PEROT SYSTEMS CORP
Form 10-Q
May 02, 2006

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

þ **Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended March 31, 2006

or

o **Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from to

Commission File Number 0-22495
PEROT SYSTEMS CORPORATION
(Exact name of registrant as specified in its charter)

DELAWARE	75-2230700
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

2300 WEST PLANO PARKWAY
PLANO, TEXAS
75075
(Address of principal executive offices)
(Zip Code)
(972) 577-0000
(Registrant s telephone number, including area code)

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. þYes o 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.

þ Large accelerated filer o Accelerated filer o 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 o No þ

Number of shares of registrant s common stock outstanding as of April 28, 2006: 118,707,881 shares of Class A Common Stock and 816,638 shares of Class B Common Stock.

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
FORM 10-Q
For the Quarter Ended March 31, 2006

INDEX

Table of Contents

ITEM 1: FINANCIAL STATEMENTS (UNAUDITED)

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF MARCH 31, 2006 AND DECEMBER 31, 2005
(DOLLARS IN THOUSANDS)
(UNAUDITED)

	March 31, 2006	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 238,139	$ 259,598
Accounts receivable, net	307,404	277,780
Prepaid expenses and other	67,838	65,974
Total current assets	613,381	603,352
Property, equipment and purchased software, net	187,386	180,036
Goodwill	452,055	443,439
Deferred contract costs, net	91,254	85,313
Other non-current assets	65,615	58,480
Total assets	$ 1,409,691	$ 1,370,620
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 51,724	$ 38,680
Deferred revenue	36,563	28,035
Accrued compensation	35,655	60,024
Income taxes payable	41,411	51,064
Accrued and other current liabilities	89,030	81,812
Total current liabilities	254,383	259,615
Long-term debt	76,505	76,505
Non-current deferred revenue	52,303	47,143
Other non-current liabilities	23,909	26,822
Total liabilities	407,100	410,085
Commitments and contingencies		
Stockholders equity:		
Common stock	1,208	1,205
Additional paid-in capital	494,548	502,443
Retained earnings	517,000	494,082
Treasury stock	(19,671)	(35,332)
Deferred compensation		(11,394)
Accumulated other comprehensive income	9,506	9,531

Total stockholders equity		1,002,591		960,535
Total liabilities and stockholders equity	$	1,409,691	$	1,370,620

The accompanying notes are an integral part of these financial statements.

Table of Contents

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED INCOME STATEMENTS
FOR THE THREE MONTHS ENDED MARCH 31, 2006 AND 2005
(DOLLARS AND SHARES IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	Three Months Ended March 31,	
	2006	2005
Revenue	$ 542,429	$ 473,271
Direct cost of services	443,727	369,509
Gross profit	98,702	103,762
Selling, general and administrative expenses	64,061	60,124
Operating income	34,641	43,638
Interest income	2,054	2,243
Interest expense	(980)	(845)
Other income (expense), net	641	(292)
Income before taxes	36,356	44,744
Provision for income taxes	13,438	18,302
Net income	$ 22,918	$ 26,442
Basic and diluted earnings per common share:		
Basic earnings per common share	$ 0.19	$ 0.22
Weighted average common shares outstanding	118,642	117,705
Diluted earnings per common share	$ 0.19	$ 0.22
Weighted average diluted common shares outstanding	121,553	122,017

The accompanying notes are an integral part of these financial statements.

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THREE MONTHS ENDED MARCH 31, 2006 AND 2005
(DOLLARS IN THOUSANDS)
(UNAUDITED)

	Three Months Ended March 31,	
	2006	2005
Cash flows from operating activities:		
Net income	$ 22,918	$ 26,442
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	17,858	13,895
Change in deferred taxes	7,733	(174)
Other non-cash items	3,599	3,510
Changes in assets and liabilities (net of effects from acquisitions of businesses):		
Accounts receivable, net	(25,642)	(22,079)
Prepaid expenses	(11,028)	(22,794)
Deferred contract costs, net	(7,988)	(10,374)
Accounts payable and accrued liabilities	18,703	12,182
Deferred revenue	13,887	4,644
Accrued compensation	(25,252)	(31,894)
Income taxes	(7,595)	16,792
Other current and non-current assets	(3,608)	3,736
Other current and non-current liabilities	(824)	(741)
Net cash provided by (used in) operating activities	2,761	(6,855)
Cash flows from investing activities:		
Purchases of property, equipment and purchased software	(17,169)	(14,791)
Acquisitions of businesses	(20,724)	(23,878)
Other	56	
Net cash used in investing activities	(37,837)	(38,669)
Cash flows from financing activities:		
Repayment of long-term debt		(75,498)
Proceeds from issuance of long-term debt		76,505
Proceeds from issuance of common stock	3,944	4,230
Proceeds from issuance of treasury stock	8,026	
Excess tax benefits from stock-based compensation arrangements	1,393	
Other	(463)	(757)
Net cash provided by financing activities	12,900	4,480

Effect of exchange rate changes on cash and cash equivalents	717	(1,561)
Net decrease in cash and cash equivalents	(21,459)	(42,605)
Cash and cash equivalents at beginning of period	259,598	304,786
Cash and cash equivalents at end of period	$ 238,139	$ 262,181

The accompanying notes are an integral part of these financial statements.

Table of Contents

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(SHARES AND DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

NOTE 1. GENERAL

The accompanying unaudited interim condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission. The interim condensed consolidated financial statements include the consolidated accounts of Perot Systems Corporation and its majority-owned subsidiaries with all significant intercompany transactions eliminated. In our opinion, all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of the financial position, results of operations and cash flows for the interim periods presented have been made. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such SEC rules and regulations. These financial statements should be read in conjunction with the audited financial statements for the year ended December 31, 2005, in our Annual Report on Form 10-K filed with the SEC on February 28, 2006. Operating results for the three-month period ended March 31, 2006, are not necessarily indicative of the results for the year ending December 31, 2006.

Certain of the 2005 amounts in the accompanying financial statements have been reclassified to conform to the current presentation.

NOTE 2. ACQUISITIONS

On February 28, 2006, we acquired substantially all of the assets of eServ LLC, a leading provider of high-end product engineering outsourcing services. As a result of the acquisition, we broadened our suite of BPO services for the automotive, manufacturing and industrial services markets. The initial purchase price for eServ was $20,724, $3,051 of which is being held in escrow for up to approximately two years, and we may make additional payments totaling up to $7,000 in cash in 2007 and 2008. The possible future payments are contingent upon eServ achieving certain financial targets for 2006 and 2007. The results of operations of eServ and the estimated fair value of assets acquired and liabilities assumed are included in our condensed consolidated financial statements beginning on the acquisition date. The allocation of eServ purchase consideration to the assets and liabilities acquired, including goodwill, is not final due to the pending completion of the tangible and intangible assets appraisals and a contractual purchase price adjustment. As of March 31, 2006, the estimated fair values of the acquired purchased software and intangible assets totaled $620 and $6,850, respectively, resulting in the estimated excess purchase price over net assets acquired of $9,904, which was recorded as goodwill on the condensed consolidated balance sheets, was assigned to the Industry Solutions segment, and is deductible for tax purposes. The appraisals of tangible and intangible assets are expected to be completed in the second quarter of 2006, and any additional future payments will be recorded as additional goodwill in the Industry Solutions segment.

NOTE 3. GOODWILL

The changes in the carrying amount of goodwill for the three months ended March 31, 2006, by reportable segment are as follows:

	Industry Solutions	Government Services	Consulting and Applications Solutions	Total
Balance as of December 31, 2005	$ 250,208	$ 127,552	$ 65,679	$ 443,439
Estimated goodwill from eServ acquisition	9,904			9,904
Reclassification of goodwill due to change in reporting units	(15,471)		15,471	
Other	(457)	(24)	(807)	(1,288)
Balance as of March 31, 2006	$ 244,184	$ 127,528	$ 80,343	$ 452,055

4

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(SHARES AND DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

During the first quarter of 2006, we combined the Consulting Solutions group, which was previously included in our Commercial Solutions group in the Industry Solutions line of business, with the Applications Solutions line of business. As a result of this change, we allocated a portion of the goodwill from the Commercial Solutions group to both the Commercial Solutions Group and the Consulting and Applications Solutions line of business based on the relative fair values of the Commercial Solutions group and the Consulting Solutions group.

NOTE 4. DEFERRED CONTRACT COSTS, NET, AND IDENTIFIABLE INTANGIBLE ASSETS

Deferred contract costs, net

Included in deferred contract costs, net, was $49,886 and $49,891 as of March 31, 2006 and December 31, 2005, respectively, relating to costs deferred on a contract that includes both construction services and non-construction services. The construction services relate to a software development and implementation project. In accordance with SOP 97-2, we determined that we could not recognize revenue on the software development and implementation project separately from the non-construction services. As a result, we are deferring both the revenue on the software development and implementation project, consisting of the amounts we are billing for those services, and the related costs, up to the relative fair value of the software development and implementation project. The amount of revenue that had been deferred on the software development and implementation project as of March 31, 2006, was $19,133, of which $1,364 was included in current deferred revenue and $17,769 was included in non-current deferred revenue on the condensed consolidated balance sheets. At December 31, 2005, the amount of revenue that had been deferred was $18,924, which was included in non-current deferred revenue. During the first quarter of 2006, the cumulative costs incurred on the software development and implementation project that would have been deferred exceeded the project s relative fair value. Accordingly, these excess costs of $2,630 in the first quarter of 2006 were expensed as incurred to direct cost of services.

The remaining balances of deferred contract costs, net, at March 31, 2006 and December 31, 2005, relate primarily to deferred contract setup costs, which are amortized on a straight-line basis over the lesser of their estimated useful lives or the term of the related contract. Amortization expense for deferred contract setup costs was $2,047 and $829 for the three months ended March 31, 2006 and 2005, respectively.

Identifiable intangible assets

Identifiable intangible assets are recorded in other non-current assets in the condensed consolidated balance sheets and are composed of:

	As of March 31, 2006		
	Gross Carrying Value	Accumulated Amortization	Net Book Value
Service mark	$ 6,697	$ (4,538)	$ 2,159
Customer-based intangible assets	39,949	(16,713)	23,236
Other intangible assets	7,193	(4,361)	2,832
Total	$ 53,839	$ (25,612)	$ 28,227

Total amortization expense for identifiable intangible assets was $1,910 and $1,290 for the three months ended March 31, 2006 and 2005, respectively. Amortization expense is estimated at $8,331, $7,090, $5,647, $3,823, $2,671 and $1,046 for the years ended December 31, 2006 through 2011, respectively. Identifiable intangible assets are amortized on a straight-line basis over their estimated useful lives, ranging from one to 15 years. The weighted average useful life is approximately five years.

Table of Contents

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(SHARES AND DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

NOTE 5. COMPREHENSIVE INCOME

Total comprehensive income, net of tax, was as follows:

	Three Months Ended March 31,	
	2006	2005
Net income	$ 22,918	$ 26,442
Foreign currency translation adjustments	(25)	1,070
Total comprehensive income	$ 22,893	$ 27,512

NOTE 6. STOCKHOLDERS EQUITY

At March 31, 2006, there were 118,490 shares of our Class A Common Stock outstanding and 817 shares of our Class B Common Stock outstanding. At December 31, 2005, there were 117,041 shares of our Class A Common Stock outstanding and 759 shares of our Class B Common Stock outstanding. In the first quarter of 2006, we issued 255 shares of Class A Common Stock and 1,194 shares of Class A Common Stock from treasury for our stock-based compensation plans. In addition, during the first quarter of 2006 we issued 58 shares of Class B Common Stock upon exercise of Class B stock options.

NOTE 7. STOCK OPTIONS AND STOCK-BASED COMPENSATION

Stock-based compensation

On January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123R, Share-Based Payment, which requires employee stock options and rights to purchase shares under stock participation plans to be accounted for under the fair value method and eliminates the ability to account for these instruments under the intrinsic value method prescribed by Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, which was allowed under the original provisions of FAS 123, Accounting for Stock-Based Compensation. Prior to the adoption of FAS 123R and as permitted by FAS 123 and FAS 148, Accounting for Stock-Based Compensation Transition and Disclosure, we elected to follow APB 25 and related interpretations in accounting for our employee stock options and implemented the disclosure-only provisions of FAS 123 and FAS 148. Under APB 25, stock compensation expense was recorded when the exercise price of employee stock options was less than the fair value of the underlying stock on the date of grant.

We adopted FAS 123R using the modified prospective method. Under this transition method, stock compensation expense for the first quarter of 2006 included the cost for all share-based payments granted prior to, but not yet vested, as of January 1, 2006, as well as those share-based payments granted subsequent to December 31, 2005. This compensation cost was based on the grant-date fair values determined in accordance with FAS 123 and FAS 123R, which we estimate using the Black-Scholes option pricing model and record in direct costs of services or in selling, general and administrative expenses on a straight-line basis over the vesting period. In addition, upon adoption of FAS 123R we began recording the related deferred income tax benefits associated with stock compensation expense and began reflecting the excess tax benefits from the exercise of stock-based compensation awards in cash flows from financing activities. Results for prior periods have not been restated.

For the first quarter of 2006, stock compensation expense charged against income for the first time for stock options and costs associated with our employee stock purchase plan was $3,574 ($2,364 net of tax), or approximately $0.02 per diluted share, and was recorded as $1,556 to direct costs of services and $2,018 to selling, general and administrative expenses. Stock compensation expense otherwise charged against

Table of Contents

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(SHARES AND DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

income, primarily for restricted stock units, was $510 ($321 net of tax) and $719 ($453 net of tax) for the three months ended March 31, 2006 and 2005, respectively. At March 31, 2006, there was $40,631 of total unrecognized compensation cost, net of expected forfeitures, related to nonvested share-based payments, which is expected to be recognized over a weighted-average period of 2.7 years.

The following table illustrates the effect on net income and earnings per common share as if we had elected to adopt the expense recognition provisions of FAS 123 for the three months ended March 31, 2005:

Net income	
As reported	$ 26,442
Add: stock-based compensation expense included in reported net income, net of related tax effects	453
Less: total stock-based employee compensation expense determined under fair value based methods for all awards, net of related tax effects	(3,441)
Pro forma	$ 23,454
Basic earnings per common share	
As reported	$ 0.22
Pro forma	$ 0.20
Diluted earnings per common share	
As reported	$ 0.22
Pro forma	$ 0.19

We utilize the Black-Scholes option pricing model to calculate our actual and pro forma stock-based employee compensation expense, and the assumptions used for each period are as follows:

	Three Months Ended March 31,	
	2006	2005
Weighted average risk free interest rates	4.44%	3.83%
Weighted average life (in years)	5.5	4.1
Volatility	39%	43%
Expected dividend yield	0%	0%
Weighted average grant-date fair value per share of options granted	$ 6.55	$ 5.47

Prior to January 1, 2006, with the exception of grants with cliff vesting and acceleration features, the expected life of each grant was generally estimated to be a period equal to one half of the vesting period, plus one year, for all periods presented. The expected life for cliff vesting grants was generally equal to the vesting period, and the expected life for grants with acceleration features was estimated to be equal to the midpoint of the vesting period. For those stock options granted subsequent to December 31, 2005, we estimated the expected life of each grant as the weighted average expected life of each tranche of the granted option, which was determined based on the sum of each tranche's vesting period plus one-half of the period from the vesting date of each tranche to its expiration. Separate groups of employees that have similar historical exercise behavior and forfeiture rates are considered separately for valuation purposes. Expected volatility of our stock price was based on historical volatility over the expected term of the granted option. The estimated fair value is not intended to predict actual future events or the value ultimately realized by employees who receive equity awards.

Table of Contents

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(SHARES AND DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

Description of stock-based compensation plans

Below are descriptions of our active stock-based compensation plans and our 1991 Stock Option Plan, under which a significant number of stock options remain outstanding.

2001 Long-Term Incentive Plan

In 2001, we adopted the 2001 Long-Term Incentive Plan under which employees, directors, or consultants may be granted stock options, stock appreciation rights, and restricted stock or may be issued cash awards, or a combination thereof. Under the 2001 Plan, stock option awards may be granted in the form of incentive stock options or nonstatutory stock options. The exercise price of any incentive stock option issued is the fair market value on the date of grant, and the term of which may be no longer than ten years from the date of grant. The exercise price of a nonstatutory stock option may be no less than 85% of the fair value on the date of grant, except under certain conditions specified in the 2001 Plan, and the term of a nonstatutory stock option may be no longer than eleven years from the date of grant. The vesting period for all options is determined upon grant date, and the options usually vest over a three- to ten-year period, and in some cases can be accelerated through attainment of performance criteria. The options are exercisable from the vesting date, and unexercised vested options are canceled following the expiration of a certain period after the employee s termination date.

Employee stock purchase plan

In July 1998, our Board of Directors adopted an employee stock purchase plan (the ESPP), which provides for the issuance of a maximum of 20,000 shares of Class A Common Stock. The ESPP became effective on February 2, 1999. During 2000, the ESPP was amended such that this plan was divided into separate U.S. and Non-U.S. plans in order to ensure that United States employees continue to receive tax benefits under Sections 421 and 423 of the United States Internal Revenue Code. Following this division of the ESPP into the two separate plans, an aggregate of 19,736 shares of Class A Common Stock were authorized for sale and issuance under the two plans. Eligible employees may have up to 10% of their earnings withheld to be used to purchase shares of our common stock on specified dates determined by the Board of Directors. The price of the common stock purchased under the ESPP will be equal to 85% of the fair value of the stock on the exercise date for the offering period.

1996 Non-Employee Director Stock Option/Restricted Stock Plan

In 1996, we adopted the 1996 Non-Employee Director Stock Option/Restricted Stock Plan. This plan provides for the issuance of up to 800 Class A common shares or options to Board members who are not our employees. Shares or options issued under the plan would be subject to one- to five-year vesting, with options expiring after an eleven-year term. The purchase price for shares issued and exercise price for options issued is the fair value of the shares at the date of issuance. Other restrictions are established upon issuance. The options are exercisable from the vesting date, and unexercised vested options are canceled following the expiration of a certain period after the Board member s termination date.

1991 Stock Option Plan

In 1991, we adopted the 1991 Stock Option Plan, which was amended in 1993 and 1998. In 2001 this plan was terminated; however, provisions of this plan will remain in effect for all outstanding options that were granted under this plan. Pursuant to the 1991 Plan, options to purchase Class A common shares could be granted to eligible employees. Prior to the date of our initial public offering, such options were generally granted at a price not less than 100% of the fair value of our Class A common shares, as determined by the Board of Directors and based upon an independent third-party valuation. Subsequent to our initial public offering date, the exercise price for options issued is the fair market value of the shares on the date of grant. The stock options vest over a three- to ten-year period based on the provisions of each grant, and in some cases can be accelerated through the attainment of performance criteria. The options are usually exercisable

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(SHARES AND DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

from the vesting date, and unexercised vested options are canceled following the expiration of a certain period after the employee s termination date.

Activity in our stock-based compensation plans

Activity in stock options for Class A Common Stock was as follows:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in Years)	Aggregate Intrinsic Value
Outstanding at January 1, 2006	25,342	$14.81		
Granted	41	15.14		
Exercised	(1,212)	8.43		
Forfeited	(4,042)	21.37		
Outstanding at March 31, 2006	20,129	13.87	4.83	$67,896
Exercisable at March 31, 2006	10,873	14.82	4.53	38,759

The following table summarizes information about options for Class A Common Stock outstanding at March 31, 2006:

	Options Outstanding			Options Exercisable	
Range of Prices	Number	Weighted Average Exercise Price	Weighted Average Remaining Life	Number	Weighted Average Exercise Price
$0.25 - $5.00	1,599	$ 2.19	1.70	993	$ 2.07
$5.01 - $10.00	3,078	9.69	5.38	2,391	9.69
$10.01 - $15.00	8,932	12.38	4.82	2,865	11.62
$15.01 - $20.00	2,522	16.37	5.63	1,003	16.83
$20.01 - $25.00	3,998	23.52	5.16	3,621	23.68
Total	20,129	13.87	4.83	10,873	14.82

The aggregate intrinsic value of Class A stock options exercised and restricted stock units vesting during the three months ended March 31, 2006 and 2005 was $8,059 and $4,365, respectively. During the three months ended March 31, 2006 and 2005, we realized income tax benefits of $2,718 and $647, respectively, related to the exercise of Class A and Class B stock options. Of the total income tax benefit of $2,718 for the three months ended March 31, 2006, $1,393 was reflected as excess tax benefits from stock-based compensation arrangements in net cash provided by financing activities in our condensed consolidated statements of cash flow for the same period. For the three months ended March 31, 2006 and 2005, we received $11,970 and $4,230, respectively, in cash from our stock-based compensation arrangements, including cash received upon exercise of stock options and from participants in our employee stock purchase plan, and from the exercise of Class B stock options. In addition, upon adoption of FAS 123R, we reclassified the deferred compensation balance at December 31, 2005, of $11,394, which related primarily to the unearned compensation expense on restricted stock units, to additional paid-in capital.

The number of outstanding nonvested restricted stock units as of March 31, 2006 and December 31, 2005, was 796 and 807, respectively, with a weighted-average grant-date fair value per share of $14.43 and $14.42, respectively. The number of nonvested restricted stock units that vested or forfeited during the first quarter of 2006 was insignificant.

PEROT SYSTEMS CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(SHARES AND DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
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NOTE 8. INCOME TAXES

Our effective tax rate for the first quarter of 2006 was 37.0% as compared to 40.9% for the same period in 2005. Our income tax expense for the first quarter of 2006 included income tax expense of $780 relating to the resolution of several of the tax issues raised in an audit by the Internal Revenue Service, including the impact from similar tax issues in open tax years. Our income tax expense for the first quarter of 2005 included $2,105 of income tax expense on $23,464 of foreign earnings repatriated pursuant to the American Jobs Creation Act of 2004. The income tax expense on these earnings increased our effective tax rate for the first quarter of 2005 by 4.7 percentage points. The remaining decrease in our first quarter 2006 effective tax rate as compared to the same period in 2005 related primarily to a greater impact from our foreign operations, which have tax holidays in certain Asian jurisdictions exempting specific types of income from taxation.

NOTE 9. SEGMENT DATA

We offer our services under three primary lines of business: Industry Solutions, Government Services, and Consulting and Applications Solutions. Industry Solutions, our largest line of business, provides services to our customers primarily under long-term contracts in strategic relationships. These services include technology and business process services, as well as industry domain-based, short-term project and consulting services. The Government Services segment provides consulting, engineering, and technology-based business process solutions for the Department of Defense, the Department of Homeland Security, various federal intelligence agencies, and other governmental agencies. In the first quarter of 2006, we combined the Consulting Solutions group, which was previously included in our Commercial Solutions group in the Industry Solutions line of business, with the Applications Solutions line of business. This combined line of business, Consulting and Applications Solutions, provides software-related services, including the implementation of prepackaged software applications, application development and maintenance, and application systems migration and testing primarily under short-term contracts related to specific projects. Other includes our remaining operating areas and corporate activities, income and expenses that are not related to the operations of the other reportable segments, and the elimination of intersegment revenue and direct costs of services of approximately $11,767 and $9,525 for the quarters ended March 31, 2006 and 2005, respectively, related to the provision of services by the Consulting and Applications Solutions segment to the Industry Solutions segment.

The reportable segments follow the same accounting policies that we use for our consolidated financial statements. Segment performance is evaluated based on income before taxes, exclusive of income and expenses that are included in the Other category. Substantially all corporate and centrally incurred costs are allocated to the segments based principally on expenses, employees, square footage, or usage.

The following is a summary of certain financial information by reportable segment for the quarters ended March 31, 2006 and 2005.

	Industry Solutions	Government Services	Consulting and Applications Solutions	Other	Total
For the quarter ended March 31, 2006:					
Revenue	$418,090	$76,074	$ 60,032	$(11,767)	$542,429
Income before taxes	22,524	4,559	8,567	706	36,356