

Infosys Technologies Limited and subsidiary
Consolidated balance sheets as of March 31,

	2002	2003
ASSETS		
<i>Current Assets</i>		
Cash and cash equivalents	\$210,485,940	\$354,362,918
Trade accounts receivable, net of allowances	69,017,110	109,119,856
Deferred tax assets	774,107	288,541
Prepaid expenses and other current assets	15,239,915	24,384,316
Unbilled revenue	3,635,989	19,702,186
<i>Total current assets</i>	299,153,061	507,857,817
Property, plant and equipment, net	147,211,731	157,194,190
Intangible assets, net	–	6,471,236
Deferred tax assets	4,560,934	7,264,885
Investments	7,777,393	4,613,833
Prepaid income taxes	–	4,452,678
Other assets	12,458,615	16,454,328
TOTAL ASSETS	\$471,161,734	\$704,308,967
LIABILITIES AND STOCKHOLDERS' EQUITY		
<i>Current Liabilities</i>		
Accounts payable	–	\$426,611
Client deposits	\$2,215,001	3,208,295
Other accrued liabilities	22,424,646	46,249,269
Income taxes payable	678,703	–
Unearned revenue	3,464,018	13,202,115
<i>Total current liabilities</i>	28,782,368	63,086,290
<i>Non-current liabilities</i>	–	5,217,758
<i>Preferred stock of subsidiary</i>		
0.0005% Cumulative Convertible Preference Shares, par value \$2 each, 4,375,000 preference shares Authorized, issued and outstanding – 4,375,000 preference shares as of March 31, 2003	–	10,000,000
<i>Stockholders' Equity</i>		
Common stock, \$0.16 par value 100,000,000 equity shares authorized, Issued and outstanding – 66,186,130 and 66,243,078 as of March 31, 2002 and 2003, respectively	8,597,001	8,602,909
Additional paid-in capital	123,079,948	127,042,751
Accumulated other comprehensive income	(45,441,148)	(31,444,835)
Deferred stock compensation	(7,620,600)	(2,817,066)
Retained earnings	363,764,165	524,621,160
Total stockholders' equity	442,379,366	626,004,919
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$471,161,734	\$704,308,967

See accompanying notes to the consolidated financial statements

Infosys Technologies Limited and subsidiary
 Consolidated statements of income for the years ended March 31,

	2001	2002	200
Revenues	\$413,850,510	\$545,051,214	\$753,807,025
Cost of revenues (including amortization of stock compensation expenses of \$3,162,283, \$2,999,457 and \$2,818,887)	216,776,027	293,031,689	417,359,025
Gross profit	197,074,483	252,019,525	336,448,000
Operating Expenses:			
Selling and marketing expenses	20,682,776	27,113,122	55,649,913
General and administrative expenses	36,957,609	44,348,181	57,808,445
Amortization of stock compensation expenses	1,919,512	2,010,315	1,984,647
Amortization of intangible assets	–	–	2,360,799
Total operating expenses	59,559,897	73,471,618	117,803,804
Operating income	137,514,586	178,547,907	218,644,196
Other income, net	9,505,343	13,865,294	18,048,110
Income before income taxes	147,019,929	192,413,201	236,692,306
Provision for income taxes	15,071,825	27,946,892	41,822,265
Net income	\$131,948,104	\$164,466,309	\$194,870,041
Earnings per equity share			
Basic	\$2.01	\$2.51	\$2.97
Diluted	\$1.98	\$2.49	\$2.93
Weighted equity shares used in computing earnings per equity share			
Basic	65,771,256	65,556,648	65,571,002
Diluted	66,714,739	66,084,874	66,479,009

See accompanying notes to the consolidated financial statements

Infosys Technologies Limited and subsidiary

Consolidated statements of stockholders' equity and comprehensive income

	Common stock		Additional paid-in capital	Comprehensive income	Accumulated other comprehensive income	Deferred stock compensation	Retained earnings	Total stockholders' equity
	Shares	Par value						
Balance as of March 31, 2000	66,150,700	\$8,593,510	\$121,506,726		\$(14,137,933)	\$(17,598,813)	\$99,773,031	\$198,136,521
Cash dividends declared	-	-	-	-	-	-	(9,359,068)	(9,359,068)
Common stock issued	7,417	596	510,792	-	-	-	-	511,388
Amortization of compensation related to stock option grants	-	-	-	-	-	5,081,795	-	5,081,795
Comprehensive income	-	-	-	\$131,948,104	-	-	131,948,104	131,948,104
Net income	-	-	-	\$131,948,104	-	-	131,948,104	131,948,104
Other comprehensive income	-	-	-	(14,527,039)	(14,527,039)	-	-	(14,527,039)
Translation adjustment	-	-	-	(14,527,039)	(14,527,039)	-	-	(14,527,039)
Comprehensive income	-	-	-	\$117,421,065	-	-	-	\$117,421,065
Balance as of March 31, 2001	66,158,117	\$8,594,106	\$122,017,518	\$(28,664,972)	\$(12,517,018)	\$222,362,067	\$311,791,701	\$311,791,701
Common stock issued	28,013	2,895	949,076	-	-	-	-	951,971
Cash dividends declared	-	-	-	-	-	-	(23,064,211)	(23,064,211)
Deferred stock compensation related to stock option grants	-	-	113,354	-	-	(113,354)	-	-
Amortization of compensation related to stock option grants	-	-	-	-	-	5,009,772	-	5,009,772
Comprehensive income	-	-	-	\$164,466,309	-	-	164,466,309	164,466,309
Net income	-	-	-	\$164,466,309	-	-	164,466,309	164,466,309
Other comprehensive income	-	-	-	(16,776,176)	(16,776,176)	-	-	(16,776,176)
Translation adjustment	-	-	-	(16,776,176)	(16,776,176)	-	-	(16,776,176)
Comprehensive income	-	-	\$147,690,133	-	-	-	-	\$147,690,133
Balance as of March 31, 2002	66,186,130	\$8,597,001	\$123,079,948	\$(45,441,148)	\$(7,620,600)	\$363,764,165	\$442,379,366	\$442,379,366
Common stock issued	56,948	5,908	2,799,780	-	-	-	-	2,805,688
Cash dividends declared	-	-	-	-	-	-	(34,013,046)	(34,013,046)
Income tax benefit arising on exercise of stock options	-	-	1,163,023	-	-	-	-	1,163,023
Amortization of compensation related to stock option grants	-	-	-	-	-	4,803,534	-	4,803,534
Comprehensive income	-	-	-	194,870,041	-	-	194,870,041	194,870,041
Net income	-	-	-	194,870,041	-	-	194,870,041	194,870,041
Other comprehensive income	-	-	-	-	-	-	-	-
Translation adjustment	-	-	-	13,996,313	13,996,313	-	-	13,996,313
Comprehensive income	-	-	\$208,866,354	-	-	-	-	\$208,866,354
Balance as of March 31, 2003	66,243,078	\$8,602,909	\$127,042,751	\$(31,444,835)	\$(2,817,066)	\$524,621,160	\$626,004,919	\$626,004,919

See accompanying notes to the consolidated financial statements

Infosys Technologies Limited and subsidiary
Consolidated statements of cash flows for the years ended March 31,

	2001	2002	2003
OPERATING ACTIVITIES:			
Net income	\$131,948,104	\$164,466,309	\$194,870,041
Adjustments to reconcile net income to net cash provided by operating activities			
Gain on sale of property, plant and equipment	(20,053)	(16,754)	(2,070)
Depreciation	24,527,867	33,608,391	37,023,974
Amortization of intangible assets	–	–	2,360,799
Provision for investments	3,480,300	–	3,219,030
Deferred tax benefit	(769,304)	(1,999,471)	(2,418,210)
Amortization of stock compensation expenses	5,081,795	5,009,772	4,803,534
Changes in assets and liabilities			
Trade accounts receivable	(36,310,272)	(7,196,700)	(37,657,569)
Prepaid expenses and other current assets	(2,150,772)	1,079,574	(5,236,301)
Unbilled revenue	(503,694)	(3,132,295)	(15,436,197)
Income taxes	(1,973,114)	869,109	(3,922,235)
Accounts payable	(901,961)	(27,382)	419,750
Client deposits	833,215	1,075,855	919,545
Unearned revenue	3,770,772	(3,753,943)	9,491,122
Other accrued liabilities	9,651,967	1,492,616	22,756,370
Net cash provided by operating activities	136,664,850	191,475,081	211,191,583
INVESTING ACTIVITIES:			
Expenditure on property, plant and equipment	(101,235,420)	(68,347,644)	(43,157,754)
Expenditure on intangible assets	–	–	(3,551,433)
Proceeds from sale of property, plant and equipment	49,676	335,079	70,383
Loans to employees	(4,932,703)	(5,547,203)	(7,249,008)
Purchase of investments	(5,879,755)	(2,200,000)	(54,378)
Net cash used in investing activities	(111,998,202)	(75,759,768)	(53,942,190)
FINANCING ACTIVITIES:			
Proceeds from issuance of common stock	511,388	963,351	2,805,688
Proceeds from issuance of preferred stock by subsidiary	–	–	10,000,000
Payment of dividends	(9,220,142)	(22,902,618)	(33,913,973)
Net cash used in financing activities	(8,708,754)	(21,939,267)	(21,108,285)
Effect of exchange rate changes on cash	(8,473,135)	(7,374,351)	7,735,870
Net increase in cash and cash equivalents during the period	7,484,759	86,401,695	143,876,978
Cash and cash equivalents at the beginning of the period	116,599,486	124,084,245	210,485,940
Cash and cash equivalents at the end of the period	\$124,084,245	\$210,485,940	\$354,362,918
Supplementary information:			
Cash paid towards taxes	\$16,950,802	\$27,493,194	\$45,398,138
Non-cash transaction (See Note 2.5)	–	–	\$5,000,000

See accompanying notes to the consolidated financial statements

Infosys Technologies Limited and subsidiary

Notes to the consolidated financial statements

1 Company overview and significant accounting policies

1.1 Company overview

Infosys Technologies Limited (“Infosys” or “the Company”) along with its majority owned and controlled subsidiary, Progeon Limited (“Progeon”) is a leading global information technology, or IT, services company. The Company provides end-to-end business solutions that leverage technology thus enabling its clients to enhance business performance. The Company provides solutions that span the entire software life cycle encompassing consulting, design, development, re-engineering, maintenance, systems integration and package evaluation and implementation. In addition, the Company offers software products for the banking industry and business process management services.

1.2 Basis of preparation of financial statements

The accompanying consolidated financial statements are prepared in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”). Inter-company balances and transactions are eliminated on consolidation. All amounts are stated in U.S. dollars, except as otherwise specified.

1.3 Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities on the date of the financial statements, and the reported amounts of revenues and expenses during the period. Examples of estimates include accounting for contract costs expected to be incurred to complete software development, allowance for uncollectible accounts receivable, future obligations under employee benefit plans, provisions for post-sales customer support and the useful lives of property, plant and equipment and intangible assets. Actual results could differ from those estimates.

1.4 Revenue recognition

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. Revenue from the end of the last billing to the balance sheet date is recognized as unbilled revenues. Revenue from fixed-price, fixed-time frame contracts is recognized as per the percentage-of-completion method. Guidance has been drawn from paragraph 95 of Statement of Position (SOP) 97-2 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-time frame 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, Software Revenue Recognition, 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 our 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 recognised 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 recognised 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-time frame bases. Revenue on time-and-material contracts is recognized as the related services are rendered. Revenue from fixed-price, fixed-time frame 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.

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 to be cash equivalents. Cash and cash equivalents comprise cash, cash on deposit with banks, marketable securities and deposits with corporations.

1.6 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	Plant and equipment	5 years
Furniture and fixtures	5 years	Vehicles	5 years
Computer equipment	2-5 years		

The cost of software purchased for internal use is accounted under SOP 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use. Deposits paid towards the acquisition of property, plant and equipment outstanding at each balance sheet date and the cost of property, plant and equipment not put to use before such date are disclosed under “*Capital work-in-progress*”.

1.7 Intangible assets

Intangible assets are amortized over their respective individual estimated useful lives on a straight-line basis, commencing from the date the asset is available to the company for its use. Management estimates the useful lives of acquired rights in software applications to range between one through five years.

1.8 Impairment of long-lived assets

The company evaluates the recoverability of its long-lived assets and certain identifiable intangibles, if any, 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. Assets to be disposed are reported at the lower of the carrying value or the fair value less the cost to sell.

1.9 Research and development

Research and development costs are expensed as incurred. Software product development costs are expensed as incurred until technological feasibility is achieved.

1.10 Foreign currency translation

The accompanying financial statements are reported in U.S. dollars. The functional currency of the company is the Indian rupee (“Rs.”). 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 and expense accounts using a monthly average exchange rate for the respective periods. The gains or losses resulting from such translation are reported as “*Other comprehensive income*”, a separate component of stockholders’ equity. The method for translating expenses of overseas operations depends upon the funds used. If the payment is made from a rupee denominated bank account, the exchange rate prevailing on the date of the payment would apply. If the payment is made from a foreign currency, i.e., non-rupee denominated account, the translation into rupees is performed at the average monthly exchange rate.

1.11 Earnings per share

In accordance with Statement of Financial Accounting Standards (“SFAS”) 128, *Earnings Per Share*, basic earnings per share are computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common and dilutive common equivalent shares outstanding during the period, using the treasury stock method for options and warrants, except where the result would be anti-dilutive.

1.12 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 and operating loss carry-forwards. 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 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 uncertain.

1.13 Fair value of financial instruments

The carrying amounts reflected in the balance sheets for cash, cash equivalents, accounts receivable and accounts payable approximate their respective fair values due to the short maturities of these instruments.

1.14 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, 2002 and March 31, 2003, 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 company’s cash resources are invested with corporations, financial institutions and banks with high investment grade credit ratings. Limitations are established by the company as to the maximum amount of cash that may be invested with any such single entity.

1.15 Retirement benefits to employees

1.15.1 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, based upon which, Infosys contributes to the Infosys Technologies Limited Employees’ Gratuity Fund

Trust (the “Trust”). Trustees administer contributions made to the Trust and invest in specific designated securities as mandated by law, which generally comprise central and state government bonds and debt instruments of government-owned corporations.

In accordance with the Payment of Gratuity Act, 1972, Progeon provides for gratuity, a defined benefit retirement plan covering eligible employees. The 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.

1.15.2 Superannuation

Apart from being covered under the Gratuity Plan described above, certain employees of Infosys are also participants of a defined contribution plan. The company makes 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. Infosys has no further obligations to the Plan beyond its monthly contributions.

Certain employees of Progeon are also participants of a defined contribution plan. The company makes monthly provisions under the superannuation plan based on a specified percentage of each covered employee’s salary. The company has no further obligations to the superannuation plan beyond its monthly provisions.

1.15.3 Provident fund

Eligible employees also receive benefits from a provident fund, which is a defined contribution plan. Both the employee and the company make monthly contributions to this provident fund plan equal to a specified percentage of the covered employee’s salary. Infosys contributes a part of the contributions to the Infosys Technologies Limited Employees’ Provident Fund Trust. The remainders of the contributions are made to the Government administered provident fund. There are no further obligations under the provident fund plan beyond its monthly contributions.

In respect of Progeon, eligible employees receive benefits from a provident fund, which is a defined contribution plan. Both the employee and the company 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. The company has no further obligations under the provident fund plan beyond its monthly contributions.

1.16 Investments

The company accounts by the equity method for investments between 20% and 50% or where it is otherwise able to exercise significant influence over the operating and financial policies of the investee. Investment securities in which the company controls less than 20% voting interest are currently classified as “available-for-sale securities”. Non-readily marketable equity securities for which there are no readily determinable fair values are recorded at cost.

Investment securities designated as “available-for-sale” are carried at their fair value. Fair value is based on quoted market prices. Unquoted securities are carried at cost, adjusted for declines in value judged to be other than temporary. 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 the statements of income. The cost of securities sold is based on the specific identification method. Interest and dividend income is recognized when earned.

1.17 Stock-based compensation

The company applies 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 is 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 has elected to continue to apply the intrinsic value-based method of accounting described above, and has adopted the disclosure requirements of SFAS 148, *Accounting for Stock-Based Compensation – Transition and Disclosure, an amendment of FASB Statement No. 123*. All stock options issued to date have been accounted as a fixed stock option plan.

The following table illustrates the effect on net income and earnings per share 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.

	Year ended March 31,		
	2001	2002	2003
Net income, as reported	\$131,948,104	\$164,466,309	\$194,870,041
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	5,081,795	5,009,772	4,803,534
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(37,339,233)	(64,294,987)	(62,447,389)
Pro forma net income	\$99,690,666	\$105,181,094	\$137,226,186
Earnings per share:			
Basic – as reported	2.01	2.51	2.97
Basic – pro forma	1.52	1.60	2.09
Diluted – as reported	1.98	2.49	2.93
Diluted – pro forma	1.49	1.59	2.09

The fair value of each option is estimated on the date of grant using the Black-Scholes model with the following assumptions:

	Year ended March 31,		
	2001	2002	2003
Dividend yield %	0.1%	0.2%	0.2%
Expected life	1-5years	1-5years	1-5years
Risk free interest rate	10.8%	9.5%	6.0%
Volatility	44.0%	69.0%	60-75%

1.18 Dividends

Dividend on common stock are recorded as a liability on the date of declaration by the stockholders.

1.19 Derivative financial instruments

On April 1, 2001, the company adopted SFAS 133, *Accounting for Derivative Instruments and Hedging Activities* as amended, when the rules became effective for companies with fiscal years ending March 31. The company enters into forward foreign exchange contracts where the counter party is generally a bank. The company purchases forward foreign exchange contracts to mitigate the risk of changes in foreign exchange rates on accounts receivable and forecasted cash flows denominated in certain foreign currencies. Although these contracts are effective as hedges from an economic perspective, they do not qualify for hedge accounting under SFAS 133, as amended. Any derivative that is either not designated hedge, or is so designated but is ineffective per SFAS 133, is marked to market and recognized in earnings immediately.

1.20 Reclassifications

Certain reclassifications have been made to conform prior period data to the current presentations. These reclassifications had no effect on reported earnings.

1.21 Recent accounting pronouncements

In November 2002, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables* applicable for fiscal periods beginning after June 2003. This Issue addresses when and, if so, how an arrangement involving multiple deliverables should be divided into separate units of accounting, where the deliverable (the revenue generating activities) are sufficiently separable and have standalone value to the customer. It is also necessary that there exists sufficient evidence of fair value to separately account for some or all of the deliverables. The Company believes that the adoption of the consensus will not have a material impact on the Company's revenue recognition policies as the accounting for the revenue from a significant portion of the Company's service offerings is governed by higher level GAAP literature.

In November 2002, the FASB issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees Including Indirect Guarantees of Indebtedness of Others*. The adoption of the Interpretation did not have a material impact on the Company's accounting or disclosure policies.

In January 2003, the FASB issued Interpretation No. 46, *Consolidation of Variable Interest Entities*, an interpretation of Accounting Research Bulletin (ARB) 51, that applies to variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. The company has assessed the implication of this interpretation and does not have to consolidate or disclose information about variable interest entities when the interpretation becomes applicable to existing entities from July 1, 2003.

2 Notes to the consolidated financial statements

2.1 Cash and cash equivalents

The cost and fair values for cash and cash equivalents as of March 31, 2002 and 2003 are as follows:

	As of March 31,	
	2002	2003
<i>Cost and fair values</i>		
Cash and bank deposits	\$158,274,886	\$283,302,326
Deposits with corporations	52,211,054	71,060,592
	<u>\$210,485,940</u>	<u>\$354,362,918</u>

Cash and cash equivalents include restricted cash balances in the amount of \$284,839 and \$336,610 as of March 31, 2002 and 2003 respectively. The restrictions are primarily on account of unclaimed dividend.

2.2 Trade accounts receivable

Trade accounts receivable as of March 31, 2002 and 2003, net of allowance for doubtful accounts of \$3,941,245 and \$3,010,568 respectively, amounted to \$ 69,017,110 and \$109,119,856. The age profile of trade accounts receivable, net of allowances is given below.

	As of March 31,	
	2002	2003
		In %
Period (in days)		
0 – 30	69.0	65.8
31 – 60	30.0	29.0
61 – 90	0.5	3.9
More than 90	0.5	1.3
	<u>100.0</u>	<u>100.0</u>

2.3 Prepaid expenses and other current assets

Prepaid expenses and other current assets consist of the following:

	As of March 31,	
	2002	2003
Rent deposits	\$2,079,155	\$2,856,226
Security deposits with service providers	1,220,401	2,814,216
Loans to employees	8,331,779	12,252,004
Prepaid expenses	2,990,523	5,209,907
Other current assets	618,057	1,251,963
	<u>\$15,239,915</u>	<u>\$24,384,316</u>

Other current assets represent advance payments to vendors for the supply of goods and rendering of services and certain costs incurred towards software. Deposits with service providers relate principally to leased telephone lines and electricity supplies.

2.4 Property, plant and equipment – net

Property, plant and equipment consist of the following:

	As of March 31,	
	2002	2003
Land	\$8,955,962	\$9,948,480
Buildings	58,481,413	81,114,141
Furniture and fixtures	32,683,315	43,969,763
Computer equipment	59,006,470	77,299,299
Plant and equipment	37,685,337	47,832,904
Vehicles	72,085	73,995
Capital work-in-progress	30,881,704	16,281,831
	<u>227,766,286</u>	<u>276,520,413</u>
Accumulated depreciation	(80,554,555)	(119,326,223)
	<u>\$147,211,731</u>	<u>\$157,194,190</u>

Depreciation expense amounted to \$24,527,867, \$33,608,391 and \$37,023,974 for fiscal 2001, 2002 and 2003 respectively. The amount of third party software expensed during fiscal 2001, 2002 and 2003 was \$6,979,492, \$7,147,614 and \$11,607,776 respectively.

2.5 Intangible assets

During fiscal 2003, the company acquired the intellectual property rights of Trade IQ product from IQ Financial Systems Inc., USA for its banking business unit. The consideration paid amounted to US\$ 3.47 million. The consideration has been recorded as an intangible asset, which is being amortized over two years representing management's estimate of the useful life of the intellectual property.

The company also entered into an agreement with the Aeronautical Development Agency, India ("ADA") for transferring the intellectual property rights in AUTOLAY, a commercial software application product used in the design of high performance structural systems. The company will pay the committed consideration of US\$ 5 million within ten years of the contract date. The ownership of intellectual property in AUTOLAY transfers to the company on remittance of the consideration to ADA. The committed consideration of US\$ 5 million is recorded as an intangible asset and is being amortized over five years, which is management's estimate of the useful life. The amount payable to ADA is disclosed as a non-current liability as of March 31, 2003 and as a non-cash transaction in the consolidated statement of cash flows.

As of March 31, 2003, intangible assets (net of accumulated amortization of \$2,360,799) were \$6,471,236.

2.6 Investments

The carrying value and the fair values of the Company's investments are as follows:

	Carrying cost	Fair value
As of March 31, 2002		
M-Commerce Ventures Pte Ltd – 70 units, each unit representing 1 Ordinary Share of S\$1 each at par and 9 Redeemable Preference Shares of S\$1 each at par, with a premium of S\$1,110 per Redeemable Preference Share	\$399,485	\$399,485
Asia Net Media BVI Limited – 30,000,000 Ordinary Shares at \$0.05 each, fully paid, par value \$0.01 each	1,500,000	1,500,000
CiDRA Corporation – 33,333 Series D Convertible Preferred Stock, at \$90 each, fully paid, par value \$0.01 each	2,999,970	2,999,970
Workadia Inc., USA – 880,000 Series B Preferred Stock at \$2.5 each, fully paid, par value \$0.0005 each	2,200,000	2,200,000
JASDIC Park Company – 480 Common Stock, at ¥ 50,000 each, fully paid, par value ¥ 50,000 each	177,576	177,576
Stratify, Inc. (formerly Purple Yogi Inc.) – 276,243 Series D Convertible Preferred Stock, at \$1.81 each fully paid, par value \$0.001 each	500,000	500,000
Others	362	362
	<u>\$7,777,393</u>	<u>\$7,777,393</u>

	Carrying cost	Fair value
As of March 31, 2003		
M-Commerce Ventures Pte Ltd – 80 units, each unit representing 1 Ordinary Share of S\$1 each at par and 9 Redeemable Preference Shares of S\$1 each at par, with a premium of S\$1,110 per Redeemable Preference Share	\$453,863	\$453,863
CiDRA Corporation – 33,333 Series D Convertible Preferred Stock, at \$90 each, fully paid, par value \$0.01 each	2,999,970	2,999,970
Workadia Inc., USA – 880,000 Series B Preferred Stock at \$2.5 each, fully paid, par value \$0.0005 each	660,000	660,000
Stratify, Inc. (formerly Purple Yogi Inc.) – 276,243 Series D Convertible Preferred Stock, at \$1.81 each fully paid, par value \$0.001 each	500,000	500,000
	<u>\$4,613,833</u>	<u>\$4,613,833</u>

An amount of \$619,161 received from Workadia Inc. towards recovery of investment is shown under “other current assets,” pending clearance from regulatory authorities for setting-off against the investment.

2.7 Other assets

Other assets represent the non-current portion of loans to employees.

2.8 Related parties

The company grants loans to employees for acquiring assets such as property and cars. Such loans are repayable over fixed periods ranging from 1 to 100 months. The annual rates of interest at which the loans have been made to employees vary between 0% through 4%. No loans have been made to employees in connection with equity issues. The loans are generally secured by the assets acquired by the employees. As of March 31, 2002 and 2003, amounts receivable from executive officers amounting to \$473,464 and nil, respectively, are included in prepaid expenses and other current assets, and other assets in the accompanying balance sheets.

The required repayments of loans by employees are as detailed below.

	As of March 31	
	2002	2003
2003	\$8,331,779	–
2004	3,755,840	\$12,252,004
2005	2,670,075	4,298,780
2006	1,826,748	3,206,683
2007	1,454,086	2,416,202
2008	–	2,099,781
Thereafter	2,751,866	4,432,882
	<u>\$20,790,394</u>	<u>\$28,706,332</u>

The estimated fair values of related party receivables amounted to \$17,905,507 and \$24,422,419 as of March 31, 2002 and 2003 respectively. These amounts have been determined using available market information and appropriate valuation methodologies. Considerable judgment is required to develop these estimates of fair value. Consequently, these estimates are not necessarily indicative of the amounts that the company could realize in the market.

2.9 Other accrued liabilities

Other accrued liabilities comprise the following:

	As of March 31	
	2002	2003
Accrued compensation to staff	\$11,575,996	\$25,382,793
Accrued dividends	229,839	336,610
Provision for post sales client support	2,255,573	1,015,022
Employee withholding taxes payable	2,614,479	4,964,118
Provision for expenses	3,356,760	12,196,810
Retainage	1,918,203	1,120,938
Others	473,796	1,232,978
	<u>\$22,424,646</u>	<u>\$46,249,269</u>

2.10 Employee post-retirement benefits

2.10.1 Gratuity

The following tables set out the funded status of the gratuity plans and the amounts recognized in the company's financial statements in fiscal 2001, 2002 and 2003.

	Year ended March 31,		
	2001	2002	2003
<i>Change in benefit obligations</i>			
Benefit obligations at the beginning of the year	\$11,043,208	\$13,581,972	\$15,851,898
Unrecognized actuarial loss	(329,928)	–	(514,983)
Service cost	2,627,599	1,341,313	2,158,209
Interest cost	1,183,461	1,376,398	1,082,815
Benefits paid	(184,247)	(175,364)	(238,823)
Effect of exchange rate changes	(758,121)	(272,421)	450,082
Benefit obligations at the end of the year	13,581,972	15,851,898	18,789,198
<i>Change in plan assets</i>			
Fair value of plan assets at the beginning of the year	4,375,821	10,147,905	12,448,532
Effect of exchange rate changes	(468,275)	(524,191)	385,738
Actual return on plan assets	1,061,611	1,324,702	1,369,206
Employer contributions	5,362,995	1,675,480	2,100,113
Benefits paid	(184,247)	(175,364)	(238,823)
Plan assets at the end of the year	10,147,905	12,448,532	16,064,766
<i>Funded status</i>			
Excess of actual return over estimated return on plan assets	301,791	141,394	552,688
Unrecognized transitional obligation	639,319	594,784	402,646
Unrecognized actuarial cost	4,216,291	3,131,389	2,235,222
(Accrued) / prepaid benefit	\$1,723,334	\$464,201	\$466,124

Net gratuity cost for fiscal 2001, 2002 and 2003 comprises the following components:

	Year ended March 31,		
	2001	2002	2003
Service cost	\$2,627,599	\$1,341,313	\$2,158,209
Interest cost	1,183,461	1,376,398	1,082,815
Expected return on assets	(759,820)	(1,183,308)	(816,518)
Amortization of unrecognized transitional obligation	55,127	44,535	43,980
Amortization of unrecognized actuarial loss	329,928	105,330	129,701
Net gratuity cost	\$3,436,295	\$1,684,268	\$2,598,187

The assumptions used in accounting for the gratuity plan in fiscal 2001, 2002 and 2003 are set out below.

	Year ended March 31,		
	2001	2002	2003
Discount rate	10%	10%	7%
Rate of increase in compensation levels	9%	9%	5-7%
Rate of return on plan assets	10%	10%	7%

The company assesses these assumptions with its projected long-term plans of growth and prevalent industry standards.

2.10.2 Superannuation

The company contributed \$796,739, \$1,220,716 and \$1,216,282 to the superannuation plan in fiscal 2001, 2002 and 2003 respectively.

2.10.3 Provident fund

The company contributed \$2,339,794, \$3,146,742, and \$3,820,331 to the provident fund in fiscal 2001, 2002 and 2003, respectively.

2.11 Stockholders' equity

Infosys has only one class of capital stock referred to as equity shares. All references in these financial statements to number of shares, per share amounts and market prices of equity shares are retroactively restated to reflect stock splits made. The rights of equity shareholders are set out below.

2.11.1 Voting

Each holder of equity shares is entitled to one vote per share. The equity shares represented by American Depositary Shares ("ADS") carry similar rights to voting and dividends as the other equity shares. Two ADSs represent one underlying equity share.

2.11.2 Dividends

Should the company declare and pay dividends, such dividends will be paid in Indian Rupees. Indian law mandates that any dividend be declared out of distributable profits only after the transfer of a specified percentage of net income computed in accordance with current regulations to a general reserve. Moreover, the remittance of dividends outside India is governed by Indian law on foreign exchange and is subject to applicable taxes.

2.11.3 Liquidation

In the event of liquidation of the company, the holders of common stock shall be entitled to receive any of the remaining assets of the company, after distribution of all preferential amounts. The amounts will be in proportion to the number of equity shares held by the stockholders.

2.11.4 Stock options

There are no voting, dividend or liquidation rights to the holders of warrants issued under the company's stock option plans.

2.12 Share capital of Progeon

In April 2002, Progeon issued 12,250,000 equity shares of par value \$0.20 per share to its holding company, Infosys, in exchange for an aggregate consideration of \$2,500,000 ("First Tranche subscription"). In terms of the stock subscription agreement between Infosys, Citicorp International Finance Corporation ("CIFIC") and Progeon, Infosys is also required to subscribe to an additional 12,250,000 equity shares in Progeon, on or before the date of the first anniversary of the First Tranche Subscription.

On June 14, 2002, Progeon issued 4,375,000 0.0005% cumulative convertible preference shares to CIFIC at an issue price of \$2.28 (equivalent to Rs. 112) per share, in exchange for an aggregate consideration of \$10,000,000. Unless earlier converted, pursuant to an agreement between the company and CIFIC, these cumulative convertible preference shares shall automatically be converted into equity shares, (i) one year prior to the Initial Public Offering ("IPO") date or (ii) September 30, 2005 or (iii) at the holder's option, immediately upon the occurrence of any Liquidity Event; whichever is earlier. The term "Liquidity Event" includes any of a decision of the Board of Directors of the company to make an IPO, merger, reconstruction, capital reorganization or other event which, in the sole opinion of the holder of the convertible preference shares, amounts to an alteration in the capital structure of the company. Each preference share is convertible into one equity share, par value \$0.20 each. The dividend on the preference shares for the period ended March 31, 2003 is payable.

Each holder of these cumulative convertible preference shares is entitled to receive notice of, and to attend, any shareholders' meeting and shall be entitled to vote together with holders of equity shares on any matters that affect their rights as preference shareholders including any resolution for winding up the company or for the repayment or reduction of the company's share capital.

In the event of any liquidation, dissolution or winding up of the company, either voluntary or involuntary, each holder of the preference shares will be paid a dollar equivalent of Rs. 112 per preference share, as adjusted for stock dividends, combinations, splits, recapitalizations and the like, in preference to any distribution of any assets of the company to the holders of equity shares.

Upon the completion of the distribution described above, the remaining assets and funds of the company available for distribution to shareholders shall be distributed among all holders of preference shares and equity shares based on the number of equity shares held by each of them (assuming a full conversion of all the preference shares).

2.13 Other income, net

Other income, net, consists of the following:

	Year ended March 31,		
	2001	2002	2003
Interest income	\$8,526,635	\$10,423,654	\$16,701,515
Income from sale of special import licenses	14,800	–	–
Exchange gains	4,444,208	2,749,162	4,157,373
Provision for investments	(3,480,300)	–	(3,219,030)
Others	–	692,478	408,252
	<u>\$9,505,343</u>	<u>\$13,865,294</u>	<u>\$18,048,110</u>

In fiscal 2003, we provided for write-downs to our investments in the aggregate amount of approximately \$3.2 million. These included approximately \$1.5 million for Asia Net Media BVI Limited, \$0.2 million for JASDIC Park Company, \$1.5 million for Workadia Inc., and other miscellaneous investments. These write-downs were required due to the non-temporary impact of adverse market conditions on these entities' business models and their inability to continue operations. In addition, these entities are currently in liquidation. It is unlikely that we will recover any significant additional funds on their liquidation.

2.14 Operating leases

The company has various operating leases for office buildings that are renewable on a periodic basis. Rental expenses for operating leases in fiscal 2001, 2002 and 2003 were \$3,689,822, \$5,109,690, and \$6,141,298 respectively. The operating leases can be renewed or canceled at the company's option.

The company leases some of its office space under non-cancelable operating leases. The schedule of future minimum rental payments in respect of these leases is set out below.

Year ending March 31,	
2004	\$3,772,447
2005	3,341,814
2006	2,491,325
2007	1,050,362
2008	689,691
Thereafter	1,472,132
	<u>\$12,817,771</u>

2.15 Research and development

General and administrative expenses in the accompanying statements of income include research and development expenses of \$3,610,550, \$3,083,994 and \$2,950,949 for fiscal 2001, 2002 and 2003 respectively.

2.16 Employees' Stock Offer Plans ("ESOP")

In September 1994, the company established the 1994 plan, which provided for the issue of 6,000,000 warrants, as adjusted, to eligible employees. The warrants were issued to an employee welfare trust (the "Trust"). In 1997, in anticipation of a share dividend to be declared by the company, the Trust exercised all warrants held by it and converted them into equity shares. As and when the Trust issued options/stock to eligible employees, the difference between the market price and the exercise price was accounted as deferred stock compensation expense and amortized over the vesting period. Such amortized deferred compensation expense was \$5,081,795, \$5,009,772 and \$4,803,534 for fiscal 2001, 2002, and 2003 respectively. The 1994 plan lapsed in fiscal 2000, and consequently no further shares will be issued to employees under this plan.

1998 Employees Stock Offer Plan (the "1998 Plan"). The company's 1998 Plan provides for the grant of non-statutory stock options and incentive stock options to employees of the company. The establishment of the 1998 Plan was approved by the board of directors in December 1997 and by the stockholders in January 1998. The Government of India has approved the 1998 Plan, subject to a limit of 1,470,000 equity shares representing 2,940,000 ADS to be issued under the 1998 Plan. Unless terminated sooner, the 1998 Plan will terminate automatically in January 2008. All options under the 1998 Plan will be exercisable for equity shares represented by ADSs. The 1998 Plan is administered by a Compensation Committee comprising five members, all of who are independent directors on the Board of Directors. All options under the 1998 Plan are exercisable for equity shares represented by ADSs.

1999 Stock Offer Plan (the "1999 Plan"). In fiscal 2000, the company instituted the 1999 Plan. The stockholders and the Board of Directors approved the 1999 Plan in June 1999. The 1999 Plan provides for the issue of 6,600,000 equity shares to employees. The 1999 Plan is administered by a Compensation Committee comprising five members, all of who are independent directors on the Board of Directors. Under the 1999 Plan, options will be issued to employees at an exercise price, which shall not be less than the Fair Market Value ("FMV"). Under the 1999 Plan, options may also be issued to employees at exercise prices that are less than FMV only if specifically approved by the members of the company in a general meeting. All options under the 1999 plan are exercisable for equity shares.

The options under the 1998 Plan and 1999 Plan vest over a period of one through four years and expire 5 years from the date of completion of vesting.

The activity in the warrants / equity shares of the 1994, 1998 and 1999 ESOP in fiscal 2001, 2002 and 2003 are set out below.

	Year ended March 31,					
	2001		2002		2003	
	Shares arising out of options	Weighted average exercise price	Shares arising out of options	Weighted average exercise price	Shares arising out of options	Weighted average exercise price
1994 Option plan:						
Outstanding at the beginning of the period	341,400	–	330,000	–	321,400	–
Granted	–	–	–	–	–	–
Forfeited	(10,600)	\$1.15	(8,600)	\$1.15	(3,200)	\$1.15
Exercised	(800)	\$1.15	–	–	–	–
Outstanding at the end of the period	330,000	–	321,400	–	318,200	–
Exercisable at the end of the period	–	–	–	–	–	–
Weighted-average fair value of grants during the period at less than market	–	–	–	–	–	–
1998 Option plan:						
Outstanding at the beginning of the period	344,750	–	782,753	–	1,131,247	–
Granted	482,420	\$230.88	454,250	\$98.06	290,100	\$123.69
Forfeited	(38,200)	\$172.58	(77,773)	\$240.90	(124,874)	\$92.43
Exercised	(6,217)	\$53.82	(27,983)	\$44.32	(44,770)	\$47.21
Outstanding at the end of the period	782,753	–	1,131,247	–	1,251,703	–
Exercisable at the end of the period	55,558	–	164,527	–	315,002	–
Weighted-average fair value of options granted during the period	–	\$45.85	–	\$31.10	–	\$32.04
1999 Option plan:						
Outstanding at the beginning of the period	1,006,800	–	2,793,980	–	4,668,815	–
Granted	1,957,830	\$136.68	2,050,500	\$64.74	616,850	\$78.41
Forfeited	(169,450)	\$110.06	(175,635)	\$119.23	(212,316)	\$96.63
Exercised	(1,200)	\$89.98	(30)	\$84.95	(12,178)	\$56.24
Outstanding at the end of the period	2,793,980	–	4,668,815	–	5,061,171	–
Exercisable at the end of the period	93,400	–	448,530	–	1,222,639	–
Weighted-average fair value of options granted during the period	–	\$51.92	–	\$32.47	–	\$34.80

The following table summarizes information about stock options outstanding as of March 31, 2003

Range of exercise prices per share (\$)	No. of shares arising out of options	Options Outstanding		Options Exercisable	
		Weighted average remaining contractual life in years	Weighted average exercise price	No. of shares arising out of options	Weighted average exercise price
1994 Plan					
1.15	318,200	1.58	\$1.15	–	–
1998 Plan					
34–50	98,250	3.94	\$34	98,250	\$34
51-100	265,566	6.51	\$84	17,338	\$86
101-150	391,560	7.18	\$127	14,910	\$132
151-200	349,347	5.57	\$192	132,229	\$189
201-300	71,560	5.63	\$240	22,455	\$240
301-400	60,070	5.12	\$324	22,170	\$327
401-660	15,350	4.92	\$514	7,650	\$525
	1,251,703			315,002	
1999 Plan					
51-100	3,301,853	6.12	\$72	702,478	\$81
101-150	1,343,913	5.70	\$122	389,646	\$123
151-200	409,305	5.44	\$160	128,295	\$161
201-250	6,100	5.01	\$216	2,220	\$222
	5,061,171			1,222,639	

Progeon's 2002 Plan provides for the grant of stock options to employees of the company and was approved by its board of directors and stockholders in June 2002. All options under the 2002 Plan are exercisable for equity shares. The 2002 Plan is administered by a Compensation Committee comprising three members, all of whom are directors of the company. The 2002 Plan provides for the issue of 5,250,000 equity shares to employees, at an exercise price, which shall not be less than the FMV. Options may also be issued to employees at exercise prices that are less than FMV only if specifically approved by the members of the company in general meeting. The options issued under the 2002 Plan vest in periods ranging between four through seven years, although accelerated vesting based on performance conditions is provided in certain instances. All options granted have been accounted for as a fixed plan. Options to purchase 1,801,175 shares of Progeon, with a weighted average exercise price of \$0.69 and fair value \$0.30 have been granted during fiscal 2003 and are outstanding as of March 31, 2003. There were no forfeitures or exercises on these grants. The outstanding options have a weighted average remaining contractual life of 4.33 years and weighted average exercise price of \$0.69. No options were exercisable as of March 31, 2003.

2.17 Income taxes

The provision for income taxes comprises:

	Year ended March 31		
	2001	2002	2003
Current taxes			
Domestic taxes	\$5,315,961	\$6,483,255	\$18,717,241
Foreign taxes	10,525,168	23,463,108	25,523,234
	15,841,129	29,946,363	\$44,240,475
Deferred taxes			
Domestic taxes	(769,304)	27,126	(1,122,604)
Foreign taxes	–	(2,026,597)	(1,295,606)
	(769,304)	(1,999,471)	(2,418,210)
Aggregate taxes	\$15,071,825	\$27,946,892	\$41,822,265

The tax effects of significant temporary differences that resulted in deferred tax assets and liabilities, and a description of the financial statement items that created these differences are as follows:

	As of March 31	
	2002	2003
Deferred tax assets:		
Property, plant and equipment	\$2,989,348	\$4,719,124
Provision for doubtful debts	1,448,407	1,093,701
Investments	1,571,586	2,545,761
	6,009,341	8,358,586
Less: Valuation allowance	(674,300)	(614,004)
	5,335,041	7,744,582
Deferred tax liability on exchange gains	–	(191,156)
Net deferred tax assets	\$5,335,041	\$7,553,426

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which the temporary differences become deductible. Management considers the scheduled reversal of the projected future

taxable income, and tax planning strategies in making this assessment. Based on the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes that it is more likely than not the company will realize the benefits of those deductible differences, net of the existing valuation differences at March 31, 2003. The amount of the deferred tax assets considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carry forward period are reduced.

All deferred tax expenses / (benefits) are allocated to the continuing operations of the company.

A reconciliation of the income tax provision to the amount computed by applying the statutory income tax rate to the income before provision for income taxes is summarized below.

	Year ended March 31		
	2001	2002	2003
Net income before taxes	\$147,019,929	\$192,413,201	\$236,692,306
Enacted tax rates in India	39.55%	35.70%	36.75%
Computed expected tax expense	58,146,382	68,691,513	86,984,422
Less: Tax effect due to non-taxable income for Indian tax purposes	(57,334,527)	(67,338,527)	(71,851,761)
Others	3,437,865	5,014,830	2,517,994
Effect of tax rate change	(8,077)	142,565	(56,018)
Effect of prior period tax adjustments	305,014	–	–
Provision for Indian income tax	4,546,657	6,510,381	17,594,637
Effect of tax on foreign income	10,525,168	21,436,511	24,227,628
Aggregate taxes	\$15,071,825	\$27,946,892	\$41,822,265

The provision for foreign taxes is due to income taxes payable overseas, principally in the United States of America. The company benefits from certain significant tax incentives provided to software firms under Indian tax laws. These incentives presently include: (i) an exemption from payment of Indian corporate income taxes for a period of ten consecutive years of operation of software development facilities designated as “Software Technology Parks” (the “STP Tax Holiday”); and (ii) a tax deduction for profits derived from exporting computer software (the “Export Deduction”). All but one of the company’s software development facilities are located in designated Software Technology Parks (“STP”). The Government of India has recently amended the tax incentives available to companies set up in designated STPs. The period of the STP Tax Holiday available to such companies is restricted to ten consecutive years, beginning from the financial year when the unit started producing computer software or April 1, 1999, whichever is earlier. The Finance Act 2002 provides that the exempt income from an export oriented undertaking, for the year commencing April 1, 2002, be restricted to 90% of its export income. Additionally, the Export Deduction is being phased out equally over a period of five years starting from fiscal 2000.

The Company is subject to a 15% Branch Profit Tax (BPT) in the U.S. to the extent its U.S. branch’s net profit during the year is greater than the increase in the net assets of the Company’s U.S. branch during the fiscal year, computed in accordance with the Internal Revenue Code. At March 31, 2003, the Company’s US branch net assets amounted to approximately \$106.3 million. The Company has not triggered the BPT and intends to maintain the current level of its net assets in the US, as it is consistent with its business plan. Accordingly, a BPT provision has not been recorded.

2.18 Earnings per share

The following is a reconciliation of the equity shares used in the computation of basic and diluted earnings per equity share:

	Year ended March 31		
	2001	2002	2003
Basic earnings per equity share – weighted average number of common shares outstanding excluding unallocated shares of ESOP	65,771,256	65,556,648	65,571,002
Effect of dilutive common equivalent shares – stock options outstanding	943,483	528,226	908,007
Diluted earnings per equity share – weighted average number of common shares and common equivalent shares outstanding	66,714,739	66,084,874	66,479,009

Options to purchase 666,772 shares under the 1998 Plan and 1,845,378 shares under the 1999 Plan were not considered for calculating diluted earnings per share as their effect was antidilutive.

2.19 Derivative financial instruments

The Company enters into forward foreign exchange contracts where the counter party is generally a bank. The Company considers the risks of non-performance by the counter party as non-material. Infosys held foreign exchange forward contracts of \$2,000,000 and \$88,000,000 as of March 31, 2002 and 2003, respectively. The foreign forward exchange contracts mature between one to six months.

2.20 Segment reporting

SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, establishes standards for the way that public business enterprises report information about operating segments and related disclosures about products and services, geographic areas, and major customers. The company’s operations predominantly relate to providing IT solutions, delivered to customers located globally, across various industry segments. In the year ended March 31, 2000, the company provided segmental disclosures based on the geographical segment. However, from the fiscal year ended March 31, 2001, the Chief Operating Decision Maker evaluates the company’s performance and allocates resources based on an analysis of various performance indicators by industry classes and geographic segmentation of customers. Accordingly, revenues represented along industry classes comprise the principal basis of segmental information set out in these financial statements. Secondary segmental reporting

is performed on the basis of the geographical location of customers. The accounting principles consistently used in the preparation of the financial statements are consistently applied to record revenue and expenditure in individual segments, and are as set out in the summary of significant accounting policies.

Industry segments for the company are primarily *financial services* comprising enterprises providing banking, finance and insurance services, *manufacturing* enterprises, enterprises in the *telecommunications* ("telecom") and *retail* industries, and *others* such as utilities, transportation and logistics companies.

Geographic segmentation is based on business sourced from that geographic region and delivered from both on-site and off-shore. *North America* comprises the United States of America, Canada and Mexico; *Europe* includes continental Europe (both the east and the west), Ireland and the United Kingdom; and the *Rest of the World* comprising all other places except those mentioned above and *India*.

Revenue in relation to segments is categorized based on items that are individually identifiable to that segment, while expenditure is categorized in relation to the associated turnover of the segment. Allocated expenses of the geographic segments include expenses incurred for rendering services from the company's offshore software development centres and on-site expenses. Certain expenses such as depreciation, which form a significant component of total expenses, are not specifically allocable to specific segments as the underlying services are used interchangeably. Management believes that it is not practical to provide segment disclosures relating to those costs and expenses, and accordingly these expenses are separately disclosed as "unallocated" and adjusted only against the total income of the company.

Fixed assets used in the company's business are not identified to any of the reportable segments, as these are used interchangeably between segments. Management believes that it is currently not practicable to provide segment disclosures relating to total assets and liabilities since a meaningful segregation of the available data is onerous.

Geographical information on revenue and industry revenue information is collated based on individual customers invoiced or in relation to which the revenue is otherwise recognized.

2.20.1 Industry segments

Year ended March 31, 2001

	Financial services	Manufacturing	Telecom	Retail	Others	Total
Revenues	\$139,616,739	\$74,004,867	\$76,412,722	\$37,684,446	\$86,131,736	\$413,850,510
Identifiable operating expenses	49,021,150	28,363,069	19,219,376	11,893,574	26,233,048	134,730,217
Allocated expenses	38,589,808	19,736,596	20,423,026	10,057,009	23,189,607	111,996,046
Segmental operating income	52,005,781	25,905,202	36,770,320	15,733,863	36,709,081	167,124,247
Unallocable expenses						29,609,661
Operating income						137,514,586
Other income, net						9,505,343
Income before income taxes						147,019,929
Provision for income taxes						15,071,825
Net income						\$131,948,104

Year ended March 31, 2002

	Financial services	Manufacturing	Telecom	Retail	Others	Total
Revenues	\$199,725,558	\$93,404,474	\$85,190,054	\$67,027,323	\$99,703,805	\$545,051,214
Identifiable operating expenses	74,364,097	38,112,096	23,873,023	18,696,233	34,831,145	189,876,594
Allocated expenses	51,905,935	23,321,898	21,273,366	16,667,939	24,840,829	138,009,967
Segmental operating income	73,455,526	31,970,480	40,043,665	31,663,151	40,031,831	217,164,653
Unallocable expenses						38,616,746
Operating income						178,547,907
Other income, net						13,865,294
Income before income taxes						192,413,201
Provision for income taxes						27,946,892
Net income						\$164,466,309

Year ended March 31, 2003

	Financial services	Manufacturing	Telecom	Retail	Others	Total
Revenues	\$283,305,475	\$123,755,305	\$114,309,356	\$85,841,812	\$146,595,077	\$753,807,025
Identifiable operating expenses	113,522,995	50,493,841	38,470,934	27,432,075	54,817,856	284,737,701
Allocated expenses	81,032,424	32,793,395	31,096,470	22,779,164	39,122,548	206,824,001
Segmental operating income	88,750,056	40,468,069	44,741,952	35,630,573	52,654,673	262,245,323
Unallocable expenses						43,601,127
Operating income						218,644,196
Other income, net						18,048,110
Income before income taxes						236,692,306
Provision for income taxes						41,822,265
Net income						\$194,870,041

2.20.2 Geographic segments

Year ended March 31, 2001

	North America	Europe	India	Rest of the World	Total
Revenues	\$304,242,537	\$77,892,656	\$5,778,286	\$25,937,031	\$413,850,510
Identifiable operating expenses	96,358,758	27,210,316	1,943,571	9,217,572	134,730,217
Allocated expenses	82,053,059	20,951,885	1,866,259	7,124,843	111,996,046
Segmental operating income	125,830,720	29,730,455	1,968,456	9,594,616	167,124,247
Unallocable expenses					29,609,661
Operating income					137,514,586
Other income, net					9,505,343
Income before income taxes					147,019,929
Provision for income taxes					15,071,825
Net income					\$131,948,104

Year ended March 31, 2002

	North America	Europe	India	Rest of the World	Total
Revenues	\$388,168,447	\$106,103,448	\$10,735,626	\$40,043,693	\$545,051,214
Identifiable operating expenses	135,362,671	38,013,083	4,183,775	12,317,065	189,876,594
Allocated expenses	98,093,268	26,809,588	3,119,373	9,987,738	138,009,967
Segmental operating income	154,712,508	41,280,777	3,432,478	17,738,890	217,164,653
Unallocable expenses					38,616,746
Operating income					178,547,907
Other income, net					13,865,294
Income before income taxes					192,413,201
Provision for income taxes					27,946,892
Net income					\$164,466,309

Year ended March 31, 2003

	North America	Europe	India	Rest of the World	Total
Revenues	\$550,075,653	\$133,236,361	\$16,132,922	\$54,362,089	\$753,807,025
Identifiable operating expenses	218,257,001	46,559,987	4,084,049	15,836,664	284,737,701
Allocated expenses	149,621,377	35,920,484	5,823,309	15,458,831	206,824,001
Segmental operating income	182,197,275	50,755,890	6,225,564	23,066,594	262,245,323
Unallocable expenses					43,601,127
Operating income					218,644,196
Other income, net					18,048,110
Income before income taxes					236,692,306
Provision for income taxes					41,822,265
Net income					\$194,870,041

2.20.3 Significant clients

No clients individually accounted for more than 10% of the revenues in fiscal 2001, 2002 and 2003.

2.21 Commitments and contingencies

The company has outstanding performance guarantees for various statutory purposes totaling \$3,334,700 and \$1,681,044 as of March 31, 2002 and 2003, respectively. These guarantees are generally provided to governmental agencies.

2.22 Non-monetary transaction

During the year ended March 31, 2001, the company and certain of its employees founded OnMobile Systems Inc. ("OnMobile"). These founding employees resigned as employees of Infosys and hold senior management positions in OnMobile. The company transferred certain Intellectual Property Rights ("IPR") that it had developed and owned in a product called OnScan to OnMobile Systems Inc. (formerly OnScan, Inc). OnScan is a web-enabled wireless notification product. In exchange for the transfer, the company received consideration in the form of securities including 100,000 shares of Common Stock, par value \$0.001 each, 100,000 shares of Series A Voting Convertible Preferred Stock, par value \$0.001 each and 4,400,000 shares of Series A Nonvoting Convertible Preferred Stock, par value \$0.001 each. Convertible Preferred Stock is convertible in to Common Stock automatically upon the closing of an Initial Public Offering by OnMobile Systems Inc.

As of the date of the transfer technological feasibility had not been achieved during product development. The cost of development was expensed as incurred and had not been capitalized. The transfer was recorded at historical cost and accordingly, no values were assigned to IPR. The fair value of the securities was also determined to be zero given the uncertainty regarding the success of OnMobile; no gain was recognized on this transaction.

2.23 Litigation

The company is subject to legal proceedings and claims, which have arisen, in the ordinary course of its business. Legal actions, when ultimately concluded and determined, will not, in the opinion of management, have a material effect on the results of operations or the financial position of the company.