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UNISYS CORP  
Form 10-Q  
August 08, 2007

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

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FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2007

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission file number 1-8729

UNISYS CORPORATION  
(Exact name of registrant as specified in its charter)

|   |   |
|---|---|
| Delaware  | 38-0387840                              |
| (State or other jurisdiction<br>of incorporation or organization) | (I.R.S. Employer<br>Identification No.) |

|  |            |
|--|------------|
| Unisys Way                               |            |
| Blue Bell, Pennsylvania                  | 19424      |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: (215) 986-4011

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES  NO

Number of shares of Common Stock outstanding as of June 30, 2007:  
349,948,612.

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### Part I - FINANCIAL INFORMATION

#### Item 1. Financial Statements.

#### UNISYS CORPORATION CONSOLIDATED BALANCE SHEETS (Millions)

|   | June 30,<br>2007<br>(Unaudited) | December 31,<br>2006 |
|---|---------------------------------|----------------------|
|   | -----                           | -----                |
| Assets  |                                 |                      |
| -----   |                                 |                      |
| Current assets                                    |                                 |                      |
| Cash and cash equivalents                         | \$ 520.7                        | \$ 719.3             |
| Accounts and notes receivable, net                | 1,045.2                         | 1,164.6              |
| Inventories:                                      |                                 |                      |
| Parts and finished equipment                      | 101.2                           | 95.0                 |
| Work in process and materials                     | 86.5                            | 81.2                 |
| Deferred income taxes                             | 30.0                            | 30.0                 |
| Prepaid expenses and other current assets         | 173.1                           | 148.4                |
|   | -----                           | -----                |
| Total   | 1,956.7                         | 2,238.5              |
|   | -----                           | -----                |
| Properties  | 1,294.7                         | 1,233.4              |
| Less-Accumulated depreciation and<br>amortization | 943.8                           | 892.1                |
|   | -----                           | -----                |
| Properties, net                                   | 350.9                           | 341.3                |
|   | -----                           | -----                |
| Outsourcing assets, net                           | 419.2                           | 401.1                |
| Marketable software, net                          | 286.8                           | 304.3                |
| Prepaid postretirement assets                     | 308.8                           | 250.1                |
| Deferred income taxes                             | 191.3                           | 191.3                |
| Goodwill  | 196.8                           | 193.9                |
| Other long-term assets                            | 121.8                           | 117.4                |
|   | -----                           | -----                |
| Total   | \$3,832.3                       | \$4,037.9            |
|   | =====                           | =====                |
| Liabilities and stockholders' equity              |                                 |                      |
| -----   |                                 |                      |
| Current liabilities                               |                                 |                      |
| Notes payable                                     | \$ .6                           | \$ 1.2               |
| Current maturities of long-term debt              | 200.3                           | .5                   |
| Accounts payable                                  | 373.3                           | 460.9                |
| Other accrued liabilities                         | 1,342.1                         | 1,469.1              |
|   | -----                           | -----                |
| Total   | 1,916.3                         | 1,931.7              |
|   | -----                           | -----                |
| Long-term debt                                    | 849.3                           | 1,049.1              |
| Long-term postretirement liabilities              | 642.7                           | 667.7                |
| Other long-term liabilities                       | 426.2                           | 453.6                |
|   | -----                           | -----                |
| Stockholders' equity (deficit)                    |                                 |                      |
| Common stock, shares issued: 2007; 352.1          |                                 |                      |
| 2006, 347.5                                       | 3.5                             | 3.5                  |
| Accumulated deficit                               | (2,448.7)                       | (2,386.8)            |
| Other capital                                     | 3,984.2                         | 3,945.1              |
| Accumulated other comprehensive loss              | (1,541.2)                       | (1,626.0)            |
|   | -----                           | -----                |

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|                                |           |           |
|--------------------------------|-----------|-----------|
| Stockholders' equity (deficit) | (2.2)     | (64.2)    |
|                                | -----     | -----     |
| Total                          | \$3,832.3 | \$4,037.9 |
|                                | =====     | =====     |

See notes to consolidated financial statements.

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UNISYS CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)  
(Millions, except per share data)

|                                      | Three Months<br>Ended June 30 |            | Six Months<br>Ended June 30 |            |
|--------------------------------------|-------------------------------|------------|-----------------------------|------------|
|                                      | 2007                          | 2006       | 2007                        | 2006       |
|                                      | ----                          | ----       | ----                        | ----       |
| Revenue                              |                               |            |                             |            |
| Services                             | \$1,208.6                     | \$1,224.5  | \$2,361.5                   | \$2,400.9  |
| Technology                           | 167.1                         | 182.8      | 362.2                       | 394.2      |
|                                      | -----                         | -----      | -----                       | -----      |
|                                      | 1,375.7                       | 1,407.3    | 2,723.7                     | 2,795.1    |
| Costs and expenses                   |                               |            |                             |            |
| Cost of revenue:                     |                               |            |                             |            |
| Services                             | 992.2                         | 1,136.3    | 1,986.1                     | 2,212.8    |
| Technology                           | 84.1                          | 108.1      | 180.8                       | 217.5      |
|                                      | -----                         | -----      | -----                       | -----      |
|                                      | 1,076.3                       | 1,244.4    | 2,166.9                     | 2,430.3    |
| Selling, general and administrative  | 247.4                         | 282.7      | 492.0                       | 578.1      |
| Research and development             | 49.5                          | 63.9       | 91.9                        | 139.2      |
|                                      | -----                         | -----      | -----                       | -----      |
|                                      | 1,373.2                       | 1,591.0    | 2,750.8                     | 3,147.6    |
|                                      | -----                         | -----      | -----                       | -----      |
| Operating profit (loss)              | 2.5                           | (183.7)    | (27.1)                      | (352.5)    |
| Interest expense                     | 18.7                          | 19.1       | 37.6                        | 38.9       |
| Other income (expense), net          | (8.7)                         | (.7)       | 16.8                        | 152.7      |
|                                      | -----                         | -----      | -----                       | -----      |
| Loss before income taxes             | (24.9)                        | (203.5)    | (47.9)                      | (238.7)    |
| Provision (benefit) for income taxes | 40.6                          | (8.9)      | 14.0                        | (16.2)     |
|                                      | -----                         | -----      | -----                       | -----      |
| Net loss                             | \$ (65.5)                     | \$ (194.6) | \$ (61.9)                   | \$ (222.5) |
|                                      | =====                         | =====      | =====                       | =====      |
| Loss per share                       |                               |            |                             |            |
| Basic                                | \$ (.19)                      | \$ (.57)   | \$ (.18)                    | \$ (.65)   |
|                                      | =====                         | =====      | =====                       | =====      |
| Diluted                              | \$ (.19)                      | \$ (.57)   | \$ (.18)                    | \$ (.65)   |
|                                      | =====                         | =====      | =====                       | =====      |

See notes to consolidated financial statements.

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## UNISYS CORPORATION CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited) (Millions)

|  | Six Months Ended<br>June 30 |            |
|--|-----------------------------|------------|
|  | 2007                        | 2006       |
| Cash flows from operating activities   |                             |            |
| Net loss   | \$ (61.9)                   | \$ (222.5) |
| Add (deduct) items to reconcile net loss<br>to net cash used for operating activities: |                             |            |
| Equity loss  | -                           | 4.3        |
| Employee stock compensation  | 5.5                         | 3.2        |
| Company stock issued for U.S. 401(k) plan  | 23.0                        | 8.9        |
| Depreciation and amortization of properties  | 56.9                        | 58.5       |
| Depreciation and amortization of outsourcing assets                                    | 70.6                        | 66.7       |
| Amortization of marketable software  | 62.1                        | 66.2       |
| Gain on sale of assets   | (23.1)                      | (153.2)    |
| Increase in deferred income taxes, net   | -                           | (41.9)     |
| Decrease in receivables, net   | 136.0                       | 66.7       |
| (Increase) decrease in inventories   | (9.0)                       | 10.2       |
| (Decrease) increase in accounts payable and other<br>accrued liabilities               | (250.5)                     | 8.0        |
| Decrease in other liabilities  | (50.9)                      | (44.5)     |
| (Increase) decrease in other assets  | (39.9)                      | 1.2        |
| Other  | .1                          | 2.2        |
|  | (81.1)                      | (166.0)    |
| Net cash used for operating activities   |                             |            |
| Cash flows from investing activities   |                             |            |
| Proceeds from investments  | 3,942.4                     | 3,729.3    |
| Purchases of investments   | (3,941.0)                   | (3,731.3)  |
| Investment in marketable software  | (48.9)                      | (55.3)     |
| Capital additions of properties  | (39.8)                      | (32.7)     |
| Capital additions of outsourcing assets  | (78.5)                      | (50.1)     |
| Purchases of businesses  | (1.6)                       | -          |
| Proceeds from sale of assets   | 27.7                        | 380.6      |
|  | (139.7)                     | 240.5      |
| Net cash (used for) provided by<br>investing activities                                |                             |            |
| Cash flows from financing activities   |                             |            |
| Net reduction in short-term borrowings   | (.6)                        | (7.4)      |
| Proceeds from exercise of stock options  | 11.3                        | .9         |
| Payments of long-term debt   | -                           | (57.9)     |
| Cost of credit agreement   | -                           | (4.6)      |
|  | 10.7                        | (69.0)     |
| Net cash provided by (used for) financing<br>activities                                |                             |            |
| Effect of exchange rate changes on<br>cash and cash equivalents                        | 11.5                        | 7.1        |
|  | (198.6)                     | 12.6       |
| (Decrease) increase in cash and cash equivalents                                       |                             |            |
| Cash and cash equivalents, beginning of period   | 719.3                       | 642.5      |
|  |                             |            |

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|  |          |          |
|--|----------|----------|
| Cash and cash equivalents, end of period | \$ 520.7 | \$ 655.1 |
|  | =====    | =====    |

See notes to consolidated financial statements.

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Unisys Corporation  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

In the opinion of management, the financial information furnished herein reflects all adjustments necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods specified. These adjustments consist only of normal recurring accruals except as disclosed herein. Because of seasonal and other factors, results for interim periods are not necessarily indicative of the results to be expected for the full year.

a. The following table shows how earnings (loss) per share were computed for the three and six months ended June 30, 2007 and 2006 (dollars in millions, shares in thousands):

|  | Three Months<br>Ended June 30 |            | Six Months<br>Ended June 30 |            |
|--|-------------------------------|------------|-----------------------------|------------|
|  | 2007                          | 2006       | 2007                        | 2006       |
|  | ----                          | ----       | ----                        | ----       |
| Basic Loss Per Share   |                               |            |                             |            |
| Net loss   | \$ (65.5)                     | \$ (194.6) | \$ (61.9)                   | \$ (222.5) |
|  | =====                         | =====      | =====                       | =====      |
| Weighted average shares  | 348,958                       | 343,414    | 347,690                     | 342,936    |
|  | =====                         | =====      | =====                       | =====      |
| Basic loss per share   | \$ (.19)                      | \$ (.57)   | \$ (.18)                    | \$ (.65)   |
|  | =====                         | =====      | =====                       | =====      |
| Diluted Loss Per Share   |                               |            |                             |            |
| Net loss   | \$ (65.5)                     | \$ (194.6) | \$ (61.9)                   | \$ (222.5) |
|  | =====                         | =====      | =====                       | =====      |
| Weighted average shares  | 348,958                       | 343,414    | 347,690                     | 342,936    |
| Plus incremental shares<br>from assumed conversions<br>of employee stock plans | -                             | -          | -                           | -          |
|  | -----                         | -----      | -----                       | -----      |
| Adjusted weighted average shares   | 348,958                       | 343,414    | 347,690                     | 342,936    |
|  | =====                         | =====      | =====                       | =====      |
| Diluted loss per share   | \$ (.19)                      | \$ (.57)   | \$ (.18)                    | \$ (.65)   |
|  | =====                         | =====      | =====                       | =====      |

At June 30, 2007, no shares related to employee stock plans were included in the computation of diluted earnings per share since inclusion of these shares would be antidilutive because of the net loss incurred in the three and six months ended June 30, 2007.

b. In October 2005, the company announced a cost-reduction plan to right size the company's cost structure. 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, and was comprised of (a) a charge of \$72.4 million for 2,250 employees in the U.S. and (b) a

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charge of \$257.7 million for 3,415 employees outside the U.S.

As part of the company's continuing repositioning plan to right size its cost structure, during the three months ended June 30, 2007, the company consolidated facility space and committed to an additional reduction of 551 employees. This resulted in a pretax charge in the quarter of \$33.3 million. The charge related to work force reductions of \$19.8 million is broken down as follows: (a) 425 employees in the U.S. for a charge of \$12.0 million and (b) 126 employees outside the U.S. for a charge of \$7.8 million. The facility charge of \$13.5 million principally relates to leased property that the company ceased using as of June 30, 2007. The facility charge represents the fair value of the liability at the cease-use date and was determined based on the remaining lease rental payments, reduced by estimated sublease rentals that could be reasonably obtained for the property. The pretax charge was recorded in the following statement of income classifications: cost of revenue-services, \$6.8 million; cost of revenue-technology, \$.5 million; selling, general and administrative expenses, \$16.5 million; research and development expenses, \$9.7 million; and other income (expense), net, \$.2 million. The income recorded in other income (expense), net relates to minority shareholders' portion of the charge related to majority owned subsidiaries which are fully consolidated by the company.

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During the three months ended March 31, 2007, the company committed to a reduction of 966 employees. This resulted in a pretax charge in the March 2007 quarter of \$32.7 million, principally related to severance costs. The charge was broken down as follows: (a) 451 employees in the U.S. for a charge of \$11.6 million and (b) 515 employees outside the U.S. for a charge of \$21.1 million. The pretax charge was recorded in the following statement of income classifications: cost of revenue-services, \$25.0 million; selling, general and administrative expenses, \$2.1 million; research and development expenses, \$6.2 million; and other income (expense), net, \$.6 million.

The cost reduction actions taken in the first half of 2007 when combined with the 2006 actions bring the total pretax charge to \$396.1 million, comprised of \$382.6 million for 7,182 work force reductions and \$13.5 million for idle lease cost. The combined employee reduction actions are expected to be substantially completed by the end of 2007. During the current quarter, the company took the first steps to consolidate lease space around the world to reflect its recent headcount reductions and its continued move to an increasingly mobile services delivery work force. The company is currently looking at other potential opportunities and may take additional actions later in the year to further consolidate facility space.

For the six months ended June 30, 2007, the pretax charge of \$66.0 million was recorded in the following statement of income classifications: cost of revenue-services, \$31.8 million; cost of revenue-technology, \$.5 million; selling, general and administrative expenses, \$18.6 million; research and development expenses, \$15.9 million; and other income (expense), net, \$.8 million.

On March 31, 2006, the company committed to a reduction of approximately 3,600 employees. This resulted in a pretax charge in the first quarter of 2006 of \$145.9 million, principally related to severance costs. The charge was broken down as follows: (a) approximately 1,600 employees in the U.S. for a charge of \$50.3 million and (b) approximately 2,000 employees outside the U.S. for a charge of \$95.6 million. The pretax charge was recorded in the following statement of income classifications: cost of revenue-services, \$83.4 million; cost of revenue-technology, \$2.0 million; selling, general

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and administrative expenses, \$45.4 million; research and development expenses, \$17.6 million; and other income (expense), net, \$2.5 million.

During the three months ended June 30, 2006, the company committed to a reduction of approximately 1,900 employees. This resulted in a pretax charge in the second quarter of 2006 of \$141.2 million, principally related to severance costs. The charge is broken down as follows: (a) approximately 650 employees in the U.S. for a charge of \$22.1 million and (b) approximately 1,250 employees outside the U.S. for a charge of \$119.1 million. The pretax charge was recorded in the following statement of income classifications: cost of revenue-services, \$101.4 million; selling, general and administrative expenses, \$28.3 million; research and development expenses, \$11.8 million; and other income (expense), net, \$.3 million.

For the six months ended June 30, 2006, the pretax charge of \$287.1 million was recorded in the following statement of income classifications: cost of revenue-services, \$184.8 million; cost of revenue-technology, \$2.0 million; selling, general and administrative expenses, \$73.7 million; research and development expenses, \$29.4 million; and other income (expense), net, \$2.8 million.

A further breakdown of the individual components of these costs follows (in millions of dollars):

|                                    | Headcount | Total   | Work Force<br>Reductions |         | Idle<br>Lease Cost |
|------------------------------------|-----------|---------|--------------------------|---------|--------------------|
|                                    |           |         | U.S.                     | Int'l.  |                    |
|                                    | -----     | -----   | -----                    | -----   | -----              |
| Balance at December 31, 2006       | 757       | \$142.6 | \$ 26.1                  | \$116.5 |                    |
| Additional provisions              | 1,517     | 66.0    | 23.6                     | 28.9    | \$13.5             |
| Minority interest                  |           | .8      |                          | .8      |                    |
| Utilized                           | (911)     | (82.3)  | (22.4)                   | (59.9)  |                    |
| Changes in estimates and revisions | (110)     | (15.7)  | 6.0                      | (21.7)  |                    |
| Translation adjustments            |           | 1.7     |                          | 1.7     |                    |
|                                    | -----     | -----   | -----                    | -----   | -----              |
| Balance at June 30, 2007           | 1,253     | \$113.1 | \$33.3                   | \$ 66.3 | \$13.5             |
|                                    | =====     | =====   | =====                    | =====   | =====              |

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Expected future utilization:

|                           |       |        |        |         |        |
|---------------------------|-------|--------|--------|---------|--------|
| 2007 remaining six months | 1,082 | \$70.1 | \$25.1 | \$ 43.4 | \$ 1.6 |
| Beyond 2007               | 171   | 43.0   | 8.2    | 22.9    | 11.9   |

c. 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. In addition, 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 plan participants. 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 the first quarter of 2006.

Net periodic pension expense (income) for the three and six months ended June 30, 2007 and 2006 is presented below (in millions of dollars):

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|   | Three Months<br>Ended June 30, 2007 |          |         | Three Months<br>Ended June 30, 2006 |         |         |
|---|-------------------------------------|----------|---------|-------------------------------------|---------|---------|
|   | Total                               | U.S.     | Int'l.  | Total                               | U.S.    | Int'l.  |
|   |                                     | Plans    | Plans   |                                     | Plans   | Plans   |
| Service cost                                    | \$ 11.0                             | \$ -     | \$ 11.0 | \$ 27.4                             | \$ 15.2 | \$ 12.2 |
| Interest cost                                   | 100.3                               | 69.6     | 30.7    | 111.9                               | 84.2    | 27.7    |
| Expected return on<br>plan assets               | (133.3)                             | (97.3)   | (36.0)  | (140.7)                             | (110.3) | (30.4)  |
| Amortization of prior<br>service (benefit) cost | .1                                  | -        | .1      | (.2)                                | (.5)    | .3      |
| Recognized net actuarial<br>loss                | 33.3                                | 24.4     | 8.9     | 42.1                                | 29.9    | 12.2    |
| Net periodic pension<br>expense (income)        | \$ 11.4                             | \$ (3.3) | \$ 14.7 | \$ 40.5                             | \$ 18.5 | \$ 22.0 |

|   | Six Months<br>Ended June 30, 2007 |          |         | Six Months<br>Ended June 30, 2006 |         |         |
|---|-----------------------------------|----------|---------|-----------------------------------|---------|---------|
|   | Total                             | U.S.     | Int'l.  | Total                             | U.S.    | Int'l.  |
|   |                                   | Plans    | Plans   |                                   | Plans   | Plans   |
| Service cost                                    | \$ 21.8                           | \$ .1    | \$ 21.7 | \$ 57.2                           | \$ 33.6 | \$ 23.6 |
| Interest cost                                   | 200.1                             | 139.0    | 61.1    | 206.8                             | 152.3   | 54.5    |
| Expected return on<br>plan assets               | (266.5)                           | (194.9)  | (71.6)  | (260.6)                           | (201.0) | (59.6)  |
| Amortization of prior<br>service (benefit) cost | .3                                | -        | .3      | (.5)                              | (1.0)   | .5      |
| Recognized net actuarial<br>loss                | 66.3                              | 48.7     | 17.6    | 90.5                              | 66.4    | 24.1    |
| Curtailment gain                                | -                                 | -        | -       | (45.0)                            | (45.0)  | -       |
| Net periodic pension<br>expense (income)        | \$ 22.0                           | \$ (7.1) | \$ 29.1 | \$ 48.4                           | \$ 5.3  | \$ 43.1 |

The company currently expects to make cash contributions of approximately \$77 million to its worldwide defined benefit pension plans in 2007 compared with \$78.0 million in 2006. For the six months ended June 30, 2007 and 2006, \$34.3 million and \$33.7 million, respectively, of cash contributions have been made. In accordance with regulations governing contributions to U.S. defined benefit pension plans, the company is not required to fund its U.S. qualified defined benefit pension plan in 2007.

Net periodic postretirement benefit expense for the three and six months ended June 30, 2007 and 2006 is presented below (in millions of dollars):

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| Three Months<br>Ended June 30 |      | Six Months<br>Ended June 30 |      |
|-------------------------------|------|-----------------------------|------|
| 2007                          | 2006 | 2007                        | 2006 |

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|  |       |       |        |        |
|--|-------|-------|--------|--------|
|  | ----  | ----  | ----   | ----   |
| Interest cost                                  | \$3.1 | \$3.2 | \$ 6.1 | \$ 6.4 |
| Expected return on assets                      | (.2)  | -     | (.3)   | (.1)   |
| Amortization of prior<br>service benefit       | -     | (.5)  | -      | (1.0)  |
| Recognized net actuarial<br>loss               | 1.3   | 1.3   | 2.6    | 2.6    |
|  | ----  | ----  | ----   | ----   |
| Net periodic postretirement<br>benefit expense | \$4.2 | \$4.0 | \$ 8.4 | \$ 7.9 |
|  | ====  | ====  | ====   | ====   |

The company expects to make cash contributions of approximately \$30 million to its postretirement benefit plan in 2007 compared with \$26.9 million in 2006. For the six months ended June 30, 2007 and 2006, \$16.7 million and \$12.7 million, respectively, of cash contributions have been made.

d. In March 2006, the company sold all of the shares it owned in Nihon Unisys, Ltd. (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 the first quarter of 2006. NUL will remain the exclusive distributor of the company's hardware and software in Japan.

In February 2007, the company sold its media business for gross proceeds of \$27.7 million and recognized a pretax gain of \$23.1 million.

e. Under the company's stockholder approved stock-based plans, stock options, stock appreciation rights, restricted stock and restricted stock units may be granted to officers, directors and other key employees. As of June 30, 2007, the company has granted non-qualified stock options and restricted stock units under these plans. At June 30, 2007, 3.5 million shares of unissued common stock of the company were available for granting under these plans.

For the six months ended June 30, 2007, no stock options were granted. The company currently expects that any future grants of stock option awards will be principally to newly hired individuals.

The fair value of stock option awards was estimated using the Black-Scholes option pricing model with the following assumptions and weighted-average fair values:

|                                      | Six Months Ended June 30, |        |
|--------------------------------------|---------------------------|--------|
|                                      | 2007                      | 2006   |
|                                      | ----                      | ----   |
| Weighted-average fair value of grant | N/A                       | \$2.53 |
| Risk-free interest rate              | N/A                       | 4.35%  |
| Expected volatility                  | N/A                       | 45.88% |
| Expected life of options in years    | N/A                       | 3.67   |
| Expected dividend yield              | -                         | -      |

For periods after January 1, 2006, the company has granted an annual restricted stock unit award to officers, directors and other key employees in lieu of an annual stock option grant. The restricted stock unit awards granted in March 2006 contained both time-based units (25% of the grant) and performance-based units (75% of the grant). The time-based units vest in three equal annual installments beginning with the first anniversary of the grant, and the performance-based units vest in three equal annual installments, beginning with the first anniversary of the grant, based upon the achievement of pretax profit and revenue growth rate goals in 2006 (the first installment), 2006-2007 (the second installment), and 2006-2008 (the

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third installment). The restricted stock unit awards granted in March 2007 consist of only performance-based units which vest at the end of three years, based upon the achievement of pretax profit and revenue growth rate

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goals for the three-year period from 2007-2009. Each performance-based unit will vest into zero to 1.5 shares depending on the degree to which the performance goals are met. Compensation expense resulting from these awards is recognized as expense ratably for each installment from the date of grant until the date the restrictions lapse and is based on the fair market value at the date of grant and the probability of achievement of the specific performance-related goals. The company records share-based expense in selling, general and administrative expense.

During the six months ended June 30, 2007 and 2006, the company recorded \$5.5 million and \$3.2 million of share-based compensation expense, respectively, which is comprised of \$5.3 million and \$3.0 million of restricted stock unit expense and \$.2 million and \$.2 million of stock option expense, respectively.

A summary of stock option activity for the six months ended June 30, 2007 follows (shares in thousands):

| Options   | Shares          | Weighted-<br>Average<br>Exercise<br>Price | Weighted-<br>Average<br>Remaining<br>Contractual<br>Term (years) | Aggregate<br>Intrinsic<br>Value<br>(\$ in millions) |
|---|-----------------|---|--|---|
| -----   | -----           | -----                                     | -----  | -----   |
| Outstanding at<br>December<br>31, 2006                | 43,190          | \$16.44                                   |  |   |
| Granted   | -               | -   |  |   |
| Exercised   | (1,578)         | 7.13                                      |  |   |
| Forfeited and<br>expired                              | (1,978)         | 16.87                                     |  |   |
|   | -----           |   |  |   |
| Outstanding at<br>June 30, 2007                       | 39,634<br>===== | 16.79                                     | 3.76   | \$19.3  |
| Vested and<br>expected to<br>vest at<br>June 30, 2007 | 39,634<br>===== | 16.79                                     | 3.76   | 19.3  |
| Exercisable at<br>June 30, 2007                       | 39,164<br>===== | 16.92                                     | 3.76   | 17.9  |

The aggregate intrinsic value in the above table reflects the total pretax intrinsic value (the difference between the company's closing stock price on the last trading day of the period and the exercise price of the options, multiplied by the number of in-the-money stock options) that would have been received by the option holders had all option holders exercised their options on June 30, 2007. The intrinsic value of the company's stock options changes based on the closing price of the company's stock. The total intrinsic value of options exercised for the six months ended June 30, 2007 was \$2.8 million; the amount for the six months ended June 30, 2006 was immaterial. As of June 30, 2007, \$1.1 million of total unrecognized compensation cost related to stock options is expected to be recognized over a weighted-average period of 1.1 years.

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A summary of restricted stock unit activity for the six months ended June 30, 2007 follows (shares in thousands):

|                                     | Restricted<br>Stock<br>Units<br>----- | Weighted-<br>Average<br>Grant Date<br>Fair Value<br>----- |
|-------------------------------------|---------------------------------------|---|
| Outstanding at<br>December 31, 2006 | 1,963                                 | \$6.66  |
| Granted                             | 3,223                                 | 8.32  |
| Vested                              | (342)                                 | 6.95  |
| Forfeited and expired               | (305)                                 | 5.71  |
|                                     | ----                                  |   |
| Outstanding at<br>June 30, 2007     | 4,539<br>=====                        | 7.80  |

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The fair value of restricted stock units is determined based on the average of the high and low trading price of the company's common shares on the date of grant. The weighted-average grant-date fair value of restricted stock units granted during the six months ended June 30, 2007 and 2006 was \$8.32 and \$6.63, respectively. As of June 30, 2007, there was \$26.8 million of total unrecognized compensation cost related to outstanding restricted stock units granted under the company's plans. That cost is expected to be recognized over a weighted-average period of 2.3 years. The total fair value of restricted share units vested during the six months ended June 30, 2007 and 2006 was \$2.9 million and \$.8 million, respectively.

Common stock issued upon exercise of stock options or upon lapse of restrictions on restricted stock units is newly issued shares. Cash received from the exercise of stock options for the six months ended June 30, 2007 and 2006 was \$11.3 million and \$.9 million, respectively. The company is currently not recognizing any tax benefits from the exercise of stock options or upon issuance of stock upon lapse of restrictions on restricted stock units in light of its tax position. Tax benefits resulting from tax deductions in excess of the compensation costs recognized are classified as financing cash flows.

f. 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 profits 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 sales of hardware and software sold to the Services segment for internal use in Services engagements. The amount of such profit included in operating

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income of the Technology segment for the three and six months ended June 30, 2007 and 2006 was \$1.3 million and \$2.0 million, and \$1.8 million and \$3.3 million, respectively. The profit on these transactions is eliminated in Corporate.

The company evaluates business segment performance on operating income exclusive of restructuring 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 items mentioned above.

A summary of the company's operations by business segment for the three and six month periods ended June 30, 2007 and 2006 is presented below (in millions of dollars):

|  | Total<br>----- | Corporate<br>----- | Services<br>----- | Technology<br>----- |
|--|----------------|--------------------|-------------------|---------------------|
| Three Months Ended<br>June 30, 2007<br>----- |                |                    |                   |                     |
| Customer revenue                             | \$1,375.7      |                    | \$1,208.6         | \$ 167.1            |
| Intersegment                                 |                | \$ (47.4)          | 3.6               | 43.8                |
|  | -----          | -----              | -----             | -----               |
| Total revenue                                | \$1,375.7      | \$ (47.4)          | \$1,212.2         | \$ 210.9            |
|  | =====          | =====              | =====             | =====               |
| Operating income (loss)                      | \$ 2.5         | \$ (27.0)          | \$ 30.7           | \$ (1.2)            |
|  | =====          | =====              | =====             | =====               |

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|  |            |            |           |           |
|--|------------|------------|-----------|-----------|
| Three Months Ended<br>June 30, 2006<br>----- |            |            |           |           |
| Customer revenue                             | \$1,407.3  |            | \$1,224.5 | \$ 182.8  |
| Intersegment                                 |            | \$ (53.2)  | 3.8       | 49.4      |
|  | -----      | -----      | -----     | -----     |
| Total revenue                                | \$1,407.3  | \$ (53.2)  | \$1,228.3 | \$ 232.2  |
|  | =====      | =====      | =====     | =====     |
| Operating income (loss)                      | \$ (183.7) | \$ (143.9) | \$ (11.6) | \$ (28.2) |
|  | =====      | =====      | =====     | =====     |

|  |           |           |           |          |
|--|-----------|-----------|-----------|----------|
| Six Months Ended<br>June 30, 2007<br>----- |           |           |           |          |
| Customer revenue                           | \$2,723.7 |           | \$2,361.5 | \$ 362.2 |
| Intersegment                               |           | \$ (87.5) | 7.5       | 80.0     |
|  | -----     | -----     | -----     | -----    |
| Total revenue                              | \$2,723.7 | \$ (87.5) | \$2,369.0 | \$ 442.2 |
|  | =====     | =====     | =====     | =====    |
| Operating income (loss)                    | \$ (27.1) | \$ (53.1) | \$ 19.2   | \$ 6.8   |
|  | =====     | =====     | =====     | =====    |

|  |           |  |           |          |
|--|-----------|--|-----------|----------|
| Six Months Ended<br>June 30, 2006<br>----- |           |  |           |          |
| Customer revenue                           | \$2,795.1 |  | \$2,400.9 | \$ 394.2 |

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|                         |            |            |           |           |
|-------------------------|------------|------------|-----------|-----------|
| Intersegment            |            | \$ (95.8)  | 7.2       | 88.6      |
|                         | -----      | -----      | -----     | -----     |
| Total revenue           | \$2,795.1  | \$ (95.8)  | \$2,408.1 | \$ 482.8  |
|                         | =====      | =====      | =====     | =====     |
| Operating income (loss) | \$ (352.5) | \$ (288.7) | \$ (22.1) | \$ (41.7) |
|                         | =====      | =====      | =====     | =====     |

Presented below is a reconciliation of total business segment operating income (loss) to consolidated loss before income taxes (in millions of dollars):

|                                       | Three Months<br>Ended June 30 |            | Six Months<br>Ended June 30 |            |
|---------------------------------------|-------------------------------|------------|-----------------------------|------------|
|                                       | 2007                          | 2006       | 2007                        | 2006       |
|                                       | -----                         | -----      | -----                       | -----      |
| Total segment operating income (loss) | \$ 29.5                       | \$ (39.8)  | \$ 26.0                     | \$ (63.8)  |
| Interest expense                      | (18.7)                        | (19.1)     | (37.6)                      | (38.9)     |
| Other income (expense), net           | (8.7)                         | (.7)       | 16.8                        | 152.7      |
| Cost reduction charges                | (33.3)                        | (141.2)    | (66.0)                      | (287.1)    |
| Corporate and eliminations            | 6.3                           | (2.7)      | 12.9                        | (1.6)      |
|                                       | -----                         | -----      | -----                       | -----      |
| Total loss before income taxes        | \$ (24.9)                     | \$ (203.5) | \$ (47.9)                   | \$ (238.7) |
|                                       | =====                         | =====      | =====                       | =====      |

Customer revenue by classes of similar products or services, by segment, is presented below (in millions of dollars):

|                                    | Three Months<br>Ended June 30 |           | Six Months<br>Ended June 30 |           |
|------------------------------------|-------------------------------|-----------|-----------------------------|-----------|
|                                    | 2007                          | 2006      | 2007                        | 2006      |
|                                    | -----                         | -----     | -----                       | -----     |
| Services                           |                               |           |                             |           |
| Systems integration and consulting | \$ 370.8                      | \$ 404.0  | \$ 713.4                    | \$ 785.3  |
| Outsourcing                        | 504.7                         | 471.2     | 973.8                       | 926.4     |
| Infrastructure services            | 224.2                         | 229.5     | 458.8                       | 454.5     |
| Core maintenance                   | 108.9                         | 119.8     | 215.5                       | 234.7     |
|                                    | -----                         | -----     | -----                       | -----     |
|                                    | 1,208.6                       | 1,224.5   | 2,361.5                     | 2,400.9   |
| Technology                         |                               |           |                             |           |
| Enterprise-class servers           | 127.5                         | 145.6     | 277.9                       | 313.7     |
| Specialized technologies           | 39.6                          | 37.2      | 84.3                        | 80.5      |
|                                    | -----                         | -----     | -----                       | -----     |
|                                    | 167.1                         | 182.8     | 362.2                       | 394.2     |
|                                    | -----                         | -----     | -----                       | -----     |
| Total                              | \$1,375.7                     | \$1,407.3 | \$2,723.7                   | \$2,795.1 |
|                                    | =====                         | =====     | =====                       | =====     |

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g. Comprehensive income (loss) for the three and six months ended June 30, 2007 and 2006 includes the following components (in millions of dollars):

Three Months

Six Months

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|  | Ended June 30 |            | Ended June 30 |            |
|--|---------------|------------|---------------|------------|
|  | 2007          | 2006       | 2007          | 2006       |
|  | ----          | ----       | ----          | ----       |
| Net loss                                 | \$ (65.5)     | \$ (194.6) | \$ (61.9)     | \$ (222.5) |
| Other comprehensive income (loss)        |               |            |               |            |
| Cash flow hedges                         |               |            |               |            |
| Income (loss)                            | (.2)          | (.4)       | (.4)          | (.2)       |
| Reclassification adj.                    | .3            | .2         | .4            | -          |
| Foreign currency translation adjustments | 24.3          | (1.7)      | 29.4          | (12.2)     |
| Postretirement adjustments               | 23.2          | -          | 55.4          | 1,446.0    |
|  | -----         | -----      | -----         | -----      |
| Total other comprehensive income (loss)  | 47.6          | (1.9)      | 84.8          | 1,433.6    |
|  | -----         | -----      | -----         | -----      |
| Comprehensive income (loss)              | \$ (17.9)     | \$ (196.5) | \$ 22.9       | \$ 1,211.1 |
|  | =====         | =====      | =====         | =====      |

Accumulated other comprehensive income (loss) as of December 31, 2006 and June 30, 2007 is as follows (in millions of dollars):

|                              | Total        | Translation Adjustments | Cash Flow Hedges | Postretirement Plans |
|------------------------------|--------------|-------------------------|------------------|----------------------|
|                              | -----        | -----                   | -----            | -----                |
| Balance at December 31, 2006 | \$ (1,626.0) | \$ (633.1)              | \$ -             | \$ (992.9)           |
| Change during period         | 84.8         | 29.4                    | -                | 55.4                 |
|                              | -----        | -----                   | -----            | -----                |
| Balance at June 30, 2007     | \$ (1,541.2) | \$ (603.7)              | \$ -             | \$ (937.5)           |
|                              | =====        | =====                   | =====            | =====                |

h. For equipment manufactured by the company, the company warrants that it will substantially conform to relevant published specifications for 12 months after shipment to the customer. The company will repair or replace, at its option and expense, items of equipment that do not meet this warranty. For company software, the company warrants that it will conform substantially to then-current published functional specifications for 90 days from customer's receipt. The company will provide a workaround or correction for material errors in its software that prevents its use in a production environment.

The company estimates the costs that may be incurred under its warranties and records a liability in the amount of such costs at the time revenue is recognized. Factors that affect the company's warranty liability include the number of units sold, historical and anticipated rates of warranty claims and cost per claim. The company quarterly assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary. Presented below is a reconciliation of the aggregate product warranty liability (in millions of dollars):

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| Three Months  |      | Six Months    |      |
|---------------|------|---------------|------|
| Ended June 30 |      | Ended June 30 |      |
| -----         |      | -----         |      |
| 2007          | 2006 | 2007          | 2006 |
| ----          | ---- | ----          | ---- |

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|   |        |        |        |        |
|---|--------|--------|--------|--------|
| Balance at beginning of period  | \$ 8.5 | \$ 9.3 | \$ 8.2 | \$ 8.0 |
| Accruals for warranties issued during the period  | 1.1    | 2.1    | 2.5    | 5.0    |
| Settlements made during the period  | (1.4)  | (2.4)  | (3.8)  | (4.8)  |
| Changes in liability for pre-existing warranties during the period, including expirations | .4     | (.1)   | 1.7    | .7     |
| Balance at June 30  | \$ 8.6 | \$ 8.9 | \$ 8.6 | \$ 8.9 |
|   | =====  | =====  | =====  | =====  |

i. Net cash refunds received during the six months ended June 30, 2007 for income taxes was \$30.1 million compared with net cash paid for income taxes during the six months ended June 30, 2006 of \$47.4 million.

Cash paid during the six months ended June 30, 2007 and 2006 for interest was \$41.8 million and \$49.0 million, respectively.

During the six months ended June 30, 2007, the company financed \$22.7 million of internal use software licenses.

j. 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. Adoption of FIN 48 did not have a material impact on the company's consolidated results of operations and financial position. See note (1).

Effective January 1, 2007, the company adopted EITF 06-2, "Accounting for Sabbatical Leave and Other Similar Benefits Pursuant to FASB Statement No. 43." EITF 06-2 applies to compensated absences that require a minimum service period but have no increase in the benefit even with additional years of service and requires the benefit to be recognized as a liability over the service period. Adoption of EITF 06-2 did not have a material impact on the company's consolidated results of operations and financial position.

Effective January 1, 2007, the company adopted EITF 06-5, "Accounting for Purchases of Life Insurance - Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4." EITF 06-5 requires that a policyholder should consider any additional amounts included in the contractual terms of the policy in determining the amount that could be realized under the insurance contract on a policy-by-policy basis. Adoption of EITF 06-5 did not have a material impact on the company's consolidated results of operations and financial position.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This statement applies under other accounting pronouncements that require or permit fair value measurements. Accordingly, SFAS No. 157 does not require any new fair value measurements. The

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provisions of SFAS No. 157 are to be applied prospectively and are effective for financial statements issued for fiscal years beginning after November 15, 2007. The company is currently evaluating what effect, if any, adoption of SFAS No. 157 will have on the company's consolidated results of operations and financial position.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (SFAS No. 159). SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reportable in earnings. The provisions of SFAS No. 159 shall be effective as of the beginning of each reporting entity's first fiscal year that begins after November 15, 2007. SFAS No. 159 should not be applied retrospectively to fiscal years beginning prior to the effective date. The company is currently evaluating whether it will adopt the provisions of SFAS No. 159, and if adopted, what effect adoption of SFAS No. 159 will have on the company's consolidated results of operations and financial position.

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EITF 06-4, "Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements," was issued in September 2006 and is effective for fiscal years beginning after December 15, 2007. EITF 06-4 requires that, for split-dollar life insurance arrangements that provide a benefit to an employee that extends to postretirement periods, an employer should recognize a liability for future benefits in accordance with SFAS No. 106. EITF 06-4 requires that recognition of the effects of adoption should be either by (a) a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption or (b) a change in accounting principle through retrospective application to all prior periods. The company is reviewing EITF 06-4 and does not currently expect that its adoption will have a material impact on the company's consolidated results of operations and financial position.

k. In 2002, the company and the Transportation Security Administration (TSA) entered into a competitively awarded contract providing for the establishment of secure information technology environments in airports. The Defense Contract Audit Agency (DCAA), at the request of TSA, reviewed contract performance and raised some government contracting issues. The company continues to work to address certain contracts administration issues raised by the DCAA. In addition, the company has learned that the Civil Division of the Department of Justice, working with the Inspector General's Office of the Department of Homeland Security, is reviewing issues raised by the DCAA relating to labor categorization and overtime on the TSA contract. The company understands that the Civil Division is at an early stage in its review. The company is working cooperatively with the Civil Division. The company does not know whether the Civil Division will pursue the matter, or, if pursued, what effect this might have on the company.

l. 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. Adoption of FIN 48 did not have a material impact on the company's consolidated results of operations and financial position.

The company and its subsidiaries file income tax returns in the U.S. federal

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jurisdiction, and various states and foreign jurisdictions. The company recently concluded a U.S. federal income tax audit of the years 2000-2003 with no material impact. Several U.S. state and foreign income tax audits are in process. There are currently no income tax audits in process in either Brazil or the United Kingdom, which are the most significant jurisdictions outside the U.S. For Brazil, the audit period through 2000 is closed and for the United Kingdom, the audit period through 2004 is closed. All of the various ongoing income tax audits throughout the world are not expected to have a material impact on the company's financial position.

The company recognizes penalties and interest accrued related to income tax liabilities in the provision (benefit) for income taxes in its consolidated statements of income. The company had an accrual of \$11.4 million for the payment of penalties and interest at June 30, 2007 and \$10.3 million at December 31, 2006. The increase in the liability of \$1.1 million was recognized as part of the company's income tax provision during the six months ended June 30, 2007.

As of December 31, 2006, the company had \$38.3 million of a liability for unrecognized tax benefits. In March 2007, the company settled an income tax audit in the Netherlands and as a result, recorded a tax benefit of \$39.4 million and received a refund, including interest, of approximately \$58 million during the second quarter of 2007.

After the settlement discussed above, the company had \$13.4 million of a liability for unrecognized tax benefits as of June 30, 2007, all of which, if recognized, would affect the company's effective tax rate. The company does not currently expect that the total amount of unrecognized tax benefits at June 30, 2007 will significantly increase or decrease within the next 12 months.

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

#### Overview

For the six months ended June 30, 2007, the company reported a net loss of \$61.9 million, or \$.18 per share, compared with a net loss of \$222.5 million, or \$.65 per share, for the six months ended June 30, 2006. The current six-month period includes pretax charges relating to cost reduction actions of \$66.0 million compared with \$287.1 million in the prior six-month period.

During the first half of 2007, the company:

- \* recorded cost reduction charges of \$66.0 million for 1,517 personnel reductions and idle facility costs (see note (b));

- \* continued its program to divest non-core assets by selling its media business for cash proceeds of approximately \$28 million (see note (d));
- and

- \* settled a Netherlands income tax audit and, as a result, recorded a tax benefit of approximately \$39 million and received a cash refund, including interest, of approximately \$58 million (see note (l)).

#### Results of operations

##### Company results

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For the three months ended June 30, 2007, the company reported a net loss of \$65.5 million, or \$.19 per share, compared with a net loss of \$194.6 million, or \$.57 per share, for the three months ended June 30, 2006. The current period includes pretax charges relating to cost reduction actions of \$33.3 million compared with \$141.2 million in the prior-year period.

Revenue for the quarter ended June 30, 2007 was \$1.38 billion compared with \$1.41 billion for the second quarter of 2006, a decrease of 2% from the prior year. This decrease was principally due to a decrease of 9% in Technology revenue and a decrease of 1% in Services revenue. Foreign currency had a 3-percentage-point positive impact on revenue in the current period compared with the year-ago period. U.S. revenue declined 7% in the quarter compared with the year-ago period, principally driven by continued weakness in systems integration and consulting. Revenue in international markets increased 2% due to increases in Europe, Latin America (excluding Brazil), South Pacific and Asia, offset in part by decreases in Japan and Brazil. On a constant currency basis, international revenue declined 4% in the three months ended June 30, 2007 compared with the three months ended June 30, 2006.

As part of the company's continuing repositioning plan to right size its cost structure, during the three months ended June 30, 2007, the company consolidated facility space and committed to an additional reduction of 551 employees. This resulted in a pretax charge in the quarter of \$33.3 million. The \$19.8 million charge related to work force reductions is broken down as follows: (a) 425 employees in the U.S. for a charge of \$12.0 million and (b) 126 employees outside the U.S. for a charge of \$7.8 million. The facility charge of \$13.5 million principally relates to leased property that the company ceased using as of June 30, 2007. The facility charge represents the fair value of the liability at the cease-use date and was determined based on the remaining lease rental payments, reduced by estimated sublease rentals that could be reasonably obtained for the property. The pretax charge was recorded in the following statement of income classifications: cost of revenue-services, \$6.8 million; cost of revenue-technology, \$.5 million; selling, general and administrative expenses, \$16.5 million; research and development expenses, \$9.7 million; and other income (expense), net, \$.2 million. The income recorded in other income (expense), net relates to minority shareholders' portion of the charge related to majority owned subsidiaries which are fully consolidated by the company.

The cost reduction actions taken in the first half of 2007, when combined with the 2006 actions, bring the total pretax charge to \$396.1 million, comprised of \$382.6 million for 7,182 work force reductions and \$13.5 million for idle lease cost. The combined employee reduction actions are expected to be substantially completed by the end of 2007. Net of investments in offshore resources and outsourcing of certain internal, non-client facing functions, the company anticipates that these combined actions will yield, on a run-rate basis, annualized cost savings in excess of \$340 million by the second half of 2007 and in excess of \$365 million by the first half of 2008. During the current quarter, the company took the first steps to consolidate lease space around the world to reflect its recent headcount reductions and its continued move to an increasingly mobile services delivery work force. The company is currently looking at other potential opportunities and may take additional actions later in the year to further consolidate facility space.

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During the three months ended June 30, 2006, the company committed to a reduction of approximately 1,900 employees. This resulted in a pretax charge in the second quarter of 2006 of \$141.2 million, principally related to severance costs. The charge is broken down as follows: (a) approximately 650 employees in the U.S. for a charge of \$22.1 million and (b) approximately 1,250 employees outside the U.S. for a charge of \$119.1 million. The pretax charge was recorded

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in the following statement of income classifications: cost of revenue-services, \$101.4 million; selling, general and administrative expenses, \$28.3 million; research and development expenses, \$11.8 million; and other income (expense), net, \$.3 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 and 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. In addition, 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 plan participants. 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 the first quarter of 2006.

Pension expense for the three months ended June 30, 2007 was \$11.4 million compared with \$40.5 million for the three months ended June 30, 2006. The decrease was principally due to the change in the U.S. defined benefit pension plans. 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 sales; 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.

Total gross profit margin was 21.8% in the three months ended June 30, 2007 compared with 11.6% in the three months ended June 30, 2006. Included in the gross profit margin in 2007 and 2006 were cost reduction charges of \$7.3 million and \$101.4 million, respectively. The increase in gross profit margin excluding these charges principally reflects the benefits derived from the cost reduction actions as well as a decline in pension expense of \$20.8 million (\$8.4 million for the three months ended June 30, 2007 compared with \$29.2 million in the year-ago period).

Selling, general and administrative expenses were \$247.4 million for the three months ended June 30, 2007 (18.0% of revenue) compared with \$282.7 million (20.1% of revenue) in the year-ago period. Included in selling, general and administrative expense in 2007 and 2006 were cost reduction charges of \$16.5 million and \$28.3 million, respectively. The decrease in selling, general and administrative expense excluding these charges principally reflects the benefits derived from the cost reduction actions as well as a decline in pension expense of \$5.3 million (\$3.2 million for the three months ended June 30, 2007 compared with \$8.5 million in the year-ago period).

Research and development (R&D) expenses in the second quarter of 2007 were \$49.5 million compared with \$63.9 million in the second quarter of 2006. The company continues to invest in proprietary operating systems and in key programs within its industry practices. Included in R&D expense in 2007 and 2006 were cost reduction charges of \$9.7 million and \$11.8 million, respectively. The reduction in R&D in 2007 compared with 2006, excluding these charges, principally reflects the benefits derived from the cost reduction actions as well as a decline in pension expense of \$3.0 million (\$.2 million income for the three months ended June 30, 2007 compared with expense of \$2.8 million in the year-ago period).

For the second quarter of 2007, the company reported a pretax operating profit of \$2.5 million compared with a pretax operating loss of \$183.7 million in the second quarter of 2006. The principal items affecting the comparison of 2007

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with 2006 were a \$33.5 million and a \$141.5 million charge in 2007 and 2006, respectively, relating to the cost reduction actions, as well as the benefits derived from the cost reduction actions. Contributing to the increase in operating profit was a decline in pension expense of \$29.1 million (\$11.4 million for the three months ended June 30, 2007 compared with \$40.5 million in the year-ago period).

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Interest expense for the three months ended June 30, 2007 was \$18.7 million compared with \$19.1 million for the three months ended June 30, 2006.

Other income (expense), net, which can vary from period to period, was expense of \$8.7 million in the second quarter of 2007, compared with expense of \$.7 million in 2006. The difference in 2007 from 2006 was principally due to expense of \$6.1 million in the current quarter compared with expense of \$2.2 million in last year's second quarter related to minority shareholders' portion of income of iPSL, a 51% owned subsidiary which is fully consolidated by the company. The change was due to increased profit from iPSL resulting from the renegotiated contract in January 2006 and benefits derived from cost reduction actions. Additionally, lower interest income in the current quarter (\$6.5 million compared with \$8.7 million in the prior-year quarter) due to reduced cash levels contributed to the increase in expense.

Income (loss) before income taxes for the three months ended June 30, 2007 was a loss of \$24.9 million compared with a loss of \$203.5 million in 2006. The provision for income taxes was \$40.6 million in the current quarter compared with a benefit of \$8.9 million in the year-ago period. Due to the establishment of a full valuation allowance for all of the company's U.S. deferred tax assets and certain international subsidiaries in the third quarter of 2005, the company no longer has a meaningful effective tax rate. 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 quarter to quarter depending on the geographic distribution of income. In the current quarter, income increased in certain international jurisdictions where the company still provides for income taxes due in large part to profit improvement caused by the company's cost reduction actions.

For the six months ended June 30, 2007, the company reported a net loss of \$61.9 million, or \$.18 per share, compared with a net loss of \$222.5 million, or \$.65 per share, for the six months ended June 30, 2006. The current six-month period includes pretax charges relating to cost reduction actions of \$66.0 million compared with \$287.1 million in the prior six-month period.

Total revenue for the six months ended June 30, 2007 and 2006 was \$2.72 billion and \$2.80 billion, respectively. Foreign currency translations had a 3-percentage-point positive impact on revenue in the current six months when compared with the year-ago period. In the current six-month period, Services revenue decreased 2% and Technology revenue decreased 8%.

U.S. revenue declined 5% in the current six-month period compared with the year-ago period and revenue in international markets decreased 1%. On a constant currency basis, international revenue decreased 7% in the six months ended June 30, 2007.

Pension expense for the six months ended June 30, 2007 was \$22.0 million compared with \$48.4 million of pension expense for the six months ended June 30, 2006. The decrease in pension expense in 2007 from 2006 was principally due to the change in the U.S. defined benefit pension plans, discussed above.

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Total gross profit margin was 20.4% in the six months ended June 30, 2007 compared with 13.1% in the year-ago period. Included in the gross profit margin in 2007 and 2006 were cost reduction charges of \$32.3 million and \$186.8 million, respectively. The increase in gross profit margin excluding these charges principally reflects the benefits derived from the cost reduction actions as well as a decline in pension expense of \$20.6 million (\$16.3 million for the six months ended June 30, 2007 compared with \$36.9 million in the year-ago period).

For the six months ended June 30, 2007, selling, general and administrative expenses were \$492.0 million (18.1% of revenue) compared with \$578.1 million (20.7% of revenue) for the six months ended June 30, 2006. Included in selling, general and administrative expense in 2007 and 2006 were cost reduction charges of \$18.6 million and \$73.7 million, respectively. The decrease in selling, general and administrative expense excluding these charges principally reflects the benefits derived from the cost reduction actions as well as a decline in pension expense of \$4.1 million (\$6.2 million for the six months ended June 30, 2007 compared with \$10.3 million in the year-ago period).

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R&D expense for the six months ended June 30, 2007 was \$91.9 million compared with \$139.2 million a year ago. Included in R&D expense in 2007 and 2006 were cost reduction charges of \$15.9 million and \$29.4 million, respectively. The reduction in R&D in 2007 compared with 2006 excluding these charges principally reflects the benefits derived from the cost reduction actions as well as a decline in pension expense of \$1.7 million (\$.5 million income for the six months ended June 30, 2007 compared with \$1.2 million of expense in the year-ago period).

For the six months ended June 30, 2007, the company reported an operating loss of \$27.1 million compared with an operating loss of \$352.5 million for the six months ended June 30, 2006. The principal items affecting the comparison of 2007 with 2006 were a \$66.8 million and a \$289.9 million charge in 2007 and 2006, respectively, relating to the cost reduction actions, as well as the benefits derived from the cost reduction actions. Contributing to the increase in operating profit was a decline in pension expense of \$26.4 million (\$22.0 million for the six months ended June 30, 2007 compared with \$48.4 million in the year-ago period).

Interest expense for the six months ended June 30, 2007 was \$37.6 million compared with \$38.9 million for the six months ended June 30, 2006.

Other income (expense), net was income of \$16.8 million in the current six-month period compared with income of \$152.7 million in the year-ago period. Other income (expense) in 2007 principally reflects a gain of \$23.1 million on the sale of the company's media business and 2006 principally reflects a gain of \$149.9 million from the sale of all of the company's shares in NUL (see note (d)).

Income (loss) before income taxes was a loss of \$47.9 million in the six months ended June 30, 2007 compared with a loss of \$238.7 million last year. The provision for income taxes was \$14.0 million in the current period compared with a benefit of \$16.2 million in the year-ago period. The tax provision in the current six-month period includes a \$39.4 million benefit related to the Netherlands income tax audit settlement (see note (1)).

In 2002, the company and the Transportation Security Administration (TSA) entered into a competitively awarded contract providing for the establishment of secure information technology environments in airports. The Defense Contract Audit Agency (DCAA), at the request of TSA, reviewed contract performance and

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raised some government contracting issues. The company continues to work to address certain contracts administration issues raised by the DCAA. In addition, the company has learned that the Civil Division of the Department of Justice, working with the Inspector General's Office of the Department of Homeland Security, is reviewing issues raised by the DCAA relating to labor categorization and overtime on the TSA contract. The company understands that the Civil Division is at an early stage in its review. The company is working cooperatively with the Civil Division. The company does not know whether the Civil Division will pursue the matter, or, if pursued, what effect this might have on the company.

### 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 sales of 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 three and six months ended June 30, 2007 and 2006 was \$1.3 million and \$2.0 million, and \$1.8 million and \$3.3 million, respectively. The profit on these transactions is eliminated in Corporate.

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The company evaluates business segment performance on operating income exclusive of restructuring 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 items mentioned above.

Information by business segment is presented below (in millions of dollars):

|  | Total<br>----- | Elimi-<br>nations<br>----- | Services<br>----- | Technology<br>----- |
|--|----------------|----------------------------|-------------------|---------------------|
| Three Months Ended<br>June 30, 2007<br>----- |                |                            |                   |                     |
| Customer revenue                             | \$1,375.7      |                            | \$1,208.6         | \$167.1             |
| Intersegment                                 |                | \$(47.4)                   | 3.6               | 43.8                |
|  | -----          | -----                      | -----             | -----               |
| Total revenue                                | \$1,375.7      | \$(47.4)                   | \$1,212.2         | \$210.9             |
|  | =====          | =====                      | =====             | =====               |
| Gross profit percent                         | 21.8 %         |                            | 17.3 %            | 43.3 %              |
|  | =====          |                            | =====             | =====               |

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|                        |           |           |           |         |
|------------------------|-----------|-----------|-----------|---------|
| Operating profit       | .2 %      |           | 2.5 %     | (.6)%   |
| (loss) percent         | =====     |           | =====     | =====   |
| Three Months Ended     |           |           |           |         |
| June 30, 2006          |           |           |           |         |
| -----                  |           |           |           |         |
| Customer revenue       | \$1,407.3 |           | \$1,224.5 | \$182.8 |
| Intersegment           |           | \$ (53.2) | 3.8       | 49.4    |
|                        | -----     | -----     | -----     | -----   |
| Total revenue          | \$1,407.3 | \$ (53.2) | \$1,228.3 | \$232.2 |
|                        | =====     | =====     | =====     | =====   |
| Gross profit percent   | 11.6 %    |           | 14.3 %    | 37.6 %  |
|                        | =====     |           | =====     | =====   |
| Operating loss percent | (13.1)%   |           | ( .9)%    | (12.2)% |
|                        | =====     |           | =====     | =====   |

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

In the Services segment, customer revenue was \$1.21 billion for the three months ended June 30, 2007 compared with \$1.22 billion for the three months ended June 30, 2006. Foreign currency translation had a 4-percentage-point positive impact on Services revenue in the current quarter compared with the year-ago period. Revenue in the second quarter of 2007 declined 1% compared with 2006, principally due to an 8% decrease in systems integration and consulting revenue (\$370.8 million in 2007 compared with \$404.0 million in 2006), a 9% decrease in core maintenance revenue (\$108.9 million in 2007 compared with \$119.8 million in 2006), and a 2% decrease in infrastructure services (\$224.2 million in 2007 compared with \$229.5 million in 2006), offset in part by a 7% increase in outsourcing (\$504.7 million in 2007 compared with \$471.2 million in 2006). Services gross profit was 17.3% in the second quarter of 2007 compared with 14.3% in the year-ago period. Services operating income (loss) percent was 2.5% in the three months ended June 30, 2007 compared with (.9)% in the three months ended June 30, 2006. The increase in Services operating profit margin principally reflects the benefits derived from the cost reduction actions as well as a decline in pension expense of \$24.1 million (\$11.3 million for the three months ended June 30, 2007 compared with \$35.4 million in the year-ago period). During the quarter, the company continued to experience lower volume in systems integration and consulting, and higher temporary contract labor costs primarily due to changes and disruptions associated with the repositioning program. The company is currently addressing these issues.

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In the Technology segment, customer revenue was \$167 million in the current quarter compared with \$183 million in the year-ago period. Foreign currency translation had a positive impact of approximately 1-percentage point on Technology revenue in the current period compared with the prior-year period. Revenue in the three months ended June 30, 2007 was down 9% from the three months ended June 30, 2006, due to a 12% decrease in sales of enterprise-class servers (\$127.5 million in 2007 compared with \$145.6 million in 2006) offset in part by a 6% increase in sales of specialized technology products (\$39.6 million in 2007 compared with \$37.2 million in 2006). Technology gross profit was 43.3% in the current quarter compared with 37.6% in the year-ago quarter. Technology operating income (loss) percent was (.6)% in the three months ended June 30, 2007 compared with (12.2)% in the three months ended June 30, 2006. The increase in Technology operating profit margin principally reflects the benefits derived from the cost reduction actions as well as a decline in pension expense of \$4.9 million (\$.1 million for the three months ended June 30, 2007 compared with \$5.0 million in the year-ago period). The decline in revenue in 2007 compared with 2006 primarily reflected the continuing secular decline in

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enterprise servers.

### New accounting pronouncements

See note (j) 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

Cash and cash equivalents at June 30, 2007 were \$520.7 million compared with \$719.3 million at December 31, 2006.

During the six months ended June 30, 2007, cash used for operations was \$81.1 million compared with cash used of \$166.0 million for the six months ended June 30, 2006. The current-year period included a tax refund of approximately \$58 million. Cash expenditures in the current period related to the current year and prior-year restructuring actions (which are included in operating activities) were approximately \$86.7 million compared with \$39.6 million for the prior-year period. Cash expenditures for the current-year and the prior-year restructuring actions are expected to be approximately \$75.1 million for the remainder of 2007, resulting in an expected cash expenditure of approximately \$161.8 million in 2007 compared with \$198 million in 2006. In addition, there was a reduction in the amount of receivables sold in the company's U.S. securitization. At June 30, 2007 and December 31, 2006, receivables of \$125 million and \$170 million, respectively, were sold under the company's U.S. securitization.

Cash used for investing activities for the six months ended June 30, 2007 was \$139.7 million compared with \$240.5 million of cash provided during the six months ended June 30, 2006. The principal reason for the decrease was that in 2006, the company received net proceeds of \$380.6 million from the sale of the NUL shares and other assets. In the current period, the investment in marketable software was \$48.9 million compared with \$55.3 million in the year-ago period, capital additions of properties were \$39.8 million in 2007 compared with \$32.7 million in 2006 and capital additions of outsourcing assets were \$78.5 million in 2007 compared with \$50.1 million in 2006. The increase in capital expenditures for outsourcing assets reflects higher expenditures on outsourcing projects as the company began new client projects. During the six months ended June 30, 2007, the company financed \$22.7 million of internal use software licenses.

Cash provided by financing activities during the six months ended June 30, 2007 was \$10.7 million compared with \$69.0 million of cash used during the six months ended June 30, 2006. The prior-year period includes a cash expenditure of \$57.9 million to retire at maturity all of the company's remaining 8 1/8% senior notes. The current-year period includes \$11.3 million of cash received due to employee exercise of stock options during the six months ended June 30, 2007 compared with \$.9 million in the prior-year period.

At June 30, 2007, total debt was \$1.05 billion, unchanged from December 31, 2006.

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The company has a three-year, secured revolving credit facility which expires in 2009 that provides for loans and letters of credit up to an aggregate of \$275 million. 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

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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 non-payment, 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. Also, the credit facility may be terminated if the 7 7/8% senior notes due 2008 have not been repaid, refinanced or defeased by payment of amounts due to an escrow agent on or prior to January 1, 2008. The credit facility is secured by the company's assets, except that the collateral does not include accounts receivable that are subject to the receivable facility, U.S. real estate or the stock or indebtedness of the company's U.S. operating subsidiaries. As of June 30, 2007, there were letters of credit of \$45.5 million issued under the facility and there were no cash borrowings.

In addition, the company and certain international subsidiaries have access to uncommitted lines of credit from various banks. Other sources of short-term funding are operational cash flows, including customer prepayments, and the company's U.S. trade accounts receivable facility.

At June 30, 2007, the company had an agreement to sell, on an on-going basis, through Unisys Funding Corporation I, a wholly owned subsidiary, interests in up to \$300 million of eligible U.S. trade accounts receivable. The receivables are sold at a discount that reflects a margin based on, among other things, the company's then-current S&P and Moody's credit rating. The facility is terminable by the purchasers if the company's corporate rating is below B by S&P or B2 by Moody's and requires the maintenance of certain ratios related to the sold receivables. At June 30, 2007, the company's corporate rating was B+ and B2 by S&P and Moody's, respectively. The facility is renewable annually in November at the purchasers' option until November 2008. At June 30, 2007 and December 31, 2006, the company had sold \$125 million and \$170 million, respectively, of eligible receivables.

At June 30, 2007, 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. The company believes that it will have adequate sources and availability of short-term funding to meet its expected cash requirements.

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 a registration statement covering \$650 million of debt or equity securities, which enables the company to be prepared for future market opportunities.

Stockholders' equity increased \$62.0 million during the six months ended June 30, 2007, principally reflecting a decrease in other comprehensive loss due to amortization of postretirement losses recognized in accumulated other comprehensive income, offset in part by a net loss of \$61.9 million.

### Factors that may affect future results

From time to time, the company provides information containing "forward-looking"

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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.

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Statements in this report regarding the company's cost reduction plan are subject to the risk that the company may not implement the planned headcount reductions, increase its offshore resources, or reduce its use of third-party contract labor as quickly as currently planned. All of these factors could affect the timing of anticipated cost savings. The amount of anticipated cost savings is also subject to currency exchange rate fluctuations with regard to actions taken outside the U.S.

Other factors that could affect future results include the following:

The company's business is affected by changes in general economic and business conditions. The company continues to face a highly competitive business environment. If the level of demand for the company's products and services declines in the future, the company's business could be adversely affected. 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 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 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 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 in part on the success of its efforts

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to control and reduce costs through the development and use of low-cost subsidiaries and low-cost offshore and global sourcing models. Future results will also depend in part on the success of the company's focused investment and sales and marketing strategies. These strategies are 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.

The company's future results will depend in part on its ability to grow outsourcing and infrastructure services. 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.

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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 on the company's ability to continue to effectively address its challenging outsourcing operations through negotiations or operationally and to fully recover the associated outsourcing assets.

Future results will also depend in part on the company's ability to drive profitable growth in systems integration and consulting. The company's ability to grow profitably in this business will depend on the level of demand for systems integration projects. It will also depend on an improvement in the utilization of services delivery personnel. 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 head count.

Future results will also depend, in part, on market demand for the company's high-end enterprise servers and customer acceptance of the new models introduced in 2006. The company continues to apply its resources to develop value-added

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software capabilities and optimized solutions for these server platforms which provide competitive differentiation. Future results will depend, in part, on customer acceptance of new 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. In addition, future results will depend, in part, on the company's ability to generate new customers and increase sales of the Intel-based ES7000 line. The company believes there is growth potential in the market for high-end, Intel-based servers running Microsoft and Linux operating system software. However, the company's ability to succeed will depend on its ability to compete effectively against enterprise server competitors with more substantial resources and its ability to achieve market acceptance of the ES7000 technology by clients, systems integrators and independent software vendors. Future results of the technology business will also depend, in part, on the successful implementation of the company's arrangements with NEC.

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, its systems and policies, including the contractor's purchasing, property, estimating, accounting, compensation and management information systems. Any costs found to be overcharged or improperly allocated to a specific contract 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. Other risks and uncertainties associated with government contracts include the availability of appropriated funds and contractual provisions that allow governmental entities to terminate agreements at their discretion before the end of their terms. 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.

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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.

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 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,

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if a client is not satisfied with the company's services or products, its reputation could be damaged and its business adversely affected. In addition, 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.

The company has commercial relationships with suppliers, channel partners and other parties that have complementary products, services or skills. The company has announced that alliance partnerships with select IT companies are a key factor in the development and delivery of the company's refocused portfolio. 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.

More than half of the company's total revenue derives 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, and weaker intellectual property protections in some jurisdictions.

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.

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### Item 4. Controls and Procedures

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The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of June 30, 2007. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective for gathering, analyzing and disclosing the information the Company is required to disclose in the reports it files under the Securities Exchange Act of 1934, within the time periods specified in the SEC's rules and forms. Such evaluation did not identify any change in the Company's internal controls over financial reporting that occurred during the quarter ended June 30, 2007 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## Part II - OTHER INFORMATION

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### Item 1A. Risk Factors

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See "Factors that may affect future results" in Management's Discussion and Analysis of Financial Condition and Results of Operations for a discussion of risk factors.

### Item 4. Submission of Matters to a Vote of Security Holders

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- (a) The company's 2007 Annual Meeting of Stockholders (the "Annual Meeting") was held on April 26, 2007 in Philadelphia, Pennsylvania.
- (b) The following matters were voted upon at the Annual Meeting and received the following votes:
- (1) Election of Directors as follows:
- Henry C. Duques - 309,811,117 votes for; 12,414,882 votes withheld
- Clayton M. Jones - 309,618,973 votes for; 12,607,026 votes withheld
- Theodore E. Martin - 308,556,030 votes for; 13,659,969 votes withheld
- (2) Ratification of the selection of the company's independent registered public accounting firm for 2007 - 316,358,692 votes for; 3,488,294 votes against; 2,379,015 abstentions.
- (3) Approval of the Unisys Corporation 2007 Long-Term Incentive and Equity Compensation Plan - 211,375,645 votes for; 58,785,518 votes against; 2,885,245 abstentions; 49,179,593 broker non-votes.
- (4) Consideration and vote upon a stockholder proposal to provide a report concerning political contributions by the company - 110,229,306 votes for; 105,613,155 votes against; 57,203,947 abstentions; 49,179,593 broker non-votes.
- (5) Consideration and vote upon a stockholder proposal requesting the Board of Directors to issue a sustainability report relating to the company's social and environmental practices - 17,267,505 votes for; 200,272,719 votes against; 55,506,184 abstentions; 49,179,593 broker non-votes.

Item 5. Other Information

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See note (b) of the notes to consolidated financial statements for information on the restructuring charge taken in the second quarter of 2007.

Item 6. Exhibits

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- (a) Exhibits
- See Exhibit Index

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SIGNATURES

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Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

UNISYS CORPORATION

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Date: August 6, 2007

By: /s/ Janet Brutschea Haugen

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Janet Brutschea Haugen  
Senior Vice President and  
Chief Financial Officer  
(Principal Financial Officer)

By: /s/ Joseph M. Munnelly

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Joseph M. Munnelly  
Vice President and  
Corporate Controller  
(Chief Accounting Officer)

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## EXHIBIT INDEX

| Exhibit<br>Number<br>----- | Description<br>-----   |
|----------------------------|--|
| 3.1                        | Restated Certificate of Incorporation of Unisys Corporation<br>(incorporated by reference to Exhibit 3.1 to the registrant's Quarterly<br>Report on Form 10-Q for the quarterly period ended September 30, 1999)                   |
| 3.2                        | Bylaws of Unisys Corporation, as amended through February 8, 2007<br>(incorporated by reference to Exhibit 3 to the registrant's Current<br>Report on Form 8-K dated February 8, 2007)   |
| 10                         | Unisys Corporation 2007 Long-Term Incentive and Equity Compensation<br>Plan (incorporated by reference to Appendix A to the registrant's Proxy<br>Statement, dated March 15, 2007, for its 2007 annual meeting of<br>stockholders) |
| 12                         | Statement of Computation of Ratio of Earnings to Fixed Charges   |
| 31.1                       | Certification of Joseph W. McGrath required by Rule 13a-14(a)<br>or Rule 15d-14(a)   |
| 31.2                       | Certification of Janet Brutschea Haugen required by Rule 13a-14(a)<br>or Rule 15d-14(a)  |
| 32.1                       | Certification of Joseph W. McGrath required by Rule 13a-14(b)<br>or Rule 15d-14(b) and Section 906 of the Sarbanes-Oxley Act of 2002,<br>18 U.S.C. Section 1350  |
| 32.2                       | Certification of Janet Brutschea Haugen required by Rule 13a-14(b)<br>or Rule 15d-14(b) and Section 906 of the Sarbanes-Oxley Act of 2002,<br>18 U.S.C. Section 1350   |