

# Unisys Corporation

## Management's Discussion and Analysis of Financial Condition and Results of Operations

### Overview

For 2008, the company reported a net loss of \$130.1 million. Revenue for 2008 was \$5.23 billion, down 7% from 2007 revenue of \$5.65 billion. The results include pretax charges of \$103.1 million related primarily to cost reduction actions announced in the fourth quarter of 2008. The company's 2008 financial results also reflect the global economic slowdown in the second half of the year. The company saw this slowdown particularly in its financial services business, but also in other key commercial industries, as clients reacted to economic uncertainties by reducing information technology (IT) spending. Reduced demand for the company's services and products impacted the company's revenue and profit margins for the year.

In the fourth quarter of 2008, the company announced an aggressive turnaround program, led by new Chairman and CEO Ed Coleman, to strengthen its profitability and competitive position. The actions involve focusing the company's global resources, simplifying its business structure, and reducing its cost and expense base. These actions include:

- Concentrating the company's investments and resources on business opportunities in fewer, more profitable markets in the IT marketplace;
- Creating clearly differentiated value propositions within each of its focused markets and solution offerings;
- Enhancing the cost-efficiency of its services labor delivery model to drive gross margin expansion; and
- Reducing overhead expense by simplifying its business, streamlining reporting lines and processes, and creating clear lines of accountability for results.

As part of this program, the company announced that it was exploring and taking action upon a wide range of options to reduce its cost base. Initial actions currently underway, which are focused on reducing selling, general and administrative expenses and service delivery costs, are expected to reduce the company's annual cost structure by more than \$225 million. The cost-reduction actions include reductions in third-party expenses, facility consolidations, headcount reductions of approximately 1,300 positions worldwide, and a suspension of company matching contributions to the U.S. 401(k) plan, which had been costing about \$50 million annually. The headcount reductions have begun and will continue into 2009. In addition, the company plans to forgo 2009 salary increases in most of its markets.

For 2008, the company reported a net loss of \$130.1 million, or \$.36 per share. The results included:

- Pretax cost reduction and other charges of \$103.1 million, principally for 1,304 personnel reductions, idle facility costs and asset write downs associated with portfolio exits and lease guarantees. See Note 3 of the Notes to Consolidated Financial Statements; and
- Pretax pension income of \$51.3 million. See Note 17 of the Notes to Consolidated Financial Statements.

For 2007, the company reported a net loss of \$79.1 million, or \$.23 per share. The results included:

- Pretax cost reduction and other charges of \$116.8 million, principally for 1,737 personnel reductions and idle facility costs. See Note 3 of the Notes to Consolidated Financial Statements;
- Pretax pension expense of \$35.0 million. See Note 17 of the Notes to Consolidated Financial Statements;
- A pretax gain of \$24.7 million on the sale of the company's media solutions business. See Note 9 of the Notes to Consolidated Financial Statements; and
- A \$39.4 million tax benefit related to an income tax audit settlement. See Note 7 of the Notes to Consolidated Financial Statements.

For 2006, the company reported a net loss of \$278.7 million, or \$.81 per share. The results included:

- Pretax cost-reduction charges of \$330.1 million, for the cost of 5,665 personnel reductions. See Note 3 of the Notes to Consolidated Financial Statements;
- Pretax pension expense of \$135.5 million, which included a \$45.0 million pretax curtailment gain related to changes adopted in the company's U.S. defined benefit pension plans. See Note 17 of the Notes to Consolidated Financial Statements; and
- A pretax gain of \$149.9 million on the sale of the company's shares in Nihon Unisys, Ltd. (NUL), a publicly traded company and the exclusive distributor of the company's hardware and software in Japan. The company sold all of its 30.5 million shares in NUL, generating cash proceeds of approximately \$378 million. See Note 9 of the Notes to Consolidated Financial Statements.

## Results of operations

### *Key factors impacting 2006, 2007 and 2008 results of operations*

The company's results in each year reflect a number of actions to reduce costs to achieve profitability. In the last three years, the company has recorded total pretax charges of \$550.0 million, comprised of \$435.0 million for 8,706 work-force reductions, \$61.0 million for idle lease cost and \$54.0 million principally related to asset write downs associated with portfolio exits and lease guarantees.

During 2006, the company committed to a reduction of 5,665 employees. This resulted in pretax charges in 2006 of \$330.1 million, principally related to severance costs, which were comprised of: (a) a charge of \$72.4 million for 2,250 employees in the U.S. and (b) a charge of \$257.7 million for 3,415 employees outside the U.S. The pretax charges were recorded in the following statement of income classifications: cost of revenue – services, \$216.9 million; cost of revenue – technology, \$2.0 million; selling, general and administrative expenses, \$84.6 million; research and development expenses, \$29.4 million; and other income (expense), net, \$2.8 million. The income recorded in other income (expense), net relates to minority shareholders' portion of the charge related to the company's fully consolidated majority-owned subsidiaries.

During 2007, the company consolidated facility space and committed to an additional reduction of 1,737 employees. This resulted in pretax charges of \$116.8 million. The charges related to work-force reductions of \$62.3 million were comprised of the following components: (a) 1,031 employees in the U.S. for a charge of \$29.9 million and (b) 706 employees outside the U.S. for a charge of \$32.4 million. The facility charges of \$40.6 million principally relate to 46 leased properties that the company ceased using during 2007. The facility charges represent the fair value of the liability at the cease-use date and were determined based on the remaining lease rental payments, reduced by estimated sublease rentals that could be reasonably obtained for the property. In addition, the company recorded pretax charges of \$13.9 million, principally related to asset impairments and leasehold improvement write-offs, lease guarantees, as well as other expenses related to the cost reduction efforts. The pretax charges of \$116.8 million were recorded in the following statement of income classifications: cost of revenue – services, \$31.8 million; cost of revenue – technology, \$3.9 million; selling, general and administrative expenses, \$62.0 million; research and development expenses, \$20.6 million; and other income (expense), net, \$1.5 million.

As described above, during 2008, the company consolidated facility space and committed to an additional reduction of 1,304 employees. This resulted in pretax charges of \$103.1 million. The charges related to work-force reductions of \$42.6 million were comprised of the following components: (a) 866 employees in the U.S. for a charge of \$20.2 million and (b) 438 employees outside the U.S. for a charge of \$22.4 million. The facility charges of \$20.4 million principally relate to 15 leased properties that the company ceased using during 2008. In addition, the company recorded pretax charges of \$40.1 million, principally related to asset write downs related to portfolio exits and lease guarantees. The pretax charges of \$103.1 million were recorded in the following statement of income classifications: cost of revenue – services, \$36.1 million; cost of revenue – technology, \$14.3 million; selling, general and administrative expenses, \$49.0 million; and research and development expenses, \$3.7 million.

In March 2006, the company adopted changes to its U.S. defined benefit pension plans effective December 31, 2006. The changes affected most U.S. employees including senior management and included ending the accrual of future benefits in the company's defined benefit pension plans for employees effective December 31, 2006. No new entrants to the plans are allowed after that date. The changes do not affect the vested accrued pension benefits of current and former employees, including retirees. As a result of the amendment to stop accruals for future benefits in its U.S. defined benefit pension plans, the company recorded a pretax curtailment gain of \$45.0 million in 2006. Effective January 1, 2007, the company increased its matching contribution for its U.S. defined contribution plan to 100 percent of the first 6 percent of eligible pay contributed by participants. The company match was made in company common stock. Effective January 1, 2009, the company match to the U.S. employee savings plan was suspended.

In April 2008, the company adopted changes to certain of its U.K. defined benefit pension plans whereby effective June 30, 2008 all future accruals of benefits under the plans ceased. As a result of this change, the company recorded a pretax curtailment loss of \$1.4 million in the second quarter of 2008. In addition, the company has enhanced its contributions to certain U.K. defined contribution plans, effective July 1, 2008.

### *Company results*

Revenue for 2008 was \$5.23 billion compared with 2007 revenue of \$5.65 billion, a decrease of 7%. Services revenue in 2008 decreased by 5% and Technology revenue declined by 22%. Foreign currency had a 1-percentage-point positive impact on revenue in 2008 compared with 2007. Revenue for 2007 was \$5.65 billion compared with 2006 revenue of \$5.76 billion, a decrease of 2%. Services revenue in 2007 decreased by 1% and Technology revenue declined by 4%. Foreign currency had a 4-percentage-point positive impact on revenue in 2007 compared with 2006. Revenue from international operations in 2008, 2007 and 2006 was \$2.99 billion, \$3.22 billion and \$3.22 billion, respectively. On a constant currency basis, international revenue decreased 9% in 2008 compared with 2007 and decreased 7% in 2007 compared with 2006. Revenue from U.S. operations was \$2.24 billion in 2008, \$2.43 billion in 2007 and \$2.54 billion in 2006.

Pension income for 2008 was \$51.3 million compared with pension expense of \$35.0 million in 2007 and pension expense of \$135.5 million in 2006. The change in 2008 from 2007 was principally due to increases in discount rates and higher returns on plan assets in prior years. The decrease in pension expense in 2007 from 2006 was principally due to the changes made in the U.S. defined benefit pension plans in 2006, discussed above, as well as the higher fair market value of plan assets, higher discount rates, a lower level of employees and a \$5.7 million curtailment gain in a defined benefit plan in the Netherlands. The company records pension income or expense, as well as other employee-related costs such as payroll taxes and medical insurance costs, in operating income in the following income statement categories: cost of revenue; selling, general and administrative expenses; and research and development expenses. The amount allocated to each category is based on where the salaries of active employees are charged.

Gross profit percent was 21.5% in 2008, 22.8% in 2007 and 17.5% in 2006. Included in gross profit percent in 2008, 2007 and 2006 were cost reduction charges of \$50.4 million, \$35.7 million and \$218.9 million, respectively. Gross profit percent in 2008 compared with 2007 reflects a decline in pension expense of \$66.5 million (income of \$39.7 million in 2008 compared with expense of \$26.8 million in 2007). Gross profit percent in 2007 compared with 2006 reflects a decline in pension expense of \$72.5 million (\$26.8 million expense in 2007 compared with \$99.3 million expense in 2006).

Selling, general and administrative expenses were \$957.0 million in 2008 (18.3% of revenue), \$1.02 billion in 2007 (18.1% of revenue) and \$1.10 billion in 2006 (19.2% of revenue). Included in selling, general and administrative expenses in 2008, 2007 and 2006 were cost reduction charges of \$49.0 million, \$62.0 million and \$84.6 million, respectively. Selling, general and administrative expenses in 2008 compared with 2007 reflect a decline in pension expense of \$14.0 million (income of \$4.7 million in 2008 compared with expense of \$9.3 million in 2007). In addition in 2008, the company (a) reversed \$13.2 million of previously-accrued compensation expense related to performance-based restricted stock units due to a change in the assessment of the achievability of performance goals and (b) recorded approximately \$9 million of charges associated with prior year items related principally to employee benefits and lease accounting. See Note 17 of the Notes to Consolidated Financial Statements. Selling, general and administrative expenses in 2007 compared with 2006 reflect a

decline in pension expense of \$19.5 million (\$9.3 million expense in 2007 compared with \$28.8 million expense in 2006). Also contributing to the decline in 2007 compared with 2006 was a reduction of \$16.7 million in bad debt expense as 2007 benefited from the reversal of bad debt expense due to collections of some long-outstanding receivables.

Research and development (R&D) expenses in 2008 were \$129.0 million compared with \$179.0 million in 2007 and \$231.7 million in 2006. Included in R&D expenses in 2008, 2007 and 2006 were cost reduction charges of \$3.7 million, \$20.6 million and \$29.4 million, respectively. The decrease in R&D expenses in 2008 and 2007, excluding these charges, principally reflects changes in the company's development model as the company has focused its investments on value-added software and services while partnering with outside companies on hardware and systems design and development.

In 2008, the company reported an operating profit of \$40.7 million compared with an operating profit of \$85.9 million in 2007 and an operating loss of \$326.8 million in 2006. The principal items affecting the comparison of 2008 with 2007 were the overall revenue decline and the expiration of the one-time fixed royalty fee from NUL, discussed below. Revenue in 2008 declined approximately \$56 million due to the expiration of this royalty fee. Operating profit in 2008 compared with 2007 also reflected a decline in pension expense of \$86.3 million (pension income of \$51.3 million in 2008 compared with pension expense of \$35.0 million in 2007) and cost reduction charges of \$103.1 million in 2008 compared with \$118.3 million in 2007. The principal item affecting the comparison of 2007 with 2006 was a \$118.3 million charge in 2007 compared with \$332.9 million charge in 2006 related to the cost reduction actions.

Interest expense was \$85.1 million in 2008, \$76.3 million in 2007 and \$77.2 million in 2006. The increase in interest expense in 2008 was primarily due to increased interest rates related to the refinancing of the \$200 million 7 <sup>7</sup>/<sub>8</sub>% notes due 2008 with the company's \$210 million 12 <sup>1</sup>/<sub>2</sub>% notes due 2016. The decrease in 2007 compared with 2006 was principally due to lower average debt.

Other income (expense), net was expense of \$32.6 million in 2008, compared with expense of \$6.1 million in 2007 and income of \$153.1 million in 2006. The difference in 2008 from 2007 was principally due to a gain of \$24.7 million on the sale of the company's media business in 2007. The difference in 2007 from 2006 was principally due to (a) a gain of \$24.7 million on the sale of the company's media business in 2007 compared with a gain of \$149.9 million on the sale of all of the company's shares of NUL in 2006 (see Note 9 of the Notes to Consolidated Financial Statements), (b) minority interest expense of \$23.4 million in 2007 compared with minority interest expense of \$6.0 million in 2006 related to minority shareholders' portion of earnings of Intelligent Processing Solutions Limited, and (c) an expense in 2007 of \$10.7 million to settle an escheat audit.

Income (loss) before income taxes in 2008 was a loss of \$77.0 million compared with income of \$3.5 million in 2007 and losses of \$250.9 million in 2006. The changes were principally due to the revenue declines, discussed above.

The company accounts for income taxes in accordance with SFAS No. 109, "Accounting for Income Taxes," which requires that deferred tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities. SFAS No. 109 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion or the entire deferred tax asset will not be realized.

The company evaluates quarterly the realizability of its deferred tax assets by assessing its valuation allowance and by adjusting the amount of such allowance, if necessary. The factors used to assess the likelihood of realization are the company's forecast of future taxable income and available tax-planning strategies that could be implemented to realize the net deferred tax assets. The company uses tax-planning strategies to realize or renew net deferred tax assets to avoid the potential loss of future tax benefits.

In 2005, based upon the level of historical taxable income and projections of future taxable income over the periods during which the deferred tax assets are deductible, management concluded that it is more likely than not that the U.S. and certain foreign deferred tax assets in excess of deferred tax liabilities would not be realized. A full valuation allowance was recognized in 2005 and is currently maintained for all U.S. and certain foreign deferred tax assets in excess of deferred tax liabilities. The company will record a tax provision or benefit for those international subsidiaries that do not have a full

valuation allowance against their deferred tax assets. Any profit or loss recorded for the company's U.S. operations will have no provision or benefit associated with it. As a result, the company's provision or benefit for taxes will vary significantly depending on the geographic distribution of income.

The realization of the remaining net deferred tax assets of approximately \$85 million as of December 31, 2008 is primarily dependent on forecasted future taxable income within certain foreign jurisdictions. Any reduction in estimated forecasted future taxable income may require the company to record an additional valuation allowance against the remaining deferred tax assets. Any increase or decrease in the valuation allowance would result in additional or lower income tax expense in such period and could have a significant impact on that period's earnings.

The provision for income taxes in 2008 was \$53.1 million compared with a provision of \$82.6 million in 2007 and a provision of \$27.8 million in 2006. The 2008 income tax provision includes a \$7.8 million benefit related to provisions in the Housing and Economic Recovery Act of 2008 permitting certain research and alternative minimum tax (AMT) credit carryforwards to be refundable, a \$9.7 million benefit due to a change in judgment resulting in a decrease in valuation allowances and a tax benefit of \$8.7 million related to prior year tax adjustments. The 2007 income tax provision includes a benefit of \$39.4 million related to a Netherlands income tax audit settlement and a provision of \$8.9 million due to a reduction of the UK income tax rate and its impact on the UK deferred tax assets (see Note 7 of the Notes to Consolidated Financial Statements). The increases in the 2008 and 2007 tax provision as compared with 2006 resulted from foreign withholding taxes and improved earnings in certain foreign jurisdictions during 2008 and 2007, while the company continues to record a full valuation allowance on pretax losses in jurisdictions where it is not more likely than not that the benefit of such losses will be realized.

In March 2006, the company sold all of the shares it owned in NUL, a publicly traded Japanese company. The company received gross proceeds of \$378.1 million and recognized a pretax gain of \$149.9 million in 2006. NUL continues to be the exclusive distributor of the company's hardware and software in Japan.

During the year ended December 31, 2006, the company recorded an equity loss related to NUL of \$4.2 million, which was recorded in "Other income (expense), net" in the company's consolidated statements of income. For the years ended December 31, 2008, 2007 and 2006, total direct and indirect sales to NUL were approximately \$134 million, \$185 million and \$245 million, respectively.

In 2005, the company and NUL amended the terms of a license and support agreement pursuant to which NUL receives access to certain of the company's intellectual property and support services. Under the revised arrangement, the company has granted NUL a perpetual license to the intellectual property, and, in lieu of an annual royalty, NUL paid the company a one-time fixed fee of \$225 million, one-half of which was paid in October 2005 and one-half of which was paid in September 2006. The company recognized the \$225 million as revenue over the three-year period ended March 31, 2008. The royalty fees are included in the direct and indirect sales disclosed above. In addition, the parties agreed that NUL would pay the company a fee of \$20 million per year during the three years ended March 31, 2008 for the support services it provides under the license and support agreement. In 2007, NUL exercised an option to renew the support services arrangement for an additional two years at the same price.

### *Segment results*

The company has two business segments: Services and Technology. Revenue classifications by segment are as follows: Services – systems integration and consulting, outsourcing, infrastructure services and core maintenance; Technology – enterprise-class servers and specialized technologies. The accounting policies of each business segment are the same as those followed by the company as a whole. Intersegment sales and transfers are priced as if the sales or transfers were to third parties. Accordingly, the Technology segment recognizes intersegment revenue and manufacturing profit on hardware and software shipments to customers under Services contracts. The Services segment, in turn, recognizes customer revenue and marketing profit on such shipments of company hardware and software to customers. The Services segment also includes the sale of hardware and software products sourced from third parties that are sold to customers through the

company's Services channels. In the company's consolidated statements of income, the manufacturing costs of products sourced from the Technology segment and sold to Services customers are reported in cost of revenue for Services.

Also included in the Technology segment's sales and operating profit are hardware and software sold to the Services segment for internal use in Services agreements. The amount of such profit included in operating income of the Technology segment for the years ended December 31, 2008, 2007 and 2006, was \$38.5 million, \$17.3 million and \$16.4 million, respectively. The profit on these transactions is eliminated in Corporate.

The company evaluates business segment performance on operating income exclusive of cost-reduction charges and unusual and nonrecurring items, which are included in Corporate. All other corporate and centrally incurred costs are allocated to the business segments, based principally on revenue, employees, square footage or usage. Therefore, the segment comparisons below exclude the cost-reduction charges mentioned above. See Note 16 of the Notes to Consolidated Financial Statements.

Information by business segment for 2008, 2007 and 2006 is presented below:

(millions of dollars)	Total	Eliminations	Services	Technology
<b>2008</b>				
Customer revenue	\$5,233.2		\$4,603.6	\$ 629.6
Intersegment		\$(232.0)	13.9	218.1
Total revenue	\$5,233.2	\$(232.0)	\$4,617.5	\$ 847.7
Gross profit percent	21.5%		18.1%	43.5%
Operating income percent	.8%		3.0%	4.1%
<b>2007</b>				
Customer revenue	\$5,652.5		\$4,846.7	\$ 805.8
Intersegment		\$(206.7)	13.9	192.8
Total revenue	\$5,652.5	\$(206.7)	\$4,860.6	\$ 998.6
Gross profit percent	22.8%		17.4%	47.0%
Operating income percent	1.5%		2.5%	8.3%
<b>2006</b>				
Customer revenue	\$5,757.2		\$4,917.2	\$ 840.0
Intersegment		\$(250.3)	14.8	235.5
Total revenue	\$5,757.2	\$(250.3)	\$4,932.0	\$1,075.5
Gross profit percent	17.5%		15.1%	44.2%
Operating income (loss) percent	(5.7)%		(.5)%	1.7%

*Gross profit percent and operating income percent are as a percent of total revenue.*

Customer revenue by classes of similar products or services, by segment, for 2008, 2007 and 2006 is presented below:

Year ended December 31 (millions)	2008	2007	Percent Change	2006	Percent Change
<b>Services</b>					
Systems integration and consulting	\$1,490.5	\$1,504.2	(.9)%	\$1,591.8	(5.5)%
Outsourcing	2,006.6	2,039.7	(1.6)%	1,916.2	6.4%
Infrastructure services	735.1	878.2	(16.3)%	948.2	(7.4)%
Core maintenance	371.4	424.6	(12.5)%	461.0	(7.9)%
	<u>4,603.6</u>	<u>4,846.7</u>	(5.0)%	<u>4,917.2</u>	(1.4)%
<b>Technology</b>					
Enterprise-class servers	515.8	647.3	(20.3)%	668.6	(3.2)%
Specialized technologies	113.8	158.5	(28.2)%	171.4	(7.5)%
	<u>629.6</u>	<u>805.8</u>	(21.9)%	<u>840.0</u>	(4.1)%
<b>Total</b>	<b>\$5,233.2</b>	<b>\$5,652.5</b>	<b>(7.4)%</b>	<b>\$5,757.2</b>	<b>(1.8)%</b>

In the Services segment, customer revenue was \$4.60 billion in 2008, \$4.85 billion in 2007 and \$4.92 billion in 2006. Foreign currency had about a 1-percentage-point positive impact on Services revenue in 2008 compared with 2007.

Revenue from systems integration and consulting decreased .9% from \$1.50 billion in 2007 to \$1.49 billion in 2008; in 2007 it decreased 5.5% from \$1.59 billion in 2006. The 2007 decline was due to disruptions in this business related to streamlining of the portfolio, personnel retraining and other repositioning actions.

Outsourcing revenue decreased 1.6% from \$2.04 billion in 2007 to \$2.01 billion in 2008; in 2007 it increased by 6.4% from \$1.92 billion in 2006, led by increases in both information technology outsourcing (ITO) and business processing outsourcing (BPO).

Infrastructure services revenue declined 16.3% from \$878.2 million in 2007 to \$735.1 million in 2008; in 2007 it decreased 7.4% from \$948.2 million in 2006. The decline in both periods was due to weakness in demand for network design and consulting projects, the shift of project-based infrastructure work to managed outsourcing contracts and the company's shift away from low-margin project work.

Core maintenance revenue declined 12.5% from \$424.6 million in 2007 to \$371.4 million in 2008; it decreased 7.9% in 2007 from \$461.0 million in 2006. The company expects the secular decline of core maintenance to continue.

Services gross profit was 18.1% in 2008, 17.4% in 2007 and 15.1% in 2006. Services operating income (loss) percent was 3.0% in 2008 compared with 2.5% in 2007 and (0.5)% in 2006. Services margins in 2008 reflect a decline in pension expense in gross profit of \$64.7 million (income of \$37.5 million in 2008 compared with expense of \$27.2 million in 2007) and a decline in pension expense in operating income of \$76.4 million (income of \$41.2 million in 2008 compared with expense of \$35.2 million in 2007). The improvement in the Services margins in 2007 compared with 2006 was principally due to the benefits derived from the cost-reduction actions as well as a decline in pension expense in gross profit of \$70.6 million (\$27.2 million in 2007 compared with \$97.8 million in 2006) and a decline in pension expense in operating income of \$85.9 million (\$35.2 million in 2007 compared with \$121.1 million in 2006).

In the Technology segment, customer revenue was \$629.6 million in 2008, \$805.8 million in 2007 and \$840.0 million in 2006. Foreign currency translation had about a 1-percentage-point positive impact on Technology revenue in 2008 compared with 2007. The decline in Technology revenue in 2008 reflects the NUL revenue decline beginning in April 2008 due to expiration of the royalty fee, discussed above. The company had recognized revenue of \$18.8 million per quarter (\$8.5 million in enterprise-class servers and \$10.3 million in specialized technologies) under this royalty agreement over the three-year period ended March 31, 2008. The expiration of this royalty from NUL contributed about 7 percentage points, or approximately \$56 million, of the technology segment's 22% decline in revenue. The company expects that future technology revenue will reflect the continuing secular decline in enterprise servers.

Revenue for the company's enterprise-class servers, which includes the company's ClearPath and ES7000 product families, declined 20.3% from \$647.3 million in 2007 to \$515.8 million in 2008; it decreased 3.2% in 2007 from \$668.6 million in 2006. The decline in 2008 compared with 2007 was principally due to the secular decline in enterprise-class servers and the expiration of the NUL royalty, described above.

Revenue from specialized technologies, which includes third-party technology products, the company's payment systems products and royalties from the company's agreement with NUL, decreased 28.2% from \$158.5 million in 2007 to \$113.8 million in 2008; it decreased 7.5% in 2007 from \$171.4 million in 2006. The 2008 decline was principally due to the ending of the NUL royalties, discussed above.

Technology gross profit was 43.5% in 2008, 47.0% in 2007 and 44.2% in 2006. Technology operating income percent was 4.1% in 2008 compared with 8.3% in 2007 and 1.7% in 2006. The decline in operating profit margin in 2008 compared with 2007 primarily reflects the NUL revenue decline, discussed above, as well as the continuing secular decline in enterprise servers. The improvement in the Technology margins in 2007 compared with 2006 was principally due to a higher mix of high margin software revenue in 2007 compared with 2006 as well as a decline in pension expense included in gross profit of \$1.9 million (\$.4 million income in 2007 compared with \$1.5 million of expense in 2006) and a decline in pension expense included in operating income of \$14.6 million (\$.2 million income in 2007 compared with \$14.4 million of expense in 2006).

## New accounting pronouncements

See Note 5 of the Notes to Consolidated Financial Statements for a full description of recent accounting pronouncements, including the expected dates of adoption and estimated effects on results of operations and financial condition.

## Financial condition

The company's principal sources of liquidity are cash on hand, cash from operations and its U.S. trade accounts receivable facility, which is discussed below. The company's anticipated future cash expenditures are discussed below and include anticipated contributions to its defined benefit pension plans and payments in respect of cost-reduction actions. The company also has a revolving credit facility, which expires in May 2009 that provides for loans and letters of credit up to an aggregate of \$275 million. Given the global economic slowdown and resultant tight credit markets, the company does not expect to renew or replace its existing revolving credit facility before its expiration on May 31, 2009. In addition, the company's ability to refinance or exchange its \$300 million senior notes due in March 2010 could be affected by the adverse credit market conditions. The volatility and disruption in financial markets could also impact the company's ability to utilize surety bonds, letters of credit, foreign exchange derivatives and other financial instruments the company uses to conduct its business. In addition to the actions discussed above to reduce its cost structure, the company will continue to focus on working capital management and to tightly manage capital expenditures. Given these actions and its cash on hand at December 31, 2008, the company believes that it will have adequate sources of liquidity to meet its expected 2009 cash requirements.

Cash and cash equivalents at December 31, 2008 were \$544.0 million compared with \$830.2 million at December 31, 2007. Cash and cash equivalents at December 31, 2007 included \$204 million of proceeds from a debt issuance in December 2007 used to refinance other debt in January 2008, discussed below.

During 2008, cash provided by operations was \$254.6 million compared with \$173.1 million in 2007. Cash expenditures related to current-year and prior-year restructuring actions (which are included in operating activities) in 2008 and 2007 were \$60.4 million and \$151.7 million, respectively. Cash expenditures for the current-year and prior-year restructuring actions are expected to be approximately \$68 million in 2009. In 2007, the company received a tax refund of approximately \$57 million from the Netherlands related to a settlement of an income tax audit. At December 31, 2008 and December 31, 2007, receivables of \$141 million and \$140 million, respectively, were sold under the company's U.S. securitization.

Cash used for investing activities in 2008 was \$283.0 million compared with cash used of \$290.7 million in 2007. Proceeds from investments and purchases of investments reflect the cash flows from derivative financial instruments used to manage the company's currency exposure to market risks from changes in foreign currency exchange rates. In 2008, net proceeds of investments were \$17.9 million compared with net purchases of \$9.8 million in 2007. In addition in 2008, the investment in marketable software was \$84.5 million compared with \$94.0 million in 2007, capital additions of properties were \$76.9 million in 2008 compared with \$77.5 million in 2007 and capital additions of outsourcing assets were \$133.1 million in 2008 compared with \$137.5 million in 2007. During 2007, the company financed the acquisition of \$22.6 million of internal-use software licenses and \$6.8 million of outsourcing assets. The company has announced its plans to significantly reduce capital expenditures from \$294.5 million in 2008 to approximately \$200 million to \$250 million in 2009.

Cash used for financing activities during 2008 was \$200.9 million compared with cash provided of \$209.6 million in 2007. The prior-year period includes \$204.2 million net proceeds from the December 2007 issuance of \$210 million of 12 1/2% senior notes due 2016. Using the proceeds from such notes, on January 11, 2008, the company redeemed, at par, all \$200 million of its 7 7/8% senior notes due April 1, 2008. The prior-year period includes \$12.3 million of cash received due to the exercise of stock options compared with zero received in 2008. The prior-year period also includes a cash expenditure of \$5.8 million for dividends paid to minority shareholders.

At December 31, 2008, total debt was \$1.1 billion, a decrease of \$202.1 million from December 31, 2007, due to the debt refinancing described above.

The company's revolving credit facility, which expires in May 2009 provides for loans and letters of credit up to an aggregate of \$275 million. As of December 31, 2008, there were letters of credit of \$62.1 million issued under the facility and there were no cash borrowings. The credit facility is secured by the company's assets, except that the collateral does not include accounts receivable that are subject to the receivables facility, U.S. real estate or the stock or indebtedness of the company's U.S. operating subsidiaries. Under the terms of the maturing facility, the company expects to be required to cash collateralize the letters of credit outstanding under the facility as at March 2, 2009. Borrowings under the facility bear interest based on short-term rates and the company's credit rating. The credit agreement contains customary representations and warranties, including no material adverse change in the company's business, results of operations or financial condition. It also contains financial covenants requiring the company to maintain certain interest coverage, leverage and asset coverage ratios and a minimum amount of liquidity, which could reduce the amount the company is able to borrow. The credit facility also includes covenants limiting liens, mergers, asset sales, dividends and the incurrence of debt. Events of default include nonpayment, failure to perform covenants, materially incorrect representations and warranties, change of control and default under other debt aggregating at least \$25 million. If an event of default were to occur under the credit agreement, the lenders would be entitled to declare all amounts borrowed under it immediately due and payable. The occurrence of an event of default under the credit agreement could also cause the acceleration of obligations under certain other agreements and the termination of the company's U.S. trade accounts receivable facility, discussed below.

In addition, the company and certain international subsidiaries have access to uncommitted lines of credit from various banks.

On May 16, 2008, the company entered into a new three-year, U.S. trade accounts receivable facility. Under this facility, the company has agreed to sell, on an ongoing basis, through Unisys Funding Corporation I, a wholly owned subsidiary, up to \$150 million of interests in eligible U.S. trade accounts receivable. The facility replaced the company's U.S. trade accounts receivable facility that was scheduled to terminate on May 28, 2008. Under the new facility, receivables are sold at a discount that reflects, among other things, a yield based on LIBOR subject to a minimum rate. The new facility includes customary representations and warranties, including no material adverse change in the company's business, assets, liabilities, operations or financial condition. It also requires the company to maintain a minimum fixed charge coverage ratio and requires the maintenance of certain ratios related to the sold receivables. The facility will be subject to early termination if, as of February 28, 2010, the company's 6.875% Senior Notes due 2010 have not been refinanced or extended to a date later than May 16, 2011. Other termination events include failure to perform covenants, materially incorrect representations and warranties, change of control and default under debt aggregating at least \$25 million. The average life of the receivables sold is about 54 days. At December 31, 2008 and December 31, 2007, the company had sold \$141 million and \$140 million, respectively, of eligible receivables.

At December 31, 2008, the company has met all covenants and conditions under its various lending and funding agreements. The company expects to continue to meet these covenants and conditions.

As described more fully in Notes 3, 10 and 13 of the Notes to Consolidated Financial Statements, at December 31, 2008, the company had certain cash obligations, which are due as follows:

(millions of dollars)	Total	Less than			
		1 year	1-3 years	4-5 years	After 5 years
Long-term debt	\$1,062.1	\$ .5	\$301.0	\$400.6	\$360.0
Internal-use software financing	10.3	8.3	2.0	—	—
Interest payments on long-term debt	445.0	91.6	152.3	110.0	91.1
Capital lease obligations	1.1	1.0	.1	—	—
Operating leases	453.3	100.4	141.5	87.0	124.4
Minimum purchase obligations	38.3	8.7	15.8	13.8	—
Work-force reductions	52.3	52.3	—	—	—
<b>Total</b>	<b>\$2,062.4</b>	<b>\$262.8</b>	<b>\$612.7</b>	<b>\$611.4</b>	<b>\$575.5</b>

As described in Note 17 of the Notes to Consolidated Financial Statements, the company expects to make cash contributions of approximately \$90 million to its worldwide defined benefit pension plans, principally international plans, in 2009. In accordance with regulations governing contributions to U.S. defined benefit pension plans, the company is not required to make cash contributions to its U.S. qualified defined benefit pension plan in 2009. Under current U.S. Pension Protection Act (PPA) rules, the company believes the cash contribution it would be required to make in 2010 to its U.S. qualified defined benefit pension plan would be approximately \$90 million. This amount could be less if the markets have a significant rally in 2009 or if Congress makes legislative changes to the PPA.

At December 31, 2008, the company had outstanding standby letters of credit and surety bonds of approximately \$265 million related to performance and payment guarantees. On the basis of experience with these arrangements, the company believes that any obligations that may arise will not be material.

The company may, from time to time, redeem, tender for, or repurchase its securities in the open market or in privately negotiated transactions depending upon availability, market conditions and other factors. The company has on file with the Securities and Exchange Commission an effective registration statement covering \$440 million of debt or equity securities, which expires in May 2009 and enables the company to be prepared for future market opportunities. In November 2008, the company filed a registration statement for an additional \$660 million of securities. This registration statement is not yet effective.

Stockholders' equity decreased \$1.82 billion during 2008, principally reflecting a decline of \$1.63 billion in the funded status of the company's defined benefit plans, a net loss of \$130.1 million, and \$106.2 million of currency translation losses, offset in part by \$42.8 million from share-based plans.

## **Market risk**

The company has exposure to interest rate risk from its short-term and long-term debt. In general, the company's long-term debt is fixed rate, and, to the extent it has any, its short-term debt is variable rate. See Note 10 of the Notes to Consolidated Financial Statements for components of the company's long-term debt. The company believes that the market risk assuming a hypothetical 10% increase in interest rates would not be material to the fair value of these financial instruments, or the related cash flows, or future results of operations.

The company is also exposed to foreign currency exchange rate risks. The company is a net receiver of currencies other than the U.S. dollar and, as such, can benefit from a weaker dollar, and can be adversely affected by a stronger dollar relative to major currencies worldwide. Accordingly, changes in exchange rates, and in particular a strengthening of the U.S. dollar, may adversely affect consolidated revenue and operating margins as expressed in U.S. dollars. To minimize currency exposure gains and losses, the company enters into forward exchange contracts and has natural hedges by purchasing components and incurring expenses in local currencies. The company uses derivative financial instruments to reduce its exposure to market risks from changes in foreign currency exchange rates. The derivative instruments used are foreign exchange forward contracts and foreign exchange options. See Note 14 of the Notes to Consolidated Financial Statements for additional information on the company's derivative financial instruments.

The company has performed a sensitivity analysis assuming a hypothetical 10% adverse movement in foreign currency exchange rates applied to these derivative financial instruments described above. As of December 31, 2008 and 2007, the analysis indicated that such market movements would have reduced the estimated fair value of these derivative financial instruments by approximately \$3 million and \$50 million, respectively. The decline in the estimated fair value of these derivative financial instruments reflects the fact that in the fourth quarter of 2008 the company capitalized certain intercompany balances for foreign subsidiaries which reduced the need for these derivatives. Based on changes in the timing and amount of interest rate and foreign currency exchange rate movements and the company's actual exposures and hedges, actual gains and losses in the future may differ from the above analysis.

## Critical accounting policies

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates, judgments and assumptions that affect the amounts reported in the financial statements and accompanying notes. Certain accounting policies, methods and estimates are particularly important because of their significance to the financial statements and because of the possibility that future events affecting them may differ from management's current judgments. The company bases its estimates and judgments on historical experience and on other assumptions that it believes are reasonable under the circumstances; however, to the extent there are material differences between these estimates, judgments and assumptions and actual results, the financial statements will be affected. Although there are a number of accounting policies, methods and estimates affecting the company's financial statements as described in Note 1 of the Notes to Consolidated Financial Statements, the following critical accounting policies reflect the significant estimates, judgments and assumptions. The development and selection of these critical accounting policies have been determined by management of the company and the related disclosures have been reviewed with the Audit Committee of the Board of Directors.

### *Outsourcing*

Typically, the initial terms of the company's outsourcing contracts are between 3 and 10 years. In certain of these arrangements, the company hires certain of the customers' employees and often becomes responsible for the related employee obligations, such as pension and severance commitments. In addition, system development activity on outsourcing contracts often requires significant upfront investments by the company. The company funds these investments, and any employee-related obligations, from customer prepayments and operating cash flow. Also, in the early phases of these contracts, gross margins may be lower than in later years when the work force and facilities have been rationalized for efficient operations, and an integrated systems solution has been implemented.

Revenue under these contracts is recognized when the company performs the services or processes transactions in accordance with contractual performance standards. Customer prepayments (even if nonrefundable) are deferred (classified as a liability) and recognized systematically as revenue over future periods as services are delivered or performed.

Costs on outsourcing contracts are charged to expense as incurred. However, direct costs incurred related to the inception of an outsourcing contract are deferred and charged to expense over the contract term. These costs consist principally of initial customer setup and employment obligations related to employees hired under terms of the outsourcing contracts. In addition, the costs of equipment and software, some of which are internally developed, are capitalized and depreciated over the shorter of their life or the term of the contract.

Recoverability of outsourcing assets is subject to various business risks, including the timely completion and ultimate cost of the outsourcing solution, and realization of expected profitability of existing outsourcing contracts. The company quarterly compares the carrying value of the outsourcing assets with the undiscounted future cash flows expected to be generated by the outsourcing assets to determine if there is an impairment. If impaired, the outsourcing assets are reduced to an estimated fair value on a discounted cash flow approach. The company prepares its cash flow estimates based on assumptions that it believes to be reasonable but are also inherently uncertain. Actual future cash flows could differ from these estimates. At December 31, 2008 and 2007, the net capitalized amount related to outsourcing contracts was \$314.9 million and \$409.4 million, respectively.

### *Revenue recognition*

The majority of the company's sales agreements contain standard business terms and conditions; however, some agreements contain multiple elements or non-standard terms and conditions. As discussed in Note 1 of the Notes to Consolidated Financial Statements, the company enters into multiple-element arrangements, which may include any combination of hardware, software or services. As a result, significant contract interpretation is sometimes required to determine the appropriate accounting, including whether the deliverables specified in a multiple-element arrangement should be treated as separate units of accounting for revenue recognition purposes, and, if so, how the price should be allocated

among the elements and when to recognize revenue for each element. The company recognizes revenue on delivered elements only if: (a) any undelivered products or services are not essential to the functionality of the delivered products or services, (b) the company has an enforceable claim to receive the amount due in the event it does not deliver the undelivered products or services, (c) there is evidence of the fair value for each undelivered product or service, and (d) the revenue recognition criteria otherwise have been met for the delivered elements. Otherwise, revenue on delivered elements is recognized as the undelivered elements are delivered. For arrangements with multiple elements where software is more than incidental to the arrangement, fair value of undelivered products or services is determined by “vendor-specific objective evidence,” which is based upon normal pricing and discounting practices for those products and services when sold separately. The company’s continued ability to determine vendor-specific objective evidence of fair value will depend on continued sufficient volumes and sufficient consistent pricing of stand-alone sales of such undelivered elements. In addition, the company’s revenue recognition policy states that revenue is not recognized until collectibility is deemed probable. Changes in judgments on these assumptions and estimates could materially impact the timing of revenue recognition.

For long-term fixed price systems integration contracts, the company recognizes revenue and profit as the contracts progress using the percentage-of-completion method of accounting, which relies on estimates of total expected contract revenues and costs. The company follows this method because reasonably dependable estimates of the revenue and costs applicable to various elements of a contract can be made. The financial reporting of these contracts depends on estimates, which are assessed continually during the term of the contracts and therefore, recognized revenues and profit are subject to revisions as the contract progresses to completion. Revisions in profit estimates are reflected in the period in which the facts that give rise to the revision become known. Accordingly, favorable changes in estimates result in additional revenue and profit recognition, and unfavorable changes in estimates result in a reduction of recognized revenue and profit. When estimates indicate that a loss will be incurred on a contract upon completion, a provision for the expected loss is recorded in the period in which the loss becomes evident. As work progresses under a loss contract, revenue continues to be recognized, and a portion of the contract costs incurred in each period is charged to the contract loss reserve. For other systems integration projects, the company recognizes revenue when the services have been performed.

#### *Income Taxes*

The company accounts for income taxes in accordance with SFAS No. 109, “Accounting for Income Taxes,” which requires that deferred tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities. SFAS No. 109 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion or the entire deferred tax asset will not be realized. In 2005, the company recorded a noncash charge of \$1.6 billion to increase the valuation allowance against deferred taxes.

At December 31, 2008 and 2007, the company had deferred tax assets in excess of deferred tax liabilities of \$2,672 million and \$2,042 million, respectively. For the reasons cited below, at December 31, 2008 and 2007, management determined that it is more likely than not that \$85 million and \$75 million, respectively, of such assets will be realized, resulting in a valuation allowance of \$2,587 million and \$1,967 million, respectively.

The company evaluates the realizability of its deferred tax assets by assessing its valuation allowance and by adjusting the amount of such allowance, if necessary. The factors used to assess the likelihood of realization are the company’s historical profitability, forecast of future taxable income and available tax-planning strategies that could be implemented to realize the net deferred tax assets. The company uses tax-planning strategies to realize or renew net deferred tax assets to avoid the potential loss of future tax benefits.

Failure to achieve forecasted taxable income might affect the ultimate realization of the net deferred tax assets. Factors that may affect the company’s ability to achieve sufficient forecasted taxable income include, but are not limited to, the following: increased competition, a continuing decline in sales or margins, loss of market share, delays in product availability or technological obsolescence. See “Factors that may affect future results.”

The company’s provision for income taxes and the determination of the resulting deferred tax assets and liabilities involve a significant amount of management judgment and are based on the best information available at the time. The company

operates within federal, state and international taxing jurisdictions and is subject to audit in these jurisdictions. These audits can involve complex issues, which may require an extended period of time to resolve. As a result, the actual income tax liabilities in the jurisdictions with respect to any fiscal year are ultimately determined long after the financial statements have been published.

Effective January 1, 2007, the company adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109" (FIN 48). FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The company maintains reserves for estimated tax exposures including penalties and interest. Income tax exposures include potential challenges of research and development credits and intercompany pricing. Exposures are settled primarily through the settlement of audits within these tax jurisdictions, but can also be affected by changes in applicable tax law or other factors, which could cause management of the company to believe a revision of past estimates is appropriate. Management believes that an appropriate liability has been established for estimated exposures; however, actual results may differ materially from these estimates. The liabilities are reviewed quarterly for their adequacy and appropriateness (see Note 7 of the Notes to Consolidated Financial Statements).

### *Pensions*

The company accounts for its defined benefit pension plans in accordance with SFAS No. 87, "Employers' Accounting for Pensions," and SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)," which require that amounts recognized in financial statements be determined on an actuarial basis. The measurement of the company's pension obligations, costs and liabilities is dependent on a variety of assumptions selected by the company and used by the company's actuaries. These assumptions include estimates of the present value of projected future pension payments to plan participants, taking into consideration the likelihood of potential future events such as salary increases and demographic experience. The assumptions used in developing the required estimates include the following key factors: discount rates, salary growth, retirement rates, inflation, expected return on plan assets and mortality rates.

As permitted for purposes of computing pension expense, the company uses a calculated value of plan assets (which is further described below). This allows that the effects of the performance of the pension plan's assets and changes in pension liability discount rates on the company's computation of pension income (expense) be amortized over future periods. A substantial portion of the company's pension plan assets and liabilities relates to its qualified defined benefit plan in the United States.

A significant element in determining the company's pension income (expense) is the expected long-term rate of return on plan assets. The company sets the expected long-term rate of return based on the expected long-term return of the various asset categories in which it invests. The company considers the current expectations for future returns and the actual historical returns of each asset class. Also, because the company's investment policy is to actively manage certain asset classes where the potential exists to outperform the broader market, the expected returns for those asset classes are adjusted to reflect the expected additional returns. For 2009 and 2008, the company has assumed that the expected long-term rate of return on U.S. plan assets will be 8.75%. A change of 25 basis points in the expected long-term rate of return for the company's U.S. pension plan causes a change of approximately \$11 million in pension expense. The assumed long-term rate of return on assets is applied to a calculated value of plan assets, which recognizes changes in the fair value of plan assets in a systematic manner over four years. This produces the expected return on plan assets that is included in pension income (expense). The difference between this expected return and the actual return on plan assets is deferred. The net deferral of past asset gains (losses) affects the calculated value of plan assets and, ultimately, future pension income (expense). At December 31, 2008, for the company's U.S. qualified defined benefit pension plan, the calculated value of plan assets was \$4.58 billion and the fair value was \$3.30 billion.

At the end of each year, the company determines the discount rate to be used to calculate the present value of plan liabilities. The discount rate is an estimate of the current interest rate at which the pension liabilities could be effectively

settled at the end of the year. In estimating this rate, the company looks to rates of return on high-quality, fixed-income investments that (a) receive one of the two highest ratings given by a recognized ratings agency and (b) are currently available and expected to be available during the period to maturity of the pension benefits. At December 31, 2008, the company determined this rate to be 6.75% for its U.S. defined benefit pension plans, an increase of 37 basis points from the rate used at December 31, 2007. A change of 25 basis points in the U.S. discount rate causes a change in pension expense of approximately \$11 million and a change of approximately \$111 million in the benefit obligation. The net effect of changes in the discount rate, as well as the net effect of other changes in actuarial assumptions and experience, has been deferred, as permitted.

Gains and losses are defined as changes in the amount of either the projected benefit obligation or plan assets resulting from experience different from that assumed and from changes in assumptions. Because gains and losses may reflect refinements in estimates as well as real changes in economic values and because some gains in one period may be offset by losses in another and vice versa, the accounting rules do not require recognition of gains and losses as components of net pension cost of the period in which they arise.

As a minimum, amortization of an unrecognized net gain or loss must be included as a component of net pension cost for a year if, as of the beginning of the year, that unrecognized net gain or loss exceeds 10 percent of the greater of the projected benefit obligation or the calculated value of plan assets. If amortization is required, the minimum amortization is that excess above the 10 percent divided by the average remaining service period of active employees expected to receive benefits under the plan. For the company's U.S. defined benefit pension plan, that period is approximately 8.2 years. At December 31, 2008, based on the calculated value of plan assets, the estimated unrecognized loss was \$1.11 billion.

For the year ended December 31, 2008, the company recognized consolidated pretax pension income of \$51.3 million, compared with pretax pension expense of \$35.0 million of consolidated pretax pension expense for the year ended December 31, 2007. The decrease in pension expense in 2008 from 2007 was principally due to increases in discount rates and higher return on plan assets in prior years. See Note 17 of the Notes to Consolidated Financial Statements.

For 2009, the company expects to recognize pension income of approximately \$11 million comprising \$12 million of income in the U.S. and \$1 million of expense in international plans. This would represent a decrease in pension income of approximately \$40 million from 2008.

During 2008, the company made cash contributions to its worldwide defined benefit pension plans (principally international plans) of approximately \$78 million and expects to make cash contributions of approximately \$90 million during 2009. In accordance with regulations governing contributions to U.S. defined benefit pension plans, the company is not required to make cash contributions to its U.S. qualified defined benefit pension plan in 2009. However, under current U.S. Pension Protection Act (PPA) rules, the company believes the cash contribution it would be required to make in 2010 to its U.S. qualified defined benefit pension plan would be approximately \$90 million. This amount could be less if the markets have a significant rally in 2009 or if Congress makes legislative changes to the PPA.

### *Restructuring*

In each of the last three years, the company engaged in actions associated with cost reduction initiatives which are accounted for under SFAS No. 112, "Employers' Accounting for Postemployment Benefits," SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," and SFAS No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits." The company's cost-reduction actions require significant estimates including (a) expenses for severance and other employee separation costs, (b) remaining lease obligations, including sublease income, and (c) other exit costs. The company has accrued amounts that it believes are its best estimates of the obligations it expects to incur in connection with these actions, but these estimates are subject to change due to market conditions and final negotiations. Should the actual amounts differ from the estimated amounts, the charges could be materially impacted. In 2008, 2007 and 2006, the company recognized \$550.0 million in cost reduction charges, which are discussed in more detail in Note 3 of the Notes to Consolidated Financial Statements.

## Factors that may affect future results

From time to time, the company provides information containing “forward-looking” statements, as defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements provide current expectations of future events and include any statement that does not directly relate to any historical or current fact. Words such as “anticipates,” “believes,” “expects,” “intends,” “plans,” “projects” and similar expressions may identify such forward-looking statements. All forward-looking statements rely on assumptions and are subject to risks, uncertainties and other factors that could cause the company’s actual results to differ materially from expectations. Factors that could affect future results include, but are not limited to, those discussed below. Any forward-looking statement speaks only as of the date on which that statement is made. The company assumes no obligation to update any forward-looking statement to reflect events or circumstances that occur after the date on which the statement is made.

Factors that could affect future results include the following:

*The company’s business is affected by the economic and business environment.* The company’s 2008 financial results were impacted by a global economic slowdown in the second half of the year. The company saw this slowdown particularly in its financial services business but also in other key commercial industries, as clients reacted to economic uncertainties by reducing IT spending. Decreased demand for the company’s services and products impacted its revenue and profit margins for the year. If current economic conditions continue or worsen, including if the company’s customers are unable to obtain financing to purchase the company’s services and products due to tight credit conditions, the company could see further reductions in demand and increased pressure on revenue and profit margins. The company could also see a further consolidation of firms in the financial services industry, which could also result in a decrease in demand. In addition, during the recent period of disruption in the financial markets, the market price for the company’s common shares has declined substantially. The company’s business could also be affected by acts of war, terrorism or natural disasters. Current world tensions could escalate, and this could have unpredictable consequences on the world economy and on the company’s business.

*The company’s future results may depend on its ability to access external credit markets.* The capital and credit markets have been experiencing extreme volatility and disruption during the past year. In addition, the commercial lending market has contracted, with limited new loan originations or refinancings taking place. Based on the current lending environment, the company expects to have difficulty accessing significant additional capital in the credit markets on acceptable terms. Given tight credit markets, along with the company’s credit rating, the company does not expect to renew or replace its existing revolving credit facility before its expiration on May 31, 2009. Under the terms of the maturing facility the company expects to be required to cash collateralize the letters of credit outstanding under the facility as of March 2, 2009. Also, the company’s ability to refinance or exchange its \$300 million senior notes due in March 2010 could be affected by the adverse credit market conditions. The turmoil and volatility in financial markets may also impact the company’s ability to utilize surety bonds, letters of credit, foreign exchange derivatives and other financial instruments the company uses to conduct its business. Although the company intends to use cash on hand to address its 2009 liquidity needs, its ability to do so assumes that its operations will continue to generate sufficient cash and that its cash requirements will not materially exceed current estimates.

*The company has significant pension obligations.* The company has unfunded obligations under its domestic and international defined benefit pension plans. The company expects to make cash contributions of approximately \$90 million to its worldwide, primarily international, defined benefit pension plans in 2009. Although the company is not required to make cash contributions to its U.S. qualified defined benefit pension plan in 2009 under current Pension Protection Act rules, the company believes the cash contribution it would be required to make to this plan in 2010 is approximately \$90 million. A further deterioration in the value of the company’s worldwide defined benefit pension plan assets could require the company to make larger cash contributions to its defined benefit pension plans in the future, which would reduce the cash available for working capital and other corporate uses and may have an adverse impact on the company’s operations, financial condition and liquidity.

*The company's future results will depend on the success of its turnaround program.* Over the past several years, the company has implemented and is continuing to implement, significant cost-reduction measures intended to achieve profitability. The company has incurred significant cost reduction charges in connection with these efforts. If the cost reduction actions are not fully completed or are not completed in a timely manner, the company may not realize their full potential benefits. The expected amount of anticipated cost savings from these actions is also subject to currency exchange rate fluctuations with regard to actions taken outside the United States. Future results will also depend in part on the success of the company's program to focus its global resources and simplify its business structure. This program is based on various assumptions, including assumptions regarding market segment growth, client demand, and the proper skill set of and training for sales and marketing management and personnel, all of which are subject to change. Furthermore, the company's institutional stockholders may attempt to influence these strategies.

*The company faces aggressive competition in the information services and technology marketplace.* The information services and technology markets in which the company operates include a large number of companies vying for customers and market share both domestically and internationally. The company's competitors include consulting and other professional services firms, systems integrators, outsourcing providers, infrastructure services providers, computer hardware manufacturers and software providers. Some of the company's competitors may develop competing products and services that offer better price-performance or that reach the market in advance of the company's offerings. Some competitors also have or may develop greater financial and other resources than the company, with enhanced ability to compete for market share, in some instances through significant economic incentives to secure contracts. Some also may be better able to compete for skilled professionals. Any of these factors could lead to reduced demand for the company's products and services and could have an adverse effect on the company's business. Future results will depend on the company's ability to mitigate the effects of aggressive competition on revenues, pricing and margins and on the company's ability to attract and retain talented people.

*The company faces volatility and rapid technological change in its industry.* The company operates in a highly volatile industry characterized by rapid technological change, evolving technology standards, short product life cycles and continually changing customer demand patterns. Future success will depend in part on the company's ability to anticipate and respond to these market trends and to design, develop, introduce, deliver or obtain new and innovative products and services on a timely and cost-effective basis. The company may not be successful in anticipating or responding to changes in technology, industry standards or customer preferences, and the market may not demand or accept its services and product offerings. In addition, products and services developed by competitors may make the company's offerings less competitive.

*The company's future results will depend on its ability to retain significant clients.* The company has a number of significant long-term contracts with clients, including governmental entities, and its future success will depend, in part, on retaining its relationships with these clients. The company could lose clients due to contract expiration, conversion to a competing service provider, disputes with clients or a decision to in-source services, including for contracts with governmental entities as part of the rebid process. The company could also lose clients as a result of their merger, acquisition or business failure. The company may not be able to replace the revenue and earnings from any such lost client.

*The company's future results will depend in part on its ability to grow outsourcing.* The company's outsourcing contracts are multiyear engagements under which the company takes over management of a client's technology operations, business processes or networks. In a number of these arrangements, the company hires certain of its clients' employees and may become responsible for the related employee obligations, such as pension and severance commitments. In addition, system development activity on outsourcing contracts may require the company to make significant upfront investments. The company will need to have available sufficient financial resources in order to take on these obligations and make these investments.

Recoverability of outsourcing assets is dependent on various factors, including the timely completion and ultimate cost of the outsourcing solution, and realization of expected profitability of existing outsourcing contracts. These risks could result in an impairment of a portion of the associated assets, which are tested for recoverability quarterly.

As long-term relationships, outsourcing contracts provide a base of recurring revenue. However, outsourcing contracts are highly complex and can involve the design, development, implementation and operation of new solutions and the transitioning of clients from their existing business processes to the new environment. In the early phases of these contracts, gross margins may be lower than in later years when an integrated solution has been implemented, the duplicate costs of transitioning from the old to the new system have been eliminated and the work force and facilities have been rationalized for efficient operations. Future results will depend on the company's ability to effectively and timely complete these implementations, transitions and rationalizations.

*Future results will also depend in part on the company's ability to drive profitable growth in consulting and systems integration.* The company's ability to grow profitably in this business will depend on the level of demand for systems integration projects and the portfolio of solutions the company offers for specific industries. It will also depend on an improvement in the utilization of services delivery personnel and on the company's ability to work through disruptions in this business related to the turnaround program. In addition, profit margins in this business are largely a function of the rates the company is able to charge for services and the chargeability of its professionals. If the company is unable to attain sufficient rates and chargeability for its professionals, profit margins will suffer. The rates the company is able to charge for services are affected by a number of factors, including clients' perception of the company's ability to add value through its services; introduction of new services or products by the company or its competitors; pricing policies of competitors; and general economic conditions. Chargeability is also affected by a number of factors, including the company's ability to transition employees from completed projects to new engagements, and its ability to forecast demand for services and thereby maintain an appropriate headcount.

*Future results will also depend, in part, on market demand for the company's high-end enterprise servers and maintenance on these servers.* In the company's technology business, high-end enterprise servers and maintenance on these servers continue to experience secular revenue declines. The company continues to apply its resources to develop value-added software capabilities and optimized solutions for these server platforms which provide competitive differentiation. Future results will depend, in part, on customer acceptance of ClearPath systems and the company's ability to maintain its installed base for ClearPath and to develop next-generation ClearPath products that are purchased by the installed base. Future results of the technology business will also depend, in part, on the successful execution of the company's arrangements with NEC.

*The company's contracts with U.S. governmental agencies may be subject to audits, criminal penalties, sanctions and other expenses and fines.* The company frequently enters into contracts with governmental entities. U.S. government agencies, including the Defense Contract Audit Agency and the Department of Labor, routinely audit government contractors. These agencies review a contractor's performance under its contracts, cost structure and compliance with applicable laws, regulations and standards. The U.S. government also may review the adequacy of, and a contractor's compliance with contract terms and conditions, its systems and policies, including the contractor's purchasing, property, estimating, billing, accounting, compensation and management information systems. Any costs found to be overcharged or improperly allocated to a specific contract or any amounts improperly billed for products or services will be subject to reimbursement to the government. If an audit uncovers improper or illegal activities, the company may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts, forfeiture of profits, suspension of payments, fines and suspension or prohibition from doing business with the U.S. government.

*The company's contracts may not be as profitable as expected or provide the expected level of revenues.* A number of the company's long-term contracts for infrastructure services, outsourcing, help desk and similar services do not provide for minimum transaction volumes. As a result, revenue levels are not guaranteed. In addition, some of these contracts may permit customer termination or may impose other penalties if the company does not meet the performance levels specified in the contracts.

The company's contracts with governmental entities are subject to the availability of appropriated funds. These contracts also contain provisions allowing the governmental entity to terminate the contract at the governmental entity's discretion

before the end of the contract's term. In addition, if the company's performance is unacceptable to the customer under a government contract, the government retains the right to pursue remedies under the affected contract, which remedies could include termination.

Certain of the company's outsourcing agreements require that the company's prices be benchmarked and provide for a downward adjustment to those prices if the pricing for similar services in the market has changed. As a result, anticipated revenues from these contracts may decline.

Some of the company's systems integration contracts are fixed-price contracts under which the company assumes the risk for delivery of the contracted services and products at an agreed-upon fixed price. At times the company has experienced problems in performing some of these fixed-price contracts on a profitable basis and has provided periodically for adjustments to the estimated cost to complete them. Future results will depend on the company's ability to perform these services contracts profitably.

*The company may face damage to its reputation or legal liability if its clients are not satisfied with its services or products.* The success of the company's business is dependent on strong, long-term client relationships and on its reputation for responsiveness and quality. As a result, if a client is not satisfied with the company's services or products, its reputation could be damaged and its business adversely affected. Allegations by private litigants or regulators of improper conduct, as well as negative publicity and press speculation about the company, whatever the outcome and whether or not valid, may harm its reputation. In addition to harm to reputation, if the company fails to meet its contractual obligations, it could be subject to legal liability, which could adversely affect its business, operating results and financial condition.

*Future results will depend in part on the performance and capabilities of third parties.* The company has commercial relationships with suppliers, channel partners and other parties that have complementary products, services or skills. Future results will depend, in part, on the performance and capabilities of these third parties, on the ability of external suppliers to deliver components at reasonable prices and in a timely manner, and on the financial condition of, and the company's relationship with, distributors and other indirect channel partners.

*The company is subject to the risks of doing business internationally.* More than half of the company's total revenue is derived from international operations. The risks of doing business internationally include foreign currency exchange rate fluctuations, changes in political or economic conditions, trade protection measures, import or export licensing requirements, multiple and possibly overlapping and conflicting tax laws, new tax legislation, weaker intellectual property protections in some jurisdictions and additional legal and regulatory compliance requirements applicable to businesses that operate internationally, including the Foreign Corrupt Practices Act and non-U.S. laws and regulations.

*If the company does not meet New York Stock Exchange listing requirements, its common stock may be delisted.* The company's common stock is listed on the New York Stock Exchange (NYSE) and is subject to various NYSE listing requirements. The company was notified in writing by the NYSE on December 4, 2008 that it was below the NYSE's criteria for continued listing because the average per share closing price of the common stock over a consecutive 30-trading-day period was less than \$1.00. On December 12, 2008, the company notified the NYSE of its intent to take actions to cure the deficiency, including a plan to pursue a reverse stock split. If the company fails to complete the reverse stock split or otherwise fails to meet the NYSE listing requirements, the NYSE may suspend trading in the company's common stock or delist it from the NYSE. A delisting could negatively impact the company by reducing the liquidity and market price of the common stock and reducing the number of investors willing to hold or acquire it, which could negatively affect the company's ability to raise equity financing.

*The company could face business and financial risk in implementing future dispositions or acquisitions.* As part of the company's business strategy, it may from time to time consider disposing of existing technologies, products and businesses that may no longer be in alignment with its strategic direction, including transactions of a material size or acquiring complementary technologies, products and businesses. Potential risks with respect to dispositions include difficulty finding buyers or alternative exit strategies on acceptable terms in a timely manner; potential loss of employees; and dispositions at unfavorable prices or on unfavorable terms, including relating to retained liabilities. Any acquisitions may result in the

incurrence of substantial additional indebtedness or contingent liabilities. Acquisitions could also result in potentially dilutive issuances of equity securities and an increase in amortization expenses related to intangible assets. Additional potential risks associated with acquisitions include integration difficulties; difficulties in maintaining or enhancing the profitability of any acquired business; risks of entering markets in which the company has no or limited prior experience; potential loss of employees or failure to maintain or renew any contracts of any acquired business; and expenses of any undiscovered or potential liabilities of the acquired product or business, including relating to employee benefits contribution obligations or environmental requirements. Further, with respect to both dispositions and acquisitions, management's attention could be diverted from other business concerns. Current adverse credit conditions could also affect the company's ability to consummate divestments or acquisitions. The risks associated with dispositions and acquisitions could have a material adverse effect upon the company's business, financial condition and results of operations. There can be no assurance that the company will be successful in consummating future dispositions or acquisitions on favorable terms or at all.

*The company's services or products may infringe upon the intellectual property rights of others.* The company cannot be sure that its services and products do not infringe on the intellectual property rights of third parties, and it may have infringement claims asserted against it or against its clients. These claims could cost the company money, prevent it from offering some services or products, or damage its reputation.

*Pending litigation could affect the company's results of operations or cash flow.* There are various lawsuits, claims, investigations and proceedings that have been brought or asserted against the company, which arise in the ordinary course of business, including actions with respect to commercial and government contracts, labor and employment, employee benefits, environmental matters and intellectual property. See Note 15 of the Notes to Consolidated Financial Statements for more information on litigation. The company believes that it has valid defenses with respect to legal matters pending against it. Litigation is inherently unpredictable, however, and it is possible that the company's results of operations or cash flow could be affected in any particular period by the resolution of one or more of the legal matters pending against it.