

COGNIZANT TECHNOLOGY SOLUTIONS CORP  
Form 10-Q  
August 06, 2012  
[Table of Contents](#)

**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 June 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)

Edgar Filing: COGNIZANT TECHNOLOGY SOLUTIONS CORP - Form 10-Q

**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  (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 August 1, 2012:

Class	Number of Shares
Class A Common Stock, par value \$.01 per share	298,565,179

**Table of Contents**

**COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION**

**TABLE OF CONTENTS**

	<b>Page</b>
<b>PART I. <u>FINANCIAL INFORMATION</u></b>	<b>1</b>
Item 1. <u>Condensed Consolidated Financial Statements (Unaudited)</u>	1
<u>Condensed Consolidated Statements of Operations (Unaudited) for the Three Months Ended June 30, 2012 and 2011 and for the Six Months Ended June 30, 2012 and 2011</u>	1
<u>Condensed Consolidated Statements of Comprehensive Income (Unaudited) for the Three Months Ended June 30, 2012 and 2011 and for the Six Months Ended June 30, 2012 and 2011</u>	2
<u>Condensed Consolidated Statements of Financial Position (Unaudited) as of June 30, 2012 and December 31, 2011</u>	3
<u>Condensed Consolidated Statements of Cash Flows (Unaudited) for the Six Months Ended June 30, 2012 and 2011</u>	4
<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	5
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	15
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	32
Item 4. <u>Controls and Procedures</u>	33
<b><u>PART II. OTHER INFORMATION</u></b>	<b>33</b>
Item 1A. <u>Risk Factors</u>	33
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	51
Item 6. <u>Exhibits</u>	52
<b><u>SIGNATURES</u></b>	<b>53</b>

**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 June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Revenues	\$ 1,795,220	\$ 1,485,242	\$ 3,506,569	\$ 2,856,495
Operating expenses:				
Cost of revenues (exclusive of depreciation and amortization expense shown separately below)	1,030,889	860,871	2,015,409	1,643,047
Selling, general and administrative expenses	396,771	326,718	770,949	623,048
Depreciation and amortization expense	35,602	27,695	70,354	55,077
Income from operations	331,958	269,958	649,857	535,323
Other income (expense), net:				
Interest income	9,984	9,474	21,056	18,411
Other, net	(6,850)	(1,827)	(13,544)	4,371
Total other income (expense), net	3,134	7,647	7,512	22,782
Income before provision for income taxes	335,092	277,605	657,369	558,105
Provision for income taxes	83,160	69,560	161,786	141,733
Net income	\$ 251,932	\$ 208,045	\$ 495,583	\$ 416,372
Basic earnings per share	\$ 0.83	\$ 0.68	\$ 1.64	\$ 1.37
Diluted earnings per share	\$ 0.82	\$ 0.67	\$ 1.61	\$ 1.34
Weighted average number of common shares outstanding - Basic	302,225	303,989	302,827	304,015
Dilutive effect of shares issuable under stock-based compensation plans	5,101	7,488	5,440	7,625
Weighted average number of common shares outstanding - Diluted	307,326	311,477	308,267	311,640

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

**Table of Contents**

**COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(Unaudited)

(in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net income	\$ 251,932	\$ 208,045	\$ 495,583	\$ 416,372
Other comprehensive income, net of tax:				
Foreign currency translation adjustments	(9,380)	8,408	2,254	17,245
Change in unrealized (loss) gain on cash flow hedges, net of taxes of (\$37,791) and \$6,974 for the three months ended and (\$14,849) and \$12,399 for the six months ended, respectively	(193,578)	26,526	(73,686)	22,584
Change in unrealized gain on available-for-sale securities, net of taxes of (\$133) and \$1,255 for the three months ended and \$47 and \$884 for the six months ended, respectively	(452)	1,753	85	1,210
Other comprehensive income	(203,410)	36,687	(71,347)	41,039
Comprehensive income	\$ 48,522	\$ 244,732	\$ 424,236	\$ 457,411

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

**Table of Contents**

**COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**

(Unaudited)

(in thousands, except par values)

	June 30, 2012	December 31, 2011
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 1,050,245	\$ 1,310,906
Short-term investments	1,295,897	1,121,358
Trade accounts receivable, net of allowances of \$26,883 and \$24,658, respectively	1,296,175	1,179,043
Unbilled accounts receivable	207,712	139,627
Deferred income tax assets, net	104,151	109,042
Other current assets	198,172	225,530
<b>Total current assets</b>	<b>4,152,352</b>	<b>4,085,506</b>
Property and equipment, net of accumulated depreciation of \$515,153 and \$455,506, respectively	837,683	758,034
Goodwill	289,211	288,772
Intangible assets, net	86,530	97,616
Deferred income tax assets, net	167,462	164,192
Other noncurrent assets	120,981	113,813
<b>Total assets</b>	<b>\$ 5,654,219</b>	<b>\$ 5,507,933</b>
<b>Liabilities and Stockholders Equity</b>		
Current liabilities:		
Accounts payable	\$ 104,411	\$ 72,205
Deferred revenue	106,625	105,713
Accrued expenses and other current liabilities	940,059	1,031,787
<b>Total current liabilities</b>	<b>1,151,095</b>	<b>1,209,705</b>
Deferred income tax liabilities, net	3,073	3,339
Other noncurrent liabilities	407,718	342,003
<b>Total liabilities</b>	<b>1,561,886</b>	<b>1,555,047</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, 1,000,000 shares authorized, 299,252 and 303,106 shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively	2,993	3,031
Additional paid-in capital	407,972	692,723
Retained earnings	4,078,109	3,582,526
Accumulated other comprehensive income (loss)	(396,741)	(325,394)
<b>Total stockholders equity</b>	<b>4,092,333</b>	<b>3,952,886</b>
<b>Total liabilities and stockholders equity</b>	<b>\$ 5,654,219</b>	<b>\$ 5,507,933</b>

Edgar Filing: COGNIZANT TECHNOLOGY SOLUTIONS CORP - Form 10-Q

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

**Table of Contents**

**COGNIZANT TECHNOLOGY SOLUTIONS CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited)

(in thousands)

	For the Six Months Ended June 30,	
	2012	2011
Cash flows from operating activities:		
Net income	\$ 495,583	\$ 416,372
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	74,058	58,237
Provision for doubtful accounts	2,673	2,517
Deferred income taxes	17,129	(1,819)
Stock-based compensation expense	57,650	39,744
Excess tax benefits on stock-based compensation plans	(15,853)	(22,041)
Other	(1,764)	164
Changes in assets and liabilities:		
Trade accounts receivable	(119,949)	(170,419)
Other current assets	(39,178)	(37,511)
Other assets	(1,549)	(17,163)
Accounts payable	27,185	7,644
Other current and noncurrent liabilities	(70,122)	(14,983)
Net cash provided by operating activities	425,863	260,742
Cash flows from investing activities:		
Purchases of property and equipment	(138,772)	(89,550)
Purchases of investments	(817,429)	(771,018)
Proceeds from maturity or sale of investments	638,275	383,486
Acquisition, net of cash acquired	(24,877)	(19,321)
Net cash used in investing activities	(342,803)	(496,403)
Cash flows from financing activities:		
Issuance of common stock under stock-based compensation plans	61,527	40,282
Excess tax benefits on stock-based compensation plans	15,853	22,041
Repurchases of common stock	(418,783)	(192,130)
Net cash used in financing activities	(341,403)	(129,807)
Effect of currency translation on cash and cash equivalents	(2,318)	17,539
Decrease in cash and cash equivalents	(260,661)	(347,929)
Cash and cash equivalents, beginning of year	1,310,906	1,540,969
Cash and cash equivalents, end of period	\$ 1,050,245	\$ 1,193,040

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, 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 of common stock and extended the expiration date from June 30, 2012 to December 31, 2013. As of June 30, 2012, \$218,590 is available for future repurchases under this program. During the six months ended June 30, 2012, we repurchased 6,623,617 shares for \$401,019, inclusive of fees and expenses, under this program.

**Note 2 Investments**

Investments were as follows:

	June 30, 2012	December 31, 2011
Available-for-sale investment securities:		
U.S. Treasury and agency debt securities	\$ 500,298	\$ 464,938
Corporate and other debt securities	304,557	202,705
Asset-backed securities	113,253	100,894
Municipal debt securities	48,817	43,889
Foreign government debt securities	13,245	10,500
Total available-for-sale investment securities	980,170	822,926
Time deposits	315,727	298,432
Total investments	\$ 1,295,897	\$ 1,121,358

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, debt securities issued by supranational institutions 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 June 30, 2012 and December 31, 2011.

**Table of Contents****Available-for-Sale Investment Securities**

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

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and agency debt securities	\$ 499,199	\$ 1,186	\$ (87)	\$ 500,298
Corporate and other debt securities	303,691	1,180	(314)	304,557
Asset-backed securities	113,256	218	(221)	113,253
Municipal debt securities	48,757	117	(57)	48,817
Foreign government debt securities	13,149	103	(7)	13,245
Total available-for-sale investment securities	\$ 978,052	\$ 2,804	\$ (686)	\$ 980,170

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	Gross Unrealized Gains	Gross 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 June 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	\$ 165,802	\$ (87)	\$	\$	\$ 165,802	\$ (87)
Corporate and other debt securities	115,735	(314)			115,735	(314)
Asset-backed securities	23,530	(103)	7,272	(118)	30,802	(221)
Municipal debt securities	12,281	(33)	708	(24)	12,989	(57)
Foreign government debt securities	2,120	(7)			2,120	(7)
Total	\$ 319,468	\$ (544)	\$ 7,980	\$ (142)	\$ 327,448	\$ (686)

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
---------------------	-------------------	-------

Edgar Filing: COGNIZANT TECHNOLOGY SOLUTIONS CORP - Form 10-Q

	<b>Fair Value</b>	<b>Unrealized Losses</b>	<b>Fair Value</b>	<b>Unrealized Losses</b>	<b>Fair Value</b>	<b>Unrealized Losses</b>
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)

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

**Table of Contents**

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

	Amortized Cost	Fair Value
Due within one year	\$ 148,638	\$ 148,936
Due after one year up to two years	309,350	310,520
Due after two years up to three years	391,235	391,852
Due after three years up to four years	15,573	15,609
Asset-backed securities	113,256	113,253
Total available-for-sale investment securities	\$ 978,052	\$ 980,170

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 June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Proceeds from sales of available-for-sale investment securities	\$ 144,342	\$ 132,201	\$ 351,866	\$ 259,728
Gross gains	\$ 542	\$ 828	\$ 987	\$ 1,310
Gross losses	(115)	(35)	(335)	(168)
Net gains on sales of available-for-sale investment securities	\$ 427	\$ 793	\$ 652	\$ 1,142

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

Accrued expenses and other current liabilities were as follows:

	June 30, 2012	December 31, 2011
Compensation and benefits	\$ 490,237	\$ 632,649
Income taxes	33,370	27,676
Professional fees	33,654	32,861
Travel and entertainment	22,305	18,215
Customer volume incentives	106,591	104,989
Derivative financial instruments	164,729	126,731
Deferred income taxes	724	73
Other	88,449	88,593
Total accrued expenses and other current liabilities	\$ 940,059	\$ 1,031,787

**Note 4 Income Taxes**

## Edgar Filing: COGNIZANT TECHNOLOGY SOLUTIONS CORP - Form 10-Q

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.

**Table of Contents**

Our effective income tax rates were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Effective income tax rate	24.8%	25.1%	24.6%	25.4%

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 5 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 June 30, 2012:

	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	\$ 308,948	\$	\$	\$ 308,948
Time deposits		50,064		50,064
Commercial paper		4,698		4,698
<b>Total cash equivalents</b>	<b>308,948</b>	<b>54,762</b>		<b>363,710</b>
Investments:				
Time deposits		315,727		315,727
Available-for-sale investment securities:				
U.S. Treasury and agency debt securities	344,362	155,936		500,298
Corporate and other debt securities		304,557		304,557
Asset-backed securities		113,253		113,253
Municipal debt securities		48,817		48,817

Edgar Filing: COGNIZANT TECHNOLOGY SOLUTIONS CORP - Form 10-Q

Foreign government debt securities		13,245		13,245
Total available-for-sale investment securities	344,362	635,808		980,170
Total investments	344,362	951,535		1,295,897
Derivative financial instruments — foreign exchange forward contracts:				
Other current assets		11,000		11,000
Accrued expenses and other current liabilities		(164,729)		(164,729)
Other noncurrent liabilities		(309,629)		(309,629)
Total	\$ 653,310	\$ 542,939	\$	\$ 1,196,249



**Table of Contents**

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
<b>Cash equivalents:</b>				
Money market funds	\$ 128,004	\$	\$	\$ 128,004
Time deposits		13,283		13,283
Commercial paper		11,626		11,626
<b>Total cash equivalents</b>	<b>128,004</b>	<b>24,909</b>		<b>152,913</b>
<b>Investments:</b>				
Time deposits		298,432		298,432
<b>Available-for-sale investment securities:</b>				
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
<b>Total available-for-sale investment securities</b>	<b>326,659</b>	<b>496,267</b>		<b>822,926</b>
<b>Total investments</b>	<b>326,659</b>	<b>794,699</b>		<b>1,121,358</b>
<b>Derivative financial instruments – foreign exchange forward contracts:</b>				
Other current assets		30,935		30,935
Accrued expenses and other current liabilities		(126,731)		(126,731)
Other noncurrent liabilities		(259,104)		(259,104)
<b>Total</b>	<b>\$ 454,663</b>	<b>\$ 464,708</b>	<b>\$</b>	<b>\$ 919,371</b>

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, 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 six months ended June 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 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. 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

Edgar Filing: COGNIZANT TECHNOLOGY SOLUTIONS CORP - Form 10-Q

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.

**Table of Contents**

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	June 30, 2012		December 31, 2011	
		Assets	Liabilities	Assets	Liabilities
<b>Cash Flow Hedges Designated as hedging instruments</b>					
Foreign exchange forward contracts	Accrued expenses and other current liabilities	\$	\$ 164,546	\$	\$ 126,536
	Other noncurrent liabilities		309,629		259,104
	<b>Total</b>		<b>474,175</b>		<b>385,640</b>
<b>Other Derivatives Not designated as hedging instruments</b>					
Foreign exchange forward contracts	Other current assets	11,000		30,935	
	Accrued expenses and other current liabilities		183		195
	<b>Total</b>	<b>11,000</b>	<b>183</b>	<b>30,935</b>	<b>195</b>
<b>Total</b>		<b>\$ 11,000</b>	<b>\$ 474,358</b>	<b>\$ 30,935</b>	<b>\$ 385,835</b>

*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 June 30, 2012, we estimate that \$137,670 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:

	June 30, 2012	December 31, 2011
2012	\$ 634,500	\$ 1,193,500
2013	1,217,000	1,080,000
2014	1,170,000	810,000
2015	660,000	420,000
2016	120,000	
<b>Total notional value of contracts outstanding</b>	<b>\$ 3,801,500</b>	<b>\$ 3,503,500</b>
<b>Net unrealized loss included in accumulated other comprehensive income (loss), net of taxes</b>	<b>\$ (396,725)</b>	<b>\$ (323,039)</b>

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



**Table of Contents**

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 June 30:

	<b>Location of Net Derivative Gains</b>			
	<b>Increase (decrease) in Derivative Gains (Losses) Recognized in Accumulated Other Comprehensive Income (Loss) (effective portion)</b>		<b>(Losses) Reclassified from Accumulated Other Comprehensive Income (Loss) into Income (effective portion)</b>	
	<b>2012</b>	<b>2011</b>	<b>Net Gain (Loss) Reclassified from Accumulated Other Comprehensive Income (Loss) into Income (effective portion)</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
Cash Flow Hedges Designated as hedging instruments				