

COGNIZANT TECHNOLOGY SOLUTIONS CORP

Form 10-Q

November 08, 2012

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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 September 30, 2012

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

13-3728359
(I.R.S. Employer

Incorporation or Organization)

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 (Do not check if a smaller reporting company) 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 November 2, 2012:

Class	Number of Shares
Class A Common Stock, par value \$.01 per share	300,191,775

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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)**

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 30,	September 30,
	2012	2011	2012	2011
Revenues	\$ 1,891,688	\$ 1,600,954	\$ 5,398,257	\$ 4,457,449
Operating expenses:				
Cost of revenues (exclusive of depreciation and amortization expense shown separately below)	1,111,898	924,886	3,127,307	2,567,933
Selling, general and administrative expenses	384,951	353,161	1,155,900	976,209
Depreciation and amortization expense	39,453	29,905	109,807	84,982
Income from operations	355,386	293,002	1,005,243	828,325
Other income (expense), net:				
Interest income	12,041	9,970	33,097	28,381
Other, net	(3,044)	(15,008)	(16,588)	(10,637)
Total other income (expense), net	8,997	(5,038)	16,509	17,744
Income before provision for income taxes	364,383	287,964	1,021,752	846,069
Provision for income taxes	87,482	60,845	249,268	202,578
Net income	\$ 276,901	\$ 227,119	\$ 772,484	\$ 643,491
Basic earnings per share	\$ 0.93	\$ 0.75	\$ 2.56	\$ 2.12
Diluted earnings per share	\$ 0.91	\$ 0.73	\$ 2.52	\$ 2.07
Weighted average number of common shares outstanding - Basic	299,058	302,723	301,571	303,584
Dilutive effect of shares issuable under stock-based compensation plans	4,074	6,574	4,984	7,275
Weighted average number of common shares outstanding - Diluted	303,132	309,297	306,555	310,859

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 COMPREHENSIVE INCOME

(Unaudited)

(in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Net income	\$ 276,901	\$ 227,119	\$ 772,484	\$ 643,491
Other comprehensive income, net of tax:				
Foreign currency translation adjustments	6,669	(18,137)	8,923	(892)
Change in unrealized (loss) gain on cash flow hedges, net of taxes of \$38,761 and (\$28,599) for the three months ended and \$23,912 and (\$16,200) for the nine months ended, respectively	198,549	(108,781)	124,863	(86,197)
Change in unrealized gain on available-for-sale securities, net of taxes of \$254 and (\$288) for the three months ended and \$301 and \$596 for the nine months ended, respectively	1,480	(400)	1,565	810
Other comprehensive income	206,698	(127,318)	135,351	(86,279)
Comprehensive income	\$ 483,599	\$ 99,801	\$ 907,835	\$ 557,212

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)

	September 30, 2012	December 31, 2011
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,324,739	\$ 1,310,906
Short-term investments	1,307,009	1,121,358
Trade accounts receivable, net of allowances of \$27,370 and \$24,658, respectively	1,363,454	1,179,043
Unbilled accounts receivable	213,741	139,627
Deferred income tax assets, net	166,164	109,042
Other current assets	166,424	225,530
Total current assets	4,541,531	4,085,506
Property and equipment, net of accumulated depreciation of \$551,624 and \$455,506, respectively	878,561	758,034
Goodwill	301,403	288,772
Intangible assets, net	87,583	97,616
Deferred income tax assets, net	154,927	164,192
Other noncurrent assets	143,034	113,813
Total assets	\$ 6,107,039	\$ 5,507,933
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 111,420	\$ 72,205
Deferred revenue	116,427	105,713
Accrued expenses and other current liabilities	1,047,741	1,031,787
Total current liabilities	1,275,588	1,209,705
Deferred income tax liabilities, net	4,593	3,339
Other noncurrent liabilities	254,488	342,003
Total liabilities	1,534,669	1,555,047
Commitments and contingencies (See Note 8)		
Stockholders Equity:		
Preferred stock, \$.10 par value, 15,000 shares authorized, none issued		
Class A common stock, \$.01 par value, 1,000,000 shares authorized, 299,940 and 303,106 shares issued and outstanding at September 30, 2012 and December 31, 2011, respectively	2,999	3,031
Additional paid-in capital	404,404	692,723
Retained earnings	4,355,010	3,582,526
Accumulated other comprehensive income (loss)	(190,043)	(325,394)
Total stockholders equity	4,572,370	3,952,886
Total liabilities and stockholders equity	\$ 6,107,039	\$ 5,507,933

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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 Nine Months Ended September 30,	
	2012	2011
Cash flows from operating activities:		
Net income	\$ 772,484	\$ 643,491
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	115,424	89,876
Provision for doubtful accounts	4,348	3,533
Deferred income taxes	(61,890)	(26,204)
Stock-based compensation expense	79,911	64,244
Excess tax benefits on stock-based compensation plans	(24,960)	(30,966)
Other	(4,382)	24,019
Changes in assets and liabilities:		
Trade accounts receivable	(184,537)	(207,242)
Other current assets	(8,069)	(41,680)
Other assets	(18,691)	(20,884)
Accounts payable	39,386	(2,654)
Other current and noncurrent liabilities	101,699	94,553
Net cash provided by operating activities	810,723	590,086
Cash flows from investing activities:		
Purchases of property and equipment	(208,716)	(163,660)
Purchases of investments	(1,179,674)	(1,181,460)
Proceeds from maturity or sale of investments	1,002,952	743,111
Acquisitions, net of cash acquired	(43,896)	(75,040)
Net cash used in investing activities	(429,334)	(677,049)
Cash flows from financing activities:		
Issuance of common stock under stock-based compensation plans	91,883	57,277
Excess tax benefits on stock-based compensation plans	24,960	30,966
Repurchases of common stock	(483,895)	(364,974)
Net cash used in financing activities	(367,052)	(276,731)
Effect of currency translation on cash and cash equivalents	(504)	3,944
Increase (decrease) in cash and cash equivalents	13,833	(359,750)
Cash and cash equivalents, beginning of year	1,310,906	1,540,969
Cash and cash equivalents, end of period	\$ 1,324,739	\$ 1,181,219

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

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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, 2011. 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.

In May 2012, our Board of Directors amended our existing share repurchase program increasing the amount of our Class A common stock that can be repurchased from an aggregate of \$600,000 to \$1,000,000 and extended the expiration date of the program from June 30, 2012 to December 31, 2013. As of September 30, 2012, \$159,584 is available for future repurchases under this program. During the nine months ended September 30, 2012, we repurchased 7,671,035 shares for \$460,041, inclusive of fees and expenses, under this program.

Note 2 Acquisitions

During the first nine months of 2012, we completed two business combinations. The total cash consideration was approximately \$15,158 (net of cash acquired). In the third quarter of 2012, we entered into a transaction pursuant to which we signed a multi-year service agreement, assumed an assembled workforce, and acquired land, building and other assets. Under the current authoritative business combination guidelines, this transaction qualified as a business combination. This transaction expands our business process services capabilities within the insurance industry. In the third quarter of 2012, we also completed an acquisition to strengthen our knowledge process outsourcing and research capabilities within the media industry. As part of this acquisition, we acquired customer relationship assets, an assembled workforce, and other assets. In addition, during the first nine months of 2012, we settled contingent payment provisions of approximately \$28,921 related to acquisitions completed in prior years.

These acquisitions were included in our unaudited condensed consolidated financial statements as of the date on which the businesses were acquired and were not material to our operations, financial position or cash flow. We have allocated the purchase price related to these transactions to tangible and intangible assets and liabilities based upon their fair values.

Note 3 Investments

Our investments were as follows:

	September 30, 2012	December 31, 2011
Available-for-sale investment securities:		
U.S. Treasury and agency debt securities	\$ 501,939	\$ 464,938
Corporate and other debt securities	307,678	202,705
Asset-backed securities	115,588	100,894
Municipal debt securities	48,179	43,889
Foreign government debt securities	19,894	10,500
Total available-for-sale investment securities	993,278	822,926
Time deposits	313,731	298,432

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Total investments	\$	1,307,009	\$	1,121,358
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Our available-for-sale investment securities consist of U.S. dollar denominated investments primarily in U.S. Treasury notes, U.S. government agency debt securities, municipal debt securities, non-U.S. government debt securities, U.S. and international corporate bonds, certificates of deposit, commercial paper, debt securities issued by supranational institutions

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and asset-backed securities, including those backed by auto loans, credit card receivables, mortgage loans and other receivables. Our investment guidelines are to purchase securities which are investment grade at the time of acquisition. We monitor the credit ratings of the securities in our portfolio on an ongoing basis. The carrying value of the time deposits approximated fair value as of September 30, 2012 and December 31, 2011.

Available-for-Sale Investment Securities

The amortized cost, gross unrealized gains and losses and fair value of available-for-sale investment securities at September 30, 2012 were as follows:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. Treasury and agency debt securities	\$ 500,819	\$ 1,162	\$ (42)	\$ 501,939
Corporate and other debt securities	305,515	2,174	(11)	307,678
Asset-backed securities	115,252	455	(119)	115,588
Municipal debt securities	48,090	135	(46)	48,179
Foreign government debt securities	19,750	144		19,894
Total available-for-sale investment securities	\$ 989,426	\$ 4,070	\$ (218)	\$ 993,278

The amortized cost, gross unrealized gains and losses and fair value of available-for-sale investment securities at December 31, 2011 were as follows:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. Treasury and agency debt securities	\$ 463,318	\$ 1,742	\$ (122)	\$ 464,938
Corporate and other debt securities	202,284	902	(481)	202,705
Asset-backed securities	101,068	100	(274)	100,894
Municipal debt securities	43,873	101	(85)	43,889
Foreign government debt securities	10,397	105	(2)	10,500
Total available-for-sale investment securities	\$ 820,940	\$ 2,950	\$ (964)	\$ 822,926

The fair value and related unrealized losses of available-for-sale investment securities in a continuous unrealized loss position for less than 12 months and for 12 months or longer were as follows as of September 30, 2012:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury and agency debt securities	\$ 86,484	\$ (42)	\$	\$	\$ 86,484	\$ (42)
Corporate and other debt securities	16,433	(11)			16,433	(11)
Asset-backed securities	16,234	(85)	2,885	(34)	19,119	(119)
Municipal debt securities	7,002	(17)	703	(29)	7,705	(46)
Foreign government debt securities	3,034				3,034	
Total	\$ 129,187	\$ (155)	\$ 3,588	\$ (63)	\$ 132,775	\$ (218)

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The fair value and related unrealized losses of available-for-sale investment securities in a continuous unrealized loss position for less than 12 months and for 12 months or longer were as follows as of December 31, 2011:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury and agency debt securities	\$ 122,124	\$ (122)	\$	\$	\$ 122,124	\$ (122)
Corporate and other debt securities	75,076	(481)			75,076	(481)
Asset-backed securities	58,503	(241)	2,292	(33)	60,795	(274)
Municipal debt securities	5,149	(17)	1,732	(68)	6,881	(85)
Foreign government debt securities	1,507	(2)			1,507	(2)
Total	\$ 262,359	\$ (863)	\$ 4,024	\$ (101)	\$ 266,383	\$ (964)

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The unrealized losses for the above securities as of September 30, 2012 and December 31, 2011 are primarily attributable to changes in interest rates. As of September 30, 2012, we do not consider any of the investments to be other-than-temporarily impaired. The unrealized gains and losses in the above tables were recorded, net of tax, in accumulated other comprehensive income (loss).

The contractual maturities of available-for-sale investment securities as of September 30, 2012 are set forth in the following table:

	Amortized Cost	Fair Value
Due within one year	\$ 134,164	\$ 134,474
Due after one year up to two years	327,695	329,018
Due after two years up to three years	406,590	408,443
Due after three years up to four years	5,725	5,755
Asset-backed securities	115,252	115,588
Total available-for-sale investment securities	\$ 989,426	\$ 993,278

Asset-backed securities were excluded from the maturity categories because the actual maturities may differ from the contractual maturities since the underlying receivables may be prepaid without penalties. Further, actual maturities of debt securities may differ from those presented above since certain obligations provide the issuer the right to call or prepay the obligation prior to scheduled maturity without penalty.

Proceeds from sales of available-for-sale investment securities and the gross gains and losses that have been included in earnings as a result of those sales were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Proceeds from sales of available-for-sale investment securities	\$ 207,229	\$ 224,439	\$ 559,095	\$ 484,167
Gross gains	\$ 870	\$ 1,044	\$ 1,857	\$ 2,354
Gross losses		(93)	(335)	(261)
Net gains on sales of available-for-sale investment securities	\$ 870	\$ 951	\$ 1,522	\$ 2,093

Note 4 Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities were as follows:

	September 30, 2012	December 31, 2011
Compensation and benefits	\$ 610,253	\$ 632,649
Income taxes	46,912	27,676
Professional fees	33,590	32,861
Travel and entertainment	28,368	18,215
Customer volume incentives	131,965	104,989
Derivative financial instruments	106,395	126,731
Deferred income taxes	774	73
Other	89,484	88,593
Total accrued expenses and other current liabilities	\$ 1,047,741	\$ 1,031,787

Note 5 Income Taxes

Our Indian subsidiaries, collectively referred to as Cognizant India, are primarily export-oriented companies and are eligible for certain income tax holiday benefits granted by the government of India for export activities conducted within Special Economic Zones, or SEZs, for periods of up to 15 years. Our Indian operations outside of SEZs are subject to corporate income tax at a rate of 32.4%. In addition, all Indian profits, including those generated within SEZs, are subject to the Minimum Alternative Tax, or MAT, at the current rate of 20.0%. Any MAT paid is creditable against future Indian corporate income tax within a 10-year expiration period, subject to other limitations.

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Our effective income tax rates were as follows:

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
Effective income tax rate	24.0%	21.1%	24.4%	23.9%

For the 2012 and 2011 periods, the principal difference between our effective income tax rates 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 6 Fair Value Measurements

We measure our cash equivalents, investments 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.

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. The following table summarizes our financial assets and (liabilities) measured at fair value on a recurring basis as of September 30, 2012:

	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	\$ 329,140	\$	\$	\$ 329,140
Time deposits		131,653		131,653
Commercial paper		4,199		4,199
Total cash equivalents	329,140	135,852		464,992
Investments:				
Time deposits		313,731		313,731
Available-for-sale investment securities:				
U.S. Treasury and agency debt securities	338,318	163,621		501,939
Corporate and other debt securities		307,678		307,678
Asset-backed securities		115,588		115,588

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Municipal debt securities		48,179		48,179
Foreign government debt securities		19,894		19,894
Total available-for-sale investment securities	338,318	654,960		993,278
Total investments	338,318	968,691		1,307,009
Derivative financial instruments foreign exchange forward contracts:				
Other current assets		1,932		1,932
Accrued expenses and other current liabilities		(106,395)		(106,395)
Other noncurrent assets		12,838		12,838
Other noncurrent liabilities		(155,053)		(155,053)
Total	\$ 667,458	\$ 857,865	\$	\$ 1,525,323

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The following table summarizes our financial assets and (liabilities) measured at fair value on a recurring basis as of December 31, 2011:

	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	\$ 128,004	\$	\$	\$ 128,004
Time deposits		13,283		13,283
Commercial paper		11,626		11,626
Total cash equivalents	128,004	24,909		152,913
Investments:				
Time deposits		298,432		298,432
Available-for-sale investment securities:				
U.S. Treasury and agency debt securities	326,659	138,279		464,938
Corporate and other debt securities		202,705		202,705
Asset-backed securities		100,894		100,894
Municipal debt securities		43,889		43,889
Foreign government debt securities		10,500		10,500
Total available-for-sale investment securities	326,659	496,267		822,926
Total investments	326,659	794,699		1,121,358
Derivative financial instruments – foreign exchange forward contracts:				
Other current assets		30,935		30,935
Accrued expenses and other current liabilities		(126,731)		(126,731)
Other noncurrent liabilities		(259,104)		(259,104)
Total	\$ 454,663	\$ 464,708	\$	\$ 919,371

We measure the fair value of money market funds and U.S. Treasury securities based on quoted prices in active markets for identical assets. The fair value of commercial paper, certificates of deposit, U.S. government agency securities, municipal debt securities, U.S. and international corporate bonds and foreign government debt securities is measured based on relevant trade data, dealer quotes, or model driven valuations using significant inputs derived from or corroborated by observable market data, such as yield curves and credit spreads. We measure the fair value of our asset-backed securities using model driven valuations based on significant inputs derived from or corroborated by observable market data such as dealer quotes, available trade information, spread data, current market assumptions on prepayment speeds and defaults and historical data on deal collateral performance.

We estimate the fair 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 include a discount and credit risk factor. The amounts are aggregated by type of contract and maturity.

During the nine months ended September 30, 2012 and the year ended December 31, 2011, there were no transfers among Level 1, Level 2, or Level 3 financial assets and liabilities.

Note 7 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. Derivatives may give rise to credit risks from the possible non-performance by counterparties. Credit risk is generally limited to the fair value of those contracts that are favorable to us. We have limited our credit risk by entering into derivative transactions only with

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highly-rated global financial institutions, limiting the amount of credit exposure with any one financial institution and conducting ongoing evaluation of the creditworthiness of the financial institutions with which we do business.

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The following table provides information on the location and fair values of derivative financial instruments included in our unaudited condensed consolidated statements of financial position as of:

Designation of Derivatives	Location on Statement of Financial Position	September 30, 2012		December 31, 2011	
		Assets	Liabilities	Assets	Liabilities
Cash Flow Hedges Designated as hedging instruments					
Foreign exchange forward contracts	Other current assets	\$ 1,790	\$	\$	\$
	Other noncurrent assets	12,838			
	Accrued expenses and other current liabilities		96,440		126,536
	Other noncurrent liabilities		155,053		259,104
	Total	14,628	251,493		385,640
Other Derivatives Not designated as hedging instruments					
Foreign exchange forward contracts	Other current assets	142		30,935	
	Accrued expenses and other current liabilities		9,955		195
	Total	142	9,955	30,935	195
Total		\$ 14,770	\$ 261,448	\$ 30,935	\$ 385,835

Cash Flow Hedges

We have entered into a series of foreign exchange forward contracts that are designated as cash flow hedges of Indian rupee denominated 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 2012, 2013, 2014, 2015 and 2016. Under these contracts, we purchase Indian rupees and sell U.S. dollars. The changes in fair value of these contracts are initially reported in the caption accumulated other comprehensive income (loss) in our consolidated statements of financial position and are subsequently reclassified to earnings in the same period the hedge contract matures. As of September 30, 2012, we estimate that \$79,190 of the net losses related to derivatives designated as cash flow hedges recorded in accumulated other comprehensive income (loss) is expected to be reclassified into earnings within the next 12 months.

The notional value of our outstanding contracts by year of maturity and the net unrealized (loss) gain included in accumulated other comprehensive income (loss) for such contracts were as follows as of:

	September 30, 2012	December 31, 2011
2012	\$ 324,750	\$ 1,193,500
2013	1,253,000	1,080,000
2014	1,200,000	810,000
2015	780,000	420,000
2016	120,000	
Total notional value of contracts outstanding	\$ 3,677,750	\$ 3,503,500
Net unrealized (loss) included in accumulated other comprehensive income (loss), net of taxes	\$ (198,176)	\$ (323,039)

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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, with the hedged Indian rupee denominated expense reported within cost of revenues and selling, general and administrative expenses. Hedge ineffectiveness was immaterial for all periods presented.

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The following table provides information on the location and amounts of pre-tax gains (losses) on our cash flow hedges for the three months ended September 30:

			Location of Net Derivative Gains	
			(Losses) Reclassified	
	Increase (decrease) in		from Accumulated Other	
	Derivative Gains		Comprehensive Income (Loss)	
	(Losses) Recognized		into Income	
	in Accumulated Other		(effective portion)	
	Comprehensive Income (Loss)		Comprehensive Income (Loss)	
	(effective portion)		into Income	
	2012	2011	2012	2011
Cash Flow Hedges Designated as hedging instruments				
Foreign exchange forward contracts	\$ 206,693	\$ (130,402)	Cost of revenues	\$ (25,124) \$ 5,756
			Selling, general and administrative expenses	(5,493) 1,222
			Total	\$ (30,617) \$ 6,978

The following table provides information on the location and amounts of pre-tax gains (losses) on our cash flow hedges for the nine months ended September 30:

			Location of Net Derivative Gains	
			(Losses) Reclassified	
	Increase (decrease) in		from Accumulated Other	
	Derivative Gains		Comprehensive Income (Loss)	
	(Losses) Recognized		into Income	
	in Accumulated Other		(effective portion)	
	Comprehensive Income (Loss)		Comprehensive Income (Loss)	
	(effective portion)		into Income	
	2012	2011	2012	2011
Cash Flow Hedges Designated as hedging instruments				
Foreign exchange forward contracts	\$ 80,020	\$ (69,300)	Cost of revenues	\$ (56,621) \$ 27,282
			Selling, general and administrative expenses	(12,134) 5,815
			Total	\$ (68,755) \$ 33,097

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The activity related to the change in net unrealized (losses) gains on cash flow hedges in accumulated other comprehensive income (loss) was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Net unrealized (losses) gains on cash flow hedges, net of taxes, beginning of period	\$ (396,725)	\$ 53,307	\$ (323,039)	\$ 30,723
Change in fair value, net of tax	172,933	(103,255)	67,338	(59,990)
Reclassification into earnings, net of tax	25,616	(5,526)	57,525	(26,207)
Net unrealized (losses) gains on cash flow hedges, net of taxes, end of period	\$ (198,176)	\$ (55,474)	\$ (198,176)	\$ (55,474)

Other Derivatives

We use foreign exchange forward contracts, which have not been designated as hedges, to hedge balance sheet exposure to certain monetary assets and liabilities denominated in currencies other than the functional currency of our foreign subsidiaries. We entered into a series of foreign exchange forward contracts scheduled to mature in 2012 and 2013 which are primarily 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, net in our consolidated statements of operations.

Additional information related to our outstanding contracts is as follows:

	September 30, 2012	December 31, 2011
Notional value of contracts outstanding	\$ 202,571	\$ 234,239

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The following table provides information on the location and amounts of realized and unrealized pre-tax gains (losses) on our other derivative financial instruments for the three and nine months ended September 30, 2012 and 2011:

	Location of Net Gains/ (Losses) on Derivative Instruments	Amount of Net Gains (Losses) on Derivative Instruments			
		Three Months Ended September 30,		Nine Months Ended September 30,	
		2012	2011	2012	2011
Other Derivatives Not designated as hedging instruments					
Foreign exchange forward contracts	Other, net	\$ (12,535)	\$ 16,437	\$ (12,271)	\$ 6,922

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

Note 8 Commitments and Contingencies

Our current India real estate development program includes planned construction of 10.5 million square feet of new space between 2011 and the end of 2015. This program includes the expenditure of over \$700,000 during this period on land acquisition, facilities construction and furnishings to build new company-owned state-of-the-art IT development and delivery centers in regions primarily designated as SEZs located in India. As of September 30, 2012, we had outstanding fixed capital commitments of approximately \$253,810 related to our India development center expansion program.

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, results of operations and cash flows. 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, could have a material adverse effect on our business, results of operations, financial condition and cash flows.

In the normal course of business and in conjunction with certain client engagements, we have entered into contractual arrangements through which we may be obligated to indemnify clients or other parties with whom we conduct business with respect to certain matters. These arrangements can include provisions whereby we agree to hold the indemnified party and certain of their affiliated entities harmless with respect to third-party claims related to such matters as our breach of certain representations or covenants, or out of our intellectual property infringement, our gross negligence or willful misconduct or certain other claims made against certain parties. Payments by us under any of these arrangements are generally conditioned on the client making a claim and providing us with full control over the defense and settlement of such claim. It is not possible to determine the maximum potential amount under these indemnification agreements due to the unique facts and circumstances involved in each particular agreement. Historically, we have not made payments under these indemnification agreements so they have not had any impact on our operating results, financial position, or cash flows. However, if events arise requiring us to make payment for indemnification claims under our indemnification obligations in contracts we have entered, such payments could have material impact on our business, results of operations, financial condition and cash flows.

Table of Contents**Note 9 Accumulated Other Comprehensive Income (Loss)**

The components of accumulated other comprehensive income (loss) were as follows:

	September 30, 2012	December 31, 2011
Foreign currency translation adjustments	\$ 5,362	\$ (3,561)
Unrealized (loss) on cash flow hedges, net of taxes	(198,176)	(323,039)
Unrealized gain on available-for-sale securities, net of taxes	2,771	1,206
Total accumulated other comprehensive income (loss)	\$ (190,043)	\$ (325,394)

Note 10 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 our information, media and entertainment 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 the development and delivery centers. Certain selling, general and administrative expenses, excess or shortfall of incentive compensation for delivery personnel as compared to target, stock-based compensation expense, a portion of depreciation and amortization and the impact of the settlements of our cash flow hedges are not allocated to individual segments in internal management reports used by the chief operating decision maker. Accordingly, such expenses are excluded from segment operating profit and 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.

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Revenues from external customers and segment operating profit, before unallocated expenses, for the Financial Services, Healthcare, Manufacturing/Retail/Logistics, and Other reportable segments were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Revenues:				
Financial Services	\$ 788,439	\$ 655,761	\$ 2,220,048	\$ 1,838,426
Healthcare	483,109	429,798	1,434,808	1,165,201
Manufacturing/Retail/Logistics	396,557	310,056	1,089,962	878,767
Other	223,583	205,339	653,439	575,055
Total revenue	\$ 1,891,688	\$ 1,600,954	\$ 5,398,257	\$ 4,457,449
Segment Operating Profit:				
Financial Services	\$ 263,866	\$ 222,165	\$ 752,550	\$ 620,660
Healthcare	171,365	171,261	543,215	436,873
Manufacturing/Retail/Logistics	140,142	112,960	394,053	321,482
Other	77,156	66,753	219,036	182,122
Total segment operating profit	652,529	573,139	1,908,854	1,561,137
Less: unallocated costs ⁽¹⁾	297,143	280,137	903,611	732,812
Income from operations	\$ 355,386	\$ 293,002	\$ 1,005,243	\$ 828,325

(1) Includes \$22,261 and \$79,911 of stock-based compensation expense for the three and nine months ended September 30, 2012, respectively and \$24,500 and \$64,244 of stock-based compensation expense for the three and nine months ended September 30, 2011, respectively.

Geographic Area Information

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Revenues: ⁽¹⁾				
North America ⁽²⁾	\$ 1,504,706	\$ 1,250,708	\$ 4,300,399	\$ 3,475,707
Europe ⁽³⁾	302,648	290,606	869,254	823,232
Other ⁽⁴⁾	84,334	59,640	228,604	158,510
Total	\$ 1,891,688	\$ 1,600,954	\$ 5,398,257	\$ 4,457,449

	As of	
	September 30, 2012	December 31, 2011
Long-lived Assets: ⁽⁵⁾		
North America ⁽²⁾	\$ 50,638	\$ 27,387
Europe	9,021	5,232

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Other ⁽⁴⁾⁽⁶⁾	818,902	725,415
Total	\$ 878,561	\$ 758,034

- (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 \$195,538 and \$183,737 for the three months and \$558,854 and \$522,908 for the nine months ended September 30, 2012 and 2011, respectively.
- (4) Includes our operations in Asia Pacific, the Middle East and Latin 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.

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In June 2011, the Financial Accounting Standards Board, or FASB, issued new guidance, which requires that comprehensive income be presented either in a single continuous statement of comprehensive income or in two separate consecutive statements, thus eliminating the option of presenting the components of other comprehensive income as part of the statement of changes in stockholders' equity. In addition, the new guidance requires that the reclassification adjustments for items that are reclassified from other comprehensive income to net income be presented on the face of the financial statements. In December 2011, the FASB deferred the new requirements related to the presentation of reclassification adjustments. However, the requirement to present comprehensive income either in a single continuous statement of comprehensive income or in two separate consecutive statements has not been deferred and became effective January 1, 2012. We adopted this standard on January 1, 2012 and elected to present comprehensive income in two consecutive statements. The adoption of this standard affects financial statement presentation only and had no effect on our financial condition or consolidated results of operations.

In September 2011, the FASB issued new guidance related to goodwill impairment testing. This standard allows, but does not require, an entity to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. However, if an entity concludes otherwise, then it is required to perform the first step of the two-step impairment test by calculating the fair value of the reporting unit and comparing the fair value with the carrying amount of the reporting unit. If the carrying amount of a reporting unit exceeds its fair value, then the entity is required to perform the second step of the goodwill impairment test to measure the amount of the impairment loss, if any. The new standard gives an entity the option to bypass the qualitative assessment for any reporting unit in any period and proceed directly to performing the first step of the two-step goodwill impairment test. An entity may resume performing the qualitative assessment in any subsequent period. This standard is effective for periods beginning on January 1, 2012 and had no effect on our financial condition or consolidated results of operations.

In December 2011, the FASB issued guidance requiring enhanced disclosures related to the nature of an entity's rights to offset and any related arrangements associated with its financial instruments and derivative instruments. The new guidance requires the disclosure of the gross amounts subject to rights of set-off, amounts offset in accordance with the accounting standards followed and the related net exposure. The new guidance will be effective for periods beginning on or after January 1, 2013. The adoption of this standard affects financial statement disclosures only and will have no effect on our financial condition or consolidated results of operations.

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

During the three and nine months ended September 30, 2012, our revenue increased to \$1,891.7 million and \$5,398.3 million compared to \$1,601.0 million and \$4,457.4 million during the three and nine months ended September 30, 2011. Net income increased to \$276.9 million and \$772.5 million, or \$0.91 and \$2.52 per diluted share, including stock-based compensation expense, net of tax, equal to \$0.06 and \$0.20 per diluted share, during the three and nine months ended September 30, 2012, respectively. This is compared to net income of \$227.1 million and \$643.5 million, or \$0.73 and \$2.07 per diluted share, including stock-based compensation expense, net of tax, of \$0.07 and \$0.16 per diluted share, during the three and nine months ended September 30, 2011, respectively. The key drivers of our revenue growth during the three months ended September 30, 2012 were as follows:

Strong performance across all of our business segments, particularly our Manufacturing/Retail/Logistics and Financial Services business segments, which reported revenue growth of 27.9% and 20.2%, respectively, for the quarter as compared to the quarter ended September 30, 2011;

Increased customer spending on discretionary development projects;

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

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management, business process outsourcing, or BPO, and business intelligence. We finished the quarter with approximately 821 active clients compared to 777 as of September 30, 2011 and increased the number of strategic clients by six during the quarter bringing the total number of our strategic clients to 208. We define a strategic client as one offering the potential to generate at least \$5 million to \$50 million or more in annual revenues at maturity. Our top five and top ten customers accounted for approximately 14.0% and 25.0%, respectively, of our total revenues during the quarter ended September 30, 2012 as compared to approximately 16.3% and 27.8%, respectively, for the quarter ended September 30, 2011. 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.

Our revenue growth is also attributed to increasing market acceptance of, and strong demand for, offshore IT software and services and business process outsourcing. NASSCOM (India's National Association of Software and Service Companies) reports indicate that export revenues from India's IT software and services and business process outsourcing sectors are expected to experience growth in the range of approximately 11 to 14% for NASSCOM's fiscal year 2013. According to NASSCOM's 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.

During the quarter ended September 30, 2012, our revenue from European customers increased by 4.1% to approximately \$302.6 million compared to approximately \$290.6 million in the quarter ended September 30, 2011. For the quarter ended September 30, 2012, revenue from Europe, excluding the UK, increased by approximately \$0.2 million from approximately \$106.9 million in the quarter ended September 30, 2011 to approximately \$107.1 million, while revenue from the UK increased by approximately \$11.8 million from approximately \$183.7 million in the quarter ended September 30, 2011 to approximately \$195.5 million. As a result of the ongoing uncertainty in the European economy, we continue to expect revenues generated from European customers to grow at a slower rate than the rest of the Company for the remainder of 2012. We believe that Europe will continue to be an area of significant investment for us as we see this region, as well as the Middle East and the Asia Pacific regions, particularly Japan, India, Australia and Singapore, as growth opportunities for the long term.

Our operating margin increased to approximately 18.8% for the quarter ended September 30, 2012 compared to 18.3% for the quarter ended September 30, 2011. Excluding stock-based compensation expense of approximately \$22.3 million, operating margin for the quarter ended September 30, 2012 was approximately 20.0%. This was within our historic targeted operating margin range, excluding stock-based compensation expense, of 19% to 20% of total revenues. The increase in operating margin was primarily due to the favorable impact of the depreciation of the Indian rupee versus the U.S. dollar, net of the impact of our cash flow hedge losses, and 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, partially offset by continued investments to grow our business. Historically, we have invested our profitability above the 19% to 20% operating margin level, which excludes stock-based compensation, back into our business, which we believe is a significant contributing factor to our strong revenue growth. This investment is primarily focused in the areas of: hiring client partners and relationship personnel with specific industry experience or domain expertise; training our technical staff in a broader range of service offerings; strengthening our business analytic capabilities; strengthening and expanding our portfolio of services; continuing to expand our geographic presence for both sales and delivery; and 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. We expect to continue to invest amounts in excess of our targeted operating margin levels back into the business.

We finished the third quarter of 2012 with total headcount of approximately 150,400, which is an increase of approximately 20,000 as compared to the total headcount at September 30, 2011. 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 2012. Annualized turnover, including both voluntary and involuntary, was approximately 13.0% during the three months ended September 30, 2012. The majority of our turnover occurs in India. As a result, annualized attrition rates on-site at clients are below our global attrition rate. In addition, attrition is weighted towards the more junior members of our staff. We have experienced increases in compensation and benefits costs, including incentive-based compensation costs, in India which may continue in the future; however, historically, this has not had a material impact on our results of operations as we have been able to absorb such cost increases through price increases or cost management strategies such as managing discretionary costs, the mix of our professional staff as well as utilization levels, and achieving other operating efficiencies.

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Our current India real estate development program includes planned construction of 10.5 million square feet of new space between 2011 and the end of 2015. This program includes the expenditure of over \$700.0 million during this period on land acquisition, facilities construction and furnishings to build new company-owned state-of-the-art development and delivery centers in regions primarily designated as Special Economic Zones, or SEZs, located in India. During 2012, we expect to spend approximately \$370 million globally for capital expenditures, including the Indian real estate development program.

At September 30, 2012, we had cash, cash equivalents and short-term investments of \$2,631.7 million and working capital of \$3,265.9 million. Accordingly, we do not anticipate any near-term liquidity issues. During the three months ended September 30, 2012, we repurchased \$59.0 million of our Class A common stock under our stock repurchase program. Stock repurchases were funded from working capital.

We believe the global economic environment remains fragile. During the remainder of 2012, barring any unforeseen events, we expect the following factors to affect our business and our operating results:

Continued focus by customers on directing IT spending towards cost containment projects, s