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

FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2004

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission File No. 0-25837

HEIDRICK & STRUGGLES INTERNATIONAL, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware	**36-2681268**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification Number)**

233 South Wacker Drive, Suite 4200, Chicago, Illinois 60606-6303
(Address of principal executive offices) (Zip Code)

(312) 496-1200
(Registrant’s telephone number, including area code)

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

Title of each class	Name of each exchange on which registered
Common Stock, $.01 par value	**Nasdaq National Market**

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

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ☒ No ☐

The aggregate market value of the Registrant’s Common Stock held by non-affiliates of the Registrant on June 30, 2004 was approximately $548,641,804 based upon the closing market price of $29.68 on that date of a share of Common Stock as reported on the Nasdaq National Market. As of February 25, 2005, there were 19,185,976 shares of the Company’s Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant’s definitive Proxy Statement for its Annual Meeting of Stockholders to be held on May 17, 2005, are incorporated by reference into Part III of this Form 10-K.

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PART I

ITEM 1. BUSINESS

Heidrick & Struggles International, Inc. (“Heidrick & Struggles”) is a premier provider of executive search and leadership consulting services. We help our clients build leadership teams by facilitating the recruitment, development and retention of personnel for their executive management and board director positions. Focusing on top-level services offers us several advantages, including access and influence with decision makers, increased potential for downstream work, higher fees per search, enhanced brand visibility, and added barriers to entry. Working at the top also allows us to attract and retain high-caliber consultants.

In addition to executive search, we provide other leadership services including executive assessment and professional development and—through an alliance—executive coaching. We market our leadership services to current and prospective clients as four offerings: talent management, board building, executive on-boarding, and M&A effectiveness.

Heidrick & Struggles and its predecessors have been in the executive search business for more than 50 years. We provide our services to a broad range of clients through the expertise of 297 consultants located in major cities around the world. For many of our clients, our global access to and knowledge of markets and candidates is an important characteristic of our business. We provide our executive search services on a retained basis, recruiting senior executives who often earn more than $200,000 annually. Our clients include the following:

- Fortune 500 companies
- Major non-U.S. companies
- Middle market and emerging growth companies
- Governmental and not-for-profit organizations
- Other leading private and public entities

The executive search industry is highly fragmented, consisting of several thousand executive search firms worldwide. Based on trade publication reports, we estimate that fewer than 10 executive search firms/alliances generated more than $100 million in worldwide revenue during 2004. Executive search firms are generally separated into two broad categories: retained search firms and contingency search firms. Retained executive search firms fulfill their clients’ senior leadership needs by identifying potentially qualified candidates and assisting clients in evaluating and assessing these candidates for positions typically with annual cash compensation of $150,000 and above. Retained executive search firms generally are compensated for their services whether or not the client employs a candidate identified by the search firm, and are generally retained on an exclusive basis. In contrast, contingency search firms usually focus primarily on positions with annual cash compensation of less than $150,000 and are compensated only upon successfully placing a recommended candidate. Executive search firms normally charge a fee for their services equal to approximately one-third of the first year’s total compensation for the position being filled.

We are a retained executive search firm. Our search process typically consists of the following steps:

- Analyze the client’s needs in order to understand its organizational structure, relationships and culture; determine the required set of skills for the position; define the required experience; and identify the other characteristics desired of the successful candidate
- Interview and evaluate candidates on the basis of experience and potential cultural fit with the client organization
- Present confidential written reports on the candidates who potentially fit the position specification

- Schedule a mutually convenient meeting between the client and each candidate
- Collect references on the final candidate
- Assist in structuring the compensation package and supporting the successful candidate's integration into the client team

We have begun to expand our services beyond executive search. For several years, we have offered executive assessment services in Europe. In late 2000, we extended our executive assessment business to North America and other parts of the world. This service provides senior-level executives with assessments of the individuals and teams reporting to them. We formed an alliance in March 2002 with Lore International Institute, a global executive coaching and professional development firm.

We reduced our focus on mid-level management search, with the completion of the integration of this business into our executive search business in January 2002.

Available Information

We maintain an Internet website at *http://www.heidrick.com*. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to these reports are available free of charge on this site as soon as reasonably practicable after the reports are filed with or furnished to the Securities and Exchange Commission. We also post quarterly press releases on our financial results, investor presentations and other documents containing additional information related to our company on this site. Our Internet website and the information contained in or connected to our website are for informational purposes only and are not incorporated into this annual report on Form 10-K.

Organization

Our structure, which is organized by geography and client services specialties, is designed to enable us to better understand our clients' cultures, operations, business strategies and industries, thereby improving our ability to serve them.

Geographic Structure. We provide executive-level search and leadership consulting to our clients worldwide through our offices in 26 countries. Major locations are managed by an Office Managing Partner, and staffed with consultants, associates, administrative assistants and other support staff. Administrative functions are centralized where possible, although certain support and research functions are situated regionally because of variations in local requirements.

We also have affiliates in six countries. We have no financial investment in these affiliates but receive licensing fees from them for the use of our name and our databases. Licensing fees were $476,000 and $122,000 for the years ended December 31, 2004 and 2003, respectively.

Client Services. Our market-facing activities are primarily structured around four groups: Board Search & Services, Target Accounts, Industry Practices and Functional Practices. The needs of each client are often served by one or more of these groups, as a combination of specialized skills are sometimes required to effectively serve the client.

- *Board Search & Services.* Those consultants in our company who have the most extensive experience placing members of boards of directors and chief executive officers are part of this group, which is coordinated by one of our Vice Chairmen. The services we perform for boards of directors and chief executive officers contribute substantially to our reputation.

- *Target Accounts.* We established this group because we believe it is valuable to both our company and our major clients to focus on serving these clients with an integrated services approach. Our target accounts are identified by the amount of work we historically have been engaged to perform for these clients or by revenue potential. Each identified account is managed by an account leader who has overall responsibility for drawing on the proper resources and skill sets within our company to serve that particular client.
- *Industry Practices.* We report and operate our executive search business in seven broad industry categories: Financial Services, Industrial, Consumer, Technology, Health Care, Professional Services and Higher Education/Nonprofit. These industry categories and their relative sizes, as measured by net revenue for 2004, are as follows:

Industry Categories	Percentage of Net Revenue
Financial Services	31%
Industrial	17
Consumer	17
Technology	14
Health Care	9
Professional Services	8
Higher Education/Nonprofit	4
	100%

Understanding the unique needs of each client—in terms of such factors as competitive landscape, business strategy and operations—is integral to providing quality service. Our internal practice structure reflects the needs of our clients and our enhanced focus on certain market sectors. Certain practices are organized as global entities, while others have a regional or local focus, as follows.

Our Global Industry Practices are: Business & Professional Services; Communications & Media; Consumer; Consumer Technology & Entertainment; Energy & Materials; Financial Services; Industrial; Life Sciences; Private Equity & Venture Capital; and Software, Hardware & Semiconductors.

Our Practices with a regional or local focus are: Diversity Services; Education/Nonprofit; Hospitals, Systems & Services; Interim Executives; Leadership Services; Managed Care; and Middle East.

Certain markets have a significant concentration of companies within particular industry sectors. For example, our Financial Services practice has its largest concentration of consultants in New York and London, two of the largest financial centers in the world. Each industry practice is coordinated by a Practice Managing Partner who facilitates the group's marketing activities.

- *Functional Practices.* We recognize that searching for candidates for particular executive positions often requires specialized skill in much the same way as a search for an executive in a particular industry. As a result, many of our executive search consultants also specialize in searches for specific "C-level" functional positions which are roles that report directly to the chief executive officer such as chief financial officers, chief information officers, chief legal officers, chief marketing officers and chief human resources officers. Our functional specialists tend to have experience with appropriate candidates from many different industries.

Our Global Functional Practices are: Board of Directors; Chief Information Officer; Finance; Human Resources; Legal; Real Estate; Research & Development; and Supply Chain.

Executive search consultants from each of our Client Services groups may work from any one of our offices around the world. For example, an executive search for a chief financial officer of an industrial company located in the United Kingdom may involve a consultant in the United Kingdom with an existing relationship with the client, another executive search consultant in the United States with expertise in our Industrial practice and a third executive search consultant with expertise in chief financial officer recruiting. This same industrial client may also engage us to perform skill-based assessments on each of its senior managers, which could require the expertise of a professional trained in this service. If the client company is designated as a target account, all of our services will be coordinated by our account leader for that client.

Information by Geographic Segment

North America. As of December 31, 2004, we had 140 executive search consultants in our North America segment, which includes the United States (except Miami, which we include in our Latin America geographic segment) and Canada. Our North America segment generated approximately 54% of our worldwide net revenue in 2004. The largest offices in this segment in terms of net revenue are located in New York, Chicago and Tysons Corner.

Latin America. As of December 31, 2004, we had 20 executive search consultants in our Latin America segment, which includes Mexico and the rest of Latin America, as well as Miami, which serves as the gateway office to the region and is where much of the region's business is managed. Approximately 3% of our worldwide net revenue in 2004 was generated in this segment.

Europe. As of December 31, 2004, we had 100 executive search consultants in 13 European countries. Our Europe segment generated approximately 35% of our worldwide net revenue in 2004. The United Kingdom, Germany and France produced the highest levels of net revenue in this segment.

Asia Pacific. As of December 31, 2004, we had 37 executive search consultants in the Asia Pacific segment. This segment generated approximately 8% of our worldwide net revenue in 2004.

For financial information relating to each geographic segment, see Note 18, *Segment Information*, in the Notes to Consolidated Financial Statements.

Seasonality

Historically, in years that were not affected by significant economic change, there has been some seasonality in our business. As a percentage of total annual net revenue, the first and fourth quarters of the year are typically the lowest. On average, the variance between the highest and lowest net revenue quarters is approximately three percentage points. In the last two years, as general economic conditions have improved, the fourth quarter has been the highest net revenue quarter of the year.

Clients and Marketing

Our consultants market the firm's executive search services through two principal means: targeted client calling and industry networking with clients and referral sources. These efforts are supported by our databases, which provide all our consultants with information as to contacts made by their colleagues with particular referral sources, candidates and clients. In addition, we benefit from a significant number of referrals generated by our reputation for high quality service and successfully completed assignments.

Either by agreement with clients or for client relations purposes, executive search firms sometimes refrain from recruiting employees of a client, and possibly other entities affiliated with that client, for a specified period,

generally not more than one year from the commencement of a search. We seek to mitigate the adverse effects of these blocking arrangements by strengthening our long-term relationships, thereby communicating our belief to prospective clients that we can conduct searches without these off-limit arrangements impeding the quality of our work.

No single client accounted for more than 3% of our net revenue in 2004, 2003 or 2002.

Information Management

We rely on technology to support our consultants and staff in the search process. Our technology infrastructure consists of internally developed databases containing candidate profiles and client records, coupled with online services and industry reference sources. We use technology to manage and share information on current and potential clients and candidates, to communicate to both internal and external constituencies and to support administrative functions. Over the past several years, we have invested in improving our systems. We intend to continue to invest in our own systems, focusing on our global search system and on our financial management and reporting systems.

Professional Staff and Employees

Our executive search professionals are categorized either as consultants or associates. Associates assist consultants by conducting research, making initial contact with candidates in some instances and performing other functions. As of December 31, 2004, we had 1,271 full-time equivalent employees, of whom 297 were executive search consultants, 327 were associates and 647 were other search, support and corporate staff.

In each of the past five years, no single consultant accounted for a material portion of our net revenues. We most frequently recruit our consultants from other executive search firms or, on occasion, from the industries represented by our practices. In the latter case, these are often seasoned executives who are entering the search profession as a second career, and who we train in our techniques and methodologies. We are not a party to any collective bargaining agreement, and we consider relations with our employees to be good.

Competition

The executive search industry is highly competitive. While we face competition to some degree from all firms in the industry, we believe our most direct competition comes from established global retained executive search firms that conduct searches primarily for the most senior-level positions within an organization. In particular, our competitors include Spencer Stuart & Associates, Egon Zehnder International, Russell Reynolds Associates, Inc. and Korn/Ferry International. To a lesser extent, we also face competition from smaller boutique or specialty firms that specialize in certain regional markets or industry segments. Each firm with which we compete is also a competitor in seeking to attract the most effective consultants.

The overall search industry has relatively few barriers to entry. Higher barriers exist, however, for firms like ours that focus primarily on conducting searches for executive-level positions. At this level, clients rely more heavily on a search firm's reputation, global access and the experience level of its consultants. We believe that the segment of executive search in which we compete is more quality-sensitive than price-sensitive. As a result, we compete on the level of service we offer, reflected by our client services specialties and, ultimately, by the quality of our search results. We believe that our emphasis on senior-level executive search, the depth of experience of our search consultants and our global presence enable us to compete favorably with other executive search firms.

Competition in our other leadership consulting services, including executive assessment and coaching, is highly fragmented, with no universally recognized market leaders.

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EXECUTIVE OFFICERS

Our executive officers as of March 1, 2005 are as follows:

Name	Age	Position With Company
Thomas J. Friel	57	Chairman and Chief Executive Officer; Director
Fritz E. Freidinger	40	Chief Legal Officer and Corporate Secretary
Bonnie W. Gwin	45	Regional Managing Partner, Americas
Eileen A. Kamerick	46	Chief Financial Officer
L. Kevin Kelly	39	Regional Managing Partner, Asia Pacific
Vincent C. Perro	51	Managing Partner, Leadership Services
Jeff R. Scherb	47	Chief Technology and Operations Officer
Scott W. Sherwood	53	Chief Talent and Human Resources Officer

There are no family relationships between any executive officer or director. The following information sets forth the business experience for at least the past five years for each of our executive officers as of March 1, 2005:

Thomas J. Friel has been our Chairman and Chief Executive Officer since June 2003. Previously, Mr. Friel was Chairman of the Technology Practice, Chairman of the Leadership Services Group and a Vice Chairman of Heidrick & Struggles from October 2001 to June 2003. Prior to that, Mr. Friel was President of Heidrick & Struggles Ventures from 1999 to 2001. Mr. Friel also served on our Board of Directors subsequent to our initial public offering in 1999 until 2002 when the Board transitioned to a majority of independent directors. He joined us in 1979.

Fritz E. Freidinger has been our Chief Legal Officer and Corporate Secretary since January 2004. Previously, Mr. Freidinger had been our General Counsel and Corporate Secretary since joining us in December 2002. Prior to that, Mr. Freidinger was Vice President, Global General Counsel and Corporate Secretary of Jones Lang LaSalle Incorporated from 2001 to 2002. From 1997 to 2001, Mr. Freidinger was with Hagan & Associates, a law firm providing services to Jones Lang LaSalle and its clients. In February 2005, we announced that Mr. Freidinger has resigned effective March 31, 2005. The search for his successor is currently underway.

Bonnie W. Gwin has been our Regional Managing Partner, Americas since January 2005. Previously, Ms. Gwin was Regional Managing Partner, North America from January 2004 to January 2005; Managing Partner, Technology and Professional Services Practice from October 2002 to May 2004; Managing Partner, North American Operations from February 2003 to December 2003; Managing Partner, Chicago, Cleveland, and Toronto from October 2001 to October 2002; Office Managing Partner, Cleveland from January 2001 to October 2001; and Partner in Charge of our Software specialty practice from October 2000 to February 2001. She joined us in 1997.

Eileen A. Kamerick has been our Chief Financial Officer since joining us in June 2004. Previously, Ms. Kamerick was Chief Financial Officer and Executive Vice President of Bcom3 Group, Inc. from 2001 to 2003 and Chief Financial Officer and Executive Vice President at United Stationers, Inc. from 2000 to 2001.

L. Kevin Kelly has been our Regional Managing Partner, Asia Pacific since September 2002. Previously, Mr. Kelly was Office Managing Partner, Tokyo from February 2002 to September 2002. He joined us in 1997.

Vincent C. Perro has been our Managing Partner, Leadership Services since joining us in July 2004. Previously, Mr. Perro was head of Sibson Consulting from 2001 to 2004. From 2000 to 2002, when Nextera Enterprises owned Sibson Consulting, he was head of Sibson Consulting, President of Sibson International, Chief Operating Officer of Sibson Consulting as a Nextera Enterprises officer, and a member of the Nextera Enterprises Board of Directors. From 1987 to 2000, Mr. Perro held various positions with Sibson & Company, including Chairman of the Board, President of Sibson International, and Financial Services Practice Leader.

Jeff R. Scherb has been our Chief Technology and Operations Officer since January 2004. Previously, Mr. Scherb had been our Chief Information Officer since joining us in September 2002. Prior to that, Mr. Scherb was Senior Vice President and Chief Technology Officer of Tribune Company from 1996 to 2002. Mr. Scherb also was President of Tribune Interactive at Tribune Company from 1999 to 2000.

Scott W. Sherwood has been our Chief Talent and Human Resources Officer since joining us in January 2004. Prior to that, Mr. Sherwood was President of Scott Sherwood & Associates, Inc. from 1997 to 2004.

RISK FACTORS

In addition to other information in this Form 10-K, the following risk factors should be carefully considered in evaluating our business because such factors may have a significant impact on our business, operating results, cash flows and financial condition. As a result of the risks set forth below and elsewhere in this Form 10-K, and the risks discussed in our other Securities and Exchange Commission filings, actual results could differ materially from those projected in any forward-looking statements.

We depend on attracting and retaining qualified consultants.

Our success depends upon our ability to attract and retain consultants who possess the skills and experience necessary to fulfill our clients' executive search needs. Our ability to hire and retain qualified consultants could be impaired by any diminution of our reputation, decrease in compensation levels relative to our competitors or restructuring of our compensation system or competitor hiring programs. If we cannot attract, hire and retain qualified consultants, our business, financial condition and results of operations may suffer.

We may not be able to prevent our consultants from taking our clients with them to another firm.

Our success depends upon our ability to develop and maintain strong, long-term relationships with our clients. Although we work on building these relationships between our firm and our clients, in many cases, one or two consultants have primary responsibility for a client relationship. When a consultant leaves one executive search firm and joins another, clients that have established relationships with the departing consultant may move their business to the consultant's new employer. We may also lose clients if the departing consultant has widespread name recognition or a reputation as a specialist in executing searches in a specific industry or management function. Historically, we have not experienced significant revenue loss from this client portability. If we fail to limit departing consultants from moving business to another employer, our business, financial condition and results of operations may be adversely affected.

Our success depends on our ability to maintain our professional reputation and brand name.

We depend on our overall reputation and brand name recognition to secure new engagements and hire qualified consultants. Our success also depends on the individual reputations of our consultants. We obtain many of our new engagements from existing clients or from referrals by those clients. A client who is dissatisfied with our work can adversely affect our ability to secure new engagements. If any factor hurts our reputation, including poor performance, we may experience difficulties in competing successfully for both new engagements and qualified consultants. Failure to maintain our professional reputation and brand name could seriously harm our business, financial condition and results of operations.

Because our clients may restrict us from recruiting their employees we may be unable to fill existing executive search assignments.

Clients frequently require us to refrain from recruiting certain of their employees when conducting executive searches on behalf of other clients. These restrictions generally remain in effect for no more than one year following the commencement of an engagement. However, the specific duration and scope of the blocking arrangements depend on the length of the client relationship, the frequency with which the client engages us to perform searches, the number of assignments we have performed for the client and the potential for future business with the client.

If a prospective client believes that we are overly restricted by these blocking arrangements from recruiting the employees of our existing clients, these prospective clients may not engage us to perform their executive searches, and as a result, our business, financial condition and results of operations may suffer.

We face aggressive competition.

The global executive search industry is extremely competitive and highly fragmented. We compete with other large global executive search firms and with smaller specialty firms. Specialty firms can focus on regional or functional markets or on particular industries. Some of our competitors possess greater resources, greater name recognition and longer operating histories than we do in particular markets or practice areas. There are limited barriers to entry into the search industry and new search firms continue to enter the market. Many executive search firms that have a smaller client base may be subject to fewer blocking arrangements. In addition, our clients or prospective clients may decide to perform executive searches using in-house personnel. Finally, competitors sometimes reduce their fees in order to attract clients and increase market share. Because we typically do not discount our fees, we may experience some loss of net revenue. We may not be able to continue to compete effectively with existing or potential competitors. Our inability to meet these competitive challenges could have an adverse impact on our business, financial condition and results of operations.

We rely heavily on information management systems.

Our success depends upon our ability to store, retrieve, process and manage substantial amounts of information. To achieve our goals, we must continue to improve and upgrade our information management systems. We may be unable to license, design and implement, in a cost-effective and timely manner, improved information systems that allow us to compete effectively. In addition, business process reengineering efforts may recommend a change in software platforms and programs. Such plans may result in an acceleration of depreciation expense over the shortened expected remaining life of the software. In addition, if we experience any interruptions or loss in our information processing capabilities, our business, financial condition and results of operations may suffer.

We face the risk of liability in the services we perform.

We are exposed to potential claims with respect to the executive search process. The growth and development of our other leadership consulting services brings with it the potential for new types of claims. A client could assert a claim for violations of blocking arrangements, breaches of confidentiality agreements or malpractice. In addition, candidates and client employees could assert claims against us. Possible claims include failure to maintain the confidentiality of the candidate's employment search or for discrimination or other violations of the employment laws or malpractice. In various countries, we are subject to data protection laws impacting the handling of candidate resumes and other data. We maintain professional liability insurance in amounts and coverage that we believe are adequate. However, we cannot guarantee that our insurance will cover all claims and that the coverage will be available at reasonable rates. Significant uninsured liabilities could have a negative impact on our business, financial condition and results of operations.

Our multinational operations may be adversely affected by social, political, legal and economic risks.

We generate substantial revenue outside the United States. We offer our services through our offices in 26 countries around the world. We are exposed to the risk of changes in social, political, legal and economic conditions inherent in international operations which could have a significant impact on our business, financial condition and results of operations. In particular, we conduct business in countries where the legal systems and trade practices are evolving. Commercial laws in these countries are often vague, arbitrary and inconsistently applied. Under these circumstances, it is difficult for us to determine at all times the exact requirements of such local laws. If we fail to comply with local laws, our business, financial condition and results of operations could suffer. In addition, the global nature of our operations poses challenges to our management, and financial and accounting systems. Failure to meet these challenges could seriously harm our business, financial condition and results of operations.

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We may not be able to align our cost structure with net revenue.

Over the last several years, we took steps to reduce our workforce, consolidate and close offices and reduce other expenses. However, our cost structure, particularly in certain areas in Europe, continues to be high in relation to net revenue. Although we have not yet finalized our action plans, we expect to record restructuring charges of between $9 million and $15 million for severance and office closures and consolidations, primarily in Europe, beginning in the second quarter of 2005. If we do not reduce our costs in proportion to demand for our services in a timely manner or if we reduce our workforce so that we are unable to service increased demand, our business, financial condition and results of operations could be adversely affected.

Our net revenue may be affected by adverse economic conditions.

Although our net revenue increased 18% in 2004, coinciding with signs of an economic recovery, there can be no assurances that economic conditions will continue to improve or even remain stable. If economic conditions weaken, our business, financial condition and results of operations could suffer.

We may not be able to generate sufficient profits to realize our net deferred tax assets.

In 2001, 2002 and 2003, we reported net losses, primarily due to restructuring activities necessary to align our cost structure with expected net revenue levels. The timing and strength of an economic recovery in the United States, Europe and other areas of the world continues to be unclear. During the fourth quarter of 2003, we recorded a full valuation allowance for our deferred tax assets for the U.S. and foreign operations which comprise the U.S. income tax entity. While we were profitable in 2004 and expect to be profitable in 2005 and beyond, there is no assurance that future taxable income will be sufficient to realize the benefit of deferred tax assets. If after future assessments of the realizability of the deferred tax assets, we determine that a lesser allowance is required, we would record a reduction to the income tax expense and the valuation allowance in the period of such determination. If we are unable to generate taxable income in the long-term, our business, financial condition, results of operations and cash flow could suffer.

We may experience impairment of our goodwill and other intangible assets.

Periodically, we perform assessments of the carrying value of our goodwill and other intangible assets. Current valuation estimates indicate that there has been no impairment of our goodwill or other intangible assets. However, future events, including our financial performance and economic conditions, could cause these assets to become impaired in the future. Any resulting impairment loss could have an adverse impact on our business, financial condition and results of operations.

Our ability to sublease or assign unused office space could affect our earnings and cash flows.

In 2001 and 2002, we consolidated and closed offices in order to reduce costs. This left us with a significant amount of unused office space with respect to which we are still required to make lease payments. At the time of the office closings we accrued the estimated costs associated with these actions. During 2004 and 2003, we recorded restructuring expense of $0.6 million and $22.2 million, respectively, to increase accruals for unused office space, reflecting the expectation of longer vacancy periods due primarily to weakness in the real estate markets in which the leased properties are located. While we have made progress in securing subleases for the majority of properties, at December 31, 2004, there was approximately 77 thousand square feet of unused real estate. The total remaining commitment related to these properties, is $33 million of which $17 million has been accrued at December 31, 2004, net of estimated sublease income. Inherent in these accruals are estimates concerning vacancy periods and sublease income. If we are unable to sublease or assign this unused office space within the estimated time frame, if we sublease or assign this office space for amounts less than we had

anticipated or if one of our tenants default on a sublease, our business, financial condition, results of operations and cash flow could suffer.

We have antitakeover provisions that make an acquisition of us difficult and expensive.

Antitakeover provisions in our Certificate of Incorporation, our Bylaws and the Delaware laws make it difficult and expensive for us to be acquired in a transaction which is not approved by our Board of Directors. Some of the provisions in our Certificate of Incorporation and Bylaws include:

- a classified board of directors
- limitations on the removal of directors
- limitations on stockholder actions
- the ability to issue one or more series of preferred stock by action of our Board of Directors

These provisions could discourage an acquisition attempt or other transaction in which stockholders could receive a premium over the current market price for the common stock.

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ITEM 2. PROPERTIES

Our corporate office is located in Chicago, Illinois. We have offices in major metropolitan areas in 26 countries around the world. All of our offices are leased. We do not own any real estate. The aggregate square footage of office space under lease was approximately 791 thousand as of December 31, 2004. These office leases call for future minimum lease payments of $149.9 million and have terms that expire between 2005 and 2016, exclusive of renewal options that we can exercise. Approximately 148 thousand square feet of office space has been sublet to third parties. See *Risk Factors* included in Item 1 of this Form 10-K for further information concerning unused office space.

ITEM 3. LEGAL PROCEEDINGS

We have contingent liabilities from various pending claims and litigation matters arising in the course of our business, some of which involve claims for damages that are substantial in amount. Some of these matters are covered by insurance. Although our ultimate liability in these matters cannot be determined, based upon information currently available, we believe the ultimate resolution of such claims and litigation will not have a material adverse effect on our financial condition, results of operations or liquidity.

In December 2002, Mt. Sinai Medical Center of Miami filed suit against us regarding a search for a chief executive officer we performed in 1998 seeking damages, including between $59 million and $75 million based primarily upon the operating loss incurred by Mt. Sinai in 2001, the chief executive officer’s last year at the hospital. On June 30, 2004, the judge presiding over this case in the U.S. District Court for the Southern District of Florida granted summary judgment, dismissing all the claims made by Mt. Sinai. Mt Sinai has filed an appeal with respect to this decision. While there can be no assurance as to the outcome, we believe that the claims are without merit.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of 2004.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market for Registrant's Common Equity

Our common stock is listed on the Nasdaq National Market under the symbol "HSII." The following table sets forth the high and low stock price per share of the common stock for the periods indicated, as reported on the Nasdaq National Market.

Year Ended December 31, 2004	High	Low
First Quarter	$24.23	$19.72
Second Quarter	30.46	23.50
Third Quarter	30.24	22.87
Fourth Quarter	35.36	27.06
Year Ended December 31, 2003		
First Quarter	$16.14	$ 9.96
Second Quarter	15.04	11.45
Third Quarter	20.00	12.35
Fourth Quarter	24.29	16.97

As of February 25, 2005, the last reported price on the Nasdaq National Market for our common stock was $35.15 per share and there were approximately 175 stockholders of record of the common stock.

We have never paid cash dividends on our common stock and do not presently anticipate paying any cash dividends on our common stock in the foreseeable future. Any determination to pay dividends in the future will be at the discretion of our Board of Directors and will be dependent upon our results of operations, financial condition, contractual restrictions, restrictions imposed by applicable law and other factors deemed relevant by the Board of Directors. Future indebtedness and loan facilities may also prohibit or restrict our ability to pay dividends and make distributions to our stockholders.

Issuer Purchases of Equity Securities

The following table provides information related to the Company's purchase of common shares for the year ended December 2004. For further information of the Company's share repurchase activity, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources."

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares That May Yet Be Purchased Under Publicly Announced Plans or Programs
Nov. 1, 2004—Nov. 30, 2004	85,000	$ 29.43	85,000	$27,498,131

a) On October 22, 2004, the Company's Board of Directors authorized management to purchase shares of the Company's common stock with an aggregate purchase price up to $30 million.

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ITEM 6. SELECTED FINANCIAL DATA

The selected financial data presented below have been derived from our audited consolidated financial statements. The data as of December 31, 2004 and 2003 and for the years ended December 31, 2004, 2003 and 2002 are derived from the audited historical consolidated financial statements which are included elsewhere in this Form 10-K. The data as of December 31, 2002, 2001 and 2000 and for the years ended December 31, 2001 and 2000 are derived from audited historical consolidated financial statements that are not included in this report. The data set forth are qualified in their entirety by, and should be read in conjunction with, "Management's Discussion and Analysis of Financial Condition and Results of Operations," the audited consolidated financial statements, the notes thereto, and the other financial data and statistical information included in this Form 10-K.

	Year Ended December 31,				
	2004	2003	2002	2001	2000
	(in thousands, except per share and other operating data)				
Statement of Operations Data:					
Revenue:					
Revenue before reimbursements (net revenue)	$375,432	$317,934	$350,712	$455,534	$594,394
Reimbursements	22,744	22,683	26,133	32,065	33,221
Total revenue	398,176	340,617	376,845	487,599	627,615
Operating expenses:					
Salaries and employee benefits:					
Salaries and employee benefits	251,186	223,537	242,330	302,792	395,105(5)
Nonrecurring compensation expense	—	—	—	—	12,222(6)
General and administrative expenses:					
General and administrative expenses	96,533	87,250	106,913	157,404	156,242
Nonrecurring general and administrative expenses	—	—	—	—	1,753(6)
Reimbursed expenses	21,247	22,683	26,133	32,065	33,221
Restructuring charges	550(1)	29,443(1)	48,532(1)	53,230(1)	—
Total operating expenses	369,516	362,913	423,908	545,491	598,543
Operating income (loss)	28,660	(22,296)	(47,063)	(57,892)	29,072
Non-operating income (expense):					
Interest income	2,588	1,687	2,018	5,523	8,723
Interest expense	(197)	(166)	(210)	(166)	(209)
Net realized and unrealized gains (losses) on equity and warrant portfolio	57,072(2)	673(2)	(1,325)(2)	(3,703)(2)	7,399(2)
Write-down of long-term investments	—	—	(5,000)(4)	(14,760)(4)	(240)(4)
Other, net	(1,024)	(1,722)	(73)	(517)	418
Net non-operating income (expense)	58,439	472	(4,590)	(13,623)	16,091
Income (loss) before income taxes and cumulative effect of accounting change	87,099	(21,824)	(51,653)	(71,515)	45,163
Provision for (benefit from) income taxes	4,791	58,844(3)	(11,491)	(24,094)	25,746
Income (loss) before cumulative effect of accounting change	82,308	(80,668)	(40,162)	(47,421)	19,417
Cumulative effect of accounting change, net of tax	—	—	—	4,494(2)	—
Net income (loss)	$ 82,308	$ (80,668)	$ (40,162)	$ (42,927)	$ 19,417
Basic earnings (loss) per common share	$ 4.35	$ (4.43)	$ (2.22)	$ (2.28)	$ 1.02
Basic weighted average common shares outstanding	18,941	18,217	18,107	18,839	18,979
Diluted earnings (loss) per common share	$ 4.11	$ (4.43)	$ (2.22)	$ (2.28)	$ 0.95
Diluted weighted average common shares outstanding	20,012	18,217	18,107	18,839	20,389
Balance Sheet Data (at end of period):					
Working capital	$150,198	$ 65,211	$ 84,276	$ 92,786	$120,340
Total assets	421,284	304,430	367,835	411,106	523,644
Long-term debt, less current maturities	—	26	294	1,959	610
Stockholders' equity	216,126	126,209	199,711	229,591	287,677
Other Operating Data:					
Average number of consultants during the period	299	328	391	507	441

Notes to Selected Financial Data:

(1) In 2001, we began the restructuring of our business to better align costs with expected net revenue levels. These initiatives related to reductions of our workforce, consolidation and closing of offices, goodwill and intangible asset write-offs and, in 2001, the settlement of a former Chief Executive Officer's contract upon his retirement. For the years ended 2004, 2003, 2002 and 2001, we recorded restructuring charges of $0.6 million, $29.4 million, $48.5 million and $53.2 million, respectively. See Note 14, *Restructuring Charges*, in the Notes to Consolidated Financial Statements.

(2) In 2004, we recognized a realized gain of $57.0 million related to the equity and warrant portfolio, net of the consultants' share of the gain and other costs, including $56.8 million related to the monetization of our shares of common stock of Google Inc. See Note 15, *Significant Warrant Monetization*, in the Notes to the Consolidated Financial Statements. In 2003, 2002, 2001 and 2000, we recorded realized gains, net of the consultants' share of the gain and other costs, of $0.7 million, $1.6 million, $1.0 million and $7.4 million, respectively, related to the equity and warrant portfolio.

In 2004 and 2003, the unrealized losses, net of the consultants' share of the losses and other costs, were less than $0.1 million, related to the equity and warrant portfolio. In 2002 and 2001, we recorded unrealized losses, net of the consultants' share of the losses and other costs, of $3.0 million and $4.7 million, respectively, related to the equity and warrant portfolio. See Note 2, *Summary of Significant Accounting Policies*, in the Notes to Consolidated Financial Statements.

(3) The 2003 income tax provision includes a non-cash income tax expense of $57.9 million, recorded in the fourth quarter of 2003, to provide a full valuation allowance against the net deferred tax assets for the U.S. and foreign operations which comprise the U.S. income tax entity. See Note 17, *Income Taxes*, in the Notes to Consolidated Financial Statements.

(4) During 2002, we wrote-down our remaining investment in the ETF Group, incurring a non-cash charge of $5.0 million. During 2001, we recorded non-cash charges of $14.8 million to write down of our investments in Silicon Valley Internet Capital ("SVIC") and ETF Group. During 2000, we recorded a non-cash charge of $0.2 million related to our investment in SVIC.

(5) Includes non-cash compensation expense of $2.7 million, due to the issuance of options by LeadersOnline, at a price below the deemed fair market value, for accounting purposes, at the time of issuance.

(6) We incurred $14.0 million of nonrecurring expenses during the third quarter of 2000 as a result of the withdrawal of LeadersOnline's proposed initial public offering. This included a non-cash compensation expense of $12.2 million which represents the remainder of the non-cash compensation expense related to the issuance of options by LeadersOnline, at a price below the deemed fair market value for accounting purposes, at the time of issuance. The remaining $1.8 million is due to the write-off of expenses related to the proposed initial public offering and is included in nonrecurring general and administrative expenses.

ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Management’s Discussion and Analysis of Financial Condition and Results of Operations as well as other sections of this annual report on Form 10-K contain forward-looking statements. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. The forward-looking statements are based on current expectations, estimates, forecasts and projections about the industry in which we operate and management’s beliefs and assumptions. Forward-looking statements may be identified by the use of words such as “expects,” “anticipates,” “intends,” “plans,” “believes,” “seeks,” “estimates,” and similar expressions. Forward-looking statements are not guarantees of future performance and involve certain known and unknown risks, uncertainties and assumptions that are difficult to predict. Actual outcomes and results may differ materially from what is expressed, forecasted or implied in the forward-looking statements. Factors that may affect the outcome of the forward-looking statements include, among other things, our ability to attract and retain qualified executive search consultants; the condition of the economies in the United States, Europe, or elsewhere; social or political instability in markets where we operate; price competition; our ability to achieve the planned cost savings from our cost reduction initiatives; our ability to sublease or assign unused office space; our ability to realize our tax loss carryforwards; the mix of profit or loss by country: an impairment of our goodwill and other intangible assets; and delays in the development and/or implementation of new technology and systems. For more information on the factors that could affect the outcome of forward-looking statements, see Risk Factors in Item 1 of this Form 10-K. We caution the reader that the list of factors may not be exhaustive. We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Executive Overview

Our Business

We are a premier provider of executive search and leadership consulting services. We help our clients build leadership teams by facilitating the recruitment, development and retention of personnel for their executive management and board positions. In addition to executive search, we provide other leadership services, including executive assessment and professional development and—through an alliance—executive coaching. We provide our services to a broad range of clients through the expertise of 297 consultants located in 26 countries throughout the world. Our executive search services are provided on a retained basis. Revenue before reimbursements of out-of-pocket expenses (“net revenue”) consists of retainers and indirect expenses billed to clients. Typically, we are paid a retainer for our executive search services equal to approximately one-third of the estimated first year compensation for the position to be filled. In addition, if the actual compensation of a placed candidate exceeds the estimated compensation, we often will be authorized to bill the client for one-third of the excess. Indirect expenses are calculated as a percentage of the retainer with certain dollar limits per search.

Our Compensation Model

Our compensation model closely aligns the interests of our consultants, our Company and our shareholders. Consultants are rewarded for individual performance based on a system which directly ties compensation to the amount of net revenue for which the consultant is responsible. Actual compensation is adjusted, up or down, based on the Company’s performance against profitability targets approved by the Compensation Committee of the Board of Directors. Each quarter, we evaluate the expected annual performance of both the consultants and the Company. As annualized performance estimates are revised each quarter, compensation accruals are adjusted in each region. As a result, the discretionary portion of compensation expense may fluctuate significantly from quarter to quarter.

2004 Overview

In 2004, the global economy showed signs of recovery and favorably affected the demand for our services. The recovery in Europe was not as strong as in other regions of the world. Net revenue increased 18.1%, or $57.5 million in 2004, compared to 2003. Double-digit increases were reported across all regions. All of our industry practices experienced increases in net revenue with the exception of the Industrial and Higher Education/Nonprofit practices which had modest declines. Consultant productivity increased as executive search revenue per consultant increased 31%, to $1.2 million in 2004, compared to 2003.

As a percent of net revenue, salary and employee benefits expense decreased to 66.9% in 2004 from 70.3% in 2003. General and administrative expenses were 25.7% of net revenue in 2004 compared to 27.4% in 2003.

During the fourth quarter of 2004, we adjusted our restructuring accruals and recorded $0.6 million of restructuring charges to reflect changes in lease estimates primarily due to a tenant default on a sublease and the final determination and payment of certain severance-related accruals.

During the third quarter of 2004, we exercised warrants to purchase shares of common stock of Google Inc. ("Google") which we received in 2001 in connection with recruitment fees, and subsequently sold all of the shares of common stock of Google that we held resulting in net proceeds of approximately $128.8 million. As a result of this warrant monetization, we recorded a realized gain of $56.8 million, net of the consultants' share of the gain.

Historically, our policy with respect to warrants was that 55% of the net proceeds resulting from the monetizations of warrants was payable to the consultants involved in the search. For warrants received after February 16, 2005, the portion of the net proceeds payable to the consultants was reduced from 55% to 50% and is limited to $10.0 million per monetization. In addition, of the 50% of the net proceeds we retain, 20% (or 10% of the total net proceeds) will be reserved for distribution to the broader employee population.

The effective tax rate was 5.5% in 2004, which is significantly lower than the statutory rate, primarily as a result of the partial reduction of the previously recorded valuation allowance related to net deferred tax assets associated with tax deductions that will be available for carryback to recover taxes paid in the current year and the utilization of net operating loss and capital loss carryforwards.

We ended the year with a cash balance of $222.8 million, an increase of $103.5 million, compared to $119.3 million at December 31, 2003. This increase is primarily as a result of the net proceeds of $128.8 million from the sale of our shares of common stock of Google offset by the portion of the consultants' share of the gain that was paid in 2004. Approximately $17 million of the consultants' share of the gain will be paid in 2005.

2005 Outlook

As we look forward to 2005, we have numerous business and cost initiatives in place to help us improve revenue growth and operating margin. An essential component to continued operating margin expansion in 2005 is a focus on raising profitability in Europe. Although the European region reported operating income in 2004, compared to an operating loss in 2003, we have assembled a team of executives to focus on increasing profitability further in 2005. Although we have not yet finalized our action plans, we expect to record restructuring charges of between $9 million and $15 million for severance and office closures and consolidations beginning in the second quarter of 2005. The restructuring charges relate primarily to the European region where initiatives are underway to improve operating margin in order to meet our profitability objectives.

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Results of Operations

We operate our executive search and complementary leadership services in four geographic regions: North America, which includes the United States (except Miami) and Canada; Latin America, which includes Mexico and the rest of Latin America, as well as Miami, which serves as our gateway office to the region; Europe; and Asia Pacific.

For segment purposes, reimbursements of out-of-pocket expenses classified as revenue are reported separately and therefore are not included in the net revenue by geographic region. The Company believes that analyzing trends in revenue before reimbursements (net revenue) and analyzing operating expenses as a percentage of net revenue more appropriately reflects the Company's core operations.

The following table summarizes the results of operations for the periods indicated (in thousands):

	Year Ended December 31,		
	2004	2003	2002
Revenue:			
Revenue before reimbursements (net revenue)	$375,432	$317,934	$350,712
Reimbursements	22,744	22,683	26,133
Total revenue	398,176	340,617	376,845
Operating expenses:			
Salaries and employee benefits	251,186	223,537	242,330
General and administrative expenses	96,533	87,250	106,913
Reimbursed expenses	21,247	22,683	26,133
Restructuring charges	550	29,443	48,532
Total operating expenses	369,516	362,913	423,908
Operating income (loss)	28,660	(22,296)	(47,063)
Net non-operating income (expense)	58,439	472	(4,590)
Income (loss) before income taxes	87,099	(21,824)	(51,653)
Provision for (benefit from) income taxes	4,791	58,844	(11,491)
Net income (loss)	$ 82,308	$ (80,668)	$ (40,162)

The following table sets forth, for the periods indicated, our selected statements of operations data as a percentage of revenue before reimbursements (net revenue):

	Year Ended December 31,		
	2004	2003	2002
Revenue:			
Revenue before reimbursements (net revenue)	100.0%	100.0%	100.0%
Reimbursements	6.1	7.1	7.5
Total revenue	106.1	107.1	107.5
Operating expenses:			
Salaries and employee benefits	66.9	70.3	69.1
General and administrative expenses	25.7	27.4	30.5
Reimbursed expenses	5.7	7.1	7.5
Restructuring charges	0.1	9.3	13.8
Total operating expenses	98.4	114.1	120.9
Operating income (loss)	7.6	(7.0)	(13.4)
Net non-operating income (expense)	15.6	0.1	(1.3)
Income (loss) before income taxes	23.2	(6.9)	(14.7)
Provision for (benefit from) income taxes	1.3	18.5	(3.3)
Net income (loss)	21.9%	(25.4)%	(11.5)%

Note: Totals and subtotals may not equal the sum of individual line items due to rounding.

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2004 Compared to 2003

Total revenue. Consolidated total revenue increased $57.6 million, or 16.9%, to $398.2 million in 2004 from $340.6 million in 2003. The increase in total revenue was due primarily to the increase in revenue before reimbursements (net revenue).

Revenue before reimbursements (net revenue). Consolidated net revenue increased $57.5 million, or 18.1%, to $375.4 million in 2004 from $317.9 million in 2003. Net revenue increased across all regions in 2004. All of our industry practices experienced increases in net revenue, with the exception of the Industrial and Higher Education/Nonprofit practices which had modest declines. In 2004, the number of confirmed executive searches increased 6% to 3,975 from 3,757 in 2003. We believe this increase reflects the impact of the continuing economic improvement in the global economy and our success in winning business. Excluding the $13.9 million positive impact of exchange rate fluctuations, which management believes provides a better comparison of operational performance, net revenue increased approximately 14%.

Net revenue in North America was $201.7 million in 2004, an increase of $29.7 million, or 17.3%, from $172.0 million in 2003. All of our industry practices experienced increases in net revenue, with the exception of the Higher Education/Nonprofit and Professional Services practices. In Latin America, net revenue was $12.7 million in 2004, an increase of $1.5 million, or 12.6%, from $11.2 million in 2003. Increases in the Financial Services, Health Care, Higher Education, Technology and Professional Services practices' net revenue was partially offset by declines across the other practices. Excluding a positive impact of $0.1 million due to exchange rate fluctuations, Latin America's net revenue increased by approximately 12% from 2003. Net revenue in Europe was $129.3 million in 2004, an increase of $16.3 million, or 14.4%, from $113.0 million in 2003. All of the industry practices experienced increases in net revenue, with the exception of Industrial and Technology practices which had modest declines. Excluding a positive impact of $12.0 million due to exchange rate fluctuations, Europe's net revenue increased by approximately 4% from 2003. In Asia Pacific, net revenue was $31.7 million in 2004, an increase of $10.1 million, or 46.7%, from $21.6 million in 2003. Net revenue increased across all practices in 2004. Excluding a positive impact of $1.6 million due to exchange rate fluctuations, Asia Pacific's net revenue increased approximately 39% compared to 2003.

Salaries and employee benefits. Consolidated salaries and employee benefits expense increased $27.7 million, or 12.4%, to $251.2 million in 2004 from $223.5 million in 2003. Fixed salaries and employee benefits expense decreased $4.6 million in 2004 as the average number of consultants decreased from 328 in 2003 to 299 in 2004. Performance-related compensation increased $32.3 million as a result of higher net revenue.

The net expense related to our German pension plan increased $1.6 million in 2004. Salaries and employee benefits expense in 2003 includes $6.1 million of expense related to the separation agreements of the former Chief Executive Officer, the former President and Chief Operating Officer and the former Chief Financial Officer and a benefit of $1.3 million from the reversal of accruals recorded in 2002 for the Performance Share Program. Excluding these items, which we believe more appropriately reflects our core operations, consolidated salaries and employee benefits expense would have been $249.6 million in 2004, an increase of $30.9 million, or 14.1%, compared to $218.7 million in 2003.

As a percentage of net revenue, salaries and employee benefits expense decreased to 66.9% in 2004 from 70.3% in 2003. Excluding the $1.6 million of pension expense in 2004 and the $6.1 million of severance-related expenses and the $1.3 million of benefit resulting from the reversal of accruals related to the Performance Share Program in 2003, which we believe more appropriately reflects our core operations, salaries and employee benefits expense as a percentage of net revenue would have been 66.5% in 2004 compared to 68.8% in 2003. The decrease as a percentage of net revenue is primarily due to lower fixed salaries and employee benefits expense in relation to the net revenue levels, offset by a greater percentage of net revenue accrued for performance-based compensation.

General and administrative expenses. Consolidated general and administrative expenses increased $9.2 million, or 10.6%, to $96.5 million in 2004 from $87.3 million in 2003. This increase was primarily due to $1.6 million of professional fees related to compliance with the requirements imposed by the Sarbanes-Oxley Act, a $1.9 million increase in tax, legal and other professional services, a $4.6 million increase in operating expenses associated with higher net revenue levels and discretionary spending related to marketing and business development activities, $1.3 million of legal settlement costs and a $0.3 million increase in bad debt expense. These increases were offset by $0.5 million of lower infrastructure expenses.

As a percentage of net revenue, general and administrative expenses decreased to 25.7% in 2004 from 27.4% in 2003.

Reimbursed expenses. We incur certain out-of-pocket expenses that are reimbursed by our clients. Historically, we have not established a receivable for reimbursable expenses incurred but not yet billed as the amount was determined to be immaterial. During the fourth quarter of 2004, we enhanced our estimation technique related to reimbursable expenses resulting in a non-recurring favorable impact to operating income of $1.5 million. We have accounted for this as a change in accounting estimate. This change in accounting estimate is not expected to have a significant impact on our results of operations in future periods.

Restructuring charges. During the fourth quarter of 2004, we adjusted our restructuring accruals and recorded $0.6 million of restructuring charges to reflect changes in lease estimates primarily due to a tenant default on a sublease and the final determination and payment of certain severance-related restructuring accruals.

In 2003, the Company recorded restructuring charges of $29.4 million. The charges include severance and other employee-related costs of $3.9 million related to reductions in workforce, primarily in Europe, expense of $22.2 million to increase accruals for leased properties that had been identified as excess in previous office consolidation charges and $3.3 million of expense for goodwill and other intangible impairment, related primarily to a wholly-owned subsidiary in Finland which was converted to a licensee. The accruals for excess real estate were increased to reflect the expectation of longer vacancy periods due primarily to weakness in the real estate markets in which the leased properties are located. The restructuring charges by segment are as follows: North America $7.0 million, Europe $22.1 million, and Corporate $0.3 million. Of the $29.4 million of restructuring charges recorded in 2003, approximately $25.8 million represents cash charges.

Operating income (loss). Our consolidated operating income was $28.7 million in 2004 compared to an operating loss of $22.3 million in 2003. The following table summarizes our consolidated operating income (loss) for the years ended December 31, 2004 and 2003, respectively:

Operating income (loss):	2004	2003	Change
		(in millions)	
Total regions	$ 56.8	$ 35.3	$ 21.5
Corporate	(27.6)	(28.2)	0.6
Operating income before restructuring charges	29.2	7.1	22.1
Restructuring charges	(0.6)	(29.4)	28.9
Consolidated operating income (loss)	$ 28.7	$(22.3)	$ 51.0

Note: Totals and subtotals may not equal the sum of individual line items due to rounding.

The increase in the consolidated operating income was primarily due to lower restructuring charges and improved net revenue and profitability in the geographic regions.

In North America, operating income in 2004 increased $9.8 million to $45.8 million from $36.0 million in 2003. The increase of $29.7 million in North America's net revenue, lower fixed salaries and employee benefits

expense of $6.0 million and lower bad debt expense of $0.6 million was partially offset by increases of $25.6 million in performance-related compensation and $0.9 million in general and administrative expenses.

In Latin America, operating income was $1.1 million in 2004 compared to $0.9 million in 2003. The increase of $1.5 million in net revenue was offset by higher salaries and employee benefits expense.

In Europe, operating income was $3.6 million in 2004 compared to an operating loss of $3.8 million in 2003. The increase in net revenue of $16.3 million and lower facilities-related costs of $1.1 million was partially offset by increases of $5.8 million in fixed salaries and employee benefits expense, $1.8 million of performance-related compensation, $0.8 million of bad debt expense and $0.3 million of discretionary spending. In 2004, general and administrative expenses also include $1.3 million of legal settlement costs relating to a claim arising from certain professional services provided by one of our consultants to a client.

In Asia Pacific, operating income in 2004 was $6.3 million, an increase of $4.0 million, compared to $2.3 million in 2003. The increase in net revenue of $10.1 million was partially offset by increases of $5.4 million of salaries and employee benefits expense, $0.2 million of bad debt expense and $0.5 million of discretionary spending.

Corporate expenses decreased $0.6 million, or 2.0%, to $27.6 million in 2004 from $28.2 million in 2003. Corporate expenses in 2003 include $6.1 million of severance-related expenses for the separation agreements of three former executives. Excluding these severance expenses, which we believe more appropriately reflects our core operations, corporate expenses would have been $22.1 million in 2003. Excluding these severance expenses, corporate expenses increased $5.5 million, or 25.1%, in 2004. The increase in corporate expenses was primarily due to $1.6 million of professional fees related to compliance with the requirements imposed by the Sarbanes-Oxley Act, a $1.3 million increase in tax, legal and other professional services, a $0.4 million increase in systems-related spending and $2.2 million of additional discretionary spending.

Restructuring charges were $0.6 million in 2004. The restructuring charges are explained in the preceding section captioned, *Restructuring charges.*

Net non-operating income (expense). The following table presents the components of our net non-operating income (expense) for 2004 and 2003, respectively:

Non-operating income (expense):	2004	2003	Change
		(in millions)	
Interest income	$ 2.6	$ 1.7	$ 0.9
Interest expense	(0.2)	(0.2)	—
Realized and unrealized gains (losses) on equity and warrant portfolio net of the consultants' share of the gains (losses):			
Realized gains on investments	57.0	0.7	56.3
Unrealized losses on derivative instruments	—	—	—
Net realized and unrealized gains	57.1	0.7	56.4
Other, net	(1.0)	(1.7)	0.7
Net non-operating income (expense)	$58.4	$ 0.5	$ 58.0

Note: Totals and subtotals may not equal the sum of individual line items due to rounding.

Interest income in 2004 was approximately $2.6 million compared to $1.7 million in 2003. The increase is primarily due to higher cash balances and higher returns on the invested cash.

We receive warrants for equity securities in client companies, in addition to the cash fee, for services rendered on some searches. Some of the warrants meet the definition of a derivative instrument under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and its subsequent amendments. SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument be recorded in the balance sheet as either an asset or liability measured at its fair value. These derivative instruments are initially recorded at their fair value, using the Black Scholes model, in the Consolidated Balance Sheets, with a corresponding amount recorded as net revenue in the Consolidated Statements of Operations. Compensation expense related to this net revenue is also recorded. Subsequent changes in the fair value of these derivative instruments are recorded in the Consolidated Statements of Operations as unrealized gains (losses), net of the consultants' share of the gains (losses).

Other warrants received and which do not meet the definition of a derivative instrument under SFAS No. 133 are initially recorded at their fair value, using the Black Scholes model, in the Consolidated Balance Sheets, with a corresponding amount recorded as net revenue in the Consolidated Statements of Operations. Compensation expense related to this net revenue is also recorded. These warrants are accounted for using the cost method, and subsequent changes in fair value are not recognized. However, these warrants are regularly reviewed for other-than-temporary declines in fair value. Any permanent declines in the fair value of these warrants are recorded in the Consolidated Statements of Operations as unrealized losses, net of the consultants' share of the losses.

Upon a value event such as an initial public offering or an acquisition, any changes in the fair value of the warrants, both derivatives and non-derivatives, are recorded in the Consolidated Statements of Operations as unrealized gains (losses), net of the consultants' share of the gains (losses).

Any equity securities arising from the exercise of a warrant are accounted for as available-for-sale investments in accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Subsequent changes in the fair value of these available-for-sale investments are recorded as a component of accumulated other comprehensive income (loss). Upon the sale of these investments, the Company records a realized gain (loss), net of the consultants' share of the gain (loss) and other costs.

In 2001, we received warrants to purchase 1,194,308 shares of Class B common stock of Google at a price of $0.30 per share issued in connection with recruitment fees. On August 19, 2004, we exercised the warrants pursuant to their cashless exercise feature and received 1,190,092 shares of Google common stock.

In multiple transactions on September 13, 2004 and September 14, 2004, we sold all the shares of common stock of Google that we held in ordinary brokerage transactions at an average price of $108.22 less expenses associated with the transaction resulting in aggregate net proceeds of approximately $128.8 million.

During 2004, we recognized realized gains of $57.0 million, net of the consultants' share of the gain and other costs, including $56.8 million related to the monetization of our shares of common stock of Google. During 2003, we recognized $0.7 million of realized gains and less than $0.1 million of unrealized gains, net of the consultants' share of the gains and other costs, related to our equity and warrant portfolio.

Net other non-operating expense was $1.0 million in 2004 compared to $1.7 million in 2003. Other non-operating expense consists primarily of foreign exchange gains and losses on intercompany balances which are denominated in currencies other than the functional currency and which are not considered permanent in nature.

Income taxes. In 2003, we had a pre-tax loss of $21.8 million and recorded income tax expense of $58.8 million. The 2003 income tax provision includes a non-cash income tax expense of $57.9 million, recorded in the fourth quarter of 2003, to provide a full valuation allowance against the net deferred tax assets for the U.S. and foreign operations which comprise the U.S. income tax entity.

Judgment is required in developing our income tax provision, including the determination of deferred tax assets and liabilities and any valuation allowances that might be required against the deferred tax assets. In assessing the need for a valuation allowance, we considered all positive and negative evidence, including scheduled reversals of deferred tax liabilities, tax-planning strategies, projected future taxable income and recent financial performance. In 2003, 2002 and 2001, we reported net losses, primarily due to restructuring activities necessary to align our cost structure with expected net revenue levels. SFAS No. 109, "Accounting for Income Taxes," states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years. In considering how the loss was created, evidence indicating that the loss was unusual, infrequent, or an aberration, rather than a continuing condition is an example of positive evidence that might support a conclusion that a valuation allowance is not needed when there is negative evidence. Until the fourth quarter of 2003, we considered the fact that the cumulative losses were primarily the result of the restructuring charges along with other positive evidence to be sufficient to support a conclusion that a valuation allowance was not needed. However, when we recorded a restructuring charge totaling $22.5 million in the fourth quarter of 2003, management no longer felt it appropriate, for purposes of SFAS No. 109, to regard the restructuring charges as unusual, infrequent, or as an aberration, based on the number of restructuring charges recorded from 2001 through 2003 and the magnitude of the charge taken in the fourth quarter of 2003. As a result, the significant negative evidence of cumulative losses in recent years could not be overcome by other positive evidence, most of which was subjective in nature. Based upon the provisions of SFAS No. 109, we recorded, in the fourth quarter of 2003, a full valuation allowance against our net deferred tax assets.

The income tax expense recorded in 2003 also includes an expense of $4.3 million, recorded in the first half of 2003, to reduce certain deferred tax assets, representing the excess of expense for accounting purposes over the deduction for tax purposes, required to be recorded upon the vesting of restricted stock units. In prior years, a portion of executive search consultant and management compensation was granted in restricted stock units at the then-average market price of approximately $39 per share. This price served as the basis for the compensation expense and the related tax benefit and deferred tax asset. The restricted stock units vested in 2003 at an average market price of approximately $12 per share. As this share price serves as the basis for the current tax deduction, we will realize a smaller tax benefit than initially recorded. Accordingly, we adjusted the deferred tax asset to reflect the lower tax benefit.

At the time we recorded a full valuation allowance against the net deferred tax assets, we anticipated that we would generate a loss for U.S. income tax purposes in 2004, due primarily to the timing of tax deductions related to restructuring charges recorded in prior years, and therefore did not anticipate recording or paying any U.S. federal income tax in 2004. These tax estimates excluded the affects of any warrant monetizations due to the uncertainty of the amount and timing of such transactions.

As a result of a significant warrant monetization in the third quarter of 2004, we generated income in 2004 for U.S. income tax purposes. Accordingly, we determined that a lesser valuation allowance is required related to net deferred tax assets associated with tax deductions that will be available for carryback to recover taxes paid in the current year and recorded a $10.5 million reduction to the income tax expense and the valuation allowance.

In 2004, the effective tax rate was 5.5%, which is significantly lower than the statutory rate, primarily as a result of the partial reduction of the previously recorded valuation allowance relating to net deferred tax assets associated with tax deductions that will be available for carryback to recover taxes paid in the current year and the utilization of net operating loss and capital loss carryforwards.

We anticipate that the effective tax rate will continue to fluctuate in the future due to the mix of earnings and profits in the jurisdictions in which we operate. While the Company expects to be profitable in 2005 and beyond, there is no assurance that future taxable income will be sufficient to realize the benefit of the deferred tax assets. If after future assessments of the realizability of the deferred tax assets, we determine a lesser allowance is required, we would record a reduction to the income tax expense and the valuation allowance in the period of such determination.

2003 Compared to 2002

Total revenue. Consolidated total revenue decreased $36.2 million, or 9.6%, to $340.6 million in 2003 from $376.8 million in 2002. The decline in total revenue was due primarily to the decline in revenue before reimbursements (net revenue).

Revenue before reimbursements (net revenue). Consolidated net revenue decreased $32.8 million, or 9.3%, to $317.9 million in 2003 from $350.7 million in 2002. Excluding the $17.9 million positive impact of exchange rate fluctuations, net revenue declined approximately 14%. We believe information regarding changes in net revenue excluding the impact of exchange rate fluctuations is helpful in providing an understanding of the volume of business activity. Most of our practices experienced declines in net revenue. In 2003, the number of confirmed executive searches decreased 5% to 3,757 from 3,973 in 2002. We believe this decrease reflects the impact of the continuing weak global economic conditions.

Net revenue in North America was $172.0 million in 2003, a decrease of $22.2 million, or 11.4%, from $194.2 million in 2002. Most of the practices experienced declines in net revenue with the most significant declines in the Technology and Financial Services practices. In Latin America, net revenue was $11.2 million in 2003, an increase of $0.2 million, or 2.0%, from $11.0 million in 2002, reflecting increases in the Financial Services and Professional Services practices, despite the loss of net revenue from operations that were converted to licensees in 2002. Net revenue in Europe was $113.0 million in 2003, a decrease of $11.4 million, or 9.1%, from $124.4 million in 2002. Excluding a positive impact of $16.5 million due to exchange rate fluctuations, Europe’s net revenue decreased by approximately 22% from 2002. The decline in net revenue is attributable to general economic weakness, particularly in the Financial Services and Industrial practices, and the loss of net revenue from unprofitable operations that were converted to licensees or shut down during 2002. In Asia Pacific, net revenue was $21.6 million in 2003, an increase of $0.5 million, or 2.6%, from $21.1 million in 2002. Excluding a positive impact of $1.3 million due to exchange rate fluctuations, Asia Pacific’s net revenue was $20.3 million, a decrease of approximately 3% compared to 2002. Increases in the Industrial and Consumer practices were more than offset by declines in the Technology and other practices.

Salaries and employee benefits. Consolidated salaries and employee benefits expense decreased $18.8 million, or 7.8%, to $223.5 million in 2003 from $242.3 million in 2002. Salaries and employee benefits expense in 2003 includes $6.1 million of expense related to the separation agreements of the former Chief Executive Officer, the former President and Chief Operating Officer and the Chief Financial Officer, approximately $2.8 million of other severance-related expenses, primarily in Europe and North America, partially offset by a $0.9 million reduction in employee benefit expense accruals and a benefit of $1.3 million from the reversal of accruals recorded in 2002 for the Performance Share Program. Excluding these items, which we believe more appropriately reflects our core operations, consolidated salaries and employee benefits expense would have been $216.8 million in 2003, a decrease of $25.5 million, or 10.5%, compared to $242.3 million in 2002. The decrease was primarily attributable to $35.8 million of lower fixed costs as a result of the elimination of approximately 400 positions since March 2002, partially offset by $10.3 million of additional performance-related compensation expense for executive search consultants and support staff. The average number of executive search consultants in 2003 was 328, a decrease of 16%, compared to an average of 391 in 2002.

As a percentage of net revenue, salaries and employee benefits expense increased to 70.3% in 2003 from 69.1% in 2002. Excluding the $8.9 million of severance-related expenses, the $0.9 million reduction of employee benefit accruals and the $1.3 million of benefit resulting from the reversal of accruals related to the Performance Share Program, which we believe more appropriately reflects our core operations, salaries and employee benefits expense as a percentage of net revenue would have been 68.2% in 2003 compared to 69.1% in 2002. The decrease as a percentage of net revenue is primarily due to lower fixed salaries and employee benefits expense in relation to the net revenue levels, partially offset by a greater percentage of net revenue accrued for performance-based compensation.

General and administrative expenses. Consolidated general and administrative expenses decreased $19.6 million, or 18.4%, to $87.3 million in 2003 from $106.9 million in 2002. This decrease was due to $11.5 million of lower discretionary spending, a reduction in bad debt expense of $2.8 million and $5.3 million of cost savings in rent, depreciation and other infrastructure expenses, primarily related to the consolidation and closing of offices and lower systems-related spending.

As a percentage of net revenue, general and administrative expenses decreased to 27.4% in 2003 from 30.5% in 2002.

2003 and 2002 Restructuring charges. In 2003, we recorded restructuring charges of $29.4 million. In 2002, we recorded restructuring charges of $48.5 million. The following table summarizes the workforce reductions as well as the restructuring charges recorded in each year:

	Employee Reductions			Restructuring Charges		
2003 and 2002 Restructuring Charges:	**Consultants**	**All Other**	**Total**	**Employee-related**	**Office-related**	**Total**
					(in millions)	
Restructuring Charges Recorded in 2003:						
Q1 2003	—	—	—	$ —	$ 5.5	$ 5.5
Q3 2003	—	—	—	—	1.4	1.4
Q4 2003	7	25	32	3.9	18.6	22.5
Total	7	25	32	$ 3.9	$25.5	$29.4
Restructuring Charges Recorded in 2002:						
Q1 2002	51	115	166	$ 10.4	$12.8	$23.2
Q4 2002	61	175	236	12.2	13.2	25.4
Total	112	290	402	$ 22.6	$26.0	$48.5

Note: Totals and subtotals may not equal the sum of individual line items due to rounding.

The restructuring charges of $29.4 million recorded in 2003 include severance and other employee-related costs of $3.9 million related to reductions in our workforce, primarily in Europe, expense of $22.2 million to increase accruals for leased properties that had been identified as excess in previous office consolidation charges and $3.3 million of expense for impairment of goodwill and other intangible assets related primarily to a wholly-owned subsidiary in Finland which is expected to be converted to a licensee. The workforce reductions, which occurred during the fourth quarter of 2003, affected 32 people, primarily in Europe, and included 7 executive search consultants. The accruals for excess real estate were increased to reflect the expectation of longer vacancy periods due primarily to weakness in the real estate markets in which the leased properties are located. The restructuring charges by segment are as follows: North America $7.0 million; Europe $22.1 million; and Corporate $0.3 million. Of the $29.4 million of restructuring charges recorded in 2003, approximately $25.8 million represents cash charges.

In October 2001, we announced company-wide cost reduction initiatives to better align costs with the expected net revenue levels. During the first quarter of 2002, we recorded $23.2 million of restructuring charges related to these announced initiatives. The actions, which occurred during the first quarter of 2002, affected 166 people, including 51 executive search and management search consultants. The remainder was search and corporate support staff. Over two-thirds of the layoffs were in North America, 20% were in Europe, and the rest were in Latin America and Asia Pacific. The 2002 first quarter restructuring charges include severance and other employee-related costs of $10.4 million and costs related to the consolidation and closing of offices of $12.8 million. By segment, the restructuring charges recorded in the first quarter of 2002 are as follows: North America $13.3 million; Latin America $0.1 million; Europe $7.0 million; Asia Pacific $0.3 million; and Corporate $2.5 million. Of the $23.2 million of restructuring charges recorded in the 2002 first quarter, approximately $15.2 million represents cash charges. No restructuring charges were recorded in the second or third quarters of 2002.

In October 2002, we announced additional reductions in our workforce and the consolidation and closing of offices, recording a charge of $25.4 million. The actions affected 236 employees, of which 156 were in Europe. Of the reductions, 61 were executive and management search consultants and the remainder was support staff. Of the $25.4 million restructuring charge, $12.2 million was for severance and related costs, $10.6 million was facilities-related and $2.6 million was for the write-off of goodwill, intangible assets and software. By segment, the restructuring charges recorded in the fourth quarter of 2002 are as follows: North America $6.4 million; Latin America $0.5 million; Europe $17.7 million; Asia Pacific $0.4 million; and Corporate $0.4 million. Of the $25.4 million of restructuring charges recorded in the 2002 fourth quarter, approximately $20.9 million represents cash charges.

Approximately $45.8 million of the 2003 and 2002 restructuring charges remained unpaid as of December 31, 2003. The majority of the amounts remaining to be paid relate to real estate leases. Cash disbursements lag the charges because charges related to disposing of leases are recorded currently, while the cash spending for each affected lease will continue until sub-leasing, or negotiations with the lessor to terminate the lease, are completed. Based on current estimates, approximately $18.1 million is expected to be paid in 2004, with the remaining $27.7 million payable in years subsequent to 2004.

Operating loss. Our consolidated operating loss was $22.3 million in 2003, a decrease of $24.8 million compared to the operating loss of $47.1 million in 2002. The following table summarizes our consolidated operating loss for the years ended December 31, 2003 and 2002, respectively:

Operating income (loss):	**2003**	**2002**	**Change**
		(in millions)	
Total regions	$ 35.3	$ 29.2	$ 6.1
Corporate	(28.2)	(27.8)	(0.4)
Operating income before restructuring charges	7.1	1.5	5.7
Restructuring charges	(29.4)	(48.5)	19.1
Consolidated operating loss	$ (22.3)	$ (47.1)	$ 24.8

Note: Totals and subtotals may not equal the sum of individual line items due to rounding.

The decrease in the consolidated operating loss was primarily due to lower restructuring charges and improved profitability in the geographic regions.

In North America, operating income in 2003 increased $2.3 million to $36.0 million from $33.7 million in 2002. The decline of $22.2 million in North America's net revenue was offset by $18.0 million of lower fixed salaries and employee benefits expense, including a benefit from the forfeiture of certain restricted stock units and a reduction of accruals for employee benefits expense, a benefit of $0.6 million related to the reversal of accruals for the Performance Share Program which were recorded in 2002 and $9.5 million of lower discretionary spending and lower facilities-related expenses. Most of the cost savings are attributable to the reductions in workforce, and the consolidation and closing of offices, that have occurred since the 2002 first quarter. The cost reductions were offset by a $3.6 million increase in performance-based compensation expense for executive search consultants and support staff.

In Latin America, operating income was $0.9 million in 2003 compared to an operating loss of $2.8 million in 2002. The operating loss in 2002 included $1.7 million of costs associated with converting certain wholly- owned subsidiaries to licensees and an adjustment for value-added taxes.

In Europe, the operating loss was $3.8 million in 2003, an increase of $0.6 million, compared to an operating loss of $3.2 million in 2002. The operating loss in 2003 includes approximately $2.0 million of severance-related expenses. Excluding these severance-related expenses, which we believe more appropriately

reflects our core operations, Europe's operating loss in 2003 would have been $1.9 million, a decrease of $1.3 million, compared to the $3.2 million operating loss in 2002. The decline in net revenue of $11.4 million was offset by $10.4 million of lower fixed salaries and employee benefits expense, a reduction in bad debt expense of $2.7 million, $2.8 million of lower discretionary spending and approximately $2.2 million of lower systems-related spending. These cost savings reflect the reductions in workforce and cost reduction initiatives which have occurred since the first quarter of 2002. These cost savings were partially offset by a $5.4 million increase in performance-based compensation expense for executive search consultants and support staff.

In Asia Pacific, operating income in 2003 was $2.3 million, an increase of $0.8 million, compared to operating income of $1.5 million in 2002. The increase was attributable to the increase in net revenue of $0.5 million and lower fixed salaries and employee benefits expense.

Unallocated corporate expenses increased $0.4 million, or 1.4%, to $28.2 million in 2003 from $27.8 million in 2002. Corporate expenses in 2003 include $6.1 million of severance-related expenses for the separation agreements of three executives. Excluding these severance expenses, which we believe more appropriately reflects our core operations, unallocated corporate expenses would have been $22.1 million, a decrease of $5.7 million, or 20.5%, compared to 2002. This decline in corporate expenses reflects $3.2 million of lower salaries and employee benefits expense and $3.8 million of lower systems-related spending and operating expenses, partially offset by $1.3 million of higher infrastructure-related costs.

Restructuring charges were $29.4 million in 2003 compared to $48.5 million in 2002. The restructuring charges are explained in the preceding section captioned, *2003 and 2002 Restructuring charges.*

Net non-operating income (expense). The following table presents the components of our net non-operating income (expense) for 2003 and 2002, respectively:

Non-operating income (expense):	2003	2002	Change
		(in millions)	
Interest income	$ 1.7	$ 2.0	$ (0.3)
Interest expense	(0.2)	(0.2)	—
Realized and unrealized gains (losses) on equity and warrant portfolio:			
Realized gains on investments	0.7	1.6	(0.9)
Unrealized losses on derivative instruments	—	(3.0)	3.0
Net realized and unrealized gains (losses)	0.7	(1.3)	2.0
Write-down of long-term investment	—	(5.0)	5.0
Other, net	(1.7)	(0.1)	(1.6)
Net non-operating income (expense)	$ 0.5	$(4.6)	$ 5.1

Note: Totals and subtotals may not equal the sum of individual line items due to rounding.

Interest income in 2003 was approximately $1.7 million compared to $2.0 million in 2002. The decline is primarily due to lower returns on invested cash balances.

We receive warrants for equity securities in our client companies, in addition to our cash fee, for services rendered on some searches. The warrants are recorded at fair value. Some of the warrants in our portfolio meet the definition of a derivative instrument under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and its subsequent amendments. In accordance with SFAS No. 133, subsequent changes in the fair value of these derivative instruments are recorded in the Consolidated Statements of Operations rather than as a component of accumulated other comprehensive income. Warrants which do not meet the definition of a derivative instrument are regularly reviewed for declines in value. Upon a value event such as an initial public

offering or an acquisition, the equity securities arising from the exercise of the warrants are monetized, resulting in a realized gain, net of the consultants' share of the gain and other costs.

During 2003, we recognized $0.7 million of realized gains and less than $0.1 million of unrealized losses, net of the consultants' share of the gains (losses) and other costs, related to our equity and warrant portfolio. During 2002, we recognized $1.6 million of realized gains and $3.0 million of unrealized losses, net of the consultants' share of the gains (losses) and other costs, related to our equity and warrant portfolio. With improvements in economic conditions, it is possible, although not certain, that we could realize gains which are significant to our reported earnings in the future.

The write-down of the long-term investment of $5.0 million in 2002 resulted from the write-down of the remainder of our investment in ETF Group. ETF Group is a Europe-based venture capital firm that helps emerging companies expand into international markets.

Net other non-operating expense was $1.7 million in 2003 compared to $0.1 million in 2002. Other non-operating expense consists primarily of exchange gains and losses on intercompany balances which are denominated in currencies other than the functional currency and which are not considered permanent in nature.

Income taxes. In 2003, we had a pre-tax loss of $21.8 million and recorded income tax expense of $58.8 million. The 2003 income tax provision includes a non-cash income tax expense of $57.9 million, recorded in the fourth quarter of 2003, to provide a full valuation allowance against the net deferred tax assets for the U.S. and foreign operations which comprise the U.S. income tax entity.

Judgment is required in developing our income tax provision, including the determination of deferred tax assets and liabilities and any valuation allowances that might be required against the deferred tax assets. In assessing the need for a valuation allowance, we considered all positive and negative evidence, including scheduled reversals of deferred tax liabilities, tax-planning strategies, projected future taxable income and recent financial performance. In 2003, 2002 and 2001, we reported net losses, primarily due to restructuring activities necessary to align our cost structure with expected net revenue levels. SFAS No. 109, "Accounting for Income Taxes," states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years. In considering how the loss was created, evidence indicating that the loss was unusual, infrequent, or an aberration, rather than a continuing condition is an example of positive evidence that might support a conclusion that a valuation allowance is not needed when there is negative evidence. Until the fourth quarter of 2003, we considered the fact that the cumulative losses were primarily the result of the restructuring charges along with other positive evidence to be sufficient to support a conclusion that a valuation allowance was not needed. However, when we recorded a restructuring charge totaling $22.5 million in the fourth quarter of 2003, management no longer felt it appropriate, for purposes of SFAS No. 109, to regard the restructuring charges as unusual, infrequent, or as an aberration, based on the number of restructuring charges recorded from 2001 through 2003 and the magnitude of the charge taken in the fourth quarter of 2003. As a result, the significant negative evidence of cumulative losses in recent years could not be overcome by other positive evidence, most of which was subjective in nature. Based upon the provisions of SFAS No. 109, we recorded, in the fourth quarter of 2003, a full valuation allowance against our net deferred tax assets.

The income tax expense recorded in 2003 also includes an expense of $4.3 million, recorded in the first half of 2003, to reduce certain deferred tax assets, representing the excess of expense for accounting purposes over the deduction for tax purposes, required to be recorded upon the vesting of restricted stock units. In prior years, a portion of executive search consultant and management compensation was granted in restricted stock units at the then-average market price of approximately $39 per share. This price served as the basis for the compensation expense and the related tax benefit and deferred tax asset. The restricted stock units vested in 2003 at an average market price of approximately $12 per share. As this share price serves as the basis for the current tax deduction, we will realize a smaller tax benefit than initially recorded. Accordingly, we adjusted the deferred tax asset to reflect the lower tax benefit.

In 2002, we had a pre-tax loss of $51.7 million and an income tax benefit of $11.5 million. The effective tax benefit rate in 2002 was 22.2%, reflecting valuation allowances related to the recoverability of foreign tax credits, foreign net operating losses and other tax-related allowances. In addition, the income tax benefit in 2002 is reduced by approximately $0.8 million of additional provision for income taxes in certain Latin American subsidiaries. The income tax provision and related current and deferred tax balances are more fully described in Note 17, *Income Taxes*, in the Notes to Consolidated Financial Statements.

Liquidity and Capital Resources

General. We continually evaluate our liquidity requirements, capital needs and availability of capital resources based on our operating needs. We believe that our existing cash balances together with the funds expected to be generated from operations and funds available under our committed line of credit will be sufficient to finance our operations for the foreseeable future, as well as to finance the cash payments associated with our restructuring charges. We historically have paid a portion of our bonuses in December and the remainder in March. Employee bonuses are accrued throughout the year and are based on our performance and the performance of the individual employee. Our ability to undertake acquisitions may depend, in part, on access to additional funds.

In 2001, we received warrants to purchase 1,194,308 shares of Google at a price of $0.30 per share issued in connection with recruitment fees. On August 19, 2004, we exercised the warrants pursuant to their cashless exercise feature and received 1,190,092 shares of Google common stock.

In multiple transactions on September 13, 2004 and September 14, 2004, we sold all the shares of common stock of Google that we held in ordinary brokerage transactions at an average price of $108.22 less expenses associated with the transaction resulting in aggregate net proceeds of approximately $128.8 million.

Pursuant to the terms of our compensation policy with respect to warrants, 55% of the net proceeds from these sales of shares of common stock of Google is payable to our consultants involved with the search in the month following the monetization. Our current Chief Executive Officer, Thomas J. Friel, was a member of this search team and will receive 25% of the consultants' team share. Mr. Friel has elected to defer receipt of his share of the net proceeds until 2005 under an existing deferred compensation plan. The remaining 75% of the consultants' team share of the net proceeds, approximately $53.1 million, was paid in October 2004.

We do not have material off-balance sheet arrangements, special purpose entities, trading activities of non-exchange traded contracts or transactions with related parties.

Some deferred compensation arrangements with certain employees, which were executed prior to July 30, 2002, are structured as forgivable loans. The forgivable loans are accounted for as deferred compensation, and are therefore amortized to compensation expense over the forgiveness period. At December 31, 2004, we had $0.3 million of deferred compensation structured as forgivable loans, none of which were with any executive officer of the Company.

Lines of credit. In December 2003, the Company entered into a $60.0 million committed revolving credit facility the ("Facility"). The Facility replaced a $50.0 million committed revolving credit facility and a $5.0 million uncommitted credit facility. Under this Facility, the Company may borrow U.S. dollars, euros, sterling and other major traded currencies, as agreed by the banks. Borrowings under the Facility bear interest at the existing Alternate Base Rate or LIBOR plus a margin as determined by the Company's compliance with certain tests of financial condition. The Facility has financial tests the Company must meet or exceed relating to:

- fixed charge coverage (defined as consolidated EBITDAR minus consolidated capital expenditures to consolidated interest expense plus consolidated rental obligations plus restricted payments.) (EBITDAR is defined as earnings before interest expense, taxes, depreciation, amortization and rental expense plus interest income);

- leverage (defined as consolidated total indebtedness to consolidated EBITDA plus interest income);
- current ratio (defined as current assets divided by current liabilities); and
- net worth.

The Facility sets limits on the Company's ability to make acquisitions without bank approval and to incur additional debt outside of the Facility. The Company must pay a facility fee whether or not the Facility is used during the year.

In March 2004, the Company amended the Facility to reduce the net worth covenant from $145.0 million to $110.0 million. This amendment was required as a result of the non-cash income tax expense of $57.9 million, recorded in the fourth quarter of 2003, which provided a full valuation allowance for the net deferred tax assets related to the U.S. and foreign operations which comprise the U.S. income tax entity. See Note 17, *Income Taxes*, in the Notes to Consolidated Financial Statements.

There were no borrowings outstanding under the lines of credit existing at December 31, 2004 or December 31, 2003, nor were there any borrowings during the years ended December 31, 2004 and 2003, respectively, under the then existing lines of credit. At December 31, 2004, the Company was in compliance with the financial covenants of the Facility, and no event of default existed.

Cash and cash equivalents. Cash and cash equivalents at December 31, 2004 were $222.8 million, an increase of $103.5 million, compared to $119.3 million at December 31, 2003.

Cash from operating activities. In 2004, cash provided by operating activities was $25.7 million, primarily as a result of our net income adjusted for non-cash items, offset by payments related to the restructuring charges.

In 2003, cash provided by operating activities was $10.4 million, reflecting our net loss, adjusted for non-cash items, a $12.9 million reduction of net income taxes recoverable, which includes the refund of approximately $15.0 million of U.S. income taxes paid in prior years arising from the carryback of net operating losses, partially offset by payments related to our restructuring charges and payments of bonuses in March and December 2003.

In 2002, cash provided by operating activities was $6.0 million, reflecting our net loss adjusted for non-cash items, a reduction of our trade receivables, and the $16.6 million reduction of net income taxes recoverable, which includes the refund of approximately $25.0 million of U.S. income taxes paid in prior years arising from the carryback of net operating losses to prior years and the recovery of estimated taxes paid in the first half of 2001, partially offset by the payments related to our restructuring charges and payment of bonuses in March 2002 and December 2002.

Cash from investing activities. Cash provided by investing activities was $68.4 million in 2004 primarily as a result of the net proceeds of $128.8 million from the sale of our shares of common stock of Google offset by the portion of the consultants' share of the gain which was paid in 2004. Cash used in investing activities was $4.7 million in 2003 and $3.9 million in 2002 primarily due to capital expenditures, partially offset by net proceeds from sales of equity securities.

Capital expenditures were $6.0 million, $5.8 million and $5.2 million in 2004, 2003 and 2002, respectively. Capital expenditures were primarily for computer equipment and software. We anticipate that our capital expenditures for 2005 will be approximately $6 million to $7 million.

During 2004, 2003 and 2002, the amount of cash received from the sale of equity securities related to our warrant program, net of the consultants' share of the gain and other costs, was $74.3 million, $0.7 million and $1.5 million, respectively. A portion of the consultants' share of the gain related to the sale of equity securities in 2004, approximately $17 million, will be paid in 2005.

Cash from financing activities. Cash from financing activities was $5.5 million in 2004. Cash used in financing activities was $2.0 million in 2003 and $1.8 million in 2002. The cash from financing activities in 2004 was primarily the result of proceeds from the exercise of stock options offset by repurchases of our common stock. The cash used in financing activities in 2003 and 2002 is primarily for repurchases of our common stock and payments on debt related to acquisitions of executive search firms.

The repurchases of our common stock in 2002 and 2003 were made in accordance with the March 6, 2001 Board of Directors' authorization for management to repurchase up to an aggregate of 2 million shares of our common stock with an aggregate purchase price up to $100 million through March 5, 2003. From February 25, 2003 through March 5, 2003, we repurchased 288,000 shares of common stock for $3.2 million. During 2002, we purchased 4,032 shares of common stock for $0.1 million.

On May 22, 2003, our Board of Directors authorized management to repurchase up to an aggregate of 1 million shares of our common stock with an aggregate purchase price up to $20 million through May 21, 2005. No purchases of our common stock were made under this authorization.

On October 22, 2004, our Board of Directors authorized management to repurchase shares of our common stock with an aggregate purchase price up to $30 million. Also at this time, the previous authorization to purchase up to $20 million through May 21, 2005 was cancelled. We have purchased 85,000 shares of our common stock for $2.5 million under this authorization through December 31, 2004.

Contractual obligations. The following table presents our known contractual obligations as of December 31, 2004 and the expected timing of cash payments related to these contractual obligations:

	Payments due for the years ended December 31,				
Contractual obligations:	**Total**	**2005**	**2006 and 2007**	**2008 and 2009**	**Thereafter**
			(in millions)		
Office space and equipment lease obligations (1)	$152.9	$31.8	$54.6	$43.5	$ 23.0
Accrued restructuring charges—severance (2)	2.4	1.8	0.6	—	—
Asset retirement obligations (3)	1.5	—	0.2	1.3	—
Executives' separation agreements (4)	0.1	0.1	—	—	—
Consultants' share of warrant monetization (5)	17.4	17.4	—	—	—
Total	$174.3	$51.1	$55.4	$44.8	$ 23.0

(1) See Note 20, *Commitments and Contingencies*, in the Notes to Consolidated Financial Statements for additional information.

(2) See Note 14, *Restructuring Charges*, in the Notes to Consolidated Financial Statements for additional information.

(3) Represents the fair value of the obligation associated with a retirement of tangible long-lived assets, primarily related to our obligation at the end of the lease term to return office space to the landlord in its original condition. The obligation is recorded in accordance with SFAS No. 143, "Accounting for Asset Retirement Obligations."

(4) Represents obligations for separation payments related to the resignation of our former Chief Financial Officer.

(5) As a result of a significant warrant monetization in 2004, our Chief Executive Officer, Thomas J. Friel, will receive $17.4 million representing his share of the gain. Mr. Friel has elected to defer until 2005 receipt of his share of the net proceeds under an existing deferred compensation plan. See Note 15, *Significant Warrant Monetization*, in the Notes to Consolidated Financial Statements.

In addition to the contractual obligations included in the above table, we have liabilities related to certain employee benefit plans. These liabilities are recorded in our Consolidated Balance Sheet at December 31, 2004. The obligations related to these employee benefit plans are described in Note 9, *Employee Benefit Plans*, and Note 10, *Pension Plan and Life Insurance Contract.* As the timing of cash disbursements related to these employee benefit plans is uncertain, we have not included these obligations in the above table.

Application of Critical Accounting Policies and Estimates

General. Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our Consolidated Financial Statements, which have been prepared in accordance with generally accepted accounting principles in the United States. Our significant accounting policies are discussed in Note 2, *Summary of Significant Accounting Policies*, in the Notes to Consolidated Financial Statements. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. If actual amounts are ultimately different from previous estimates, the revisions are included in our results of operations for the period in which the actual amounts become known.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used, or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact the financial statements. Management believes the following critical accounting policies reflect its more significant estimates and assumptions used in the preparation of the Consolidated Financial Statements:

Revenue recognition. Revenue before reimbursements for out-of-pocket expenses ("net revenue") is recognized when earned and realizable and therefore when the following criteria have been met: (a) persuasive evidence of an arrangement exists; (b) services have been rendered; (c) the fee to our client is fixed or determinable; and (d) collectibility is reasonably assured. Net revenue consists of retainers and indirect expenses billed to clients. Typically, we are paid a retainer for our executive search services equal to approximately one-third of the estimated first year compensation of the position to be filled. If actual compensation of the placed candidate exceeds the estimated compensation, we are generally authorized to bill the client for one-third of the excess. Net revenue from executive search engagements is recognized over the expected average period of performance, in proportion to the estimated personnel time incurred to fulfill our obligations under the arrangements. Net revenue in excess of the retainer, resulting from actual compensation of the placed candidate exceeding estimated compensation, is recognized upon completion of the executive search when the amount of the additional fee is known. Our assumptions about the duration of the time and extent of efforts for search teams to complete our services in an executive search engagement require significant judgment as these variables have fluctuated in the past and are expected to continue to do so. These assumptions are updated annually or whenever conditions exist to indicate that more frequent updates are necessary.

Accruals related to the consolidation and closing of offices recorded as part of our restructuring charges. In 2001, we began the restructuring of our business to better align costs with expected net revenue levels. These initiatives included the consolidation and closing of offices where we had long-term leases. At the time of the office closings and consolidations, we accrued the estimated costs associated with these actions. For initiatives which were announced prior to January 1, 2003, the accruals were established in accordance with EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." For cost reduction initiatives announced in the fourth quarter of 2003, the accruals were established in accordance with SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities."

Inherent in these accruals are estimates concerning vacancy periods, expected sublease income, and costs to terminate the leases. These accruals are periodically updated to reflect information concerning the commercial real estate markets in which the offices are located. During 2003, we recorded $22.2 million of restructuring

charges to increase accruals for leased properties that had been identified as excess in previous office consolidation charges. During 2004, we recorded $0.6 million of restructuring charges to reflect changes in lease estimates primarily due to a tenant default on a sublease and the final determination and payment of certain severance related restructuring accruals. We believe that the accounting estimate related to accruals for the consolidation and closing of offices is a critical accounting estimate because it is highly susceptible to changes in the commercial real estate markets and the local regional economic factors where this leased office space is located.

Income taxes. Deferred taxes are recognized for the future tax effects of temporary differences between financial and income tax reporting using tax rates in effect for the years in which the differences are expected to reverse. In assessing the realizability of deferred tax assets, we consider 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.

Judgment is required in developing our income tax provision, including the determination of deferred tax assets and liabilities and any valuation allowances that might be required against the deferred tax assets. In assessing the need for a valuation allowance, we consider all positive and negative evidence, including scheduled reversals of deferred tax liabilities, tax-planning strategies, projected future taxable income and recent financial performance. We reported net losses in 2003, 2002 and 2001, primarily as a result of recording restructuring charges in connection with aligning our cost structure with expected net revenue levels. SFAS No. 109, “Accounting for Income Taxes,” states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years. In considering how the loss was created, evidence indicating that the loss was unusual, infrequent, or an aberration, rather than a continuing condition is an example of positive evidence that might support a conclusion that a valuation allowance is not needed when there is negative evidence. Until the fourth quarter of 2003, we considered the fact that the cumulative losses were primarily the result of the restructuring charges along with other positive evidence to be sufficient to support a conclusion that a valuation allowance was not needed. However, when we recorded a restructuring charge totaling $22.5 million in the fourth quarter of 2003, management no longer felt it appropriate, for purposes of SFAS No. 109, to regard the restructuring charges as unusual, infrequent, or as an aberration, based on the number of restructuring charges recorded in the last three years and the magnitude of the charge taken in the fourth quarter of 2003. As a result, the significant negative evidence of cumulative losses in recent years could not be overcome by other positive evidence, most of which was subjective in nature. Based upon the provisions of SFAS No. 109, we recorded, in the fourth quarter of 2003, a non-cash income tax expense of $57.9 million, providing a full valuation allowance against the net deferred tax assets for the U.S. and foreign operations which comprise the U.S. income tax entity.

At the time we recorded a full valuation allowance against the net deferred tax assets, we anticipated that we would generate a loss in 2004 for U.S. income tax purposes, due primarily to the timing of tax deductions related to restructuring charges recorded in prior years, and therefore did not anticipate recording or paying any U.S. federal income tax in 2004. These tax estimates excluded the affects of any warrant monetizations due to the uncertainty of the amount and timing of such transactions.

As a result of a significant warrant monetization in the third quarter of 2004, we generated income in 2004 for U.S. income tax purposes. Accordingly, we determined that a lesser valuation allowance is required related to net deferred tax assets associated with tax deductions that will be available for carryback to recover taxes paid in the current year and recorded a $10.5 million reduction to the income tax expense and the valuation allowance.

We anticipate that the effective tax rate will continue to fluctuate in the future due to the mix of earnings and profits in the jurisdictions in which we operate. While the Company expects to be profitable in 2005 and beyond, there is no assurance that future taxable income will be sufficient to realize the benefit of the deferred tax assets. If after future assessments of the realizability of the deferred tax assets, we determine a lesser

allowance is required, we would record a reduction to the income tax expense and the valuation allowance in the period of such determination.

We believe that the accounting estimate related to our income tax provision, deferred tax assets and liabilities and income taxes payable and recoverable is a critical accounting estimate because it is highly susceptible to our ability to generate taxable income in future years and to adequately provide for potential income tax-related liabilities.

Goodwill and other intangible assets. We review goodwill for impairment annually and whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable in accordance with SFAS No. 142, “Goodwill and Other Intangible Assets.” The goodwill impairment test compares the fair value of a reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, goodwill of the reporting unit would be considered impaired. To measure the amount of the impairment loss, the implied fair value of a reporting unit’s goodwill is compared to the carrying amount of that goodwill. If the carrying amount of a reporting unit’s goodwill exceeds the implied fair value of that goodwill, an impairment loss shall be recognized in an amount equal to that excess. The implied fair value of goodwill shall be determined in the same manner as the amount of goodwill recognized in a business combination is determined. The fair value of each of the Company’s reporting units was determined using a combination of valuation techniques, including a discounted cash flow methodology and comparable public company methodology, with the assistance of an independent valuation firm.

The discounted cash flow approach is dependent on a number of factors including estimates of future market growth and trends, forecasted revenue and costs, capital investments, appropriate discount rates, certain assumptions to allocate shared assets and liabilities, and other variables to calculate the carrying values for each of our reporting units. We base our fair value estimates on assumptions we believe to be reasonable, but which are unpredictable and inherently uncertain. Actual future results may differ from those estimates. These assumptions are updated annually, at a minimum, to reflect information concerning our reportable segments.

In accordance with SFAS No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets,” long-lived assets, such as property, equipment, and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge, equal to the amount by which the carrying amount of the asset exceeds the fair value of the asset, is recognized.

We believe that the accounting estimate related to goodwill and other intangible asset impairment is a critical accounting estimate because the assumptions used are highly susceptible to changes in the operating results and cash flows of our reportable segments.

Allowance for doubtful accounts. Accounts receivable from our customers are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is our best estimate of the amount of probable credit losses in existing accounts receivable balances. We determine the allowance for doubtful accounts through an analysis of several factors, including the aging of our accounts receivable, historical write-off experience, and specific account analyses. We consider current and projected economic conditions and historical trends when determining the allowance for doubtful accounts. Actual collections of accounts receivable could differ from our estimates due to changes in future economic or industry conditions or specific customers’ financial condition.

Recently Issued Financial Accounting Standards

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (revised 2004), "Share-Based Payment" (SFAS No. 123R). This statement requires that the costs of employee share-based payments be measured at fair value on the awards grant date using an option-pricing model and recognized in the financial statements over the requisite service period. SFAS No. 123R supersedes APB 25 and its related interpretations, and eliminates the alternative use of an intrinsic value method of accounting under APB 25, which we are currently using. The effective date for us is the beginning of the third quarter of 2005. We are currently evaluating the impact that the adoption of SFAS No. 123R will have on our financial condition and results of operations and anticipate that the application of the expensing provisions of SFAS 123R will be relatively consistent with the expense that we have historically disclosed in pro-forma disclosures required by SFAS 123.

In December 2004, the FASB issued Staff Position No. 109-2, "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004". The American Jobs Creation Act of 2004 ("FSP 109-2"), signed into law on October 22, 2004, provides for a special one-time tax deduction, or dividend received deduction ("DRD"), of 85% of qualifying foreign earnings that are repatriated in either a company's last tax year that began before the enactment date or the first tax year that begins during the one-year period beginning on the enactment date. FSP 109-2 provides entities additional time to assess the effect of repatriating foreign earnings under the Act for purposes of applying SFAS No. 109, "Accounting for Income Taxes," which typically requires the effect of a new tax law to be recorded in the period of enactment. We do not anticipate applying the special one-time tax deduction or DRD to repatriate foreign earnings during 2005.

In March 2004, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairments and Its Application to Certain Investments" (EITF 03-1). EITF 03-1 provides a three-step impairment model for determining whether an investment is other-than-temporarily impaired and requires the recognition of such impairments as an impairment loss equal to the difference between the investments cost and fair value at the reporting date. The effective date for us was the beginning of the third quarter 2004. In September 2004, the FASB issued Staff Position No. EITF Issue 03-1-1, "Effective Date of Paragraphs 10-20 of EITF Issue No. 03-01, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" (FSP EITF 03-1-1), which delayed the effective date for the measurement and recognition guidance contained in EITF 03-1-1; however did not change the disclosure requirements. The adoption of EITF 03-1 impacted the disclosures related to our investments in 2004 and is not expected to have a material impact on our financial condition or results of operations.

In December 2003, the FASB issued FASB Interpretation No. 46 (revised December 2003), "Consolidation of Variable Interest Entities," which addresses how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity. This Interpretation replaced FASB Interpretation No. 46, "Consolidation of Variable Interest Entities," which was issued in January 2003. We currently do not have any controlling financial interests that are within the scope of this Interpretation.

In December 2003, the FASB issued SFAS No. 132 (revised 2003), "Employers' Disclosures about Pensions and Other Postretirement Benefits" (SFAS No. 132R). The disclosure requirements of SFAS 132R require more complete information in both annual and interim financial statements about pension and postretirement benefits as well as increase the transparency of the financial reporting related to those plans and benefits. Except as noted, the revised disclosure requirements are effective for financial statements with fiscal years ending after December 15, 2003. The interim-period disclosures relating to net periodic benefit cost required by the revised Statement are effective for interim periods beginning after December 15, 2003. We adopted the interim-period disclosure requirements of SFAS 132 related to net periodic benefit cost on January 1, 2004. The additional disclosure of information about employer contributions related to foreign plans required by the revised statement is effective for fiscal years ending after June 15, 2004 and interim periods beginning with

the first quarter of 2005. The adoption of SFAS No. 132R impacted the disclosures related to our foreign pension plan in 2004 and will further impact the disclosures in 2005, and is not expected to have a material impact on our financial condition or results of operations.

Quarterly Financial Information

The following table sets forth certain financial information for each quarter of 2004 and 2003. The information is derived from our quarterly consolidated financial statements which are unaudited but which, in the opinion of management, have been prepared on the same basis as the audited annual consolidated financial statements included in this document. The consolidated financial data shown below should be read in conjunction with the consolidated financial statements and notes thereto. The operating results for any quarter are not necessarily indicative of results for any future period.

	Quarter Ended							
	2004				2003			
	March 31	June 30	Sept. 30	Dec. 31	March 31	June 30	Sept. 30	Dec. 31
Revenue before reimbursements (net revenue)	$ 87,229	$ 97,926	$ 91,607	$98,670	$ 77,311	$ 81,674	$ 76,941	$ 82,008
Operating income (loss) before restructuring charges	5,113	8,603	8,196	7,298	599	(1,641)	4,712	3,477
Restructuring charges	—	—	—	550(1)	5,500(2)	—	1,413(3)	22,530(4)
Operating income (loss)	5,113	8,603	8,196	6,748	(4,901)	(1,641)	3,299	(19,053)
Income (loss) before income taxes	5,161	9,643	65,451(5)	6,844	(5,041)	(1,520)	3,976	(19,239)
Provision for (benefit from) income taxes	936	2,717	3,302	(2,164)(6)	1,696	1,089	2,924	53,135(7)
Net income (loss)	4,225	6,926	62,149	9,008	(6,737)	(2,609)	1,052	(72,374)
Basic earnings (loss) per common share	0.23	0.36	3.25	0.47	(0.37)	(0.14)	0.06	(3.95)
Diluted earnings (loss) per common share	0.22	0.34	3.08	0.44	(0.37)	(0.14)	0.05	(3.95)

(1) During the fourth quarter of 2004, we recorded $0.6 million of restructuring charges to reflect changes in lease estimates primarily due to a tenant default on a sublease and the final determination and payment of certain severance related restructuring accruals.

(2) During the first quarter of 2003, we recorded $5.5 million of restructuring charges to increase accruals for leased properties that had been identified as excess in previously announced cost reduction initiatives.

(3) During the third quarter of 2003, we recorded $1.4 million of restructuring charges to increase accruals for leased properties that had been identified as excess in previously announced cost reduction initiatives.

(4) During the fourth quarter of 2003, we recorded $22.5 million of restructuring charges for severance related to reductions in our workforce, to increase accruals for leased properties that had been identified as excess in previously announced cost reduction initiatives, and to write-off goodwill and other intangible assets primarily related to a wholly-owned subsidiary in Finland which was converted to a licensee.

(5) During the third quarter of 2004, we recognized a realized gain of $57.0 million, net of the consultants' share of the gain and other costs, including $56.8 million related to the monetization of our shares of common stock of Google.

(6) The full year effective tax rate was 5.5%. At September 30, 2004, the estimated full year effective tax rate was 8.7%. In the fourth quarter of 2004, we recorded an income tax benefit of $2.2 million to reflect the decrease of 3.2% in the full year effective rate.

(7) During the fourth quarter of 2003, we recorded a full valuation allowance against our net deferred tax assets for the U.S. and foreign operations which comprise the U.S. income tax entity. The increase in the valuation allowance, which resulted in a non-cash charge to income tax expense in the amount of $57.9 million, was based on the provisions of SFAS No. 109, "Accounting for Income Taxes."

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ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Derivative instruments. We receive warrants for equity securities in our client companies, in addition to our cash fee, for services rendered on some searches. Some of the warrants meet the definition of a derivative instrument under Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," and its subsequent amendments. SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument be recorded in the balance sheet as either an asset or liability measured at its fair value. These derivative instruments are initially recorded at their fair value using a Black-Scholes model, in the Consolidated Balance Sheets, with a corresponding amount recorded as net revenue in the Consolidated Statements of Operations. Bonus expense related to this net revenue is also recorded. Subsequent changes in the fair value of these derivative instruments are recorded in the Consolidated Statements of Operations as unrealized gains (losses), net of the consultants' share of the gains (losses). Upon a value event such as an initial public offering or an acquisition, the warrants are monetized, resulting in a realized gain, net of the consultants' share of the gain and other costs. In 2004, 2003 and 2002, we recorded realized gains, net of the consultants' share of the gain and other costs, of $57.0 million, $0.7 million, $1.6 million, respectively, related to the equity and warrant portfolio.

Currency market risk. With our operations primarily in North America, Latin America, Europe and Asia Pacific we conduct business using various currencies. Revenue earned in each country is generally matched with the associated expenses incurred, thereby reducing currency risk to earnings. However, because certain assets and liabilities are denominated in currencies other than the U.S. dollar, changes in currency rates may cause fluctuations in the valuation of such assets and liabilities. As the local currency of our subsidiaries has been designated as the functional currency, we are affected by the translation of foreign currency financial statements into U.S. dollars. Outside of North America, Europe is our largest region in terms of net revenue. A 1% change in the average exchange rate of the British pound and the euro would have increased or decreased our 2004 net income less than $0.1 million. For financial information by geographic segment, see Note 18, *Segment Information*, in the Notes to Consolidated Financial Statements.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Heidrick & Struggles International, Inc.:

We have audited the accompanying consolidated balance sheets of Heidrick & Struggles International, Inc. and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2004. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule, Valuation and Qualifying Accounts. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule 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 financial statements referred to above present fairly, in all material respects, the financial position of Heidrick & Struggles International, Inc. and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Heidrick & Struggles International, Inc.'s internal control over financial reporting as of December 31, 2004, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 10, 2005 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

/s/ KPMG LLP

Chicago, Illinois
March 10, 2005

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	December 31,	
	2004	2003
Current assets:		
Cash and cash equivalents	$222,753	$119,289
Accounts receivable, less allowance for doubtful accounts of $3,049 and $4,387 at December 31, 2004 and 2003, respectively	51,843	47,245
Other receivables	4,453	3,191
Prepaid expenses	8,377	9,022
Deferred income taxes, net	2,744	—
Total current assets	290,170	178,747
Property and equipment:		
Leasehold improvements	27,686	27,416
Office furniture, fixtures and equipment	25,812	26,879
Computer equipment and software	53,664	49,959
	107,162	104,254
Accumulated depreciation and amortization	(79,485)	(70,788)
Property and equipment, net	27,677	33,466
Other non-current assets:		
Assets designated for retirement and pension plans	32,468	28,751
Investments	4,089	2,842
Other non-current assets	3,406	4,226
Goodwill	48,818	48,627
Other intangible assets, net	6,890	7,771
Deferred income taxes, net	7,766	—
Total other non-current assets	103,437	92,217
Total assets	$421,284	$304,430

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

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	December 31,	
	2004	2003
Current liabilities:		
Current maturities of long-term debt	$ 27	$ 568
Accounts payable	10,986	7,196
Accrued salaries and employee benefits	68,044	59,788
Other accrued liabilities	42,843	23,545
Current portion of accrued restructuring charges	10,609	18,090
Income taxes payable, net	7,463	4,349
Total current liabilities	139,972	113,536
Non-current liabilities:		
Long-term debt, less current maturities	—	26
Retirement and pension plans	37,941	32,232
Non-current portion of accrued restructuring charges	21,632	27,698
Other non-current liabilities	5,613	4,729
Total non-current liabilities	65,186	64,685
Total liabilities	205,158	178,221
Stockholders' equity:		
Preferred stock, $.01 par value, 10,000,000 shares authorized, no shares issued at December 31, 2004 and 2003	—	—
Common stock, $.01 par value, 100,000,000 shares authorized, of which 19,158,588 and 18,339,567 shares were outstanding at December 31, 2004 and 2003, respectively	196	196
Treasury stock at cost, 427,189 and 1,246,210 shares at December 31, 2004 and 2003, respectively	(8,448)	(21,898)
Additional paid in capital	242,655	250,489
Accumulated deficit	(24,587)	(106,895)
Accumulated other comprehensive income	9,033	6,712
Deferred stock-based compensation	(2,723)	(2,395)
Total stockholders' equity	216,126	126,209
Total liabilities and stockholders' equity	$421,284	$ 304,430

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

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)

	Year Ended December 31,		
	2004	2003	2002
Revenue:			
Revenue before reimbursements (net revenue)	$375,432	$317,934	$350,712
Reimbursements	22,744	22,683	26,133
Total revenue	398,176	340,617	376,845
Operating expenses:			
Salaries and employee benefits	251,186	223,537	242,330
General and administrative expenses	96,533	87,250	106,913
Reimbursed expenses	21,247	22,683	26,133
Restructuring charges	550	29,443	48,532
Total operating expenses	369,516	362,913	423,908
Operating income (loss)	28,660	(22,296)	(47,063)
Non-operating income (expense):			
Interest income	2,588	1,687	2,018
Interest expense	(197)	(166)	(210)
Net realized and unrealized gains (losses) on equity and warrant portfolio, net of the consultant’s share of the gains (losses)	57,072	673	(1,325)
Write-down of long-term investments	—	—	(5,000)
Other, net	(1,024)	(1,722)	(73)
Net non-operating income (expense)	58,439	472	(4,590)
Income (loss) before income taxes	87,099	(21,824)	(51,653)
Provision for (benefit from) income taxes	4,791	58,844	(11,491)
Net income (loss)	$ 82,308	$ (80,668)	$ (40,162)
Basic earnings (loss) per common share	$ 4.35	$ (4.43)	$ (2.22)
Basic weighted average common shares outstanding	18,941	18,217	18,107
Diluted earnings (loss) per common share	$ 4.11	$ (4.43)	$ (2.22)
Diluted weighted average common shares outstanding	20,012	18,217	18,107

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

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS)

(In thousands)

	Common Stock							
	Shares	Amount	Treasury Stock	Additional Paid in Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income (Loss)	Deferred Stock-Based Compensation	Total
Balance at December 31, 2001	**18,041**	**$ 195**	**$ (27,459)**	**$ 258,699**	**$ 13,935**	**$ (5,872)**	**$ (9,907)**	**$229,591**
Net loss		—	—	—	(40,162)	—	—	(40,162)
Other comprehensive income:								
Unrealized gain on available-for-sale investments, net of tax (pretax $83)		—	—	—	—	48	—	48
Foreign currency translation adjustment		—	—	—	—	4,640	—	4,640
Total comprehensive income (loss)		—	—	—	(40,162)	4,688	—	(35,474)
Treasury and common stock transactions:								
Issuance of restricted stock units		—	—	2,055	—	—	(2,055)	—
Amortization of deferred compensation		—	—	—	—	—	5,096	5,096
Forfeitures of restricted stock units		—	—	(2,900)	—	—	768	(2,132)
Issuance of common stock	47	—	—	332	—	—	—	332
Exercise of stock options	63	1	—	889	—	—	—	890
Net (purchases) re-issuances of treasury stock	1	—	38	63	—	—	—	101
Accrued compensation under performance share program		—	—	1,307	—	—	—	1,307
Balance at December 31, 2002	**18,152**	**196**	**(27,421)**	**260,445**	**(26,227)**	**(1,184)**	**(6,098)**	**199,711**
Net loss		—	—	—	(80,668)	—	—	(80,668)
Other comprehensive income (loss):								
Unrealized loss on available-for-sale investments, net of tax (pretax $97)		—	—	—	—	(57)	—	(57)
Foreign currency translation adjustment		—	—	—	—	7,953	—	7,953
Total comprehensive income (loss)		—	—	—	(80,668)	7,896	—	(72,772)
Treasury and common stock transactions:								
Issuance of restricted stock units		—	—	3,203	—	—	(3,203)	—
Amortization of deferred compensation		—	—	—	—	—	5,167	5,167
Other stock based compensation		—	—	396	—	—	—	396
Forfeitures of restricted stock units		—	—	(3,625)	—	—	1,739	(1,886)
Exercise of stock options	102	—	1,806	(145)	—	—	—	1,661
Purchases of treasury stock	(288)	—	(3,175)	—	—	—	—	(3,175)
Re-issuances of treasury stock	21	—	399	(91)	—	—	—	308
Vesting of restricted stock units, net of tax withholdings	353	—	6,493	(8,387)	—	—	—	(1,894)
Decrease in accrued compensation under performance share program		—	—	(1,307)	—	—	—	(1,307)
Balance at December 31, 2003	**18,340**	**196**	**(21,898)**	**250,489**	**(106,895)**	**6,712**	**(2,395)**	**126,209**
Net income		—	—	—	82,308	—	—	82,308
Other comprehensive income:								
Unrealized gain on available-for-sale investments		—	—	—	—	342	—	342
Foreign currency translation adjustment		—	—	—	—	1,979	—	1,979
Total comprehensive income		—	—	—	82,308	2,321	—	84,629
Treasury and common stock transactions:								
Issuance of restricted stock units		—	—	3,567	—	—	(3,567)	—
Amortization of deferred compensation		—	—	—	—	—	3,224	3,224
Other stock based compensation		—	—	183	—	—	—	183
Forfeitures of restricted stock units		—	—	(1,357)	—	—	15	(1,342)
Exercise of stock options	551	—	9,748	(1,180)	—	—	—	8,568
Purchases of treasury stock	(85)	—	(2,502)	—	—	—	—	(2,502)
Vesting of restricted stock units, net of tax withholdings	353	—	6,204	(9,047)	—	—	—	(2,843)
Balance at December 31, 2004	**19,159**	**$ 196**	**$ (8,448)**	**$ 242,655**	**$ (24,587)**	**$ 9,033**	**$ (2,723)**	**$216,126**

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

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Year Ended December 31,		
	2004	2003	2002
Cash flows from operating activities:			
Net income (loss)	$ 82,308	$ (80,668)	$ (40,162)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization	13,185	14,073	15,262
Loss on sale of property and equipment	197	27	339
Gain on sale of equity securities	(57,041)	(688)	(1,630)
Write-down of long-term investments	—	—	5,000
Deferred income taxes	(10,554)	59,333	(12,030)
Net unrealized (gain) loss on derivative instruments	(31)	15	2,955
Stock-based compensation expense, net	2,065	2,370	4,271
Restructuring charges	550	29,443	48,532
Cash paid for restructuring charges	(13,971)	(19,230)	(25,396)
Changes in assets and liabilities:			
Trade and other receivables	(3,827)	(440)	17,112
Accounts payable	3,496	(2,299)	(5,172)
Accrued expenses	2,918	(14,269)	(30,231)
Income taxes recoverable (payable), net	3,131	12,856	16,583
Retirement and pension plan liabilities	3,197	2,231	2,887
Other assets and liabilities, net	36	7,650	7,710
Net cash provided by operating activities	25,659	10,404	6,030
Cash flows from investing activities:			
Capital expenditures	(6,021)	(5,806)	(5,201)
Proceeds from sales of equity securities	128,993	1,546	3,271
Payments to consultants related to sales of equity securities	(54,702)	(858)	(1,814)
Other, net	83	399	(204)
Net cash provided by (used in) investing activities	68,353	(4,719)	(3,948)
Cash flows from financing activities:			
Proceeds from stock options exercised	8,568	1,661	890
Purchases of treasury stock	(2,502)	(3,175)	(81)
Payments on debt	(569)	(476)	(2,583)
Net cash provided by (used in) financing activities	5,497	(1,990)	(1,774)
Effect of foreign currency exchange rates on cash and cash equivalents	3,955	5,374	1,180
Net increase in cash and cash equivalents	103,464	9,069	1,488
Cash and cash equivalents:			
Beginning of year	119,289	110,220	108,732
End of year	$222,753	$119,289	$110,220
Supplemental disclosures of cash flow information			
Cash paid (refunded) for—			
Interest	$ 105	$ 96	$ 37
Income taxes, net	(10,767)	(12,136)	(15,335)
Supplemental schedule of noncash financing and investing activities			
Unrealized gain (loss) on available-for-sale investments	$ 342	$ (97)	$ 83

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

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(All tables in thousands, except per share figures)

1. Basis of Presentation

Heidrick & Struggles International, Inc. and Subsidiaries (the "Company") are engaged in providing executive search and leadership consulting services to clients on a retained basis. The Company operates in North America, Latin America, Europe and Asia Pacific.

The consolidated financial statements include Heidrick & Struggles International, Inc. and its wholly-owned subsidiaries and have been prepared in accordance with generally accepted accounting principles in the United States ("GAAP"). The preparation of these financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses and certain financial statement disclosures. Significant items subject to estimates and assumptions include revenue recognition, allowance for doubtful accounts, allowances for deferred tax assets, assessment of goodwill and other intangible assets for impairment, and accruals related to the consolidation and closing of offices recorded in conjunction with the Company's restructuring charges. Actual results could differ from these estimates.

2. Summary of Significant Accounting Policies

Cash and Cash Equivalents

The Company considers all highly liquid instruments with an original maturity of three months or less to be cash equivalents.

Concentration of Credit Risk

Financial instruments that potentially expose the Company to concentrations of credit risk consist primarily of accounts receivable. Concentrations of credit risk with respect to accounts receivable are limited due to the Company's large number of clients and their dispersion across many different industries and geographies. At December 31, 2004, the Company had no significant concentrations of credit risk.

The allowance for doubtful accounts is developed based upon several factors including the age of our accounts receivable, historical write-off experience and specific account analysis. As such, these factors may change over time causing the allowance level to adjust accordingly.

Fair Value of Financial Instruments

Cash and Cash Equivalents are stated at cost, which approximates fair market value. The carrying value for receivables from clients, accounts payable, deferred revenue and other accrued liabilities reasonably approximate fair market value due to the nature of the financial instrument and the short term nature of the these items.

Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization are computed using the straight-line method over the estimated useful life of the asset or, for leasehold improvements, the shorter of the lease term or the estimated useful life of the asset, as follows:

Office furniture, fixtures and equipment	5-10 years
Computer equipment and software	3-8 years

Depreciation is calculated for tax purposes using accelerated methods, where applicable.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Long-lived Assets

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," the Company reviews its long-lived assets, including property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge, equal to the amount by which the carrying amount of the asset exceeds the fair value of the asset, is recognized.

Investments

The Company receives warrants for equity securities in client companies, in addition to the cash fee, for services rendered on some searches. Some of the warrants meet the definition of a derivative instrument under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and its subsequent amendments. SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument be recorded in the balance sheet as either an asset or liability measured at its fair value. These derivative instruments are initially recorded at their fair value, using a Black-Scholes model, in the Consolidated Balance Sheets, with a corresponding amount recorded as net revenue in the Consolidated Statements of Operations. Bonus expense related to this net revenue is also recorded. Subsequent changes in the fair value of these derivative instruments are recorded in the Consolidated Statements of Operations as unrealized gains (losses), net of the consultants' share of the gains (losses).

Other warrants received and which do not meet the definition of a derivative instrument under SFAS No. 133 are initially recorded at their fair value, using a Black-Scholes model, in the Consolidated Balance Sheets, with a corresponding amount recorded as net revenue in the Consolidated Statements of Operations. Bonus expense related to this net revenue is also recorded. These warrants are accounted for using the cost method, and subsequent changes in fair value are not recognized. However, these warrants are regularly reviewed for other-than-temporary declines in fair value. Any permanent declines in the fair value of these warrants are recorded in the Consolidated Statements of Operations as unrealized losses, net of the consultants' share of the losses.

Upon a value event such as an initial public offering or an acquisition, any changes in the fair value of the warrants, both derivatives and non-derivatives, are recorded in the Consolidated Statements of Operations as unrealized gains (losses), net of the consultants' share of the gains (losses).

Any equity securities arising from the exercise of a warrant are accounted for as available-for-sale investments in accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Subsequent changes in the fair value of these available-for-sale investments are recorded as a component of accumulated other comprehensive income (loss). Upon the sale of these investments, the Company records a realized gain (loss), net of the consultants' share of the gain (loss) and other costs.

Goodwill and Other Intangible Assets

Pursuant to the requirements of SFAS No. 142, "Goodwill and Other Intangible Assets," the Company evaluates its goodwill for impairment on an annual basis during the fourth quarter, or whenever indicators of impairment exist. The goodwill impairment test compares the fair value of a reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, goodwill of the reporting unit would be considered impaired. To measure the amount of the impairment loss, the implied fair value of a reporting unit's goodwill is compared to the carrying amount of that goodwill. If the carrying amount

of a reporting unit's goodwill exceeds the implied fair value of that goodwill, an impairment loss shall be recognized in an amount equal to that excess. The implied fair value of goodwill shall be determined in the same manner as the amount of goodwill recognized in a business combination is determined. The fair value of each of the Company's reporting units was determined using a combination of valuation techniques, including a discounted cash flow methodology and comparable public company methodology, with the assistance of an independent valuation firm. These impairment tests indicated that the fair value of each reporting unit exceeded its carrying amount. As a result, no impairment charge was recorded.

Other intangible assets are amortized using the straight-line method over their estimated useful lives and have been segregated as a separate line item on the Consolidated Balance Sheets.

Restructuring Charges

For restructuring activities announced prior to January 1, 2003, the accruals for restructuring charges were established in accordance with EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." For restructuring activities initiated subsequent to December 31, 2002, the accruals for restructuring charges were established in accordance with SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," which the Company adopted on January 1, 2003.

Revenue Recognition

Revenue before reimbursements of out-of-pocket expenses ("net revenue") consists of retainers and indirect expenses billed to clients. For each assignment, the Company and its client enter into a contract that outlines the general terms and conditions of the assignment. Typically, the Company is paid a retainer for its executive search services equal to approximately one-third of the estimated first year compensation for the position to be filled. In addition, if the actual compensation of a placed candidate exceeds the estimated compensation, the Company often will be authorized to bill the client for one-third of the excess. Indirect expenses are calculated as a percentage of the retainer with certain dollar limits per search. The Company generally bills its clients for its retainer and indirect expenses in one-third increments over a three-month period commencing in the month of a client's acceptance of the contract.

Net revenue is recognized when earned and realizable and therefore when the following criteria have been met: (a) persuasive evidence of an arrangement exists, (b) services have been rendered, (c) the fee to our client is fixed or determinable, and (d) collectibility is reasonably assured. Net revenue from executive search engagements is recognized over the expected average period of performance, in proportion to the estimated personnel time incurred to fulfill our obligations under the arrangements. Net revenue in excess of the retainer, resulting from actual compensation of the placed candidate exceeding the estimated compensation, is recognized upon completion of the executive search when the amount of the additional fee is known.

Reimbursements

The Company incurs certain out-of-pocket expenses that are reimbursed by our clients. Historically, the Company had not established a receivable for reimbursable expenses incurred but not yet billed as the amount was determined to be immaterial. During the fourth quarter of 2004, the Company enhanced its estimation technique related to reimbursable expenses resulting in a favorable impact to operating income of $1.5 million. The Company has accounted for this as a change in accounting estimate. This change in accounting estimate is not expected to have a significant impact on the Company's results of operations in future periods.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Salaries and Employee Benefits

Salaries and employee benefits consist of compensation and benefits paid to consultants, executive officers, and administrative and support personnel, of which the most significant elements are salaries and annual performance-related bonuses. Other items in this category are expenses related to signing bonuses and minimum guaranteed bonuses (often incurred in connection with the hiring of new consultants), payroll taxes, profit sharing and retirement benefits, and employee insurance benefits.

Salaries and employee benefits are recognized on an accrual basis. Certain signing bonuses and minimum guaranteed compensation are capitalized and amortized up to a maximum of three years, consistent with the terms associated with these payments.

Some deferred compensation arrangements with certain employees, which were executed prior to July 30, 2002, are structured as forgivable loans. The forgivable loans are accounted for as deferred compensation, and are therefore amortized to compensation expense over the forgiveness period. At December 31, 2004, $0.3 million of deferred compensation was structured as forgivable loans. The terms of a deferred compensation arrangement structured as a forgivable loan and granted to an executive officer are included in the employee's employment agreement as filed with the Securities and Exchange Commission.

Stock-Based Compensation

The Company applies the intrinsic-value-based method of accounting prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations to account for its fixed-plan stock options. Under this method, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. SFAS No. 123, "Accounting for Stock-Based Compensation," amended by SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure" established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic-value-based method of accounting described above, and has adopted only the disclosure requirements of SFAS No. 123.

Had compensation expense been determined based upon fair value at the grant date for all awards in accordance with SFAS No. 123, the Company's pro forma net earnings and basic and diluted earnings per share for the years ended December 31, 2004, 2003 and 2002 would have been as follows:

	2004	2003	2002
Net income (loss):			
As reported	$ 82,308	$ (80,668)	$ (40,162)
Add: Stock-based compensation expense already included in net income, net of tax in 2002	2,065	2,370	2,520
Deduct: Pro forma employee compensation cost related to stock options, restricted stock units and the performance share program, net of tax in 2002	(10,300)	(8,813)	(11,880)
Pro forma	$ 74,073	$ (87,111)	$ (49,522)
Basic earnings (loss) per share:			
As reported	$ 4.35	$ (4.43)	$ (2.22)
Pro forma	3.91	(4.78)	(2.73)
Diluted earnings (loss) per share:			
As reported	$ 4.11	$ (4.43)	$ (2.22)
Pro forma	3.78	(4.78)	(2.73)

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The weighted average fair value of options at their grant date during 2004, 2003 and 2002, were $12.78, $5.42, and $8.75, respectively. The estimated fair value of each option granted is calculated using the Black-Scholes option-pricing model. The weighted average assumptions used in the model were as follows:

	2004	2003	2002
Risk-free interest rate	3.6%	2.6%	4.4%
Expected years until exercise	4.5	4.5	4.5
Expected stock volatility	48.0%	50.0%	52.0%
Dividend yield	0%	0%	0%

Compensation expense resulting from grants of restricted stock units is measured on the date of grant and is amortized primarily on a straight-line basis over the vesting period.

Consultants' Share of Gains Related to Warrant Monetizations

Historically, the Company's policy with respect to warrants was that 55% of the net proceeds resulting from the monetizations of warrants was payable to the consultants involved in the search. For warrants received after February 16, 2005, the portion of the net proceeds payable to consultants was reduced from 55% to 50% and is limited to $10.0 million per monetization. In addition, of the 50% of the net proceeds retained by the Company, 20% (or 10% of the total net proceeds) will be reserved for distribution to the broader employee population.

Income Taxes

Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax basis of assets and liabilities, applying enacted statutory tax rates in effect for the year in which the tax differences are expected to reverse. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Earnings (Loss) per Common Share

Basic earnings (loss) per common share is computed by dividing net income (loss) by weighted average common shares outstanding for the year. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted. Common equivalent shares are excluded from the determination of diluted earnings per share in periods in which they have an anti-dilutive effect.

Translation of Foreign Currencies

The translation of financial statements into U.S. dollars has been performed in accordance with SFAS No. 52, "Foreign Currency Translation." The local currency for all subsidiaries has been designated as the functional currency. Assets and liabilities have been translated into U.S. dollars at the current rate of exchange prevailing at the balance sheet date. Revenue and expenses have been translated at an average exchange rate for the period. Translation adjustments are reported as a component of accumulated other comprehensive income.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Reclassifications

Certain amounts in previously issued financial statements have been reclassified to conform to the current year presentation.

Recently Issued Financial Accounting Standards

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (revised 2004), “Share-Based Payment” (SFAS No. 123R). This statement requires that the costs of employee share-based payments be measured at fair value on the awards grant date using an option-pricing model and recognized in the financial statements over the requisite service period. SFAS No. 123R supersedes APB 25 and its related interpretations, and eliminates the alternative use of an intrinsic value method of accounting under APB 25, which the Company is currently using. The effective date for the Company is the beginning of the third quarter of 2005. The Company is currently evaluating the impact that the adoption of SFAS No. 123R will have on the Company’s financial condition and results of operations and anticipate that the application of the expensing provisions of SFAS 123R will be relatively consistent with the expense that we have historically disclosed in pro-forma disclosures required by SFAS 123.

In December 2004, the FASB issued Staff Position No. 109-2, “Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004” (“FSP 109-2”). The American Jobs Creation Act of 2004 (the “Act”), signed into law on October 22, 2004, provides for a special one-time tax deduction, or dividend received deduction (“DRD”), of 85% of qualifying foreign earnings that are repatriated in either a company’s last tax year that began before the enactment date or the first tax year that begins during the one-year period beginning on the enactment date. FSP 109-2 provides entities additional time to assess the effect of repatriating foreign earnings under the Act for purposes of applying SFAS No. 109, “Accounting for Income Taxes,” which typically requires the effect of a new tax law to be recorded in the period of enactment. The Company does not anticipate applying the special one-time tax deduction or DRD to repatriate foreign earnings during 2005.

In March 2004, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 03-1, “The Meaning of Other-Than-Temporary Impairments and Its Application to Certain Investments” (EITF 03-1). EITF 03-1 provides a three-step impairment model for determining whether an investment is other-than-temporarily impaired and requires the recognition of such impairments as an impairment loss equal to the difference between the investments cost and fair value at the reporting date. The effective date for the Company was the beginning of the third quarter 2004. In September 2004, the FASB issued Staff Position No. EITF Issue 03-1-1, “Effective Date of Paragraphs 10-20 of EITF Issue No. 03-01, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments” (FSP EITF 03-1-1), which delayed the effective date for the measurement and recognition guidance contained in EITF 03-1; however did not change the disclosure requirements. The adoption of EITF 03-1 impacted the disclosures related to the Company’s investments in 2004 and is not expected to have a material impact on the Company’s financial condition or results of operations.

In December 2003, the FASB issued FASB Interpretation No. 46 (revised December 2003), “Consolidation of Variable Interest Entities,” which addresses how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity. This Interpretation replaced FASB Interpretation No. 46, “Consolidation of Variable Interest Entities,” which was issued in January 2003. The Company currently does not have any controlling financial interests that are within the scope of this Interpretation.

In December 2003, the FASB issued SFAS No. 132 (revised 2003), “Employers’ Disclosures about Pensions and Other Postretirement Benefits” (SFAS No. 132R). The disclosure requirements of SFAS 132R require more complete information in both annual and interim financial statements about pension and postretirement benefits as well as increase the transparency of the financial reporting related to those plans and benefits. Except as noted, the revised disclosure requirements are effective for financial statements with fiscal years ending after December 15, 2003. The interim-period disclosures relating to net periodic benefit cost required by the revised Statement are effective for interim periods beginning after December 15, 2003. The Company adopted the interim-period disclosure requirements of SFAS 132 related to net periodic benefit cost on January 1, 2004. The additional disclosure of information about employer contributions related to foreign plans required by the revised statement is effective for fiscal years ending after June 15, 2004 and interim periods beginning with the first quarter of 2005. The adoption of SFAS No. 132R impacted the disclosures related to the Company’s foreign pension plan in 2004 and will further impact the disclosures in 2005, and is not expected to have a material impact on the Company’s financial condition or results of operations.

3. Investments

The Company had investments of $4.1 million and $2.8 million at December 31, 2004 and 2003, respectively. Investments primarily include the fair value of the Company’s warrants and equity securities in publicly traded and private companies. The aggregate cost of the Company’s cost method investments totaled $1.2 million at December 31, 2004, all of which were evaluated for impairment.

On October 26, 2000, the Company announced that it entered into an alliance with and invested $10.0 million in ETF Group. In the fourth quarter of 2001, the Company wrote down half of its investment in ETF Group incurring a non-cash charge of $5.0 million. The Company wrote down the remaining $5.0 million in the second quarter of 2002.

4. Other Non-current Assets

Other non-current assets primarily include the assets related to the non-current portion of deferred compensation and the non-current portion of prepaid rent. At December 31, 2004 and 2003, the Company had $3.4 million and $4.2 million of non-current assets, respectively.

5. Goodwill and Other Intangible Assets

Goodwill

In accordance with SFAS No. 142, “Goodwill and Other Intangible Assets,” the Company’s annual goodwill impairment test was performed in the fourth quarter of 2004, 2003 and 2002. A transitional goodwill impairment test was performed as of January 1, 2002, upon adoption of SFAS No. 142. The goodwill impairment test compares the fair value of a reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, goodwill of the reporting unit would be considered impaired. To measure the amount of the impairment loss, the implied fair value of a reporting unit’s goodwill is compared to the carrying amount of that goodwill. If the carrying amount of a reporting unit’s goodwill exceeds the implied fair value of that goodwill, an impairment loss shall be recognized in an amount equal to that excess. The implied fair value of goodwill shall be determined in the same manner as the amount of goodwill recognized in a business combination is determined. For each of these tests, the fair value of each of the Company’s reporting units was determined using a combination of valuation techniques, including a discounted cash flow methodology and a comparable public company methodology, with the assistance of an independent valuation firm. These impairment tests indicated that the fair value of each reporting unit exceeded its carrying amount. As a result, no impairment charge was recorded.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Changes in the carrying amount of goodwill, by segment, for the year ended December 31, 2004 were as follows:

	North America	Europe	Asia Pacific	Total
Balance at December 31, 2003	$18,362	$28,701	$1,564	$48,627
Exchange rate fluctuations	—	129	62	191
Balance at December 31, 2004	$18,362	$28,830	$1,626	$48,818

As part of the cost reduction initiatives announced in October 2003, the Company wrote off $2.3 million of goodwill. The write-down related primarily to a wholly-owned subsidiary in Finland which was converted to a licensee. The operation had been acquired in 2000.

As part of the cost reduction initiatives announced in October 2002, the Company exited a management search operation in Europe that had been acquired by the Company in 2001. This management search operation had not been fully integrated with the other operations in the Europe reporting unit. As a result of exiting this operation, the Company wrote off $1.8 million of goodwill related to this operation.

See Note 14, *Restructuring Charges*, for additional information.

Other Intangible Assets

As part of the cost reduction initiatives announced in October 2003, the Company wrote off $1.1 million of intangible assets. The write-down related primarily to a wholly-owned subsidiary in Finland which was converted to a licensee. The operation had been acquired in 2000.

As part of the cost reduction initiatives announced in October 2002, the Company wrote off approximately $0.5 million of intangible assets primarily related to the Company's exit from a management search operation in Europe that had been acquired by the Company in 2001.

See Note 14, *Restructuring Charges*, for additional information.

The carrying amount of amortizable intangible assets and the related accumulated amortization at December 31, 2004 and 2003 are as follows:

		2004			2003		
	Weighted Average Life	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Client relationships	14.9	$11,302	$ (4,412)	$ 6,890	$11,302	$ (3,537)	$ 7,765
Other intangible assets		1,625	(1,625)	—	1,625	(1,619)	6
Total		$12,927	$ (6,037)	$ 6,890	$12,927	$ (5,156)	$ 7,771

The aggregate intangible amortization expense for the years ended December 31, 2004, 2003 and 2002 was $0.9 million, $1.5 million and $2.0 million, respectively. The estimated intangible amortization expense for the five succeeding years is approximately $874 thousand per year.

6. Other Accrued Liabilities

The components of other accrued liabilities at December 31, 2004 and 2003 are as follows:

	2004	2003
Deferred revenue	$10,398	$10,148
Accrued rent	3,603	2,542
Accrued sales and value-added taxes	3,988	2,986
Consultants’ share of equity and warrant gains	18,764	1,487
Other	6,090	6,382
Total	$42,843	$23,545

7. Long-term Debt

At December 31, 2004 and 2003, long-term debt consists of a note payable resulting from an acquisition. At December 31, 2004, the current portion of long-term debt was $27 thousand which approximates its fair value based on current rates for similar debt.

8. Line of Credit

In December 2003, the Company entered into a $60.0 million committed revolving credit facility (the “Facility”). The Facility replaced a $50.0 million committed revolving credit facility and a $5.0 million uncommitted credit facility. The Company pays a facility fee even if no portion of the Facility is used. Under this Facility, the Company may borrow U.S. dollars, euros, sterling and other major traded currencies, as agreed by the banks. Borrowings under the Facility bear interest at the existing Alternate Base Rate or LIBOR plus a margin as determined by the Company’s compliance with certain tests of financial condition. The Facility sets limits on the Company’s ability to make acquisitions without bank approval and to incur additional debt outside of the Facility. The Facility has financial tests the Company must meet or exceed relating to:

- fixed charge coverage (defined as consolidated EBITDAR minus consolidated capital expenditures to consolidated interest expense plus consolidated rental obligations plus restricted payments). (EBITDAR is defined as earnings before interest expense, taxes, depreciation, amortization and rental expense plus interest income);
- leverage (defined as consolidated total indebtedness to consolidated EBITDA plus interest income);
- current ratio (defined as current assets divided by current liabilities); and
- net worth.

In March 2004, the Company amended the Facility to reduce the net worth covenant from $145.0 million to $110.0 million. This amendment was required as a result of the non-cash income tax expense of $57.9 million, recorded in the fourth quarter of 2003, which provided a full valuation allowance for the net deferred tax assets related to the U.S. and foreign operations which comprise the U.S. income tax entity. See Note 17, *Income Taxes*, in the Notes to Consolidated Financial Statements.

There were no borrowings outstanding under the lines of credit existing at December 31, 2004 or 2003, nor were there any borrowings during the years ended December 31, 2004 and 2003, respectively, under the then existing lines of credit. At December 31, 2004, the Company was in compliance with the financial covenants of the Facility, and no event of default existed.

9. Employee Benefit Plans

Qualified Retirement Plan

The Company has a defined contribution retirement plan for all eligible employees in the United States. The plan contains a 401(k) provision which provides for employee tax-deferred contributions. The Company matched employee contributions on a two-for-one basis up to a maximum contribution of $2,000 per participant for each of the years ended December 31, 2004, 2003 and 2002. The plan provides that forfeitures will be used to reduce the Company's contributions. Forfeitures are created when participants terminate employment before becoming entitled to their full benefits under the plan. The Company also has the option of making discretionary contributions. Plan expense for the years ended December 31, 2004, 2003 and 2002 was $0.8 million, $0.8 million, and $1.0 million, respectively. Discretionary contributions were not made for the years ended December 31, 2004, 2003 and 2002.

Through September 30, 2004, the plan allowed participants the option of having their account balances or portions thereof invested in the Company's common stock. As of October 1, 2004, participants were no longer allowed the option of purchasing the Company's common stock under the plan. However, those participants who held the Company's common stock were allowed to maintain their shares. At December 31, 2004 and 2003, respectively, the plan held 496,067 and 661,230 shares of the Company's common stock.

Nonqualified Retirement Plan

The Company has a nonqualified retirement plan for employees in the United States classified as senior associates and senior information specialists. This plan provides for discretionary employer contributions. There was no plan expense for the years ended December 31, 2004, 2003 and 2002. The liability for this retirement plan at December 31, 2004, 2003 and 2002, was $0.5 million, $0.7 million and $0.9 million, respectively.

Deferred Compensation Plans

In 2002, the Company adopted a Deferred Compensation Plan in the United States (the "U.S. Plan") and in the United Kingdom (the "U.K. Plan"). Participation in these plans is not mandatory.

For the U.S. Plan, certain U.S.-based employees are given the opportunity to defer up to 100% of their eligible cash compensation into several different investment vehicles, including a Company stock fund. Cash deferrals must be made for a minimum of one year. These deferrals are always vested and are not subject to a risk of forfeiture. The U.S. Plan also allows participants to continue to defer beyond the mandatory initial two-year deferral period any share-based deferrals earned under the Management Incentive Plan ("MIP"). The extension of the deferral must be for a minimum of one year. As of December 31, 2004, 2003 and 2002, the compensation deferred in the U.S. Plan was $1.2 million, $1.2 million and $0.9 million, respectively. As of December 31, 2004, the U.S. Plan was not funded. In addition, as of December 31, 2004, approximately $17 million has been deferred under this plan relating to the portion of the consultant's share of the gain that will be paid in 2005 related to the sale of our shares of common stock of Google.

For the U.K. Plan, certain U.K.-based employees are given the opportunity to waive the right to their annual discretionary bonus payment. The Company may then choose to make a contribution on the employee's behalf into an Employee Benefit Trust ("EBT"). The trustee of the EBT has full discretion over the administration and the EBT's choice of investments. The assets and liabilities of the EBT are included in the Consolidated Balance Sheets at December 31, 2004 and 2003. As of December 31, 2004, the compensation deferred in the U.K. Plan was $5.6 million of which $5.6 million was funded. As of December 31, 2003, the compensation deferred in the U.K. Plan was $2.6 million of which $2.6 million was funded.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

10. Pension Plan and Life Insurance Contract

The Company maintains a pension plan for certain employees in Germany. The pensions are individually fixed euro amounts depending on the function and the eligible years of service of the employee.

The following table provides a reconciliation of the benefit obligation for the years ended December 31, 2004 and 2003:

	2004	2003
Change in benefit obligation:		
Benefit obligation at January 1,	$24,662	$22,700
Service cost	391	668
Interest cost	1,247	1,278
Actuarial gain	(526)	(3,776)
Benefits paid	(838)	(820)
Translation difference	1,939	4,612
Benefit obligation at December 31,	26,875	24,662
Unrecognized net gain	3,755	3,136
Net amount recognized	$30,630	$27,798
Accrued benefit cost at December 31:		
Unfunded status of the plan	$26,875	$24,662
Unrecognized net gain	3,755	3,136
Accrued benefit cost	$30,630	$27,798

	2004	2003	2002
Assumptions:			
Discount rate	4.75%	5.25%	6.00%
Rate of compensation increase	1.75%	2.50%	4.00%
Components of net periodic benefit cost:			
Service cost	$ 391	$ 668	$ 618
Interest cost	1,247	1,278	1,104
Net periodic benefit cost	$1,638	$1,946	$1,722

The pension benefits are fully reinsured within a group insurance contract with Victoria Lebensversicherung AG. The surrender value, which approximates fair value, at December 31, 2004 and 2003 was $26.8 million and $26.2 million, respectively. The expected contribution to be paid to the plan in 2005 is $0.3 million. Because the reinsurance is not segregated from the Company's assets for purposes of SFAS No. 87, "Employers' Accounting for Pensions," the reinsurance is not regarded as an asset with respect to the pension plan. This asset is included in the Consolidated Balance Sheets at December 31, 2004 and 2003, as a component of assets designated for retirement and pension plans.

The benefits expected to be paid in each of the next five years, and in the aggregate for the five years thereafter are as follows:

Years Ended December 31,	
2005	$1,122
2006	1,433
2007	1,360
2008	1,374
2009	1,389
2010 through 2014	7,872

11. Stock-Based Compensation

In 1998, the Company adopted the 1998 Heidrick & Struggles GlobalShare Program I and the 1998 Heidrick & Struggles GlobalShare Program II (collectively, the “Plan”). The Plan serves as a means to attract, reward and retain selected key employees, outside directors and independent contractors. The Plan is administered by the Compensation Committee of the Board of Directors. Awards may be in the form of options, which may be incentive stock options or non-qualified stock options, stock appreciation rights, or other awards, such as restricted stock units, that are valued based upon the fair market value of shares. Awards may be paid in shares, cash or a combination thereof. No incentive option can be for a term of greater than ten years and the option price per share of common stock cannot be less than 100% of the fair market value of the Company’s common stock on the date of grant.

The maximum number of underlying shares of common stock authorized or reserved for issuance under the Plan is based on a formula which shall not exceed an aggregate amount equal to forty percent of the highest number of shares of the Company’s common stock which are issued and outstanding from time to time during the term of the Plan, provided, however, that in no event will the sum of the total number of shares authorized or reserved for issuance upon the exercise or issuance of all awards granted under the Plan plus the total amount of the Company’s issued and outstanding shares of common stock exceed the number of shares of common stock authorized for issuance under the Company’s Amended and Restated Certificate of Incorporation.

The Plan further provides that the total number of shares with respect to which incentive stock options may be granted shall not exceed 2,000,000. No incentive stock options have been granted under the Plan as of December 31, 2004.

Under the Plan, the maximum number of shares of common stock for which awards may be granted during a calendar year to any participant is 400,000. The maximum amount of a cash award received by any participant under the Plan may not exceed $3,000,000 in any one fiscal year.

In 2000, the Company adopted the Heidrick & Struggles International, Inc. Restricted Stock Unit Plan (the “RSU Plan”). The RSU Plan was designed to reward and retain certain employees and independent contractors of the Company, who hold the internal title of Partner or Senior Partner, through the issuance of restricted stock units, which upon vesting, are immediately convertible into shares of the Company’s common stock at a ratio of 1:1.

The total number of restricted stock units and the underlying shares of the Company’s common stock which may be issued or delivered under the RSU Plan shall be determined by the Compensation Committee of the Board of Directors on an annual basis. Under both the Plan and the RSU Plan, the maximum number of shares of common stock reserved for issuance are subject to adjustment for certain anti-dilution provisions.

Under the RSU Plan, the restricted stock units have vesting periods ranging from ratable vesting over a 3 to 5 year period to a cliff vest of 3 to 5 years from the date of grant. The deferred stock-based compensation related to restricted stock units is recorded in stockholders' equity and is amortized to expense on a straight-line basis over the vesting period.

In 2002, the Company adopted a management compensation program which consists of an annual Management Incentive Plan ("MIP"), a Management Stock Option Plan ("MSOP") and a Performance Share Program ("PSP"). These plans provide for designated participants to receive annual and longer-term incentive compensation and were designed to replace the prior practice of issuing options and restricted stock units under the Plan and the RSU Plan. Terms of these plans may be modified and are subject to change.

The MIP is an annual bonus program designed to link participant performance with the attainment of pre-established Company, strategic business unit and individual performance goals. It provides for an annual bonus ranging from 0% to 150% of target incentive compensation. Bonuses are paid in cash for awards up to 100% of target incentive compensation. Any amounts awarded in excess of 100% of the target incentive compensation are paid in shares of the Company's common stock. The employee must be employed by the Company on the date of payment to receive a bonus under the MIP.

The MSOP is designed to align the interests of executives and stockholders with the common goal of increasing stockholder value. It provides for annual grants of options. Generally, the options vest over a three-year period, are forfeited in the event the participant is not in the Company's employ on the vesting date and have a five-year term.

The PSP provides long-term incentive compensation based on the Company's cumulative performance and the price of the Company's common stock measured at the end of a three-year award cycle. The awards are expressed as shares of the Company's common stock and the participants will earn and be paid from zero to 150% of their performance shares based on the Company's achievement against specific performance goals. The value of the PSP award at the payout date is determined by a combination of the Company's performance against the specific performance goals and the price of the Company's common stock on the payout date. Performance shares are paid in cash or shares of the Company's common stock at the sole discretion of the Company. The cost of the performance shares is expensed over the three-year service period at an amount anticipated to be earned. During 2002, the compensation expense recorded for the 2002 PSP grant was $1.3 million. During 2003, the Company reversed this accrual as the Company determined that the targets established for the 2002 – 2004 PSP cycle would not be achieved due primarily to the restructuring charges which were recorded in 2003. In addition, no expense was recorded for the 2003 PSP grant as the Company determined that the targets established for the 2003 – 2005 PSP cycle would not be achieved. Consistent with these determinations, no expense was recorded for the 2002 PSP grant or 2003 PSP grant in 2004. In December 2003, the Compensation Committee of the Company's Board of Directors determined that no further PSP awards would be granted.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Restricted Stock Units

Restricted stock unit activity for the three years ended December 31, 2004 is as follows:

	Number of Restricted Stock Units
Outstanding on December 31, 2001	1,142,217
Granted	152,074
Vested and converted to common stock	(75,978)
Forfeited	(89,503)
Outstanding on December 31, 2002	1,128,810
Granted	262,264
Vested and converted to common stock	(500,145)
Forfeited	(146,629)
Outstanding on December 31, 2003	744,300
Granted	139,353
Vested and converted to common stock	(473,217)
Forfeited	(46,977)
Outstanding on December 31, 2004	363,459

Total deferred stock-based compensation amortization expense for restricted stock units for 2004, 2003 and 2002 was $3.2 million, $5.2 million, and $5.1 million, respectively. The weighted average fair value, at the time of grant, of restricted stock units granted during 2004, 2003, and 2002 was $25.60, $12.21, and $19.94, respectively.

Non-qualified Stock Options

Activity for non-qualified stock options for the three years ended December 31, 2004 is as follows:

	Number of Shares	Weighted Average Exercise Price Per Share
Outstanding on December 31, 2001	3,457,469	$ 30.62
Granted	1,154,000	18.37
Exercised	(63,330)	14.00
Forfeited	(446,270)	31.06
Outstanding on December 31, 2002	4,101,869	27.44
Granted	920,000	12.01
Exercised	(102,846)	14.74
Forfeited	(1,419,615)	29.61
Outstanding on December 31, 2003	3,499,408	22.85
Granted	534,570	26.19
Exercised	(550,911)	15.56
Forfeited	(455,114)	26.78
Outstanding on December 31, 2004	3,027,953	$ 24.18

Information about non-qualified stock options at December 31, 2004 is as follows:

Options Outstanding				Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life in Years	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
$ 11.90-$15.08	1,197,729	3.7	$ 13.14	605,680	$ 13.64
$ 18.02-$27.00	804,507	3.4	22.86	185,321	18.42
$ 27.04-$37.55	556,655	4.7	34.56	341,049	35.69
$ 40.73-$44.88	469,062	2.6	42.28	420,280	42.47
$ 11.90-$44.88	3,027,953	3.6	$ 24.18	1,552,330	$ 26.86

12. Comprehensive Income (Loss)

SFAS No. 130, "Reporting Comprehensive Income," establishes standards for reporting comprehensive income (loss). Comprehensive income (loss) includes net income (loss) as currently reported under generally accepted accounting principles in the United States and also considers the effect of additional economic events that are not required to be reported in determining net income (loss), but rather are reported as a separate component of stockholders' equity. The Company reports foreign currency translation gains and losses and unrealized gains and losses on available-for-sale investments, net of tax, as components of comprehensive income (loss). The components of comprehensive income (loss) for the years ended December 31, 2004, 2003 and 2002 are as follows:

	2004	2003	2002
Net income (loss)	$82,308	$(80,668)	$(40,162)
Change in foreign currency translation adjustment	1,979	7,953	4,640
Change in unrealized gain on available-for-sale investments, net of tax in 2002	342	(57)	48
Comprehensive income (loss)	$84,629	$(72,772)	$(35,474)

13. Basic and Diluted Earnings (Loss) Per Common Share

A reconciliation of the basic and diluted earnings (loss) per share, and the shares used in the computation, for the years ended December 31, 2004, 2003 and 2002 is as follows:

	2004	2003	2002
Basic earnings (loss) per common share:			
Net income (loss) available to common stockholders	$82,308	$(80,668)	$(40,162)
Weighted average common shares outstanding	18,941	18,217	18,107
Basic earnings (loss) per common share	$ 4.35	$ (4.43)	$ (2.22)
Diluted earnings (loss) per common share:			
Net income (loss) available to common stockholders	$82,308	$(80,668)	$(40,162)
Weighted average common shares outstanding	18,941	18,217	18,107
Dilutive common shares	1,071	—	—
Weighted average diluted common shares outstanding	20,012	18,217	18,107
Diluted earnings (loss) per common share	$ 4.11	$ (4.43)	$ (2.22)

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

For the years ended December 31, 2003 and 2002, there were approximately 0.7 million and 0.9 million dilutive common shares, respectively, that were not included in the computation of the loss per common share because the effect of their inclusion would be anti-dilutive.

Options to purchase 0.9 million, 1.9 million and 3.0 million shares of common stock that were outstanding during 2004, 2003 and 2002, respectively, were not included in the computation of diluted earnings per share as the exercise prices of these options were greater than the average market price of the common shares.

14. Restructuring Charges

In 2001, the Company began the restructuring of its business to better align costs with expected net revenue levels. During 2002, 2003 and 2004, the Company recorded restructuring charges of $48.5 million, $29.4 million and $0.6 million, respectively.

The following table summarizes the workforce reductions and the restructuring charges for the years ended December 31, 2002, 2003 and 2004:

	Employee Reductions			Restructuring Charges		
Restructuring Charges by Year:	Consultants	All Other	Total	Employee-related	Office-related	Total
2002	112	290	402	$ 22,560	$ 25,972	$ 48,532
2003	7	25	32	3,946	25,497	29,443
2004	—	—	—	(63)	613	550

In 2002, the Company recorded $48.5 million of restructuring charges which include $22.6 million of severance and other related costs, $23.3 million related to the consolidation and closing of offices and $2.6 million of goodwill and intangible asset write-offs. By segment, the restructuring charges recorded in 2002 are as follows: North America $19.7 million, Latin America $0.6 million, Europe $24.7 million, Asia Pacific $0.7 million and Corporate $2.8 million. Of the $48.5 million of restructuring charges recorded in 2002, approximately $36.1 million represents cash charges.

In 2003, the Company recorded restructuring charges of $29.4 million. The charges include severance and other employee-related costs of $3.9 million related to reductions in workforce, primarily in Europe, expense of $22.2 million to increase accruals for leased properties that had been identified as excess in previous office consolidation charges and $3.3 million of expense for goodwill and other intangible impairment, related primarily to a wholly-owned subsidiary in Finland which was converted to a licensee. The accruals for excess real estate were increased to reflect the expectation of longer vacancy periods due primarily to weakness in the real estate markets in which the leased properties are located. The restructuring charges by segment are as follows: North America $7.0 million, Europe $22.1 million, and Corporate $0.3 million. Of the $29.4 million of restructuring charges recorded in 2003, approximately $25.8 million represents cash charges.

In the fourth quarter of 2004, the Company recorded $0.6 million of restructuring charges to reflect changes in lease estimates primarily due to a tenant default on a sublease and the final determination and payment of certain severance-related restructuring accruals.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The table below outlines the restructuring charges along with related cash payments and non-cash write-offs for each of the years in the three-year period ended December 31, 2004:

	Employee-related	Office-related	Other Cash Charges	Total
Accrued restructuring charges as of December 31, 2001	$ 4,981	$ 23,282	$ 267	$ 28,530
Restructuring charges	22,560	25,972	—	48,532
Cash payments	(12,635)	(12,494)	(267)	(25,396)
Non-cash write-offs	(2,903)	(9,527)	—	(12,430)
Accrued restructuring charges as of December 31, 2002	12,003	27,233	—	39,236
Restructuring charges	3,946	25,497	—	29,443
Cash payments	(9,506)	(9,724)	—	(19,230)
Non-cash write-offs	—	(3,661)	—	(3,661)
Accrued restructuring charges as of December 31, 2003	6,443	39,345	—	45,788
Restructuring charges (benefit)	(63)	613	—	550
Cash payments	(4,002)	(9,969)	—	(13,971)
Non-cash write-offs	—	(126)	—	(126)
Accrued restructuring charges as of December 31, 2004	$ 2,378	$ 29,863	$ —	$ 32,241

The majority of the accrued restructuring charges as of December 31, 2004 relates to real estate leases which require cash payments through the lease term, reduced by sub-lease income, or until such time in which negotiations with the lessor to terminate the lease are completed. Based on current estimates, of the $32.2 million of restructuring charges unpaid as of December 31, 2004, approximately $10.6 million is expected to be paid in 2005 with the remainder payable in years subsequent to 2005.

15. Significant Warrant Monetization

In 2001, the Company received warrants to purchase 1,194,308 shares of Class B common stock of Google Inc. (“Google”) at a price of $0.30 per share issued in connection with recruitment fees. On August 19, 2004, the Company exercised the warrants pursuant to their cashless exercise feature and received 1,190,092 shares of Google common stock.

In multiple transactions on September 13, 2004 and September 14, 2004, the Company sold all the shares of common stock of Google that it held in ordinary brokerage transactions at an average price of $108.22 less expenses associated with the transactions resulting in aggregate net proceeds of approximately $128.8 million.

Pursuant to the terms of the Company’s compensation policy with respect to warrants, 55% of the net proceeds from these sales of shares of common stock of Google is payable to our consultants involved with the search in the month following the monetization. The Company’s current Chief Executive Officer, Thomas J Friel, was a member of this search team and will receive 25% of the consultants’ team share. Mr. Friel’s share is solely related to his work as a search consultant in 2001, at which time he was not the Company’s Chief Executive Officer. Mr. Friel has elected to defer receipt of his share of the net proceeds until 2005 under an existing deferred compensation plan. The remaining 75% of the consultants’ team share of the net proceeds, approximately $53.1 million, was paid in October 2004.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

16. Realized and Unrealized Gains (Losses) on Equity and Warrant Portfolio

The realized and unrealized gains (losses) on the equity and warrant portfolio, net of the consultants' share of the gains (losses) and other costs, for the years ended December 31, 2004, 2003 and 2002 are as follows:

	2004	2003	2002
Realized gains on investments	$57,041	$688	$ 1,630
Unrealized gains (losses) on derivative instruments	31	(15)	(2,955)
Net realized and unrealized gains (losses) on equity and warrant portfolio, net of the consultant's share of the gains (losses)	$57,072	$673	$(1,325)

During 2004, the Company recognized realized gains of $57.0 million, net of the consultants' share of the gain and other costs, including $56.8 million related to the monetization of its shares of common stock of Google.

17. Income Taxes

The sources of income (loss) before income taxes for the years ended December 31, 2004, 2003 and 2002 are as follows:

	2004	2003	2002
United States	$77,375	$ (5,970)	$(27,323)
Foreign	9,724	(15,854)	(24,330)
Income (loss) before income taxes	$87,099	$(21,824)	$(51,653)

The provision for (benefit from) income taxes for the years ended December 31, 2004, 2003 and 2002 is as follows:

	2004	2003	2002
Current—			
Federal	$ 12,216	$ —	$(12,446)
State and local	1,355	254	1,988
Foreign	1,730	2,413	12,375
Deferred	(10,510)	56,177	(13,408)
Total provision for (benefit from) income taxes	$ 4,791	$58,844	$(11,491)

A reconciliation of the provision for (benefit from) income taxes for the years ended December 31, 2004, 2003 and 2002 to income taxes at the statutory U.S. federal income tax rate of 35% is as follows:

	2004	2003	2002
Income tax provision (benefit) at the statutory U.S. federal rate	$ 30,485	$ (7,638)	$(18,078)
State income tax provision (benefit), net of federal tax benefit	1,374	(224)	(1,588)
Nondeductible expenses	(799)	614	4,679
Effect of foreign tax credits	—	—	(15,127)
Foreign tax higher than U.S.	2,577	2,292	4,120
Increase (decrease) in valuation allowance	(29,754)	57,889	14,700
Vesting of restricted stock units	—	4,273	—
Other, net	908	1,638	(197)
Total provision for (benefit from) income taxes	$ 4,791	$58,844	$(11,491)

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The deferred tax amounts have been classified in the Consolidated Balance Sheets as of December 31, 2004 and 2003 as follows:

	2004	2003
Current deferred tax assets	$ 19,764	$ 16,638
Current deferred tax liabilities	(541)	(117)
Valuation allowance	(16,479)	(16,521)
Current deferred tax asset, net	2,744	—
Non-current deferred tax assets	50,492	77,705
Non-current deferred tax liabilities	(2,289)	(7,616)
Valuation allowance	(40,437)	(70,089)
Non-current deferred tax asset, net	7,766	—
Net deferred tax assets	$ 10,510	$ —

The deferred tax assets and liabilities as of December 31, 2004 and 2003 are attributable to the following components:

	2004	2003
Deferred tax assets attributable to:		
Receivable allowances	$ 1,213	$ 1,648
Accrued vacations	1,633	1,254
Accrued bonuses	3,997	9,081
Liability for nonqualified retirement plans	6,286	6,239
Other accrued expenses	4,787	6,492
Leasehold improvements and equipment	3,232	2,438
Foreign net operating loss carryforwards	15,791	15,706
Write-down of investments	402	6,855
Goodwill	933	3,410
Accrued restructuring charges	12,503	17,331
Deferred compensation	10,601	—
Unrealized foreign currency exchange losses	695	—
Federal and state tax benefit on net operating loss carryforwards	244	10,874
U.S. foreign tax credit carryforwards	6,572	13,015
Deferred tax assets, before valuation allowance	68,889	94,343
Deferred tax liabilities attributable to:		
System development costs	—	(2,941)
Unrealized gain on equity and warrant portfolio	(921)	(1,280)
Prepaid expenses	(505)	—
Other	(36)	(3,512)
Deferred tax liabilities	(1,462)	(7,733)
Valuation allowance	(56,917)	(86,610)
Net deferred tax assets	$ 10,510	$ —

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Judgment is required in developing our income tax provision, including the determination of deferred tax assets and liabilities and any valuation allowances that might be required against the deferred tax assets. In assessing the need for a valuation allowance, the Company considered all positive and negative evidence, including scheduled reversals of deferred tax liabilities, tax-planning strategies, projected future taxable income and recent financial performance. In 2003, 2002 and 2001, the Company reported net losses, primarily due to restructuring activities necessary to align our cost structure with expected net revenue levels. SFAS No. 109, “Accounting for Income Taxes,” states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years. In considering how the loss was created, evidence indicating that the loss was unusual, infrequent, or an aberration, rather than a continuing condition is an example of positive evidence that might support a conclusion that a valuation allowance is not needed when there is negative evidence. Until the fourth quarter of 2003, the Company considered the fact that the cumulative losses were primarily the result of the restructuring charges along with other positive evidence to be sufficient to support a conclusion that a valuation allowance was not needed. However, when the Company recorded a restructuring charge totaling $22.5 million in the fourth quarter of 2003, management no longer felt it appropriate, for purposes of SFAS No. 109, to regard the restructuring charges as unusual, infrequent, or as an aberration, based on the number of restructuring charges recorded in the last three years and the magnitude of the charge taken in the fourth quarter of 2003. As a result, the significant negative evidence of cumulative losses in recent years could not be overcome by other positive evidence, most of which was subjective in nature. Based upon the provisions of SFAS No. 109, the Company recorded, in the fourth quarter of 2003, a full valuation allowance against its net deferred tax assets.

At the time the Company recorded a full valuation allowance against its net deferred tax assets, the Company anticipated that it would generate a loss for U.S. income tax purposes in 2004, due primarily to the timing of tax deductions related to restructuring charges recorded in prior years, and therefore did not anticipate recording or paying any U.S. federal income tax in 2004. These tax estimates excluded the affects of any warrant monetizations due to the uncertainty of the amount and timing of such transactions.

As a result of a significant warrant monetization in the third quarter of 2004, the Company generated income in 2004 for U.S. income tax purposes. Accordingly, the Company determined that a lesser valuation allowance is required related to net deferred tax assets associated with tax deductions that will be available for carryback to recover taxes paid in the current year and recorded a $10.5 million reduction to the income tax expense and the valuation allowance.

The Company anticipates that the effective tax rate will continue to fluctuate in the future due to the mix of earnings and profits in the jurisdictions in which it operates. While the Company expects to be profitable in 2005 and beyond, there is no assurance that future taxable income will be sufficient to realize the benefit of the deferred tax assets. If after future assessments of the realizability of the deferred tax assets, the Company determines a lesser allowance is required, the Company would record a reduction to the income tax expense and the valuation allowance in the period of such determination.

The tax benefit for stock option deductions in excess of financial reporting deductions is recognized as an increase in Additional Paid In Capital on the Company’s consolidated balance sheet. When realization of the deferred tax asset is more likely than not to occur, the benefit related to the valuation allowance release attributable to stock option deductions will be recognized as an increase in Additional Paid In Capital. At December 31, 2004, the benefit related to the valuation allowance release attributable to stock option deductions to be recognized as an increase to Additional Paid In Capital was $2.7 million.

At December 31, 2004, the Company has $51.4 million of loss carryforwards related to its foreign tax filings. Depending on the tax rules of the foreign tax jurisdictions, the losses can be carried forward indefinitely

or the carryforward periods are limited, ranging from 5 years to 15 years. The Company also has U.S. foreign tax credits of $6.6 million, which expire in 2010 through 2012.

As of December 31, 2004, the Company had unremitted earnings held in its foreign subsidiaries of approximately $19 million. The Company has not recognized a deferred tax liability for the unremitted earnings of its foreign operations that arose in 2004 and prior years because the Company currently does not expect to remit those earnings in the foreseeable future. Determination of the amount of unrecognized deferred tax liability related to unremitted earnings of foreign subsidiaries is not practicable. A deferred tax liability will be recognized if and when the Company is no longer able to demonstrate that it plans to permanently reinvest unremitted earnings.

18. Segment Information

The Company operates its executive search and complementary leadership services in four geographic regions: North America which includes the United States (except Miami) and Canada; Latin America, which includes Mexico and the rest of Latin America, as well as Miami, which serves as the gateway office to the region; Europe; and Asia Pacific.

For segment purposes, reimbursements of out-of-pocket expenses classified as revenue are reported separately and therefore are not included in the net revenue by geographic region. The Company believes that analyzing trends in revenue before reimbursements (net revenue) and analyzing operating expenses as a percentage of net revenue more appropriately reflects the Company’s core operations.

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The revenue, operating income (loss), depreciation and amortization, and capital expenditures, by segment, for the years ended December 31, 2004, 2003 and 2002 are as follows:

	2004	2003	2002
Revenue:			
North America	$201,751	$172,043	$194,241
Latin America	12,659	11,242	11,020
Europe	129,323	113,034	124,391
Asia Pacific	31,699	21,615	21,060
Revenue before reimbursements (net revenue)	375,432	317,934	350,712
Reimbursements	22,744	22,683	26,133
Total	$398,176	$340,617	$376,845
Operating income (loss):			
North America	$ 45,778	$ 35,994	$ 33,711
Latin America	1,104	863	(2,775)
Europe	3,593	(3,818)	(3,209)
Asia Pacific	6,312	2,258	1,497
Total regions	56,787	35,297	29,224
Corporate	(27,577)	(28,150)	(27,755)
Operating income before restructuring charges	29,210	7,147	1,469
Restructuring charges	(550)	(29,443)	(48,532)
Total	$ 28,660	$ (22,296)	$ (47,063)
Depreciation and amortization:			
North America	$ 5,847	$ 5,631	$ 5,760
Latin America	421	393	431
Europe	4,363	5,886	7,098
Asia Pacific	754	846	787
Total regions	11,385	12,756	14,076
Corporate	1,800	1,317	1,186
Total	$ 13,185	$ 14,073	$ 15,262
Capital expenditures:			
North America	$ 1,982	$ 2,116	$ 1,747
Latin America	211	207	215
Europe	2,545	1,715	2,236
Asia Pacific	401	974	343
Total regions	5,139	5,012	4,541
Corporate	882	794	660
Total	$ 6,021	$ 5,806	$ 5,201

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The identifiable assets, and goodwill and other intangible assets, by segment, at December 31, 2004 and 2003 are as follows:

	December 31,	
	2004	2003
Identifiable assets:		
North America	$ 63,026	$ 64,801
Latin America	7,078	5,139
Europe	137,715	138,057
Asia Pacific	28,575	21,165
Total regions	236,394	229,162
Corporate	184,890	75,268
Total	$ 421,284	$ 304,430
Goodwill and other intangible assets, net:		
North America	$ 21,509	$ 22,099
Latin America	—	—
Europe	32,573	32,735
Asia Pacific	1,626	1,564
Total regions	55,708	56,398
Corporate	—	—
Total	$ 55,708	$ 56,398

19. Guarantees

The Company has issued a letter of credit and guarantees on the payment of lease commitments for office space for certain subsidiaries in Europe and Asia Pacific. The guarantees were made to secure the respective lease agreements. The guarantees are for the term of the lease agreements, which extend through 2009. For each guarantee issued, if the subsidiary defaults on a lease payment, the Company would have to perform under the guarantee. The maximum amount of undiscounted payments the Company would be required to make in the event of default is approximately $8.9 million as of December 31, 2004. No amount has been accrued for the Company's obligation under these guaranty arrangements.

20. Commitments and Contingencies

Operating Leases

The Company leases office space in various buildings for its own use. The terms of these office-related leases provide that the Company pay base rent and a share of increases in operating expenses and real estate taxes in excess of defined amounts. These leases expire at various dates through 2016. The Company also leases certain computer equipment, the terms of which are accounted for as operating leases. Rent expense, which includes the base rent, operating expenses and real estate taxes, and the costs of equipment leases for the years ended December 31, 2004, 2003 and 2002, was $29.8 million, $32.0 million and $35.5 million, respectively.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Minimum future office space and equipment lease payments due in each of the next five years and thereafter are as follows:

	Office Leases	Equipment Leases	Total
Year ending December 31,			
2005	$ 30,445	$ 1,404	$ 31,849
2006	27,533	909	28,442
2007	25,806	339	26,145
2008	22,919	170	23,089
2009	20,306	104	20,410
Thereafter	22,877	133	23,010
Total	$149,886	$ 3,059	$152,945

The aggregate minimum future lease payments on office leases is $149.9 million. The Company has contractual sub-lease arrangements to receive aggregate sublease income of $18.4 million related to certain leases that expire at various dates through 2016. The sublease income relates to properties which were sublet as part of the office consolidations and closings announced in 2003, 2002 and 2001. See Note 14, *Restructuring Charges*, for additional information.

Certain of the leases provide for renewal options and the payments of real estate taxes and other occupancy costs. In addition, certain leases contain rent escalation clauses that require additional rental amounts in later years of the term. Rent expense for leases with rent escalation clauses is recognized on a straight-line basis over the minimum lease term.

Litigation

The Company has contingent liabilities from various pending claims and litigation matters arising in the course of the Company’s business, some of which involve claims for damages that are substantial in amount. Some of these matters are covered by insurance. Although the Company’s ultimate liability in these matters cannot be determined, based upon information currently available, the Company believes the ultimate resolution of such claims and litigation will not have a material adverse effect on its financial condition, results of operations or liquidity.

In December 2002, Mt. Sinai Medical Center of Miami filed suit against the Company regarding a search for a chief executive officer that the Company performed in 1998 seeking damages, including between $59 million and $75 million based primarily upon the operating loss incurred by Mt. Sinai in 2001, the chief executive officer’s last year at the hospital. On June 30, 2004, the judge presiding over this case in the U.S. District Court for the Southern District of Florida granted summary judgment, dismissing all the claims made by Mt. Sinai. Mt Sinai has filed an appeal with respect to this decision. While there can be no assurance as to the outcome, the Company believes that the claims are without merit.

21. Subsequent Event

In February 2005, the Company announced that it expects to record restructuring charges of between $9 million and $15 million for severance and office closures and consolidations beginning in the second quarter of 2005. The restructuring charges relate primarily to the European region where initiatives are underway to improve operating margin in order to meet our profitability objectives.

SCHEDULE II

HEIDRICK & STRUGGLES INTERNATIONAL, INC.

VALUATION AND QUALIFYING ACCOUNTS

Allowance for Doubtful Accounts:	Balance at Beginning of Year	Charged to Costs & Expenses	Deduction Including Currency Translation	Balance at End of Year
Year Ended December 31,				
2004	$ 4,387	(668)	(670)	$ 3,049
2003	$ 6,527	(989)	(1,151)	$ 4,387
2002	$ 12,923	1,871	(8,267)	$ 6,527

See accompanying Report of Independent Registered Public Accounting Firm.

PART II (continued)

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports filed under the Exchange Act is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

As of December 31, 2004, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports the Company files or submits under the Exchange Act is recorded, processed, summarized and reported as and when required.

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2004 using criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and concluded that the Company maintained effective internal controls over financial reporting as of December 31, 2004.

Because of its inherent limitations, although designed and operated to provide reasonable assurance that the objectives of the control system are met, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies may deteriorate.

Our assessment of the effectiveness of our internal control over financial reporting as of December 31, 2004 has been audited by KPMG LLP, an independent registered public accounting firm, as stated in their report which is included on page 71.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Heidrick & Struggles International, Inc.:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control Over Financial Reporting (page 70), that Heidrick & Struggles International, Inc. maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Heidrick & Struggles International, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Heidrick & Struggles International, Inc. maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Also, in our opinion, Heidrick & Struggles International, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Heidrick & Struggles International, Inc. and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2004, and our report dated March 10, 2005 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP

Chicago, Illinois
March 10, 2005

Changes in Internal Control Over Financial Reporting

During 2004, the Company has taken a number of steps that have improved the effectiveness of internal control over financial reporting including increasing the levels of review, documenting the reviews that have been performed, utilizing outside resources, including subject matter experts, and additional training of staff. More specifically, the Company has identified and implemented improvements in internal controls over financial reporting in the following areas.

- The Company has utilized significant outside resources to supplement the Company's tax function and to support the preparation of tax related financial matters.
- The Company has improved its procedures for reviewing the calculation of basic and diluted average shares outstanding.
- The Company has adopted internal controls related to certain out-of-pocket expenses that are reimbursed by our clients. Historically, the Company had not established a receivable for reimbursable expenses incurred but not yet billed as the amount was determined to be immaterial. During the fourth quarter of 2004, the Company enhanced its estimation technique relating to reimbursable expenses.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required by this Item will be included under the captions “Election of Directors,” “Nominees for Director,” “Class 2006 Directors,” and “Class 2007 Directors” in our 2005 Proxy Statement and is incorporated herein by reference. See also “Executive Officers” included in Part I of this report.

In addition, information required by this Item will be included under the caption “Audit Committee,” in our 2005 Proxy Statement and is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item will be included under the captions “Executive Compensation—Summary Compensation Table,” “Executive Compensation—Option Grant Table,” “Executive Compensation—Aggregated Option Exercises and Year-End Option Values” and “Employment Agreements” in our 2005 Proxy Statement and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this Item will be included under the caption “Voting Securities of Certain Beneficial Owners and Management” in our 2005 Proxy Statement and is incorporated herein by reference.

Equity Compensation Plan Information

The following table sets forth additional information as of December 31, 2004, about shares of our common stock that may be issued upon the exercise of options and other rights under our existing equity compensation plans and arrangements, divided between plans approved by our stockholders and plans or arrangements not submitted to the stockholders for approval.

	(a)	(b)	(c)
Plan Category	**Number of securities to be issued upon exercise of outstanding options, warrants and rights**	**Weighted-average exercise price of outstanding options, warrants and rights**	**Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))**
Equity compensation plans approved by stockholders (1)	3,391,412(2)	$ 24.18	2,617,595
Equity compensation plans not approved by stockholders	—	—	—
Total equity compensation plans	3,391,412	$ 24.18	2,617,595

(1) For a description of the types of securities that may be issued under our GlobalShare Program I and GlobalShare Program II (collectively, the “Plan”), please read Note 11, *Stock-Based Compensation*, in the Notes to Consolidated Financial Statements contained in Item 8 to this annual report on Form 10-K. The amount of any type of security to be issued under the Plan is to be determined by the Compensation Committee at the date of grant.

(2) Includes 363,459 restricted stock units.

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ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this Item will be included under the caption "Certain Relationships and Related Transactions" in our 2005 Proxy Statement and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this Item will be included under the caption "Principal Accountant Fees and Services" in our 2005 Proxy Statement and is incorporated herein by reference.

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PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) THE FOLLOWING DOCUMENTS ARE FILED AS PART OF THIS REPORT:

1. Index to Consolidated Financial Statements:

   See Consolidated Financial Statements included as part of this Form 10-K beginning on page 38.

2. Financial Statement Schedules:

	Page
Schedule II—Valuation and Qualifying Accounts	69

3. Exhibits:

Exhibit No.	Description
3.01	Amended and Restated Certificate of Incorporation of the Registrant (Incorporated by reference to Exhibit 3.02 of this Registrant's Registration Statement on Form S-4 (File No. 333-61023))
3.02	Amended and Restated By-laws of the Registrant (Incorporated by reference to Exhibit 3.02 of the Registrant's Form 10-K Filed March 26, 2003)
4.01	Specimen Stock Certificate (Incorporated by reference to Exhibit 4.01 of this Registrant's Registration Statement on Form S-4 (File No. 333-61023))
10.01	Credit Agreement among Heidrick & Struggles International, Inc., the Lenders party thereto and JPMorgan Chase Bank, as administrative Agent (Incorporated by reference to Exhibit 10.01 of the Registrants Form 10-K, filed March 12, 2004)
10.02	Amendment No. 1 to Credit Agreement between Heidrick & Struggles International, Inc., the Lenders Party Hereto and JPMorgan Chase Bank, as Administrative Agent dated December 22, 2003 (Incorporated by reference to Exhibit 10.01 of the Registrant's Form 10-Q filed August 6, 2004)
10.03	Employment Agreement of Thomas J. Friel (Incorporated by reference to Exhibit 10.01 of the Registrants From 10-Q filed on August 14, 2003)
10.04	Employment Agreement of Jocelyn Dehnert (Incorporated by reference to Exhibit 10.02 of the Registrants From 10-Q filed on May 15, 2003)
10.05	Employment agreement of Eileen A. Kamerick (Incorporated by reference to Exhibit 10.02 of the Registrant's Form 10-Q filed on August 6, 2004)
*10.06	Employment Agreement of Jeff R. Scherb
*10.07	Employment Agreement of Bonnie W. Gwin
*10.08	Employment Agreement of L. Kevin Kelly
10.09	Heidrick & Struggles International, Inc. Restricted Stock Unit Plan (Incorporated by reference to Exhibit 4.03 of this Registrant's Registration Statement on Form S-8 (File No. 333-32544))
10.10	Amendment No. 1 to the Heidrick & Struggles Restricted Stock Unit Plan (Incorporated by reference to Exhibit 99.05 of the Registrant's Form 10-K filed on March 29, 2002)
10.11	Heidrick & Struggles International, Inc. Deferred Compensation Plan (Incorporated by reference to Exhibit 4.1 of this Registrant's Registration Statement on Form S-8 (File No. 333-82424))
10.12	Form of Heidrick & Struggles Non-Qualified Stock Option Agreement (Incorporated by reference to Exhibit 10.01 of the Registrant's Form 10-Q filed on November 9, 2004)

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Exhibit No.	Description
10.13	Form of Heidrick & Struggles Restricted Stock Unit Participation Agreement (Incorporated by reference to Exhibit 10.02 of the Registrant's Form 10-Q filed on November 9, 2004)
*21.01	Subsidiaries of the Registrant
*23.01	Consent of Independent Registered Public Accounting Firm
*31.1	Certification of the Company's Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
*31.2	Certification of the Company's Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
*32.1	Certification of the Company's Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
*32.2	Certification of the Company's Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Filed herewith.

(b) REPORTS ON FORM 8-K

On October 28, 2004 we furnished a report under Item 2.02 and Item 9.01 regarding a news release reporting our 2004 third quarter financial results.

(c) SEE EXHIBIT INDEX ABOVE

(d) FINANCIAL STATEMENTS NOT PART OF ANNUAL REPORT

None

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized in the City of Chicago, State of Illinois, on March 11, 2005.

HEIDRICK & STRUGGLES INTERNATIONAL, INC.

By /S/ EILEEN A. KAMERICK
Title Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on March 11, 2005.

Signature	Title
/S/ THOMAS J. FRIEL Thomas J. Friel (principal executive officer)	Chairman, Chief Executive Officer and Director
/S/ EILEEN A. KAMERICK Eileen A. Kamerick (principal financial and accounting officer)	Chief Financial Officer
/S/ RICHARD I. BEATTIE Richard I. Beattie	Director
/s/ ANTONIO BORGES Antonio Borges	Director
/S/ JOHN A. FAZIO John A. Fazio	Director
/s/ JILL KANIN-LOVERS Jill Kanin-Lovers	Director
/S/ ROBERT E. KNOWLING, JR. Robert E. Knowling, Jr.	Director
/S/ GERARD R. ROCHE Gerard R. Roche	Director
/s/ V. PAUL UNRUH V. Paul Unruh	Director
/S/ DOUGLAS C. YEARLEY Douglas C. Yearley	Director

Exhibit 10.06

HEIDRICK & STRUGGLES
INTERNATIONAL

Stephanie W. Abramson
Chief Legal Officer
Chief Corporate Development Officer
Corporate Secretary

July 12, 2002

PERSONAL & CONFIDENTIAL

Mr. Jeff R. Scherb
3363 White Eagle Drive
Naperville, Illinois 60564

Dear Jeff:

On behalf of Heidrick & Struggles, Inc., 1 am pleased to confirm the terms of your employment to you, subject to the approval of the Board of Directors of Heidrick & Struggles International, Inc.

Start Date: You will commence employment on September 9, 2002.

Title. You will serve as Chief Information Officer reporting to the Chief Executive Officer of Heidrick & Struggles International, Inc. (the "Company"). You will also have the internal title of Senior Partner. You will be a member of the Global Operating Committee ("GOC") or its equivalent. Initially you will be located in the Company's corporate offices in Chicago.

Base Salary. Your base salary is $300,000 annually, subject to review on a 24-month basis.

Target Bonus. Your target bonus for 2003 will be 100% of base salary to be paid when bonuses are paid to executive officers in March of 2004, in accordance with the Company's Management Incentive Plan. Your bonus for 2002 will be $150,000 and will be paid when bonuses are paid to executive officers in March of 2003. Bonuses (other than your 2002 bonus) are discretionary and are not earned until approved by the Compensation Committee and/or the Board of Directors of the Company and, subject to the provisions of the Change in Control Severance Plan, will be payable only if you are in the Company's employ on the regular bonus payment date.

245 Park Avenue New York, NY 10167-0152 Phone: 212/551-1639 Fax: 046/487-0412 Voice Mail: 800/846-8456 Email: _____

Incentive Compensation and Other Plans. You will be eligible to participate in the incentive and other executive compensation plans applicable to members of GOC and executive officers, including, without limitation, the performance share plan, the annual bonus plan and the management stock option plan which have been provided to you. In 2003, you will receive a grant of 20,000 options under the Management Stock Option Plan and an award of 10,000 shares under the Performance Share Plan for the three-year period ending in 2006. In addition, as soon as administratively feasible after your start date you will receive a pro-rated award under the Performance Share Plan for the Performance Cycle ending in 2005. You will also be eligible to participate in the Change In Control Severance Plan in Tier One and the Severance Plan in the tier for Top Management.

Sign-On Arrangements.

Options. You will receive a stock option grant to purchase 20,000 shares of Heidrick & Struggles International, Inc. common stock as soon as administratively feasible after you commence employment. The options will be granted at the closing price of the common stock as reported on NASDAQ on the trading day on which you commence employment, will vest at the rate of one-third on each of the first, second and third anniversaries of the date of grant and will have a term of 5 years from the date of grant; provided, however, that all of your unvested options shall vest immediately if the Company terminates your employment without Cause or you resign for Good Reason prior to the date on which all of such options have vested.

Restricted Stock. You will receive an award of 10,000 restricted shares of Heidrick & Struggles International, Inc. common stock as soon as administratively feasible after you commence employment. Such shares will vest at the rate of 50% on March 31, 2003 and 25% on each of September 30, 2003 and 2004; provided, however, that all of your unvested restricted stock shall vest immediately if the Company terminates your employment without Cause or you resign for Good Reason prior to the date on which all such restricted stock has vested.

The term “Good Reason” shall mean (i) a diminution of the amount of your base salary or target bonus or benefits or level of eligibility for stock options or other incentive programs unless such diminution is consistent with other employees at your level; (ii) the elimination of your position or a diminution of responsibilities associated with your position, or (iii) a requirement by the company that you perform your duties on a full-time basis in the Chicago corporate office.

The term “Cause” shall mean (a) fraud, or the embezzlement or misappropriation of funds or property of the Company or any of its affiliates by you, the conviction of, or the entrance of a plea of guilty or nolo contendere by you, to a felony, or a crime involving moral turpitude; (b) neglect, misconduct or willful malfeasance which is materially

injurious to the Company or any of its affiliates; or (c) willful failure or refusal to perform your duties, or a willful, material breach of contract.

Benefits. You will be eligible to participate in the Company's benefit programs and will receive a detailed guide shortly after your starting date. The Company's benefit programs include group health and life/AD&D insurance, long-term disability, short-term disability salary continuation, time-off benefits (vacation, paid holidays, paid sick time), the Flexible Spending Account and the Heidrick & Struggles, Inc. 401(k) Profit-Sharing and Retirement Plan. The Company's benefit programs, bonus programs and polices are reviewed from time to time by Company management and may be modified, amended, or terminated at any time.

Expenses. The Company's Physical Examinations Policy will apply to you effective immediately upon your employment commencement date. The Financial Planning Program for Senior Partners will also apply to you. The Company will reimburse you for all of your business expenses in accordance with its policies.

Confidentiality. Your employment with the Company under this Agreement necessarily involves your access to and understanding of certain trade secrets and confidential information pertaining to the business of the Company and its affiliates. During the term of your employment with the Company and thereafter, you will not, directly or indirectly, without the prior written consent of the Company, disclose or use for the benefit of any person, corporation or other entity, or for yourself any and all files, trade secrets or other confidential information concerning the internal affairs of the Company and its affiliates, including, but not limited to, information pertaining to its clients, services, products, earnings, finances, operations, methods or other activities; provided, however, that the foregoing shall not apply to information which is of public record or is generally known, disclosed or available to the general public or the industry generally (other than as a result of your breach of this covenant). Notwithstanding the foregoing, you may disclose such information as is required by law during any legal proceeding or to your personal representatives and professional advisers and, with respect to such personal representatives and professional advisers, you shall inform them of your obligations hereunder and take all reasonable steps to ensure that such professional advisers do not disclose the existence or substance thereof. Further, you shall not. directly or indirectly, remove or retain, and upon termination of employment for any reason you shall return to the Company, any records, computer disks, computer printouts, business plans or any copies or reproductions thereof, or any information or instruments derived therefrom, arising out of or relating to the business of the Company and its affiliates or obtained as a result of your employment by the Company.

Non-Solicitation/Non-Competition. During the term of your employment with the Company and for a period of six-months after the termination of your employment with the Company, you shall not (i) become an employee of or consultant to any principal

competitor of the Company in substantially the same function as your employment with the Company or its affiliates in the twelve-months prior to termination of your employment or (ii) directly or indirectly solicit or hire, or assist any other person in soliciting or hiring, any employee of the Company or its affiliates (as of your termination of employment with the Company) or any person who, as of such date, was in the process of being recruited by the Company or its affiliates, or induce any such employee to terminate his or her employment with the Company or its affiliates.

Other Legal Matters.

You will be an "employee at will" unless or until you and the Company otherwise agree in writing. The purpose of this arrangement is to permit either of us to terminate employment and compensation at any time with or without Cause or Good Reason, except for such period of notice as may be expressly provided in writing under written Company employment policies in effect at the time of such termination. Your initial and continuing employment will be subject to your having the ability to work legally in the United States.

You have advised the Company that your execution and performance of the terms of this Agreement do not and will not violate any other agreement binding on you or the rights of any third parties and you understand that in the event this advice is not accurate the Company will not have any obligation to you under this Agreement.

This letter agreement contains our entire understanding and can be amended only in writing and signed by you and the Chief Executive Officer. You specifically acknowledge that no promises or commitments have been made to you that are not set forth in this letter.

Any controversy or claim arising out of or relating to this agreement or for the breach thereof, or your employment, including without limitation any statutory claims (for example, claims for discrimination including but not limited to discrimination based on race, sex, sexual orientation, religion, national origin, age, marital status, handicap or disability; and claims relating to leaves of absence mandated by state or federal law), breach of any contract or covenant (express or implied), tort claims, violation of public policy or any other alleged violation of statutory, contractual or common law rights (and including claims against the Company's officers, directors, employees or agents) if not otherwise settled between the parties, shall be conclusively settled by arbitration to be held in New York, New York, in accordance with the American Arbitration Association's Employment Dispute Resolution Rules (the "Rules"). Arbitration shall be the parties' exclusive remedy for any such controversies, claims or breaches. The parties agree they shall not seek any award for punitive damages for any claims they may have under this Agreement. The parties also consent to personal jurisdiction in New York, New York with respect to such arbitration. The award resulting from such arbitration shall be final

and binding upon both parties. Judgment upon said award may be entered in any court having jurisdiction.

You and the Company hereby waive the right to pursue any claims, including but not limited to employment termination - related claims, through civil litigation outside the arbitration procedures of this provision, unless otherwise required by law. You and the Company each have the right to be represented by counsel with respect to arbitration of any dispute pursuant to this paragraph. The arbitrator shall be selected by agreement between the parties, but if they do not agree on the selection of an arbitrator within 30 days after the date of the request for arbitration, the arbitrator shall be selected pursuant to the Rules.

In the event of any arbitration hereunder, the parties agree each shall bear its or his own attorneys' fees and costs associated with or arising from such arbitration or other proceeding.

Yours sincerely,

/s/ Stephanie W. Abramson

Stephanie W. Abramson
Chief Legal Officer

I hereby accept the terms and conditions of employment as outlined above:

/s/ Jeff Scherb — 7-21-02

Jeff Scherb — Date

HEIDRICK & STRUGGLES

Consultants in Executive Search

October 1, 1997

PERSONAL AND CONFIDENTIAL

Ms. Bonnie W. Gwin
3505 Croydon Drive, N.W.
Canton, Ohio 44718

Dear Bonnie:

I am pleased to confirm Heidrick & Struggles, Inc.'s offer of employment to you.

We are looking forward to your arrival and want to set forth our understanding:

1. You will join our Cleveland Office recruiting staff with the title of Consultant at a monthly base salary of $12,500 (which is $150,000 annually), commencing on your first day of employment, which shall be November 10, 1997, unless otherwise mutually agreed. Currently salaries are reviewed annually in November/ December, so that your first salary review will be in November/ December 1998.

2. You will first be eligible to be considered for a discretionary bonus for the bonus year ending on September 30, 1998. Currently all bonuses are paid in December. You understand that, except for the sign-on and minimum bonuses referred to below, all bonuses are discretionary and not earned until declared by the Board of Directors or the Executive Committee of the Board of Directors, and that all discretionary, incentive and/or minimum bonuses are payable only if you are in our employ on the bonus payment dates. A copy of our current U.S. Partner/Consultant Cash Compensation Policy is enclosed with this letter.

   As we discussed, you will receive bonuses as follows:

   A. Sign-On Bonus. You will receive a $75,000 sign-on bonus payable with your first paycheck.

B. Fiscal Year 1998 Minimum Bonus. You will receive a $175,000 minimum bonus for the bonus year ending September 30, 1998 payable in quarterly installments starting December 1997, payable when bonuses are paid for the 1997 fiscal year.

C. Fiscal Year 1999 and 2000 Minimum Bonus. Further, you will a receive minimum bonus of $150,000 for the bonus year ending September 30, 1999; and a minimum bonus of $125,000 for the bonus year ending September 30, 2000, payable when bonuses are paid for those fiscal years.

Our actual fee and SOB expectations of you are as follows:

Fiscal Year	Fee	SOB
November 1, 1997 to September 30, 1998	$ 900,000	$ 600,000
October 1, 1998 to September 30, 1999	$ 1,000,000	$ 800,000
October 1, 1999 to September 30, 2000	$ 1,250,000	$ 1,000,000

with future years' numbers exceeding the foregoing (after inflation). You understand that you are expected to be a "self-starter" and you have stated that you will be developing business from your industry contacts.

3. You will be eligible to participate in our fringe benefit programs in accordance with the programs' terms. Copies of the booklets and Summary Plan Descriptions describing our group health, life/AD&D insurance, long-term disability, time-off benefits such as vacation, paid holidays, paid sick time, short-term disability salary continuation, and the Flexible Spending Account and Heidrick & Struggles, Inc. 401(k) Profit-Sharing and Retirement Plan will be provided at a later date.

4. Our fringe benefit programs, bonus programs, and policies are reviewed from time to time by the company's management. Therefore, our programs and policies may be modified, amended or terminated at any time.

5. You will be an "employee at will" unless or until we may otherwise agree in writing. This gives both of us maximum flexibility and permits either of us to terminate employment and compensation at any time for any reason.

6. Two copies of an agreement relating to trade secrets, confidential information, clients, et cetera, are enclosed. We ask that all Consultants sign this agreement. Please review and sign both copies and return one to me for processing. Of course, please call me if you have any questions about this agreement.
7. You have advised us that you have not signed any agreements that will, in any way, affect your joining our firm or the performance of your work with us.
8. This agreement, which contains our entire understanding, can be amended only in a writing which is signed by you, the Cleveland Managing Partner, together with either the CEO or CFO of the company. You specifically acknowledge that no promises or commitments have been made to you that are not set forth in this letter.

To acknowledge your acceptance of our offer of employment, please sign and return to me the enclosed copy of this letter, together with the agreement referred to in Item 6 above.

Sincerely

/s/ CHARLES E. WALLACE, JR.

Charles E. Wallace, Jr.
Office Managing Partner

Enclosures

cc: Richard D. Nelson
Patrick S. Pittard

ACCEPTED:

/s/ BONNIE W. GWIN
Bonnie W. Gwin

10/5/97
Date

June 9, 2003

Bonnie W. Gwin
3505 Croydon Drive NW
Canton, OH 44718

Dear Bonnie:

I set out below the compensation and other arrangements for your role in the management of the North American region and your client facing responsibilities. This agreement is between Heidrick & Struggles International, Inc. (a Delaware corporation, and any successor (the firm)) and Bonnie W. Gwin (the Employee). As agreed in your earlier conversations with colleagues, the terms of your agreement are as follows:

1. Employment

The Firm shall employ the Employee as Managing Partner, North American Operations and the Employee agrees and accepts such a position. The Employee shall report to the Chief Executive Officer and shall devote substantially all of her business time and attention to the performance of her duties and responsibilities in the best interests of the Firm. The Employee will remain her client facing responsibilities and, specifically, will remain as Practice Managing Partner, Technology and Professional Services Practice.

2. Compensation

The Employee's compensation will comprise the following elements:

a. Annual Base Salary

Effective June 1, 2003, the Employee will receive an annual base salary of **$350,000** pursuant to the Firm's normal payroll procedures.

b. Fee and Source of Business Bonus Plan

The Employee will participate in the Firm's Fee and SOB Bonus Plan in the same way as other North American consultants save that for the year to 31 December 2003 there will be an off-set of **$150,000** of the Employee's base salary against the tier-base compensation. We will review and agree the level of any base salary set off for the year 31 December 2004 by no later than 31 December 2003.

The Employee will receive a guaranteed minimum bonus of **$125,000** for the calendar year 2003, payable pursuant to the normal bonus payment schedule.

c. <u>Incentive Plans</u>

The Employee will be eligible for the Employer's Management Incentive Plan, Management Stock Option Plan, Change in Control Severance Plan, Performance Share Plan, and the Deferred Compensation Plan.

1. Management Incentive Plan (MIP)

   The Employee will be in Tier 1 of the MIP and the Employee's Target Bonus will be **$200,000.**

   The Employee may earn from **0% to 150%** of the Target Bonus based on Firm performance against its Profitability (Operating Income) target, the Employee's Strategic Business Unit (SBU) performance (if applicable) against specific financial metrics, and the Employee's own individual performance against Key Performance Indicators (KPIs). The Employee's KPIs should be developed in collaboration with the CEO within the next 30 days. The Company's Operating Income target for the 2003 MIP is:

Threshold	Target	Maximum
$6.4 MM	$9.8 MM	$18.0 MM

   It is important for the Employee to know that the Company must meet its Threshold level of Operating Income before any MIP bonuses may be paid out.

2. Management Stock Option Plan (MSOP)

   The Employee received **50,000** Stock Options under the MSOP

   The exercise price for these options is $11.90, which was the fair market value of the Firm's stock at closing on the date of grant, March 6, 2003. Your stock options will vest ratably over three years and have a five-year term from the date of grant.

3. Change in Control Severance Plan

   The Employee will participate in Tier 1 of the Change in Control Severance Plan.

4. Performance Share Plan **(Actual number needs to be inserted)**

Performance Shares are like phantom shares of HSII Stock. You will be eligible to earn from **0% to 150%** of your target number of Performance Shares at the end of the three-year PSP cycle based on the Company's cumulative performance against Operating Income Targets. Operating Income is critical to long-term growth and building shareholder value. The better the Company performs against its targets during the PSP cycle, the more Performance Shares you will earn. Further, the more HSII Stock grows during the performance cycle, the more your earn-out will be worth. The PSP Targets for cycle 2, 2003 to 2005, are:

	Cymulative Operating Income
Threshold	**$45.4 MM**
Target	**$56.8 MM**
Maximum	**$68.2 MM**

5. Deferred Compensation Plan

The Employee will be eligible to participate in the US Deferred Compensation Plan.

6. Other Plans

The Employee will be eligible to participate in all other savings and retirement plans, policies, practices and programs of the Firm, which are made generally available to other employees of the Firm.

Yours sincerely,

/S/ JOIE GREGOR

Joie Gregor
President, North America

Date

cc: Grover N. Wray

I have read and accept the terms of this agreement:

/S/ BONNIE W. GWIN — 6/24/03

Bonnie W. Gwin

Date

HEIDRICK & STRUGGLES

Consultants in Executive Search

May 27, 1997

Mr. L. Kevin Kelly
Homat Green Hill #120
4-2-8 Shibuya, Shibuya-ku
Tokyo, Japan

Dear Kevin:

Thank you for taking the time with our key partners. We are very much looking forward to having you as a member of the H&S family worldwide. Based on the parameters we discussed previously, we are pleased to confirm Heidrick & Struggles Japan Co. Ltd.'s offer of employment to you and want to set forth our agreement, which is as follows:

1. Employment:

   You will join our Tokyo, Japan, branch office ("Company") on July 15th, 1997, with the title of Partner to perform the duties of an executive search consultant as you have agreed to perform those duties for us. You will report to the Tokyo Office Managing Partner with the understanding that we may change this at any time. As an executive search Partner, the Company will expect you to achieve an acceptable level of Fee and Source of Business Credits after a reasonable break-in period. Based on your level of experience, we expect that your Fee and Source of Business Credits (Execution Fee plus Business Development) will be at least ¥150,000,000 for our fiscal year ending September 30th, 1998, and ¥170,000,000 for our fiscal year ending September 30th, 1999, with the following year's figures exceeding the foregoing after inflation.

2. Probationary Period:

   As is customary in Japan, you shall serve a six-month probationary period from the effective date of employment. During this probationary period we shall determine if you are suitable for the duties referred to in Item 1 above. Should we determine, during this period, that you are, for any reason, unsuitable for the position, we may terminate this agreement and your employment with the company with no liability whatsoever. Along the same lines, you may decide that H&S does not offer you the type of employment that you are comfortable with.

3. Compensation:

   Your compensation will consist of Items 4 through 8 below.

Kasurnigaseki Building Suite 3118 3-2-5 Kasurnigaseki Chiyoda-ka Tokyo 100 Phone: 03-3500-5310 FAX: 03-3500-5350

4. Wages (Base):

Your monthly base salary will be ¥1,330,000 (¥15,960,000 annually). Your position with the Company is an exempt position and does not qualify for overtime pay. The monthly base salary will be paid on the 24th of each month. We may revise your monthly salary, taking into consideration your work performance and ability. Currently, salaries are reviewed in November of each year; therefore your first salary review will be in November, 1998.

5. Housing Allowance and Home Leave:

You will receive ¥650,000 per month as housing allowance. This amount will be paid at the time you move in one year from now*. You are also entitled to one home leave per year. We will cover the cost of airline tickets for you and your family one time per year.

* This could be sooner depending your circumstances.

6. Local District Tax (Tokyo Ward):

Your Tokyo Ward taxes will be paid by H&S for the tax year of 1997, beginning July 15th, 1997 and thereafter.

7. Discretionary Bonus:

You will be eligible for an annual Partner's Incentive Bonus for our fiscal year ending September 30th, 1997, and you will be paid in December of that year. Currently these types of bonuses are discretionary and are not earned until declared by the Board of Directors or the Executive Committee of the Board of Directors. Further, all discretionary and incentive bonuses are paid only if you are in our employ on the bonus payment dates. A Partner Incentive Bonus is calculated based on performance and guided by a published formula. However, we will guarantee a minimum bonus of ¥25,000,000 for the fiscal year ending in 1998. As agreed, there will be no guaranteed bonus for the 1997 fiscal year. When the guarantee expires, your bonus will be calculated based on the formula and paid to you in full. This calculation will include your base salary, housing allowance and district tax as the base line.

8. Commuting Allowance:

We will pay your commuting expenses in full. This amount will be added to your regular monthly salary. We are currently not encouraging the use of a private car as a method of commuting. In the future, we may re-examine this commuting method.

9. Retirement Plan:

As we discussed, H&S Japan Co. Ltd. may establish a retirement plan in 1997 for its employees after studying other professional firms' retirement programs in Japan.

10. Work Hours:

Your regular work hours will be between 9:00 a.m. and 5:00 p.m. We may change the regular work hours from time to time depending on business circumstances.

11. Holidays and Paid Vacations:

Holidays and paid vacations shall be in accordance with company policy.

12. Confidentiality Agreement:

Three copies of an agreement relating to trade secrets, confidential information, clients, et cetera, are enclosed. We ask all of our employees to sign this agreement. Please review and sign all three copies and return two of them to us for processing.

13. Rules of Employment:

The terms and conditions of your employment shall be governed by the provisions, provided, however, that if in the future we establish any Rules of Employment, any conflicting terms and conditions of employment shall be governed by the Rules of Employment.

14. No Conflicting Agreement:

As you have advised us, you have not and will not sign any agreement that will, in any way, affect your joining our firm or the performance of your work for us. However, as you have informed us, we understand that there may be some minor exceptions.

15. Entire Agreement and Amendment:

This agreement contains our entire understanding and can be amended only in the form of a written amendment signed by you and either the President or Treasurer of the Company.

Please confirm your acceptance of this employment agreement by signing and returning to me the enclosed copy of this letter, together with the agreement referred to in item 12 above. We are all looking forward to working with you to build solid worldwide and Japan Financial practices.

Sincerely,

/s/ Koichi "Kris" Fukuda

Koichi "Kris" Fukuda
Managing Partner

cc:	Mr. Tom Friel	phone 415-234-1500	fax 415-854-4191
	Mr. Rick Nelson	phone 312-496-1795	fax 312-496-1290

I accept the above position and agree to the above terms.

/s/ L. Kevin Kelly
L. Kevin Kelly

5-27-97
Date

Addendum:

1. Moving Expenses will be paid for by H.S.

2. Premium for Medical / Dental Insurance will be paid by H.S.

3. Tax preparation by A.A. will be paid by H.S.

4. Continuing Membership at American Club.

5. Home Trip back to the U.S. (one-way) in case of termination.

Exhibit 21.01

SUBSIDIARIES OF REGISTRANT

HEIDRICK & STRUGGLES, INC., a Delaware corporation
HEIDRICK & STRUGGLES ASIA-PACIFIC, LTD., an Illinois corporation
HEIDRICK & STRUGGLES JAPAN, LTD., an Illinois corporation
HEIDRICK & STRUGGLES AUSTRALIA, LTD., an Illinois corporation
HEIDRICK & STRUGGLES HONG KONG LTD., an Illinois corporation
HEIDRICK & STRUGGLES SINGAPORE PTE LTD., a Singapore corporation
HEIDRICK & STRUGGLES (INDIA) PRIVATE LIMITED, an India corporation
HEIDRICK & STRUGGLES (KOREA), INC., a Korea corporation
HEIDRICK & STRUGGLES FAR EAST LIMITED (Hong Kong), a Hong Kong corporation
HEIDRICK & STRUGGLES TAIWAN LIMITED, a Taiwan corporation
HEIDRICK & STRUGGLES CANADA, INC., a Canada corporation
HEIDRICK & STRUGGLES ARGENTINA, S.A., an Argentina corporation
HEIDRICK & STRUGGLES LATIN AMERICA, INC., an Illinois corporation
HEIDRICK & STRUGGLES DE CHILE LIMITADA, a Chile corporation
HEIDRICK & STRUGGLES HOLDINGS DO BRASIL LTDA, a Brazilian corporation
HEIDRICK & STRUGGLES DO BRASIL LTDA, a Brazilian corporation
HEIDRICK & STRUGGLES, S.A. de C.V., a Mexico corporation
HEIDRICK & STRUGGLES ESPANA, INC., an Illinois corporation
HEIDRICK & STRUGGLES AB, a Sweden corporation
HEIDRICK & STRUGGLES INTERNATIONAL SRL, an Italy corporation
HEIDRICK & STRUGGLES Sp.zo.o, a Poland corporation
HEIDRICK & STRUGGLES AG, a Switzerland corporation
HEIDRICK & STRUGGLES BV, a Netherlands corporation
HEIDRICK & STRUGGLES CONSULTORES de GESTAO Lda, a Portugul corporation
HEIDRICK & STRUGGLES UNTERNEHMENSBERATUNG GmbH & Co. KG, a Germany Limited Partnership
HEIDRICK & STRUGGLES UNTERNEHMENSBERATUNG VERWALTUNG, GmbH, a Germany Limited Liability Company
HEIDRICK & STRUGGLES LTD., an Israel corporation
HEIDRICK & STRUGGLES UNTERNEHMENSBERATUNG, GmbH, an Austria corporation
HEIDRICK & STRUGGLES UK LIMITED, a UK corporation
H&S SOFTWARE DEVELOPMENT and KNOWLEDGE MANAGEMENT CENTRE PRIVATE LIMITED, an India corporation
SHPA ESOP, LTD., a UK corporation
LEADERSONLINE, LIMITED, a Cayman Islands corporation
LEADERSONLINE EUROPE S.A.R.L, a Luxembourg corporation
LEADERSONLINE NETHERLANDS B.V., a Netherlands corporation
HEIDRICK & STRUGGLES DUTCH PARTNERSHIP, a Netherlands partnership
BEIJING HEIDRICK & STRUGGLES INTERNATIONAL MANAGEMENT CONSULTING COMPANY LIMITED, a China Limited Partnership (Joint Venture 90% Ownership)
PROTEM GMBH, a Germany Limited Liability Company

Exhibit 23.01

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors
Heidrick & Struggles International, Inc.:

We consent to the incorporation by reference in the registration statements (No. 333-82424, No. 333-58118, No. 333-32544, and No. 333-73443) on Form S-8 of Heidrick & Struggles International, Inc. of our reports dated March 10, 2005, with respect to the consolidated balance sheets of Heidrick & Struggles International, Inc. as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2004, and the related financial statement schedule, management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2004 and the effectiveness of internal control over financial reporting as of December 31, 2004, which reports appear in the December 31, 2004 annual report on Form 10-K of Heidrick & Struggles International, Inc.

/S/ KPMG LLP

Chicago, Illinois
March 10, 2005

Exhibit 31.1

CERTIFICATION

I, Thomas J. Friel, certify that:

1. I have reviewed this annual report on Form 10-K of Heidrick & Struggles International, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrants's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ THOMAS J. FRIEL

Chief Executive Officer

Dated: March 11, 2005

Exhibit 31.2

CERTIFICATION

I, Eileen A. Kamerick, certify that:

1. I have reviewed this annual report on Form 10-K of Heidrick & Struggles International, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrants's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ EILEEN A. KAMERICK

Chief Financial Officer

Dated: March 11, 2005

Exhibit 32.1

CERTIFICATION
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), the undersigned officer of Heidrick & Struggles International, Inc., a Delaware corporation (the “Company”), does hereby certify that:

The Annual Report on Form 10-K for the year ended December 31, 2004 (the “Form 10-K”) of the Company fully complies with the requirements of section 13 (a) or 15 (d) of the Securities Exchange Act of 1934 and the information contained in the Form 10-K fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ THOMAS J. FRIEL

Chief Executive Officer

Dated: March 11, 2005

Exhibit 32.2

CERTIFICATION
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), the undersigned officer of Heidrick & Struggles International, Inc., a Delaware corporation (the "Company"), does hereby certify that:

The Annual Report on Form 10-K for the year ended December 31, 2004 (the "Form 10-K") of the Company fully complies with the requirements of section 13 (a) or 15 (d) of the Securities Exchange Act of 1934 and the information contained in the Form 10-K fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Eileen A. Kamerick

Chief Financial Officer

Dated: March 11, 2005