

INFOSYS TECHNOLOGIES LTD

Form 6-K

October 24, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington , D.C. 20549

FORM 6-K

Report of Foreign Private Issuer

Pursuant to Rule 13a-16 or 15d-16 of the Securities Exchange Act of 1934

For the quarter ended September 30, 2006

Commission File Number: 000-25383

INFOSYS TECHNOLOGIES LIMITED

(Exact name of Registrant as specified in its charter)

Not Applicable

(Translation of Registrant's name into English)

Bangalore , Karnataka, India

(Jurisdiction of incorporation or organization)

Electronics City, Hosur Road, Bangalore, Karnataka, India 560 100. 80-2852-0261

(Address of principal executive offices)

Indicate by check mark registrant files or will file annual reports under cover Form 20-F or Form 40-F.

Form 20-F Form 40-F

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g 3-2(b) under the Securities Exchange Act of 1934

Yes No

If Yes is marked, indicate below the file number assigned to registrant in connection with Rule 12g 3-2(b).

Not Applicable

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Currency of Presentation and Certain Defined Terms

In this Report, references to U.S. or United States are to the United States of America, its territories and its possessions. References to India are to the Republic of India. References to \$ or dollars or U.S. dollars are to the currency of the United States and references to Rs. or rupees or Indian rupees are to the legal currency of India. Our financial statements are presented in Indian rupees and translated into U.S. dollars and are prepared in accordance with United States Generally Accepted Accounting Principles, or U.S. GAAP. References to Indian GAAP are to Indian Generally Accepted Accounting Principles. References to a particular fiscal year are to our fiscal year ended March 31 of such year.

All references to we, us, our, Infosys or the Company shall mean Infosys Technologies Limited, and, unless specifically indicated otherwise or the context indicates otherwise, our consolidated subsidiaries. Infosys is a registered trademark of Infosys Technologies Limited in the United States and India. All other trademarks or tradenames used in this Report are the property of their respective owners.

Except as otherwise stated in this Report, all translations from Indian Rupees to U.S. dollars are based on the noon buying rate in the City of New York on September 29, 2006, for cable transfers in Indian rupees as certified for customs purposes by the Federal Reserve Bank of New York which was Rs. 45.95 per \$1.00. September 29, 2006 was the last day of the quarter ended September 30, 2006 for which the noon buying rate is available. No representation is made that the Indian rupee amounts have been, could have been or could be converted into U.S. dollars at such a rate or any other rate. Any discrepancies in any table between totals and sums of the amounts listed are due to rounding.

Information contained in our website, www.infosys.com, is not part of this Report.

Cautionary Note regarding Forward-Looking Statements

In addition to historical information, this Report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The forward-looking statements contained herein are subject to certain risks and uncertainties that could cause actual results to differ materially from those reflected in the forward-looking statements. Factors that might cause such differences include but are not limited to, those discussed in the section entitled Risk Factors and elsewhere in this Report, as well as the sections entitled Risk Factors in our Annual Report on Form 20-F for the fiscal year ended March 31, 2006 and our Report on Form 6-K for the three months ended June 30, 2006. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's analysis only as of the date of this Report. In addition, readers should carefully review the other information in this Report and in the Company's periodic reports and other documents filed with the Securities and Exchange Commission (SEC) from time to time.

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	March 31, 2006 (1)	As of September 30, 2006
ASSETS		
<i>Current Assets</i>		
Cash and cash equivalents	\$ 889	\$ 328
Investments in liquid mutual fund units	170	615
Trade accounts receivable, net of allowances	361	454
Unbilled revenue	48	74
Prepaid expenses and other current assets	40	49
Deferred tax assets	1	2
<i>Total current assets</i>	1,509	1,522
Property, plant and equipment, net	491	540
Goodwill	8	91
Intangible assets, net		18
Deferred tax assets	13	13
Advance income taxes	18	5
Other assets	27	31
Total Assets	\$ 2,066	\$ 2,220
LIABILITIES AND STOCKHOLDERS EQUITY		
<i>Current Liabilities</i>		
Accounts payable	\$ 3	\$ 4
Income taxes payable		2
Client deposits	2	2
Unearned revenue	44	67
Other accrued liabilities	160	183
<i>Total current liabilities</i>	209	258
<i>Non-current liabilities</i>		
Other non-current liabilities	5	5
Minority interests	15	2
<i>Stockholders Equity</i>		
Common stock, \$0.16 par value 600,000,000 equity shares authorized, Issued and outstanding 551,109,960 and 555,785,001 as of March 31, 2006 and September 30, 2006, respectively	31	62
Additional paid-in capital	410	477
Accumulated other comprehensive income	9	(49)
Retained earnings	1,387	1,465

Total stockholders' equity	1,837		1,955
Total Liabilities And Stockholders' Equity	\$ 2,066	\$	2,220

(1) March 31, 2006 balances were obtained from audited financial statements
See accompanying notes to the unaudited consolidated financial statements

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Table of Contents**Infosys Technologies Limited and subsidiaries
Unaudited Consolidated Statements of Income***(Dollars in millions except per share data)*

	Three months ended September 30,		Six months ended September 30					
	2005	2006	2005 (2)	2006				
Revenues	\$	524	\$	746	\$	1,000	\$	1,406
Cost of revenues		297		423		571		812
Gross profit		227		323		429		594
Operating Expenses:								
Selling and marketing expenses		35		48		67		93
General and administrative expenses		46		63		83		119
Amortization of intangible assets				1				1
Total operating expenses		81		112		150		213
Operating income		146		211		279		381
Gain on sale of long term investment								1
Other income, net		9		14		16		42
Income before income taxes and minority interest		155		225		295		424
Provision for income taxes		16		26		34		49
Income before minority interest		139		199		261		375
Minority interest		1				1		2
Net income	\$	138	\$	199	\$	260	\$	373
Earnings per equity share								
Basic	\$	0.25	\$	0.36	\$	0.48	\$	0.68
Diluted	\$	0.25	\$	0.35	\$	0.47	\$	0.66
Weighted average equity shares used in computing earnings per equity share								
Basic		541,375,238		551,938,696		540,269,462		550,964,911
Diluted		556,608,116		564,858,570		555,390,222		563,832,673

(2) Six months ended September 30, 2005 figures were obtained from audited financial statements.
See accompanying notes to the unaudited consolidated financial statements

Table of Contents**Infosys Technologies Limited and subsidiaries****Unaudited Consolidated Statements of Stockholders Equity and Comprehensive Income***(Dollars in millions)*

	Common stock Shares	Common stock Par value	Additional paid-in capital	Comprehensive income	Accumulated other comprehensive income	Retained earnings	Total stockholders equity
Balance as of March 31, 2005	541,141,098	\$ 31	\$ 266		\$ 33	\$ 923	\$ 1,253
Common stock issued	4,177,926		57				57
Cash dividends						(46)	(46)
Change in proportionate share of subsidiary resulting from issuance of stock by subsidiary			12				12
Comprehensive income							
Net income				\$ 260		260	260
Other comprehensive income							
Unrealized gain on mutual fund investments, net of taxes				1	1		1
Translation adjustment				(9)	(9)		(9)
Comprehensive income				\$ 252			
Balance as of September 30, 2005(3)	545,319,024	\$ 31	\$ 335		\$ 25	\$ 1,137	\$ 1,528
Balance as of March 31, 2006	551,109,960	\$ 31	\$ 410		\$ 9	\$ 1,387	\$ 1,837
Common stock issued	4,675,041	1	62				63
Cash dividends						(265)	(265)
Stock compensation expenses			2				2

Income tax benefit arising on exercise of stock options			3				3				
Stock split effected in the form of a stock dividend	30				(30)						
Comprehensive income											
Net income			\$	373		373	373				
Other comprehensive income											
Translation adjustment				(58)	(58)		(58)				
Comprehensive income			\$	315							
Balance as of											
September 30, 2006	555,785,001	\$	62	\$	477	\$	(49)	\$	1,465	\$	1,955

(3) Activity for the six months period ended September 30, 2005 has been obtained from the audited financial statements.

See accompanying notes to the unaudited consolidated financial statements

Table of Contents**Infosys Technologies Limited and subsidiaries
Unaudited Consolidated Statements of Cash Flows***(Dollars in millions)*

	Six months ended September 30,	
	2005 (4)	2006
Operating Activities:		
Net income	\$ 260	\$ 373
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	40	51
Minority interest		2
Stock compensation expenses		2
Deferred taxes	(2)	(3)
Others		(3)
Changes in assets and liabilities		
Trade accounts receivable	(3)	(104)
Prepaid expenses and other current assets	(1)	(10)
Unbilled revenue	(9)	(27)
Accounts payable		1
Income taxes	(2)	16
Client deposits	(4)	
Unearned revenue	20	24
Other accrued liabilities	5	27
Net cash provided by operating activities	304	349
Investing Activities:		
Expenditure on property, plant and equipment	(127)	(114)
Acquisition of minority interest in subsidiary		(116)
Investment in liquid mutual fund units	(371)	(651)
Redemption of liquid mutual fund units	115	201
Non-current deposits placed with corporations	(9)	(11)
Withdrawal of non-current deposits placed with corporations	1	2
Loans to employees	(1)	2
Others		1
Net cash used in investing activities	(392)	(686)
Financing Activities:		
Proceeds from issuance of common stock on exercise of employee stock options	57	63
Payment of dividends	(46)	(265)
Others		2
Net cash provided by / (used in) financing activities	11	(200)

Effect of exchange rate changes on cash	1	(24)
Net decrease in cash and cash equivalents during the period	(76)	(561)
Cash and cash equivalents at the beginning of the period	410	889
Cash and cash equivalents at the end of the period	\$ 334	\$ 328

Supplementary information:

Cash paid towards taxes	\$ 38	\$ 37
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(4) Six months ended September 30, 2005 cash flows were obtained from audited financial statements

See accompanying notes to the unaudited consolidated financial statements

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Infosys Technologies Limited and subsidiaries
Notes to the Unaudited Consolidated Financial Statements
1 Company overview and significant accounting policies

1.1 Company overview

Infosys Technologies Limited (Infosys), along with its majority owned and controlled subsidiary, Infosys BPO Limited (Infosys BPO), formerly Progeon Limited and wholly-owned subsidiaries Infosys Technologies (Australia) Pty. Limited (Infosys Australia), Infosys Technologies (China) Co. Limited (Infosys China), formerly Infosys Technologies (Shanghai) Co. Limited and Infosys Consulting Inc. (Infosys Consulting) is a leading global technology services firm. The company provides end-to-end business solutions that leverage technology. The company provides solutions that span the entire software life cycle encompassing consulting, design, development, software re-engineering, maintenance, systems integration, package evaluation and implementation and infrastructure management services. In addition, the company offers software products for the banking industry and business process management services.

1.2 Basis of preparation of financial statements and consolidation

The consolidated financial statements include Infosys and its subsidiaries (the company) and are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). Infosys consolidates entities in which it owns or controls more than 50% of the voting shares. The results of acquired businesses are included in the consolidated financial statements from the date of acquisition. Inter-company balances and transactions are eliminated on consolidation.

Unaudited interim information presented in the consolidated financial statements has been prepared by management and, in the opinion of management, includes all adjustments of a normal recurring nature that are necessary for the fair presentation of the financial position, results of operations and cash flows for the periods shown, and is in accordance with GAAP. These financial statements should be read in conjunction with the consolidated financial statements and related notes included in the company's annual report on Form 20-F for the fiscal year ended March 31, 2006.

1.3 Use of estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates and assumptions are used for, but not limited to, accounting for costs and efforts expected to be incurred to complete performance under software development arrangements, allowance for uncollectible accounts receivable, future obligations under employee benefit plans, provisions for post-sales customer support, the useful lives of property, plant, equipment and intangible assets and income tax valuation allowances. Actual results could differ from those estimates. Appropriate changes in estimates are made as management becomes aware of changes in circumstances surrounding the estimates. Changes in estimates are reflected in the financials statements in the period in which changes are made and, if material, their effects are disclosed in the notes to the consolidated financial statements.

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The company derives revenues primarily from software development and related services, licensing of software products and from business process management services. Arrangements with customers for software development and related services are either on a fixed-price, fixed-timeframe or on a time and material basis.

Revenue on time-and-material contracts is recognized as the related services are performed and revenue from the end of the last billing to the balance sheet date is recognized as unbilled revenues. Revenue from fixed-price, fixed-timeframe contracts is recognized as per the percentage-of-completion method. Guidance has been drawn from paragraph 95 of Statement of Position (SOP) 97-2, Software Revenue Recognition, to account for revenue from fixed price arrangements for software development and related services in conformity with SOP 81-1. The input (efforts expended) method has been used to measure progress towards completion as there is a direct relationship between input and productivity. Provisions for estimated losses, if any, on uncompleted contracts are recorded in the period in which such losses become probable based on the current contract estimates. Costs and earnings in excess of billings are classified as unbilled revenue while billings in excess of costs and earnings are classified as unearned revenue. Maintenance revenue is recognized ratably over the term of the underlying maintenance agreement.

The company provides its clients with a fixed-period warranty for corrections of errors and telephone support on all its fixed-price, fixed-timeframe contracts. Costs associated with such support services are accrued at the time related revenues are recorded and included in cost of revenues. The company estimates such costs based on historical experience and estimates are reviewed on a periodic basis for any material changes in assumptions and likelihood of occurrence.

In accordance with SOP 97-2, license fee revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred, the license fee is fixed and determinable, and the collection of the fee is probable.

Arrangements to deliver software products generally have three elements: license, implementation and Annual Technical Services (ATS). The company has applied the principles in SOP 97-2 to account for revenue from these multiple element arrangements. Vendor specific objective evidence of fair value (VSOE) has been established for ATS. VSOE is the price charged when the element is sold separately. When other services are provided in conjunction with the licensing arrangement, the revenue from such contracts are allocated to each component of the contract using the residual method, whereby revenue is deferred for the undelivered services and the residual amounts are recognized as revenue for delivered elements. In the absence of an established VSOE for implementation, the entire arrangement fee for license and implementation is recognized as the implementation is performed. Revenue from client training, support and other services arising due to the sale of software products is recognized as the services are performed. ATS revenue is recognized ratably over the period in which the services are rendered.

Revenues from business process management and other services are recognized on both, the time-and-material and fixed-price, fixed-timeframe basis. Revenue on time-and-material contracts is recognized as the related services are rendered. Revenue from fixed-price, fixed-timeframe contracts is recognized as per the proportional performance method using an output measure of performance.

When the company receives advances for services and products, such amounts are reported as client deposits until all conditions for revenue recognition are met.

The company accounts for volume discounts and pricing incentives to customers using the guidance in EITF Issue 01-09, Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products). The discount terms in the company's arrangements with customers generally entitle the customer to discounts if the customer completes a specified cumulative level of revenue transactions. In some arrangements, the level of discount varies with increases in the levels of revenue transactions. The discounts are passed on to the customer either as check payments or as a reduction of payments due from the customer. The company recognizes discount obligations as a reduction of revenue based on the ratable

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allocation of the discount to each of the underlying revenue transactions that result in progress by the customer toward earning the discount. The company recognizes the liability based on its estimate of the customer's future purchases. Also, when the level of discount varies with increase in levels of revenue transactions, the company recognizes the liability based on its estimate of the customer's future purchases. If the company cannot reasonably estimate the customer's future purchases, then the liability is recorded based on the maximum potential level of discount. The company recognizes changes in the estimated amount of obligations for discounts using a cumulative catch-up adjustment. Furthermore, the company does not recognize any revenue up front for breakages immediately on the inception of an arrangement.

1.5 Cash and cash equivalents

The company considers all highly liquid investments with a remaining maturity at the date of purchase / investment of three months or less and that are readily convertible to known amounts of cash to be cash equivalents. Cash and cash equivalents comprise cash and cash on deposit with banks, and corporations.

1.6 Investments

Investments in non-readily marketable equity securities of other entities where the company is unable to exercise significant influence and for which there are no readily determinable fair values are recorded at cost. Declines in value judged to be other than temporary are included in earnings.

Investment securities designated as available for sale are carried at their fair value. Fair value is based on quoted market prices. Temporary unrealized gains and losses, net of the related tax effect are reported as a separate component of stockholders' equity until realized. Realized gains and losses and declines in value judged to be other than temporary on available for sale securities are included in earnings.

The cost of securities sold is based on the specific identification method. Interest and dividend income are recognized when earned.

1.7 Property, plant and equipment

Property, plant and equipment are stated at cost, less accumulated depreciation. The company depreciates property, plant and equipment over their estimated useful lives using the straight-line method. The estimated useful lives of assets are as follows:

Buildings	15 years	Vehicles	5 years
Plant and equipment	5 years	Computer equipment	2-5 years
Furniture and fixtures	5 years		

The cost of software purchased for internal use is accounted for under SOP 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use. Deposits paid towards the acquisition of long lived assets that are outstanding at each balance sheet date and the cost of assets not put to use before such date are disclosed under Capital work-in-progress. Costs of improvements that substantially extend the useful life of particular assets are capitalized. Repairs and maintenance cost are charged to earnings when incurred. The cost and related accumulated depreciation are removed from the consolidated financial statements upon sale or disposition of the asset.

The company evaluates the recoverability of these assets whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying value of the assets exceeds the fair value of

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the assets. Assets to be disposed are reported at the lower of the carrying value or the fair value less the cost to sell.

1.8 Business combinations

Business combinations have been accounted using the purchase method under the provisions of Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standard (SFAS) No. 141, Business Combinations. Cash and amounts of consideration that are determinable at the date of acquisition are included in determining the cost of the acquired business.

1.9 Goodwill

Goodwill represents the cost of the acquired businesses in excess of the fair value of identifiable tangible and intangible net assets purchased. Goodwill is tested for impairment on an annual basis, relying on a number of factors including operating results, business plans and future cash flows. Recoverability of goodwill is evaluated using a two-step process. The first step involves a comparison of the fair value of a reporting unit with its carrying value. If the carrying amount of the reporting unit exceeds its fair value, the second step of the process involves a comparison of the fair value and carrying value of the goodwill of that reporting unit. If the carrying value of the goodwill of a reporting unit exceeds the fair value of that goodwill, an impairment loss is recognized in an amount equal to the excess. Goodwill of a reporting unit is tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying amount.

1.10 Intangible assets

Intangible assets are amortized over their respective individual estimated useful lives on a straight-line basis. The estimated useful life of an identifiable intangible asset is based on a number of factors including the effects of obsolescence, demand, competition, and other economic factors (such as the stability of the industry, and known technological advances), and the level of maintenance expenditures required to obtain the expected future cash flows from the asset.

Intangible assets are evaluated for recoverability whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying value of the assets exceeds the fair value of the assets.

1.11 Research and development

Research and development costs are expensed as incurred. Software product development costs are expensed as incurred until technological feasibility is achieved. Research and development costs and software development costs incurred under contractual arrangements with customers are accounted for as cost of revenues.

1.12 Foreign currency

The functional currency of the company and Infosys BPO is the Indian rupee (Rs.). The functional currency for Infosys Australia, Infosys China and Infosys Consulting is the respective local currency. The consolidated financial statements are reported in U.S. dollars. The translation of Rs. to U.S. dollars is performed for balance sheet accounts using the exchange rate in effect at the balance sheet date and for revenue, expense and cash-flow items using a monthly average exchange rate for the respective periods. The gains or losses resulting from such translation are included in Other comprehensive income, a separate

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component of stockholders' equity. The translation of the financial statements of foreign subsidiaries from the local currency to the functional currency of the company is also performed on the same basis.

Foreign-currency denominated assets and liabilities are translated into the functional currency at exchange rates in effect at the balance sheet date. The gains or losses resulting from such translation are included in earnings.

Transaction gains or losses realized upon settlement of foreign currency transactions are included in determining net income for the period in which the transaction is settled. Revenue, expense and cash-flow items denominated in foreign currencies are translated into the functional currency using the exchange rate in effect on the date of the transaction.

1.13 Earnings per share

Basic earnings per share is computed by dividing net income for the period by the weighted average number of equity shares outstanding during the period. Diluted earnings per share is computed by dividing net income by the diluted weighted average number of equity shares outstanding during the period. Diluted earnings per share reflect the potential dilution from equity shares issuable through employee stock options. The dilutive effect of employee stock options is reflected in diluted earnings per share by application of the treasury stock method. The dilutive effect of convertible securities is reflected in diluted earnings per share by application of the if-converted method. If securities have been issued by a subsidiary that enable their holders to obtain the subsidiary's common stock, the earnings of the subsidiary shall be included in the consolidated diluted earnings per share computations based on the consolidated group's holding of the subsidiary's securities.

If the number of common shares outstanding increases as a result of a stock dividend or stock split or decreases as a result of a reverse stock split, the computations of basic and diluted earnings per share are adjusted retroactively for all periods presented to reflect that change in capital structure. If such changes occur after the close of the reporting period but before issuance of the financial statements, the per-share computations for that period and any prior-period financial statements presented are based on the new number of shares.

1.14 Income taxes

Income taxes are accounted for using the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities, and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of changes in tax rates on deferred tax assets and liabilities is recognized as income or expense in the period that includes the enactment date. The measurement of deferred tax assets is reduced, if necessary, by a valuation allowance for any tax benefits of which future realization is not more likely than not. Changes in valuation allowance from period to period are reflected in the income statement of the period of change. Deferred taxes are not provided on the undistributed earnings of subsidiaries outside India where it is expected that the earnings of the foreign subsidiary will be permanently reinvested. Tax benefits of deductions earned on exercise of employee stock options in excess of compensation charged to earnings are credited to additional paid in capital. The income tax provision for the interim period is based on the best estimate of the effective tax rate expected to be applicable for the full fiscal year.

1.15 Fair value of financial instruments

In determining the fair value of its financial instruments, the company uses a variety of methods and assumptions that are based on market conditions and risks existing at each balance sheet date. The methods used to determine fair value include discounted cash flow analysis and dealer quotes. All methods of assessing fair value result in general approximation of value, and such value may never actually be realized.

Table of Contents***1.16 Concentration of risk***

Financial instruments that potentially subject the company to concentrations of credit risk consist principally of cash equivalents, trade accounts receivable, investment securities and hedging instruments. By nature, all such financial instruments involve risk, including the credit risk of non-performance by counterparties. In management's opinion, as of March 31, 2006 and September 30, 2006 there was no significant risk of loss in the event of non-performance of the counterparties to these financial instruments, other than the amounts already provided for in the financial statements, if any. Exposure to credit risk is managed through credit approvals, establishing credit limits and monitoring procedures. The factors which affect the fluctuations in the company's provisions for bad debts and write offs for uncollectible accounts include the financial health and economic environment of the clients. The company specifically identifies the potential credit loss and then makes the provision. The company's cash resources are invested with corporations, financial institutions and banks with high investment grade credit ratings. Limits are established by the company as to the maximum amount of cash that may be invested with any such single entity.

1.17 Derivative financial instruments

The company uses derivative financial instruments such as foreign exchange forward and option contracts to mitigate the risk of changes in foreign exchange rates on accounts receivable and forecasted cash flows denominated in certain foreign currencies. The counterparty for these contracts is generally a bank. Although the company believes that these financial instruments constitute hedges from an economic perspective, they do not qualify for hedge accounting under SFAS 133, as amended. Any derivative that is either not designated a hedge, or is so designated but is ineffective per SFAS 133, is marked to market and recognized in earnings immediately and included in other income, net.

1.18 Retirement benefits to employees***1.18.1 Gratuity***

In accordance with the Payment of Gratuity Act, 1972, Infosys provides for gratuity, a defined benefit retirement plan (the Gratuity Plan) covering eligible employees. The Gratuity Plan provides a lump-sum payment to vested employees at retirement, death, incapacitation or termination of employment, of an amount based on the respective employee's salary and the tenure of employment.

Liabilities with regard to the Gratuity Plan are determined by actuarial valuation. The company fully contributes all ascertained liabilities to the Infosys Technologies Limited Employees' Gratuity Fund Trust (the Trust). In case of Infosys BPO, contributions are made to the Infosys BPO's Employees' Gratuity Fund Trust. Trustees administer contributions made to the Trusts and contributions are invested in specific designated instruments as permitted by law and investments are also made in mutual funds that invest in the specific designated instruments.

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1.18.2 Superannuation

Certain employees of Infosys are also participants in a defined contribution plan. Until March 2005, the company made monthly contributions under the superannuation plan (the Plan) to the Infosys Technologies Limited Employees Superannuation Fund Trust based on a specified percentage of each covered employee's salary. The company has no further obligations to the Plan beyond its monthly contributions. Certain employees of Infosys BPO Ltd are also eligible for superannuation benefit. Infosys BPO makes monthly provisions under the superannuation plan based on a specified percentage of each covered employee's salary. Infosys BPO has no further obligations to the superannuation plan beyond its monthly provisions which are periodically contributed to a trust fund, the corpus of which is invested with the Life Insurance Corporation of India.

Effective April 1, 2005, a portion of the monthly contribution amount was paid directly to the employees as an allowance and the balance amount was contributed to the trusts.

1.18.3 Provident fund

Eligible employees of Infosys receive benefits from a provident fund, which is a defined contribution plan. Both the employee and the company make monthly contributions to the provident fund plan equal to a specified percentage of the covered employee's salary. The company contributes a part of the contributions to the Infosys Technologies Limited Employees Provident Fund Trust. The remaining portion is contributed to the government administered pension fund. The rate at which the annual interest is payable to the beneficiaries by the trust is being administered by the government. The company has an obligation to fund any shortfall on the yield of the trust's investments over the administered interest rates.

In respect of Infosys BPO, eligible employees receive benefits from a provident fund, which is a defined contribution plan. Both the employee and Infosys BPO make monthly contributions to this provident fund plan equal to a specified percentage of the covered employee's salary. Amounts collected under the provident fund plan are deposited in a government administered provident fund.

1.19 Stock-based compensation

Until March 31, 2006, the company applied the intrinsic value-based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations including FASB Interpretation No. 44, Accounting for Certain Transactions involving Stock Compensation an interpretation of APB Opinion No. 25, issued in March 2000, to account for its fixed stock option plans. Under this method, compensation expense was recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. SFAS 123, Accounting for Stock-Based Compensation, established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS 123, the Company elected to continue to apply the intrinsic value-based method of accounting described above, and adopted the disclosure requirements of SFAS 148, Accounting for Stock-Based Compensation Transition and Disclosure, an amendment of FASB Statement No. 123 until March 2006.

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The following table illustrates the effect on net income and earnings per share for the three months ended and six months ended September 30, 2005 and if the company had applied the fair value recognition provisions of SFAS Statement No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation.

(Dollars in millions except per share data)

	Three months ended September 30, 2005	Six months ended September 30, 2005
Net income, as reported	\$ 138	\$ 260
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(3)	(7)
Pro forma net income	\$ 135	\$ 253
Earnings per share:		
Basic as reported	\$ 0.25	\$ 0.48
Basic pro forma	\$ 0.25	\$ 0.47
Diluted as reported	\$ 0.25	\$ 0.47
Diluted pro forma	\$ 0.24	\$ 0.46

From April 1, 2006, the company adopted FASB Statement No.123 (revised 2004), *Share-Based Payment* using the modified prospective approach. The company recorded stock compensation expense of \$1 million during the three months ended September 30, 2006 and \$2 million during the six months ended September 30, 2006, using the fair value recognition provisions.

The impact on the company's financial statements for the three months ended and six months ended September 30, 2006 due to the adoption of FASB Statement No.123 (revised 2004), *Share Based Payment* using the modified prospective approach is given below.

(Dollars in millions)

Details	Three months ended September 30, 2006	Six months ended September 30, 2006
Operating income	(1)	(2)
Income before income taxes and minority interest	(1)	