COGNIZANT TECHNOLOGY SOLUTIONS CORP
Form 10-Q
August 08, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended June 30, 2007

¨ **Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.**
For the transition period from ______ to______

Commission File Number 0-24429

COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**13-3728359**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
Glenpointe Centre West	
500 Frank W. Burr Blvd.	
Teaneck, New Jersey	**07666**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant s telephone number, including area code (201) 801-0233

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 x No: ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

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

Indicate the number of shares outstanding of each of the issuer s class of common stock, as of August 1, 2007:

Class	**Number of Shares**
Class A Common Stock, par value $.01 per share	144,661,431

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements (unaudited)

COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

AND COMPREHENSIVE INCOME

(Unaudited)

(in thousands, except per share data)

	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Revenues	$ 516,514	$ 336,836	$ 976,784	$ 622,315
Operating expenses:				
Cost of revenues (exclusive of depreciation and amortization expense shown separately below)	292,326	188,320	547,235	346,908
Selling, general and administrative expenses	120,464	80,044	229,963	146,749
Depreciation and amortization expense	13,053	7,801	25,313	14,831
Income from operations	90,671	60,671	174,273	113,827
Other income, net:				
Interest income	6,450	3,853	13,121	7,290
Other income net	529	1,508	512	1,467
Total other income, net	6,979	5,361	13,633	8,757
Income before provision for income taxes	97,650	66,032	187,906	122,584
Provision for income taxes	15,373	10,961	30,183	20,349
Net income	$ 82,277	$ 55,071	$ 157,723	$ 102,235
Basic earnings per share	$ 0.57	$ 0.39	$ 1.10	$ 0.73
Diluted earnings per share	$ 0.54	$ 0.37	$ 1.04	$ 0.68
Weighted average number of common shares outstanding Basic	144,052	140,542	143,477	140,103
Dilutive effect of shares issuable under stock option plans	7,996	9,951	8,426	9,821
Weighted average number of common shares outstanding Diluted	152,048	150,493	151,903	149,924
Comprehensive income:				
Net income	$ 82,277	$ 55,071	$ 157,723	$ 102,235
Foreign currency translation adjustments	1,690	4,218	2,298	4,940
Total comprehensive income	$ 83,967	$ 59,289	$ 160,021	$ 107,175

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements.

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COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(Unaudited)

(in thousands, except par values)

	June 30, 2007	December 31, 2006
Assets		
Current assets:		
Cash and cash equivalents	$ 268,985	$ 265,937
Short-term investments	441,251	382,222
Trade accounts receivable, net of allowances of $5,283 and $3,719, respectively	348,878	259,210
Unbilled accounts receivable	54,721	39,265
Deferred income tax assets, net	78,728	61,257
Other current assets	37,007	32,500
Total current assets	1,229,570	1,040,391
Property and equipment, net of accumulated depreciation of $117,436 and $95,539, respectively	265,749	220,154
Goodwill	43,351	27,190
Intangible assets, net	14,755	20,463
Deferred income tax assets, net	6,275	1,024
Other assets	24,654	16,759
Total assets	$ 1,584,354	$ 1,325,981
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 24,619	$ 27,839
Deferred revenue	15,004	19,401
Accrued expenses and other current liabilities	219,496	202,263
Total current liabilities	259,119	249,503
Other noncurrent liabilities	7,992	2,979
Total liabilities	267,111	252,482
Commitments and Contingencies (See Notes 2 and 5)		
Stockholders equity:		
Preferred stock, $.10 par value, 15,000 shares authorized, none issued		
Class A common stock, $.01 par value, 500,000 shares authorized, 144,603 and 142,513 shares issued and outstanding, at June 30, 2007 and December 31, 2006, respectively	1,446	1,425
Additional paid-in-capital	494,571	410,019
Retained earnings	807,150	650,277
Accumulated other comprehensive income	14,076	11,778
Total stockholders equity	1,317,243	1,073,499
Total liabilities and stockholders equity	$ 1,584,354	$ 1,325,981

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements.

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COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands)

	For the Six Months Ended June 30, 2007	2006
Cash flows from operating activities:		
Net income	$ 157,723	$ 102,235
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	25,313	14,831
Provision for doubtful accounts	1,622	847
Deferred income taxes	(23,570)	(1,734)
Stock-based compensation expense	16,950	14,371
Tax benefit related to stock option exercises	32,466	15,751
Excess tax benefit on stock option exercises	(30,401)	(14,563)
Changes in assets and liabilities:		
Trade accounts receivable	(91,604)	(74,209)
Other current assets	(19,580)	(21,028)
Other assets	(7,454)	(2,742)
Accounts payable	(1,876)	6,973
Other current liabilities	4,932	6,940
Net cash provided by operating activities	64,521	47,672
Cash flows from investing activities:		
Purchases of property and equipment	(70,871)	(44,989)
Purchases of short-term investments	(302,725)	(186,899)
Proceeds from maturity or sale of short-term investments	244,702	148,867
Net cash used in investing activities	(128,894)	(83,021)
Cash flows from financing activities:		
Proceeds from issued shares	35,988	22,872
Excess tax benefit on stock option exercises	30,401	14,563
Cash flows provided by financing activities	66,389	37,435
Effect of currency translation on cash and cash equivalents	1,032	4,081
Increase in cash and cash equivalents	3,048	6,167
Cash and cash equivalents, beginning of year	265,937	196,938
Cash and cash equivalents, end of period	$ 268,985	$ 203,105

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements.

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COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(dollar amounts in thousands)

Note 1 Interim Condensed Consolidated Financial Statements

The accompanying unaudited condensed consolidated financial statements included herein have been prepared by Cognizant Technology Solutions Corporation (Cognizant or the Company) in accordance with generally accepted accounting principles in the United States of America and Article 10 of Regulation S-X under the Securities and Exchange Act of 1934, as amended, and should be read in conjunction with the Company s consolidated financial statements (and notes thereto) included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006. In the opinion of the Company s management, all adjustments considered necessary for a fair presentation of the accompanying unaudited condensed consolidated financial statements have been included, and all adjustments are of a normal and recurring nature. Operating results for the interim periods are not necessarily indicative of results that may be expected to occur for the entire year. Certain reclassifications have been made to prior year numbers to conform to the current year presentation.

Note 2 Acquisitions

In connection with the acquisition of substantially all the assets of Fathom Solutions, LLC (Fathom) in April 2005, additional purchase price, not to exceed $16,000, payable in 2007, was contingent on Fathom achieving certain financial and operating targets over the two years ended April 30, 2007. As of June 30, 2007, the Company accrued approximately $12,000 of additional purchase price due to the sellers of Fathom and allocated this additional purchase price to goodwill. Payment of the $12,000 of additional purchase price was made in July 2007. In addition, the Company increased goodwill and decreased intangible assets by approximately $4,000 in connection with the final allocation of purchase price relating to the acquisition of AimNet Solutions, Inc.

Note 3 Short-term Investments

The following is a summary of short-term investments:

	June 30, 2007	December 31, 2006
Available-for-sale securities		
Auction rate securities	$ 382,350	$ 330,275
Other	13,002	13,137
Total available-for-sale securities	395,352	343,412
Time deposits	45,899	38,810
Total short-term investments	$ 441,251	$ 382,222

The carrying value of the short-term investments approximated fair value as of June 30, 2007 and December 31, 2006. Realized gains or losses, if any, on these investments were insignificant for the periods presented.

Note 4 Income Taxes

The Company adopted the provisions of Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of SFAS No. 109 (FIN 48), on January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes by prescribing a minimum recognition threshold for a tax position taken or expected to be taken in a tax return that is required to be met before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. The cumulative effect of adopting FIN 48 of $850 was recorded as a reduction to beginning retained earnings and an increase to noncurrent liabilities. The total amount of unrecognized tax benefits as of the date of adoption was $7,700 of which $7,500 would impact the effective income tax rate if recognized. During the three months ended June 30, 2007, the Company recognized a tax benefit of $740 for certain foreign tax positions that were effectively settled. Included in the balance of unrecognized tax benefits as of January 1, 2007, is $2,921 related to certain U.S. Federal and state unrecognized tax benefits that could reasonably be recognized during the next 12 months due to expiration of statutes of limitations.

The Company continues to classify accrued interest and penalties related to unrecognized tax benefits in income tax expense. At January 1, 2007, the Company had $614 accrued for interest relating to certain tax matters in India. The Company has not accrued interest on U.S. unrecognized tax benefits as the Company currently has net operating loss carry forwards that would mitigate any current interest cost.

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As of January 1, 2007, the Company is subject to U.S. Federal income tax examinations for the years 2003 through 2006 and various state and local income tax examinations for the tax years 2000 through 2006. The Company is also subject to examination in India and other foreign jurisdictions for the tax years 2001 through 2006. Currently, the Company is under income tax examination in India. The Company does not believe that the outcome of any examination will have a material effect on its financial statements.

Our Indian subsidiary, Cognizant India, is an export-oriented company, which, under the Indian Income Tax Act of 1961, is entitled to claim tax holidays for a period of ten consecutive years for each Software Technology Park (STP) with respect to export profits for each STP. Substantially all of the earnings of Cognizant India are attributable to export profits. The majority of the Company s STP s in India are currently entitled to a 100% exemption from Indian income tax. Under current law, these tax holidays will be completely phased out by March of 2009. The incremental Indian taxes related to the taxable STP s have been incorporated into the Company s effective income tax rate for 2007. The effective tax rate of 15.7% and 16.1%, respectively, for the three and six months ended June 30, 2007 decreased from 16.6% for the three and six months ended June 30, 2006 primarily due to the Company s overall growth, which resulted in a greater percentage of Cognizant India s revenue falling under the income tax holiday, net reductions in statutory income tax rates and a net benefit from the effective settlement of certain foreign income tax positions during the quarter ended June 30, 2007. The principal difference between the effective income tax rates for the 2007 and 2006 periods and the Company s U.S. federal statutory rate is the effect of the income tax holiday in India.

Note 5 Commitments and Contingencies

As of June 30, 2007, the Company had outstanding fixed capital commitments of approximately $91,110 related to its India development center expansion program.

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the outcome of such claims and legal actions, if decided adversely, is not expected to have a material adverse effect on the Company s quarterly or annual results of operations, cash flows, or consolidated financial position. Additionally, many of the Company s engagements involve projects that are critical to the operations of its customers businesses and provide benefits that are difficult to quantify. Any failure in a customer s computer system could result in a claim for substantial damages against the Company, regardless of the Company s responsibility for such failure. Although the Company attempts to contractually limit its liability for damages arising from negligent acts, errors, mistakes, or omissions in rendering its software development and maintenance services, there can be no assurance that the limitations of liability set forth in its contracts will be enforceable in all instances or will otherwise protect the Company from liability for damages. Although the Company has general liability insurance coverage, including coverage for errors or omissions, there can be no assurance that such coverage will continue to be available on reasonable terms or will be sufficient in amount to cover one or more large claims, or that the insurer will not disclaim coverage as to any future claim. The successful assertion of one or more large claims against the Company that exceed available insurance coverage or changes in the Company s insurance policies, including premium increases or the imposition of large deductible or co-insurance requirements, could have a material adverse effect on the Company s business, results of operations, cash flows and financial condition.

In connection with the split-off of the Company from IMS Health Incorporated (IMS Health) on February 13, 2003, the Company entered into a Distribution Agreement, dated January 7, 2003, with IMS Health (the Distribution Agreement), that provides, among other things, that IMS Health and the Company will comply with, and not take any action during the relevant time period that is inconsistent with, the representations made to and relied upon by McDermott, Will & Emery in connection with rendering its opinion regarding the U.S. federal income tax consequences of the exchange offer. In addition, pursuant to the Distribution Agreement, the Company indemnified IMS Health for any tax liability to which they may be subject as a result of the exchange offer but only to the extent that such tax liability resulted solely from a breach in the representations the Company made to and were relied upon by McDermott, Will & Emery in connection with rendering its opinion regarding the U.S. federal income tax consequences of the exchange offer. If the Company breaches any of its representations in connection with the Distribution Agreement, the related indemnification liability could be material to the Company s results of operations, financial position and cash flows.

Note 6 Segment Information

The Company s reportable segments are: Financial Services, which includes customers providing banking/transaction processing, capital markets and insurance services; Healthcare, which includes healthcare providers and payers as well as life sciences customers; Manufacturing/Retail/Logistics, which includes manufacturers, retailers, travel and other hospitality customers, as well as customers providing logistics services; and Other, which is an aggregation of industry segments which,

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individually, are less than 10% of consolidated revenues and segment operating profit. The Other reportable segment includes media and information services, telecommunications and high technology operating segments. The Company s sales managers, account executives, account managers and project teams are aligned in accordance with the specific industries they serve.

The Company s chief operating decision maker evaluates the Company s performance and allocates resources based on segment revenues and operating profit. Segment operating profit is defined as income from operations before unallocated costs. Expenses included in segment operating profit consist principally of direct selling and delivery costs as well as a per seat charge for use of the Company s IT development centers. Certain expenses, such as general and administrative, and a portion of depreciation and amortization, are not specifically allocated to specific segments as management does not believe it is practical to allocate such costs to individual segments because they are not directly attributable to any specific segment. Further, stock-based compensation expense is not allocated to individual segments in internal management reports used by the chief operating decision maker. Accordingly, these expenses are separately disclosed as unallocated and adjusted only against the total income from operations of the Company. Additionally, management has determined that it is not practical to allocate identifiable assets, by segment, since such assets are used interchangeably among the segments.

Revenues from external customers and segment operating profit, before unallocated expenses, for the Financial Services, Healthcare, Manufacturing/Retail/Logistics, and Other reportable segments for the three and six months ended June 30, 2007 and 2006 are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Revenues:				
Financial services	$ 243,059	$ 162,597	$ 457,239	$ 298,442
Healthcare	118,625	73,392	228,665	135,897
Manufacturing/retail/logistics	77,214	52,242	146,997	97,237
Other	77,616	48,605	143,883	90,739
Total revenue	$ 516,514	$ 336,836	$ 976,784	$ 622,315
Segment Operating Profit:				
Financial services	$ 80,809	$ 58,878	$ 155,078	$ 108,512
Healthcare	41,080	28,859	81,260	55,713
Manufacturing/retail/logistics	21,311	17,994	45,328	34,060
Other	26,363	15,758	51,585	31,293
Total segment operating profit	169,563	121,489	333,251	229,578
Less: unallocated costs(1)	78,892	60,818	158,978	115,751
Income from operations	$ 90,671	$ 60,671	$ 174,273	$ 113,827

(1) Includes $9,512 and $6,769 and $16,950 and $14,371 of stock-based compensation expense for the three months and six months ended June 30, 2007 and 2006, respectively.

Geographic Area Information

Revenue and long-lived assets, by geographic area, are as follows

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Revenues(1)				
North America(2)	$ 435,246	$ 291,797	$ 826,318	$ 539,003

Europe[3]	75,847	42,413	140,489	77,522
Asia	5,421	2,626	9,977	5,790
Total	$ 516,514	$ 336,836	$ 976,784	$ 622,315

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	As of June 30, 2007	As of December 31, 2006
Long-lived Assets[4]		
North America[2]	$ 60,617	$ 50,792
Europe	6,599	6,328
Asia[5]	256,639	210,687
Total	$ 323,855	$ 267,807

(1) Revenues are attributed to regions based upon customer location.
(2) Substantially all relates to operations in the United States.
(3) Includes revenue from operations in the United Kingdom of $48,025 and $32,081 and $90,325 and $59,311 for the three and six months ended June 30, 2007 and 2006, respectively.
(4) Long-lived assets include property and equipment and intangible assets, net of accumulated depreciation and amortization, respectively, and goodwill.
(5) Substantially all of these long-lived assets relate to the Company s operations in India.

No customer accounted for revenues in excess of 10% of total revenues for the three and six months ended June 30, 2007 and 2006.

Note 7 Recent Accounting Pronouncements

In February 2007, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, Including an Amendment of FASB Statement No. 115 (SFAS No. 159), which is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. SFAS No. 159 permits entities to measure eligible financial assets, financial liabilities and firm commitments at fair value, on an instrument-by-instrument basis, that are otherwise not permitted to be accounted for at fair value under other generally accepted accounting principles. The fair value measurement election is irrevocable and subsequent changes in fair value must be recorded in earnings. The Company is currently evaluating the impact that SFAS No. 159 will have on its consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is currently evaluating the impact that SFAS No. 157 will have on its consolidated financial statements.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.

Executive Summary

During the three and six months ended June 30, 2007, our revenue increased to $516.5 million and $976.8 million compared to $336.8 million and $622.3 million during the three and six months ended June 30, 2006. Net income increased to $82.3 million and $157.7 million, respectively, or $0.54 and $1.04 per diluted share, including stock-based compensation expense, net of tax, equal to $0.05 and $0.09 per diluted share, during the three and six months ended June 30, 2007. This is compared to net income of $55.1 million and $102.2 million, respectively, or $0.37 and $0.68 per diluted share, including stock-based compensation expense, net of tax, equal to $0.04 and $0.08 per diluted share, during the three and six months ended June 30, 2006. The key drivers of our revenue growth during the quarter ended June 30, 2007 were as follows:

- continued strength in our Financial Services Segment, particularly with our banking customers;
- strong performance of our Healthcare and Other segments, which had revenue growth of approximately 62% and 60%, respectively, for the quarter as compared to the quarter ended June 30, 2006;

expansion of our service offerings, which enabled us to cross-sell new services to our customers and meet the rapidly growing demand for complex large-scale outsourcing solutions;

increased penetration at existing customers, including strategic customers; and

greater penetration of the European market.

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We saw a continued increase in demand from our customers for a broad range of IT solutions, particularly high performance web development initiatives and complex systems development engagements, testing, enterprise resource planning, or ERP, infrastructure management, business process outsourcing and business intelligence. We finished the quarter with approximately 430 active clients compared to 270 as of June 30, 2006 and increased the number of strategic clients by five during the quarter bringing the total number of our strategic clients to 97. We define a strategic client as one offering the potential to generate between $5 million and $40 million or more in annual revenues at maturity. Our top five and top ten customers accounted for approximately 25% and 35%, respectively, of our total revenues during the quarter ended June 30, 2007 as compared to approximately 30% and 41%, respectively, for the quarter ended June 30, 2006. As we continue to add new customers and increase our penetration at existing customers, we expect the percentage of revenues from our top five and top ten customers to continue to decline over time.

In Europe, we continue to experience strong growth. During the quarter ended June 30, 2007, our revenue from European customers increased by approximately 79% to approximately $75.8 million compared to approximately $42.4 million in the quarter ended June 30, 2006. For the quarter ended June 30, 2007, revenue from Europe, excluding the UK, increased by approximately $17.5 million from approximately $10.3 million in the quarter ended June 30, 2006 to approximately $27.8 million. Europe will continue to be an area of heavy investment for us in 2007 as we see this region as a growth opportunity for the long term.

Our revenue growth is also attributed to increasing market acceptance of, and strong demand for, offshore IT services. Recent NASSCOM (India s National Association of Software and Services Companies) reports state that India s IT services export industry was expected to grow by approximately 33% during the twelve-month period ended March 31, 2007.

Our operating margin decreased to approximately 17.6% for the quarter ended June 30, 2007 compared to 18.0% for the quarter ended June 30, 2006. Excluding stock-based compensation costs of approximately $9.5 million, operating margin for the quarter ended June 30, 2007 was approximately 19.4%. This was in line with our historic targeted operating margin range, excluding stock-based compensation costs, of 19% to 20% of total revenues. Historically, we have invested the profitability above the 19% to 20% operating margin level, which excludes stock-based compensation, back into our business, which we believe is a significant contributing factor to our strong revenue growth. This investment is primarily focused in the areas of: (i) hiring client partners and relationship personnel with specific industry experience or domain expertise; (ii) training our technical staff in a broader range of IT service offerings; (iii) strengthening our business analytic capabilities; (iv) strengthening and expanding our portfolio of services; (v) continuing to expand our geographic presence for both sales and delivery; and (vi) recognizing and rewarding exceptional performance by our employees. In addition, this investment includes maintaining a deep bench of resources, trained in a broad range of service offerings, in order to be well positioned to respond to our customer requests to take on additional projects. For the year ending December 31, 2007, we expect to continue to invest amounts in excess of our historical targeted operating margin levels back into the business.

During the quarter, we experienced pressure on our cost structure due to the appreciation of the Indian rupee versus the U.S. dollar. This is in addition to the continuing wage inflation, primarily in India, that we have experienced over the last several years. During the quarter, approximately 31% of our global costs were denominated in the Indian rupee. The appreciation of the Indian rupee versus the U.S. dollar during the second quarter of 2007 as compared to the quarter ended March 31, 2007 had the effect of decreasing our operating margin by approximately 150 basis points or 1.5 percentage points. Each additional 1% appreciation of the Indian rupee will have the effect of decreasing our operating margin by approximately 20 basis points or 0.2 percentage points. In addition, the budget approved by the government of India during the second quarter of 2007, included certain provisions that will increase our operating costs. We have already implemented actions which are intended to mitigate these negative cost trends, including increasing our global utilization rates of our technical staff and reducing discretionary spending. Accordingly, we believe this balanced response will permit us to continue to maintain operating margins in our historic targeted operating margin range, which excludes stock compensation costs, of 19% to 20% of total revenues and permit us to continue to make the necessary investments to continue to grow the Company.

We finished the second quarter of 2007 with total headcount of approximately 45,550, an increase of approximately 15,875 over the total headcount at June 30, 2006. The increases in the number of our technical personnel and the related infrastructure costs, to meet the demand for our services, are the primary drivers of the increase in our operating expenses in 2007. Annualized turnover, including both voluntary and involuntary, was approximately 17% during the three months ended June 30, 2007. The majority of our turnover occurs in India. As a result, annualized attrition rates on-site at clients are below our global attrition rate. In addition, attrition is weighted towards the more junior members of our staff. We have experienced wage inflation in India, which may continue in the future; however, this has not had a material impact on our results of operations as Indian wages represented slightly more than 20% of our total operating expenses for the three months ended June 30, 2007.

We are continuing with our strategy of moving from leased facilities to owned facilities as a way of reducing overall operating costs. Our updated India real estate development program now includes planned construction of over four and a half million square feet of new space. The expanded program, which commenced during the quarter ended March 31, 2007, includes the expenditure of approximately $300 million through the end of 2009 on land acquisition, facilities construction and furnishings to build new state-of-the-art IT development centers in regions primarily designated as Special Economic Zones located in Chennai, Pune, Kolkata, Hyderabad and Coimbatore, India. Additionally, we expect to continue to expand our capacity and capabilities in Bangalore and Kochi, India. Further, we plan to lease additional space in Special Economic Zones located in India to meet our capacity requirements.

At June 30, 2007, we had cash and cash equivalents and short-term investments of $710.2 million and working capital of approximately $970.5 million. Accordingly, we do not anticipate any near-term liquidity issues.

Critical Accounting Estimates and Risks

Management s discussion and analysis of our financial condition and results of operations is based on our consolidated financial statements that have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and assumptions that affect the amounts reported for assets and liabilities, including the recoverability of tangible and intangible assets, disclosure of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. On an on-going basis, we evaluate our estimates. The most significant estimates relate to the recognition of revenue and profits based on the percentage of completion method of accounting for certain fixed-bid contracts, the allowance for doubtful accounts, income taxes, valuation of goodwill and other long-lived assets, assumptions used in valuing stock-based compensation arrangements, contingencies and litigation. We base our 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. The actual amounts may differ from the estimates used in the preparation of the accompanying unaudited condensed consolidated financial statements. Our significant accounting policies are described in Note 1 to the audited consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2006.

We believe the following critical accounting policies require a higher level of management judgments and estimates than others in preparing the consolidated financial statements:

Revenue Recognition. Revenues related to our highly complex information technology application development contracts, which are predominantly fixed-priced contracts, are recognized as the service is performed using the percentage of completion method of accounting. Under this method, total contract revenue during the term of an agreement is recognized on the basis of the percentage that each contract s cost to date bears to the total estimated cost (cost to cost method). This method is followed where reasonably dependable estimates of revenues and costs can be made. Management reviews estimated future labor costs, the driver of total expected contract costs, on an ongoing basis. Revisions to our estimates may result in increases or decreases to revenues and income and are reflected in the consolidated financial statements in the periods in which they are first identified. If our estimates indicate that a contract loss will be incurred, a loss provision is recorded in the period in which the loss first becomes probable and reasonably estimable. Contract losses are determined to be the amount by which the estimated costs of the contract exceed the estimated total revenues that will be generated by the contract and are included in cost of revenues in our unaudited condensed consolidated statement of operations. Contract losses for the 2007 and 2006 periods presented were immaterial.

Stock-Based Compensation. Under the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123R, Share-Based Payment (SFAS No. 123R), stock-based compensation cost is measured at the grant date based on the value of the award and is recognized as expense over the vesting period. Determining the fair value of stock-based awards at the grant date requires judgment, including estimating the expected term of stock options and the expected volatility of our stock. In addition, judgment is also required in estimating the income tax benefits related to the stock-based awards and the amount of stock-based awards that are expected to be forfeited. If actual results differ significantly from our estimates, stock-based compensation expense and our results of operations could be materially impacted.

Effective April 1, 2007, we are obligated to pay a fringe benefit tax related to the exercise of stock options by our employees in India and the amount of such tax was immaterial for the three months ended June 30, 2007. The tax due is recovered by us from our employees at the time of exercise. The accounting guidance for this fringe benefit tax has not yet been finalized. We will continue to follow the accounting discussion regarding the accounting for fringe benefit tax and evaluate its impact on our consolidated financial statements when the accounting for such transactions becomes final.

Income Taxes. Determining the consolidated provision for income tax expense, deferred tax assets and liabilities and related valuation allowance, if any, involves judgment. As a global company, we are required to calculate and provide for income taxes in each of the jurisdictions where we operate. This involves estimating current tax exposures in each jurisdiction as well as making judgments regarding the recoverability of deferred tax assets. Tax exposures can involve complex issues and may require an extended period to resolve. In the period of resolution, adjustments may need to be recorded that result in increases or decreases to income. Changes in the geographic mix or estimated level of annual pre-tax income can also affect the overall effective income tax rate.

On an on-going basis, we evaluate whether a valuation allowance is needed to reduce our deferred tax assets to the amount that is more likely than not to be realized. While we have considered future taxable income and on-going prudent and feasible tax planning strategies in assessing the need for the valuation allowance, in the event we determine that we will be able to realize deferred tax assets in the future in excess of the net recorded amount, an adjustment to the deferred tax asset would increase income in the period such determination was made. Likewise, should we determine that we will not be able to realize all or part of the net deferred tax asset in the future, an adjustment to the deferred tax asset would be charged to income in the period such determination was made.

Our Indian subsidiary, Cognizant India, is an export-oriented company, which, under the Indian Income Tax Act of 1961, is entitled to claim tax holidays for a period of ten consecutive years for each Software Technology Park (STP) with respect to export profits for each STP. Substantially all of the earnings of Cognizant India are attributable to export profits. The majority of our STP s in India are currently entitled to a 100% exemption from Indian income tax. Under current law, these tax holidays will be completely phased out by March of 2009. The incremental Indian taxes related to the taxable STP s have been incorporated into our effective income tax rate for 2007. In anticipation of the complete phase out of the tax holidays in March 2009, we expect to locate a portion of our new development centers in areas designated as Special Economic Zones (SEZ). Development centers operating in SEZ will be entitled to certain income tax incentives for periods up to 15 years. Under current Indian tax law, export profits after March 31, 2009 from our existing STP s will be fully taxable at the Indian statutory rate (33.99% as of June 30, 2007) in effect at such time.

Allowance for Doubtful Accounts. We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. The allowance for doubtful accounts is determined by evaluating the relative credit-worthiness of each customer, historical collections experience and other information, including the aging of the receivables. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Goodwill. We evaluate goodwill for impairment at least annually, or as circumstances warrant. When determining the fair value of our reporting units, we utilize various assumptions, including projections of future cash flows. Any adverse changes in key assumptions about our businesses and their prospects or an adverse change in market conditions may cause a change in the estimation of fair value and could result in an impairment charge. As of June 30, 2007, our goodwill balance was approximately $43.4 million.

Long-Lived Assets. In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets , we review long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In general, we will recognize an impairment loss when the sum of undiscounted expected future cash flows is less than the carrying amount of such asset. The measurement for such an impairment loss is then based on the fair value of the asset. If such assets were determined to be impaired, it could have a material adverse effect on our business, results of operations and financial condition.

Risks. Most of our IT development centers, including a majority of our employees, are located in India. As a result, we may be subject to certain risks associated with international operations, including risks associated with foreign currency exchange rate fluctuations and risks associated with the application and imposition of protective legislation and regulations relating to import and export or otherwise resulting from foreign policy or the variability of foreign economic or political conditions. Additional risks associated with international operations include difficulties in enforcing intellectual property rights, the burdens of complying with a wide variety of foreign laws, potential geo-political and other risks associated with terrorist activities and local and cross border conflicts, potentially adverse tax consequences, tariffs, quotas and other barriers. We are also subject to risks associated with our overall compliance with Section 404 of the Sarbanes-Oxley Act of 2002. The inability of our management and our independent auditor to provide us with an unqualified report as to the adequacy and effectiveness of our internal controls over financial reporting for future year ends could result in adverse consequences to us, including, but not limited to, a loss of investor confidence in the reliability of our financial statements, which could cause the market price of our stock to decline. See Part II, Item 1A. Risk Factors .

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Results of Operations

Three Months Ended June 30, 2007 Compared to Three Months Ended June 30, 2006

The following table sets forth, for the periods indicated, certain financial data expressed for the three months ended June 30:

(Dollars in thousands)

	2007	% of Revenues	2006	% of Revenues	Increase	% Increase
Revenues	$ 516,514	100.0%	$ 336,836	100.0%	$ 179,678	53.3%
Operating Expenses:						
Cost of revenues[(1)]	292,326	56.6	188,320	55.9	104,006	55.2
Selling, general and administrative[(2)]	120,464	23.3	80,044	23.8	40,420	50.5
Depreciation and amortization	13,053	2.5	7,801	2.3	5,252	67.3
Income from operations	90,671	17.6%	60,671	18.0%	30,000	49.4
Other income, net	6,979		5,361		1,618	30.2
Provision for income taxes	15,373		10,961		4,412	40.3
Net income	$ 82,277	15.9%	$ 55,071	16.3%	27,206	49.4

(1) Includes stock-based compensation expense of $4,828 in 2007 and $3,332 in 2006 and excludes depreciation and amortization expense.
(2) Includes stock-based compensation expense of $4,684 in 2007 and $3,437 in 2006 and excludes depreciation and amortization expense.

The table below includes non-GAAP income from operations, excluding stock-based compensation, a measure defined by the Securities and Exchange Commission as a non-GAAP financial measure. This non-GAAP financial measure is not based on any comprehensive set of accounting rules or principles and should not be considered a substitute for, or superior to, financial measures calculated in accordance with GAAP, and may be different from non-GAAP measures used by other companies. In addition, this non-GAAP measure, the financial statements prepared in accordance with GAAP and reconciliations of our GAAP financial statements to such non-GAAP measure should be carefully evaluated.

We seek to manage the company to targeted operating margin, excluding stock-based compensation costs, of 19% to 20% of revenues. Accordingly, we believe that non-GAAP income from operations, excluding stock-based compensation costs, is a meaningful measure for investors to evaluate our financial performance. For our internal management reporting and budgeting purposes, we use financial statements that do not include stock-based compensation expense related to employee stock options and employee stock purchases for financial and operational decision making, to evaluate period-to-period comparisons and for making comparisons of our operating results to that of our competitors. Moreover, because of varying available valuation methodologies and the variety of award types that companies can use under SFAS No. 123R, we believe that providing a non-GAAP financial measure that excludes stock-based compensation allows investors to make additional comparisons between our operating results to those of other companies. Accordingly, we believe that the presentation of non-GAAP income from operations when read in conjunction with our reported GAAP income from operations can provide useful supplemental information to our management and to investors regarding financial and business trends relating to our financial condition and results of operations.

A limitation of using non-GAAP income from operations versus income from operations reported in accordance with GAAP is that non-GAAP income from operations, excludes a cost, namely, stock-based compensation that is recurring. Stock-based compensation has been and will continue to be for the foreseeable future a significant recurring expense in our business. In addition, other companies may calculate non-GAAP financial measures differently than us, thereby limiting the usefulness of this non-GAAP financial measure as a comparative tool. We compensate for this limitation by providing specific information regarding the GAAP amounts excluded from non-GAAP income from operations and evaluating such non-GAAP financial measure with financial measures calculated in accordance with GAAP.

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A reconciliation of income from operations as reported and non-GAAP income from operations, excluding stock-based compensation expense, is as follows for the three months ended June 30:

(Dollars in thousands)

	2007	% of Revenues	2006	% of Revenues
Income from operations, as reported	$ 90,671	17.6%	$ 60,671	18.0%
Add: stock-based compensation expense	9,512	1.8	6,769	2.0
Non-GAAP income from operations, excluding stock-based compensation expense	$ 100,183	19.4%	$ 67,440	20.0%

Revenue. Revenue increased by 53.3%, or approximately $179.7 million, from approximately $336.8 million during the three months ended June 30, 2006 to approximately $516.5 million during the three months ended June 30, 2007. This increase is attributed to greater acceptance of the on-site/offshore delivery model among an increasing number of industries, continued strength in our customers discretionary spending and greater penetration in the European market. Revenue from customers existing as of June 30, 2006 increased by approximately $146.5 million and revenue from new customers added since June 30, 2006 was approximately $33.2 million or approximately 6.4% of total revenues for the three months ended June 30, 2007. In addition, revenue from European customers for the quarter ended June 30, 2007 increased by $33.4 million over the comparable 2006 quarter. We had approximately 430 active clients as of June 30, 2007 as compared to 270 active clients as of June 30, 2006. In addition, we experienced strong demand across all of our business segments for an increasingly broad range of services. Our Financial Services and Healthcare business segments accounted for approximately $80.5 million and $45.2 million, respectively, of the $179.7 million increase. Our IT consulting and technology services and IT outsourcing revenues increased by approximately 49.9% and 56.6%, respectively, compared to the quarter ended June 30, 2006 and represented approximately 47.7% and 52.3%, respectively, of total revenues for the quarter ended June 30, 2007. No customer accounted for sales in excess of 10% of revenues during the quarter ended June 30, 2007 or 2006.

Cost of Revenues (Exclusive of Depreciation and Amortization Expense). Cost of revenues consists primarily of the cost of salaries, stock-based compensation expense, payroll taxes, benefits, immigration and project-related travel for technical personnel, the cost of subcontracting and the cost of sales commissions related to revenues. Our cost of revenues increased by 55.2%, or approximately $104.0 million, from approximately $188.3 million during the three months ended June 30, 2006 to approximately $292.3 million during the three months ended June 30, 2007. The increase was primarily due to higher compensation and benefits costs of approximately $91.6 million.

Selling, General and Administrative Expenses. Selling, general and administrative expenses consist primarily of salaries, stock-based compensation expense, employee benefits, travel, promotion, communications, management, finance, administrative and occupancy costs. Selling, general and administrative expenses, including depreciation and amortization, increased by 52.0%, or approximately $45.7 million, from approximately $87.8 million during the three months ended June 30, 2006 to approximately $133.5 million during the three months ended June 30, 2007, and decreased as a percentage of revenue from 26.1% to 25.8%. The decrease as a percentage of revenues was due primarily to economies of scale that allowed us to leverage our cost structure over a larger organization.

Income from Operations. Income from operations increased 49.4%, or approximately $30.0 million, from approximately $60.7 million during the three months ended June 30, 2006 to approximately $90.7 million during the three months ended June 30, 2007, representing operating margins of 18.0% and 17.6% of revenues, respectively. The decrease in operating margin was due primarily to appreciation of the Indian rupee versus the U.S. dollar and wage inflation, primarily in India, partially offset by cost containment actions such as control of discretionary spending and scale efficiencies, including increased utilization rates of our technical staff. Excluding stock-based compensation expense of $9.5 million in 2007 and $6.8 million in 2006, operating margin for the three months ended June 30, 2007 and June 30, 2006 was 19.4% and 20.0% of revenues, respectively. On an annual basis, we expect stock-based compensation costs to continue to decrease as a percentage of total revenues.

Other Income, Net. Other income, net consists primarily of interest income and foreign currency gains or losses. The increase in other income, net of $1.6 million is attributed to an increase in interest income of $2.6 million from $3.9 million during the three months ended June 30, 2006 to approximately $6.5 million during the three months ended June 30, 2007 partially offset by a $1.0 million reduction in other income due to remeasurement of certain balance sheet accounts for movements in foreign currency rates. Interest income increased due to higher average invested cash and short-term investments balances in 2007 compared to 2006.

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Provision for Income Taxes. The provision for income taxes increased from approximately $11.0 million during the three months ended June 30, 2006 to approximately $15.4 million during the three months ended June 30, 2007. The effective tax rate of 16.6% for the three months ended June 30, 2006 decreased to 15.7% for the three months ended June 30, 2007 primarily due to our overall growth, which resulted in a greater percentage of Cognizant India s revenue falling under the income tax holiday, net reductions in statutory income tax rates and a net benefit attributed to the effective settlement of certain foreign income tax positions during the three months ended June 30, 2007.

Net Income. Net income increased from approximately $55.1 million for the three months ended June 30, 2006 to approximately $82.3 million for the three months ended June 30, 2007, representing 16.3% and 15.9% of revenues, respectively.

Six Months Ended June 30, 2007 Compared to Six Months Ended June 30, 2006

The following table sets forth, for the periods indicated, certain financial data for the six months ended June 30:

(Dollars in thousands)

	2007	% of Revenues	2006	% of Revenues	Increase	% Increase
Revenues	$ 976,784	100.0%	$ 622,315	100.0%	$ 354,469	57.0%
Operating Expenses:						
Cost of revenues (1)	547,235	56.0	346,908	55.7	200,327	57.7
Selling, general and administrative (2)	229,963	23.6	146,749	23.6	83,214	56.7
Depreciation and amortization	25,313	2.6	14,831	2.4	10,482	70.7
Income from operations	174,273	17.8%	113,827	18.3%	60,446	53.1
Other income, net	13,633		8,757		4,876	55.7
Provision for income taxes	30,183		20,349		9,834	48.3
Net income	$ 157,723	16.1%	$ 102,235	16.4%	55,488	54.3

(1) Includes stock-based compensation expense of $8,096 in 2007 and $6,479 in 2006 and excludes depreciation and amortization expense.

(2) Includes stock-based compensation expense of $8,854 in 2007 and $7,892 in 2006 and excludes depreciation and amortization expense.

The table below includes non-GAAP income from operations, excluding stock-based compensation, a measure defined by the Securities and Exchange Commission as a non-GAAP financial measure. This non-GAAP financial measure is not based on any comprehensive set of accounting rules or principles and should not be considered a substitute for, or superior to, financial measures calculated in accordance with GAAP, and may be different from non-GAAP measures used by other companies. In addition, this non-GAAP measure, the financial statements prepared in accordance with GAAP and reconciliations of our GAAP financial statements to such non-GAAP measure should be carefully evaluated.

We seek to manage the company to targeted operating margin, excluding stock-based compensation costs, of 19% to 20% of revenues. Accordingly, we believe that non-GAAP income from operations, excluding stock-based compensation costs, is a meaningful measure for investors to evaluate our financial performance. For our internal management reporting and budgeting purposes, we use financial statements that do not include stock-based compensation expense related to employee stock options and employee stock purchases for financial and operational decision making, to evaluate period-to-period comparisons and for making comparisons of our operating results to that of our competitors. Moreover, because of varying available valuation methodologies and the variety of award types that companies can use under SFAS No. 123R, we believe that providing a non-GAAP financial measure that excludes stock-based compensation allows investors to make additional comparisons between our operating results to those of other companies. Accordingly, we believe that the presentation of non-GAAP income from operations when read in conjunction with our reported GAAP income from operations can provide useful supplemental information to our management and to investors regarding financial and business trends relating to our financial condition and results of operations.

A limitation of using non-GAAP income from operations versus income from operations reported in accordance with GAAP is that non-GAAP income from operations, excludes a cost, namely, stock-based compensation that is recurring. Stock-based compensation has been and will continue to be for the foreseeable future a significant recurring expense in our business. In addition, other companies may calculate non-GAAP financial measures differently than us, thereby limiting the usefulness of this non-GAAP financial measure as a comparative tool. We compensate for this limitation by providing specific information regarding the GAAP amounts excluded from non-GAAP income from operations and evaluating such non-GAAP financial measure with financial measures calculated in accordance with GAAP.

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A reconciliation of income from operations as reported and non-GAAP income from operations, excluding stock-based compensation expense, is as follows for the six months ended June 30:

(Dollars in thousands)

	2007	% of Revenues	2006	% of Revenues
Income from operations, as reported	$ 174,273	17.8%	$ 113,827	18.3%
Add: stock-based compensation expense	16,950	1.8	14,371	2.3
Non-GAAP income from operations, excluding stock-based compensation expense	$ 191,223	19.6%	$ 128,198	20.6%

Revenue. Revenue increased by 57.0%, or approximately $354.5 million, from approximately $622.3 million during the six months ended June 30, 2006 to approximately $976.8 million during the six months ended June 30, 2007. This increase is attributed to greater acceptance of the on-site/offshore delivery model among an increasing number of industries, continued strength in our customers discretionary spending and greater penetration in the European market. Revenue from customers existing as of June 30, 2006 increased by approximately $295.3 million and revenue from new customers added since June 30, 2006 was approximately $59.2 million or approximately 6.1% of total revenues for the six months ended June 30, 2007. In addition, revenue from European customers during the six months ended June 30, 2007 increased by $63.0 million over the comparable six-month period in 2006. We had approximately 430 active clients as of June 30, 2007 as compared to 270 active clients as of June 30, 2006. In addition, we experienced strong demand across all of our business segments for an increasingly broad range of services. Our Financial Services and Healthcare business segments accounted for approximately $158.8 million and $92.8 million, respectively, of the $354.5 million increase. Our IT consulting and technology services and IT outsourcing revenues increased by approximately 50.0% and 63.8%, respectively, compared to the six months ended June 30, 2006 and represented approximately 47.5% and 52.5%, respectively, of total revenues for the six months ended June 30, 2007. No customer accounted for sales in excess of 10% of revenues during the six months ended June 30, 2007 or 2006.

Cost of Revenues (Exclusive of Depreciation and Amortization Expense). Cost of revenues consists primarily of the cost of salaries, stock-based compensation expense, payroll taxes, benefits, immigration and project-related travel for technical personnel, the cost of subcontracting and the cost of sales commissions related to revenues. Our cost of revenues increased by 57.7%, or approximately $200.3 million, from approximately $346.9 million during the six months ended June 30, 2006 to approximately $547.2 million during the six months ended June 30, 2007. The increase was primarily due to higher compensation and benefits costs of approximately $172 million.

Selling, General and Administrative Expenses. Selling, general and administrative expenses consist primarily of salaries, stock-based compensation expense, employee benefits, travel, promotion, communications, management, finance, administrative and occupancy costs. Selling, general and administrative expenses, including depreciation and amortization, increased by 58.0%, or approximately $93.7 million, from approximately $161.6 million during the six months ended June 30, 2006 to approximately $255.3 million during the six months ended June 30, 2007, and increased as a percentage of revenue from 26.0% to 26.1%. The increase in such expenses in absolute dollars was due primarily to expenses incurred to expand our sales and marketing activities and increased infrastructure expenses to support our growth.

Income from Operations. Income from operations increased 53.1%, or approximately $60.4 million, from approximately $113.8 million during the six months ended June 30, 2006 to approximately $174.3 million during the six months ended June 30, 2007, representing operating margins of 18.3% and 17.8% of revenues, respectively. The decrease in operating margin was due primarily to appreciation of the Indian rupee versus the U.S. dollar and wage inflation, primarily in India, partially offset by cost containment actions such as control of discretionary spending and scale efficiencies, including increased utilization rates of our technical staff. Excluding stock-based compensation expense of $17.0 million in 2007 and $14.4 million in 2006, operating margin for the six months ended June 30, 2007 and June 30, 2006 was 19.6% and 20.6%, respectively. On an annual basis, we expect stock-based compensation costs to continue to decrease as a percentage of total revenues.

Other Income, Net. Other income, net consists primarily of interest income and foreign currency gains or losses. The increase in other income, net of $4.9 million is attributed to an increase in interest income of $5.8 million from $7.3 million during the six months ended June 30, 2006 to approximately $13.1 million during the six months ended June 30, 2007, partially offset

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by a reduction of approximately $0.9 million in other income due to remeasurement of certain balance sheet accounts for movements in foreign currency rates. Interest income increased due to higher average invested cash and short-term investments balances in 2007 compared to 2006.

Provision for Income Taxes. The provision for income taxes increased from approximately $20.3 million during the six months ended June 30, 2006 to approximately $30.2 million during the six months ended June 30, 2007. The effective tax rate of 16.6% for the six months ended June 30, 2006 decreased to 16.1% for the six months ended June 30, 2007 primarily due to our overall growth, which resulted in a greater percentage of Cognizant India s revenue falling under the income tax holiday, net reductions in statutory income tax rates and a net benefit attributed to the effective settlement of certain foreign income tax positions during the three months ended June 30, 2007.

Net Income. Net income increased from approximately $102.2 million for the six months ended June 30, 2006 to approximately $157.7 million for the six months ended June 30, 2007, representing 16.4% and 16.1% of revenues, respectively.

Results by Business Segment

Our reportable segments are: Financial Services, which includes customers providing banking/transaction processing, capital markets and insurance services; Healthcare, which includes healthcare providers and payers as well as life sciences customers; Manufacturing/Retail/Logistics, which includes manufacturers, retailers, travel and other hospitality customers, as well as customers providing logistics services; and Other, which is an aggregation of industry operating segments which, individually, are less than 10% of consolidated revenues and segment operating profit. The Other reportable segment includes media and information services, telecommunications and high technology operating segments. Our sales managers, account executives, account managers and project teams are aligned in accordance with the specific industries they serve.

The Company s chief operating decision maker evaluates Cognizant s performance and allocates resources based on segment revenues and operating profit. Segment operating profit is defined as income from operations before unallocated costs. Generally, operating expenses for each operating segment have similar characteristics and are subject to the same factors, pressures and challenges. However, the economic environment and its effects on industries served by our operating groups may affect revenue and operating expenses to differing degrees. Expenses included in segment operating profit consist principally of direct selling and delivery costs as well as a per seat charge for use of the development centers. Certain expenses, such as general and administrative, and a portion of depreciation and amortization, are not specifically allocated to specific segments as management does not believe it is practical to allocate such costs to individual segments because they are not directly attributable to any specific segment. Further, stock-based compensation expense is not allocated to individual segments in internal management reports used by the chief operating decision maker. Accordingly, these expenses are separately disclosed as unallocated and adjusted only against the total income from operations.

Three Months Ended June 30, 2007 Compared to Three Months Ended June 30, 2006

Revenues from external customers and segment operating profit, before unallocated expenses, for the Financial Services, Healthcare, Manufacturing/Retail/Logistics, and Other reportable segments for the three months ended June 30, 2007 and 2006 are as follows:

(Dollars in thousands)

	June 30, 2007	June 30, 2006	Increase	%
Revenues:				
Financial services	$ 243,059	$ 162,597	$ 80,462	49.5%
Healthcare	118,625	73,392	45,233	61.6
Manufacturing/retail/logistics	77,214	52,242	24,972	47.8
Other	77,616	48,605	29,011	59.7
Total revenues	$ 516,514	$ 336,836	$ 179,678	53.3
Segment Operating Profit:				
Financial services	$ 80,809	$ 58,878	$ 21,931	37.2%

Healthcare	41,080	28,859	12,221	42.3
Manufacturing/retail/logistics	21,311	17,994	3,317	18.4
Other	26,363	15,758	10,605	67.3
Total segment operating profit	$ 169,563	$ 121,489	$ 48,074	39.6

Financial Services Segment

Revenue. Revenue increased by 49.5%, or approximately $80.5 million, from approximately $162.6 million during the three months ended June 30, 2006 to approximately $243.1 million during the three months ended June 30, 2007. The increase in revenue was driven by continued expansion of existing customer relationships as well as new customers. The increase in revenue from customers existing as of June 30, 2006 and customers added since such date was approximately $70.3 million and approximately $10.2 million, respectively. Within the segment, growth was particularly strong among our banking customers, where revenue increased approximately $63.9 million over the second quarter of last year. The increase can also be attributed to leveraging sales and marketing investments in this business segment as well as greater acceptance of the onsite/offshore IT services delivery model.

Segment Operating Profit. Segment operating profit increased 37.2%, or approximately $21.9 million, from approximately $58.9 million during the three months ended June 30, 2006 to approximately $80.8 million during the three months ended June 30, 2007. The increase in segment operating profit was attributable primarily to increased revenues partially offset by additional headcount to support our revenue growth, continued investment in sales and marketing, the impact of the appreciation of the Indian Rupee and wage inflation, primarily in India.

Healthcare Segment

Revenue. Revenue increased by 61.6%, or approximately $45.2 million, from approximately $73.4 million during the three months ended June 30, 2006 to approximately $118.6 million during the three months ended June 30, 2007. The increase in revenue was driven by continued expansion of existing customer relationships as well as new customers. The increase in revenue from customers existing as of June 30, 2006 and customers added since such date was approximately $40.5 million and approximately $4.7 million, respectively. Within the segment, growth was particularly strong among our healthcare customers, where revenue increased by approximately $26.9 million over the second quarter of last year. The increase can also be attributed to leveraging sales and marketing investments in this business segment as well as greater acceptance of the onsite/offshore IT services delivery model.

Segment Operating Profit. Segment operating profit increased 42.3%, or approximately $12.2 million, from approximately $28.9 million during the three months ended June 30, 2006 to approximately $41.1 million during the three months ended June 30, 2007. The increase in segment operating profit was attributable primarily to increased revenues partially offset by additional headcount to support our revenue growth, continued investment in sales and marketing, the impact of the appreciation of the Indian Rupee and wage inflation, primarily in India.

Manufacturing/Retail/Logistics Segment

Revenue. Revenue increased by 47.8%, or approximately $25.0 million, from approximately $52.2 million during the three months ended June 30, 2006 to approximately $77.2 million during the three months ended June 30, 2007. The increase in revenue within the manufacturing, logistics and retail groups was driven by continued expansion of existing customer relationships as well as new customers. The increase in revenue from customers existing as of June 30, 2006 and customers added since such date was approximately $17.6 million and approximately $7.4 million, respectively. The increase can also be attributed to leveraging sales and marketing investments in this business segment as well as greater acceptance of the onsite/offshore IT services delivery model.

Segment Operating Profit. Segment operating profit increased 18.4%, or approximately $3.3 million, from approximately $18.0 million during the three months ended June 30, 2006 to approximately $21.3 million during the three months ended June 30, 2007. The increase in segment operating profit was attributable primarily to increased revenues partially offset by additional headcount to support our revenue growth, continued investment in sales and marketing, the impact of the appreciation of the Indian Rupee and wage inflation, primarily in India.

Other Segment

Revenue. Revenue increased by 59.7%, or approximately $29.0 million, from approximately $48.6 million during the three months ended June 30, 2006 to approximately $77.6 million during the three months ended June 30, 2007. The increase in revenue was primarily due to continued expansion of existing customer relationships as well as new customers. The increase in revenue from customers existing as of June 30, 2006 and customers added since such date was approximately $18.1 million and approximately $10.9 million, respectively. Within the other segment, growth was particularly strong among our media and information services customers, where revenue increased approximately $15.1 million over the second quarter of last year. The increase can also be attributed to leveraging sales and marketing investments in this business segment and greater acceptance of the onsite/offshore IT services delivery model.

Segment Operating Profit. Segment operating profit increased 67.3%, or approximately $10.6 million from approximately $15.8 million during the three months ended June 30, 2006 to approximately $26.4 million during the three months ended June 30, 2007. The increase in segment operating profit was attributable primarily to increased revenues and achieving

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operating efficiencies, including continued leverage on prior sales and marketing investments partially offset by additional headcount to support our revenue growth, the impact of the appreciation of the Indian Rupee and wage inflation, primarily in India.

Six Months Ended June 30, 2007 Compared to Six Months Ended June 30, 2006

Revenues from external customers and segment operating profit, before unallocated expenses, for the Financial Services, Healthcare, Manufacturing/Retail/Logistics, and Other reportable segments for the six months ended June 30, 2007 and 2006 are as follows:

(Dollars in thousands)

	June 30, 2007	June 30, 2006	Increase	%
Revenues:				
Financial services	$ 457,239	$ 298,442	$ 158,797	53.2%
Healthcare	228,665	135,897	92,768	68.3
Manufacturing/retail/logistics	146,997	97,237	49,760	51.2
Other	143,883	90,739	53,144	58.6
Total revenues	$ 976,784	$ 622,315	$ 354,469	57.0
Segment Operating Profit:				
Financial services	$ 155,078	$ 108,512	$ 46,566	42.9%
Healthcare	81,260	55,713	25,547	45.9
Manufacturing/retail/logistics	45,328	34,060	11,268	33.1
Other	51,585	31,293	20,292	64.8
Total segment operating profit	$ 333,251	$ 229,578	$ 103,673	45.2

Financial Services Segment

Revenue. Revenue increased by 53.2%, or approximately $158.8 million, from approximately $298.4 million during the six months ended June 30, 2006 to approximately $457.2 million during the six months ended June 30, 2007. The increase in revenue was driven by continued expansion of existing customer relationships as well as new customers. The increase in revenue from customers existing as of June 30, 2006 and customers added since such date was approximately $141.8 million and approximately $17.0 million, respectively. Within the segment, growth was particularly strong among our banking customers, where revenue increased approximately $122.5 million over last year. The increase can also be attributed to leveraging sales and marketing investments in this business segment as well as greater acceptance of the onsite/offshore IT services delivery model.

Segment Operating Profit. Segment operating profit increased 42.9%, or approximately $46.6 million, from approximately $108.5 million during the six months ended June 30, 2006 to approximately $155.1 million during the six months ended June 30, 2007. The increase in segment operating profit was attributable primarily to increased revenues partially offset by additional headcount to support our revenue growth, continued investment in sales and marketing, the impact of the appreciation of the Indian Rupee and wage inflation, primarily in India.

Healthcare Segment

Revenue. Revenue increased by 68.3%, or approximately $92.8 million, from approximately $135.9 million during the six months ended June 30, 2006 to approximately $228.7 million during the six months ended June 30, 2007. The increase in revenue was driven by continued expansion of existing customer relationships as well as new customers. The increase in revenue from customers existing as of June 30, 2006 and customers added since such date was approximately $83.2 million and approximately $9.6 million, respectively. Within the segment, growth was particularly strong among our healthcare customers, where revenue increased by approximately $56.9 million over last year. The increase can also be attributed to leveraging sales and marketing investments in this business segment as well as greater acceptance of the onsite/offshore IT services delivery model.

Segment Operating Profit. Segment operating profit increased 45.9%, or approximately $25.5 million, from approximately $55.7 million during the six months ended June 30, 2006 to approximately $81.3 million during the six months ended

June 30, 2007. The increase in segment operating profit was attributable primarily to increased revenues partially offset by additional headcount to support our revenue growth, continued investment in sales and marketing, the impact of the appreciation of the Indian Rupee and wage inflation, primarily in India.

Manufacturing/Retail/Logistics Segment

Revenue. Revenue increased by 51.2%, or approximately $49.8 million, from approximately $97.2 million during the six months ended June 30, 2006 to approximately $147.0 million during the six months ended June 30, 2007. The increase in revenue within the manufacturing, logistics and retail groups was driven by continued expansion of existing customer relationships as well as new customers. The increase in revenue from customers existing as of June 30, 2006 and customers added since such date was approximately $35.3 million and approximately $14.5 million, respectively. The increase can also be attributed to leveraging sales and marketing investments in this business segment as well as greater acceptance of the onsite/offshore IT services delivery model.

Segment Operating Profit. Segment operating profit increased 33.1%, or approximately $11.3 million, from approximately $34.1 million during the six months ended June 30, 2006 to approximately $45.3 million during the six months ended June 30, 2007. The increase in segment operating profit was attributable primarily to increased revenues partially offset by additional headcount to support our revenue growth, continued investment in sales and marketing, the impact of the appreciation of the Indian Rupee and wage inflation, primarily in India.

Other Segment

Revenue. Revenue increased by 58.6%, or approximately $53.1 million, from approximately $90.7 million during the six months ended June 30, 2006 to approximately $143.9 million during the six months ended June 30, 2007. The increase in revenue was primarily due to continued expansion of existing customer relationships as well as new customers. The increase in revenue from customers existing as of June 30, 2006 and customers added since such date was approximately $35.0 million and approximately $18.1 million, respectively. Within the other segment, growth was particularly strong among our media and information services customers, where revenue increased approximately $29.6 million over last year. The increase can also be attributed to leveraging sales and marketing investments in this business segment and greater acceptance of the onsite/offshore IT services delivery model.

Segment Operating Profit. Segment operating profit increased 64.8%, or approximately $20.3 million from approximately $31.3 million during the six months ended June 30, 2006 to approximately $51.6 million during the six months ended June 30, 2007. The increase in segment operating profit was attributable primarily to increased revenues and achieving operating efficiencies, including continued leverage on prior sales and marketing investments partially offset by additional headcount to support our revenue growth, the impact of the appreciation of the Indian Rupee and wage inflation, primarily in India.

Liquidity and Capital Resources

At June 30, 2007, we had cash and cash equivalents and short-term investments of approximately $710.2 million. We have used, and plan to use, such cash for: (i) expansion of existing operations, including our offshore IT development centers; (ii) continued development of new service lines; (iii) possible acquisitions of related businesses; (iv) formation of joint ventures; and (v) general corporate purposes, including working capital. As of June 30, 2007, we had working capital of approximately $970.5 million as compared to working capital of approximately $790.9 million as of December 31, 2006. Accordingly, we do not anticipate any near-term liquidity issues.

Net cash provided by operating activities was approximately $64.5 million during the six months ended June 30, 2007 as compared to cash provided by operations of approximately $47.7 million during the six months ended June 30, 2006. The increase is primarily attributed to the increase in net income in 2007 partially offset by investments in working capital. Trade accounts receivable increased from approximately $259.2 million at December 31, 2006 to approximately $348.9 million at June 30, 2007. Unbilled accounts receivable increased from approximately $39.3 million at December 31, 2006 to approximately $54.7 million at June 30, 2007. The increase in trade accounts receivable and unbilled receivables as of June 30, 2007 was due primarily to increased revenues and a higher number of days of sales outstanding. We monitor turnover, aging and the collection of accounts receivable through the use of management reports that are prepared on a customer basis and evaluated by our finance staff. At June 30, 2007, our days of sales outstanding, including unbilled receivables, was approximately 71 days as compared to 65 days at December 31, 2006 and 72 days as of June 30, 2006.

Our investing activities used net cash of approximately $128.9 million during the six months ended June 30, 2007 as compared to $83.0 million during the six months ended June 30, 2006. The increase in net cash used in investing activities primarily relates to greater investment in 2007 of excess cash generated from operations into short-term investments to achieve a higher return on invested balances and increased capital expenditure spending in 2007 to expand our offshore IT development centers.

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Our financing activities provided net cash of approximately $66.4 million during the six months ended June 30, 2007 as compared to $37.4 million during the six months ended June 30, 2006. The increase relates to a higher level of cash proceeds from the exercise of stock options and employee purchases of Company stock as well as greater levels of windfall income tax benefits generated on stock option exercises in 2007.

We believe that our available funds and the cash flows expected to be generated from operations will be adequate to satisfy our current and planned operations and needs for at least the next 12 months. Our ability to expand and grow our business in accordance with current plans, to make acquisitions and form joint ventures and to meet our long-term capital requirements beyond this 12-month period will depend on many factors, including the rate, if any, at which our cash flow increases, our ability and willingness to accomplish acquisitions and joint ventures with capital stock, our continued intent not to repatriate earnings from India, our ability not to breach the Distribution Agreement with IMS Health, especially as it relates to our tax indemnities, and the availability of public and private debt and equity financing. We cannot be certain that additional financing, if required, will be available on terms favorable to us, if at all.

During 2007 and 2006, we have not entered into any hedging arrangements nor have we entered into off-balance sheet transactions, arrangements or other relationships with unconsolidated entities or other persons that are likely to affect liquidity or the availability of or requirements for capital resources.

Commitments and Contingencies

Our updated India real estate development program now includes planned construction of over four and a half million square feet of new space. The expanded program, which commenced during the quarter ended March 31, 2007, includes the expenditure of approximately $300 million through the end of 2009 on land acquisition, facilities construction and furnishings to build new state-of-the-art IT development centers in regions primarily designated as Special Economic Zones located in Chennai, Pune, Kolkata, Hyderabad and Coimbatore, India. As of June 30, 2007, we had outstanding fixed capital commitments of approximately $91 million related to our existing India development center expansion program.

In connection with the acquisition of substantially all the assets of Fathom Solutions, LLC, or Fathom, in April 2005, additional purchase price, not to exceed $16 million, payable in 2007, was contingent on Fathom achieving certain financial and operating targets over the two years ended April 30, 2007. As of June 30, 2007, we have accrued approximately $12 million of additional purchase price payable to the sellers of Fathom, which amount was paid in July 2007 and was funded by cash flows from operations.

We are involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the outcome of such claims and legal actions, if decided adversely, is not expected to have a material adverse effect on our quarterly or annual operating results, cash flows, or consolidated financial position. Additionally, many of our engagements involve projects that are critical to the operations of our customers business and provide benefits that are difficult to quantify. Any failure in a customer s computer system could result in a claim for substantial damages against us, regardless of our responsibility for such failure. Although we attempt to contractually limit our liability for damages arising from negligent acts, errors, mistakes, or omissions in rendering our application design, development and maintenance services, there can be no assurance that the limitations of liability set forth in our contracts will be enforceable in all instances or will otherwise protect us from liability for damages. Although we have general liability insurance coverage, including coverage for errors or omissions, there can be no assurance that such coverage will continue to be available on reasonable terms or will be sufficient in amount to cover one or more large claims, or that the insurer will not disclaim coverage as to any future claim. The successful assertion of one or more large claims against us that exceed available insurance coverage or changes in our insurance policies, including premium increases or the imposition of large deductible or co-insurance requirements, could have a material adverse effect on our quarterly and annual operating results, financial position and cash flows.

In connection with our split-off from IMS Health, we entered into a Distribution Agreement, dated January 7, 2003, with IMS Health, referred to as the Distribution Agreement. The Distribution Agreement provides, among other things, that IMS Health and we will comply with, and not take any action during the relevant time period that is inconsistent with, the representations made to and relied upon by McDermott, Will & Emery in connection with rendering its opinion regarding the United States federal income tax consequences of the exchange offer. In addition, pursuant to the Distribution Agreement, we indemnified IMS Health for any tax liability to which they may be subject as a result of the exchange offer but only to the extent that such tax liability resulted solely from a breach in the representations we made to and were relied upon by McDermott, Will & Emery in connection with rendering its opinion regarding the United States federal income tax consequences of the exchange offer. If we breach any of our representations in connection with the Distribution Agreement, the related indemnification liability could be material to our quarterly and annual operating results, financial position and cash flows.

Foreign Currency Translation

Overall, we believe that we are not exposed to significant revenue risk resulting from movement in foreign exchange rates as approximately 84% of our revenues for the quarter ended June 30, 2007 are generated from customers located in North America. However, a portion of our costs in India, representing approximately 31% of our global operating costs for the quarter ended June 30, 2007, are denominated in local currency and subject to foreign exchange rate fluctuations, which has an impact on our results of operations. In addition, a portion of our balance sheet is exposed to foreign exchange rate fluctuations, which results in non-operating foreign exchange gains and losses. On an ongoing basis, we manage a portion of this risk by limiting our net monetary asset exposure to the Indian rupee in our Indian subsidiary.

Recent Accounting Pronouncements

We adopted the provisions of the Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of SFAS No. 109 (FIN 48), on January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes by prescribing a minimum recognition threshold for a tax position taken or expected to be taken in a tax return that is required to be met before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. The cumulative effect of adopting FIN 48 of $0.85 million was recorded as a reduction of beginning retained earnings and an increase to noncurrent liabilities. The total amount of unrecognized tax benefits as of the date of adoption was $7.7 million of which $7.5 million would impact our effective income tax rate if recognized. Included in the balance of unrecognized tax benefits as of January 1, 2007, is $2.9 million related to certain U.S. Federal and state unrecognized tax benefits that could reasonably be recognized during the next 12 months due to expiration of statutes of limitations. During the quarter ending June 30, 2007, we reduced our liability for unrecognized tax benefits by approximately $0.74 million upon effective settlement of certain foreign income tax positions.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, Including an Amendment of FASB Statement No. 115 (SFAS No. 159), which is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. SFAS No. 159 permits entities to measure eligible financial assets, financial liabilities and firm commitments at fair value, on an instrument-by-instrument basis, that are otherwise not permitted to be accounted for at fair value under other generally accepted accounting principles. The fair value measurement election is irrevocable and subsequent changes in fair value must be recorded in earnings. We are currently evaluating the impact that SFAS No. 159 will have on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. We are currently evaluating the impact that SFAS No. 157 will have on our consolidated financial statements.

Effects of Inflation

Our most significant costs are the salaries and related benefits for our programming staff and other professionals. Competition in India, the United States and Europe for professionals with advanced technical skills necessary to perform our services offered have caused wages to increase at a rate greater than the general rate of inflation. As with other IT service providers, we must adequately anticipate wage increases, particularly on our fixed-price contracts. There can be no assurance that we will be able to recover cost increases through increases in the prices that we charge for our services in the United States and elsewhere. We have experienced wage inflation in India; however, this has not had a material impact on our results of operations as Indian wages represented slightly more than 20% of our total operating expenses for the three months ended June 30, 2007.

Forward Looking Statements

The statements contained in this Quarterly Report on Form 10-Q that are not historical facts are forward-looking statements (within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended) that involve risks and uncertainties. Such forward-looking statements may be identified by, among other things, the use of forward-looking terminology such as believes, expects, may, will, should or anticipates o negative thereof or other variations

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thereon or comparable terminology, or by discussions of strategy that involve risks and uncertainties. From time to time, we or our representatives have made or may make forward-looking statements, orally or in writing. Such forward-looking statements may be included in various filings made by us with the Securities and Exchange Commission, or press releases or oral statements made by or with the approval of one of our authorized executive officers. These forward-looking statements, such as statements regarding anticipated future revenues, contract percentage completions, capital expenditures, and other statements regarding matters that are not historical facts, involve predictions. Our actual results, performance or achievements could differ materially from the results expressed in, or implied by, these forward-looking statements. There are a number of important factors that could cause our results to differ materially from those indicated by such forward-looking statements. These factors include those set forth in Item 1A. Risk Factors .

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

We are exposed to foreign currency exchange rate risk in the ordinary course of doing business as we transact or hold a portion of our funds in foreign currencies, particularly the Indian rupee. Accordingly, we periodically evaluate the need for hedging strategies, including the use of derivative financial instruments, to mitigate the effect of foreign currency fluctuations and may use such instruments in the future to reduce foreign currency exposure to appreciation or depreciation in the value of certain foreign currencies. In 2007 and 2006, we have not entered into any off-balance sheet transactions, arrangements or other relationships with unconsolidated entities or other persons that are likely to affect liquidity or the availability of or requirements for capital resources.

We do not believe we are exposed to material direct risks associated with changes in interest rates other than with our cash and cash equivalents and short-term investments. As of June 30, 2007, we had approximately $710.2 million of cash and cash equivalents and short-term investments which are impacted almost immediately by changes in short-term interest rates. We limit our credit risk by investing primarily in AAA/Aaa rated securities as rated by Moody s, Standard & Poor s and Fitch rating services and restricting amounts that can be invested with any single issuer.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures and Changes in Internal Control over Financial Reporting

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of June 30, 2007. In designing and evaluating our disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applied its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on this evaluation, our chief executive officer and chief financial officer concluded that, as of June 30, 2007, our disclosure controls and procedures were (1) effective in that they were designed to ensure that material information relating to us, including our consolidated subsidiaries, is made known to our chief executive officer and chief financial officer by others within those entities, as appropriate, to allow timely decisions regarding required disclosures, and (2) effective in that they provide reasonable assurance that information required to be disclosed by us in our reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms.

No changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended June 30, 2007 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1A. Risk Factors

Additional Factors That May Affect Future Results

In addition to the risks and uncertainties detailed elsewhere in this Quarterly Report on Form 10-Q, if any of the following risks occur, our business, financial condition, results of operations or prospects could be materially adversely affected. In such case, the trading price of our Common Stock could decline.

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A substantial portion of our assets and operations are located in India and we are subject to regulatory, economic and political uncertainties in India.

We intend to continue to develop and expand our offshore facilities in India where, as of June 30, 2007, a majority of our technical professionals were located. While wage costs are lower in India than in the United States and other developed countries for comparably skilled professionals, wages in India are increasing at a faster rate than in the United States, which could result in our incurring increased costs for technical professionals and reduced operating margins. In addition, there is intense competition in India for skilled technical professionals and we expect that competition to increase.

India has also experienced civil unrest and terrorism and has been involved in conflicts with neighboring countries. In recent years, there have been military confrontations between India and Pakistan that have occurred in the region of Kashmir and along the India-Pakistan border. The potential for hostilities between the two countries has been high in light of tensions related to recent terrorist incidents in India and the unsettled nature of the regional geopolitical environment, including events in and related to Afghanistan and Iraq. If India were to become engaged in armed hostilities, particularly if these hostilities were protracted or involved the threat of or use of weapons of mass destruction, our operations would be materially adversely affected. In addition, U.S. companies may decline to contract with us for services in light of international terrorist incidents or armed hostilities even where India is not involved because of more generalized concerns about relying on a service provider utilizing international resources.

In the past, the Indian economy has experienced many of the problems confronting the economies of developing countries, including high inflation, erratic gross domestic product growth and shortages of foreign exchange. The Indian government has exercised and continues to exercise significant influence over many aspects of the Indian economy, and Indian government actions concerning the economy could have a material adverse effect on private sector entities, including us. In the past, the Indian government has provided significant tax incentives and relaxed certain regulatory restrictions in order to encourage foreign investment in specified sectors of the economy, including the software development services industry. Programs that have benefited us include, among others, tax holidays, liberalized import and export duties and preferential rules on foreign investment and repatriation. Notwithstanding these benefits, India s central and state governments remain significantly involved in the Indian economy as regulators. In recent years, the Indian government has introduced non-income related taxes, including the fringe benefit tax and new service taxes. The elimination of any of the benefits realized by us from our Indian operations or the imposition of new taxes could have a material adverse effect on our business, results of operations and financial condition.

We are investing substantial cash assets in new facilities and physical infrastructure, and our profitability could be reduced if our business does not grow proportionately.

As of June 30, 2007, we had contractual commitments of approximately $91.1 million related to capital expenditures on construction or expansion of our IT development centers. We expect to invest approximately $300 million in new IT development centers during the three years ended December 31, 2009. We may encounter cost overruns or project delays in connection with new facilities. These expansions will likely increase our fixed costs and if we are unable to grow our business and revenues proportionately, our profitability will be reduced.

Our international sales and operations are subject to many uncertainties.

Revenues from customers outside North America represented approximately 15% of our revenues for the six months ended June 30, 2007 and 14% of our revenues for the year ended December 31, 2006. We anticipate that revenues from customers outside North America will continue to account for a material portion of our revenues in the foreseeable future and may increase as we expand our international presence, particularly in Europe. In addition, a majority of our employees and almost all of our IT development centers are located in India. As a result, we may be subject to risks associated with international operations, including risks associated with foreign currency exchange rate fluctuations and risks associated with the application and imposition of protective legislation and regulations relating to import or export or otherwise resulting from foreign policy or the variability of foreign economic conditions. From time to time, we may engage in hedging transactions to mitigate our risks relating to exchange rate fluctuations. Additional risks associated with international operations include difficulties in enforcing intellectual property rights, the burdens of complying with a wide variety of foreign laws, potentially adverse tax consequences, tariffs, quotas and other barriers and potential difficulties in collecting accounts receivable. In addition, we may face competition in other countries from companies that may have more experience with operations in such countries or with international operations. We may also face difficulties integrating new facilities in different countries into our existing operations, as well as integrating employees that we hire in different countries into our existing corporate culture. Our international expansion plans may not be successful and we may not be able to compete effectively in other countries. There can be no assurance that these and other factors will not have a material adverse effect on our business, results of operations and financial condition.

Our operating results may be adversely affected by fluctuations in the Indian rupee and other foreign currency exchange rates.

Although we report our operating results in U.S. dollars, a portion of our revenues and expenses are denominated in currencies other than the U.S. dollar. Fluctuations in foreign currency exchange rates can have a number of adverse effects on us. Because our consolidated financial statements are presented in U.S. dollars, we must translate revenues, expenses and income, as well as assets and liabilities, into U.S. dollars at exchange rates in effect during or at the end of each reporting period. Therefore, changes in the value of the U.S. dollar against other currencies will affect our revenues, income from operations and the value of balance-sheet items originally denominated in other currencies. During the six months ended June 30, 2007, the appreciation of the Indian rupee versus the U.S. dollar negatively impacted our operating margins. There is no guarantee that our financial results will not be adversely affected by currency exchange rate fluctuations, including further appreciation of the Indian rupee versus the U.S. dollar, or that any efforts by us to engage in currency hedging activities would be effective. In addition, in some countries we could be subject to strict restrictions on the movement of cash and the exchange of foreign currencies, which could limit our ability to use this cash across our global operations. Finally, as we continue to leverage our global delivery model, more of our expenses are incurred in currencies other than those in which we bill for the related services. An increase in the value of certain currencies, such as the Indian rupee, against the U.S. dollar could increase costs for delivery of services at off-shore sites by increasing labor and other costs that are denominated in local currency.

We face intense competition from other IT service providers.

The intensely competitive IT professional services market includes a large number of participants and is subject to rapid change. This market includes participants from a variety of market segments, including:

- systems integration firms;
- contract programming companies;
- application software companies;
- Internet solutions providers;
- the professional services groups of computer equipment companies; and
- infrastructure management and outsourcing companies.

The market also includes numerous smaller local competitors in the various geographic markets in which we operate. Our direct competitors who use the on-site/offshore business model include, among others, Infosys Technologies, Tata Consultancy Services and WIPRO. In addition, many of our competitors have significantly greater financial, technical and marketing resources and greater name recognition than we do. Some of these larger competitors, such as Accenture, Electronic Data Systems and IBM Global Services, have offshore operations. We cannot assure you that we will be able to sustain our current levels of profitability or growth as competitive pressures, including competition for skilled IT development professionals and pricing pressure from competitors employing an on-site/offshore business model, increase.

We may not be able to sustain our current level of profitability.

For the six months ended June 30, 2007 and the year ended December 31, 2006, we had an operating margin of 17.8% and 18.2%, respectively, compared to an operating margin of 20.1% for the year ended December 31, 2005. Our operating margin has declined as a result of the adoption of SFAS No. 123R, which required us to record stock compensation expense for stock option grants in our consolidated statement of operations effective January 1, 2006. Our operating margin may decline further if we experience declines in demand and pricing for our services or due to adverse fluctuations in foreign currency exchange rates. In addition, wages in India are increasing at a faster rate than in the United States, which could result in us incurring increased costs for technical professionals. Additionally, the number of stock options issued and the assumptions used in the stock option pricing model may change resulting in increased stock option expense and lower margins. Although we have been able to partially offset wage increases and foreign currency fluctuations through further leveraging of our low-cost operating structure, obtaining price increases and issuing a lower number of options in proportion to our overall headcount, we cannot assure you that we will be able to continue to do so in the future.

Our business will suffer if we fail to develop new services and enhance our existing services in order to keep pace with the rapidly evolving technological environment.

The IT services market is characterized by rapid technological change, evolving industry standards, changing customer preferences and new product and service introductions. Our future success will depend on our ability to develop solutions that keep pace with changes in the IT services market. We cannot assure you that we will be successful in developing new

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services addressing evolving technologies on a timely or cost-effective basis or, if these services are developed, that we will be successful in the marketplace. In addition, we cannot assure you that products, services or technologies developed by others will not render our services non-competitive or obsolete. Our failure to address these developments could have a material adverse effect on our business, results of operations and financial condition.

Our ability to remain competitive will also depend on our ability to design and implement, in a timely and cost-effective manner, solutions for customers moving from the mainframe environment to client/server or other advanced architectures. Our failure to design and implement solutions in a timely and cost-effective manner could have a material adverse effect on our business, results of operations and financial condition.

We may face difficulties in providing end-to-end business solutions for our clients that could cause clients to discontinue their work with us, which in turn could harm our business.

We have been expanding the nature and scope of our engagements and have added new service offerings, such as IT consulting, business process outsourcing, systems integration and outsourcing of entire portions of IT infrastructure. The success of these service offerings is dependent, in part, upon continued demand for such services by our existing and new clients and our ability to meet this demand in a cost-competitive and effective manner. In addition, our ability to effectively offer a wider breadth of end-to-end business solutions depends on our ability to attract existing or new clients to these service offerings. To obtain engagements for such end-to-end solutions, we also are more likely to compete with large, well-established international consulting firms, resulting in increased competition and marketing costs. Accordingly, we cannot be certain that our new service offerings will effectively meet client needs or that we will be able to attract existing and new clients to these service offerings.

The increased breadth of our service offerings may result in larger and more complex projects with our clients. This will require us to establish closer relationships with our clients and a thorough understanding of their operations. Our ability to establish such relationships will depend on a number of factors, including the proficiency of our IT professionals and our management personnel. Our failure to understand our client requirements or our failure to deliver services which meet the requirements specified by our clients could result in termination of client contracts, and we could be liable to our clients for significant penalties or damages.

Larger projects may involve multiple engagements or stages, and there is a risk that a client may choose not to retain us for additional stages or may cancel or delay additional planned engagements. These terminations, cancellations or delays may result from the business or financial condition of our clients or the economy generally, as opposed to factors related to the quality of our services. Such cancellations or delays make it difficult to plan for project resource requirements, and inaccuracies in such resource planning may have a negative impact on our profitability.

Our results of operations may be affected by the rate of growth in the use of technology in business and the type and level of technology spending by our clients.

Our business depends in part upon continued growth in the use of technology in business by our clients and prospective clients and their customers and suppliers. In challenging economic environments, our clients may reduce or defer their spending on new technologies in order to focus on other priorities. At the same time, many companies have already invested substantial resources in their current means of conducting commerce and exchanging information, and they may be reluctant or slow to adopt new approaches that could disrupt existing personnel, processes and infrastructures. If the growth of use of technology in business or our clients spending on technology in business declines, or if we cannot convince our clients or potential clients to embrace new technology solutions, our results of operations could be adversely affected.

Competition for highly skilled technical personnel is intense and the success of our business depends on our ability to attract and retain highly skilled professionals.

Our future success will depend to a significant extent on our ability to attract, train and retain highly skilled IT development professionals. In particular, we need to attract, train and retain project managers, IT engineers and other senior technical personnel. We believe there is a shortage of, and significant competition for, IT development professionals in the United States and India with the advanced technological skills necessary to perform the services we offer. We have subcontracted, to a limited extent in the past, and may do so in the future, with other service providers in order to meet our obligations to our customers. Our ability to maintain and renew existing engagements and obtain new business will depend, in large part, on our ability to attract, train and retain technical personnel with the skills that keep pace with continuing changes in information technology, evolving industry standards and changing customer preferences. Further, we must train and manage our growing work force, requiring an increase in the level of responsibility for both existing and new management personnel. We cannot assure you that the management skills and systems currently in place will be adequate or that we will be able to train and assimilate new employees successfully. Our failure to attract, train and retain current or future employees could have a material adverse effect on our business, results of operations and financial condition.

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Our growth may be hindered by immigration restrictions.

Our future success will depend on our ability to attract and retain employees with technical and project management skills from developing countries, especially India. The vast majority of our IT professionals in the United States and in Europe are Indian nationals. The ability of Indian nationals to work in the United States depends on their ability and our ability to obtain the necessary visas and work permits.

The H-1B visa classification enables United States employers to hire qualified foreign workers in positions that require an education at least equal to a Baccalaureate Degree in the United States in specialty occupations such as IT systems engineering and systems analysis. The H-1B visa usually permits an individual to work and live in the United States for a period of up to six years. There is a limit on the number of new H-1B petitions that United States Citizenship and Immigration Services, or CIS, one of the successor agencies to the Immigration and Naturalization Service, may approve in any federal fiscal year, and in years in which this limit is reached, we may be unable to obtain H-1B visas necessary to bring foreign employees to the United States. In the current federal fiscal year, the limit is 65,000. The fiscal year 2008 cap was reached on April 2, 2007. The FY 2008 cap of 20,000 for graduates of U.S. advance degree programs was reached on April 30, 2007. The FY 2007 cap was reached on May 26, 2006. The FY 2007 cap of 20,000 for graduates of U.S. advance degree programs was reached on July 26, 2006. We will be able to file H-1B applications against the FY 2009 cap beginning on April 1, 2008 for work in H-1B status beginning on October 1, 2008. Each year the H-1B cap is reached at an earlier point prior to the beginning of the fiscal year for which the H-1B s will be available. However, as a part of our advanced planning process, we believe that we have sufficient employees visa-ready to meet our anticipated business growth in the current year. In addition, there are strict labor regulations associated with the H-1B visa classification. Higher users of the H-1B visa program are often subject to investigations by the Wage and Hour Division of the United States Department of Labor. A finding by the United States Department of Labor of willful or substantial failure by us to comply with existing regulations on the H-1B classification may result in back-pay liability, substantial fines, and/or a ban on future use of the H-1B program and other immigration benefits.

We also regularly transfer employees of our subsidiary in India to the United States to work on projects and at client sites, using the L-1 visa classification. The L-1 visa allows companies abroad to transfer certain managers, executives and employees with specialized company knowledge to related U.S. companies such as a parent, subsidiary, affiliate, joint venture, or branch office. We have an approved Blanket L Program, under which the corporate relationships of our transferring and receiving entities have been pre-approved by the CIS, thus enabling individual L-1 applications to be presented directly to a U.S. consular post abroad rather than undergoing the pre-approval process in the United States. In recent years, both the U.S. consular posts that review initial L-1 applications and the CIS offices, which adjudicate extensions of L-1 status, have become more restrictive with respect to this category. As a result, the rate of refusals of initial L-1 applications and of extensions has increased. In addition, even where L-1 visas are ultimately granted and issued, security measures undertaken by U.S. consular posts around the world have delayed visa issuances. Our inability to bring qualified technical personnel into the United States to staff on-site customer locations would have a material adverse effect on our business, results of operations and financial condition.

On December 8, 2004, President Bush signed the L-1 Visa Reform Act, which was part of the FY 2005 Omnibus Appropriations Act (Public Law 108-447 at Division J, Title IV). This legislation contained several important changes to the laws governing L-1 visa holders. All of the changes took effect on June 8, 2005. Under one provision of the new law, all L-1 applicants, including those brought to the United States under a Blanket L Program, must have worked abroad with the related company for one full year in the prior three years. The provision allowing Blanket L applicants who had worked abroad for the related company for six months during the qualifying three-year period was revoked. In addition, L-1B holders (intracompany transferees with specialized company knowledge) may not be primarily stationed at the work site of another employer if the L-1B holder will be controlled and supervised by an employer other than the petitioning employer. Finally, L-1B status may not be granted where placement of the L-1B visa holder at a third party site is part of an arrangement to provide labor for the third party, rather than placement at the site in connection with the provision of a product or service involving specialized knowledge specific to the petitioning employer.

We do not place L-1B workers at third party sites where they are under the primary supervision of a different employer, nor do we place L-1B holders at third party sites in an arrangement to provide labor for the third party, without providing a service involving our specialized knowledge. Since implementation of the new law, we have not encountered any difficulty in establishing this fact to CIS s satisfaction. However, if CIS and/or the United States Department of State, through its visa-issuing U.S. consular posts abroad, decide to interpret these provisions in a very restrictive fashion, this could impair our ability to staff our projects in the United States with resources from our entities abroad. In addition, CIS has not yet issued regulations governing these new provisions. If such regulations are restrictive in nature, this could impair our ability to staff our projects in the United States with resources from our entities abroad.

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We also process immigrant visas for lawful permanent residence for employees to fill positions for which there are no able, willing and qualified U.S. workers available to fill the positions. Compliance with existing U.S. immigration and labor laws, or changes in those laws making it more difficult to hire foreign nationals or limiting our ability to successfully obtain permanent residence for our foreign employees in the United States, could require us to incur additional unexpected labor costs and expenses or could restrain our ability to retain the skilled professionals we need for our operations in the United States. Any of these restrictions or limitations on our hiring practices could have a material adverse effect on our business, results of operations and financial condition.

In addition to immigration restrictions in the United States, there are certain restrictions on transferring our employees to work in the United Kingdom, where we have experienced significant growth. The United Kingdom requires that employees who are not nationals of the European Economic Area (EEA), which includes nationals of all European Union countries (except Bulgaria and Romania) plus Iceland, Norway, Liechtenstein and Switzerland, obtain an intra-company transfer work permit before beginning to perform work. Under the work permit regulations, in order for us to transfer our non-EEA employees to the United Kingdom, we must demonstrate that the employee had been employed by us for at least six months prior to the transfer and that the position in the United Kingdom requires someone with either: (1) a United Kingdom degree level qualification; or (2) a Higher National Diploma (HND) level occupational qualification which is relevant to the UK position; or (3) a general HND level qualification plus one year s work experience doing the type of job for which the work permit is sought; or (4) at least three years high-level specialist skills acquired through doing the type of job for which the work permit is sought. These restrictions restrain our ability to add the skilled professionals we need for our operations in Europe, and could have an adverse affect on our international strategy to expand our presence in Europe. As a result, the work permit legislation in the United Kingdom could have a material adverse effect on our business, results of operations and financial condition.

Immigration and work permit laws and regulations in the United States, the United Kingdom and other countries are subject to legislative and administrative changes as well as changes in the application of standards and enforcement. Immigration and work permit laws and regulation can be significantly affected by political forces and levels of economic activity. Our international expansion strategy and our business, results of operations and financial condition may be materially adversely affected if changes in immigration and work permit laws and regulations or the administration or enforcement of such laws or regulations impair our ability to staff projects with IT professionals who are not citizens of the country where the work is to be performed.

Our global operations expose us to numerous and sometimes conflicting legal and regulatory requirements, and violation of these regulations could harm our business.

Because we provide services to clients throughout the world, we are subject to numerous, and sometimes conflicting, legal rules on matters as diverse as import/export controls, content requirements, trade restrictions, tariffs, taxation, sanctions, government affairs, internal and disclosure control obligations, data privacy and labor relations. Violations of these regulations in the conduct of our business could result in fines, criminal sanctions against us or our officers, prohibitions on doing business and damage to our reputation. Violations of these regulations in connection with the performance of our obligations to our clients also could result in liability for monetary damages, fines and/or criminal prosecution, unfavorable publicity, restrictions on our ability to process information and allegations by our clients that we have not performed our contractual obligations. Due to the varying degrees of development of the legal systems of the countries in which we operate, local laws might be insufficient to protect our rights. Our failure to comply with applicable regulatory requirements, could have a material adverse effect on our business, results of operations and financial condition.

Anti-outsourcing legislation, if adopted, could adversely affect our business, financial condition and results of operations and impair our ability to service our customers.

The issue of outsourcing of services abroad by U.S. companies is a topic of political discussion in the United States. Measures aimed at limiting or restricting outsourcing by U.S. companies are under discussion in Congress and in numerous state legislatures. While no substantive anti-outsourcing legislation has been introduced to date, given the ongoing debate over this issue, the introduction of such legislation is possible. If introduced, such measures are likely to fall within two categories: (1) a broadening of restrictions on outsourcing by federal and state government agencies and on government contracts with firms that outsource services directly or indirectly, and/or (2) measures that impact private industry, such as tax disincentives or intellectual property transfer restrictions. In the event that any of these measures become law, our business, financial condition and results of operations could be adversely affected and our ability to service our customers could be impaired.

An economic slowdown, hostilities involving the United States, and other acts of terrorism, violence or war could delay or reduce the number of new purchase orders we receive and impair our ability to service our customers, thereby adversely affecting our business, financial condition and results of operations.

Approximately 85% of our revenues during the six months ended June 30, 2007 and 86% of our revenue during the year ended December 31, 2006 was derived from customers located in the United States. In the event of an economic slowdown, our customers may delay or reduce their IT spending significantly, which may in turn lower the demand for our services and could have a material adverse affect on our financial results. Further, hostilities involving the United States and other acts of terrorism, violence or war, such as the attacks of September 11, 2001 in the United States, the attacks of July 7, 2005 in the United Kingdom, and the continuing conflict in Iraq, could materially adversely affect our operations and our ability to service our customers. Hostilities involving the United States could cause customers in the United States to delay their decisions on IT spending, which could affect our financial results. In addition, acts of terrorism, violence or war could give rise to military or travel disruptions and restrictions affecting our employees. As of June 30, 2007, a majority of our technical professionals were located in India, and the vast majority of our technical professionals in the United States and Europe are Indian nationals who are able to work in the United States and Europe only because they hold current visas and work permits. Travel restrictions could cause us to incur additional unexpected labor costs and expenses or could restrain our ability to retain the skilled professionals we need for our operations in the United States and Europe.

Although we continue to believe that we have a strong competitive position in the United States, we continue to increase our efforts to geographically diversify our clients and revenue. Despite our efforts to diversify, an economic slowdown, hostilities involving the United States, and other acts of terrorism, violence or war may reduce the demand for our services and negatively affect our revenues and profitability.

Our inability to employ and effectively implement the right systems, processes and tools to manage our large and expanding enterprise could have a material adverse effect on our business, results of operations and financial condition.

In 2006, we began implementing new financial and human resource software systems to improve our organizational processes, internal controls and efficiency, and accommodate our anticipated growth. Additionally, to streamline our general and administration infrastructure and costs as a percentage of revenue, and ensure that we can appropriately scale our operations as our business expands, we are redesigning many operational processes and transitioning certain internal, non-billable roles to our offices in India. These activities principally relate to finance, human resources and certain IT functions. If we do not timely, efficiently and effectively upgrade or replace systems, redesign processes and implement the preceding role transitions as our business requires, we may be unable to support our growth effectively or realize cost savings as quickly as expected and maintain effective internal controls over financial reporting. Additionally, the quality of our services may decline and our ability to compete successfully and achieve our business objectives could be impaired if we are unable to successfully complete these initiatives. If we do not continue to employ and effectively implement the right systems, processes and tools to manage our large and expanding enterprise, it could have a material adverse effect on our business, results of operations and financial condition.

Our ability to operate and compete effectively could be impaired if we lose key personnel or if we cannot attract additional qualified personnel.

Our future performance depends to a significant degree upon the continued service of the key members of our management team, as well as marketing, sales and technical personnel, and our ability to attract and retain new management and other personnel. We do not maintain key man life insurance on any of our executive officers or significant employees. Competition for personnel is intense, and there can be no assurance that we will be able to retain our key employees or that we will be successful in attracting and retaining new personnel in the future. The loss of any one or more of our key personnel or the failure to attract and retain key personnel could have a material adverse effect on our business, results of operations and financial condition.

Restrictions in non-competition agreements with our executive officers may not be enforceable.

We have entered into non-competition agreements with most of our executive officers. We cannot assure you, however, that the restrictions in these agreements prohibiting such executive officers from engaging in competitive activities are enforceable. Further, substantially all of our professional non-executive staff and one new executive officer are not covered by agreements that would prohibit them from working for our competitors. If any of our key professional personnel leaves our employment and joins one of our competitors, our business could be adversely affected.

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Our earnings may be adversely affected if we change our intent not to repatriate earnings in India.

Effective January 1, 2002, pursuant to Accounting Principles Board Opinion No. 23, Accounting for Income Taxes-Special Areas, we no longer accrue incremental U.S. taxes on all Indian earnings recognized in 2002 and subsequent periods as these earnings are considered to be indefinitely reinvested outside of the United States. While we have no plans to do so, events may occur in the future that could effectively force us to change our intent on repatriating Indian earnings. If we change our intent and repatriate such earnings, we will have to accrue the applicable amount of taxes associated with such earnings and pay taxes at a substantially higher rate than our effective income rate in 2006. These increased taxes could have a material adverse effect on our business, results of operations and financial condition.

A significant portion of our projects are on a fixed-price basis, subjecting us to the risks associated with cost over-runs and operating cost inflation.

We contract to provide services either on a time-and-materials basis or on a fixed-price basis, with fixed-price contracts accounting for approximately 25% of our revenues for the six months ended June 30, 2007 and the year ended December 31, 2006. We expect that an increasing number of our future projects will be contracted on a fixed-price basis. We bear the risk of cost over-runs and operating cost inflation in connection with projects covered by fixed-price contracts. Our failure to estimate accurately the resources and time required for a fixed-price project, or our failure to complete our contractual obligations within the time frame committed, could have a material adverse effect on our business, results of operations and financial condition.

If we do not continue to improve our operational, financial and other internal controls and systems to manage our rapid growth, our business may suffer and the value of our shareholders investment may be harmed.

Our anticipated growth will continue to place significant demands on our management and other resources. Our growth will require us to continue to develop and improve our operational, financial and other internal controls, both in the United States, India and elsewhere. In particular, our continued growth will increase the challenges involved in:

- recruiting and retaining sufficiently skilled technical, marketing and management personnel;
- adhering to our high quality standards;
- maintaining high levels of client satisfaction;
- developing and improving our internal administrative infrastructure, particularly our financial, operational, communications and other internal systems; and
- preserving our culture, values and entrepreneurial environment.

As part of our growth strategy, we are expanding our operations in Europe, Asia and Latin America. We may not be able to compete effectively in these markets and the cost of entering these markets may be substantially greater than we expect. If we fail to compete effectively in the new markets we enter, or if the cost of entering those markets is substantially greater than we expect, our business, results of operations and financial condition could be adversely affected. In addition, if we cannot compete effectively, we may be required to reconsider our strategy to invest in our international expansion plans and change our intent on the repatriation of our earnings.

We rely on a few customers for a large portion of our revenues.

Our top five customers generated approximately 25% of our revenues for the six months ended June 30, 2007 and 29% of our revenues in the fiscal year ended December 31, 2006. The volume of work performed for specific customers is likely to vary from year to year, and a major customer in one year may not use our services in a subsequent year. The loss of one of our large customers could have a material adverse effect on our business, results of operations and financial condition.

We generally do not have long-term contracts with our customers and our results of operations could be adversely affected if our clients terminate their contracts with us on short notice.

Consistent with industry practice, we generally do not enter into long-term contracts with our customers. A majority of our contracts can be terminated by our clients with short notice. As a result, we are substantially exposed to volatility in the market for our services, and may not be able to maintain our level of profitability.

When contracts are terminated, we lose the anticipated revenues and might not be able to eliminate associated costs in a timely manner. Consequently, our profit margins in subsequent periods could be lower than expected. If we are unable to market our services on terms we find acceptable, our financial condition and results of operations could suffer materially.

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Our profitability could suffer if we are not able to maintain favorable pricing rates.

Our profit margin, and therefore our profitability, is dependent on the rates we are able to recover for our services. If we are not able to maintain favorable pricing for our services, our profit margin and our profitability could suffer. The rates we are able to recover for our services are affected by a number of factors, including:

- our clients perceptions of our ability to add value through our services;
- competition;
- introduction of new services or products by us or our competitors;
- our competitors pricing policies;
- our ability to accurately estimate, attain and sustain contract revenues, margins and cash flows over increasingly longer contract periods;
- bid practices of clients and their use of third-party advisors;
- the use by our competitors and our clients of off-shore resources to provide lower-cost service delivery capabilities; and
- general economic and political conditions.

Our operating results experience significant quarterly fluctuations.

We historically have experienced significant quarterly fluctuations in our revenues and results of operations and expect these fluctuations to continue. Among the factors causing these variations have been:

- the number, timing, scope and contractual terms of IT development and maintenance projects in which we are engaged;
- delays incurred in the performance of those projects;
- the accuracy of estimates of resources and time required to complete ongoing projects; and
- general economic conditions.

In addition, our future revenues, operating results and margins may fluctuate as a result of:

changes in pricing in response to customer demand and competitive pressures;

the mix of on-site and offshore staffing;

the ratio of fixed-price contracts versus time-and-materials contracts;

employee wage levels and utilization rates;

changes in foreign exchange rates, including the Indian rupee versus the U. S. dollar;

the timing of collection of accounts receivable;

enactment of new taxes, including fringe benefit taxes in India;

changes in domestic and international income tax rates and regulations; and

changes to levels and types of equity-based compensation awards and assumptions used to determine the fair value of such awards.

A high percentage of our operating expenses, particularly personnel and rent, are relatively fixed in advance of any particular quarter. As a result, unanticipated variations in the number and timing of our projects or in employee wage levels and utilization rates may cause significant variations in our operating results in any particular quarter, and could result in losses. Any significant shortfall of revenues in relation to our expectations, any material reduction in utilization rates for our professional staff or variance in the on-site, offshore staffing mix, an unanticipated termination of a major project, a customer s decision not to pursue a new project or proceed to succeeding stages of a current project or the completion during a quarter of several major customer projects could require us to pay underutilized employees and could therefore have a material adverse effect on our business, results of operations and financial condition.

As a result of these factors, it is possible that in some future periods, our revenues and operating results may be significantly below the expectations of public market analysts and investors. In such an event, the price of our common stock would likely be materially and adversely affected.

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Our profitability could suffer if we are not able to maintain favorable utilization rates.

The cost of providing our services, including the utilization rate of our professionals, affects our profitability. If we are not able to maintain an appropriate utilization rate for our professionals, our profit margin and our profitability may suffer. Our utilization rates are affected by a number of factors, including:

- our ability to transition employees from completed projects to new assignments and to hire and assimilate new employees;
- our ability to forecast demand for our services and thereby maintain an appropriate headcount in each of our geographies and workforces;
- our ability to manage attrition; and
- our need to devote time and resources to training, professional development and other non-chargeable activities.

Liability claims for damages caused by disclosure of confidential information or system failures could have a material adverse effect on our business.

Many of our engagements involve projects that are critical to the operations of our customers businesses and provide benefits that are difficult to quantify. Any failure in a customer s computer system could result in a claim for substantial damages against us, regardless of our responsibility for the failure. Although we attempt to limit by contract our liability for damages arising from negligent acts, errors, mistakes or omissions in rendering our IT development and maintenance services, we cannot assure you that any contractual limitations on liability will be enforceable in all instances or will otherwise protect us from liability for damages.

In addition, we often have access to or are required to collect and store confidential client and customer data. If any person, including any of our employees, penetrates our network security or misappropriates sensitive data, we could be subject to significant liability from our clients or from our clients customers for breaching contractual confidentiality provisions or privacy laws. Unauthorized disclosure of sensitive or confidential client and customer data, whether through breach of our computer systems, systems failure or otherwise, could damage our reputation and cause us to lose clients.

Although we have general liability insurance coverage, including coverage for errors or omissions, there can be no assurance that coverage will continue to be available on reasonable terms or will be sufficient in amount to cover one or more large claims, or that the insurer will not disclaim coverage as to any future claim. The successful assertion of one or more large claims against us that exceed available insurance coverage or changes in our insurance policies, including premium increases or the imposition of large deductible or co-insurance requirements, could have a material adverse effect on our business, results of operations and financial condition.

We may have potential liability arising from the IMS Health exchange offer in the event that we breach any of our representations in connection with the Distribution Agreement entered into with IMS Health.

We entered into a Distribution Agreement, dated January 7, 2003, with IMS Health, the Distribution Agreement, that provides, among other things, that IMS Health and we will comply with, and not take any action during the relevant time period that is inconsistent with, the representations made to and relied upon by McDermott, Will & Emery in connection with rendering its opinion regarding U.S. federal income tax consequences of the exchange offer. In addition, pursuant to the Distribution Agreement, we agreed to indemnify IMS Health for any tax liability to which they may be subject as a result of the exchange offer but only to the extent that such tax liability resulted solely from a breach of the representations that we made and were relied upon by McDermott, Will & Emery in connection with rendering its opinion regarding the U.S. federal income tax consequences of the exchange offer. If we breach any of our representations in connection with the Distribution Agreement, the related indemnification liability could have a material adverse effect on our results of operations, financial position and cash flows.

We may be subject to legacy Dun & Bradstreet liabilities that could have an adverse effect on our results of operations and financial condition.

In 1996, The Dun & Bradstreet Corporation, now known as R.H. Donnelly Corporation, split itself into three separate companies: The Dun & Bradstreet Corporation, Cognizant Corporation and ACNielsen Corporation. In connection with the split-up transaction, The Dun & Bradstreet Corporation, Cognizant Corporation (renamed Nielsen Media Research), of which we were once a part, and ACNielsen Corporation (now a subsidiary of the Dutch company VNU N.A.) entered into a distribution agreement. In the 1996 distribution agreement, each party assumed the liabilities relating to the businesses allocated to it and agreed to indemnify the other parties and their subsidiaries against those liabilities and certain other matters. The 1996 distribution agreement also prohibited each party thereto from distributing to our stockholders any business allocated to it unless the distributed business delivered undertakings agreeing to be jointly and severally liable to the other parties under the 1996 distribution agreement for the liabilities of the distributing parent company under the 1996 distribution agreement. IMS Health made such undertaking when it was spun off by Nielsen Media Research in 1998 and, accordingly, IMS Health and Nielsen Media Research are jointly and severally liable to R.H. Donnelly and ACNielsen for Cognizant Corporation obligations under the terms of the 1996 distribution agreement. IMS Health has requested similar undertakings from us as a condition to the distribution of our shares in the exchange offer. IMS Health is obligated to procure similar undertakings from us to Nielsen Media Research and Synavant Inc. with respect to liabilities allocated to IMS Health in connection with Nielsen Media Research s spin-off of IMS Health and IMS Health s spin-off of Synavant Inc. In connection with the exchange offer, we gave these undertakings and, as a result, we may be subject to claims in the future in relation to legacy liabilities.

Claims have arisen in the past and may arise in the future under the 1996 distribution agreement or the distribution agreements relating to Nielsen Media Research s spin-off of IMS Health and IMS Health s spin-off of Synavant Inc., in which case we may be jointly and severally liable for any losses suffered by the parties entitled to indemnification. IMS Health has agreed to indemnify us for any and all liabilities that arise out of our undertakings to be jointly and severally liable for these liabilities, but if for any reason IMS Health does not perform on our indemnification obligation, these liabilities could have a material adverse effect on our financial condition and results of operations.

If we are unable to protect our intellectual property rights, our business may be adversely affected.

Our future success will depend in part on our ability to protect our proprietary methodologies and other intellectual property. We presently hold no patents or registered copyrights, and rely upon a combination of copyright and trade secret laws, non-disclosure and other contractual arrangements and various security measures to protect our intellectual property rights. Existing laws of some countries in which we provide services or solutions might offer only limited protection of our intellectual property rights. India is a member of the Berne Convention, and has agreed to recognize protections on copyrights conferred under the laws of foreign countries, including the laws of the United States. We believe that laws, rules, regulations and treaties in effect in the United States and India are adequate to protect us from misappropriation or unauthorized use of our copyrights. However, there can be no assurance that these laws will not change and, in particular, that the laws of India or the United States will not change in ways that may prevent or restrict the transfer of software components, libraries and toolsets from India to the United States or from the United States to India. There can be no assurance that the steps we have taken to protect our intellectual property rights will be adequate to deter misappropriation of any of our intellectual property, or that we will be able to detect unauthorized use and take appropriate steps to enforce our rights. Unauthorized use of our intellectual property may result in development of technology, products or services which compete with our products and unauthorized parties may infringe upon or misappropriate our products, services or proprietary information. If we are unable to protect our intellectual property, our business may be adversely affected.

Our services or solutions could infringe upon the intellectual property rights of others or we might lose our ability to utilize the intellectual property of others.

We cannot be sure that our services and solutions, or the solutions of others that we offer to our clients, do not infringe on the intellectual property rights of third parties, and we could have infringement claims asserted against us or against our clients. These claims could harm our reputation, cost us money and prevent us from offering some services or solutions. In a number of our contracts, we have agreed to indemnify our clients for any expenses or liabilities resulting from claimed infringements of the intellectual property rights of third parties. In some instances, the amount of these indemnities could be greater than the revenues we receive from the client. Any claims or litigation in this area, whether we ultimately win or lose, could be time-consuming and costly, injure our reputation or require us to enter into royalty or licensing arrangements. We might not be able to enter into these royalty or licensing arrangements on acceptable terms. If a claim of infringement were successful against us or our clients, an injunction might be ordered against our client or our own services or operations, causing further damages. We expect that the risk of infringement claims against us will increase if our competitors are able to obtain patents for software products and processes. Any infringement claim or litigation against us could have a material adverse effect on our business, results of operations and financial condition.

We could lose our ability or be unable to secure the right to utilize the intellectual property of others. Third-party suppliers of software, hardware or other intellectual assets could be unwilling to permit us to use their intellectual property or be acquired or used, and this could impede or disrupt use of their products or services by us and our clients. If our ability to provide services and solutions to our clients is impaired, our operating results could be adversely affected.

We may be unable to integrate acquired companies or technologies successfully and we may be subject to certain liabilities assumed in connection with our acquisitions that could harm our operating results.

We believe that opportunities exist in the fragmented IT services market to expand our business through selective strategic acquisitions and joint ventures. We believe that acquisition and joint venture candidates may enable us to expand our geographic presence, especially in the European market, enter new technology areas or expand our capacity. We cannot assure you that we will identify suitable acquisition candidates available for sale at reasonable prices, consummate any acquisition or joint venture or successfully integrate any acquired business or joint venture into our operations. Further, acquisitions and joint ventures involve a number of special risks, including diversion of management s attention, failure to retain key personnel, unanticipated events or circumstances and legal liabilities, some or all of which could have a material adverse effect on our business, results of operations and financial condition. We may finance any future acquisitions with cash, debt financing, the issuance of equity securities or a combination of the foregoing. We cannot assure you that we will be able to arrange adequate financing on acceptable terms. In addition, acquisitions financed with the issuance of our equity securities could be dilutive.

Although we conduct due diligence in connection with each of our acquisitions, there may be liabilities that we fail to discover or that we inadequately assess in our due diligence efforts. In particular, to the extent that prior owners of any acquired businesses or properties failed to comply with or otherwise violated applicable laws or regulations, or failed to fulfill their contractual obligations to customers, we, as the successor owner, may be financially responsible for these violations and failures and may suffer reputational harm or otherwise be adversely affected. While we generally require the selling party to indemnify us for any and all liabilities associated with such liabilities, if for any reason the seller does not perform their indemnification obligation, we may be held responsible for such liabilities. The discovery of any material liabilities associated with our acquisitions for which we are unable to receive indemnification for could harm our operating results.

System failure or disruptions in telecommunications could disrupt our business and result in lost customers and curtailed operations which would reduce our revenue and profitability.

To deliver our services to our customers, we must maintain a high speed network of satellite, fiber optic and land lines and active voice and data communications 24 hours a day between our main offices in Chennai, our other IT development centers in India and globally and the offices of our customers worldwide. Although we maintain redundancy facilities and satellite communications links, any systems failure or a significant lapse in our ability to transmit voice and data through satellite and telephone communications could result in lost customers and curtailed operations which would reduce our revenue and profitability.

Provisions in our charter, by-laws and stockholders rights plan and provisions under Delaware law may discourage unsolicited takeover proposals.

Provisions in our charter and by-laws, each as amended, our stockholders rights plan and Delaware General Corporate Law, or DGCL, may have the effect of deterring unsolicited takeover proposals or delaying or preventing changes in our control or management, including transactions in which stockholders might otherwise receive a premium for their shares over then current market prices. In addition, these documents and provisions may limit the ability of stockholders to approve transactions that they may deem to be in their best interests. Our board of directors has the authority, without further action by the stockholders, to fix the rights and preferences, and issue shares of preferred stock. Our charter provides for a classified board of directors, which will prevent a change of control of our board of directors at a single meeting of stockholders. The prohibition of our stockholders ability to act by written consent and to call a special meeting will delay stockholder actions until annual meetings or until a special meeting is called by our chairman or chief executive officer or our board of directors. The supermajority-voting requirement for specified amendments to our charter and by-laws allows a minority of our stockholders to block those amendments. The DGCL also contains provisions preventing stockholders from engaging in business combinations with us, subject to certain exceptions. These provisions could also discourage bids for our common stock at a premium as well as create a depressive effect on the market price of the shares of our common stock.

Compliance with new and changing corporate governance and public disclosure requirements adds uncertainty to our compliance policies and increases our costs of compliance.

Changing laws, regulations and standards relating to accounting, corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, other SEC regulations, and the NASDAQ Global Select Market rules, are creating uncertainty for companies like ours. These laws, regulations and standards may lack specificity and are subject to varying interpretations. Their application in practice may evolve over time, as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs of compliance as a result of ongoing revisions to such corporate governance standards.

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In particular, our efforts to comply with Section 404 of the Sarbanes-Oxley Act of 2002 and the related regulations regarding our required assessment of our internal controls over financial reporting and our external auditors audit of that assessment requires the commitment of significant financial and managerial resources. We consistently assess the adequacy of our internal controls over financial reporting, remediate any control deficiencies that may be identified, and validate through testing that our controls are functioning as documented. While we do not anticipate any material weaknesses, the inability of management and our independent auditor to provide us with an unqualified report as to the adequacy and effectiveness, respectively, of our internal controls over financial reporting for future year ends could result in adverse consequences to us, including, but not limited to, a loss of investor confidence in the reliability of our financial statements, which could cause the market price of our stock to decline.

We are committed to maintaining high standards of corporate governance and public disclosure, and our efforts to comply with evolving laws, regulations and standards in this regard have resulted in, and are likely to continue to result in, increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities. In addition, the new laws, regulations and standards regarding corporate governance may make it more difficult for us to obtain director and officer liability insurance. Further, our board members, chief executive officer and chief financial officer could face an increased risk of personal liability in connection with their performance of duties. As a result, we may face difficulties attracting and retaining qualified board members and executive officers, which could harm our business. If we fail to comply with new or changed laws, regulations or standards of corporate governance, our business and reputation may be harmed.

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

Our annual meeting of stockholders, or the Annual Meeting, was held on June 7, 2007. There were present at the Annual Meeting in person or by proxy stockholders holding an aggregate of 128,737,737 shares of our Class A common stock out of a total number of 143,749,939 shares of Class A common stock issued and outstanding and entitled to vote at the meeting.

The matters that were voted on at the Annual Meeting were:

(A) A proposal to elect the following two nominees as our Class I Directors to serve until our 2010 annual meeting of stockholders and until their respective successors have been duly elected and qualified:

Lakshmi Narayanan; and

John E. Klein;

(B) A proposal to amend our Amended and Restated 1999 Incentive Compensation Plan (the Incentive Plan), to (i) increase the maximum number of shares of Class A Common Stock reserved for issuance under the Incentive Plan by an additional 3,500,000 shares from 38,261,580 to 41,761,580 shares of Class A Common Stock and (ii) reconfirm the performance goals which may serve as the basis for structuring awards under the Incentive Plan to qualify as performance-based compensation for purposes of Internal Revenue Code Section 162(m); and

(C) A proposal to ratify the appointment of PricewaterhouseCoopers LLP, as our independent registered public accounting firm for the year ending December 31, 2007.

The results of the votes of the Annual Meeting were as follows:

	Number of Shares of Class A Common Stock	
Proposal	**For**	**Withheld**
Election of the following two nominees as Class I Directors:		
Lakshmi Narayanan	125,557,324	3,180,411
John E. Klein	126,523,075	2,214,660

Number of Shares of

	Class A Common Stock		
Proposal	**For**	**Against**	**Abstain**
Proposal to amend the Amended and Restated 1999 Incentive Compensation Plan	84,508,814	28,597,483	962,543

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Proposal	Number of Shares of Class A Common Stock For	Against	Abstain
Proposal to ratify the appointment of PricewaterhouseCoopers LLP as our independent registered public accounting firm for the year ending December 31, 2007	126,864,594	1,112,595	758,254

Accordingly, our stockholders elected Lakshmi Narayanan and John E. Klein to serve as Class I Directors until our 2010 annual meeting of stockholders and until their respective successors have been duly elected and qualified. Each of the following Directors who were not up for reelection at the Annual Meeting continue to serve as Directors since the Annual Meeting: Robert W. Howe, Robert E. Weissman, Thomas M. Wendel and Francisco D Souza.

Our stockholders also approved the amendment to our Incentive Plan and ratified the selection by the audit committee of our board of directors of PricewaterhouseCoopers LLP as our independent registered public accounting firm for the year ending December 31, 2007.

Item 6. Exhibits.

(a) Exhibits.

Exhibit No.	Description
10.1	Cognizant Technology Solutions Corporation Amended and Restated 1999 Incentive Compensation Plan (as amended and restated through April 26, 2007). (Incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed June 8, 2007.)
10.2	Severance and Noncompetition Agreement with Rajeev Mehta dated July 23, 2007. (Incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed July 24, 2007.)
31.1	Certification of principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of principal financial and accounting officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of principal executive officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. 1350.
32.2	Certification of principal financial and accounting officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. 1350.

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SIGNATURES

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

	Cognizant Technology Solutions Corporation
Date: August 8, 2007	By: /s/ Francisco D Souza, Francisco D Souza, President, Chief Executive Officer and Director (Principal Executive Officer)
Date: August 8, 2007	By: /s/ Gordon Coburn Gordon Coburn, Chief Financial and Operating Officer and Treasurer (Principal Financial and Accounting Officer)

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