

COGNIZANT TECHNOLOGY SOLUTIONS CORP  
Form 10-Q  
May 07, 2010  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

**Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
For the quarterly period ended March 31, 2010

**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)

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**Delaware**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**13-3728359**  
(I.R.S. Employer  
Identification No.)

**Glenpointe Centre West**

**500 Frank W. Burr Blvd.**

**Teaneck, New Jersey**  
(Address of Principal Executive Offices)

**07666**  
(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  No:

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No:

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's class of common stock, as of April 30, 2010:

Class	Number of Shares
Class A Common Stock, par value \$.01 per share	299,418,969

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**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Condensed Consolidated Financial Statements (unaudited).  
COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)****(in thousands, except per share data)**

	<b>Three Months Ended March 31,</b>	
	<b>2010</b>	<b>2009</b>
Revenues	\$ 959,720	\$ 745,862
Operating expenses:		
Cost of revenues (exclusive of depreciation and amortization expense shown separately below)	555,904	419,708
Selling, general and administrative expenses	194,993	166,872
Depreciation and amortization expense	25,806	21,152
Income from operations	183,017	138,130
Other income (expense), net:		
Interest income	6,054	2,470
Other income (expense), net	(10,319)	(5,111)
Total other income (expense), net	(4,265)	(2,641)
Income before provision for income taxes	178,752	135,489
Provision for income taxes	27,252	22,357
Net income	\$ 151,500	\$ 113,132
Basic earnings per share	\$ 0.51	\$ 0.39
Diluted earnings per share	\$ 0.49	\$ 0.38
Weighted average number of common shares outstanding Basic	297,885	291,613
Dilutive effect of shares issuable under stock-based compensation plans	8,779	6,380
Weighted average number of common shares outstanding Diluted	306,664	297,993

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)

	March 31, 2010	December 31, 2009
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 1,080,942	\$ 1,100,930
Short-term investments	352,939	298,402
Trade accounts receivable, net of allowances of \$19,143 and \$16,465, respectively	706,122	626,288
Unbilled accounts receivable	106,203	82,952
Deferred income tax assets, net	60,807	73,791
Other current assets	162,220	125,205
<b>Total current assets</b>	<b>2,469,233</b>	<b>2,307,568</b>
Property and equipment, net of accumulated depreciation of \$297,911 and \$274,570, respectively	478,363	481,516
Long-term investments	137,447	151,131
Goodwill	193,898	192,372
Intangible assets, net	76,745	75,757
Deferred income tax assets, net	86,584	80,618
Other assets	67,477	49,278
<b>Total assets</b>	<b>\$ 3,509,747</b>	<b>\$ 3,338,240</b>
<b>Liabilities and Stockholders Equity</b>		
Current liabilities:		
Accounts payable	\$ 85,630	\$ 54,640
Deferred revenue	53,576	51,605
Accrued expenses and other current liabilities	438,941	540,363
<b>Total current liabilities</b>	<b>578,147</b>	<b>646,608</b>
Other noncurrent liabilities	45,231	38,455
<b>Total liabilities</b>	<b>623,378</b>	<b>685,063</b>
Commitments and contingencies (See Note 7)		
Stockholders equity:		
Preferred stock, \$.10 par value, 15,000 shares authorized, none issued		
Class A common stock, \$.01 par value, 500,000 shares authorized, 299,380 and 297,231 shares issued and outstanding at March 31, 2010 and December 31, 2009, respectively	2,994	2,972
Additional paid-in capital	722,464	664,560
Retained earnings	2,116,868	1,965,368
Accumulated other comprehensive income	44,043	20,277
<b>Total stockholders equity</b>	<b>2,886,369</b>	<b>2,653,177</b>
<b>Total liabilities and stockholders equity</b>	<b>\$ 3,509,747</b>	<b>\$ 3,338,240</b>

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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 Three Months Ended March 31,	
	2010	2009
Cash flows from operating activities:		
Net income	\$ 151,500	\$ 113,132
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	27,381	21,152
Provision for doubtful accounts	2,658	14
Deferred income taxes	23,326	3,935
Stock-based compensation expense	13,945	11,763
Excess tax benefit on stock-based compensation plans	(15,753)	(1,819)
Other	(10,162)	675
Changes in assets and liabilities:		
Trade accounts receivable	(92,220)	(13,342)
Other current assets	(46,307)	(7,596)
Other assets	(4,989)	(66)
Accounts payable	36,088	16,861
Other current and noncurrent liabilities	(83,139)	(69,619)
Net cash provided by operating activities	2,328	75,090
Cash flows from investing activities:		
Purchases of property and equipment	(24,219)	(20,472)
Purchases of investments	(46,798)	(40,743)
Proceeds from maturity or sale of investments	13,876	18,974
Acquisitions, net of cash acquired		(1,304)
Net cash used in investing activities	(57,141)	(43,545)
Cash flows from financing activities:		
Issuance of common stock under stock-based compensation plans	30,103	8,764
Excess tax benefit on stock-based compensation plans	15,753	1,819
Repurchases of common stock	(2,315)	(12,882)
Net cash provided by (used in) financing activities	43,541	(2,299)
Effect of currency translation on cash and cash equivalents	(8,716)	(5,744)
Increase (decrease) in cash and cash equivalents	(19,988)	23,502
Cash and cash equivalents, beginning of year	1,100,930	735,066
Cash and cash equivalents, end of period	\$ 1,080,942	\$ 758,568

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





**Table of Contents****COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(dollar amounts in thousands)****Note 1 Interim Condensed Consolidated Financial Statements**

The terms Cognizant, we, our, us and Company refer to Cognizant Technology Solutions Corporation unless the context indicates otherwise. We have prepared the accompanying unaudited condensed consolidated financial statements included herein 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. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements (and notes thereto) included in our Annual Report on Form 10-K for the year ended December 31, 2009. In our opinion, 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.

We have evaluated subsequent events and have concluded no additional events or transactions have occurred that would require adjustment to, or additional disclosure in, our financial statements.

**Note 2 Investments**

Investments as of March 31, 2010 and December 31, 2009 were as follows:

	March 31, 2010	December 31, 2009
Available-for-sale securities:		
Agency discount notes	\$ 160	\$ 160
Other	2	2
Total available-for-sale securities	162	162
Trading securities    auction-rate securities	119,050	129,103
UBS Right	18,397	22,028
Time deposits	352,777	298,240
Total investments	\$ 490,386	\$ 449,533

The carrying value of the time deposits approximated fair value as of March 31, 2010 and December 31, 2009. Gross realized gains or losses on the sale of available-for-sale securities were immaterial for the periods presented. As of March 31, 2010 and December 31, 2009, available-for-sale securities in an unrealized loss or gain position were immaterial. All available-for-sale securities at March 31, 2010 and December 31, 2009 contractually mature in 2010.

Our investment in auction-rate securities are recorded at fair value and consist of AAA/A3-rated municipal bonds with an auction reset feature whose underlying assets are generally student loans, which are substantially backed by the Federal Family Education Loan Program ( FFELP ). Since February 2008, auctions for these securities have failed. The auction failures do not affect the value of the collateral underlying the auction-rate securities, and we continue to earn and receive interest on our auction-rate securities at a pre-determined formula with spreads tied to particular interest rate indices. As of March 31, 2010 and December 31, 2009, the majority of our investment in auction-rate securities was classified as a long-term investment. The classification of the auction-rate securities as long-term investments is due to continuing auction failures, the securities' stated maturity of greater than one year and our ability and intent to hold such securities beyond one year.

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In November 2008, we accepted an offer from UBS AG ( UBS ) to sell to UBS, at par value, our auction-rate securities at any time during an exercise period from June 30, 2010 to July 2, 2012 (the UBS Right ). In accepting the UBS Right, we granted UBS the authority to purchase these auction-rate securities or sell them on our behalf at par anytime after the execution of the UBS Right through July 2, 2012. The offer is non-transferable.

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Additional information regarding our auction-rate securities was as follows:

	March 31, 2010	December 31, 2009
Par value	\$ 137,575	\$ 151,275
	<b>Three Months Ended</b>	<b>Year Ended</b>
	<b>March 31, 2010</b>	<b>December 31, 2009</b>
Redemptions at par value	\$ 13,700	\$ 17,250

**Note 3. Accrued Expenses and Other Current Liabilities**

Accrued expenses and other current liabilities were as follows as of:

	March 31, 2010	December 31, 2009
Compensation and benefits	\$ 238,826	\$ 356,127
Taxes	3,386	10,300
Professional fees	33,109	26,508
Travel and entertainment	16,750	15,871
Customer volume incentives	46,613	44,537
Derivative financial instruments	36,916	20,968
Other	63,341	66,052
Total accrued expenses and other current liabilities	\$ 438,941	\$ 540,363

**Note 4 Income Taxes**

Our Indian subsidiaries, collectively referred to as Cognizant India, are export-oriented companies, which, under the Indian Income Tax Act of 1961 are entitled to claim tax holidays for a period of ten consecutive years for each Software Technology Park, or 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 STPs in India are currently entitled to a 100% exemption from Indian income tax. The tax holidays for STPs currently expire on March 31, 2011. In addition, we have constructed our new development centers in areas designated as Special Economic Zones, or SEZs. Development centers operating in SEZs will be entitled to certain income tax incentives for periods up to 15 years. The incremental Indian taxes related to the taxable STPs, for which the income tax holiday has expired, have been incorporated into our effective income tax rate for 2010. The effective tax rate for the three months ended March 31, 2010 and for the three months ended March 31, 2009 was as follows:

	Three Months Ended	
	March 31,	
	2010	2009
Effective tax rate	15.2%	16.5%

The principal difference between the income tax rates for the 2010 and 2009 periods and the U.S. federal statutory rate is the effect of the Indian tax holiday and earnings taxed in countries that have lower rates than the United States.

**Note 5 Fair Value Measurements**

We measure our cash equivalents, investments, including auction-rate securities, and foreign exchange forward contracts at fair value. The authoritative guidance defines fair value as the exit price, or the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. The authoritative guidance also establishes a fair value hierarchy that is intended to increase consistency and comparability in fair value measurements and related disclosures. The fair value hierarchy is based on inputs to valuation techniques that are used to measure fair value that are either observable or unobservable. Observable inputs reflect assumptions market participants would use in pricing an asset or liability based on market data obtained from independent sources while unobservable inputs reflect a reporting entity's pricing based upon their own market assumptions.

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The fair value hierarchy consists of the following three levels:

Level 1 Inputs are quoted prices in active markets for identical assets or liabilities.

Level 2 Inputs are quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable and market-corroborated inputs which are derived principally from or corroborated by observable market data.

Level 3 Inputs are derived from valuation techniques in which one or more significant inputs or value drivers are unobservable.

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The following table summarizes our financial assets and (liabilities) measured at fair value on a recurring basis as of March 31, 2010:

	Level 1	Level 2	Level 3	Total
<b>Cash equivalents:</b>				
Money market funds	\$ 675,740	\$	\$	\$ 675,740
<b>Investments:</b>				
Available-for-sale securities current		162		162
Trading securities noncurrent			119,050	119,050
UBS Right noncurrent			18,397	18,397
<b>Other current assets:</b>				
Derivative financial instruments foreign exchange forward contracts		36,414		36,414
<b>Other current liabilities:</b>				
Derivative financial instruments foreign exchange forward contracts		(36,916)		(36,916)
<b>Other assets:</b>				
Derivative financial instruments foreign exchange forward contracts		15,223		15,223
<b>Total assets and (liabilities) measured at fair value</b>	<b>\$ 675,740</b>	<b>\$ 14,883</b>	<b>\$ 137,447</b>	<b>\$ 828,070</b>

The following table summarizes our financial assets and (liabilities) measured at fair value on a recurring basis as of December 31, 2009:

	Level 1	Level 2	Level 3	Total
<b>Cash equivalents:</b>				
Money market funds	\$ 778,311	\$	\$	\$ 778,311
<b>Investments:</b>				
Available-for-sale securities current		162		162
Trading securities noncurrent			129,103	129,103
UBS Right noncurrent			22,028	22,028
<b>Other current assets:</b>				
Derivative financial instruments foreign exchange forward contracts		20,358		20,358
<b>Other current liabilities:</b>				
Derivative financial instruments foreign exchange forward contracts		(20,968)		(20,968)
<b>Other assets:</b>				
Derivative financial instruments foreign exchange forward contracts		688		688
<b>Other noncurrent liabilities:</b>				
Derivative financial instruments foreign exchange forward contracts		(1,917)		(1,917)
<b>Total assets and (liabilities) measured at fair value</b>	<b>\$ 778,311</b>	<b>\$ (1,677)</b>	<b>\$ 151,131</b>	<b>\$ 927,765</b>

During the three months ended March 31, 2010, there were no transfers between Level 1 and Level 2 financial assets and liabilities. Level 3 assets consist of our investment in auction-rate securities and the related UBS Right. See Note 2 for additional information. The following table provides a summary of changes in fair value of our Level 3 financial assets for the quarter ended March 31, 2010 and year ended December 31, 2009:

	Three Months Ended March 31, 2010	Twelve Months Ended December 31, 2009
Balance, at the beginning of the period	\$ 151,131	\$ 167,556
Transfers out: redemptions of called auction-rate securities	(13,700)	(17,250)
Gain related to auction-rate securities included in other income (expense), net	3,646	6,955
Loss related to UBS Right included in other income (expense), net	(3,630)	(6,130)

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Balance, at the end of the period	\$	137,447	\$	151,131
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We estimated the fair value of the auction-rate securities using a discounted cash flow model analysis which considered the following key inputs: (i) the underlying structure of each security; (ii) the timing of expected future principal and interest payments; and (iii) discount rates, inclusive of an illiquidity risk premium, that are believed to reflect current market conditions and the relevant risk associated with each security. We estimated the value of the UBS Right using a fair value model analysis, which considered the following key inputs: discount rate, timing and amount of cash flow, and UBS counterparty risk. The assumptions used in valuing both the auction-rate securities and the UBS Right are volatile and subject to change as the underlying sources of these assumptions and market conditions change.

We estimated the value of each foreign exchange forward contract by using a present value of expected cash flows model. This model calculates the difference between the current market forward price and the contracted forward price for each foreign exchange contract and applies the difference in the rates to each outstanding contract. The market forward rates included a discount and credit risk factor. The amounts were aggregated by type of contract and maturity.

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In addition to the debt securities discussed above, we had approximately \$352,777 and \$298,240 of time deposits included in short-term investments as of March 31, 2010 and December 31, 2009, respectively.

**Note 6 Derivative Financial Instruments**

In the normal course of business, we use foreign exchange forward contracts to manage foreign currency exchange rate risk. The estimated fair value of the foreign exchange forward contracts considers the following items: discount rate, timing and amount of cash flow and counterparty credit risk. The following table provides information on the location and fair values of derivative financial instruments included in our condensed consolidated statements of financial position as of March 31, 2010:

Designation of Derivatives	Location on Statement of Financial Position	Assets	Liabilities
<b>Cash Flow Hedges</b> Designated as hedging instruments			
Foreign exchange forward contracts	Other current assets	\$ 36,414	\$
	Other assets	15,223	
	Total	51,637	
<b>Other Derivatives</b> Not designated as hedging instruments			
Foreign exchange forward contracts	Accrued expenses and other current liabilities		36,916
	Total		36,916
Total		\$ 51,637	\$ 36,916

The following table provides information on the location and fair values of derivative financial instruments in our condensed consolidated statements of financial position as of December 31, 2009:

Designation of Derivatives	Location on Statement of Financial Position	Assets	Liabilities
<b>Cash Flow Hedges</b> Designated as hedging instruments			
Foreign exchange forward contracts	Other current assets	\$ 20,211	\$
	Other assets	688	
	Other noncurrent liabilities		1,917
	Total	20,899	1,917
<b>Other Derivatives</b> Not designated as hedging instruments			
Foreign exchange forward contracts	Other current assets	147	
	Accrued expenses and other current liabilities		20,968
	Total	147	20,968
Total		\$ 21,046	\$ 22,885

*Cash Flow Hedges*

We have entered into a series of foreign exchange forward contracts that are designated as cash flow hedges of certain salary payments in India. These contracts are intended to partially offset the impact of movement of exchange rates on future operating costs and are scheduled to mature each month during 2010, 2011 and 2012. Under these contracts, we purchase Indian rupees and sell U.S. dollars and the changes in fair value of these contracts are initially reported in the caption accumulated other comprehensive income on our accompanying condensed consolidated statements of financial position and is subsequently reclassified to earnings in the same period the hedge contract settles. The notional value of

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our outstanding contracts by year of maturity and the net unrealized gain included in accumulated other comprehensive income for such contracts are as follows:

	<b>March 31, 2010</b>	<b>December 31, 2009</b>
2010	\$ 420,000	\$ 450,000
2011	480,000	360,000
2012	300,000	
Total notional value of contracts outstanding	\$ 1,200,000	\$ 810,000
Net unrealized gain included in accumulated other comprehensive income	\$ 50,081	\$ 18,410



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Upon settlement or maturity of the cash flow hedge contracts, we record the related gain or loss, based on our designation at the commencement of the contract, to salary expense reported within cost of revenues and selling, general and administrative expenses. The tables below provide information on the location and amounts of gains or losses on our cash flow hedges included in our condensed consolidated statement of operations for the three months ended March 31, 2010 and 2009.

*Other Derivatives*

We also use foreign exchange forward contracts, which have not been designated as hedges, to hedge our balance sheet exposure to Indian rupee denominated net monetary assets. During 2009, we entered into a series of foreign exchange forward contracts to purchase U.S. dollars and sell Indian rupees. Realized gains or losses and changes in the estimated fair value of these derivative financial instruments are recorded in other income (expense), net as a component of foreign currency exchange gains or losses in our condensed consolidated statements of operations. Additional information related to our outstanding contracts is as follows:

	March 31, 2010	December 31, 2009
Notional value of contracts outstanding	\$ 400,000	\$ 400,000

The following table provides information on the location and amounts of pre-tax gains (losses) on our derivative financial instruments for the three months ended March 31, 2010:

Cash Flow Hedges	Designated as hedging instruments	Increase in Derivative Gains (Losses) Recognized in Accumulated Other Comprehensive Income (effective portion)	Location of Net Derivative Gains (Losses) Reclassified from Accumulated Other Comprehensive Income into Income (effective portion)	Net Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Income (effective portion)
	Foreign exchange forward contracts	\$ 42,024	Cost of revenues	\$ 8,332
			Selling, general and administrative expenses	1,037
Total		\$ 42,024		\$ 9,369

Other Derivatives	Not designated as hedging instruments	Location of Net Gains / (Losses) on Derivative Instruments	Amount of Net Gains (Losses) on Derivative Instruments
	Foreign exchange forward contracts	Other income (expense), net	\$ (16,095)
Total			\$ (16,095)

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The following table provides information on the location and amounts of pre-tax gains (losses) on our derivative financial instruments for the three months ended March 31, 2009:

	Increase in Derivative Gains (Losses) Recognized in Accumulated Other Comprehensive Income (effective portion)	Location of Net Derivative Gains (Losses) Reclassified from Accumulated Other Comprehensive Income into Income (effective portion)	Net Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Income (effective portion)
Cash Flow Hedges Designated as hedging instruments			
Foreign exchange forward contracts	\$ (11,653)	Cost of revenues	\$ (1,077)
		Selling, general and administrative expenses	(220)
Total	\$ (11,653)		\$ (1,297)

The related cash flow impacts of all of our derivative activities are reflected as cash flows from operating activities.

**Note 7 Commitments and Contingencies**

As of March 31, 2010, we had outstanding fixed capital commitments of approximately \$21,331 related to our India development center expansion program.

In connection with a 2008 acquisition, additional purchase price not to exceed \$14,000, payable in 2010, is contingent on the acquired company achieving certain financial and operating targets during an earn-out period. We expect to fund such payment, if any, from operating cash flow. The ultimate amount payable cannot be predicted with reasonable certainty because the amount is dependent on future results of operations of the acquired business. In accordance with U.S. GAAP, we have not recorded a liability for this item on our balance sheet because the definitive amount is not determinable or distributable. As this acquisition was completed in 2008, the contingent consideration, if paid, will be recorded as an additional element of the cost of the acquired company.

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 business, financial condition and results of operations. 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 systems or our failure to meet our contractual obligations to our clients, including any breach involving a customer's confidential information or sensitive data, or our obligations under applicable laws or regulations 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 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 available in sufficient amounts 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, would have a material adverse effect on our business, results of operations and financial condition.

**Note 8 Comprehensive Income**

The components of accumulated other comprehensive income as of March 31, 2010 and December 31, 2009 were as follows:

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	<b>March 31, 2010</b>	<b>December 31, 2009</b>
Foreign currency translation adjustments	\$ (6,038)	\$ 1,867
Unrealized gain on cash flow hedges, net of taxes	50,081	18,410
<b>Total accumulated other comprehensive income</b>	<b>\$ 44,043</b>	<b>\$ 20,277</b>

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The components of comprehensive income for the three months ended March 31, 2010 and 2009 were as follows:

	2010	2009
Comprehensive income:		
Net income	\$ 151,500	\$ 113,132
Foreign currency translation adjustments	(7,905)	(5,548)
Change in unrealized gain (loss) on cash flow hedges, net of taxes of \$984 and (\$386), respectively	31,671	(9,969)
Total comprehensive income	\$ 175,266	\$ 97,615

**Note 9 Segment Information**

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 segments which, individually, are less than 10% of consolidated revenues and segment operating profit. The Other reportable segment includes entertainment, media and information services, communications 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.

Our 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. 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 segments 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 our development and delivery 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 and the related stock-based Indian fringe benefit tax are 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 our total income from operations. 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 months ended March 31, 2010 and 2009, are as follows:

	Three Months Ended March 31,	
	2010	2009
<b>Revenues:</b>		
Financial Services	\$ 398,687	\$ 331,342
Healthcare	252,425	189,326
Manufacturing/Retail/Logistics	173,131	123,090
Other	135,477	102,104
Total revenue	\$ 959,720	\$ 745,862
<b>Segment Operating Profit:</b>		
Financial Services	\$ 128,264	\$ 113,386
Healthcare	92,357	69,548
Manufacturing/Retail/Logistics	54,812	36,332
Other	43,186	32,800

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Total segment operating profit	318,619	252,066
Less: unallocated costs <sup>(1)</sup>	135,602	113,936
Income from operations	\$ 183,017	\$ 138,130

- (1) Includes \$13,945 of stock-based compensation expense for the three months ended March 31, 2010, and \$11,763 of stock-based compensation expense and \$945 of stock-based Indian fringe benefit tax expense for the three months ended March 31, 2009.

**Table of Contents***Geographic Area Information*

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

	Three Months Ended March 31,	
	2010	2009
<b>Revenues</b> <sup>(1)</sup>		
North America <sup>(2)</sup>	\$ 755,690	\$ 593,790
Europe <sup>(3)</sup>	173,632	136,028
Other <sup>(4)</sup>	30,398	16,044
<b>Total</b>	<b>\$ 959,720</b>	<b>\$ 745,862</b>

	As of March 31, 2010	As of December 31, 2009
	<b>Long-lived Assets</b> <sup>(5)</sup>	
North America <sup>(2)</sup>	\$ 11,688	\$ 9,042
Europe	3,015	3,145
Other <sup>(4)(6)</sup>	463,660	469,329
<b>Total</b>	<b>\$ 478,363</b>	<b>\$ 481,516</b>

- (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 \$106,621 and \$80,382 for the three months ended March 31, 2010 and 2009, respectively.
- (4) Includes our operations in Asia Pacific, Middle East and South America.
- (5) Long-lived assets include property and equipment, net of accumulated depreciation and amortization.
- (6) Substantially all of these long-lived assets relate to our operations in India.

**Note 10 Recent Accounting Pronouncements**

In October 2009, the FASB issued a new accounting standard which provides guidance for arrangements with multiple deliverables. Specifically, the new standard requires an entity to allocate consideration at the inception of an arrangement to all of its deliverables based on their relative selling prices. In the absence of the vendor-specific objective evidence or third-party evidence of the selling prices, consideration must be allocated to the deliverables based on management's best estimate of the selling prices. In addition, the new standard eliminates the use of the residual method of allocation. In October 2009, the FASB also issued a new accounting standard which changes revenue recognition for tangible products containing software and hardware elements. Specifically, tangible products containing software and hardware that function together to deliver the tangible products' essential functionality are scoped out of the existing software revenue recognition guidance and will be accounted for under the multiple-element arrangements revenue recognition guidance discussed above. Both standards are required to be effective by no later than the first quarter of 2011 and early adoption is permitted. We have adopted both of these standards effective January 1, 2010. Our adoption of these standards did not have a material effect on our financial condition or consolidated results of operations.

In January 2010, the FASB issued new guidance requiring supplemental fair value disclosures and providing several clarifications regarding existing disclosure requirements. Specifically, the new guidance requires an entity to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and to describe the reasons for the transfers. In addition, the new standard requires a gross presentation of the Level 3 rollforward, stating separately information about purchases, sales, issuances, and settlements. The new guidance also provides clarification regarding the appropriate level of disaggregation of assets and liabilities for the purpose of fair value disclosures as well as the requirement to provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring Level 2 and Level 3 measurements. We have adopted the new guidance effective January 1, 2010 and have presented

the required information in Note 5.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.  
Executive Summary**

During the three months ended March 31, 2010, our revenue increased to \$959.7 million compared to \$745.9 million during the three months ended March 31, 2009. Net income increased to \$151.5 million, or \$0.49 per diluted share, including stock-based compensation expense, net of tax, equal to \$0.04 per diluted share, during the three months ended March 31, 2010. This is compared to net income of \$113.1 million, or \$0.38 per diluted share, including stock-based compensation expense and applicable stock-based Indian fringe benefit tax expense, net of tax, of \$0.03 per diluted share, during the three months ended March 31, 2009. The key drivers of our revenue growth during the three months ended March 31, 2010 were as follows:

Strong performance across all our business segments, with revenue growth ranging from 20.3% for Financial Services to 40.7% for Manufacturing/Retail/Logistics for the quarter as compared to the quarter ended March 31, 2009;

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continued penetration of the European market, particularly in the UK where we experienced revenue growth of 32.6% for the quarter as compared to the quarter ended March 31, 2009;

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

continued expansion of the market for global delivery of IT services and business process outsourcing.

We saw a continued increase in demand from our customers for a broad range of IT solutions, including application maintenance, complex systems development engagements, testing, enterprise resource planning, or ERP, infrastructure management, business process outsourcing and business intelligence. We finished the quarter with approximately 597 active clients compared to 560 as of March 31, 2009 and increased the number of strategic clients by five during the quarter bringing the total number of our strategic clients to 149. We define a strategic client as one offering the potential to generate \$5 million to \$50 million or more in annual revenues at maturity. Our top five and top ten customers accounted for approximately 17.6% and 30.3%, respectively, of our total revenues during the quarter ended March 31, 2010 as compared to approximately 17.6% and 29.3%, respectively, for the quarter ended March 31, 2009. 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 decline over time.

During the quarter ended March 31, 2010, our revenue from European customers increased by 27.6% to approximately \$173.6 million compared to approximately \$136.0 million in the quarter ended March 31, 2009. For the quarter ended March 31, 2010, revenue from Europe, excluding the UK, increased by approximately \$11.4 million from approximately \$55.6 million in the quarter ended March 31, 2009 to approximately \$67.0 million and revenue from the UK increased by approximately \$26.2 million from approximately \$80.4 million in the quarter ended March 31, 2009 to approximately \$106.6 million. We believe that Europe will continue to be an area of significant investment for us as we see this region and the Asia Pacific region, particularly Japan, India, Australia and Singapore, as growth opportunities for the long term.

Our revenue growth was also attributed to increasing market acceptance of, and strong demand for, offshore IT software and services and business process outsourcing. Recent NASSCOM (India's National Association of Software and Service Companies) reports state that India's IT software and services and business process outsourcing sectors was expected to reach almost \$50 billion by the end of NASSCOM's fiscal year ended March 31, 2010. This is an expected growth rate of approximately 5.5% over the prior fiscal year. Additionally, the FY 2010-11 Outlook for these sectors expects revenue growth of 13% to 15%. According to the latest NASSCOM Perspective 2020: Transform Business, Transform India report, global changes and new megatrends within economic, demographic, business, social and environmental areas are set to expand the outsourcing industry by creating new dynamics and opportunities and are expected to result in export revenues of \$175 billion by 2020.

Our operating margin increased to approximately 19.1% for the quarter ended March 31, 2010 compared to 18.5% for the quarter ended March 31, 2009. Excluding stock-based compensation expense of approximately \$13.9 million, operating margin for the quarter ended March 31, 2010 was approximately 20.5%. This was slightly above our historic targeted operating margin range, excluding stock-based compensation expense and applicable stock-based Indian fringe benefit tax expense, of 19% to 20% of total revenues. The operating margin increase was primarily due to achieving operating efficiencies partially offset by an increase in compensation costs, including incentive-based compensation expense, investments to grow our business and the appreciation of the Indian rupee versus the U.S. dollar. Historically, we have invested our profitability above the 19% to 20% operating margin level, which excludes stock-based compensation and any related stock-based Indian fringe benefit tax expense, 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 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 level of resources, trained in a broad range of service offerings, to be well positioned to respond to our customer requests to take on additional projects. For the year ending December 31, 2010, we expect to continue to invest amounts in excess of our historical targeted operating margin levels back into the business.

We finished the first quarter of 2010 with total headcount of approximately 85,500, which is an increase of approximately 21,800 as compared to the total headcount at March 31, 2009. The increase in the number of our technical personnel and the related infrastructure costs, to meet the demand for our services, is the primary driver of the increase in our operating expenses in 2010. Annualized turnover, including both voluntary and involuntary, was approximately 16.4% during the three months ended March 31, 2010. The majority of





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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 increases in compensation and benefit costs, including incentive-based compensation costs, in India which may continue in the future; however, this has not had a material impact on our results of operations as Indian wages were approximately 22% of our total operating expenses for the three months ended March 31, 2010.

During 2010, we expect to spend approximately \$180.0 million globally for capital expenditures, a portion of which relates to our India real estate development program that includes expenditures for land acquisition, facilities construction and furnishings to build new state-of-the-art development and delivery centers in regions primarily designated as Special Economic Zones located in India.

At March 31, 2010, we had cash and cash equivalents and short-term investments of \$1,433.9 million and working capital of \$1,891.1 million. Accordingly, we do not anticipate any near-term liquidity issues.

While several measures have indicated that the economy maybe improving, the economic environment remains fragile. During 2010, we expect the following factors to affect our business and our operating results:

Stabilization of global economic conditions and the financial services sector;

Normalization of customer IT budgets, which may result in spending by customers on discretionary projects, specifically application development projects. In addition, we expect a continued focus by customers on directing IT spending towards cost containment projects, such as application maintenance, infrastructure management and BPO;

Industry consolidation, which will drive demand for integration services;

Secular changes driven by evolving technologies and regulatory changes; and

Foreign currency volatility.

In response to this challenging macroeconomic environment, we plan to:

Continue to invest in our talent base and new service offerings;

Partner with our existing customers to see where we can provide innovative solutions resulting in our garnering an increased portion of our customers overall IT spend;

Continue our focus on growing our business in Europe and the Asia Pacific region, where we believe there are opportunities to gain market share;

Expand our BPO and infrastructure management practices, which are in high demand in this challenging business environment;

Continue to aggressively increase our customer base across all of our business segments;

Opportunistically look for acquisitions that can improve our overall service delivery capabilities; and

Continue operating focus and discipline to appropriately manage our cost structure.

**Critical Accounting Estimates and Risks**

Management's discussion and analysis of our financial condition and results of operations is based on our condensed 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, valuation of short and long-term investments, 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, 2009.

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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 total labor cost to date bears to the total expected labor cost (cost to cost method). This method is followed where reasonably dependable estimates of revenues and costs can be made. Management reviews total expected labor 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 condensed consolidated statement of operations. Contract losses for the three months ended March 31, 2010 and 2009, respectively, were immaterial.

*Stock-Based Compensation.* Utilizing the fair value recognition provisions prescribed by the authoritative guidance, 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 over which the stock awards will be outstanding before they are exercised, the expected volatility of our stock, the number of stock-based awards that are expected to be forfeited and the expected exercise proceeds for stock-based awards subject to the Indian fringe benefit tax, if applicable. In addition, for performance stock units, we are required to estimate the most probable outcome of the performance conditions in order to determine the amount of stock compensation costs to be recorded over the vesting period. If actual results differ significantly from our estimates, stock-based compensation expense and our results of operations could be materially impacted.

*Income Taxes.* Determining the consolidated provision for income tax expense, deferred income 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. Changes in the geographic mix or estimated level of annual pre-tax income can also affect the overall effective income tax rate.

Our provision for income taxes also includes the impact of provisions established for uncertain income tax positions, as well as the related net interest. Tax exposures can involve complex issues and may require an extended period to resolve. Although we believe we have adequately reserved for our uncertain tax positions, no assurance can be given that the final tax outcome of these matters will not be different. We adjust these reserves in light of changing facts and circumstances, such as the closing of a tax audit or the refinement of an estimate. To the extent that the final tax outcome of these matters differs from the amounts recorded, such differences will impact the provision for income taxes in the period in which such determination is made.

On an on-going basis, we evaluate whether a valuation allowance is needed to reduce our deferred income 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 income tax assets in the future in excess of the net recorded amount, an adjustment to the deferred income 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 income tax asset in the future, an adjustment to the deferred income tax asset would be charged to income in the period such determination was made.

Our Indian subsidiaries, which are referred to collectively herein as Cognizant India, are export-oriented companies which, under the Indian Income Tax Act of 1961, are entitled to claim tax holidays for a period of ten consecutive years for each Software Technology Park, or 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 STPs in India are currently entitled to a 100% exemption from Indian income tax. The tax holidays for STPs are currently scheduled to expire on March 31, 2011. Thereafter, export profits from our existing STPs will be fully taxable at the Indian statutory rate (33.99% as of March 31, 2010) in effect at such time. If the tax holidays relating to our Indian STPs are not extended or new tax incentives are not introduced that would effectively extend the income tax holiday benefits beyond March 2011, we expect that our effective income tax rate will increase significantly beginning in calendar year 2011. In addition, we expect to continue to locate a portion of our new development centers in areas designated as Special Economic Zones, or SEZs. Development centers operating in SEZs are entitled to certain income tax incentives for periods up to 15 years.

*Investments.* Historically, our investments have been in municipal debt securities with interest rates that reset through a Dutch auction process, corporate notes and bonds, debt issuances by U.S. government agencies, bank time deposits and commercial paper meeting certain criteria. We evaluate our available-for-sale investments periodically for possible other-than-temporary impairment by reviewing factors such as the length of time and extent to which fair value has been below cost basis, the financial condition of the issuer and our ability and intent to hold the

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investment for a period of time, which may be sufficient for anticipated recovery of market value. An impairment charge would be recorded to the extent that the carrying value of our available-for-sale securities exceeds the fair market value of the securities and the decline in value is determined to be other-than-temporary.

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Determining the fair value of our investment in auction-rate securities with unobservable inputs that are supported by little or no market activity requires judgment, including determining the appropriate holding period and discount rate to be used in valuing such securities. We value our investment in auction-rate securities using a discounted cash flow analysis, which incorporates the following key inputs: (i) the underlying structure of each security; (ii) frequency and amounts of cash flows; (iii) expected holding period for the security; and (iv) discount rates that are believed to reflect current market conditions and the relevant risk associated with each security. In estimating the holding period, we considered the current developments in the auction-rate market including: our ability to hold the securities for such period of time, recent calls of auction-rate securities by issuers and the possible reestablishment of an active market for the auction-rate securities that we hold. Based upon these factors, we used a holding period of five years for securities with a stated maturity beyond five years, which represents the period of time we anticipate, will elapse before a liquidity event will occur. An increase or decrease in the holding period by two years would change the fair value of our investment in auction-rate securities by approximately \$7.0 million. We derive the discount rate by considering observable interest rate yields for bonds supported by student loans and pricing of new bond issuances, and adding an illiquidity premium to such rates. The illiquidity premium was estimated by management considering current market conditions. As of March 31, 2010, we used a weighted-average illiquidity premium of 300 basis points. This weighted-average illiquidity premium has been impacted by overall issues within the credit and capital markets and related increases in volatility including uncertainty of the credit and money markets. An increase or decrease to the illiquidity premium of 100 basis points would change the estimated fair value of our investment in auction-rate securities by approximately \$6.0 million. Our valuation is also impacted by changes in market interest rates because the interest payments we receive on our auction-rate securities vary based on a pre-determined formula with spreads tied to particular interest rate indices. An increase or decrease in market interest rates of 25 basis points would change the estimated fair value of our investment in auction-rate securities by approximately \$4.0 million. We anticipate there will be ongoing developments in the credit markets and the market for the auction-rate securities that we hold. Accordingly, our estimates of the expected holding period and illiquidity premium used in valuing such securities are reasonably likely to change in the short-term.

*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 March 31, 2010, our goodwill balance was \$193.9 million.

*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.* The majority of our development and delivery 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, limitations on immigration programs, 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, and 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 ensure the adequacy and effectiveness of our internal control 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.

**Table of Contents****Results of Operations****Three Months Ended March 31, 2010 Compared to Three Months Ended March 31, 2009**

The following table sets forth, for the periods indicated, certain financial data expressed for the three months ended March 31:

(Dollars in thousands)

	2010	% of Revenues	2009	% of Revenues	\$ Change	% Change
Revenues	\$ 959,720	100.0%	\$ 745,862	100.0%	\$ 213,858	28.7%
Cost of revenues <sup>(1)</sup>	555,904	57.9	419,708	56.3	136,196	32.5
Selling, general and administrative expenses <sup>(2)</sup>	194,993	20.3	166,872	22.4	28,121	16.9
Depreciation and amortization expense	25,806	2.7	21,152	2.8	4,654	22.0
Income from operations	183,017	19.1%	138,130	18.5%	44,887	32.5
Other income (expense), net	(4,265)		(2,641)		(1,624)	61.5
Provision for income taxes	27,252		22,357		4,895	21.9
Net income	\$ 151,500	15.8%	\$ 113,132	15.2%	\$ 38,368	33.9

(1) Includes stock-based compensation expense of \$3,667 in 2010 and \$4,261 in 2009, and stock-based Indian fringe benefit tax expense of \$187 in 2009 and is exclusive of depreciation and amortization expense.

(2) Includes stock-based compensation expense of \$10,278 in 2010 and \$7,502 in 2009, and stock-based Indian fringe benefit tax expense of \$758 in 2009 and is exclusive of depreciation and amortization expense.

The following table includes non-GAAP income from operations, excluding stock-based compensation and stock-based Indian fringe benefit tax expense, 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 a targeted operating margin, excluding stock-based compensation expense and applicable stock-based Indian fringe benefit tax expense, of 19% to 20% of revenues. Accordingly, we believe that non-GAAP income from operations, excluding stock-based compensation expense and applicable stock-based Indian fringe benefit tax expense, which was repealed during the third quarter of 2009, retroactive to April 1, 2009, are meaningful measures 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 and applicable stock-based Indian fringe benefit tax expense for financial and operational decision making, to evaluate period-to-period comparisons and for making comparisons of our operating results to those of our competitors. Moreover, because of varying available valuation methodologies and the variety of award types that companies can use to account for stock-based compensation expense, we believe that providing a non-GAAP financial measure that excludes stock-based compensation expense and stock-based Indian fringe benefit tax expense allows investors to make additional comparisons between our operating results and 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 costs, namely, stock-based compensation that is recurring and applicable stock-based Indian fringe benefit tax expense. Stock-based compensation 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 these limitations by providing specific information regarding the GAAP amounts excluded

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from non-GAAP income from operations and evaluating such non-GAAP financial measures 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 and stock-based Indian fringe benefit tax expense, is as follows for the three months ended March 31:

(Dollars in thousands)

	2010	% of Revenues	2009	% of Revenues
Income from operations, as reported	\$ 183,017	19.1%	\$ 138,130	18.5%
Add: stock-based compensation expense	13,945	1.4	11,763	1.6
Add: stock-based Indian fringe benefit tax expense			945	0.1
Non-GAAP income from operations, excluding stock-based compensation expense and stock-based Indian fringe benefit tax expense	\$ 196,962	20.5%	\$ 150,838	20.2%

The fringe benefit tax regulation in India obligated us to pay, upon exercise or distribution of shares under a stock-based compensation award, a non-income related tax on the appreciation of the award from date of grant to date of vest. There was no cash cost to us as we recovered the cost of the Indian fringe benefit tax from the employee's proceeds from the award. Under U.S. GAAP, the stock-based Indian fringe benefit tax expense is required to be recorded as an operating expense and the related recovery of such tax from our employee is required to be recorded to stockholders' equity as proceeds from a stock-based compensation award. During the third quarter of 2009, the Indian government repealed the fringe benefit tax retroactive to April 1, 2009.

*Revenue.* Revenue increased 28.7%, or approximately \$213.8 million, from approximately \$745.9 million during the three months ended March 31, 2009 to approximately \$959.7 million during the three months ended March 31, 2010. This increase was primarily attributed to greater acceptance of the global delivery model among an increasing number of industries, continued interest in using the global delivery model as a means to reduce overall IT costs and greater penetration in the European market. Revenue from customers existing as of March 31, 2009 increased by approximately \$163.1 million and revenue from new customers added since March 31, 2009 was approximately \$50.7 million or approximately 23.7% of the period over period revenue increase and 5.3% of total revenues for the three months ended March 31, 2010. In addition, revenue from our North American and European customers for the three months ended March 31, 2010 increased by \$161.9 million and \$37.6 million, respectively, over the comparable 2009 quarter. We had approximately 597 active clients as of March 31, 2010 as compared to 560 active clients as of March 31, 2009. 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 \$67.3 million and \$63.1 million, respectively, of the approximately \$213.8 million increase in revenue. Additionally, our IT consulting and technology services and IT outsourcing revenues increased by approximately 30.0% and 27.6%, respectively, compared to the three months ended March 31, 2009 and represented approximately 45.1% and 54.9%, respectively, of total revenues for the three months ended March 31, 2010. No customer accounted for sales in excess of 10% of revenues during the three months ended March 31, 2010 and 2009.

*Cost of Revenues (Exclusive of Depreciation and Amortization Expense).* Our cost of revenues consists primarily of the cost of salaries, incentive-based compensation, stock-based compensation expense and related stock-based Indian fringe benefit tax expense, payroll taxes, benefits, immigration and project-related travel for technical personnel, subcontracting and sales commissions related to revenues. Our cost of revenues increased by 32.5%, or approximately \$136.2 million, from approximately \$419.7 million during the three months ended March 31, 2009 to approximately \$555.9 million during the three months ended March 31, 2010. The increase was due primarily to higher compensation and benefits costs of approximately \$118.5 million resulting from the increase in the number of our technical personnel, incentive-based compensation and the appreciation of the Indian rupee versus the U.S. dollar.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses consist primarily of salaries, incentive-based compensation, stock-based compensation expense and the related stock-based Indian fringe benefit tax expense, payroll taxes, employee benefits, travel, promotion, communications, management, finance, administrative and occupancy costs. Selling, general and administrative expenses, including depreciation and amortization, increased by 17.4%, or approximately \$32.8 million, from approximately \$188.0 million during the three months ended March 31, 2009 to approximately \$220.8 million during the three months ended March 31, 2010, and decreased as a percentage of revenue from 25.2% to 23.0%. The decrease as a percentage of revenue was due primarily to economies of scale driven by increased revenues that resulted from our expanded sales and marketing activities in the current and prior years that allowed us to leverage our cost structure over a larger organization, reductions in discretionary spending partially offset by an increase in compensation and benefit costs, including incentive-based compensation and the impact of the appreciation of the Indian rupee versus the U.S. dollar.

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*Income from Operations.* Income from operations increased 32.5%, or approximately \$44.9 million, from approximately \$138.1 million during the three months ended March 31, 2009 to approximately \$183.0 million during the three months ended March 31, 2010, representing operating margins of 19.1% of revenues in 2010 and 18.5% of revenues in 2009. The operating margin increase was primarily due to achieving operating efficiencies partially offset by an increase in compensation costs and benefit costs, including incentive-based compensation costs, the impact of the appreciation of the Indian rupee versus the U.S. dollar and investments to grow our business. Excluding the impact of applicable designated cash flow hedges, the appreciation of the Indian rupee against the U.S. dollar negatively impacted our operating margin by approximately 177 basis points or 1.77 percentage points. Each additional 1.0% change in exchange rate between the Indian rupee and the U.S. dollar will have the effect of moving our operating margin by approximately 24 basis points or 0.24 percentage points. Excluding stock-based compensation expense of \$13.9 million and \$11.8 million for the three months ended March 31, 2010 and March 31, 2009 and stock-based Indian fringe benefit tax expense of \$0.9 million for the three months ended March 31, 2009, operating margin for the three months ended March 31, 2010 and March 31, 2009 was 20.5% and 20.2% of revenues, respectively.

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We entered into foreign exchange forward contracts to hedge certain salary payments in India. These hedges are intended to mitigate the volatility of the changes in the exchange rate between the U.S. dollar and the Indian rupee. During the three months ended March 31, 2010, the settlement of certain cash flow hedges favorably impacted our operating margin by approximately 98 basis points or 0.98 percentage points. During the three months ended March 31, 2009, the settlement of certain cash flow hedges negatively impacted our operating margin by approximately 17 basis points or 0.17 percentage points.

*Other Income (Expense), Net.* Other income (expense), net consists primarily of foreign currency exchange gains and (losses) and interest income. The following table sets forth, Other income (expense), net for the three months ended March 31:

(Dollars in thousands)

	2010	2009	\$ Change
Foreign currency exchange gains (losses)	\$ 5,635	\$ (5,000)	\$ 10,635
Gains (losses) on foreign exchange forward contracts not designated as hedging instruments	(16,095)		(16,095)
Net foreign currency exchange gains (losses)	(10,460)	(5,000)	(5,460)
Interest income	6,054	2,470	3,584
Other income (expense), net	141	(111)	252
Total other income (expense), net	\$ (4,265)	\$ (2,641)	\$ (1,624)

The foreign currency exchange gains of approximately \$5.6 million were primarily attributed to (i) U.S. dollar denominated intercompany payables from our European subsidiaries to Cognizant India for services performed by Cognizant India on behalf of our European customers and (ii) the remeasurement of the Indian rupee net monetary assets on Cognizant India's books to the U.S. dollar functional currency. The \$16.1 million of losses on foreign exchange forward contracts were related to the change in fair value of foreign exchange forward contracts entered into to offset foreign currency exposure to Indian rupee denominated net monetary assets. As of March 31, 2010, the notional value of these undesignated hedges was \$400.0 million. The increase in interest income of \$3.6 million was primarily attributed to higher invested balances, including an increase in short-term investments.

*Provision for Income Taxes.* The provision for income taxes increased from approximately \$22.4 million during the three months ended March 31, 2009 to approximately \$27.3 million during the three months ended March 31, 2010. The effective income tax rate decreased from 16.5% for the three months ended March 31, 2009 to 15.2% for the three months ended March 31, 2010. The decrease in our effective rate was primarily attributed to a shift in the geographic mix of our income, which resulted in a greater percentage of our revenues falling under income tax holidays, the tax impact of our foreign forward exchange contracts and the favorable net impact of discrete items recorded in the 2010 period.

*Net Income.* Net income increased from approximately \$113.1 million for the three months ended March 31, 2009 to approximately \$151.5 million for the three months ended March 31, 2010, representing 15.2% and 15.8% of revenues, respectively. The increase in net income as a percentage of revenues was primarily attributed to a higher operating margin and a lower effective tax rate in the 2010 period.

**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 segment includes entertainment, media and information services, communications 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.

Our 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

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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

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well as a per seat charge for use of the development and delivery 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 and the related stock-based India fringe benefit tax are 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 are adjusted only against the total income from operations.

As of March 31, 2010, we had 597 active customers. Accordingly, we provide a significant volume of services to many customers in each of our business segments. Therefore, a loss of a significant customer or a few significant customers in a particular segment could materially reduce revenues for such segment. However, no individual customer exceeded 10% of our consolidated revenues for the three months ended March 31, 2010 and 2009, respectively. In addition, the services we provide to our larger customers are often critical to the operations of such customers and a termination of our services would require an extended transition period with gradual declining revenues.

**Three Months Ended March 31, 2010 Compared to Three Months Ended March 31, 2009**

Revenues from external customers and segment operating profit, before unallocated expenses, for the Financial Services, Healthcare, Manufacturing/Retail/Logistics and Other segments for the three months ended March 31, 2010 and 2009 are as follows:

(Dollars in thousands)

	March 31, 2010	March 31, 2009	\$ Change	% Change
<b>Revenues:</b>				
Financial Services	\$ 398,687	\$ 331,342	\$ 67,345	20.3%
Healthcare	252,425	189,326	63,099	33.3
Manufacturing/Retail/Logistics	173,131	123,090	50,041	40.7
Other	135,477	102,104	33,373	32.7
Total revenues	\$ 959,720	\$ 745,862	\$ 213,858	28.7%
<b>Segment Operating Profit:</b>				
Financial Services	\$ 128,264	\$ 113,386	\$ 14,878	13.1%
Healthcare	92,357	69,548	22,809	32.8
Manufacturing/Retail/Logistics	54,812	36,332	18,480	50.9
Other	43,186	32,800	10,386	31.7
Total segment operating profit	\$ 318,619	\$ 252,066	\$ 66,553	26.4%

**Financial Services Segment**

**Revenue.** Revenue increased by 20.3%, or approximately \$67.4 million, from approximately \$331.3 million during the three months ended March 31, 2009 to approximately \$398.7 million during the three months ended March 31, 2010. The increase in revenue was primarily driven by continued expansion of existing customer relationships as well as revenue contributed by new customers. The increase in revenue from customers existing as of March 31, 2009 and customers added since such date was approximately \$63.2 million and approximately \$4.2 million, respectively. Within the segment, quarterly revenue from our banking and insurance customers increased approximately \$51.0 million and \$16.4 million, respectively over the first quarter of last year. Overall, the year-over-year increase can also be attributed to leveraging sales and marketing investments in this business segment as well as greater acceptance of our global delivery model. However, revenue from our financial services segment grew slower than the rest of the company primarily due to the crisis in the financial services sector during 2009. We believe this trend, to a lesser extent, may continue during 2010.

**Segment Operating Profit.** Segment operating profit increased 13.1%, or approximately \$14.9 million, from approximately \$113.4 million during the three months ended March 31, 2009 to approximately \$128.3 million during the three months ended March 31, 2010. 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, an increase in compensation and benefit costs, including incentive based compensation, and the

impact of the appreciation of the Indian rupee versus the U.S. dollar.

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### **Healthcare Segment**

*Revenue.* Revenue increased by 33.3%, or approximately \$63.1 million, from approximately \$189.3 million during the three months ended March 31, 2009 to approximately \$252.4 million during the three months ended March 31, 2010. The increase in revenue was primarily driven by continued expansion of existing customer relationships as well as revenue contributed by new customers. The increase in revenue from customers existing as of March 31, 2009 and customers added since such date was approximately \$53.3 million and approximately \$9.8 million, respectively. Within the segment, growth was particularly strong among our healthcare customers, where revenue increased by approximately \$41.5 million over the first 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 our global delivery model.

*Segment Operating Profit.* Segment operating profit increased 32.8%, or approximately \$22.8 million, from approximately \$69.5 million during the three months ended March 31, 2009 to approximately \$92.3 million during the three months ended March 31, 2010. The increase in segment operating profit was attributable primarily to increased revenues during the quarter.

### **Manufacturing/Retail/Logistics Segment**

*Revenue.* Revenue increased by 40.7%, or approximately \$50.0 million, from approximately \$123.1 million during the three months ended March 31, 2009 to approximately \$173.1 million during the three months ended March 31, 2010. The increase in revenue was driven by continued expansion of existing customer relationships as well as revenue contributed by new customers. The increase in revenue from customers existing as of March 31, 2009 and customers added since such date was approximately \$33.8 million and approximately \$16.2 million, respectively. The increase can also be attributed to leveraging sales and marketing investments in this business segment as well as greater acceptance of our global delivery model.

*Segment Operating Profit.* Segment operating profit increased 50.9%, or approximately \$18.5 million, from approximately \$36.3 million during the three months ended March 31, 2009 to approximately \$54.8 million during the three months ended March 31, 2010. The increase in segment operating profit was attributable primarily to increased revenues and achieving operational efficiencies including continued leverage of prior sales and marketing investments.

### **Other Segment**

*Revenue.* Revenue increased 32.7%, or approximately \$33.4 million, from approximately \$102.1 million during the three months ended March 31, 2009 to approximately \$135.5 million during the three months ended March 31, 2010. The increase in revenue was driven by continued expansion of existing customer relationships as well as revenue contributed by new customers. The increase in revenue from customers existing as of March 31, 2009 and customers added since such date was approximately \$12.9 million and approximately \$20.5 million, respectively. Within the Other segment, growth was particularly strong among our entertainment, media and information services customers and our telecommunications customers where revenue increased by approximately \$14.4 million and \$13.7 million, respectively, over the first 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 our global delivery model.

*Segment Operating Profit.* Segment operating profit decreased 31.7%, or approximately \$10.4 million, from approximately \$32.8 million during the three months ended March 31, 2009 to approximately \$43.2 million during the three months ended March 31, 2010. 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, an increase in compensation and benefit costs, including incentive based compensation, and the impact of the appreciation of the Indian rupee versus the U.S. dollar.

## **Liquidity and Capital Resources**

At March 31, 2010, we had cash and cash equivalents and short-term investments of \$1,433.9 million. We have used, and plan to use, our cash for: (i) expansion of existing operations, including our offshore development and delivery centers; (ii) continued development of new service lines; (iii) possible acquisitions of related businesses; (iv) formation of joint ventures; (v) stock repurchases and (vi) general corporate purposes, including working capital. As of March 31, 2010, we had working capital of approximately \$1,891.1 million. Accordingly, we do not anticipate any near-term liquidity issues.

Net cash provided by operating activities was approximately \$2.3 million during the three months ended March 31, 2010 as compared to approximately \$75.1 million during the three months ended March 31, 2009. The decrease was primarily attributed to an increase in working capital required to support our revenue growth which was primarily impacted by the increase in trade accounts receivable and incentive-based

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compensation payments made during the three months ended March 31, 2010 offset by an increase in net income during the quarter. Trade accounts receivable increased from approximately \$626.3 million at December 31, 2009 to approximately \$706.1 million at March 31, 2010. Unbilled accounts receivable increased from approximately \$83.0 million at December 31, 2009 to approximately \$106.2 million at March 31, 2010. The increase in trade accounts receivable and unbilled receivables as of March 31, 2010 as compared to December 31, 2009 was primarily due 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 March 31, 2010, our days of sales outstanding, including unbilled receivables, were approximately 76.2 days as compared to 72.3 days at December 31, 2009 and 72.5 days as of March 31, 2009.



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Our investing activities used net cash of approximately \$57.1 million during the three months ended March 31, 2010 as compared to approximately \$43.5 million during the three months ended March 31, 2009. The decrease in net cash from investing activities primarily related to an increase in net investments and capital expenditure spending offset by decreased payments for acquisitions.

Our financing activities provided net cash of approximately \$43.5 million during the three months ended March 31, 2010 as compared to using approximately \$2.3 million during the three months ended March 31, 2009. The increase in net cash from financing activities primarily related to additional proceeds and excess tax benefits from issuances under our stock-based compensation plans and lower common stock repurchases.

As of March 31, 2010, our short-term and long-term investments totaled \$490.4 million and included \$119.1 million in long-term of AAA/A3-rated auction-rate municipal debt securities that are collateralized by debt obligations supported by student loans, substantially backed by the FFELP. In addition, the remainder of our long-term investments included \$18.4 million of an auction-rate securities related UBS Right discussed below. Since February 14, 2008, auctions failed for all the auction-rate securities still in our portfolio as of March 31, 2010. We believe that the failed auctions experienced to date are not a result of the deterioration of the underlying credit quality of the securities and we continue to earn and receive interest on the auction-rate municipal debt securities at a pre-determined formula with spreads tied to particular interest rate indices. All of the auction-rate municipal debt securities held by us are callable by the issuer at par value.

In November 2008, we accepted an offer from UBS AG, or UBS, to sell to UBS, at par value, our auction-rate securities at any time during an exercise period from June 30, 2010 to July 2, 2012, which we refer to as the UBS Right. In accepting the UBS Right, we granted UBS the authority to purchase these auction-rate securities or sell them on our behalf at par value any time through July 2, 2012. The offer is non-transferable. During the first quarter of 2010, approximately \$13.7 million of the auction-rate securities were redeemed at par value. At March 31, 2010, the par value of the auction-rate securities held by us was \$137.6 million. We anticipate that any future changes in fair value of the UBS Right will be offset by the changes in the fair values of the auction-rate securities with no material impact to our condensed consolidated financial statements.

Based on our expected operating cash flows, and our other sources of cash, we do not anticipate the potential lack of liquidity on these investments will affect our ability to execute current and planned operations and needs for at least the next 12 months. If a liquidity event does not occur prior to the exercise period under the UBS Right, we expect to obtain liquidity through the UBS Right. If UBS is unable to honor its obligations under the UBS Right, we believe we will be able to ultimately recover our investment in auction-rate municipal debt securities due to: (i) the strength of the underlying collateral substantially backed by FFELP, and (ii) the AAA/A3 credit rating of the securities held by us. However, it could take until the final maturity of the underlying security (up to 31 years) to realize our investments' recorded value.

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 a 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, 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. We expect our operating cash flow and cash and cash equivalents to be sufficient to meet our operating requirements for the next twelve months.

## **Commitments and Contingencies**

As of March 31, 2010, we had outstanding fixed capital commitments of approximately \$21.3 million related to our India development center expansion program which includes expenditures for land acquisition, facilities construction and furnishings to build new state-of-the-art development and delivery centers in regions primarily designated as SEZs located in India.

In connection with a 2008 acquisition, additional purchase price not to exceed \$14.0 million, payable in 2010, is contingent on the acquired company achieving certain financial and operating targets during an earn-out period. We expect to fund such payment, if any, from operating cash flow. The ultimate amount payable cannot be predicted with reasonable certainty because the amount is dependent on future results of operations of the acquired business. In accordance with U.S. GAAP, we have not recorded a liability for this item on our balance sheet because the definitive amount is not determinable or distributable. The contingent consideration, if paid, will be recorded as an additional element of the cost of the acquired company.

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 systems or our failure to meet our contractual obligations to our clients, including any breach involving a customer's confidential information or sensitive data, or our obligations under

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applicable laws or regulations 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

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arising from negligent acts, errors, mistakes, or omissions in rendering our 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 available in sufficient amounts 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.

**Foreign Currency Risk**

Overall, we believe that we have limited revenue risk resulting from movement in foreign currency exchange rates as approximately 78.7% of our revenues for the quarter ended March 31, 2010 are generated from customers located in North America. However, a portion of our costs in India, representing approximately 28.8% of our global operating costs for the quarter ended March 31, 2010, are denominated in the Indian rupee and are subject to foreign exchange rate fluctuations. These foreign exchange rate fluctuations have an impact on our results of operations. In addition, a portion of our balance sheet is exposed to foreign exchange rate fluctuations, which may result in non-operating foreign currency gains or losses upon remeasurement. For the quarter ended March 31, 2010, we reported foreign currency exchange gains (losses), exclusive of hedging gains or losses, of approximately \$5.6 million, which are primarily attributed to the remeasurement of (i) U.S. dollar denominated intercompany payables from our European subsidiaries to Cognizant India for services performed by Cognizant India on behalf of our European customers and (ii) Indian rupee net monetary assets on Cognizant India's books to the U.S. dollar functional currency. 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 subsidiaries.

We entered into a series of foreign exchange forward contracts that are designated as cash flow hedges of certain salary payments in India. Cognizant India converts U.S. dollar receipts from intercompany billings to Indian rupees to fund local expenses, including salaries. These U.S. dollar / Indian rupee hedges to buy Indian rupees and sell U.S. dollars are intended to partially offset the impact of movement of exchange rates on future operating costs. During the first quarter of 2010, we reported income of \$9.4 million on contracts that settled during the quarter. As of March 31, 2010, we have outstanding contracts with a notional value of \$420.0 million and weighted average forward rate of 48.9 rupees to the U.S. dollar scheduled to mature in 2010, outstanding contracts with a notional value of \$480.0 million and weighted average forward rate of 48.3 rupees to the U.S. dollar scheduled to mature in 2011 and outstanding contracts with a notional value of \$300.0 million and weighted average forward rate of 48.8 rupees to the U.S. dollar scheduled to mature in 2012.

We also use foreign currency forward contracts to hedge balance sheet exposure to our Indian rupee denominated net monetary assets. These contracts are not designated as hedges and are intended to offset the foreign currency exchange rate gains or losses upon the remeasurement of the underlying Indian rupee denominated net monetary assets. During 2009, we entered into a series of foreign exchange forward contracts, scheduled to mature in 2010, to buy U.S. dollars and sell Indian rupees. At March 31, 2010, the notional value of the outstanding contracts was \$400.0 million and the related fair value was a liability of \$36.9 million. During the three months ended March 31, 2010, inclusive of losses of \$16.1 million on these undesignated balance sheet hedges, we reported net foreign currency exchange losses of approximately \$10.5 million.

There were no off-balance sheet transactions, arrangements or other relationships with unconsolidated entities or other persons in 2010 and 2009 that would have affected our liquidity or the availability of or requirements for capital resources.

**Recent Accounting Pronouncements**

See Note 10 to our condensed consolidated financial statements for additional information.

**Effects of Inflation**

Our most significant costs are the salaries and related benefits for our 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 often increase at a rate greater than the general rate of inflation. As with other service providers in our industry, 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. Historically, we have experienced increases in compensation and benefit costs, including incentive-based compensation, in India; however, this has not had a material impact on our results of operations as Indian wages were approximately 22% of our total operating expenses for the three months ended March 31, 2010.



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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, could, would, plan, intend, estimate, predict, potential, continue, should or anticipates or the negative thereof or other variations thereon or comparable terminology, 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 or operating margins, contract percentage completions, earnings, 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. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as may be required under applicable securities laws. 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 Part II, 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 exchange rate fluctuations and expect to continue to use such instruments in the future to reduce foreign currency exposure to appreciation or depreciation in the value of certain foreign currencies. All hedging transactions are authorized and executed pursuant to regularly reviewed policies and procedures.

We have entered into a series of foreign exchange forward contracts that are designated as cash flow hedges of certain salary payments in India. Cognizant India converts U.S. dollar receipts from intercompany billings to Indian rupees to fund local expenses, including salaries. These U.S. dollar / Indian rupee hedges are intended to partially offset the impact of movement of exchange rates on future operating costs. As of March 31, 2010 and December 31, 2009, the notional value of these contracts was \$1,200.0 million and \$810.0 million, respectively. The outstanding contracts at March 31, 2010 are scheduled to mature each month during 2010, 2011 and 2012. At March 31, 2010 and December 31, 2009, the net unrealized gain on our outstanding foreign exchange forward contracts was \$51.6 million and \$19.0 million, respectively. Based upon a sensitivity analysis of our foreign exchange forward contracts at March 31, 2010, which estimates the fair value of the contracts based upon market exchange rate fluctuations, a 10.0% change in the foreign currency exchange rate against the U.S. dollar with all other variables held constant would have resulted in a change in the fair value of approximately \$120.0 million.

We also use foreign exchange forward contracts to hedge balance sheet exposure to our Indian rupee denominated net monetary assets. These contracts are not designated as hedges and are intended to offset the foreign currency exchange rate gains or losses upon the remeasurement of the underlying Indian rupee denominated net monetary assets. We entered into a series of foreign exchange forward contracts, scheduled to mature in 2010, to buy U.S. dollars and sell Indian rupees. At March 31, 2010, the notional value of the outstanding contracts was \$400.0 million and the related fair value was a liability of \$36.9 million. Based upon a sensitivity analysis of our foreign exchange forward contracts at March 31, 2010, which estimates the fair value of the contracts based upon market exchange rate fluctuations, a 10.0% change in the foreign currency exchange rate against the U.S. dollar with all other variables held constant would have resulted in a change in the fair value of approximately \$44.0 million.

There were no off-balance sheet transactions, arrangements or other relationships with unconsolidated entities or other persons in 2010 and 2009 that would have affected our 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 and long-term investments. As of March 31, 2010, we had approximately \$1,571.3 million of cash and cash equivalents and short-term and long-term investments most of which are impacted almost immediately by changes in short-term interest rates. We limit our credit risk by investing primarily in AAA/Aaa/A3 or A1/P1 rated securities as rated by Standard & Poor's, Moody's and Fitch rating services and restricting amounts that can be invested with any single issuer.

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As of March 31, 2010, our short-term and long-term investments totaled \$490.4 million and included \$119.1 million in long-term of AAA/A3-rated auction-rate municipal debt securities that are collateralized by debt obligations supported by student loans, substantially backed by the FFELP. In addition, the remainder of our long-term investments included \$18.4 million of an auction-rate related UBS Right discussed below. Since February 14, 2008, auctions failed for all the auction-rate securities still in our portfolio as of March 31, 2010. We believe that the failed auctions experienced to date are not a result of the deterioration of the underlying credit

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quality of the securities and we continue to earn and receive interest on the auction-rate municipal debt securities at a pre-determined formula with spreads tied to particular interest rate indices. All of the auction-rate municipal debt securities held by us are callable by the issuer at par value.

In November 2008, we accepted an offer from UBS to sell to UBS, at par value, our auction-rate securities at any time during an exercise period from June 30, 2010 to July 2, 2012, which we refer to as the UBS Right. In accepting the UBS Right, we granted UBS the authority to purchase these auction-rate securities or sell them on our behalf at par value any time after the execution of the UBS Right through July 2, 2012. The offer is non-transferable. At March 31, 2010, we determined the fair value of the UBS Right to be \$18.4 million. During the first quarter of 2010, approximately \$13.7 million of auction rate securities were redeemed at par value. We anticipate that any future changes in fair value of the UBS Right will be offset by the changes in the fair value of the auction-rate securities with no material impact to the consolidated financial statements.

### **Item 4. Controls and Procedures.**

#### **Evaluation of Disclosure Controls and Procedures**

Our management under the supervision and with the participation of our chief executive officer and our chief financial officer, evaluated the design and operating effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act) as of March 31, 2010. Based on this evaluation, our chief executive officer and our chief financial officer concluded that, as of March 31, 2010, our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in our reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to our chief executive officer and our chief financial officer as appropriate to allow timely decisions regarding required disclosure.

#### **Changes in Internal Control over Financial Reporting**

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 March 31, 2010 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.**

#### **Factors That May Affect Future Results**

*In addition to the risks and uncertainties described 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.*

#### **Our global operations are subject to complex risks, some of which might be beyond our control.**

We have offices and operations in various countries around the world and provide services to clients globally. During the first quarter of 2010, approximately 78.7% of our revenues were attributable to the North American region, 18.1% were attributable to the European region, and 3.2% were attributable to the rest of the world, primarily the Asia Pacific region. If we are unable to manage the risks of our global operations, including regulatory, economic, political and other uncertainties in India, fluctuations in foreign exchange and inflation rates, international hostilities, terrorism, natural disasters, and multiple legal and regulatory systems, our results of operations could be adversely affected.

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

We intend to continue to develop and expand our offshore facilities in India where a majority of our technical professionals are located. While wage costs are lower in India than in the United States and other developed countries for comparably skilled professionals, wages in India have

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historically increased at a faster rate than in the United States. If this were to continue in the future, it would result in increased costs for our skilled professionals and thereby potentially reduce our operating margins. Also, there is no assurance that in future periods competition for skilled professionals will not drive higher salaries in India thereby resulting in increased costs for our technical professionals and reduced operating margins.

India has also recently 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



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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, 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 (which was repealed as of April 1, 2009) and new service taxes, and income-related taxes, including the Minimum Alternative Tax. In addition, a change in government leadership in India or change in policies of the existing government in India that results in 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.

In addition, the emergence of a widespread health emergency or pandemic could create economic or financial disruption that could negatively affect our revenue and operations or impair our ability to manage our business in certain parts of the world.

### **Our international sales and operations are subject to many uncertainties.**

Revenues from customers outside North America represented approximately 21.3% of our revenues for the quarter ended March 31, 2010. 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, the Asia Pacific and Latin America regions. In addition, the majority of our employees and our development and delivery 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, which may cause volatility in our reported income, 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. The use of hedging contracts is intended to mitigate or reduce transactional level volatility in the results of our foreign operations, but does not completely eliminate volatility and risk. In addition, use of hedging contracts includes the risk of non-performance by the counterparty. 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, other income (expense), net and the value of balance sheet items originally denominated in other currencies. During the quarter ended March 31, 2010, the appreciation of the Indian rupee versus the U.S. dollar negatively impacted our operating margins by 177 basis points or 1.77 percentage points as compared to the same period in 2009. Additionally, during the quarter ended March 31, 2010, we recorded net foreign currency losses of \$10.5 million, inclusive of losses of \$16.1 million on undesignated balance sheet hedges. There is no guarantee that our financial results will not be adversely affected by currency exchange rate fluctuations or that any efforts by us to engage in currency hedging activities will 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 offshore sites by increasing labor and other costs that are denominated in local currency.



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### **Our operating results may be adversely affected by our use of derivative financial instruments.**

We have entered into a series of foreign exchange forward contracts that are designated as cash flow hedges of certain salary payments in India. These contracts are intended to partially offset the impact of the movement of the exchange rates on future operating costs. In addition, we also entered into foreign exchange forward contracts in order to mitigate foreign currency risk on Indian rupee denominated net monetary assets. The hedging strategies that we have implemented or may implement to mitigate foreign currency exchange rate risks may not reduce or completely offset our exposure to foreign exchange rate fluctuations and may expose our business to unexpected market, operational and counterparty credit risks. Accordingly, we may incur losses from our use of derivative financial instruments that could have a material adverse effect on our business, results of operations and financial condition.

### **Our global operations expose us to numerous and sometimes conflicting legal and regulatory requirements, and violations 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 laws or 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 laws or 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 of which we operate, local laws might be insufficient to protect our rights. Our failure to comply with applicable legal and regulatory requirements could have a material adverse effect on our business, results of operations and financial condition.

In many parts of the world, including countries in which we operate, practices in the local business community might not conform to international business standards and could violate anticorruption laws or regulations, including the U.S. Foreign Corrupt Practices Act. Although we have policies and procedures in place that are designed to promote legal and regulatory compliance, our employees, subcontractors and agents could take actions that violate these policies or procedures or applicable anticorruption laws or regulations. Violations of these laws or regulations could subject us to criminal or civil enforcement actions, including fines and suspension or disqualification from government contracting, any of which could have a material adverse effect on our business.

### **International hostilities, terrorist activities, other violence or war, natural disasters, pandemics and infrastructure disruptions, could delay or reduce the number of new service orders we receive and impair our ability to service our customers, thereby adversely affecting our business, financial condition and results of operations.**

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, the attacks of November 26, 2008 in Mumbai, India, and the continuing conflict in Iraq and Afghanistan, natural disasters, global health risks or pandemics or the threat or perceived potential for these events could materially adversely affect our operations and our ability to service our customers. Such events could cause customers to delay their decisions on spending for information technology, consulting, and business and knowledge process outsourcing services and give rise to sudden significant changes in regional and global economic conditions and cycles. These events also pose significant risks to our people and to physical facilities and operations around the world, whether the facilities are ours or those of our clients, which could affect our financial results. By disrupting communications and travel, giving rise to travel restrictions, and increasing the difficulty of obtaining and retaining highly skilled and qualified personnel, these events could make it difficult or impossible for us to deliver services to our clients. The majority of our technical professionals are 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 addition, any extended disruptions of electricity, other public utilities or network services at our facilities, as well as system failures at, or security breaches in, our facilities or systems, could also adversely affect our ability to serve our clients.

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, hostilities involving the United States, the United Kingdom, India and other countries in which we provide services to our clients, and other acts of terrorism, violence or war, natural disasters, global health risks or pandemics may reduce the demand for our services and negatively affect our revenues and profitability. While we plan and prepare to defend against each of these occurrences, we might be unable to protect our people, facilities and systems against all such occurrences. If these disruptions prevent us from effectively serving our clients, our operating results could be adversely affected.



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### **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 companies outsourcing services to organizations operating in other countries is a topic of political discussion in many countries, including the United States, which is our largest market. For example, measures aimed at limiting or restricting outsourcing by United States companies are periodically considered in Congress and in numerous state legislatures to address concerns over the perceived association between offshore outsourcing and the loss of jobs in the United States. Senators Richard Durbin (D-Illinois) and Charles Grassley (R-Iowa) have introduced a bill which would, if enacted, severely restrict the use of certain temporary business visas. Given the ongoing debate over this issue, the introduction and consideration of other restrictive legislation is possible. If enacted, such measures may: (1) broaden restrictions on outsourcing by federal and state government agencies and on government contracts with firms that outsource services directly or indirectly, (2) impact private industry with measures such as tax disincentives or intellectual property transfer restrictions, and/or (3) restrict the use of certain business visas. In the event that any of these measures become law, our business, results of operations and financial condition could be adversely affected and our ability to service our customers could be impaired.

In addition, from time to time, there has been publicity about negative experiences associated with offshore outsourcing, such as theft and misappropriation of sensitive client data, particularly involving service providers in India. Current or prospective clients may elect to perform certain services themselves or may be discouraged from transferring services from onshore to offshore providers to avoid negative perceptions that may be associated with using an offshore provider. Any slowdown or reversal of existing industry trends toward offshore outsourcing would seriously harm our ability to compete effectively with competitors that provide services from within the country in which our clients operate.

Legislation and administrative/regulatory policies enacted in certain European jurisdictions and any future legislation/regulation in Europe, countries within the Asia Pacific region or any other country in which we have clients restricting the performance of business process services from an offshore location could also have a material adverse effect on our business, results of operations and financial condition. For example, new legislation recently enacted in the United Kingdom, based on the 1977 EC Acquired Rights Directive, has been adopted in some form by many European Union, or EU, countries, and provides that if a company outsources all or part of its business to a service provider or changes its current service provider, the affected employees of the company or of the previous service provider are entitled to become employees of the new service provider, generally on the same terms and conditions as their original employment. In addition, dismissals of employees who were employed by the company or the previous service provider immediately prior to that transfer are automatically considered unfair dismissals that entitle such employees to compensation. As a result, in order to avoid unfair dismissal claims we may have to offer, and become liable for, voluntary redundancy payments to the employees of our clients who outsource business to us in the United Kingdom and other EU countries who have adopted similar laws. This legislation may materially affect our ability to obtain new business from companies in the United Kingdom and EU and to provide outsourced services to companies in the United Kingdom and EU in a cost-effective manner.

### **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 professionals in the United States and in Europe are Indian nationals. The ability of Indian nationals to work in the United States and Europe 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 four-year bachelor 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. Under certain limited circumstances, H-1B visa extensions after the six-year period may be available. There is a limit on the number of new H-1B petitions that the 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. Currently, the limit is 65,000 for holders of United States or United States-equivalent bachelor degrees (the general cap), and an additional 20,000 for holders of advanced degrees from United States post-secondary educational institutions. Although CIS has reached its general cap and advanced degree cap for fiscal year 2010, we are able to file H-1B petitions with CIS against the fiscal year 2011 caps beginning April 1, 2010 for work in H-1B status beginning on October 1, 2011. As 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. Larger 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 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 from India to the United States to work on projects, 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

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United States 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

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pre-approved by CIS, thus enabling individual L-1 visa applications to be presented directly to a visa-issuing United States consular post abroad rather than undergoing a pre-approval process through CIS in the United States. In recent years, both the United States consular posts that review initial L-1 applications and CIS, which adjudicates petitions for initial grants and extensions of L-1 status, have become increasingly restrictive with respect to this category. As a result, the rate of refusals of initial L-1 petitions and extensions has increased. In addition, even where L-1 visas are ultimately granted and issued, security measures undertaken by United States 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 fiscal year 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 this 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 visa 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 workers 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 this law, we consistently have established this fact to CIS's satisfaction. However, if CIS and/or the United States Department of State, through its visa-issuing 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 statutory 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.

We also process immigrant visas for lawful permanent residence in the United States for employees to fill positions for which there are an insufficient number of able, willing, and qualified United States workers available to fill the positions. Compliance with existing United States 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 employees to work in the United Kingdom, where we have experienced significant growth. The United Kingdom currently requires that all employees who are not nationals of European Union countries (plus nationals of Bulgaria and Romania) or EEA nationals, obtain work permission before obtaining a visa/entry clearance to travel to the United Kingdom. New European nations such as Hungary, Poland, Lithuania, Slovakia, and the Czech Republic do not have a work permit requirement but employees need to register to work within 30 days of arrival. On November 27, 2008, the United Kingdom introduced a points-based system under which certain certificates of sponsorship are issued by licensed employer sponsors, provided the employees they seek to employ in the United Kingdom can accumulate a certain number of points based on certain attributes. Where the employee has not worked for a Cognizant group company outside the United Kingdom for at least 6 months, we will need to carry out a resident labor market test to confirm that the intended role cannot be filled by an EEA national. We are currently an A-rated sponsor and were allocated certificates of sponsorship which we believe are sufficient to meet our demand for transfers to the United Kingdom.

Immigration and work permit laws and regulations in the United States, the United Kingdom, the EU, Switzerland 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 regulations 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 professionals who are not citizens of the country where the work is to be performed.

**Our revenues are highly dependent on clients primarily located in the United States and Europe, as well as on clients concentrated in certain industries, including the financial services industry. Continuing or worsening economic conditions or factors that negatively affect the economic health of the United States, Europe or these industries may adversely affect our business.**





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Approximately 78.7% of our revenues during the quarter ended March 31, 2010 were derived from customers located in North America. In the same period, approximately 18.1% of our revenues were derived from customers located in Europe. If the United States or European economy continues to weaken or slow and conditions in the financial markets continue to deteriorate, pricing for our services may be depressed and our customers may reduce or postpone their technology spending significantly, which may in turn lower the demand for our services and negatively affect our revenues and profitability. Additionally, any prolonged recession in the United States and Europe could have an adverse impact on our revenues because a large portion of our revenues are derived from the United States and Europe. In addition, during the quarter ended March 31, 2010, we earned approximately 41.5% of our revenues from the financial services industry, which includes insurance. A continuation of the current crisis in the financial services industry and significant consolidation in that industry, or a decrease in growth or consolidation in other industry segments on which we focus, may reduce the demand for our services and negatively affect our revenues and profitability. In addition, if we are unable to successfully anticipate changing economic and political conditions affecting the industries and markets in which we operate, we may be unable to effectively plan for or respond to those changes, and our business could be negatively affected.

### **We face intense competition from other service providers.**

The intensely competitive information technology, consulting and business process outsourcing professional services markets include a large number of participants and is subject to rapid change. These markets include participants from a variety of market segments, including:

systems integration firms;

contract programming companies;

application software companies;

internet solutions providers;

large or traditional consulting companies;

professional services groups of computer equipment companies; and

infrastructure management and outsourcing companies.

These markets also include numerous smaller local competitors in the various geographic markets in which we operate which may be able to provide services and solutions at lower costs or on terms more attractive to clients than we can. 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 and, therefore, may be better able to compete for new work and skilled professionals. Some of these larger competitors, such as Accenture, Electronic Data Systems (acquired by Hewlett-Packard Company), Perot Systems (acquired by Dell Inc.) and IBM Global Services, have offshore operations. There is a risk that increased competition could put downward pressure on the prices we can charge for our services and on our operating margins. Similarly, if our competitors develop and implement methodologies that yield greater efficiency and productivity, they may be able to offer services similar to ours at lower prices without adversely affecting their profit margins. Even if our offerings address industry and client needs, our competitors may be more successful at selling their services. If we are unable to provide our clients with superior services and solutions at competitive prices, our results of operations may suffer. Further, a client may choose to use its own internal resources rather than engage an outside firm to perform the types of services we provide. 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 technology professionals and pricing pressure from competitors employing a global delivery business model, increase.

In addition, we may face competition from companies that increase in size or scope as the result of strategic mergers or acquisitions. These transactions may include consolidation activity among hardware manufacturers, software companies and vendors, and service providers. The result of any such vertical integration may be greater integration of products and services that were once offered separately by independent vendors. Our access to such products and services may be reduced as a result of this industry trend, which could adversely affect our competitive position.

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

For the quarter ended March 31, 2010, we reported an operating margin of 19.1%. Our operating margin may decline if we experience declines in demand and pricing for our services, imposition of new non-income related taxes or due to adverse fluctuations in foreign currency exchange rates. In addition, historically, wages in India increased at a faster rate than in the United States. Additionally, the number and type of equity-based compensation awards and the assumptions used in valuing equity-based compensation awards may change resulting in increased stock-based compensation expense and lower margins. Although we have historically been able to partially offset wage increases and foreign currency fluctuations through further leveraging the scale of our operating structure, obtaining price increases, and issuing a lower number of stock options and other equity-based compensation awards in proportion to our overall headcount, we cannot assure you that we will be able to continue to do so in the future.

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### **Our profitability could suffer if we are not able to control our costs.**

Our ability to control our costs and improve our efficiency affects our profitability. If we are unable to control our costs or improve our efficiency, our profitability could be negatively affected.

### **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 information technology, consulting and outsourcing 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 markets in which we provide services. We cannot assure you that we will be successful in developing new 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 that both leverage their legacy systems and appropriately utilize newer technologies such as Web 2.0 models, software-as-a-service, and service oriented 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 and knowledge 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 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.

### **If our clients are not satisfied with our services, our business could be adversely affected.**

Our business model depends in large part on our ability to attract additional work from our base of existing clients. Our business model also depends on relationships our account teams develop with our clients so that we can understand our clients' needs and deliver solutions and services that are tailored to those needs. If a client is not satisfied with the quality of work performed by us, or with the type of services or solutions delivered, then we could incur additional costs to address the situation, the profitability of that work might be impaired, and the client's dissatisfaction with our services could damage our ability to obtain additional work from that client. In particular, clients that are not satisfied might seek to terminate existing contracts prior to their scheduled expiration date and could direct future business to our competitors. In addition, negative publicity related to our client services or relationships, regardless of its accuracy, may further damage our business by affecting our ability to compete for new contracts with current and prospective clients.

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

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Our top five customers generated approximately 17.6% of our revenues for the quarter ended March 31, 2010. 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.

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### **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 and without significant early termination cost. Terminations may result from factors that are beyond our control and unrelated to our work product or the progress of the project, including the business or financial conditions of the client, changes in ownership or management at our clients, changes in client strategies or the economy or markets generally. When contracts are terminated, we lose the anticipated revenues and might not be able to eliminate our associated costs in a timely manner. Consequently, our profit margins in subsequent periods could be lower than expected. If we are unable to replace the lost revenue with other work on terms we find acceptable or effectively eliminate costs, we may not be able to maintain our level of 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.

### **If we are unable to collect our receivables from or bill our unbilled services to our clients, our results of operations and cash flows could be adversely affected.**

Our business depends on our ability to successfully obtain payment from our clients of the amounts they owe us for work performed. We evaluate the financial condition of our clients and usually bill and collect on relatively short cycles. We maintain allowances against receivables and unbilled services. Actual losses on client balances could differ from those that we currently anticipate and, as a result, we might need to adjust our allowances. There is no guarantee that we will accurately assess the creditworthiness of our clients. Macroeconomic conditions, such as the continued credit crisis and related turmoil in the global financial system, could also result in financial difficulties, including limited access to the credit markets, insolvency or bankruptcy, for our clients, and, as a result, could cause clients to delay payments to us, request modifications to their payment arrangements that could increase our receivables balance, or default on their payment obligations to us. Timely collection of client balances also depends on our ability to complete our contractual commitments and bill and collect our contracted revenues. If we are unable to meet our contractual requirements, we might experience delays in collection of and/or be unable to collect our client balances, and if this occurs, our results of operations and cash flows could be adversely affected. In addition, if we experience an increase in the time to bill and collect for our services, our cash flows could be adversely affected.

### **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.**

We have made and continue to make significant contractual commitments related to capital expenditures on construction or expansion of our development and delivery centers. 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 may be reduced.

### **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 professionals so as to keep our supply of skills and resources in balance with client demand. In particular, we must attract, train and retain appropriate numbers of talented people, including project managers, IT engineers and other senior technical personnel, with diverse skills in order to serve client needs and grow our business. We are particularly dependent on retaining our senior executives and other experienced managers with the skill sets required by our business, and if we are unable to do so, our ability to develop new business and effectively lead our current projects could be jeopardized. Similarly, the profitability of our business model depends on our ability to effectively utilize personnel with the right mix of skills and experience to support our projects. The processes and costs associated with recruiting, training and retaining employees place significant demands on our resources.



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We believe there is a shortage of, and significant competition for, professionals in the United States, Europe 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 profits and ability to compete for and manage client engagements could be adversely affected if we cannot manage employee hiring and attrition to achieve an efficient workforce structure.

**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 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 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.

**Our earnings may be adversely affected if we change our intent not to repatriate earnings in India or if such earnings become subject to U.S. tax on a current basis.**

Effective January 1, 2002, and in accordance with authoritative literature, we no longer accrue incremental U.S. taxes on all Indian earnings recognized in 2002 and subsequent periods as these earnings (as well as other foreign earnings for all periods) 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 not to repatriate our foreign 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 tax rate in 2010. These increased taxes could have a material adverse effect on our business, results of operations and financial condition.

In early 2009, President Obama's Administration announced a number of tax-related legislative proposals that would, among other things, seek to effectively tax certain profits of U.S. companies earned abroad. Although the President did not include several of these proposals in the budget he announced in early 2010, Congress could consider any of these measures at any time. If enacted into law, and depending on their precise terms, these proposals could increase our tax rate and tax payments, and have a material adverse effect on our business, results of operations and financial condition.

**Our operating results may be negatively impacted upon the loss of certain tax benefits provided by India to companies in our industry as well as from proposed tax legislation in India.**

Our Indian subsidiaries are export-oriented companies which, under the Indian Income Tax Act of 1961, are entitled to claim tax holidays for a period of ten consecutive years for each Software Technology Park, or STP, with respect to export profits for each STP. Substantially all of the earnings of our Indian subsidiaries are attributable to export profits. The majority of our STPs in India are currently entitled to a 100% exemption from Indian income tax. Under current Indian tax law, export profits after March 31, 2011 from our existing STPs will be fully taxable at the Indian statutory rate (which is currently 33.99%) in effect at such time. If the tax holidays relating to our Indian STPs are not extended or new tax incentives are not introduced that would effectively extend the income tax holiday benefits beyond March 31, 2011, we expect that our effective income tax rate will increase significantly beginning in calendar year 2011.

**If our pricing structures do not accurately anticipate the cost and complexity of performing our work, then our contracts could be unprofitable.**

We negotiate pricing terms with our clients utilizing a range of pricing structures and conditions. We contract to provide services either on a time-and-materials basis or on a fixed-price basis. Our pricing is highly dependent on our internal forecasts and



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predictions about our projects and the marketplace, which might be based on limited data and could turn out to be inaccurate. If we do not accurately estimate the costs and timing for completing projects, our contracts could prove unprofitable for us or yield lower profit margins than anticipated. We face a number of risks when pricing our contracts, as many of our projects entail the coordination of operations and workforces in multiple locations and utilizing workforces with different skill sets and competencies across geographically distributed service locations. Our pricing, cost and profit margin estimates for the work that we perform frequently include anticipated long-term cost savings from transformational and other initiatives that we expect to achieve and sustain over the life of the contract. There is a risk that we will under price our projects, fail to accurately estimate the costs of performing the work or fail to accurately assess the risks associated with potential contracts. In particular, any increased or unexpected costs, delays or failures to achieve anticipated cost savings, or unexpected risks we encounter in connection with the performance of this work, including those caused by factors outside our control, could make these contracts less profitable or unprofitable, which could have an adverse effect on our profit margin.

In addition, a significant portion of our projects are on a fixed-price basis, subjecting us to the foregoing risks to an even greater extent. Fixed-price contracts accounted for approximately 30.9% of our revenues for the quarter ended March 31, 2010. We expect that an increasing number of our future projects will be contracted on a fixed-price basis. In addition to the other risks described in the paragraph above, 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.

### **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 offshore resources to provide lower-cost service delivery capabilities;

our ability to charge premium prices when justified by market demand or the type of service; and

general economic and political conditions.

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

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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.

**If we do not continue to improve our operational, financial and other internal controls and systems to manage our rapid growth and size or if we are unable to enter, operate and compete effectively in new geographic markets, our business may suffer and the value of our shareholders' investment may be harmed.**

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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, training and retaining technical, finance, marketing and management personnel with the knowledge, skills and experience that our business model requires;

maintaining high levels of client satisfaction;

developing and improving our internal administrative infrastructure, particularly our financial, operational, communications and other internal systems;

preserving our culture, values and entrepreneurial environment; and

effectively managing our personnel and operations and effectively communicating to our personnel worldwide our core values, strategies and goals.

In addition, the size and scope of our operations increase the possibility that an employee will engage in unlawful or fraudulent activity, or otherwise expose us to unacceptable business risks, despite our efforts to train our people and maintain internal controls to prevent such instances. If we do not continue to develop and implement the right processes and tools to manage our enterprise, our ability to compete successfully and achieve our business objectives could be impaired.

As part of our growth strategy, we are expanding our operations in Europe, Asia, Middle East, 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.

### **Our operating results may 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 nature, number, timing, scope and contractual terms of the 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 margins and profitability may fluctuate as a result of:

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

changes to the financial condition of our clients;

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;

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

changes to levels and types of stock-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.

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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.

### **We could be held liable for damages or our reputation could be damaged by disclosure of confidential information or personal data or system failures.**

We are dependent on information technology networks and systems to process, transmit and store electronic information and to communicate among our locations around the world and with our clients. Security breaches of this infrastructure could lead to shutdowns or disruptions of our systems and potential unauthorized disclosure of confidential information. In addition, 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 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 manage, utilize, collect and store sensitive or confidential client or employee data, including nonpublic personal data. As a result, we are subject to numerous U.S. and foreign jurisdiction laws and regulations designed to protect this information, such as the European Union Directive on Data Protection and various U.S. federal and state laws governing the protection of health or other individually identifiable information. If any person, including any of our employees, negligently disregards or intentionally breaches our established controls with respect to such data or otherwise mismanages or misappropriates that data, we could be subject to significant liability to our clients or our clients' customers for breaching contractual confidentiality provisions or privacy laws as well as liability and penalties in connection with any violation of applicable privacy laws and/or criminal prosecution. Unauthorized disclosure of sensitive or confidential client or employee data, whether through breach of computer systems, systems failure, employee negligence, fraud or misappropriation, or otherwise, could damage our reputation and cause us to lose clients. Similarly, unauthorized access to or through our information systems or those we develop or manage for our clients, whether by our employees or third parties, could result in negative publicity, legal liability and damage to our reputation.

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.

### **Our business could be negatively affected if we incur legal liability in connection with providing our solutions and services.**

If we fail to meet our contractual obligations or otherwise breach obligations to our clients, we could be subject to legal liability. We may enter into non-standard agreements because we perceive an important economic opportunity or because our personnel did not adequately adhere to our guidelines. In addition, the contracting practices of our competitors may cause contract terms and conditions that are unfavorable to us to become standard in the marketplace. If we cannot or do not perform our obligations, we could face legal liability and our contracts might not always protect us adequately through limitations on the scope and/or amount of our potential liability. If we cannot or do not meet our contractual obligations to provide solutions and services, and if our exposure is not adequately limited through the terms of our agreements, we might face significant legal liability and our business could be adversely affected.

### **We could incur liability or our reputation could be damaged if our provision of services and solutions to our clients contributes to our clients' internal control deficiencies.**

Our clients may perform audits or require us to perform audits and provide audit reports with respect to the controls and procedures that we use in the performance of services for such clients, especially when we process data belonging to them. Our ability to acquire new clients and retain existing clients may be adversely affected and our reputation could be harmed if we receive a qualified opinion, or if we cannot obtain an unqualified opinion, with respect to our controls and procedures in connection with any such audit in a timely manner. Additionally, we could incur liability if our controls and procedures, or the controls and procedures we manage for a client, were to result in internal controls failures or impair our client's ability to comply with its own internal control requirements.

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### **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, such as China, 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, India and other countries in which we operate are adequate to protect us from misappropriation or unauthorized use of our copyrights and other intellectual property. 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. Enforcing our rights might also require considerable time, money and oversight. Unauthorized use of our intellectual property may result in development of technology, products or services that compete with our products and services 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.

Depending on the circumstances, we might need to grant a specific client greater rights in intellectual property developed or used in connection with a contract than we generally do. In certain situations, we might forego all rights to the use of intellectual property we create and intend to reuse across multiple client engagements, which would limit our ability to reuse that intellectual property for other clients. Any limitation on our ability to provide a service or solution could cause us to lose revenue-generating opportunities and require us to incur additional expenses to develop new or modified solutions for future projects.

### **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 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 expect to continue our program of pursuing strategic acquisitions and joint ventures designed to enhance our capabilities, 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 successfully identify suitable acquisition candidates, consummate any acquisition or joint venture, integrate any acquired business or joint venture into our operations or achieve desired financial and operating results. Further, acquisitions and joint ventures involve a number of special risks, including diversion of management's attention and failure to retain key personnel. We might need to dedicate additional management and other resources to complete the transactions. Our organizational structure could make it difficult for us to efficiently integrate acquired businesses or technologies into our ongoing operations and assimilate employees of those businesses into our culture and operations. Accordingly, we might fail to realize the expected benefits or strategic objectives of any acquisition we undertake. If we are unable to complete the number and kind of acquisitions for which we plan, or if we are inefficient or unsuccessful at integrating any acquired businesses into our operations, we may not be able to achieve our planned rates of growth or improve our market share, profitability or competitive position in specific markets or services. Also, we may finance any future acquisitions with cash, debt financing, and 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.

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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 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. In addition, as part of an acquisition, we may assume responsibilities and obligations of the acquired business pursuant to the terms and conditions of services agreements entered by the acquired entity that are not consistent with the terms and conditions that we typically accept and require. Although we attempt to structure acquisitions in such a manner as to minimize the liability that could arise from such contractual commitments, we cannot assure you that any of our efforts to minimize the liability will be effective in all instances or will otherwise protect us from liability for damages under such agreements. The discovery of any material liabilities associated with our acquisitions for which we are unable to receive indemnification could harm our operating results.

### **System failure or disruptions in communications 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 development and delivery centers 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.

### **Consolidation in the industries that we serve could adversely affect our business.**

Companies in the industries that we serve may seek to achieve economies of scale and other synergies by combining with or acquiring other companies. If two or more of our current clients merge or consolidate and combine their operations, it may decrease the amount of work that we perform for these clients. If one of our current clients merges or consolidates with a company that relies on another provider for its consulting, systems integration and technology, or outsourcing services, we may lose work from that client or lose the opportunity to gain additional work. The increased market power of larger companies could also increase pricing and competitive pressures on us. Any of these possible results of industry consolidation could adversely affect our business.

### **Our ability to attract and retain business may depend on our reputation in the marketplace.**

Our services are marketed to clients and prospective clients based on a number of factors. Since many of our specific client engagements involve unique services and solutions, our corporate reputation is a significant factor in our clients' evaluation of whether to engage our services. We believe the Cognizant brand name and our reputation are important corporate assets that help distinguish our services from those of our competitors and also contribute to our efforts to recruit and retain talented employees. However, our corporate reputation is potentially susceptible to damage by actions or statements made by current or former clients, competitors, vendors, adversaries in legal proceedings, government regulators, as well as members of the investment community and the media. There is a risk that negative information about our company, even if based on rumor or misunderstanding, could adversely affect our business. In particular, damage to our reputation could be difficult and time-consuming to repair, could make potential or existing clients reluctant to select us for new engagements, resulting in a loss of business, and could adversely affect our recruitment and retention efforts. Damage to our reputation could also reduce the value and effectiveness of the Cognizant brand name and could reduce investor confidence in us, adversely affecting our share price.

### **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.

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### **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.

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 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.

### **Our share price could be adversely affected if we are unable to maintain effective internal controls.**

The accuracy of our financial reporting is dependent on the effectiveness of our internal controls. We are required to provide a report from management to our stockholders on our internal control over financial reporting that includes an assessment of the effectiveness of these controls. Internal control over financial reporting has inherent limitations, including human error, the possibility that controls could be circumvented or become inadequate because of changed conditions, and fraud. Because of these inherent limitations, internal control over financial reporting might not prevent or detect all misstatements or fraud. If we cannot maintain and execute adequate internal control over financial reporting or implement required new or improved controls to ensure the reliability of the financial reporting and preparation of our financial statements for external use, we could suffer harm to our reputation, fail to meet our public reporting requirements on a timely basis, or be unable to properly report on our business and the results of our operations, and the market price of our securities could be materially adversely affected.

### **We are exposed to credit risk and fluctuations in the market values of our investment portfolio.**

Recent turmoil in the financial markets has adversely affected economic activity in the United States and other regions of the world in which we do business. We believe that based on our current cash, cash equivalents and investment balances and expected operating cash flows, the current lack of liquidity in the credit markets will not have a material impact on our liquidity, cash flow or financial flexibility. Continued deterioration of the credit and capital markets could result in volatility of our investment earnings and impairments to our investment portfolio, which could negatively impact our financial condition and reported income. The continued decline in economic activity could adversely affect the ability of counterparties to certain financial instruments such as marketable securities and derivatives to meet their obligations to us.

### **Funds associated with auction-rate securities that we hold as investments may not be liquid and our auction-rate securities may decline in value.**

As of March 31, 2010, our short-term and long-term investments totaled \$490.4 million and included \$119.1 million in long-term AAA/A3-rated auction-rate municipal debt securities that are collateralized by debt obligations supported by student loans, substantially backed by the Federal Family Education Loan Program, or FFELP. In addition, the remainder of our long-term investments included an asset of \$18.4 million related to the UBS Right. Since February 14, 2008, auctions failed for all the auction-rate securities still in our portfolio as of March 31, 2010. We believe that the failed auctions experienced to date are not a result of the deterioration of the underlying credit quality of the securities and we

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continue to earn and receive interest on the auction-rate municipal debt securities at a pre-determined formula with spreads tied to particular interest rate indices. All of the auction-rate municipal debt securities held by us are callable by the issuer at par. In November 2008, we accepted an offer from UBS AG, or UBS,

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to sell to UBS, at par value (\$137.6 million at March 31, 2010), our auction-rate municipal debt securities at any time during an exercise period from June 30, 2010 to July 2, 2012, which we refer to as the UBS Right. In accepting the UBS Right, we granted UBS the authority to purchase these auction-rate municipal debt securities or sell them on our behalf at par value any time after the execution of the UBS Right through July 2, 2012. The offer is non-transferable. UBS's inability to perform under the UBS Right and the lack of liquidity for auction-rate municipal debt securities in the financial markets could have a material adverse effect on our financial condition and results of operations.

**Our stock price continues to be volatile.**

Our stock has at times experienced substantial price volatility as a result of variations between our actual and anticipated financial results, announcements by us and our competitors, projections or speculation about our business or that of our competitors by the media or investment analysts or uncertainty about current global economic conditions. The stock market as a whole also has experienced extreme price and volume fluctuations that have affected the market price of many technology companies in ways that may have been unrelated to these companies' operating performance. Furthermore, we believe our stock price should reflect future growth and profitability expectations and, if we fail to meet these expectations, our stock price may significantly decline.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

*Issuer Purchases of Equity Securities*

There were no stock repurchases made during the first quarter ended March 31, 2010.

**Item 6. Exhibits.**

(a) Exhibits.

<b>Exhibit No.</b>	<b>Description</b>
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.
101	The following materials from this Quarterly Report on Form 10-Q for the quarter ended March 31, 2010 and formatted in XBRL: (i) Condensed Consolidated Statements of Operations (Unaudited) for the Three Months Ended March 31, 2010 and 2009; (ii) Condensed Consolidated Statements of Financial Position (Unaudited) as of March 31, 2010 and December 31, 2009; (iii) Condensed Consolidated Statements of Cash Flows (Unaudited) for the Three Months Ended March 31, 2010 and 2009; and (iv) Notes to Condensed Consolidated Financial Statements (Unaudited), tagged as blocks of text.

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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: May 7, 2010

By: /s/ Francisco D Souza  
Francisco D Souza,  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: May 7, 2010

By: /s/ Gordon Coburn  
Gordon Coburn,  
Chief Financial and Operating  
Officer and Treasurer  
(Principal Financial and Accounting Officer)

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**Exhibit Index**

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