the commitment period ending January 1, 2003. Through June 30, 2001, there were no minimum utilization requirements under the ASC contract. Pursuant to the Consulting contract, SBS guaranteed that it would engage the Company to provide a minimum of $9.9 million (based on the June 30, 2001 exchange rate of GBP 0.71 to US $1.00) for consultancy services over the life of the Consulting contract. From September 1999 through June 30, 2001, the Company has recognized a total of $20.0 million in revenues under the Consulting contract (based on the June 30, 2001 exchange rate of GBP 0.71 to US $1.00).

NOTE 9--SEGMENT INFORMATION

The Company is managed through four reportable segments: U.S. Commercial Services, U.S. Government Services, Australian Operations and United Kingdom Operations. The Company evaluates the performance of its operating segments based on revenue and gross profit (net revenue less direct costs), while other operating costs are evaluated on a geographic basis. Accordingly, the Company does not include selling and marketing expenses, general and administrative expenses, depreciation and amortization expense not attributable to client projects, interest income (expense), other income (expense) or income tax expense in segment profitability. The table below presents financial information for the four reportable segments:

	U.S. Commercial Services	U.S. Government Services	Australian Operations	United Kingdom Operations
	(in thousands)			
Three Months Ended June 30, 2001:				
Revenues	$ 6,814	$ 13,751	$ 5,137	$ 1,254
Gross profit	3,241	5,819	1,920	334
Three Months Ended June 30, 2000:				
Revenues	$ 5,676	$ 12,629	$ 6,669	$ 2,683

Gross profit................................	2,435	4,985	2,390	871
Nine Months Ended June 30, 2001:				
Revenues....................................	$ 21,464	$ 38,042	$ 15,713	$ 13,528
Gross profit................................	9,848	15,153	5,499	2,910
Nine Months Ended June 30, 2000:				
Revenues....................................	$ 13,049	$ 37,370	$ 20,313	$ 9,028
Gross profit................................	4,740	15,500	7,480	3,122

NOTE 10--NEW ACCOUNTING PRONOUNCEMENTS

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" ("SAB 101"). SAB 101 is effective no later than the fourth quarter of fiscal year 2001. The Company does not expect that the adoption of SAB 101 will have a significant impact on the consolidated financial statements.

In July 2001, the FASB issued two Statements, Statement No. 141, "Business Combinations" ("SFAS No. 141"), and Statement No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"). SFAS No. 141 revises accounting treatment for business combinations requiring the use of purchase accounting and prohibiting the use of pooling-of-interests method for all business combinations initiated after June 30, 2001 and broadens the criteria for recording intangible assets separate from goodwill for all business combinations completed after June 30, 2001. SFAS No. 142 revises the accounting for goodwill and other intangible assets by not allowing amortization of goodwill and establishing accounting for impairment of goodwill and other intangible assets. SFAS No. 142 will be effective for fiscal years beginning after December 15, 2001, with early adoption allowed for companies with a fiscal year beginning after March 15, 2001. The Company expects to adopt SFAS No. 142 as of October 1, 2002, the beginning of its fiscal year 2003. The Company has not yet evaluated the effects of these changes on its consolidated financial statements.

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TIER TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS--(Continued)
(unaudited)

NOTE 11--SUBSEQUENT EVENTS

In August 2001, the Company amended its revolving credit facility increasing the amount available for borrowing from $10.0 million to $15.0 million. The amendment also removed the limit on the commitment amount based on accounts receivable and unbilled receivables balances. In addition, the amendment added a $2.5 million non-revolving equipment facility that can be drawn down through February 28, 2002 and will bear interest at the lender's announced prime rate plus 0.50% or the LIBOR rate plus 2.75%, at the Company's option.

In July 2001, the Company acquired certain assets and liabilities of The Point Group Companies, Inc. ("TPG"), a Massachusetts corporation that specializes in the criminal justice, public safety, and health and human services state and local vertical markets. The initial purchase price totaled approximately $1.9 million in cash and shares of Class B common stock, including $200,000 in estimated acquisition costs. The acquisition will be accounted for using the purchase method of accounting. Additional contingent payments of up to

approximately $2.8 million in cash and shares of Class B common stock may be paid to TPG upon the achievement of certain revenue and earnings performance targets over the three-year period ending May 31, 2004. Contingent payments will be accrued when earned and recorded as additional purchase price.
Board Statement No. 142.

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

Overview

Tier is a vertically focused global consulting firm that delivers end-to-end business solutions to its national and multinational clients. The Company provides business solutions utilizing a variety of delivery offerings that are tailored to specific client industries and governmental agencies, and include solutions that link systems and technology improvements to increased operating efficiencies. Through offices located in the United States, Australia and the United Kingdom, the Company works closely with it's Fortune 1000, government and other clients to determine, evaluate and implement strategies that allow it to rapidly channel emerging technologies into business operations. The Company's revenues increased to $88.7 million in the nine months ended June 30, 2001 from $79.8 million in the nine months ended June 30, 2000. A significant portion of the Company's revenues are derived from sales to government agencies. For the nine months ended June 30, 2001, approximately 61.3% of the Company's revenues were derived from sales to government agencies, as compared to 59.4% for the nine months ended June 30, 2000. The Company's workforce, comprised of employees, independent contractors and subcontractors, has grown to 935 on June 30, 2001 from 916 on June 30, 2000.

The Company's revenues are derived primarily from professional consulting and processing services billed to clients on either a time and materials basis, a fixed price basis, or a per-transaction basis. Time and materials revenues are recognized as services are performed and expenses are incurred. Fixed price revenues are recognized using the percentage-of-completion method, based upon the ratio of costs incurred to total estimated project costs. Revenues from performance-based contracts are recognized based on fees charged on a per-transaction basis. The percentage of the Company's revenues generated on a time and materials basis was 53.7% and 52.2% for the nine months ended June 30, 2001 and 2000, respectively. The percentage of the Company's revenues generated on a fixed price basis was 20.5% and 30.0% for the nine months ended June 30, 2001 and 2000, respectively. The percentage of revenues generated on a per-transaction basis was 25.8% and 16.1% for the nine months ended June 30, 2001 and 2000, respectively. The increase in revenues generated on a per-transaction basis results from an increase in the number of Vertical ASP operations and increased transaction volume at existing centers. Substantially all of Tier's contracts are terminable by the client following limited notice and without significant penalty to the client. From time to time, in the regular course of its business, the Company negotiates the modification, termination, renewal or transition of time and materials, fixed price and per-transaction based contracts that may involve an adjustment to the scope or nature of the project, billing rates, percent complete or gross profit margins. If the Company significantly overestimates the volume for transaction-based contracts or underestimates the resources or time required for fixed price and per-transaction based contracts, its financial condition and results of operations would be materially and adversely affected. Unsatisfactory performance or unanticipated difficulties or delays in completing projects may result in client dissatisfaction and a reduction in payment to, or payment of damages (as a result of litigation or otherwise) by the Company, which could have a material adverse effect upon our business, financial condition and result of operations.

The Company has derived a significant portion of its revenues from a small number of large clients. For some of these clients, the Company performs a number of different projects pursuant to multiple contracts or purchase orders. For the three months ended June 30, 2001, State of Missouri and District of Columbia accounted for 12.2% and 10.6% of the Company's revenues, respectively. For the nine months ended June 30, 2001, Siemens Business Services Limited ("SBS") accounted for 15.2% of the Company's revenues. The Company anticipates that a substantial portion of its revenues will continue to be derived from a small number of large clients. The completion, cancellation or significant reduction in the scope of a large project would have a material adverse effect on the Company's business, financial condition and results of operations.

Personnel, facility and depreciation and amortization expenses represent a significant percentage of the Company's operating expenses and are relatively fixed in advance of any particular quarter. The Company manages its personnel utilization rates by carefully monitoring its needs and anticipating personnel increases based on specific project requirements. To the extent revenues do not increase at a rate commensurate with these additional expenses, the Company's results of operations could be materially and adversely affected. In addition, to the extent that the Company is

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unable to hire and retain salaried employees to staff new or existing client engagements or retain hourly employees or contractors, the Company's business, financial condition and results of operations would be materially and adversely affected.

From December 1996 through June 30, 2001, the Company made fifteen acquisitions for a total cost of approximately $54.8 million in cash and shares of Class B Common Stock, excluding future contingent payments. The Company also incurred $2.5 million in compensation charges related to business combinations resulting from these acquisitions. Generally, contingent payments are recorded as additional purchase price at the time the payment can be determined beyond a reasonable doubt. If a contingent payment is based, in part, on a seller's continuing employment with the Company, the payments are recorded as compensation expense over the vesting period when the amount is deemed probable. These acquisitions helped the Company to expand its operations in the United States, to establish its operations in Australia and the United Kingdom, to broaden the Company's client base, delivery offerings and technical expertise and to supplement its human resources.

International operations accounted for 32.9% and 36.8% of revenues for the nine months ended June 30, 2001 and June 30, 2000, respectively. The Company believes that the percentage of total revenues attributable to international operations will continue to be significant. International operations may subject the Company to foreign currency translation adjustments and transaction gains and losses for amounts denominated in foreign currencies.

Results of Operations

The following summarizes the Company's operating results as a percentage of revenues for each of the periods indicated:

	Three Months Ended June 30,		
	2001	2000	200

Revenues	100.0%	100.0%	100
Cost of revenues	58.0	61.4	62
Gross profit	42.0	38.6	37
Costs and expenses:			
Selling and marketing	8.3	7.2	6
General and administrative	20.5	20.3	18
Other nonrecurring charges	--	2.3	
Depreciation and amortization	6.6	6.0	6
Income from operations	6.6	2.8	6
Interest income (expense), net	0.7	0.7	0
Income before income taxes	7.3	3.5	6
Provision for income taxes	2.8	1.4	2
Net income	4.5%	2.1%	4

Three Months Ended June 30, 2001 and June 30, 2000

Revenues. Revenues are generated primarily by providing professional consulting and processing services on client engagements. Revenues decreased 2.5% to $27.0 million for the three months ended June 30, 2001 from $27.7 million for the three months ended June 30, 2000. This decrease resulted primarily from a decrease in United Kingdom operation revenues resulting from the completion of several projects under the Alliance Agreement with Siemens Business Services Limited ("SBS").

Gross Profit. Cost of revenues consists primarily of those costs directly attributable to providing service to a client, including employee salaries and incentive compensation, independent contractor and subcontractor costs, employee benefits, payroll taxes, travel-related expenditures, and any project-related equipment, hardware or software purchases.

For payment processing center operations, cost of revenues also include facility, equipment and direct overhead costs. Included in cost of revenues is $354,000 and $312,000 of depreciation and amortization for the three months ended June 30, 2001 and 2000, respectively. Gross profit increased 5.9% to $11.3 million for the three months ended June 30, 2001 from $10.7 million in the three months ended June 30, 2000. Gross profit as a percentage of revenues increased to 42.0% for the three months ended June 30, 2001 as compared to 38.6% in the three months ended June 30, 2000. This increase resulted primarily from the decrease in United Kingdom operation revenues which had a higher use of subcontractors and lower gross profit margins.

Selling and Marketing. Selling and marketing expenses consist primarily of personnel costs, sales commissions, advertising and marketing expenditures and travel-related expenditures. Selling and marketing expenses increased 10.8% to $2.2 million for the three months ended June 30, 2001 from $2.0 million for the three months ended June 30, 2000. As a percentage of revenues, selling and marketing expenses increased to 8.3% for the three months ended June 30, 2001 from 7.2% for the three months ended June 30, 2000. The increase in selling and marketing expenses in total dollars was primarily attributable to the cost of a feasibility study performed in partnership with SBS. The Company expects selling and marketing expenses to increase in total dollars in future quarters as the

Company continues to make investments in its marketing and branding initiatives and its business development efforts.

General and Administrative. General and administrative expenses consist primarily of personnel costs related to general management, administrative and other nonbillable functions, human resources, resource management, staffing, accounting and finance, legal and information systems, as well as professional fees related to legal, audit, tax, external financial reporting and investor relations matters. General and administrative expenses decreased 1.4% to $5.5 million for the three months ended June 30, 2001 from $5.6 million for the three months ended June 30, 2000. As a percentage of revenues, general and administrative expenses increased to 20.5% for the three months ended June 30, 2001 from 20.3% for the three months ended June 30, 2000. Over the longer term, the Company expects general and administrative expenses as a percentage of revenues to be in the range of 17% to 18% on a fiscal year basis. Included in general and administrative expenses is compensation charges related to business combinations of $407,000 for the three months ended June 30, 2000. This charge resulted from the amortization of the value of shares that were released over a three-year period in connection with the acquisition of Simpson Fewster & Co. Pty Limited ("SFC") and contingent payments earned in accordance with the acquisition agreements for SFC and Infact Pty Limited as Trustee of the Infact Unit Trust. The Company may incur compensation charges related to business combinations in future quarters due to acquisition earnout payments becoming probable.

Other Nonrecurring Charges. The other nonrecurring charge of $644,000 for the three months ended June 30, 2000, resulted primarily from severance costs paid to a former officer.

Depreciation and Amortization. Depreciation and amortization consists primarily of expenses associated with the depreciation of equipment and improvements and amortization of intangible assets resulting from acquisitions and other intellectual property. Depreciation and amortization increased 7.3% to $1.8 million for the three months ended June 30, 2001 from $1.7 million for the three months ended June 30, 2000. As a percentage of revenues, depreciation and amortization increased to 6.6% for the three months ended June 30, 2001 from 6.0% for the three months ended June 30, 2000. The increase in depreciation and amortization expense in total dollars was primarily attributable to the amortization of increased intangible assets from business combinations. The Company expects depreciation and amortization will continue to increase in total dollars.

Interest Income (Expense), Net. Net interest income decreased 13.1% to $179,000 for the three months ended June 30, 2001 compared to net interest income of $206,000 for the three months ended June 30, 2000. This decrease was primarily attributable to higher interest expense as a result of the outstanding line of credit balance.

Provision for Income Taxes. The provision for income taxes was $747,000 for the three months ended June 30, 2001 compared to $405,000 for the three months ended June 30, 2000. For the three months ended June 30, 2001 and 2000, the Company's effective tax rate was 38.0% and 41.5%, respectively. The future tax rate may vary due to a variety of factors, including, but not limited to, the relative income contribution by domestic and foreign operations, changes in statutory tax rates, the amount of tax exempt interest income generated during the year, the ability to utilize foreign tax credits and any

non-deductible items related to acquisitions or other nonrecurring charges. The Company will continue to closely monitor the effective tax rate on a quarterly

basis.

Nine Months Ended June 30, 2001 and June 30, 2000

Revenues. Revenues increased 11.3% to $88.7 million for the nine months ended June 30, 2001 from $79.8 million for the nine months ended June 30, 2000. Revenues for the nine months ended June 30, 2000 include $3.1 million of revenues from the Company's U.K. subsidiary, Midas Computer Software Limited ("Midas"), which was sold in March 2000. Excluding revenue from Midas, revenues increased 15.7% to $88.7 million for the nine months ended June 30, 2001 from $76.7 million in the nine months ended June 30, 2000. This increase resulted primarily from growth in United Kingdom operations resulting from increased revenues under the Alliance Agreement with SBS and growth in U.S. Commercial Services revenues partially offset by a decrease in Australian operations resulting from the general weakness in the Australian economy.

Gross Profit. Gross profit increased 8.3% to $33.4 million for the nine months ended June 30, 2001 from $30.8 million for the nine months ended June 30, 2000. Gross profit margin decreased to 37.6% for the nine months ended June 30, 2001 from 38.7% for the nine months ended June 30, 2000. Excluding the results of Midas, gross profit increased 12.0% to $33.4 million for the nine months ended June 30, 2001 from $29.8 million in the nine months ended June 30, 2000. Gross margin, excluding Midas, decreased to 37.6% for the nine months ended June 30, 2001 from 38.9% for the nine months ended June 30, 2000. The decrease in gross profit margin, excluding the results of Midas, was primarily attributable to the increased revenue from United Kingdom operations which had a higher use of subcontractors and lower gross profit margins.

Selling and Marketing. Selling and marketing expenses increased 11.8% to $6.0 million for the nine months ended June 30, 2001 from $5.4 million for the nine months ended June 30, 2000. As a percentage of revenues, selling and marketing expenses increased to 6.8% for the nine months ended June 30, 2001 from 6.7% for the nine months ended June 30, 2000. Excluding the results of Midas, selling and marketing expenses increased 25.0% to $6.0 million for the nine months ended June 30, 2001 from $4.8 million for the nine months ended June 30, 2000. As a percentage of revenues, selling and marketing expenses, excluding Midas, increased to 6.8% of revenues for the nine months ended June 30, 2001 from 6.3% in the nine months ended June 30, 2000. The increase in selling and marketing expenses in total dollars, excluding the results of Midas, was primarily attributable to the addition of sales and marketing personnel including labor costs associated with the Company's increased use of "seller-doers", the cost of a feasibility study performed in partnership with SBS and investments in the Company's marketing and branding initiatives.

General and Administrative. General and administrative expenses decreased 4.0% to $16.7 million for the nine months ended June 30, 2001 from $17.4 million for the nine months ended June 30, 2000. As a percentage of revenues, general and administrative expenses decreased to 18.7% for the nine months ended June 30, 2001 from 21.8% for the nine months ended June 30, 2000. Excluding the results of Midas, general and administrative expenses remained consistent at $16.7 million for the nine months ended June 30, 2001 compared to $16.6 million in the nine months ended June 30, 2000. As a percentage of revenues, general and administrative expenses, excluding Midas, decreased to 18.7% for the nine months ended June 30, 2001 from 21.7% in the nine months ended June 30, 2000. Included in general and administrative expenses is compensation charges related to business combinations of $117,000 and $526,000 for the nine months ended June 30, 2001 and 2000, respectively. The charge for the nine months ended June 30, 2001 resulted from the amortization of the value of shares that were released over a three-year period in connection with the acquisition of SFC. The charge for the nine months ended June 30, 2000 resulted from the amortization of SFC shares and contingent payments earned in accordance with the acquisition agreements for SFC and Infact Pty Limited as trustee of the Infact Unit Trust.

The Company may incur compensation charges related to business combinations in the future due to acquisition earnout payments becoming probable.

Other Nonrecurring Charges. The other nonrecurring charges of $2.2 million for the nine months ended June 30, 2000, resulted primarily from the write-down and subsequent sale of Midas and severance costs for two former officers.

Depreciation and Amortization. Depreciation and amortization increased 22.7% to $5.3 million for the nine months ended June 30, 2001 from $4.4 million for the nine months ended June 30, 2000. As a percentage of revenues, depreciation and amortization increased to 6.0% for the nine months ended June 30, 2001 from 5.4% for the nine months ended June 30, 2000. Excluding the results of Midas, depreciation and amortization expenses increased 27.9% to $5.3 million for the nine months ended June 30, 2001 from $4.2 million in the nine months ended June 30, 2000. As a percentage of revenues, depreciation and amortization expenses, excluding Midas, increased to 6.0% of revenues for the nine months ended June 30, 2001 from 5.4% in the nine months ended June 30, 2000. The increase in depreciation and amortization expenses, excluding the results of Midas, was primarily attributable to the amortization of increased intangible assets from business combinations.

Interest Income (Expense), Net. The Company had net interest income of $608,000 for the nine months ended June 30, 2001 compared to net interest income of $640,000 for the nine months ended June 30, 2000. Excluding the results of Midas, net interest income decreased 5.6% to $608,000 for the nine months ended June 30, 2001 from $644,000 in the nine months ended June 30, 2000. This decrease was primarily attributable to higher interest expense as a result of the outstanding line of credit balance.

Provision for Income Taxes. Provision for income taxes was $2.3 million for the nine months ended June 30, 2001 compared to $1.5 million for the nine months ended June 30, 2000. For the nine months ended June 30, 2001, the Company's effective tax rate was 39.0%. The provision for income taxes for the nine months ended June 30, 2000 of 69.4% was impacted by other nonrecurring charges for which no tax benefit could be recorded. Excluding these nonrecurring charges, the Company's effective tax rate for the nine months ended June 30, 2000 would have been 41.5%. The future tax rate may vary due to a variety of factors, including, but not limited to, the relative income contribution by domestic and foreign operations, changes in statutory tax rates, the amount of tax exempt interest income generated during the year, the inability to utilize foreign tax credits and any non-deductible items related to acquisitions or other nonrecurring charges. The Company will continue to closely monitor the effective tax rate on a quarterly basis.

Liquidity and Capital Resources

The Company's principal capital requirement is to fund working capital to support its growth, including potential future acquisitions, purchase price installments due on previous acquisitions and potential contingent payments related to prior acquisitions. The Company maintains a $10 million revolving credit facility (the "Credit Facility"), of which $2.5 million may be used for letters of credit. The Credit Facility expires on August 26, 2002. The Credit Facility allows the Company to borrow the lesser of $10 million or an amount equal to 85% of eligible accounts receivable plus 50% of up to $6 million of eligible unbilled receivables. The Credit Facility bears interest at the adjusted LIBOR rate plus 2.5% or the lender's announced prime rate plus 0.25%, at the Company's option. The Credit Facility is secured by first priority liens and security interests in the Company's assets (excluding assets owned by Tier Technologies (Australia) Pty Ltd., Simsion Bowles & Associates ("SBA") and ADC

Consultants Pty Ltd.), including a pledge of 65% of the stock of the Company's subsidiaries excluding SBA. The Credit Facility contains certain restrictive covenants, including, but not limited to, limitations on the amount of loans the Company may extend to officers and employees and the incurrence of additional debt. The Credit Facility requires the maintenance of certain financial covenants, including a minimum quarterly net income requirement, minimum tangible net worth, a minimum ratio of debt to tangible net worth and a minimum quick ratio. As of June 30, 2001, the Company was in compliance with all financial ratios. As of June 30, 2001, the interest rate was approximately 6.6%, outstanding borrowings totaled $7.5 million and outstanding standby letters of credit totaled approximately $346,000.

In August 2001, the Company amended its revolving credit facility increasing the amount available for borrowing from $10.0 million to $15.0 million. The amendment also removed the limit on the commitment amount based on accounts receivable and unbilled receivables balances. In addition, the amendment added a $2.5 million non-revolving equipment facility that can be drawn down through February 28, 2002 and will bear interest at the lender's announced prime rate plus 0.50% or the LIBOR rate plus 2.75%, at the Company's option.

The Company (through one of it's Australian subsidiaries) also maintains a credit facility that includes a $1.3 million revolving credit line with St. George Bank Limited of Australia (based on a June 30, 2001 exchange rate of AU $1.95 to US $1.00). Under the terms of the amended credit facility, the principal balance of the credit line will be reduced during the quarter ending September 30, 2001 to a maximum line of approximately $1.0 million. The line of credit bears interest at fixed rates that are set at the time of each drawdown on the line. In December 1999, the balance of the line of credit was converted to a variable rate loan ("Loan"). The variable rate is based upon the bank's prime rate less 1.25% and interest is payable monthly. As of June 30, 2001, the interest rate was 8.0% and the outstanding balance of the Loan was approximately $1.3 million. The credit facility also provides for the issuance of letters of credit up to $148,000. Standby letters of credit totaling $141,000 were outstanding as of June 30, 2001. Among other provisions, the credit facility requires the Company's Australian subsidiary to maintain certain minimum financial ratios. As of June 30, 2001, the Company's Australian subsidiary was not in compliance with certain provisions of this credit facility; however, the bank waived such noncompliance.

Net cash provided by operating activities was $6.2 million in the nine months ended June 30, 2001 and $6.1 million in the nine months ended June 30, 2000. The change is primarily attributable to increased profitability.

Net cash used in investing activities was $10.6 million in the nine months ended June 30, 2001 and $5.7 million in the nine months ended June 30, 2000. The change is primarily attributable to an increase in business combination expenditures and increased purchases of equipment and software. Capital expenditures, including equipment acquired under capital lease, but excluding assets acquired or leased through business combinations, were approximately $2.0 million in the nine months ended June 30, 2001 and $1.7 million in the nine months ended June 30, 2000. The Company anticipates that it may have increased capital expenditures depending on the number of future payment processing center operations and other capital expenditure needs.

Net cash provided by financing activities totaled $8.6 million in the nine months ended June 30, 2001 and $877,000 in the nine months ended June 30, 2000. The increase in net cash provided by financing activities resulted primarily from the borrowings under the Credit Facility.

The Company anticipates that its existing capital resources, including cash provided by operating activities and available bank borrowings, will be adequate to fund the Company's operations for at least the next 12 months. There can be no assurance that changes will not occur that would consume available capital resources before such time. The Company's capital requirements and capital resources depend on numerous factors, including potential acquisitions, contingent payments earned, new and existing contract requirements, the timing of the receipt of accounts receivable and payments of accounts payable, the Company's ability to draw on its bank facility and employee growth. To the extent that the Company's existing capital resources are insufficient to meet its capital requirements, the Company will have to raise additional funds. There can be no assurance that additional funding, if necessary, will be available on favorable terms, if at all.

Recent Accounting Standards

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" ("SAB 101"). SAB 101 is effective no later than the fourth quarter of fiscal year 2001. The Company does not expect that the adoption of SAB 101 will have a significant impact on the consolidated financial statements.

In July 2001, the FASB issued two Statements, Statement No. 141, "Business Combinations" ("SFAS No. 141"), and Statement No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"). SFAS No. 141 revises accounting treatment for business combinations requiring the use of purchase accounting and prohibiting the use of pooling-of-interests method for all business combinations initiated after June 30, 2001 and broadens the criteria for recording intangible assets separate from goodwill for all business combinations completed after June 30, 2001. SFAS No. 142 revises the accounting for goodwill and other intangible assets by not allowing amortization of goodwill and establishing accounting for impairment of goodwill and other intangible assets. SFAS No. 142 will be effective for fiscal years beginning after December 15, 2001, with early adoption allowed for companies with a fiscal year beginning after March

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15, 2001. The Company expects to adopt the pronouncement as of October 1, 2002, the beginning of its fiscal year 2003. The Company has not yet evaluated the effects of these changes on its consolidated financial statements.

Factors That May Affect Future Results

The following factors, among others, could cause actual results to differ materially from those contained in forward-looking statements in this Form 10-Q. Tier is referred to in this section as "we" or "us".

Variability of Quarterly Operating Results. Our revenues and operating results are subject to significant variation from quarter to quarter due to a number of factors, including:

- the accuracy of estimates of resources required to complete ongoing projects,
- the number, size and scope of projects in which we are engaged,
- the contractual terms and degree of completion of such projects,
- start-up costs including software sublicense fees incurred in connection with the initiation of large projects,

- our ability to staff projects with salaried employees versus hourly employees, hourly independent contractors and subcontractors,
- competitive pressures on the pricing of our services,
- any delays or costs incurred in connection with, or early termination of, a project,
- any assessment of potential penalties or contingent obligations in connection with a project,
- employee utilization rates,
- the number of billable days in a particular quarter,
- the adequacy of provisions for losses,
- the accuracy of estimated transaction volume in computing transaction rates for payment processing center operations,
- demand for our services generated by strategic partnerships and certain prime contractors,
- our ability to increase both the number and size of engagements from existing clients, and
- economic conditions in the vertical and geographic markets we serve.

The timing and realization of opportunities in our sales pipeline make the timing and variability of revenues difficult to forecast. In addition, the achievement of anticipated revenues is substantially dependent on our ability to attract, on a timely basis, and retain skilled personnel. A high percentage of our operating expenses, particularly personnel, facility and depreciation and amortization, are fixed in advance. In addition, we typically reach the annual limitation on FICA contributions for many of our U.S. consultants before the end of the calendar year. As a result, U.S. payroll taxes will vary significantly from quarter to quarter during the fiscal year and will generally be higher at the beginning of the calendar year. Revenues are impacted by the amount of holidays and vacations taken both within our consultant base and by our clients. As a result, revenues will vary from quarter to quarter during the fiscal year. Because of the variability of our quarterly operating results, we believe that period-to-period comparisons of our operating results are not necessarily

meaningful, should not be relied upon as indications of future performance and may result in volatility in the price of our Class B Common Stock. In addition, our operating results will from time to time be below the expectations of analysts and investors.

Potential Adverse Effect on Operating Results from Dependence on Large Projects, Limited Clients or Certain Market Sectors. The completion, cancellation, significant reduction in the scope or imposition of significant penalties for the Company's failure to meet scheduled delivery requirements of a large project or a project with certain clients would have a material adverse effect on our business, financial condition and results of operations. Most of our contracts are terminable by the client following limited notice and without significant penalty to the client. We have derived, and believe that we will continue to derive, a significant portion of our revenues from a limited number of clients. For the nine months ended June 30, 2001, SBS accounted for 15.2% of the Company's revenues. The volume of work performed for specific clients is

likely to vary from period to period, and a major client in one period may not use our services in a subsequent period. In addition, as a result of our focus in specific vertical markets, economic and other conditions that affect the companies in these markets could have a material adverse effect on our business, financial condition and results of operations.

In addition, under a contract with SBS, the Company has committed to utilizing a minimum number of full-time resources that SBS is obligated to mobilize. To the extent there is a shortfall in utilization, the Company's maximum obligation under the ASC contract for under utilization shall not exceed $15.3 million (based on the June 30, 2001 exchange rate of GBP 0.71 to US $1.00) over the commitment period ending January 1, 2003.

Dependence on Contracts with Government Agencies. For the nine months ended June 30, 2001, approximately 61.3% of our revenues were derived from sales to government agencies. These government agencies may be subject to budget cuts or budgetary constraints or a reduction or discontinuation of funding. A significant reduction in funds available for government agencies to purchase professional services would have a material adverse effect on our business, financial condition and results of operations. In addition, the loss of a major government client, or any significant reduction or delay in orders by such client, would have a material adverse effect on our business, financial condition and results of operations.

Inability to Attract and Retain Professional Staff Necessary to Existing and Future Projects. If we are unable to attract, retain and train skilled employees, such inability could impair our ability to adequately manage and staff our existing projects and to bid for or obtain new projects, which would have a material adverse effect on our business, financial condition and results of operation. In addition, the failure of our employees to achieve expected levels of performance could adversely affect our business. Our success depends in large part upon our ability to attract, retain, train, manage and motivate skilled employees, particularly project managers and other senior technical personnel. There is significant competition for employees with the skills required to perform the services we offer. In particular, qualified project managers and senior technical and professional staff are in great demand worldwide. In addition, we require that many of our employees travel to client sites to perform services on our behalf, which may make a position with us less attractive to potential employees. There can be no assurance that a sufficient number of skilled employees will continue to be available, or that we will be successful in training, retaining and motivating current or future employees.

Inability to Manage Growth. If we are unable to manage our growth effectively, such inability would have a material adverse effect on the quality of our services, our ability to retain key personnel, and our business, financial condition and results of operations. Our growth has placed, and is expected to continue to place, significant demands on our management, financial, staffing and other resources. We have expanded geographically by opening new offices domestically and abroad, and intend to open additional offices. Our ability to manage growth effectively will require us to continue to develop and improve our operational, financial and other internal systems, as well as our business development capabilities, and to train, motivate and manage our employees. In addition, as the average size and number of our projects continues to increase, we must be able to manage such projects effectively. There can be no assurance that our rate of growth will continue or that we will be successful in managing any such growth.

Failure to Estimate Accurately Fixed Price and Transaction-Based Contracts. Our failure to estimate accurately the resources or time required for a fixed price project or the expected volume of transactions under a

transaction-based contract could have a material adverse effect on our business, financial condition and results of operations. Under fixed price contracts, we receive our fee if we meet specified objectives such as completing certain components of a system installation. For transaction-based contracts, we receive our fee on a per-transaction basis, such as the number of child support payments processed. To earn a profit on these contracts, we rely upon accurately estimating costs involved and assessing the probability of meeting the specified objectives or realizing the expected number of transactions within the contracted time period. If we fail to estimate accurately the factors upon which we base our contract pricing, we may incur losses on these contracts. During the nine months ended June 30, 2001, 20.5% of our revenues were generated on a fixed price basis and 25.8% of our revenues were generated from transaction-based contracts. We believe that the percentage of revenues attributable to fixed price and transaction-based contracts will continue to be significant.

Potential Failure to Identify, Acquire or Integrate New Acquisitions. An important component of our business strategy is to expand our presence in new or existing markets by acquiring additional businesses. Since December 1996, we have acquired fifteen businesses. There can be no assurance that we will be able to identify, acquire or profitably manage additional businesses or to integrate successfully any acquired businesses without substantial expense, delay or other operational or financial problems. Acquisitions involve a number of special risks, including:

- diversion of management's attention,
- failure to retain key personnel,
- increased general and administrative expenses,
- client dissatisfaction or performance problems with an acquired firm,
- assumption of unknown liabilities, and
- other unanticipated events or circumstances.

Any of these risks could have a material adverse effect on our business, financial condition and results of operations.

Substantial Competition in the IT and Consulting Services Market. The IT and consulting services markets are highly competitive and are served by numerous international, national and local firms. There can be no assurance that we will be able to compete effectively in these markets. Market participants include systems consulting and integration firms, including national accounting firms and related entities, the internal information systems groups of our prospective clients, professional services companies, hardware and application software vendors, and divisions of large integrated technology companies and outsourcing companies. Many of these competitors have significantly greater financial, technical and marketing resources, generate greater revenues and have greater name recognition than we do. In addition, there are relatively low barriers to entry into the IT and consulting services markets, and we have faced, and expect to continue to face, additional competition from new entrants into the IT and consulting services markets.

We believe that the principal competitive factors in the IT and consulting services markets include:

- reputation,
- project management expertise,

- industry expertise,

- speed of development and implementations,

- technical expertise,

- competitive pricing, and

- the ability to deliver results on a fixed price and transaction basis as well as a time and materials basis.

We believe that our ability to compete also depends in part on a number of competitive factors outside our control, including:

- the ability of our clients or competitors to hire, retain and motivate project managers and other senior technical staff,

- the ownership by competitors of software used by potential clients,

- the price at which others offer comparable services,

- the ability of our clients to perform the services themselves, and

- the extent of our competitors' responsiveness to client needs.

Our inability to compete effectively on these competitive factors would have a material adverse effect on our business, financial condition and results of operations.

Dependence on Key Personnel. Our success depends in large part upon the continued services of a number of key employees. Although we have entered into employment agreements with certain key employees, these employees and other key employees who have not entered into employment agreements may terminate their employment at any time. The loss of the services of any key employee could have a material adverse effect on our business. In addition, if one or more of our key employees resigns to join a competitor or to form a competing company, the loss of such personnel and any resulting loss of existing or potential clients to any such competitor could have a material adverse effect on our business, financial condition and results of operations.

Control of Company and Corporate Actions by Principal Shareholders. Concentration of voting control could have the effect of delaying or preventing a change in control of us and may affect the market price of our stock. All of the holders of Class A Common Stock have entered into a Voting Trust with respect to their shares of Class A Common Stock, which represents 44.5% of the total common stock voting power at June 30, 2001. All power to vote shares held in the Voting Trust has been vested in the Voting Trust's trustee, James L. Bildner. The voting power held in the Voting Trust combined with Class B Common Stock owned by Mr. Bildner and vested options to acquire both Class A and Class B Common Stock held by Mr. Bildner represents 47.0% of the total common stock voting power outstanding at June 30, 2001. As a result, Mr. Bildner may be able to control the outcome of all corporate actions requiring shareholder approval, including changes in our equity incentive plan, the election of a majority of our directors, proxy contests, mergers, tender offers, open-market purchase programs or other purchases of common stock that could give holders of our Class B Common Stock the opportunity to realize a premium over the then-prevailing market price for their shares of Class B Common Stock.

Potential Costs or Claims Resulting from Project Performance. Many of our engagements involve projects that are critical to the operations of our clients' businesses and provide benefits that may be difficult to quantify. The failure by us, or of the prime contractor on an engagement in which we are a subcontractor, to meet a client's expectations in the performance of the engagement could damage our reputation and adversely affect our ability to attract new business, and could have a material adverse effect upon our business, financial condition and results of operations. We have undertaken, and may in the future undertake, projects in which we guarantee performance based upon defined operating specifications or guaranteed delivery dates. Unsatisfactory performance or unanticipated difficulties or delays in completing such projects may result in client dissatisfaction and a reduction in payment to us, or payment of damages (as a result of litigation

or otherwise) by us, which could have a material adverse effect upon our business, financial condition and results of operations. In addition, unanticipated delays could necessitate the use of more resources than we initially budgeted for a particular project, which also could have a material adverse effect upon our business, financial condition and results of operations.

Delay or Failure to Develop New Solutions. Our success will depend in part on our ability to develop solutions that keep pace with continuing changes in technology, evolving industry standards and changing client preferences. There can be no assurance that we will be successful in developing such solutions in a timely manner or that if developed we will be successful in the marketplace. Delay in developing or failure to develop new solutions would have a material adverse effect on our business, financial condition and results of operations.

Failure to Manage and Expand International Operations. For the nine months ended June 30, 2001, international operations accounted for 32.9% of our total revenues. We believe that the percentage of total revenues attributable to international operations will continue to be significant. As a result, we may expand our existing international operations and may enter additional international markets, which will require significant management attention and financial resources and could adversely affect our operating margins and earnings. In order to expand international operations, we will need to hire additional personnel and develop relationships with potential international clients through acquisition or otherwise. To the extent that we are unable to do so on a timely basis, our growth in international markets would be limited, and our business, financial condition and results of operations would be materially and adversely affected.

Our international business operations are subject to a number of additional risks, including, but not limited to:

- fluctuations in the value of foreign currencies,
- difficulties in building and managing foreign operations,
- difficulties in enforcing agreements and collecting receivables through foreign legal systems,
- longer payment cycles, and
- unexpected regulatory, economic or political changes in foreign markets.

There can be no assurance that these factors will not have a material adverse effect on our business, financial condition and results of operations.

Potential Volatility of Stock Price. There can be no assurance that an active public market for our Class B Common Stock will be sustained. The market for securities of early stage companies has been highly volatile in recent years, and our stock price could be volatile due to a number of factors, including:

- quarterly variations in operating results,
- announcements of technological innovations or new products or services by us or our competitors,
- general conditions in the IT industry or the industries in which our clients compete,
- changes in earnings estimates by securities analysts or us, and
- general economic conditions such as recessions or high interest rates.

Further, in the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted against the issuing company. Such litigation could result in substantial costs and a diversion of management's attention and resources, which could have a material adverse effect on our business, financial

condition and results of operations. Any adverse determination in such litigation could also subject us to significant liabilities. There can be no assurance that such litigation will not be instituted in the future against us.

Insufficient Insurance Coverage for Potential Claims. Any failure in a client's system could result in a claim against us for substantial damages, regardless of our responsibility for such failure. There can be no assurance that the limitations of liability set forth in our service contracts will be enforceable or will otherwise protect us from liability for damages. Although we maintain general liability insurance coverage, including coverage for errors or omissions, there can be no assurance that such coverage will continue to be available on reasonable terms, will be available in sufficient amounts to cover one or more claims or that the insurer will not disclaim coverage as to any future claim. The successful assertion for one or more claims against us that exceed available insurance coverage or changes in our insurance policies, including premium increases or the imposition of large deductible or co-insurance requirements, would adversely affect our business, financial condition and results of operations.

Dependence on Third Parties in Performing Certain Client Engagements. We sometimes perform client engagements using third parties. We often join with other organizations to bid and perform an engagement. In these engagements, we may engage subcontractors or we may act as a subcontractor to the prime contractor of the engagement. We also use third party software or technology providers to jointly bid and perform engagements. In these situations, we depend on the software, resources and technology of these third parties in order to perform the engagement. There can be no assurance that actions or failures attributable to these third parties or to the prime contractor or subcontractor will not also negatively affect our business, financial condition or results of operations. In addition, the refusal or inability of these third parties to permit continued use of their software, resources or technology by us, or the discontinuance or termination by the prime contractor of our services or the services of a key subcontractor, would have a material adverse effect on our business, financial condition and results of operations.

Inability to Protect Proprietary Intellectual Property. The steps we take to protect our intellectual property rights may be inadequate to avoid the loss or misappropriation of such information, or to detect unauthorized use of such information. We rely on a combination of trade secrets, nondisclosure and other contractual arrangements, and copyright and trademark laws to protect our intellectual property rights. We also enter into confidentiality agreements with our employees, generally require that our consultants and clients enter into such agreements and limit access to our proprietary information.

Issues relating to the ownership of, and rights to use, software and application frameworks can be complicated, and there can be no assurance that disputes will not arise that affect our ability to resell or reuse such software and application frameworks. A portion of our business involves the development of software applications for specific client engagements. Ownership of such software is the subject of negotiation with each particular client and is typically assigned to the client. We also develop software application frameworks, and may retain ownership or marketing rights to these application frameworks, which may be adapted through further customization for future client projects. Certain clients have prohibited us from marketing the software and application frameworks developed for them entirely or for specified periods of time or to specified third parties, and there can be no assurance that clients will not demand similar or other restrictions in the future.

Although we believe that our services and products do not infringe on the intellectual property rights of others, there can be no assurance that such a claim will not be asserted against us in the future, or that if asserted, any such claim will be successfully defended. The loss or misappropriation of our intellectual property or the unsuccessful defense of any claim of infringement could have a material adverse effect on our business, financial condition and results of operations.

Facilities, Systems and Operations Interruption or Failure. Any system failure, including network, software or hardware failure, whether caused by us, a third party service provider, unauthorized intruders or hackers, computer viruses, power outages or natural disasters, could cause interruptions or delays in our business or loss of data. Although we maintain property insurance and business interruption insurance, we cannot guarantee that our insurance will be adequate to compensate us for all losses that may occur as a result of any system failure.

Power Shortages. California has experienced shortages in the available power supply. We are currently exploring alternatives to ensure continuous and reliable sources of power in the event of blackouts. Such alternatives may not be implemented in a timely manner. Shortages may also affect our employees, vendors and customers.

Issuance of Preferred Stock May Prevent Change in Control and Adversely Affect Market Price for Class B Common Stock. The Board of Directors has the authority to issue preferred stock and to determine the preferences, limitations and relative rights of shares of preferred stock and to fix the number of shares constituting any series and the designation of such series, without any further vote or action by our shareholders. The preferred stock could be issued with voting, liquidation, dividend and other rights superior to the rights of our Class B Common Stock. The potential issuance of preferred stock may delay or prevent a change in control of us, discourage bids for the Class B Common Stock at a premium over the market price and adversely affect the market price and the voting and other rights of the holders of our Class B Common Stock.

No Current Intention to Declare or Pay Dividends. We have never declared or

paid cash dividends on our capital stock and do not anticipate paying any cash dividends in the foreseeable future.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk represents the risk of loss that may impact the financial position, results of operations or cash flows of the Company due to adverse changes in market prices and rates. The Company is exposed to market risk because of changes in foreign currency exchange rates as measured against the U.S. dollar and currencies of the Company's subsidiaries and operations in Australia and the United Kingdom.

Foreign Currency Exchange Rate Risk. The Company has wholly owned subsidiaries in Australia and conducts operations in the United Kingdom through a U.S.-incorporated subsidiary. Revenues from these operations are typically denominated in Australian Dollars or British Pounds, respectively, thereby potentially affecting the Company's financial position, results of operations and cash flows due to fluctuations in exchange rates. The Company does not anticipate that near-term changes in exchange rates will have a material impact on future earnings, fair values or cash flows of the Company and has not engaged in foreign currency hedging transactions for the nine months ended June 30, 2001. There can be no assurance that a sudden and significant decline in the value of the Australian Dollar or British Pound would not have a material adverse effect on the Company's financial condition and results of operations.

Interest Rate Sensitivity. The Company maintains a portfolio of cash equivalents and investments in a variety of securities including: certificates of deposit, money market funds and government and non-government debt securities. These available-for-sale securities are subject to interest rate risk and may fall in value if market rates increase. If market interest rates increase immediately and uniformly by 10 percentage points from levels at June 30, 2001, the fair value of the portfolio would decline by $392,000. We anticipate having the ability to hold our fixed income investments until maturity, and therefore do not expect our operating results or cash flows to be affected to any significant degree by the effect of a sudden change in market interest rates on our securities portfolio.

PART II. OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits.
None.

(b) Reports on Form 8-K.

The Company did not file any reports on Form 8-K during the three months ended June 30, 2001.

SIGNATURE

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

Tier Technologies, Inc.

Dated: August 10, 2001

By: /s/ LAURA B. DEPOLE

Laura B. DePole
Chief Financial Officer
(Duly Authorized Officer and Principal
Financial and Accounting Officer)