

SIFY LTD  
Form 20-F  
June 30, 2006

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 20-F**

(Mark One)

- REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**or**

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

**For the fiscal year ended March 31, 2006.**

**or**

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

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

- SHELL COMPANY PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

**Date of event requiring this shell company report \_\_\_\_\_**

**Commission file number 000-27663**

**Sify Limited**

(Exact name of Registrant as specified in its charter)

Not Applicable

(Translation at Registrant's name into English)

Republic of India

(Jurisdiction of incorporation or organization)

Tidel Park, 2nd Floor

No. 4, Canal Bank Road

Taramani, Chennai 600 113 India

(91) 44-2254-0770

(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act: None

Securities registered or to be registered pursuant to Section 12(g) of the Act: American Depositary Shares, each representing one Equity Share, par value Rs.10 per share

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

42,389,514 Equity Shares were issued and outstanding as of March 31, 2006

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes  No

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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 which financial statement item the registrant has elected to follow

Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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**Currency of Presentation and Certain Defined Terms**

Unless the context otherwise requires, references in this annual report to we, us, the company, Sify or Satyam Infoway are to Sify Limited, a limited liability company organized under the laws of the Republic of India. References to U.S. or the United States are to the United States of America, its territories and its possessions. References to India are to the Republic of India. Until December 2002, we were a majority-owned subsidiary of Satyam Computer Services Limited, a leading Indian information technology services company which is traded on the New York Stock Exchange and the major Indian stock exchanges. In January 2003, we changed the name of our company from Satyam Infoway Limited to Sify Limited. Sify.com and SifyOnline are trademarks used by us for which we have obtained registration in India. In this annual report, references to \$, Dollars or U.S. dollars are to the legal currency of the United States, references to Rs., rupees or Indian rupees are to the legal currency of India and references to GBP are to the legal currency of the United Kingdom. References to a particular fiscal year are to our fiscal year ended March 31 of that year.

For your convenience, this annual report contains translations of some Indian rupee amounts into U.S. dollars which should not be construed as a representation that those Indian rupee or U.S. dollar amounts could have been, or could be, converted into U.S. dollars or Indian rupees, as the case may be, at any particular rate, the rate stated below, or at all. Except as otherwise stated in this annual report, all translations from Indian rupees to U.S. dollars contained in this annual report have been based on the noon buying rate in the City of New York on March 31, 2006, for cable transfers in Indian rupees as certified for customs purposes by the Federal Reserve Bank of New York. The noon buying rate on March 31, 2006 was Rs.44.48 per \$1.00.

Our financial statements are prepared in Indian rupees and presented in accordance with United States generally accepted accounting principles, or U.S. GAAP. In this annual report, any discrepancies in any table between totals and the sums of the amounts listed are due to rounding.

Information contained in our websites, including our corporate website, [www.sifycorp.com](http://www.sifycorp.com), is not part of this annual report.

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**Forward-Looking Statements May Prove Inaccurate**

IN ADDITION TO HISTORICAL INFORMATION, THIS ANNUAL REPORT CONTAINS FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF SECTION 27A OF THE SECURITIES ACT OF 1933, AS AMENDED, AND SECTION 21E OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED. THE FORWARD-LOOKING STATEMENTS CONTAINED HEREIN ARE SUBJECT TO RISKS AND UNCERTAINTIES THAT COULD CAUSE ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE REFLECTED IN THE FORWARD-LOOKING STATEMENTS. FACTORS THAT MIGHT CAUSE SUCH A DIFFERENCE INCLUDE, BUT ARE NOT LIMITED TO, THOSE DISCUSSED IN THE SECTION ENTITLED ITEM 3. KEY INFORMATION RISK FACTORS, ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS AND ELSEWHERE IN THIS ANNUAL REPORT. YOU ARE CAUTIONED NOT TO PLACE UNDUE RELIANCE ON THESE FORWARD-LOOKING STATEMENTS, WHICH REFLECT MANAGEMENT'S ANALYSIS ONLY AS OF THE DATE OF THIS ANNUAL REPORT. IN ADDITION, YOU SHOULD CAREFULLY REVIEW THE OTHER INFORMATION IN THIS ANNUAL REPORT AND IN OUR QUARTERLY REPORTS AND OTHER DOCUMENTS FILED WITH THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION, OR SEC, FROM TIME TO TIME. OUR FILINGS WITH THE SEC ARE AVAILABLE ON ITS WEBSITE, [WWW.SEC.GOV](http://WWW.SEC.GOV).

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**PART I**

**Item 1. Identity of Directors, Senior Management and Advisers.**

Not applicable.

**Item 2. Offer Statistics and Expected Timetable**

Not applicable.

**Item 3. Key Information**

**Selected Financial Data**

You should read the selected consolidated financial data below in conjunction with the consolidated financial statements, the related notes and Item 5. Operating and Financial Review and Prospects, all of which are included elsewhere in this Annual Report. The selected consolidated statements of operations data for the five years ended March 31, 2006 and the selected consolidated balance sheet data as of March 31, 2002, 2003, 2004, 2005 and 2006 have been derived from our audited consolidated financial statements and related notes, which have been prepared and presented in accordance with U.S. GAAP.

In addition, the selected consolidated historical financial data presented herein includes transitional disclosures pertaining to adoption of SFAS 142, *Goodwill and other Intangible Assets*, for the year ended March 31, 2002. The selected consolidated historical financial data includes a presentation of EBITDA from continuing operations. EBITDA from continuing operations represents earnings (loss) from continuing operations before interest, taxes, depreciation and amortization, and gain on sale of discontinued operations. EBITDA is neither an Indian GAAP measure nor a U.S. GAAP measure and should not be considered in isolation or as an alternative to net income as an indicator of operating performance or as an alternative to cash flow as a measure of liquidity. Our presentation below also includes a reconciliation of EBITDA from continuing operations to net loss, which we believe to be the most comparable financial measure under U.S. GAAP. EBITDA from continuing operations is presented because it is a basis upon which our management assesses our financial performance and because we believe some investors find it to be a useful tool for measuring a company's ability to fund operating obligations and capital expenditure. Investors evaluating our financial performance or analyzing our discounted cash flows based on EBITDA from continuing operations should consider financing activities and non-recurring charges that are not included in the calculation of EBITDA. Our calculation includes significant charges recorded to reflect the impairment of goodwill. Investors should also review carefully Item 5. Operating and Financial Review and Prospects included elsewhere in this annual report for further information regarding the underlying financial performance of our company. While EBITDA is frequently reported by many companies as a supplemental measure of operations, it is not necessarily comparable to other similarly titled captions of other companies due to potential inconsistencies in the method of calculation.

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	Fiscal year ended March 31					
	2002	2003	2004	2005	2006	2006
	Indian Rupees(1)					U.S.
	(In thousands, except share and per share data)					Dollars(2)
<b>Statement of Operations Data:</b>						
Revenues	1,560,288	1,959,855	2,751,623	3,554,237	4,606,409	103,561
Revenue from related parties	17,200	34,345	49,561	59,220	75,398	1,695
Total Revenue	1,577,488	1,994,200	2,801,184	3,613,457	4,681,807	105,256
Cost of revenues (excluding depreciation and amortization)	1,192,671	1,264,101	1,476,714	2,023,942	2,534,723	56,985
Selling, general and administrative expenses	1,256,763	1,090,935	1,208,884	1,418,757	1,852,296	41,643
Provision for doubtful debts, receivables and advances	101,500	156,233	76,487	57,579	90,670	2,038
Impairment of assets		246,999	22,251			
Depreciation	574,867	474,261	432,684	472,400	395,018	8,881
Amortization of intangible assets	29,337	69,907	99,350	84,387	68,759	1,546
Acquisition expenses	20,000					
Amortization/impairment of goodwill	4,420,644					
Amortization of deferred stock compensation expense	9,686	57,729	27,946	10,639	12,749	287
Foreign exchange (gain)/loss	(44,520)	18	52,148	(2,595)	(23,221)	(522)
Total operating expenses	7,560,948	3,360,183	3,396,764	4,065,109	4,930,994	110,858
Operating loss	(5,983,460)	(1,365,983)	(595,580)	(451,652)	(249,187)	(5,602)
Other (expense)/income, net	32,711	52,948	144,147	93,324	59,239	1,332
Loss before equity in losses of affiliates, income taxes and minority interest	(5,950,749)	(1,313,035)	(451,433)	(358,328)	(189,948)	(4,270)
Equity in profits/(losses) of affiliates (including gain on sale of investments in affiliates)	(1,225,444)	(26,061)	80,142	50,752	40,703	915
Loss before income taxes and minority interest	(7,176,193)	(1,339,096)	(371,291)	(307,576)	(149,245)	(3,355)
Income taxes		(2,856)	(72)			
Minority interest	17,928	12,564	79			

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Loss from continuing operations	(7,158,265)	(1,329,388)	(371,284)	(307,576)	(149,245)	(3,355)
Discontinued operations						
Income/(loss) from discontinued operations (3)	(125,373)					
Profit on sale of discontinued operations, net of direct costs	81,121					
Net loss	(7,202,517)	(1,329,388)	(371,284)	(307,576)	(149,245)	(3,355)
Net profit/ (loss) per equity share continuing operations	(308.59)	(51.15)	(10.76)	(8.75)	(4.05)	(0.09)
Discontinued operations	(1.91)					
Net loss per share (4)	(310.50)	(51.15)	(10.76)	(8.75)	(4.05)	(0.09)
Weighted average equity shares used in computing net loss per equity share	23,196,428	25,988,095	34,519,545	35,156,120	36,811,476	36,811,476

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	2002	Fiscal year ended March 31				2006	2006 U.S. Dollars(2)
		2003	2004	2005	2006		
		Indian Rupees(1)					
		(In thousands, except share and per share data)					
Transitional disclosures pertaining to adoption of SFAS 142 Goodwill and other Intangible Assets							
Reported net loss	(7,202,517)	(1,329,388)	(371,284)	(307,576)	(149,245)	(3,355)	
Less: Goodwill amortization	292,964						
Less: Equity goodwill amortization	75,210						
Adjusted net loss	(6,834,343)	(1,329,388)	(371,284)	(307,576)	(149,245)	(3,355)	
Reported net loss per share	(310.50)	(51.15)	(10.76)	(8.75)	(4.05)	(0.09)	
Less: Goodwill amortization	12.63						
Less: Equity goodwill amortization	3.24						
Adjusted net loss per share	(294.63)	(51.15)	(10.76)	(8.75)	(4.05)	(0.09)	
<b>Balance Sheet Data:</b>							
Cash and cash equivalents	658,111	897,596	1,325,803	1,323,912	2,822,501	63,456	
Total assets	4,146,274	3,700,387	3,799,073	4,020,782	5,951,771	133,808	
Long-term debt, including current installments							
Total shareholders equity	3,394,113	2,888,696	2,715,668	2,498,589	4,054,509	91,153	
<b>Other Financial Data:</b>							
EBITDA from continuing operations (5)	(6,589,135)	(755,394)	142,707	209,029	268,057	6,026	
Add: Interest and income tax	49,540	31,999	48,187	52,760	70,314	1,581	
Income from discontinued operations							
Profit on sale of discontinued operations	81,121						
	130,661	31,999	48,187	52,760	70,314	1,581	
Less: Depreciation and amortization	613,890	601,897	559,980	567,426	476,526	10,714	
Interest and income tax	4,780	4,096	2,198	1,939	11,090	248	
Loss from discontinued operations	125,373						
	744,043	605,993	562,178	569,365	487,616	10,962	
Net loss	(7,202,517)	(1,329,388)	(371,284)	(307,576)	(149,245)	(3,355)	

**Notes**

1. Certain prior-year data has been reclassified to conform to the current year presentation.

2. Convenience translation to U.S. Dollars done at the noon buying rate on March 31, 2006 of Rs.44.48 per \$1.00, which should not be construed as a representation that those Indian rupee or U.S. dollar amounts could have been, or could be, converted into U.S. dollars or Indian rupees, as the case may be, at this rate or at all.
3. There is no goodwill associated with discontinued operations.
4. Reference to shares and per share amounts refer to our equity shares. Our outstanding equity shares include equity shares held by a depositary underlying our ADSs. Effective September 24, 2002, one ADS represented one equity share. Our 1-for-4 reverse stock split on September 24, 2002 did not

have any effect on our equity shares or per equity share amounts, as the underlying shares representing ADSs were unchanged.

5. EBITDA from continuing operations represents earnings (loss) from continuing operations before interest, taxes, depreciation and amortization, and income or gain on sale of discontinued operations.

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The following table sets forth, for each of the months indicated, information concerning the high and low number of Indian rupees for which one U.S. dollar could be exchanged based on the noon buying rate in the City of New York for cable transfers in Indian rupees as certified for customs purposes by the Federal Reserve Bank of New York:

<b>Month</b>	<b>High Rs.</b>	<b>Low Rs.</b>
December 2005	46.26	44.94
January 2006	44.92	43.89
February 2006	44.54	44.10
March 2006	44.58	44.09
April 2006	45.09	44.39
May 2006	46.22	44.69

The following table sets forth, for the fiscal years indicated, information concerning the number of Indian rupees for which one U.S. dollar could be exchanged based on the average of the noon buying rate in the City of New York on the last day of each month during the period for cable transfers in Indian rupees as certified for customs purposes by the Federal Reserve Bank of New York:

<b>Fiscal Year Ended March 31</b>	<b>Period end Rs.</b>	<b>Average Rs.</b>	<b>High Rs.</b>	<b>Low Rs.</b>
2002	48.83	47.71	48.91	46.58
2003	47.53	48.49	49.14	47.39
2004	43.40	43.46	47.46	43.40
2005	43.62	44.86	46.45	43.27
2006	44.48	44.34	44.58	44.09

On March 31, 2006, the noon buying rate in the city of New York was Rs.44.48 per \$1.00.

**Capitalization and indebtedness**

Not applicable.

**Reasons for the offer and use of proceeds**

Not applicable.

**Risk Factors**

*Any investment in our ADSs involves a high degree of risk. You should consider carefully the following information about these risks, together with the other information contained in this annual report for the year ended March 31, 2006, before you make an investment decision regarding our ADSs. If any of the following risks actually occurs, our company could be seriously harmed. In any such case, the market price of our ADSs could decline, and you may lose all or part of the money you paid to buy our ADSs.*

**Risks Related to Sify Limited**

**Although we commenced operation of our private data network business in April 1998, launched our Internet portal website in October 1998 and Internet service provider operations in November 1998, we have added a number of new lines of business in the last five years, including the operation and licensing of public Internet cafés, as well as the provision of broadband services, security services and managed network services. It is therefore difficult to evaluate our company based on our historical results of operations.**

We commenced operation of our private data network business in April 1998 and launched our Internet portal website in October 1998 and Internet service provider operations in November 1998. We commenced retail Internet services by offering dial-up services from homes in November 1998, and later began offering public Internet access through

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a network of cybercafés in March 2000. In June 2003, we launched our high-speed Internet access through a network of independent Cable Television Operators, or CTOs. More recently, we launched our public Internet cafe business and began offering broadband services, security services and managed network services. The industry we operate in is still evolving and therefore comparable benchmarks are not readily available. As of December 2005, the Internet penetration in India was only 0.7% according to figures compiled from Telecom Regulatory Authority of India, or TRAI, Report on Performance of Telecom Industry, March 2006. Due to the relatively short operating history for our current lines of business, it is difficult to evaluate our performance in comparison to companies in other, more mature industries. You must consider the risks and difficulties frequently encountered by companies in this stage of development, particularly companies in the new and rapidly evolving Internet service markets. These risks and difficulties include our ability to:

continue to develop and upgrade our technology;

maintain and develop strategic relationships with business partners;

offer compelling online services and content; and

promptly address the challenges faced by early stage companies, which do not have an experience or performance base to draw on.

Not only is our operating history short, but we have decided to compete in three primary businesses that we believe are complementary. These three businesses are corporate network/data services, retail Internet access services, online portal services and content offerings. We cannot assure you that we will successfully address the risks or difficulties described above. Failure to do so could lead to an inability to attract and retain corporate customers for our network/data services and subscribers for our Internet access services as well as the loss of advertising revenues.

**For the fiscal year ended March 31, 2005 and 2006, we incurred net losses of Rs.307.6 million and Rs.149.2 million (\$3.4 million), respectively. As of March 31, 2006, we had an accumulated deficit of approximately Rs.12,565.9 million (\$282.5 million). We may incur additional losses in the future because our business plan, which is unproven, calls for additional corporate customers and subscribers to maintain profitability.**

For the first time since our founding, we had a profitable quarter for the quarter ended March 31, 2006. However we have, in the past, incurred significant losses and negative cash flows. For the fiscal years ended March 31, 2005 and 2006, we incurred net losses of Rs.307.6 million and Rs.149.2 million (\$3.4 million). As of March 31, 2006, we had an accumulated deficit of approximately Rs.12,565.9 million (\$282.5 million). We may incur operating losses as we expand our services, advertise and promote our brand and respond to competition. Our business plan assumes that businesses in India will demand private network and related services. Our business plan also assumes that an increasing number of consumers and corporate customers in India will be attracted to and use Internet access services, content available on the Internet and other connectivity services offered by us. This business model is not yet proven in India, and we cannot assure you that we will be able to sustain profitability or that we may not incur operating losses in the future.

**We may be required to further modify the rates we charge for our services in response to new pricing models introduced by new and existing competition which would significantly affect our revenues.**

Our corporate network/data services business faces significant competition from well-established companies, including Bharti Airtel, Videsh Sanchar Nigam Limited, or VSNL, Reliance Infocomm, HCL Infinet, Tata Teleservices and the incumbent government-owned telecommunication companies, Bharat Sanchar Nigam Limited, or BSNL, and Mahanagar Telephone Nigam Limited, or MTNL. A significant number of competitors have entered India's liberalized Internet service provider market, like Tulip IT services, and we expect additional competitors to emerge in the future. As of December 2005, there were 155 Internet service providers that were operational in India. New entrants into the national Internet service provider market in India, especially the state run telecommunication companies, may enjoy significant competitive advantages over our company, including greater financial resources, which could allow them to charge prices that are lower than ours in order to attract subscribers. These factors have

resulted in periods of significant reduction in actual average selling prices for consumer Internet Service Provider, or ISP, services. We expect the market for Internet access and other connectivity services to remain extremely price competitive. Increased competition may result in operating losses, loss of market share and diminished value in our services, as well as different pricing, service or marketing decisions. We cannot assure you that we will be able to successfully compete against current and future competitors.

**The Indian Department of Telecommunications, or DOT, has imposed a license fee for ISP s, including our company, for providing Virtual Private Network, or VPN, services. In November 2005, DOT withdrew the VPN license and announced new guidelines whereby ISPs need to have National Long Distance/International Long Distance or NLD/ILD licenses to provide VPN services and eased the eligibility criteria for the provision of NLD/ILD services.**

Our company and certain other ISP s have been providing Internet Protocol Virtual Private Network, or IP VPN, services to their customers for a considerable length of time. These services have been construed to be similar to leased line

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services offered by national and international long distance service providers in India, which have objected to the provisioning of these services by ISPs. The DOT had decided to specifically include IP VPN services in the ISP license and had imposed a one-time entry fee for this purpose. In fiscal 2005, we paid Rs.100 million as a one-time entry fee and submitted a financial bank guarantee of Rs.10 million to the Indian government as required by the DOT. The DOT also required ISP licensees to pay an annual fee of 8% of adjusted gross revenues generated under the ISP license. However the DOT had not issued any guidelines or procedures for implementing this decision. We reserved Rs. 24.6 million for the period April 1, 2005 to December 31, 2005 and Rs.12.72 million for the period January 1, 2006 to March 31, 2006 towards the 6% annual fee on Adjusted Gross Revenue or AGR as per the ILD/NLD license requirement. We had reserved Rs.5.6 million for the year ended March 31, 2005 towards the 8% annual fee on VPN revenue pursuant to the provisional license guidelines.

On November 10, 2005, the Government of India issued guidelines for obtaining a National Long Distance, or NLD, and International Long Distance, or ILD, license and the terms and conditions for the license. These guidelines eliminated the IPVPN license and permitted existing IP VPN provisional license holders to migrate to the NLD/ILD service license. The guidelines allow a period of four months to conform to the requirements of the NLD/ILD license. We have accordingly applied for these licenses through our subsidiary company Sify Communications Ltd. (formerly known as Safescrypt Ltd) and the VPN business will be transferred to this company upon receipt of the licenses. Sify Limited continues to provide IP-VPN services to its customers pending receipt of the licenses. While the guidelines are clear in respect of the adjustment of one time entry fee paid for the VPN license towards the one time for NLD/ILD fee, they are not clear as to the payment of the annual fee on the VPN services for the current period. As such, we have reserved the same payment as per the provisional license guidelines but we cannot assure you that the ultimate fees will not be higher.

**Our marketing campaign to establish brand recognition and loyalty for the Sify Broadband, Sify Max, Sify and *ipay* brands could be unsuccessful.**

In order to expand our customer base and increase traffic on our websites, we must establish, maintain and strengthen the Sify Broadband, Sify Max, Sify and *ipay* and other key brands. We plan to continue to incur significant marketing expenditure to establish brand recognition and brand loyalty. If our marketing efforts do not produce a significant increase in business to offset our marketing expenditure, our losses will increase or, to the extent that we are generating profits, our profits will decrease. Furthermore, our Internet portal will be more attractive to advertisers if we have a large audience of consumers with demographic characteristics that advertisers perceive as favorable. Therefore, we intend to introduce additional and enhanced content, interactive tools and other services and features in the future in an effort to retain our current subscribers and users and attract new ones. Our reputation and brand name could be adversely affected if we are unable to do so successfully.

**If our efforts to retain our customers through past investment in network infrastructure and ongoing investment in online content offerings and customer and technical support are unsuccessful, our revenues will decrease without a corresponding reduction in costs.**

Our sales, marketing and other costs of acquiring new customers are substantial, relative to the fees actually derived from these customers. Accordingly, our long-term success depends to a great extent on our ability to retain our existing customers, while continuing to attract new customers. We have invested significant resources in our network infrastructure and continue to invest in online content offerings and in our customer and technical support capabilities to provide high levels of customer service. We cannot be certain, however, that these investments will maintain or improve subscriber retention. We believe that intense competition from our competitors has caused, and may continue to cause, some of our customers to switch to our competitors' services. In addition, some new customers use the Internet only as a novelty and do not become consistent users of Internet services, and therefore are more likely to discontinue their service. Any decline in our customer retention rate would likely decrease the revenues generated by our Internet access services division. Therefore, we may not be able to realize sufficient future revenues to offset our past investment in network infrastructure and our ongoing investment in online content offerings and technical support or achieve positive cash flow or profitability in the future.

**Despite cost-reduction measures, our future operating results could fluctuate in part because our expenses are relatively fixed in the short term while future revenues are uncertain, and any adverse fluctuations could**

**negatively impact the price of our ADSs.**

Our revenues, expenses and operating results have varied in the past and may fluctuate significantly in the future due to a number of factors, many of which are outside our control. A significant portion of our investment and cost base is relatively fixed in the short term. Our revenues for the foreseeable future will depend on many factors, including the following:

the range of corporate network/data services provided by us and the usage thereof by our customers; and

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the number of subscribers to our ISP services and the prevailing prices charged.  
advertising revenue generated by our online portal services.

Our future revenues are difficult to forecast and, in addition to the foregoing, will depend on the following:  
the timing and nature of any agreements we enter into with strategic partners of our corporate network/data  
services division;

services, products or pricing policies introduced by our competitors;

capital expenditure and other costs relating to our operations;

the timing and nature of our marketing efforts;

our ability to successfully integrate operations and technologies from any acquisitions, joint ventures or other  
business combinations or investments;

the introduction of alternative technologies; and

technical difficulties or system failures affecting the telecommunication infrastructure in India, the Internet  
generally or the operation of our websites.

We plan to continue to expand and develop content and enhance our technology. Many of our expenses are  
relatively fixed in the short-term. We cannot assure you that our revenues will increase in proportion to the increase in  
our expenses. We may be unable to adjust spending quickly enough to offset any unexpected revenues shortfall. This  
could lead to a shortfall in revenues in relation to our expenses.

You should not rely on yearly comparisons of our results of operations as indicators of future performance. It  
is possible that in some future periods our operating results may be below the expectations of public market analysts  
and investors. In this event, the price of our ADSs will likely fall.

**Because we lack full redundancy for our computer systems, a systems failure could prevent us from  
operating our business.**

We rely on the Internet and accordingly, depend upon the continuous, reliable and secure operation of Internet  
servers, related hardware and software and network infrastructure such as lines leased from telecom operators. We  
have a back-up data facility, but we do not have full redundancy for all of our computer and telecommunications  
facilities. As a result, failure of key primary or back-up systems to operate properly could lead to a loss of customers,  
damage to our reputation and violations of our Internet service provider license and contracts with corporate  
customers. A loss of customers or damage to our reputation would result in a decrease in the number of our  
subscribers, which would cause a material decrease in revenues. A violation of our Internet service provider license  
could result in the suspension or termination of that license, which would prevent us from carrying on a significant  
portion of our operations and materially adversely affect our operating results. Violations of our contracts with  
corporate customers could result in the termination of these contracts, which would cause a decrease in the revenues  
generated by our corporate data/network services division. Any of these failures could also lead to a decrease in value  
of our ADSs, significant negative publicity and litigation. From time to time, a number of large Internet companies  
have suffered highly publicized system failures resulting in adverse reactions to their stock prices, significant negative  
publicity and, in some instances, litigation.

We have at times suffered service outages. We guarantee to a number of our corporate customers that our  
network will meet or exceed contractual reliability standards, and our Internet service provider license requires that we  
provide an acceptable level of service quality and that we remedy customer complaints within a specified time period.  
Our computer and communications hardware are protected through physical and software safeguards. However, they  
are still vulnerable to fire, storm, flood, power loss, telecommunications failures, physical or software break-ins and  
similar events. We do not carry business interruption insurance to protect us in the event of a catastrophe even though  
such an event could lead to a significant negative impact on our business.

**Security breaches could damage our reputation or result in liability to us.**

Our facilities and infrastructure must remain secure, and be perceived by our corporate and consumer customers to be secure, because we retain confidential customer information in our database. Despite the implementation of security measures, our infrastructure may be vulnerable to physical break-ins, computer hacking, computer viruses, programming errors or similar disruptive problems. If a person circumvents our security measures, he or she could jeopardize the security of confidential information stored on our systems, misappropriate proprietary information or cause interruptions in our operations. We may be required to make significant additional investments and efforts to protect against or remedy security breaches. A material security breach could damage our reputation or result in liability to us, and we do not carry insurance that protects us from this kind of loss.

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The security services that we offer in connection with our business customers' networks cannot assure complete protection from computer viruses, break-ins and other disruptive problems. Although we attempt to contractually limit our liability in such instances, the occurrence of these problems could result in claims against us or liability on our part. These claims, regardless of their ultimate outcome, could result in costly litigation and could damage our reputation and hinder our ability to attract and retain customers for our service offerings.

**Over the past several years we have experienced significant growth, and continuing this pace of growth could put excessive strain on our resources, which in turn could adversely affect our results of operations.**

Over the last several years, we have experienced a period of significant revenue growth. This growth has placed, and will continue to place, a significant strain on our managerial, operational, financial and information systems resources. We will have to implement new operational and financial systems and procedures and controls, expand our office facilities, train and manage our employee base and maintain close coordination among our technical, accounting, finance, marketing, sales and editorial staff. If we are unable to manage our growth effectively, we will be unable to implement our strategy, upon which the success of our business depends.

**We face a competitive labor market for skilled personnel and therefore are highly dependent on our existing key personnel and on our ability to hire additional skilled employees.**

Our success depends upon the continued service of our key personnel. Most of our employees are located in India. Each of our employees may voluntarily terminate his or her employment with us. We do not carry key person life insurance on any of our personnel, other than our Chief Executive Officer. Our success also depends on our ability to attract and retain additional highly qualified technical, marketing and sales personnel. The labor market for skilled employees in India is extremely competitive, and the process of hiring employees with the necessary skills is time consuming and requires the diversion of significant resources. We may not be able to continue to retain or integrate existing personnel or identify and hire additional personnel in the future. The loss of the services of key personnel, especially the unexpected death or disability of such personnel, or the inability to attract additional qualified personnel, could disrupt the implementation of our business strategy, upon which the success of our business depends.

**The failure to keep our technical knowledge confidential could erode our competitive advantage.**

Like many of our competitors, we possess extensive technical knowledge about our products. Our know-how is a significant independent asset, which may not be protected by intellectual property rights such as patents, but is protected only by maintaining its confidentiality. As a result, we cannot be certain that our know-how will remain confidential in the long run. Employment contracts with certain of our employees who have special technical knowledge about our products or our business contain a general obligation to keep all such knowledge confidential and such obligation extends for a period of two years after the termination of employment. In addition to the confidentiality provisions, these employment agreements typically contain non-competition clauses. If either the confidentiality provisions or the non-competition clauses are unenforceable, we may not be able to maintain the confidentiality of our know-how. Even if every possible precaution, whether contractual or otherwise, is taken to protect confidential technical knowledge about our products or our business, there is still a danger that such information may be disclosed to others or become public knowledge in circumstance beyond our control. In the event that confidential technical information or know-how about our products or business becomes available to third parties or to the public, our competitive advantage over other companies in the wireless based IP/VPN industry could be harmed which could have a material adverse effect on our current business, future prospects, financial condition and results of operations.

**Compliance with new and changing corporate governance and public disclosure requirements adds uncertainty to our compliance policies and increases our costs of compliance.**

Changing laws, regulations and standards relating to accounting, corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002 and, new SEC regulations and Nasdaq National Market rules, are creating uncertainty for us and similarly situated companies. These new or changed laws, regulations and standards may lack specificity and are subject to varying interpretations. Their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs of compliance as a result of ongoing revisions to such governance standards.

In particular, our efforts to comply with Section 404 of the Sarbanes-Oxley Act of 2002 and the related regulations regarding our required assessment of our internal controls over financial reporting and our independent registered public accounting firm's audit of that assessment will require the commitment of significant financial and managerial resources. We have formed an internal

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control steering committee and adopted a project work plan to assess the adequacy of our internal controls over financial reporting, remediate any control deficiencies that may be identified, and validate through testing that our controls are functioning as documented. Our independent registered public accounting firm may be unable to issue unqualified attestation reports on management's assessment on the operating effectiveness of our internal controls over financial reporting.

We are committed to maintaining high standards of corporate governance and public disclosure, and our efforts to comply with evolving laws, regulations and standards in this regard have resulted in, and are likely to continue to result in, increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities. In addition, the new laws, regulations and standards regarding corporate governance may make it more difficult for us to obtain director and officer liability insurance. Further, our board members, Chief Executive Officer, and Chief Financial Officer could face an increased risk of personal liability in connection with the performance of their duties. As a result, we may face difficulties in attracting and retaining qualified board members and executive officers, which could harm our business. If we fail to comply with new or changed laws or regulations, our business and reputation may be harmed.

**We may not comply with local laws of other countries.**

As part of our international business, we may negotiate with and enter into contracts with strategic partners, clients, suppliers, employees and other third parties in various countries. We have little or no experience conducting business in many of these countries and our failure to comply with their laws may result in lawsuits or penalties, which could adversely affect our business or results of operations.

**If there is an adverse outcome in the class action litigation that has been filed against us, our business may be harmed.**

Our company and certain of our officers and directors are named as defendants in a securities class action lawsuit filed in the United States District Court for the Southern District of New York. This action, which is captioned *In re Satyam Infoway Ltd. Initial Public Offering Securities Litigation*, also names as defendants several of the underwriters involved in our initial public offering of American Depositary Shares. This class action is brought on behalf of a purported class of purchasers of our ADSs from the time of our Initial Public Offering, or IPO in October 1999 through December 2000. The central allegation in this action is that the underwriters in our IPO solicited and received undisclosed commissions from, and entered into undisclosed arrangements with, certain investors who purchased our ADSs in the IPO and the aftermarket. The complaint also alleges that we violated the United States federal securities laws by failing to disclose in the IPO prospectus that the underwriters had engaged in these allegedly undisclosed arrangements. More than 300 issuers have been named in similar lawsuits. In June 2003, the plaintiffs in the consolidated IPO class action lawsuits currently pending against us and more than 300 other issuers who went public between 1998 and 2000 announced a proposed settlement with us and the other issuer defendants. The proposed settlement provides that the insurers of all settling issuers will guarantee that the plaintiffs recover \$1.0 billion from non-settling defendants, including the investment banks who acted as underwriters in those offerings. In the event that the plaintiffs do not recover \$1.0 billion, the insurers for the settling issuers will make up the difference. We believe that we have sufficient insurance coverage to cover the maximum amount that we may be responsible for under the proposed settlement, which we estimate to be approximately U.S. \$3.9 million. Although the Federal District Court has preliminarily approved the settlement, it is possible that the Federal District Court may not approve the settlement in whole or part. We believe that we have adequate legal defenses for these actions and that the ultimate outcome of these actions will not have a material adverse effect on our company.

**We face risks associated with potential acquisitions, investments, strategic partnerships or other ventures, including whether any such transactions can be identified, completed and the other party integrated with our business on favorable terms.**

We may attempt to grow our business through acquisitions. We are actively seeking opportunities to expand our corporate services business, including through possible acquisition transactions in India, the United States or elsewhere. We may acquire or make investments in other complementary businesses, technologies, services or products, or enter into additional strategic partnerships with parties that can provide access to those assets, if appropriate opportunities arise in the future. From time to time, we have had discussions and negotiations with a

number of companies regarding our acquiring, investing in or partnering with their businesses, products, services or technologies, and we regularly engage in such discussions and negotiations in the ordinary course of our business. Some of those discussions also contemplate the other party making an investment in our company. We may not identify suitable acquisition, investment or strategic partnership candidates in the future, or if we do identify suitable candidates, we may not complete those transactions on commercially acceptable terms or at all. In addition, the key personnel of an acquired company may decide not to work for us. If we make other types of acquisitions, we could have difficulty in integrating the acquired products, services or technologies into our operations. These difficulties could disrupt our ongoing business, distract our management and employees and increase our expenses, which could adversely affect our operating results and cause the price of our ADSs to decline. Furthermore, we may incur indebtedness or issue additional equity securities to pay for any future acquisitions. The issuance of additional equity securities would dilute the ownership interests of the holders of our ADSs.

**Table of Contents****Our financial results are impacted by the financial results of entities that we do not control.**

We have a significant, non-controlling minority interest in Man Financial Sify Securities India Private Limited (formerly known as Refco Sify Securities India Private Limited) that is accounted for under U.S. GAAP using the equity method of accounting. Under this method, we generally are obligated to report as Equity in losses (gains) of affiliates a pro rata portion of the financial results of any such company in our statement of operations even though we do not control the other company, subject to limitations in the case of losses that exceed our cost of investment. Thus, our reported results of operations can be significantly increased or decreased depending on the results of Man Financial Sify Securities India Private Limited or other companies in which we may make similar investments even though we may have only a limited ability to influence these activities.

In October 2005, Refco Group US, or Refco, the 70.15% shareholder of Man Financial Sify Securities India Private Limited or Man-Sify, sought bankruptcy protection through a Chapter 11 filing at the New York Courts. Consequent to this, the businesses of Refco were under auction process and the auction bid was won by M/s Man Financial Inc, or Man Financial. The bid includes the holding of shares of Man-Sify by Refco. In connection with the purchase of Man-Sify shares by Man Financial, Man Financial and our company executed a Shareholders Agreement on November 25, 2005, pursuant to which, among other things, the name of Refco-Sify will change to Man-Sify. We do not have the valuation basis or the amount for which Man Financial has estimated in its bid. We, however, understand that the bid is higher than the book value of the shares. Further, we understand that Man-Sify's business has not been significantly impacted due to these developments.

**Our inter-city network is leased from other service providers and is dependent on their quality and availability.**

We have provided inter-city connectivity for our wireless-based IP/VPN business through lease arrangements rather than through capital investment in connectivity assets. Our ability to offer high quality telecommunications services depends, to a large extent, on the quality of the networks maintained by other operators, and their continued availability, neither of which is under our control. However, the abundance of supply of inter-city connectivity provides us with the ability of switching to companies offering better services. Although we always use more than one service provider where required, there can be no assurance that this dependence on external parties would not affect our network availability.

**A significant majority of the *ify* cybercafés are franchised operations that we do not operate or control. We also provide Internet access services through a network of Cable Television Operators, or CTOs, whom we do not control.**

As of March 31, 2006, 3,273 cybercafés, representing substantially all of the *ify* cafes, were franchised by our company. Broadband Internet access to homes was provided through a network of about 1,500 CTOs. Our relationships with franchisees and CTOs are subject to a number of special risks. For example, we do not operate or control our franchisees or CTOs, and they may not meet their obligations under our agreements with them. The failure of a franchisee or CTO to provide quality services to its customers could result in end user dissatisfaction with our company. We may become involved in disputes with our franchisees or CTOs, which may result in litigation or the termination of one or more of our agreements. Our franchisees or CTOs could attempt to organize themselves into unions in order to negotiate more favorable terms in our agreements. Any failure to continue our relationships with our franchisees or CTOs on favorable terms could reduce the size of our market share for Internet access in India and decrease the revenues generated by our Internet access services division. Our company does not provide any financial support or guarantee to the franchisees.

**The legal system in India does not protect intellectual property rights to the same extent as the legal system of the United States, and we may be unsuccessful in protecting our intellectual property rights.**

Our intellectual property rights are important to our business. We rely on a combination of copyright and trademark laws, trade secrets, confidentiality procedures and contractual provisions to protect our intellectual property.

Our efforts to protect our intellectual property may not be adequate. We hold no patents, and our competitors may independently develop similar technology or duplicate our services. Unauthorized parties may infringe upon or misappropriate our services or proprietary information. In addition, the laws of India do not protect proprietary rights to the same extent as laws in the United States, and the global nature of the Internet makes it difficult to control the

ultimate destination of our services. For example, the legal processes to protect service marks in India are not as effective as those in place in the United States. The misappropriation or duplication of our intellectual property could disrupt our ongoing business, distract our management and employees, reduce our revenues and increase our expenses. In the future, litigation may be necessary to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. Any such litigation could be time-consuming and costly.

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We could be subject to intellectual property infringement claims as the number of our competitors grows and the content and functionality of our websites or other service offerings overlap with competitive offerings. Defending against these claims, even if not meritorious, could be expensive and divert management's attention from operating our company. If we become liable to third parties for infringing their intellectual property rights, we could be required to pay a substantial damage award and forced to develop non-infringing technology, obtain a license or cease selling the applications that contain the infringing technology. We may be unable to develop non-infringing technology or obtain a license on commercially reasonable terms, or at all.

**Our current infrastructure and its scalability may not accommodate increased use while maintaining acceptable overall performance.**

Currently, only a relatively limited number of customers use our corporate network, our Internet service provider services and our Internet portal. We must continue to add to our network infrastructure to accommodate additional users, increasing transaction volumes and changing customer requirements. We may not be able to project accurately the rate or timing of increases, if any, in the use of our websites or upgrade our systems and infrastructure to accommodate such increases. Our systems may not accommodate increased use while maintaining acceptable overall performance. Service lapses could cause our users to use the online services of our competitors.

**We do not plan to pay dividends in the foreseeable future.**

We do not anticipate paying cash dividends to the holders of our ADSs and equity share holders in the foreseeable future. Accordingly, investors must rely on sales of their ADSs after price appreciation, which may never occur, as the only way to realize a positive return on their investment. Investors seeking cash dividends should not purchase our ADSs.

***Risks Related to the ADSs and Our Trading Market*****The interests of our significant shareholder, Infinity Capital Ventures, L.P., may differ from your interests.**

Based on our review of filings made with the SEC, as of the date of this report, we believe Infinity Capital owns approximately 42% of our outstanding equity capital, and Mr. Raju Vegesna of Infinity Capital serves as our Chairman of the Board of Directors and we have appointed Mr. P.S. Raju as the second nominee of Infinity Capital to our Board of Directors. As a result, Infinity Capital will be able to exercise significant influence over many matters requiring approval by our Board of Directors and/or our shareholders, including the election of directors and approval of significant corporate transactions, such as a sale of our company. Under Indian law, a simple majority is sufficient to control all shareholder action except for those items, which require approval by a special resolution. If a special resolution is required, the number of votes cast in favor of the resolution must not be less than three times the number of votes cast against it. Examples of actions that require a special resolution include:

altering our Articles of Association;

issuing additional shares of capital stock, except for pro rata issuances to existing shareholders;

commencing any new line of business; and

commencing a liquidation.

Circumstances may arise in which the interests of Infinity Capital, or a subsequent purchaser of the shares currently owned by Infinity Capital, could conflict with the interests of our other shareholders or holders of our ADSs. Infinity Capital could delay or prevent a change of control of our company even if a transaction of that sort would be beneficial to our other shareholders, including the holders of our ADSs.

**Holders of ADSs are restricted in their ability to exercise preemptive rights under Indian law and thereby may suffer future dilution of their ownership position.**

Under the Indian Companies Act, 1956 of India, or Indian Companies Act, a public company incorporated in India must offer its holders of equity shares preemptive rights to subscribe and pay for a proportionate number of shares to maintain their existing ownership percentages prior to the issuance of any new equity shares, unless the preemptive rights have been waived by adopting a special resolution by holders, whether on a show of hands or on a poll, holding not less than three times the number of votes, if any, cast against the resolution. At our 2000 Annual

General Meeting, our shareholders approved a special resolution permitting us to issue up to one million equity shares in connection with acquisitions. We issued virtually all of these equity shares in connection with our acquisitions of India World Communications,

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Indiaplaza.com and Kheladi.com and our investment in CricInfo Limited. At our 2001 Annual General Meeting, our shareholders approved a special resolution permitting us to issue up to four million additional equity shares in connection with acquisitions or capital raising transactions, and our ADS holders are deemed to have waived their preemptive rights with respect to these shares. At our December 2002 Extraordinary General Meeting, our shareholders approved a special resolution permitting us to issue up to 12.5 million additional equity shares in connection with the sale of equity shares to SAIF and Venture Tech, and our ADS holders are deemed to have waived their preemptive rights with respect to these shares. In December 2005 at an extraordinary general meeting, our shareholders waived their preemptive rights with respect to the issuance of 6.7 million shares to Infinity capital.

U.S. holders of ADSs may be unable to exercise preemptive rights for equity shares underlying ADSs unless approval of the Ministry of Finance of the Government of India is obtained and a registration statement under the Securities Act of 1933, as amended, is effective with respect to the rights or an exemption from the registration requirements of the Securities Act is available. Our decision to file a registration statement will depend on the costs and potential liabilities associated with any given registration statement as well as the perceived benefits of enabling the holders of our ADSs to exercise their preemptive rights and any other factors that we deem appropriate to consider at the time the decision must be made. We may elect not to file a registration statement related to preemptive rights otherwise available by law to our shareholders. In the case of future issuance, the new securities may be issued to our depositary, which may sell the securities for the benefit of the holders of the ADSs. The value, if any, our depositary would receive upon the sale of such securities cannot be predicted. To the extent that holders of ADSs are unable to exercise preemptive rights granted in respect of the equity shares represented by their ADSs, their proportional interests in our company would be reduced.

**Holders of ADSs may be restricted in their ability to exercise voting rights and the information provided with respect to shareholder meetings.**

As a holder of ADSs, you generally have the right under the deposit agreement to instruct the depositary bank to exercise the voting rights for the equity shares represented by your ADSs. At our request, the depositary bank will mail to you any notice of shareholders' meeting received from us together with information explaining how to instruct the depositary bank to exercise the voting rights of the securities represented by ADSs. If the depositary bank timely receives voting instructions from a holder of ADSs, it will endeavor to vote the securities represented by the holder's ADSs in accordance with such voting instructions. However, the ability of the depositary bank to carry out voting instructions may be limited by practical and legal limitations and the terms of the securities on deposit. We cannot assure you that you will receive voting materials in time to enable you to return voting instructions to the depositary bank in a timely manner.

Under Indian law, subject to the presence in person at a shareholder meeting of persons holding equity shares representing a quorum, all resolutions proposed to be approved at that meeting are voted on by a show of hands unless a shareholder present in person and holding at least 10% of the total voting power or on which an aggregate sum of not less than Rs.50,000 has been paid-up, at the meeting demands that a poll be taken. Equity shares not represented in person at the meeting, including equity shares underlying ADSs for which a holder has provided voting instructions to the depositary bank, are not counted in a vote by show of hands. As a result, only in the event that a shareholder present at the meeting demands that a poll be taken will the votes of ADS holders be counted. Securities for which no voting instructions have been received will not be voted on a poll.

As a foreign private issuer, we are not subject to the SEC's proxy rules, which regulate the form and content of solicitations by United States-based issuers of proxies from their shareholders. To date, our practice has been to provide advance notice to our ADS holders of all shareholder meetings and to solicit their vote on such matters through the depositary, and we expect to continue this practice. The form of notice and proxy statement that we have been using does not include all of the information that would be provided under the SEC's proxy rules.

**The market price of our ADSs has been and may continue to be highly volatile.**

The market price of our ADSs has fluctuated widely and may continue to do so. Many factors could cause the market price of our ADSs to rise and fall. Some of these factors include:

- perception of the level of political and economic stability in India;

actual or anticipated variations in our quarterly operating results;

announcement of technological innovations;

conditions or trends in the corporate network/data services, Internet and electronic commerce industries;

the competitive and pricing environment for corporate network/data services and Internet access services in India and the related cost and availability of bandwidth;

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the perceived attractiveness of investment in Indian companies;

acquisitions and alliances by us or others in the industry;

changes in estimates of our performance or recommendations by financial analysts;

market conditions in the industry and the economy as a whole;

introduction of new services by us or our competitors;

changes in the market valuations of other Internet service companies;

announcements by us or our competitors of significant acquisitions, strategic partnerships, joint ventures or capital commitments;

our failure to integrate successfully our operations with those of any acquired companies;

additions or departures of key personnel; and

other events or factors, many of which are beyond our control.

The financial markets in the United States and other countries have experienced significant price and volume fluctuations, and the market prices of technology companies, particularly Internet-related companies, have been and continue to be extremely volatile with negative sentiment prevailing. Volatility in the price of our ADSs may be caused by factors outside of our control and may be unrelated or disproportionate to our operating results. In the past, following periods of volatility in the market price of a public company's securities, securities class action litigation has often been instituted against that company. Such litigation could result in substantial costs and a diversion of our management's attention and resources.

**We may not be able to maintain our Nasdaq National Market listing.**

In order to maintain the listing of our ADSs on the Nasdaq National Market, we are required to comply with, or obtain an exemption from, the continuing listing requirements of Nasdaq, including the \$1.00 minimum bid price requirement. In fiscal 2003, the price of our ADSs on the Nasdaq National Market closed below \$1.00 for more than 30 consecutive days. Effective September 24, 2002, our equity share-to-ADS exchange ratio was adjusted to one-to-one in order to reestablish compliance with Nasdaq's minimum bid price requirement. There are also material changes to the listing requirements of the Nasdaq National Market relating to implementation of the Sarbanes-Oxley Act of 2002 and other reforms that have been or will be implemented. These requirements have and will continue to impose significant additional substantive and administrative requirements on all public companies listed on the Nasdaq National Market, including foreign private issuers. We do not know whether we will be able to maintain our Nasdaq National Market listing in the future.

**An active or liquid market for the ADSs is not assured.**

We cannot predict the extent to which an active, liquid public trading market for our ADSs will continue to exist. Active, liquid trading markets generally result in lower price volatility and more efficient execution of buy and sell orders for investors. Liquidity of a securities market is often a function of the volume of the underlying shares that are publicly held by unrelated parties. Although ADS holders are entitled to withdraw the equity shares underlying the ADSs from the depository at any time, there is no public market for our equity shares in India or the United States.

**The future sales of securities by our company or existing shareholders may reduce the price of our ADSs.**

Infinity Capital holds approximately 42% of our outstanding equity capital. Any significant sales of our equity shares or ADSs or a perception that such sales may occur might reduce the price of our ADSs and make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate. We may issue additional equity shares to raise capital and to fund acquisitions and investments, and the parties to any such future

transactions could also decide to sell them.

**Forward-looking statements contained in this report may not be realized.**

This report contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of the risks faced by us described above and elsewhere in this report. We do not intend to update any of the forward-looking statements after the date of this report to conform such statements to actual results.

**Table of Contents*****Risks Related to Investments in Indian Companies***

We are incorporated in India, and a significant majority of our assets and employees are located in India. Consequently, our financial performance and the market price of our ADSs will be affected by changes in exchange rates and controls, interest rates, Government of India policies, including taxation policies, as well as political, social and economic developments affecting India.

**Political instability in India and around the world could halt or delay the liberalization of the Indian economy and adversely affect business and economic conditions in India generally and our business in particular.**

During the past decade, the Government of India has pursued policies of economic liberalization, including significantly relaxing restrictions on the private sector. Nevertheless, the role of the Indian central and state governments in the Indian economy as producers, consumers and regulators has remained significant. The Government of India has changed six times since 1996, including most recently in May 2004. The rate of economic liberalization, specific laws and policies affecting technology companies, foreign investment, currency exchange rates and other matters affecting investment in our securities could also change. A significant change in India's economic liberalization and deregulation policies could adversely affect business and economic conditions in India generally and our business in particular.

**Conflicts in South Asia and terrorist attacks in the United States, South Asia and around the world could adversely affect the economy and cause our business to suffer.**

South Asia has from time to time experienced instances of civil unrest and hostilities among neighboring countries, including between India and Pakistan. In April 1999, India and Pakistan conducted long-range missile tests. Since May 1999, military confrontations between India and Pakistan have occurred in the Himalayan region of Kargil and other border areas. In October 1999, the leadership of Pakistan changed as a result of a coup led by the military. In September 2001, terrorist attacks were conducted in the United States, which caused various adverse consequences, including adverse economic consequences. In addition, in October 2001 the United States commenced military operations against targets located in Afghanistan. In December 2001, terrorist attacks were conducted on the Indian Parliament building resulting in heightened diplomatic and military tension between India and Pakistan. In 2003 and continuing through 2006, the United States and several other countries have conducted military operations against targets in Iraq. Events of this nature could influence the Indian and/or global economy and could have a material adverse effect on the market for securities of Indian companies, including our ADSs, and the market for our services.

**We are subject to foreign investment restrictions under Indian law that limit our ability to attract foreign investors which, together with the lack of a public market for our equity shares, may adversely impact the value of our ADSs.**

Currently, there is no public trading market for our equity shares in India or elsewhere nor can we assure you that we will take steps to develop one. Our equity securities are only traded on Nasdaq through the ADSs as described in this report. Under prior Indian laws and regulations, our depository could not accept deposits of outstanding equity shares and issue ADRs evidencing ADSs representing such equity shares without prior approval of the Government of India. The Reserve Bank of India has announced fungibility regulations permitting, under limited circumstances, the conversion of ADSs to equity shares and the reconversion of equity shares to ADSs provided that the actual number of ADSs outstanding after such reconversion is not greater than the original number of ADSs outstanding. If you elect to surrender your ADSs and receive equity shares, you will not be able to trade those equity shares on any securities market and, under present law, likely will not be permitted to reconvert those equity shares to ADSs.

If in the future a market for our equity shares is established in India or another market outside of the United States, those shares may trade at a discount or premium to the ADSs. Under current Indian regulations and practice, the approval of the Reserve Bank of India is required for the sale of equity shares underlying ADSs by a non-resident of India to a resident of India as well as for renunciation of rights to a resident of India, unless the sale of equity shares underlying the ADSs is through a recognized stock exchange or in connection with the offer made under the regulations regarding takeovers. Since exchange controls still exist in India, the Reserve Bank of India will approve the price at which the equity shares are transferred based on a specified formula, and a higher price per share may not be permitted. Holders who seek to convert the rupee proceeds from a sale of equity shares in India into foreign currency and repatriate that foreign currency from India will have to obtain Reserve Bank of India approval for each

transaction. We cannot assure you that any required approval from the Reserve Bank of India or any other government agency can be obtained.

**Because we operate our business in India, exchange rate fluctuations may affect the value of our ADSs independent of our operating results.**

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The exchange rate between the rupee and the U.S. dollar has changed substantially in recent years and may fluctuate substantially in the future. Historically, the value of the rupee has declined against the U.S. dollar, although the rupee appreciated against the dollar in late 2003 and 2004. In fiscal 2005, the rupee depreciated in the first six months and thereafter appreciated considerably. Depreciation of the rupee will result in higher expenses to our company for the purchase of capital equipment, such as servers, routers, modems and other telecommunications and computer equipment, which is generally manufactured in the U.S. In addition, our market valuation could be materially adversely affected by the devaluation of the rupee if U.S. investors analyze our value based on the U.S. dollar equivalent of our financial condition and results of operations. Appreciation of the rupee against the U.S. dollar will result in foreign exchange losses to the extent we hold excess cash in U.S. dollar-denominated investments.

**The Government of India may change its regulation of our business or the terms of our license to provide Internet access services, VoIP and VPN services without our consent, and any such change could decrease our revenues and/or increase our costs, which would adversely affect our operating results.**

Our business is subject to government regulation under Indian law and to significant restrictions under our Internet service provider license issued by the Government of India. These regulations and restrictions include the following:

Our Internet service provider license has a term of 15 years and was originally issued in 1998. Our Internet service provider license was reissued in 2002 enabling us to offer telephony services over the Internet. We have no assurance that the license will be renewed in the future. If we are unable to renew our Internet service provider license for any reason, we will be unable to operate as an Internet service provider in India and will lose one of our primary sources of revenue.

In December 2004, the Government of India issued licensing guidelines to offer VPN services by ISPs. Consequently, we applied for the license, and the Government of India issued a letter of intent to our company on December 30, 2004 for amendment of our existing ISP license to include provision of VPN services. In January 2005, we paid Rs.100 million as a one-time entry fee and submitted a financial bank guarantee of Rs.10 million as required by the letter of intent.

On January 11, 2005, we received provisional permission from the DOT, to offer VPN service in accordance with the new guidelines. Final permission to offer VPN service will be effective only after we sign the amendment to the license agreement. However, the provisional permission does not carry any terms and conditions relating to the license.

The DOT also required the ISP licensees to pay an annual fee of 8% of the adjusted gross revenues generated under the ISP license.

The Internet Service Provider Association of India, or ISPAI, had filed an appeal against this license with the Telecom Disputes Settlement and Arbitration Tribunal, or TDSAT. TDSAT directed the Government of India to consult with TRAI before finalizing the license conditions.

Pending a revised guideline from DOT, we had reserved Rs.24.6 million towards the 8% annual fee on VPN revenue as per the provisional IP VPN license for the period April 1, 2005 to December 31, 2005 and Rs.12.7 million for the period January 1, 2006 to March 31, 2006 towards the 6% annual fee on adjusted gross revenue, or AGR, as per the ILD/NLD license requirement and Rs.5.6 million for the year ended March 31, 2005 towards the annual license fee.

In December 2005, DOT issued new guidelines for NLD/ILD licenses, which did away with the VPN license and permitted existing provisional VPN license holders to migrate to NLD/ILD licenses. The license fee payable is adjustable from the license fee paid for VPN license and the



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NLD/ILD licenses attracts an annual fee of 6% on AGR generated by the business carried out under this license effective January 1, 2006. DOT has further imposed 6% on AGR on VoIP services, due to ambiguity in the definition of AGR we have, in reliance upon the advice of our counsel, provided Rs. 5.3 million pursuant thereto. We are yet to receive the NLD/ILD licenses.

The Government of India maintains the right to take over our entire operations or revoke, terminate or suspend our license for national security and similar reasons without compensation to us. If the Government of India were to take any of these actions, we would be prevented from conducting all or part of our business.

In view of the increasing concerns and instances of cyber threats and attacks, the government may ask the telecom licensees (including the ISPs) to provide monitoring facility at the licensee's costs across its network as well as may ask for capture and retention of data in terms of traffic flow, usage details, etc. These may significantly increase the costs and result in lesser usage due to perceived violation of privacy by customers.

A network service provider acting as an intermediary is liable for third-party misuse / crimes under the Section 79 of the Information Technology Act, 2000 unless it can establish that it had no knowledge or that it had undertaken due diligence. While an expert committee has recommended that this clause be modified and the network service provider be made liable only if there is a direct role, as per the current stipulation a company may be held liable for any third party misuse.

There have been recent queries from certain government offices whether use of Session Initiation Protocol, or SIP, terminal to make calls to phones abroad is permissible within the ISP license. While we believe that it is permissible as the SIP terminal is a computer defined in the Information Technology Act, 2000. In case this view is not sustained, we may have to make significant investment in the SIP terminals to make it a PC-equivalent. This may entail substantial capital expenditure.

**Changes in Indian income taxes will increase our tax liability and decrease any profits we might have in the future.**

The statutory corporate income tax rate in India was 35.0% during fiscal 2005 and was subject to a 2.5% surcharge and 2% education cess, resulting in an effective tax rate of 36.6%. For fiscal year 2006, the corporate income tax rate has been reduced to 30%, subject to a surcharge of 10% and education cess of 2%, resulting in an effective tax rate of 33.7%. We cannot assure you that the surcharge will be in effect for a limited period of time or that additional surcharges will not be implemented by the Government of India. The Finance Minister of India had introduced a fringe benefits tax, or FBT, that would be levied on employers. Under this FBT, employers would be required to pay a tax of 30% exclusive of applicable surcharge and cess on the taxable value of the fringe benefits or privileges that are provided or deemed to be provided to employees on a collective, rather than individual, basis. The impact of FBT for the fiscal year ended March 31, 2006 was Rs 21 million included under selling and administration expenses.

***Risks Related to the Internet Market in India***

Our success will depend in large part on the increased use of the Internet by consumers and businesses in India. However, our ability to exploit the Internet service provider and other data service markets in India is inhibited by a number of factors. If India's limited Internet usage does not grow substantially, our business may not succeed.

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**The success of our business depends on the acceptance of the Internet in India, which may be slowed or halted by high bandwidth costs and other technical obstacles in India.**

Bandwidth, the measurement of the volume of data capable of being transported in a communications system in a given amount of time, remains very expensive in India, especially when compared to bandwidth costs in the United States. Bandwidth rates are commonly expressed in terms of Kbps (kilobytes per second, or thousands of bits of data per second) or Mbps (megabytes per second, or millions of bits of data per second). Although prices for bandwidth in India have declined recently, they are high due to, among other things, capacity constraints and lack of competition.

**The limited installed personal computer base in India limits our pool of potential customers and restricts the amount of revenues that our Internet access services division may generate.**

The market penetration rates of personal computers and online access in India are far lower than such rates in the United States. Alternate methods of obtaining access to the Internet, such as through set-top boxes for televisions, are currently not popular in India. There can be no assurance that the number or penetration rate of personal computers in India will increase rapidly or at all or that alternate means of accessing the Internet will develop and become widely available in India. While the personal computer penetration level in India is relatively low, we are addressing the demand for public Internet access through the establishment of a retail chain of public Internet access centers, which we refer to as cybercafés, under the *ipay* brand name. As of March 31, 2006, 3,273 *ipay* cybercafés were franchised and 33 *ipay* cybercafés were owned and operated by our company. Although this service creates a larger market, it also imposes on the operator of the cybercafé the considerable costs of providing the consumer access to a personal computer and related hardware and software.

**The high cost of accessing the Internet in India limits our pool of potential customers and restricts the amount of revenues that our Internet access services division might generate.**

The growth of our consumer services is limited by the cost to Indian consumers of obtaining the hardware, software and communications links necessary to connect to the Internet in India. If the costs required to access the Internet do not significantly decrease, most of India's population will not be able to afford to use our services. The failure of a significant number of additional Indian consumers to obtain affordable access to the Internet would make it very difficult to execute our business plan.

**The success of our business depends on the acceptance and growth of electronic commerce in India, which is uncertain, and, to a large extent, beyond our control.**

Many of our existing and proposed services are designed to facilitate electronic commerce in India, although there is relatively little electronic commerce currently being conducted in India. Demand and market acceptance for these services by businesses and consumers, therefore, are highly uncertain. Many Indian businesses have deferred purchasing Internet access and deploying electronic commerce initiatives for a number of reasons, including the existence or perception of, among other things:

inconsistent quality of service;

the need to deal with multiple and frequently incompatible vendors;

inadequate legal infrastructure relating to electronic commerce in India;

a lack of security of commercial data, such as credit card numbers; and

low number of Indian companies accepting credit card numbers over the Internet.

If usage of the Internet in India does not increase substantially and the legal infrastructure and network infrastructure in India are not developed further, we are not likely to realize any benefits from our investment in the development of electronic commerce services.

***Risks Related to the Internet***

**We may be liable to third parties for information retrieved from the Internet.**

Because users of our Internet service provider service and visitors to our websites may distribute our content to others, third parties may sue us for defamation, negligence, copyright or trademark infringement, personal injury or other

matters. We could also become liable if confidential information is disclosed inappropriately. These types of claims have been brought, sometimes successfully, against online services in the United States and Europe. Others could also sue us for

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the content and services that are accessible from our websites through links to other websites or through content and materials that may be posted by our users in chat rooms or bulletin boards. We do not carry insurance to protect us against these types of claims, and there is no precedent on Internet service provider liability under Indian law. Further, our business is based on establishing our network as a trustworthy and dependable provider of information and services. Allegations of impropriety, even if unfounded, could damage our reputation, disrupt our ongoing business, distract our management and employees, reduce our revenues and increase our expenses.

**The success of our strategy depends on our ability to keep pace with technological changes.**

Our future success depends, in part, upon our ability to use leading technologies effectively, to continue to develop our technical expertise, to enhance our existing services and to develop or otherwise acquire new services that meet changing customer requirements. The markets for our service are characterized by rapidly changing technology, evolving industry standards, emerging competition and frequent new service introductions. We may not successfully identify new opportunities and develop and bring new services to market in a timely manner.

**Our business may not be compatible with delivery methods of Internet access services developed in the future.**

We face the risk that fundamental changes may occur in the delivery of Internet access services. Currently, Internet services are accessed primarily by computers and are delivered by modems using telephone lines. As the Internet becomes accessible by cellular telephones, personal data assistants, television set-top boxes and other consumer electronic devices, and becomes deliverable through other means involving digital subscriber lines, coaxial cable or wireless transmission mediums, we will have to develop new technology or modify our existing technology to accommodate these developments. Our pursuit of these technological advances, whether directly through internal development or by third-party license, may require substantial time and expense. We may be unable to adapt our Internet service business to alternate delivery means and new technologies may not be available to us at all.

**Our service offerings may not be compatible with industry standards developed in the future.**

Our ability to compete successfully depends upon the continued compatibility and inter-operability of our services with products and architectures offered by various vendors. Although we intend to support emerging standards in the market for Internet access, industry standards may not be established and, if they become established, we may not be able to conform to these new standards in a timely fashion or maintain a competitive position in the market. The announcement or introduction of new services by us or our competitors and any change in industry standards could cause customers to deter or cancel purchases of existing services.

**Item 4. Information on the Company****History and Development**

Our company, Sify Limited (formerly known as Satyam Infoway Limited), was organized as a limited liability company under the laws of the Republic of India pursuant to the provisions of the Indian Companies Act on December 12, 1995. Until December 2002, we were a majority-owned subsidiary of Satyam Computer Services, a leading Indian information technology services company traded on the New York Stock Exchange and the principal Indian stock exchanges. Our company was formed as a separate business unit of Satyam Computer Services to develop and offer connectivity-based corporate services allowing businesses in India to exchange information, communicate and transact business electronically. We conduct substantially all of our business in India. Our subsidiaries include Sify Communications Limited (formerly Safescrypt Limited), Indiaworld Communications Limited, Sify International Inc. and Sify Networks Private Limited. The address of our principal executive office is Tidel Park, 2nd Floor, No. 4, Canal Bank Road, Taramani, Chennai 600 113 India, and our telephone number is (91) 44-2254-0770.

From December 1995 through 1997, we focused on the development and testing of our private data network. In 1997, we began forming strategic partnerships with a number of leading technology and electronic commerce companies, including UUNet Technologies, in order to broaden our service offerings to our corporate customers. In March 1998, we obtained network certification for conformity with Indian and international network operating standards from the Technical Evaluation Committee of India. In April 1998, we began offering private network services to businesses in India. Our initial services included electronic data interchange, e-mail and other messaging services, virtual private networks and related customer support.

In October 1998, we initiated our online content offerings with two websites: [carnaticmusic.com](http://carnaticmusic.com) and [indiaupdate.com](http://indiaupdate.com). We also started development of [www.sify.com](http://www.sify.com), our online portal, and other related content sites for personal finance, movies and automobiles with the goal of offering a comprehensive suite of websites offering content specifically tailored to Indian interests worldwide.

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On November 6, 1998, the Indian government opened the Internet service provider market place to private competition. Capitalizing on our existing private data network, we launched our Internet service provider business, *SifyOnline* (formerly known as *SatyamOnline*), on November 22, 1998 and became the first private national Internet service provider in India. We began offering *SifyOnline* Internet access and related services to India's consumer market as a complement to the network services offered to our business customers. Our *SifyOnline* service was the first in India to offer ready-to-use CD-ROMs enabling online registration and immediate usage.

In March 2000, we launched our network of public Internet cafés called *iways* to cater to the needs of Indians who do not have access to the Internet. In September 2000, we commenced our hosting services from our Tier-I data center at Vashi, Mumbai to provide colocation and managed services to our clients. In June 2001, we obtained permission to provide wireless connectivity on the 5.7 GHz spectrum from the Wireless Planning Commission. This enabled us to convert all our *iways* from Integrated Services Digital Network, or ISDN, connectivity on the last mile to wireless connectivity. This technology also enabled us to commence our high-speed/broadband access to homes, which began in March 2003. To enable quicker access to homes, we developed a model of partnering with Cable Television Operators, or CTOs, who already interface with households for providing cable television facilities to millions of households in India.

In April 2002, ISPs were permitted to provide restricted VoIP limited to outbound calls to International destinations and personal computer to personal computer calls in India. We started providing this service through our network of cybercafés, and later on through VoIP booths located in large commercial areas and corporate office complexes across major cities in India.

From the time we launched our corporate services in 1997, we have constantly upgraded our technology to provide data services to corporate clients. We were the first Internet service provider in India to make our entire network IP-based and subsequently Multi Protocol Label Switching (MPLS)-enabled, which permitted us to continue to grow our corporate customer base. As of March 31, 2006, we provide data connectivity services to more than 1,200 corporate clients in industries ranging from information technology, manufacturing, banking and financial services industry, pharmaceuticals, retail distribution and the government.

*Initial Public Offering and Subsequent Financing Transactions*

In October 1999, we completed our initial public offering on the Nasdaq National Market and issued 4,801,250 ADSs at a price of \$18.00 per ADS. We received approximately \$79.2 million, net of underwriting discounts, commissions and other offering costs. In connection with our initial public offering, we received the benefit of exemptions from the Nasdaq corporate governance rules relating to shareholder meeting quorum, solicitation of proxies and shareholder approval for issue of shares other than in a public offering under Nasdaq Rules 4350(f), 4350(g) and 4350(i)(1)(D), respectively.

In February 2000, we completed a secondary offering and issued 467,175 ADSs at a price of \$320.00 per ADS. We received approximately \$141.2 million, net of underwriting discounts, commissions and other costs.

In October 2002, we agreed to sell an aggregate of 7,558,140 ADSs to SAIF for consideration of \$13.0 million and to sell an aggregate of 2,034,884 equity shares to VentureTech for consideration of \$3.5 million. This transaction was approved by our shareholders at our Extraordinary General Meeting held on December 9, 2002. In December 2002, we completed the sale of the ADSs to SAIF and the sale of 2,034,883 equity shares to VentureTech. In April 2003, we sold an additional 1,017,442 equity shares to VentureTech. In July 2003, we sold an additional 1,017,441 ADSs to an affiliate of Venture Tech.

On November 10, 2005, Infinity Capital Ventures, LP ( *Infinity Capital* ) acquired 11,182,600 ADS of our Company from Satyam Computer Services Limited ( *Satyam* ) for US \$5.60 per share in cash through a Sponsored ADR Programme arranged by the Company. The total purchase price for the Satyam shares was approximately US \$62.6 million.

In a separate transaction, also on November 10, 2005, Infinity Capital entered into a Subscription Agreement with us pursuant to which, upon the terms and subject to the conditions set forth therein, Infinity Capital agreed to purchase from us approximately 6.7 million newly-issued equity shares or ADSs at a purchase price of US \$5.60 per share in cash. The total purchase price for the newly issued shares was approximately US \$ 37.6 million. This transaction was approved by our shareholders at our Extraordinary General Meeting held on December 23, 2005.

Subsequent to the quarter end, in January 2006, we completed the transaction. Also on November 10, 2005, Sify, Infinity Capital and Raju Vagesna entered into a Standstill Agreement pursuant to which, upon the terms and subject to the conditions set forth therein, Infinity Capital agreed not to purchase more than 45% of our fully diluted equity.

In connection with the transactions, Mr. Raju Vagesna of Infinity Capital was appointed as the Chairman of our Board of Directors. We also appointed Mr. P. S. Raju as the second nominee of Infinity Capital to our Board of Directors.

Based on our review of filings made with the SEC, we believe Infinity Capital now owns approximately 42% of our outstanding equity shares.

**Table of Contents***Investment Strategy*

In evaluating investment opportunities, we consider important factors, such as strategic fit, competitive advantage and financial benefit, through a formal net present value evaluation. There is no significant difference in the analysis undertaken in connection with an investment in an affiliate compared to other uses of cash. Our investment strategy has not undergone major changes in the last four years.

*Sify Networks Private Limited (formerly E Alcatraz Consulting Private Limited)*

In March 2004, we acquired E Alcatraz Consulting Private Limited, a company engaged in the business of providing security services to corporate customers, for a consideration of Rs.32.6 million.

**Business Overview**

We are one of the largest integrated Internet, network and electronic commerce services company in India, offering end-to-end solutions with a comprehensive range of services delivered over a common Internet backbone infrastructure. Our services enable our business and consumer customers to communicate, transmit and share information, access online content and conduct business remotely using our private data network or the Internet. Our Internet and network services include the following:

*Corporate Network/Data Services.* We offer a suite of technology and network-based services that provide our corporate customers with comprehensive Internet and private network access. Our services enable our corporate customers to offer a full range of business-to-business and electronic commerce related services.

*Internet Access Services.* We offer dial-up Internet access, e-mail and web page hosting to consumers in India through convenient online registration and user-friendly software. In addition, we offer public Internet access to consumers through a retail chain of *iway* cybercafés. We also have tie-ups with certain cable television operators through which we offer Internet access through cable. As of March 31, 2006, we had approximately 890,000 retail Internet access subscribers.

*Online Portal Services.* We operate online portals, such as [www.sify.com](http://www.sify.com), [www.samachar.com](http://www.samachar.com) and [www.sifymax.in](http://www.sifymax.in), that function as principal entry points and gateway for accessing the Internet by providing useful web-related services and links. We also offer related content sites specifically tailored to Indian interests worldwide.

*Other.* We facilitate web based learning for various organizations by digitizing and uploading content to facilitate the same .

We began providing corporate network/data services to businesses in April 1998, and as of March 31, 2006 we had more than 1,200 corporate customers. We launched our Internet service provider business in November 1998, becoming the first private Internet service provider to begin service after the Indian government opened the market to private competition. We also operate online portals, [www.sify.com](http://www.sify.com), [www.sifymax.in](http://www.sifymax.in), [www.samachar.com](http://www.samachar.com), and related content sites specifically tailored for Indian interests worldwide. *Sify.com* is one of India's leading portals with services in areas such as news, travel, finance, health and shopping in addition to e-mail, chat and search. *Sifymax* is a broadband portal offering live streaming and on demand video and audio content, news clips, TV reality shows and highlights of cricket matches.

We currently operate a large national private data network in India. Our network utilizes Internet protocol, which is an Internet industry standard for tracking Internet addresses, routing outgoing messages and recognizing incoming messages. In February 2002, we became the first Indian company to be certified ISO 9001:2000 for network services, data center operations and customer relationship management. The ISO 9001:2000 certification from Det Norske Veritas (DNV), Netherlands under the RvA accreditation scheme provides recognition for self-defined benchmarks against international companies with respect to facilities, metrics, processes and practices. In fiscal year 2003, our Enterprise Solutions division was also certified ISO 9001:2000 for provisioning of corporate VPN's, Internet bandwidth, VoIP, and integrated security solutions including pre-sales, sales, order processing and project management.

As of March 31, 2006, we operated 171 points of presence serving more than 250 cities across India, which we believe represents an estimated, 95% of the installed personal computer base in India. Points of presence are telecommunications facilities located in a particular market which allow our customers to connect to the Internet through a local telephone call. Although our Internet service provider license permits us to establish and maintain our own direct connection to the international Internet, we no longer maintain satellite gateways. We intend to provide international bandwidth by leasing capacity of multiple oceanic systems.

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We continue to seek to be the premier integrated Internet, network and electronic commerce solutions provider to businesses and consumers in India. We believe that demand for our services is significant in India and growing rapidly as businesses and consumers seek alternatives to the communications services offered by telecom providers that were formerly controlled by the Government of India. We intend to continue to focus on providing superior network performance and high levels of customer service and technical support to increase our customer base and maximize customer satisfaction.

**Industry Overview**

*Development of the Internet.* We believe that the large and increasing number of home and office computers linked to the Internet, advances in network design, increased availability of Internet-based software and applications, the emergence of useful content and electronic commerce technologies, and convenient, fast and inexpensive Internet access will continue to drive Internet growth and usage in the near future.

*Special Communications Needs of Businesses.* As the Internet becomes more developed and reliable, businesses are increasingly utilizing the Internet for functions critical to their core business strategies, such as sales and marketing, customer service and project coordination. The Internet presents a compelling profit opportunity for businesses by enabling them to reduce operating costs, access valuable information and reach new markets. To maintain a significant presence on the Internet, businesses typically purchase Internet access services and establish a website. Internet access provides a company with its basic gateway to the Internet, allowing it to transfer e-mail, access information and connect with employees, customers and suppliers. A website provides a company with a tangible identity and an interactive presence on the Internet. Many corporations are also converting their legacy information systems and databases to web-enabled systems.

*The Opportunity in India.* As with many developing nations, the telecommunications infrastructure in India had, until recently, been controlled by government-controlled telecom providers. The resulting service remains inferior to service in developed countries. At the same time, however, the Indian economy continues to modernize and expand, particularly in sectors such as software development that are dependent on a reliable communications network. The growth of these industries is leading to an increasing base of personal computers and wired homes and businesses in India with a resulting increased demand for Internet services. We believe these trends, which mirror trends in more mature economies, will continue to develop in India.

The ability to exploit the Internet service provider and other data service markets in India is currently inhibited by bandwidth limitations imposed by cost and technical obstacles. Generally, bandwidth remains very expensive in India however the emergence of private players in the last couple of years and liberalization measures have brought an increase in supply and a consequent downtrend in prices. Ceilings for bandwidth prices are set by the DOT and the TRAI plays the advisory role to the DOT.

We expect the growth in personal computers and Internet users to increase the demand for Internet content directed towards domestic Indian consumers as well as the amount of electronic commerce in India.

Private market participants historically have not been able to exploit the market opportunities in India because the regulatory environment in India largely prevented any competition with the national government-controlled telecom providers. Until November 1998, the only Internet service provider permitted in India was VSNL, which began providing Internet access on August 15, 1995. On November 6, 1998, the government opened the Indian Internet service provider market to private competition and granted Internet service provider licenses. The licensees include cable television operators and joint ventures between local companies and large international telecom providers. Internet service provider licenses are granted for 15 years, with only nominal license fees. Currently, pricing of Internet service is not regulated by the Government of India, although it has the power to do so through policy directives. However, the interconnection charges between service providers are regulated by the TRAI.

**Sify Business Model**

We believe that the growth of the Internet and other network services in India has been inhibited by relatively high costs and poor user experiences caused by an inadequate telecommunications infrastructure and slow network connection speeds. We are committed to expanding and enhancing our private network backbone and to providing high quality technical support to attract users to our services. We believe that our services provide our customers with the ability to exchange information, communicate and transact business over the Internet with speed, efficiency,

reliability and security superior to other Internet service providers. Key advantages of the Sify business model include: *End-to-end network solutions for business customers.* We provide our business customers with a comprehensive range of Internet, connectivity, security and consulting, hosting and managed service solutions complemented by a broad base of web-based business applications. Our corporate services range from dial-up and dedicated Internet access, virtual private networks, security, web implementation, electronic commerce solutions and web hosting. Our end-to-end solutions enable our corporate customers to address their networking and data communication needs efficiently without having to assemble products and services from different value-added resellers, Internet service providers and information technology firms.

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*National private Internet protocol network backbone and Wireless delivery on the last mile.* We operate a large national Internet protocol data network in India. As of March 31, 2006, we owned and operated 171 points of presence serving more than 250 cities across India, which we believe represents an estimated 95% of the installed personal computer base in India. Our network provides the platform for the national delivery of Internet access to consumers as well as the backbone for our full range of corporate network/data services. A significant portion of our last mile delivery for corporates, and almost the entire iWay cybercafe network and hi speed / broadband delivery to homes, is on the wireless mode, thereby enabling us to implement and deliver superior services compared to the wireline medium.

*Internet content and electronic commerce websites customized for the Indian market.* We view the Indian market as a series of specific market segments with unique cultural and topical interests, rather than an extension of a homogeneous, worldwide Internet market. We have assembled a team of India-based employees familiar with the local culture, language and business environments in our markets to develop Internet content and electronic commerce websites tailored for the Indian market. We regularly incorporate new and original third-party content suited to our local and regional audiences to enhance our customers online experience and to attract new users both within India and abroad. As a result of our local market knowledge, we have been able to increase traffic flow to our websites and to create brand awareness for our SifyOnline access service.

*Managed Infrastructure services and Managed Security Services.* We have customer engagements in all aspects of infrastructure services, networks security and hosting, with digital certificates based authentication service. We have extensive experience in providing information assurance and compliance certification, following frameworks such as COSO/COBIT and standards such as BS7799 and SAS 70. Our managed infrastructure and security services leverages on our rich experience and skill sets to provide constant value to our customers namely better service levels and reduced costs. We constantly look at ways to efficiently manage customer assets remotely thus providing focused superior service at lower cost.

**Strategy**

Our goal is to become the premier integrated Internet, network and electronic commerce solutions provider to businesses and consumers in India. Our principal business strategies to accomplish this objective are:

*Invest in the continued enhancement and expansion of our network infrastructure to support customer growth, enter new markets and accommodate increased customer usage.* We intend to continue to increase the capacity and geographic reach of our network in order to support subscriber growth, enter new markets and accommodate increased customer usage. We are committed to using proven technologies and equipment and to providing superior network performance. We have deployed asynchronous transfer mode, or ATM, switches on nine points of presence along our network. The rest of our network is based on Internet Protocol, or IP, and we are the first Indian service provider to have made our network Multi Protocol Label Switching (MPLS) compliant. We plan to procure international bandwidth by leasing capacity of multiple oceanic systems. As of March 31, 2006, we had leased one STM 1 from UNSL landing at Mumbai and two Chennai on the Tata Indicom cable, in addition to an STM 1 on the FLAG cable, landing at Mumbai from Reliance. We have also leased multiple links from Bharti on the i2i cable, We have also leased intercity links from multiple suppliers including BSNL, Bharti, Reliance and Power Grid corporation, in such a way that each one of our nodes are accessible from at least two other nodes, if not by two long distance operators. We believe that as the size and capacity of our network infrastructure grows, its large scale and national coverage will create economies of scale.

*Increase penetration in our existing markets by expanding awareness of the Sify brand name to capitalize on our first mover advantage in India.* We intend to capitalize on our first-to-market advantage in India to establish national service and a brand name in advance of other private competitors. As of March 31, 2006, we had approximately 890,000 retail Internet subscribers and 3,307 cybercafés, of which 34 were owned and

3,273 were franchised. Approximately 99% of these *iways* are on broadband, which provides the user with significantly faster access speeds. Our marketing strategy includes print, television and radio advertising, direct mailing campaigns targeting personal computer owners and operating cybercafés. We are also actively promoting our broadband services to homes through cable television operators. As of March 31, 2006, we had tie-ups with more than 1,500 cable television operators across 91 cities. We believe that increased focus on delivery of broadband services by the Government of India, availability of broadband content, reduced cost of personal computers and increased purchasing capacity of the middle class in India will drive this business forward in the future.

*Expand our services with new technologies to enable our customers to use the Internet more effectively. We continually seek to expand the breadth of our service offerings with new technologies. Our cybercafés prominently display the Sify and SifyOnline brands and offer a full range of our Internet connectivity services. We also introduced a number of other services, including VoIP in April 2002, video conferencing, e-mail designed for regional Indian dialects, a user customized portal site and micro-payments.*

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*Provide more value added services by leveraging on the rapid growth of wireless Internet and mobile services in India and strengthen our Internet portal with more content tailored to Indian interests worldwide.* Our portals [www.sify.com](http://www.sify.com) and [www.samachar.com](http://www.samachar.com), function as initial gateways to the Internet, the user's starting point for web browsing and other Internet services, for our consumer Internet service provider subscribers and cybercafé users. Our portals are media rich, user friendly, interactive websites offering hyperlinks to a wide variety of websites and services, including our own websites. Our websites cater to a variety of Indian interests within and outside of India. To achieve our goal of developing the premier Internet portal focused on the Indian market, we intend to continue to expand and improve the quality of [www.sify.com](http://www.sify.com), and are developing additional content oriented towards topical and cultural interests of Indians worldwide.

During the course of 2004-05, we also developed a broadband channel, *Sify Max*, that provides audio visual content to Sify subscribers. We also created a short code 4545 for downloading ringtones and sending SMS to tap the growing mobile user market. To expand our short code product offering, we are also forming business alliances with copyright owners and mobile service providers. In addition, we are forming strategic alliances with several offline media partners to deliver content to our users. As the availability of Internet access expands in India, we believe that increasing numbers of Internet users will be attracted to our high quality websites and online content designed specifically for the Indian consumer. We will seek to attract advertisers, electronic commerce merchants and third-party content providers trying to reach our users in order to generate additional revenues for [sify.com](http://sify.com).

*Expand our customer distribution channels through strategic alliances to take advantage of the sales and marketing capabilities of our strategic partners.* We intend to continue to expand our customer acquisition channels, for both our consumer Internet access and corporate network/data services. We have arrangements with leading personal computer manufacturers to bundle our *SifyOnline* Internet access service with the sale of their personal computers in India.

*Pursue selective strategic investments, alliances and acquisitions to expand our customer base, increase utilization of our network and add new technologies to our service mix.* We believe that our growth can be supplemented by selective acquisitions of complementary businesses. We may seek to expand our market presence in our corporate network business through the acquisition of web hosting, data center, web implementation and/or systems integration companies serving India, the United States or other markets. We will also consider acquisitions of Internet service providers that have a significant or growing customer base in our current or targeted markets.

*Expand into international markets for providing managed network services.* Our network and application level support can be provided remotely with a minimum of on-site presence. We are seeking to provide these services to international markets. The tools utilized to provide these services were developed in-house on Linux/open source platforms, and we plan to upgrade these tools in the future to meet customer requirements. We expect our expertise in network management, to enable us to perform these services to international customers at lower costs. We also intend to provide managed security solutions, including monitoring and vulnerability assessment, in addition to managed firewall and intrusion detection services.

*Superior end-user performance and customer support.* We provide a high level of customer service, network performance and technical support to maximize customer satisfaction. A significant number of our employees are engaged in our customer service or technical support departments, which operate 24-hours-a-day, seven-days-a-week. Our network engineers continually monitor network traffic and congestion points to deliver consistent, high quality network performance. Our backend processes are ISO 9001:2000 compliant for network operations, data center operations and customer care. Our strategy of

providing superior network performance and customer service is designed to result in significant customer growth from referrals and industry recognition.

**Service Offerings**

*Corporate network/data services.* Our corporate network/data services division addresses the network, security and application services needs of Indian enterprises by leveraging our national Tier 1 IP network infrastructure. The services include a comprehensive range of Internet protocol based Virtual Private Network, or IPVPN, offerings, including intranets, extranets and remote access applications to both small and large corporate customers. There is a strong focus on industry verticals such as IT/ITES (IT enabled services), banking and financial services industry (BFSI), government, manufacturing, pharmaceutical and FMCG. We were the first service provider in India to provide MPLS-enabled IPVPN s on its entire

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network. We also have recently entered into a strategic partnership with the Power Grid Corporation of India (PGCIL) to provide enterprise network services to end customers across the country. We provide last mile connectivity in over 150 locations throughout India. Our entire network is MPLS enabled with built in redundancy with world class design and service standards. Frost & Sullivan, in its report on IPVPN service offerings in India, reported that we had emerged as the single largest player in the IPVPN space in India with 42.72% market share. We were also awarded the Frost & Sullivan Market Leadership Award for IPVPNs in India for the years 2003 and 2005.

SecureConnect is our comprehensive offering of secure, reliable and scalable IPVPN solutions that meet both mission-critical data networking and converged voice, video and data connectivity needs. It offers a variety of intranet and extranet configurations for connecting offices, remote sites, traveling employees and business partners, whether in India or abroad. Our platform of services includes:

SiteConnect, which offers site-to-site managed MPLS-enabled IPVPN solutions, ideal for securely connecting regional and large branch offices within India to the corporate Intranet.

GlobalSiteConnect which is an international site-to-site managed MPLS-enabled IPVPN solution, ideal for securely connecting international branch offices to the corporate Intranet. It provides connectivity anywhere in the world through Sify's alliances and partnerships with global overseas service providers such as Global Crossing (GC), Asia Net Com (ANC), and BtNA to name a few.

ExpressConnect, which offers a premium range of high-performance Internet bandwidth solutions for connecting regional offices, branch offices and remote locations to the corporate network. These solutions complement our SiteConnect range of MPLS enabled IPVPN solutions, provide high-speed bandwidth in those situations where basic connectivity and cost are the top concerns

RoamConnect is our national and international remote access VPN, ideal for securely connecting employees, while they are traveling, to the corporate intranet; features single number access to SifyNet from anywhere in the country and provides access from anywhere in the world through Sify's alliances with overseas service providers such as MCI, GRIC, IPASS and Fiberlink.

PartnerConnect is our remote access VPN offering, for providing secure and restricted dial-up access to business partners such as dealers, distributors and suppliers to the corporate extranet.

In February 2002, we became the first Indian company to be certified ISO 9001:2000 for network services, data center operations and customer relationship management. The ISO 9001:2000 certification from Det Norske Veritas (DNV), Netherlands under the RvA accreditation scheme provides recognition for self-defined benchmarks against international companies with respect to facilities, metrics, processes and practices. Our corporate network/data services were also certified 9000:2001 compliant for pre-sales, sales, project management and backend operations in September 2003.

We also offer a suite of security solutions, including security design, audit, procurement and integration. Our enterprise solutions portfolio includes a range of application services, such as enterprise class e-mail platforms, audio and video conferencing solutions and business web services. Contracts for these services are negotiated on an individual basis to provide specifically tailored network/data services to each customer.

*Application Services.* We offer value-added services to organisations such as website design, development, content management, search engine optimisation, hosting and management services, including domain name management, secure socket layer (SSL) certificate for websites, and server space in required operating system and database. We provide state of the art messaging and collaboration services and solutions such as e-mail servers, LAN mail solutions, anti-spam appliances, bulk mail services, instant messaging, and also offer solutions and services to enable data & access security over the Internet. We also offer web-applications such as online merchandising with on-line payment gateways, sales force automation, supply chain management, intranet and extranets, workflow engine and knowledge management systems. We also provide infrastructure-based services on demand, including on-line testing engine and network management. On-line testing services include test management software, required servers

and proctored examination facilities at Sify's *ify* cybercafés. On-line exam engine offered allows a secure and flexible way of conducting examinations involving a wide range of question patterns.

*Security and Assurance Services.* We offer a comprehensive suite of security solutions including security design, procurement and integration services for infrastructure security, vulnerability assessment and penetration testing. Implementation services include implementation of security equipment, such as firewalls, intrusion detection systems, content security, authentication tools and VPN services. We also provide assurance services centered around auditing, risk assessment, policies and procedures, business continuity/disaster recovery planning.

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*Data Centers.* We operate India's first level 3 Internet data centers in Mumbai (Bombay) and Chennai (Madras) designed to act as reliable secure and scalable facilities to host mission-critical applications. We offer co-location services which allow customers to bring in their own rack-mountable servers and house them in shared racks, hire complete racks, and rent secure cages at the hosting facility to meet their application requirements. We also offer a wide variety of managed hosting services, such as storage, back-up and restoration, performance monitoring and reporting hardware and software procurement and configuration, network configuration as well as spares and replacement. The Fort Knox platform for security management of hosted servers offers Service Level Agreement (SLA)-based security services to protect servers. Our Infrastructure Data Management Services (IDMS) service provides specific services related to building data centers, leveraging on our proven expertise to build world-class infrastructure.

*Digital Certification.* In technical collaboration with Verisign, a leading provider of Internet trust services, we have formed a wholly-owned subsidiary, Sify Communications Limited, to provide managed digital certificate-based authentication services in India. Sify Communications Limited is the principal affiliate of Verisign in India and is a member of Verisign's Global Affiliate Network. Sify Communications Limited was accredited as the first Certifying Authority for issuance of Certificate for Digital Signature by the Ministry of Information Technology, Government of India.

*Remote Management Services.* This service provides continuous proactive management and support of customer operating systems, applications and database layers through specialized monitoring tools and infrastructure experts to ensure that our customers' infrastructure is performing optimally.

Our corporate network/data services division accounted for approximately 49.8%, 56.0% and 54% respectively, of our revenues in fiscal years 2004, 2005 and 2006. We believe that corporate services will continue to be the largest part of our business for the immediate future.

*Internet access services.*

Our Internet access services for retail consumers include high-speed/broadband access to homes over cable, public Internet access from our network of *iway* cybercafés, VoIP and dial-up access to homes.

*Public Internet Access.* We provide public Internet access to the large segment of the Indian population that does not own a personal computer through our network of *iway* cybercafés. Sify operates these *iway* cybercafés on a franchisee model. As of March 31, 2006, we had 3,307 *iways* in 153 cities, of which 3,273 cybercafés were franchised and 34 cybercafés were owned and operated by our company. We believe we are the largest branded network of cybercafés in India.

In connection with our franchised *iways*, we grant each franchisee a non-exclusive license to operate the cybercafé using our logo, brand and trade names. We enter into an agreement with the franchisee establishing the rights and obligations of each party. In connection with the establishment of a franchised *iway*, we receive an initial franchise fee that covers the following upfront services rendered by our company:

- conducting a market survey and deciding on the best location for the cybercafé;

- installing the broadband receiver equipment on the roof of the cybercafé and linking it to one of our broadcasting towers;

- obtaining the regulatory approvals for wireless transmission at the allotted frequency range;

- installing the wiring from the receiver unit to the individual personal computers;

- assistance in obtaining facilities, including computers and furnishings; and

- providing an operations manual with instructions and guidelines for running the cybercafé.

The cybercafés are owned and operated by the franchisees. The franchisee procures the retail space, invests in furniture, interior decor, personal computers, point of sale signage and employs/trains the staff. The franchisee is responsible for the maintenance of the premises and interface with customers. We provide the complete back-end

support, including bandwidth, the authentication/usage engine and the billing/collection system. The prices to be charged to the customers and the services that can be rendered are controlled by Sify. On average, these *iways* have about seven personal computers and operate in an area of about 250 square feet. All *iways* operate on a prepaid subscription model, and the end customer has the ability to browse from any of the *iways* using the roaming facility that Sify provides. The billing system allows us the option of charging different prices based on the services used, time of usage and the place of use. More than 99% of these cafés are connected through the wireless mode, on the 5.7 ghz or the 2.4 ghz spectrum, with a subscriber unit placed on the top of the building and connected to an access point in a tower that is within a 5 kilometre radius from this location. We believe the *iways* offer a superior browsing experience compared to other cybercafés that operate on either a leased line or an ISDN facility. Today, *iways* are being used for a multitude of services including VoIP, video conferencing, online examination centres, online games and also as e-distribution points.

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*Voice Over Internet Protocol.* VoIP can be used in India for making International calls. We have leveraged on our extensive network of *iways* to offer VoIP. As of March 31, 2006, more than 2,500 of the *iways* had the capability to provide VoIP. We have also started providing these services through standalone VoIP booths at various strategic locations (1063 of them) in major cities. We offer the ability of making international calls to more than 165 countries, and have partnered with a few international carriers for carrying the traffic. These services are offered at prices that are up to 70% lower than those offered by the International long distance operators, and therefore provide a distinct value advantage to the end user. We use MPLS enabled technology that ensures voice clarity. Based on statistics provided by the various ISPs to TRAI, we had more than 30% share of the Internet telephony market for the year ended March 31, 2006.

*Broadband/high-speed Internet Access.* Over the last two years, we have increasingly focused on various modes of delivering high-speed Internet service, to provide a superior browsing experience to the end customer than what he could experience from traditional dial-up access. The availability of wireless connectivity enabled us to overcome the hurdles associated with the last mile access in India. Initially, we focussed on providing high-speed service to large apartment complexes in the major cities, especially in Mumbai and Delhi, and subsequently moved to partnerships with the cable television operators, or CTOs, through a combination of wireless and wireline delivery. In India, we estimate there are more than 40,000 CTOs that provide cable access to more than 60 million households across the country.

Each CTO has a well-defined area in which it operates. By leveraging on this existing network of CTOs that are close to the household, we could reach out to the target market more easily, while ensuring that our Internet service was branded separately and distinctly from the cable TV business of the CTO. The service is delivered to homes using a unique combination of wireless and cable. While the subscriber unit at the CTO premises is connected to the Sify base station on the wireless mode, the individual subscriber is connected using optical fibre that is laid by the CTO across its area of operation. We believe we are a leader in this medium of broadband delivery to homes. We collect an initial charge for installing the Ethernet card in a customer's personal computer and for laying the initial cable infrastructure that includes the optical cable backbone, the switches and hubs that are required for the connection. We offer these services through three types of service plans - hourly, unlimited and download-based - to suit various requirements of individual users.

*Dial-up access.* This was our first retail offering after the Internet service market was deregulated in India in November 1998. We offer dial-up Internet access through convenient online registration and user-friendly software. Dial-up Internet access is sold to customers either for a specified number of hours or for an unlimited usage within a specified period of time. Our unlimited usage service allows a user up to six hours of Internet access per day. This business has been under increasing pressure from incumbent telecom operators who subsidize their Internet service offering by bundling Internet services with basic telephony services. We have, however, tried to differentiate our service to our subscribers by offering better and a more extensive range of services, with an emphasis on ease of use. Our online registration process is available to initiate service and purchase renewals. We also support our subscribers with a 24-hour-a-day, seven-day-a-week call center staffed with trained technicians. Subscribers can access a single number for customer service and technical support. Subscribers can also e-mail their questions directly to a customer service and technical support center at our company.

We expect the market for consumer Internet access to remain highly price competitive. This would be especially true of the high-speed and broadband services which are the focus of attention of both the government and our competitors. The incumbent government owned telephone companies, BSNL and MTNL, along with the large private sector telephone companies, including Bharti, Tata Internet and Reliance, are focused on growing the broadband market in India, using DSL and cable as the medium of delivery. Contemporaneously, the government is trying to encourage growth by reducing the ceiling on the prices that can be charged for both international and domestic bandwidth.

Our Internet access services division accounted for approximately 38.9%, 38.9% and 38.8%, of our revenues in fiscal years 2004, 2005 and 2006.

*Online Portal Services.*

We operate online portals, including India's first broadband content portal, [www.sifymax.in](http://www.sifymax.in), and a group of websites under [www.sify.com](http://www.sify.com) and an NRI portal, [www.samachar.com](http://www.samachar.com), that function as principal entry points and gateways for accessing the Internet by providing useful web-related services and links. We also offer related content sites specifically tailored to Indian interests worldwide in five local Indian languages. Our portal sites, [www.sifymax.in](http://www.sifymax.in) and [sify.com](http://sify.com), are designed to be the initial launch screen for all of our SifyOnline customers and iway users

SifyMax.in provides live streaming and on demand video and audio content in 17 categories, including films and music, general entertainment, lifestyle, TV reality shows, podcasts, video blogs, business, sports and national news. Sify Max streams video content live (24 X 7) from TV channels like CNN-IBN & CNBC and hosts 15 radio stations offering Bollywood hits, latest chart-busters, Indipop and international in multiple languages. Sify Max has also been the official Internet partner of India's most popular reality shows. Sify Max is a pioneer in live video streaming, having webcast Indian budget 2006, Mumbai Marathon, Lakme Fashion Week, the India Today Conclave and cricket matches.

Sify.com provides a gateway to the Internet by offering communication and search tools such as email, messaging, chat, blogs, e-greetings and search engine to classifieds, jobs, travel, online portfolio management and channels for personal finance, astrology, lifestyle, shopping, movies, sports and news. It has been designed to address a wide audience, incorporating world class design and usability. The finance portal [www.walletwatch.com](http://www.walletwatch.com) covers the entire spectrum of equity markets, business news, insurance, mutual funds, loans and a host of paid and free financial services. The community channels of Sify include discussions, dlogs and groups.

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Today, there are probably more non-resident Indians, or NRIs, than Indians residing domestically who have access to the Internet. To address this market, [www.samachar.com](http://www.samachar.com) has been designed to address the need for NRIs to stay connected with India. This portal provides a range of news in English and five Indian languages, entertainment and services, including money transfer and gifting, that help over 1.5 million NRIs. We also launched our NRI Finance site to cater to increasing financial needs of the NRI community.

Sifymall.in, the online shopping mall, stocks products from India's leading brands. It offers competitive prices and a secure and convenient method of purchase. Users can buy using their credit or debit card, pay cash on delivery or send a check.

Sify Mobile was launched during the year 2004 with 4545 as its short code. Its focus has been on providing relevant regional content to cater to the burgeoning number of mobile users in India. The range of services includes downloadable ring tones, wallpapers, news, cricket scores and a variety of other interactive services.

In fiscal years 2004, 2005 and 2006, our online portal services division accounted for approximately 3.0%, 2.9% and 3.8%, respectively, of our total revenues. The decrease in our online portal and content offerings division's revenues as a percentage of total revenues from fiscal year 2004 to fiscal year 2005 was due to a decrease in advertising revenues as a result of decreasing advertising expenditures by our customers, combined with lower advertising rates. However, a diversified service offering and increased sponsorship and advertising revenues on Sify Max reversed this trend in 2006.

**Strategic Vendor Partnerships**

We maintain a number of strategic relationships with key vendors of Internet-related hardware, software and services. Some of these relationships are exclusive to us in India, subject in some cases to minimum sales thresholds. These relationships result in two significant benefits. First, they provide us with the ability to offer valuable services to our customers in India. In addition, these relationships help us market our services by providing us with access to our partners' customer bases. Our network and related services are focused on meeting the needs of corporate customers, particularly in manufacturing and service organizations, which have a need to coordinate their activities with satellite operations such as dealers, distributors, agents and suppliers. For additional information regarding our relationships with these companies, please see Item 10. Additional Information Material Contracts.

**Corporate Customers**

We have established a diversified base of corporate customers in a variety of data intensive industries, including information technology enabled services (ITES), banking financial services and insurance (BFSI), publishing, retail, pharmaceuticals and manufacturing. Our corporate customer base has grown to over 1,200 customers. Based on fiscal year 2006 revenues generated by our corporate network/data services division, our ten largest corporate customers were GE Capital Services India, Global Crossing, The Oriental Insurance Company Limited, Ernst & Young, Sigma Distributors (P) Limited, Satyam Computer Services, Oracle Software India Limited, Bharti Infotel, Wipro Spectramind Services, and Hutchison Max Telecom. No single customer accounted for more than 10% of our revenues in fiscal year 2006. The increased scope of the services we offer, particularly the provision of broadband services to our existing customers and International IPVPN services along with the increased reach of our network, has increased our market base.

**Customer Service and Technical Support**

We believe that excellent customer support is critical to our success in attracting and retaining subscribers. We currently provide customer service and technical support via a local telephone call in most of the cities in which we have a point of presence. Our web-based help desk and MIS system provide online information to our clients. Subscribers can also e-mail their questions directly to a customer service and technical support address at our company. Our customer service and technical support staff handles all questions regarding a subscriber's account and the provision of our services and is available 24-hours-a-day, seven-days-a-week.

**Sales and Marketing**

*Corporate Offerings.* The principal focus of our sales and marketing staff is existing and potential corporate customers. We seek to penetrate this market through trade publication ads, industry trade shows and seminars for the benefit of industry associations and potential customers. As of March 31, 2006, we had 253 employees dedicated to sales and marketing exclusively for our corporate offerings.



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*Consumer Offerings.* A key element of our business strategy is to increase our brand awareness and market penetration among consumers through a number of means including an expanded advertising campaign focused primarily on print advertising, direct mail and free software to consumers who become subscribers.

In addition, we intend to continue to operate cybercafés under the *ify* brand name, and to enter into relationships with independent cybercafés to co-brand our websites with their businesses, in order to expand access to our portal and websites by consumers who do not own a personal computer or have Internet access at home. To increase Internet access and use of our websites by personal computer buyers, we have entered into arrangements with a leading personal computer manufacturers to have our Internet access software bundled with their computers sold in India.

**Technology and Network Infrastructure**

We operate a national Internet protocol private data network with 171 points of presence serving more than 250 cities and towns across India, which we believe represents an estimated 95% of the installed personal computer base in India. A point of presence is commonly defined as the ability to access online services in a market through a local telephone call or local leased lines. We operate our network facilities and customer service operations, which gives us greater control over the utilization and quality of our network. We have designed and built our network using advanced technologies and equipment which allows us to continue to expand the geographic range of our network, integrate improved data processing technologies and enhance speed and capacity with little or no disruption to our customers.

*Geographic Coverage.* Through our national network of points of presence, our business and consumer Internet access customers are able to access the Internet in 171 of the largest markets in India via a local phone call on dial-up or through our cybercafé chain or local leased lines. We have backbone points of presence, or POPs, in Ahmedabad, Bangalore, Bhopal, Kolkata (Calcutta), Chennai (Madras), Kochi (Cochin), Chandigarh, Delhi, Hyderabad, Lucknow, Mumbai (Bombay) and Pune. These backbone points of presence, or primary nodes, reside at the core of a larger Internet protocol network with a partially meshed topology architecture. We have additional points of presence, or secondary nodes/base stations, in 161 other towns and cities. Each point of presence contains data communications equipment housed in a secure facility owned, leased or operated on an infrastructure co-location basis by our company located near a Bharat Sanchar Nigam Limited (BSNL), Mahanagar Telephone Nigam Limited (MTNL) or private basic service operator (BSO) telephone switching station. Most points of presence contain a modem bank which receives and aggregates incoming calls from customers who access our system by modem connection through a local call on the public telephone system, and then switches and routes aggregating broadband subscribers on wireless and fiber. The last mile of the Internet could be a leased line, ISDN or point-to-multipoint radio link in the 5.7 or 2.5 gigahertz range which we have licensed from the Wireless Planning Commission. We also use 2.4 ghz radios, which do not require an operating license, in some locations. Our larger corporate customers access the point of presence directly through leased lines or wireless links.

*Network Architecture.* We ensure network reliability through several methods and have invested in proven technologies. We use Cisco routers to route traffic between nodes interconnected using a high speed interface. Most of our applications and network verification servers are manufactured by IBM, Sun and Hewlett-Packard.

The primary nodes on the backbone network are connected by multiple high-speed fiber optic lines that we lease from long distance operators. The secondary nodes are connected by lower speed leased lines. A number of nodes are accessible from at least two other nodes, if not, by two long distance operators, allowing us to reroute traffic in the event of failure on one route. We reduce our exposure to failures on the local loop by usually locating our points of presence within range of service providers switching equipment and purchasing connectivity from multiple providers. To further maximize our network uptime, we are almost completely connected on fiber optic cables to the switching points of our service providers from our POPs.

In addition to a fundamental emphasis on reliability and security, our network design philosophy has focused on compatibility, interoperability, scalability and quality of service. We use Internet protocol with Multi Protocol Label Switching, or MPLS, to transmit data, thus ensuring that our network is completely interoperable with other networks and systems and that we may port any application onto our network. The modular design of our network is fully scalable, allowing us to expand without changing the network design or architecture, thus ensuring little or no service

disruption.

*Network Operations Center.* We maintain a network operation center located in Chennai (Madras) and a backup secondary facility in Mumbai (Bombay). The Chennai facility houses our central network servers as well as our network staff which monitors network traffic, service quality and equipment at all our points of presence to ensure a reliable Internet service. These operation centers are staffed 24-hours-a-day, seven-days-a-week. We have backup power generators and software and hardware systems designed to prevent network downtime in the event of system failures. In the future, we may add additional facilities to supplement or add redundancy to our current network monitoring capability.

**Competition**

*General.* We face competition in each of our markets and expect that this competition will intensify as the markets in India for corporate network/data services, Internet access services and online content develop and expand. We compete primarily on the basis of service, reliability and customer support. Price and ease of use are also competitive factors.

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*Corporate Network/Data Services.* Our competitors for many private network services include government services companies that have built and operate their own private data networks. For Internet access, the main competitors are Bharti Televentures, Reliance Infocomm and VSNL, whereas for domestic VPN, the main competition includes terrestrial network providers, such as Bharti, Reliance and Tata Indicom, and satellite communications agencies, such as Bharti BT (which recently bought Comsat Max) and HCL Comnet. For international MPLS VPN, the main competition is from MCI, AT&T and Bharti BT.

*Internet Access Services.* As of December 31, 2005, approximately 155 companies were operational with an Internet service provider license in India. During the last few years, BSNL and MTNL, the leading government owned telecom providers, have grown their dial-up businesses significantly by bundling their Internet services with basic telephony services. Their subscriber base grew by around 55% during the year 2004 and by about 50% in the year 2005, while the subscriber base of the private operators increased marginally in 2004 and decreased by 1% in 2005. BSNL and MTNL have approximately 58% of the market share as of December 31, 2005. While the dial-up segment will grow, we expect the market for broadband Internet services to grow rapidly in the future due to additional telecom providers emerging as competitors. We expect the market for consumer Internet access to remain extremely price competitive as late market entrants attempt to acquire customers.

There is no single significant competitor in the cybercafé space. Reliance Infocomm, a member of the Reliance group, has around 225 webworlds. Currently, the market is highly fragmented and dominated by individual entrepreneurs who own Internet cafés, with a few personal computers connected to the Internet through a leased line or ISDN line. With considerably lower overheads, these individuals are able to offer Internet access at lower rates. We compete by offering faster browsing speeds, improved overall ambience at our *iways*, convenient billing systems and roaming facilities.

*Online Portal Services.* There are several other companies in India that have developed websites, including rediff.com which completed its initial public offering in the United States in June 2000. The market is dominated by Sify.com, Rediff.com, Indiatimes.com, Yahoo.co.in, MSN.co.in and Google.com. Most of the services offered on these portals are similar with very little differentiation. Google established an office in India and began operations during the year ended March 31, 2005.

All the above mentioned portals are competing for a share of the online services market in India, which is dominated by online advertising, mobile telephone short code revenues and e-commerce. In terms of the share of the online advertising market, we are one of the leading companies. However, we lag competitors in mobile telephony short code and e-commerce services.

Most of our online portal competitors enjoy the following advantages compared to our company:  
larger production and technical staff;

greater name recognition and larger marketing budgets and resources; and

substantially greater financial, technical and other resources.

To be competitive, we must constantly innovate and introduce new services to the market quickly. We also need to keep pace with rapidly changing technology in this area. Increased competition could result in loss of market share, reduced prices or reduced margins, any of which could adversely affect our business.

**Intellectual Property**

Our intellectual property rights are important to our business. We rely on a combination of copyright and trademark laws, trade secrets, confidentiality procedures and contractual provisions to protect our intellectual property. We have filed a number of trademark applications for registering our product and service offerings. These applications are currently pending with regulatory authorities.

Our efforts to protect our intellectual property may not be adequate. We hold no patents, and our competitors may independently develop similar technology or duplicate our services. Unauthorized parties may infringe upon or misappropriate our services or proprietary information. In addition, the laws of India do not protect proprietary rights to the same extent as laws in the United States, and the global nature of the Internet makes it difficult to control the ultimate destination of our services. For example, the legal processes to protect service marks in India are not as

effective as those in place in the United States. The misappropriation or duplication of our intellectual property could disrupt our ongoing business, distract our management and employees, reduce our revenues and increase our expenses. In the future, litigation may be necessary to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. Any such litigation could be time-consuming and costly.

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We could be subject to intellectual property infringement claims as the number of our competitors grows and the content and functionality of our websites or other service offerings overlap with competitive offerings. Defending against these claims, even if not meritorious, could be expensive and divert management's attention from operating our company. If we become liable to third parties for infringing their intellectual property rights, we could be required to pay a substantial damage award and forced to develop non-infringing technology, obtain a license or cease selling the applications that contain the infringing technology. We may be unable to develop non-infringing technology or obtain a license on commercially reasonable terms, or at all.

We also rely on a variety of technologies that are licensed from third parties. We use software developed by these and other companies to perform key functions. These third-party licenses may not be available to us on commercially reasonable terms in the future. The loss of any of these licenses could delay the introduction of software enhancements, interactive tools and other features until equivalent technology could be licensed or developed. Any such delays could materially adversely affect our business, results of operations and financial condition.

**Government Regulation**

Our business is subject to comprehensive regulation by the Ministry of Communications through the Telecom Commission and the Department of Telecommunication, or DOT, pursuant to the provisions of the Indian Telegraph Act of 1885, or Telegraph Act, the India Wireless Telegraphy Act, 1933, or Wireless Act, the Information Technology Act, 2000 or IT Act and the terms of our Internet service provider license issued by the DOT under which we operate. Pursuant to the Telegraph Act, the provision of any telecommunications services in India requires a license from the Government of India, obtained through the DOT. While the Telegraph Act sets the legal framework for regulation of the telecommunications sector and the Wireless Act regulates the possession of wireless telegraphy equipment, much of the supervision and regulation of our company is implemented more informally through the general administrative powers of the DOT, including those reserved to the DOT and other governmental agencies under our license.

In March 1997, the Government of India established the TRAI, an independent regulatory authority, under the provisions of the Telecom Regulatory Authority of India Act. The TRAI is an autonomous body consisting of a chairperson and at least two and not more than four members.

Under the Telecom Regulatory Authority of India Act, the functions of the TRAI are to:

make recommendations on (i) the need and timing for the introduction of new service providers, (ii) the terms and conditions of licenses granted to service providers, (iii) the revocation of licenses for non-compliance, (iv) measures to facilitate competition and promote efficiency in the operation of telecommunications services so as to facilitate growth in such services, (v) technological improvements in the services provided by service providers, (vi) the type of equipment to be used by service providers, (vii) measures for the development of telecommunications technology and the telecommunications industry and (viii) the efficient management of the available spectrum;

discharge the following functions: (i) ensure compliance of the terms and conditions of licenses, (ii) fix the terms and conditions of interconnectivity between service providers, (iii) ensure technical compatibility and effective interconnection between service providers, (iv) regulate revenue sharing arrangements between service providers, (v) establish standards of quality of service, (vi) establish time periods for providing local and long distance telecommunications circuits between service providers, (vii) maintain and keep for public inspection a register of interconnect agreements and (viii) ensure effective compliance of universal service obligations;

levy fees and other charges at such rates and in respect of such services as may be determined by regulation; and

perform such other functions as may be entrusted to it by the Government of India or as may be necessary to carry out the provisions of the Telecom Regulatory Authority of India Act.

The TRAI also has the authority to, from time to time, set the rates at which domestic and international telecommunications services are provided in India. The TRAI does not have authority to grant licenses to service

providers or renew licenses, functions that remain with the DOT. The TRAI, however, has the following powers:

- to call on service providers to furnish information relating to their operations;
- to appoint persons to make official inquiries;
- to inspect the books of service providers; and
- to issue directives to service providers to ensure their proper functioning.

Failure to follow TRAI directives may lead to the imposition of fines. Decisions of the TRAI may be appealed to the Telecom Disputes Settlement and Appellate Tribunal.

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In November 1998, the Government of India opened the Internet service provider market to private competition, and the DOT instituted a mandatory license requirement for the provision of Internet services. We entered into a license agreement with the DOT on November 12, 1998 with effect on the same day, under which we were granted a license to provide national Internet services on a non-exclusive basis. The terms and conditions of our license are generally consistent with the policy for licensing Internet service providers. The term of our license is 15 years. Our license can be revoked by the DOT if we breach the terms and conditions of the license. The DOT retains the right to take over our network and to modify, revoke, terminate or suspend the terms and conditions of the license at any time if, in its opinion, it is necessary or expedient to do so in the interest of general public, or for the proper operation of the telecommunications sector or for security considerations. The DOT also retains the right to review the terms of our license based on changes in national telecommunications policy. We are not allowed to assign or transfer our rights under our license without the prior written consent of the DOT.

The Government of India has revised foreign investment policies permitting up to 74% foreign equity in an Internet service provider that operates its own international gateways. We currently do not operate any international gateways and are technically allowed to have 100% foreign equity in our company, subject to all clearances and approvals.

Our license also requires us to ensure that objectionable, obscene and unauthorized content, or any other content, messages or communications infringing copyrights, intellectual property rights and domestic and international cyber laws or which is inconsistent with the laws of India, is not carried on our network.

Although under the terms of our license we are free to fix the prices we charge our subscribers, the TRAI may set prices for the provision of Internet access services generally. We are permitted to use encryption to safeguard information transmitted over our network. However, if we use a higher level of encryption than that specified by the Government of India, our license requires us to deposit a set of keys with the Government of India. License fees are waived through October 31, 2003, and a nominal license fee of Re.1 per annum is payable from November 1, 2003. Our obligations under the license are secured by a performance bank guarantee in the amount of Rs.10.0 million (\$0.2 million).

We may be required to import into India network equipment, computer hardware and Internet related software purchased from foreign manufacturers for business purposes. These imports will be subject to the Export and Import Policy as declared by the Ministry of Commerce. At the time of import, we will be required to pay a customs duty pursuant to the Customs Tariff Act, 1975.

In December 2004, the Government of India imposed new requirements on Internet Service Providers wishing to offer Virtual Private Network services. Consequently, we applied for permission to offer VPN services, and the Government of India issued a letter of intent to us on December 30, 2004 regarding amendment of our existing ISP license to include provision of VPN services. In January 2005, we paid Rs.100 million as a one time entry fee and submitted a financial bank guarantee of Rs.10 million as required by the letter of intent.

The Indian Department of Telecommunications, or DOT, also requires ISP licensees to pay an annual fee of 8% of the adjusted gross revenues generated under the ISP license. To date, the DOT has not issued any guidelines or procedures for implementing this decision.

On January 11, 2005, we received provisional permission from the DOT, Government of India to offer VPN service in accordance with the new requirements. Final permission to offer VPN service shall be effective only after we sign the amendment to the license agreement. The provisional permission does not carry any terms and conditions relating to the license.

The Internet Service Provider Association of India, or ISPAI, had filed an appeal against this license with the Telecom Disputes Settlement and Arbitration Tribunal, or TDSAT. TDSAT directed DOT, Government of India to consult with TRAI before finalizing the license conditions.

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We reserved Rs.24.6 million for the period from April 1, 2005 to December 31, 2005 towards the 8% annual fee on VPN revenue as per the provisional IP VPN license and Rs.12.7 million for the period from January 1, 2006 to March 31, 2006 towards the 6% annual fee on AGR as per the ILD/NLD license requirement. The government has also revised guidelines, defining AGR for the purpose of levying annual license fee on VoIP services. As per this guidelines and based on opinion from the company's legal counsel, we paid Rs.5.28 million for the period from January 1, 2006 to March 31, 2006, towards the annual license fee.

**Seasonality**

We believe that our operations and businesses are not seasonal in nature.

**Organization Structure**

We are not part of any group. A list of subsidiaries and relevant information about them is provided in Exhibit 8.1.

**Property, Plant and Equipment**

We own our approximately 100,000 square foot corporate headquarters located in Chennai (Madras), India and an approximately 20,000 square foot regional office in Mumbai (Bombay). We lease an approximately 3,500 square foot network operations center in Chennai, a 20,000 square foot data center in Vashi, Mumbai and a 6,000 square foot office space in Prabhadevi, Mumbai. Our Chennai facility houses our central network servers as well as our network staff which monitors network traffic, service quality and equipment at all our points of presence, or POPs, to ensure a reliable Internet service. We have POPs in 171 towns/cities across India. Most of our POPs are staffed 24-hours-a-day, seven-days-a-week. Our POPs average approximately 750 square feet at each location. We have backup power generators and software and hardware systems designed to prevent network downtime in the event of system failures. In the future, we may add additional facilities to supplement or add redundancy to our current network monitoring capability.

**Item 4A. Unresolved Staff Comments**

**None.**

**Item 5. Operating and Financial Review and Prospects**

*Investors are cautioned that this discussion contains forward-looking statements that involve risks and uncertainties. When used in this discussion, the words believe, estimate, intend, will and expect and other similar expressions as they relate to our company or its business are intended to identify such forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Actual results, performance or achievements could differ materially from those expressed or implied in such forward-looking statements. Factors that could cause or contribute to such differences include those described under the heading Risk Factors in this report. Readers are cautioned not to place undue reliance on these forward-looking statements that speak only as of their dates. The following discussion and analysis should be read in conjunction with our financial statements included herein and the notes thereto.*

**Overview**

Please see the section entitled Item 4. Information on the Company Business Overview in this annual report.

**Operating Results**

The primary operating segments of our company are:

corporate network/data services, which include private network services, messaging services, security services, remote management services and web hosting for businesses;

Internet access services;

online portal services and content offerings; and

other services, such as development of content for e-learning.

**Table of Contents****Revenues***Corporate network/data services*

Our corporate network/data services revenues primarily include connectivity services revenue and, to a lesser extent, revenues from the sale of hardware and software purchased from third party vendors, installation of the link and other ancillary services, such as e-mail, document management and domain registration. Generally, these elements are sold as a package consisting of all or some of the elements. Our connectivity services include IPVPN services, Internet connectivity, last mile connectivity (predominantly through wireless), messaging services, security services and web hosting for businesses. We provide these services for a fixed period of time at a fixed rate regardless of usage, with the rate for the services determined based on the type of service provided, scope of the engagement and the Service Level Agreement, or SLA. Our web hosting service revenues are primarily generated from co-location services and connectivity services. Our security services revenues include revenue from consulting services, vulnerability assessment and penetration testing.

*Internet access services*

Internet access services revenues are generated from the Internet connectivity we provide to our retail customers through public access and home access services. Home access services are provided through dial-up packs and broadband connectivity, which is provided through arrangements with CTOs. Our public access services are provided through franchised and company-owned cybercafés. Additionally, we generate revenue by providing Internet Telephony services, allowing customers to make international telephone calls over the Internet.

*Online portal services and content offerings*

Online portal services revenues include advertising revenues from the various channels of our Internet portal, www.sify.com. We enter into contracts with customers to serve advertisements in the portal, and we are paid on the basis of impressions, click-throughs or leads. Revenues also accrue from commissions earned on products and services rendered through www.sifymall.com, and also from value-added services that are rendered using our mobile telephone short code, 4545.

*Other services*

Other services include revenue from e-learning. We develop and upload content for e-learning to facilitate web-based learning in various organizations. We provide e-learning services on a time-and-materials or on a fixed-price bases.

In Note 29 to our consolidated financial statements, we provide supplemental segment data, which provides separate revenue and operating income (loss) information for each of these business segments. This information is available in Item 18 Financial Statements of this annual report and is incorporated herein by reference.

**Expenses****Cost of revenues***Corporate network/data services*

Cost of revenues for the corporate network/data services division consists of telecommunications costs necessary to provide services, customer support costs, cost of goods in respect of communication hardware and security services sold and the cost of providing network operations. Telecommunications costs include the costs of international bandwidth procured from VSNL and satellite gateway providers and are required for access to the Internet, providing local telephone lines to our points of presence, the costs of using third-party networks pursuant to service agreements, leased line costs and costs towards spectrum fees payable to Wireless Planning Commission, or WPC, for provision of spectrum in the 5.7 GHz range to enable connectivity to be provided on the wireless mode for the last mile. In addition, the Government of India has recently imposed an annual license fee of 8% of the adjusted gross revenue generated from the provision of IPVPN services under our ISP license for the period January 11, 2005 to December 31, 2005 and 6% of the adjusted gross revenue for the period from January 1, 2006 for incomes generated from VPN business. Depreciation of plant and equipment has not been included in the cost of revenues since a significant part of the fixed assets are not directly identifiable.

*Internet access services*

Cost of revenues for the Internet access services division consists primarily of recurring telecommunications costs necessary to provide service to subscribers, direct costs paid to franchisees for running the *iways* and to cable

television operators for providing Internet services through cable to customers as well as voice termination charges for VoIP services. The Government of India also has imposed an annual license fee of 6% of the adjusted gross revenue of the VoIP for the period January 1, 2006 to March 31, 2006. Another recurring cost included in cost of revenues is the personnel and related operating expenses associated with customer support and network operations.

**Table of Contents***Online portal services and content offerings*

Cost of revenues for the online portal services and content offerings division includes the cost of procuring and managing content for the websites and cost of ringtones downloaded by using our mobile telephone short code 4545.

*Selling, general and administrative expenses*

Selling, general and administrative expenses consists of salaries and commissions for sales and marketing personnel, salaries and related costs for executive, financial and administrative personnel, sales, marketing, advertising and other brand building costs, travel costs, and occupancy and overhead costs.

*Depreciation and amortization*

We depreciate our tangible assets on a straight-line basis over the useful life of assets, ranging from two to five years and, in the case of buildings, 28 years. We do not amortize goodwill or indefinitely lived intangible assets recognized in accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*. In accordance with our accounting policy, during fiscal 2002, our management assessed the goodwill that we were carrying on our books in connection with the significant acquisitions and investments made by us in Internet content and commerce companies in 1999 and 2000, including IndiaWorld Communications and IndiaPlaza.com. Based on that evaluation, which was measured at the enterprise level, we concluded that these intangible assets were impaired. Accordingly, during fiscal 2002, we recorded a non-cash charge of Rs.4,112.7 million to write-off all of the goodwill related to these acquisitions. Impairment of Rs.15.0 million was recognized in fiscal 2002 in respect of other investments. In addition, during fiscal 2002, we recorded a non-cash charge of Rs.1,089.9 million to reflect an impairment of investment in affiliate related to our investment in CricInfo Limited. We assess for impairment of long-lived assets under SFAS No. 144. The carrying value of long-lived assets are compared with the adjusted estimated future cash flows at the identifiable business segment level. If the sum of such undiscounted cash flows is less than the aggregate carrying amount, the asset is not recoverable and the impairment loss is recognized. During fiscal 2004, we recorded an impairment charge of Rs.22.6 million (\$0.5 million).

*Amortization of deferred stock compensation expense*

A total of 3.2 million equity shares are reserved for issuance under our Associate Stock Option Plan (ASOP). As of March 31, 2006, we had outstanding an aggregate of 2,055,297 options (net of 1,020,112 options that have been forfeited by employees or expired) under our ASOP with a weighted average exercise price equal to approximately Rs.265.31 (\$5.96) per equity share. The unamortized deferred compensation expense related to these grants amounted to Rs.41.9 million (\$0.9 million) as of March 31, 2006.

In addition to our operations and those of our consolidated subsidiaries, our financial statements include our *pro rata* share of the financial results of those companies in which we have significant, non-controlling minority interests, such as Wisden CricInfo Limited and Man Financial-Sify Securities India Private Limited. These investments are accounted for under the equity method of accounting. In December 2002, we divested our entire stake in Placements.com Private Limited. In February 2004, we sold our investments in Wisden CricInfo Limited for a total consideration of Rs.61.2 million (GBP 0.7 million), which includes repayment of loan made to Wisden CricInfo of Rs.22.9 million (GBP 0.3 million).

**Results of Operations***Year ended March 31, 2006 compared to year ended March 31, 2005*

*Revenues.* We recognized Rs.4,681.8 million (\$105.3 million) in revenues for the year ended March 31, 2006, as compared to Rs.3,613.5 million for the year ended March 31, 2005, representing an increase of Rs.1,068.3 million, or 29.6%.

The revenues generated by our corporate network/data services businesses increased by Rs.507.7 million, or 25.1%, over the previous year. The increase is attributable to increases in connectivity revenues of Rs.499.4 million, installation revenues of Rs.12.8 million and security consultancy revenues of Rs.28.9 million, offset by a decrease in hardware and software sales of Rs.33.4 million. The corporate network/data services businesses successfully obtained a significant number of new orders and a large number of incremental orders from customers with operations throughout India for providing IPVPN and Internet connectivity. We currently have more than 1,200 corporate customers of our connectivity services. Sale of hardware includes Rs.0.7 million revenue recognized against sales-type leases. These sales-type lease transactions represent the sale of certain network equipment to corporate

customers and franchises.

The increase in consumer Internet access revenues was Rs.409.2 million, or 29.1%, over the previous year. The increase was as a result of an increase in public Internet access revenues by Rs.82.6 million, or 14.5%, increased revenues of Rs.90.7 million, or 41.1%, from voice-over-IP services, increased revenues from home based broadband subscribers of Rs.274.5 million or 95% and Rs.26.5 million or 93.5% increase from sale of hardware. These increases were partially offset by a decrease of Rs.62.6 million or 33% in the revenues from the dial-up business. The franchise fees recognized were

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marginally lower at Rs.104.1 million for the year ended March 31, 2006, compared with Rs.108.0 million for the year ended March 31, 2005. During the course of the year, the number of cybercafés increased from 2,471 to 3,307 whereas the number of *iways* in operation was only 1,725 as of March 31, 2004. The subscribers of the high speed Internet access to homes increased by more than 100% during the year, from around 89,000 as of March 31, 2005 to more than 183,000 as of March 31, 2006. The average revenue per user, or ARPU, per month fell by about 24% during the year. We experienced a 65% increase in the volume of VoIP calls made from our cybercafés and VoIP booths during the year, which we believe was due in part to our competitive pricing. We also started offering VoIP services to enterprises in the IT/ ITES segment during the year. Our overall voice minutes grew by 107% during the year. The average realisation per minute dropped by about 30% during the year, part of which is attributable to the lower price range of the service offered to the IT/ ITES segment. Our dial-up business continued to decline with a decrease in the number of subscribers as well as the usage minutes. Bundling of services offered by the public sector telephone companies resulted in a marked decline in the market share of private ISPs in the dial-up market segment.

Our online portal and content offerings division accounted for Rs.179.0 million of revenues for the year ended March 31, 2006, as compared to Rs.103.1 million for the year ended March 31, 2005, representing an increase of Rs.75.9 million, or 73.7%. This increase was on account of revenues from advertising increasing by 60%, revenue from commissions earned from e-commerce increasing by 86%, and in value-added services such as downloadable ring tones and mobile content increasing by more than 250%.

Revenues from our other businesses increased from Rs 82.12 million to Rs 157.61 million, or 91.9%. A number of our existing customers increased the size of their engagements with this division, and this combined with the addition of new customers, contributed to the increase in revenues.

*Cost of Revenues.* Cost of revenues was Rs.2,534.7 million (\$57.0 million) for the year ended March 31, 2006, compared to Rs. 2,023.9 million for the year ended March 31, 2005, representing an increase of Rs.510.8 million, or 25.2%. This increase was due to a Rs.194.7 million increase in bandwidth and voice termination costs, a Rs.141.0 million increase in direct expenses paid to franchisees and CTOs, for providing broadband delivery through cable, a Rs.121.1 million increase in personnel expenses of our directly billable manpower and the technology department, a Rs.18.4 million increase in cost of goods sold and Rs.35.6 million increase in other expenses. Cost of goods sold includes Rs.37.3 million towards an annual license fee on the revenue earned for VPN Services we provided for the year ended March 31, 2006, compared to Rs.5.6 million for the year ended March 31, 2005. For the year ended March 31, 2006, the cost of goods sold also includes an amount of Rs 5.28 million towards license fees on VoIP revenues earned for the quarter ended March 31, 2006.

*Selling, general and administrative expenses.* Selling, general and administrative expenses were Rs.1,852.3 million (\$41.6 million) for the year ended March 31, 2006, compared to Rs. 1,418.8 million for the year ended March 31, 2005, representing an increase of Rs.433.5, million or 30.6%. This increase was due to an increase of Rs. 99.5 million in personnel expenses due to increased staffing and salary increases, Rs.104.6 million increase in the cost of outsourced contract personnel salaries, Rs.73.0 million increase in marketing and promotion expenses, Rs.47.1 million increase in traveling expenses, Rs.47.9 million increase in rental costs for our office premises and nodes, Rs.31.7 million increase in repairs and maintenance expenses and Rs.29.7 million increase in other expenses.

*Provision for doubtful receivables and advances.* Provision for doubtful receivables and advances was Rs.90.7 million (\$2.0 million) for the year ended March 31, 2006, compared to Rs.57.6 million for the year ended March 31, 2005, representing an increase of Rs.33.1 million, or 57.5%. The increase was primarily on account of a more stringent review of our receivables position, on account of which we provided for a higher amount during the year ended March 31, 2006. The provision for doubtful debts for the year was at 1.9% of revenues, as compared to 1.6% during the year ended March 31, 2005.

*Depreciation.* Depreciation for the year ended March 31, 2006 was Rs.395.0 million (\$8.9 million), as compared to Rs.472.4 million for the year ended March 31, 2005, representing a decrease of Rs.77.4 million, or 16.4%. There was a significant purchase of assets during the period March to September 2000. Since most of the assets are depreciated over a 5-year period on the straight line method, these assets would have been fully depreciated by September 2005, and have not contributed to the depreciation charge during the other quarters of the fiscal year ended March 31, 2006. As the purchase of new assets during the last few quarters is significantly lower than the

purchase during the 2000 period as mentioned above, the depreciation charge is lower. The decrease is also due to the change in the estimated life of certain computers and servers from 2 years to 5 years effected during the quarter ended June 30, 2005. This resulted in a decrease of Rs.32.7 million in the depreciation charge for the year ended March 31, 2006.

*Amortization of intangible assets.* Amortization of intangible assets was Rs.68.8 million (\$1.5 million) for the year ended March 31, 2006, compared to Rs.84.4 million for the year ended March 31, 2005, representing a decrease of Rs.15.6 million, or 18.5%. The decrease is as a result of certain intangible assets being fully written off in the previous year.

*Amortization of deferred stock compensation expenses.* Amortization of deferred stock compensation expenses was Rs.12.7 million (\$0.3 million) for the year ended March 31, 2006, compared to Rs.10.6 million for the year ended March 31, 2005, representing an increase of Rs.2.1 million, or 19.8%. The increase was due to new stock options granted during the year ended March 31, 2006.

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*Foreign exchange (gain)/loss.* Foreign exchange gain for the year ended March 31, 2006 was Rs.23.2 million (\$0.5 million), compared to Rs.2.6 million for the year ended March 31, 2005, representing an increase of Rs.20.6 million, or 796.1%. This is as a result of the appreciation of U.S. Dollar against the Indian Rupee as compared to March 31, 2005, which impacted the value of our U.S. Dollar denominated cash deposits. It may be noted that there were wide fluctuations in the value of the Rupee against the dollar during the fiscal year ended March 31, 2005, ranging from 43.4 to 45.99 on account of which we had converted \$ 5 million during January 2005. The proceeds of the fresh issuance of ADRs to Infinity Capital in January 2006, amounting to \$ 37.5 million were held as U.S. Dollar deposits as of March 31, 2006. The forex translation gain that was recorded on this amount represents a significant part of the gain that was recorded for the fiscal year ended March 31, 2006. To reduce the impact of forex fluctuations on our financial results and to benefit out of the higher interest levels on Indian deposits, we have since converted \$ 10 million into Indian Rupees in April 2006.

*Other income (net).* Other income was Rs.59.2 million (\$1.3 million) for the year ended March 31, 2006, compared to Rs.93.3 million for the year ended March 31, 2005, representing a decrease of Rs.34.1 million, or 36.5%. During the fiscal year ended March 31, 2006, Other Income included a reversal of liabilities that were no longer required amounting to Rs.24.2 million, and an amount of Rs.15.7 million that was recognized as gain on sale of our investment in Dr. Reddy's Biosciences Limited (formerly Satyam Institute of E- Business Limited). This was partially offset by an increase in Interest Income (net) of Rs.5.8 million.

*Equity in profit of affiliates.* Equity in the profit of affiliates was Rs.40.7 million (\$0.9 million) for the year ended March 31, 2006, compared to Rs.50.8 million for the year ended March 31, 2005, representing a decrease of Rs.10.1 million, or 19.8%. During the quarter ended March 31, 2005, Man Financial-Sify completed a rights issue, in which we chose not to participate. As a result, our equity ownership in Man Financial-Sify has been reduced from 40% to 29.85%, as of March 15, 2005. Due to additional issuance of shares, we recorded Rs.1.1 million as gain on dilution through Shareholders' equity as per Stock Accounting Bulletin 51, Accounting For Sales of Stocks by a Subsidiary ( SAB ) for the year ended March 31, 2005. The increase in net worth of Man Financial-Sify during the year ended March 31, 2005 was higher than the increase during the year ended March 31, 2006 by Rs.11.1 million which has contributed to the decrease in our share of equity in the profits of affiliates for the year ended March 31, 2006.

*Net Loss.* Our net loss was Rs.149.2 million (\$3.4 million) for the year ended March 31, 2006, compared to a net loss of Rs.307.6 million for the year ended March 31, 2005.

*Year ended March 31, 2005 compared to year ended March 31, 2004*

*Revenues.* We recognized Rs.3,613.5 million (\$82.8 million) in revenues for the year ended March 31, 2005, as compared to Rs.2,801.2 million for the year ended March 31, 2004, representing an increase of Rs.812.3 million, or 29.0%.

The revenues generated by our corporate network/data services businesses increased by Rs.627.9 million, or 45.0%, over the same period in the prior year. The increase is attributable to increases in connectivity revenues of Rs.289.3 million, installation revenues of Rs.107.1 million, security consultancy revenues of Rs.66.6 million (as a result of the acquisition of Sify Networks Private Limited, formerly E Alcatraz Consulting Private Limited) and hardware and software sales of Rs.164.9 million. The corporate network/data services businesses successfully obtained a significant number of new orders and a large number of incremental orders from customers with operations throughout India for providing IPVPN and Internet connectivity. We currently have more than 1,000 corporate customers of our connectivity services. Sale of hardware includes Rs.36.5 million revenue recognized against sales-type leases. We are not focused on such sales-type lease transactions.

The increase in consumer Internet access revenues was Rs.316.4 million, or 29.1%, over the previous year. The increase was as a result of an increase in public Internet access revenues by Rs.205.8 million, or 57.0%, increased revenues of Rs.74.9 million, or 53.6%, from voice-over-IP services and increased revenues from home based broadband subscribers of Rs.193.3 million. These increases were partially offset by a decrease of Rs.156.0 million in the revenues from the dial-up business and Rs.6.9 million from sale of hardware. The franchise fees recognized were marginally higher at Rs.108.0 million for the year ended March 31, 2005, compared with Rs.102.7 million for the year ended March 31, 2004. During the course of the year, the number of cybercafés increased from 1,725 to 2,471 whereas the number of *iways* in operation was only 844 as of March 31, 2003. We experienced a more than a 100%

increase in the number of VoIP calls made from our cybercafés during the year, which we believe was due in part to our competitive pricing. Our dial-up business continued to decline with a decrease in the number of subscribers as well as the usage minutes. Bundling of services offered by the public sector telephone companies resulted in a marked decline in the market share of private ISPs in the dial-up market segment.

Our online portal and content offerings division accounted for Rs.103.1 million of revenues for the year ended March 31, 2005, as compared to Rs.84.2 million for the year ended March 31, 2004, representing an increase of Rs.18.9 million, or 22.4%. There was an increase of Rs.23.7 million on account of increased revenues from advertising, revenue from commission earned from e-commerce, value-added services like downloadable ring tones and mobile content. This increase was offset by a decrease of Rs.4.8 million pertaining to Indiaplaza, which resulted from the sale of substantially all of the assets of Indiaplaza to a third party in June 2003.

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Revenues from our other businesses decreased by Rs.150.9 million, or 64.8%. This decrease can be attributed to the loss of revenues from Element K, which was the largest customer of our e-learning division in the previous financial year. Revenues from Element K accounted for 0.4% of our revenues during the year ended March 31, 2005, compared with 8.0% of our revenues for the year ended March 31, 2004.

*Cost of Revenues.* Cost of revenues was Rs.2,023.9 million (\$46.4 million) for the year ended March 31, 2005, compared to Rs.1,476.7 million for the year ended March 31, 2004, representing an increase of Rs.547.2 million, or 37.1%. This increase was due to a Rs.138.6 million increase in cost of goods sold, Rs.165.6 million increase in revenue share paid to franchisees of our cybercafés and CTOs, Rs.91.2 million increase in personnel expenses, a Rs.87.4 million increase in lease line expenses and a Rs.64.4 million increase in other expenses. Cost of good sold includes Rs.5.6 million towards annual license fee payable towards the revenue earned on VPN Services we provided.

*Selling, general and administrative expenses.* Selling, general and administrative expenses were Rs.1,418.8 million (\$32.5 million) for the year ended March 31, 2005, compared to Rs.1,208.9 million for the year ended March 31, 2004, representing an increase of Rs.209.9, million or 17.4%. This increase was due to an increase of Rs.185.7 million in administration and other expenses, an increase of Rs.87.2 million in personnel expenses due to increase in number of employees, partially offset by a decrease of Rs.63.0 million in marketing and promotion expenses.

*Provision for doubtful receivables and advances.* Provision for doubtful receivables and advances was Rs.57.6 million (\$1.3 million) for the year ended March 31, 2005, compared to Rs.76.5 million for the year ended March 31, 2004, representing a decrease of Rs.18.9 million, or 24.7%. This decrease is mainly on account of reduction of older debts due to improved collection.

*Depreciation.* Depreciation for the year ended March 31, 2005 was Rs.472.4 million (\$10.8 million), as compared to Rs.432.7 million for the year ended March 31, 2004, representing an increase of Rs.39.7 million, or 9.2%. This increase is due to the increase in capital equipment deployed in our network infrastructure.

*Amortization of intangible assets.* Amortization of intangible assets was Rs.84.4 million (\$1.9 million) for the year ended March 31, 2005, compared to Rs.99.4 million for the year ended March 31, 2004, representing a decrease of Rs.15.0 million, or 15.1%. There was a decrease of Rs. 22.8 million resulting from a lower amortization of system software and other intangible assets being fully written off during the fiscal year ended March 31, 2004 and during the fiscal year ended March 31, 2005..This was partially offset by an increase of Rs.6.3 million (\$0.1 million) on amortization of customer contract intangibles that arose during our acquisition of Sify Networks Private Limited (formerly E Alacatraz Consulting Private Limited) and an increase of Rs.1.5 million (\$0.03 million) on amortisation of IPVPN licence fees paid during the year.

*Amortization of deferred stock compensation expenses.* Amortization of deferred stock compensation expenses was Rs.10.6 million (\$0.2 million) for the year ended March 31, 2005, compared to Rs.27.9 million for the year ended March 31, 2004, representing a decrease of Rs.17.3 million, or 62.0%. The decrease was due to a major portion of option grants being fully amortized by March 31, 2004 and also due to a lower number of option grants during the year ended March 31, 2005 as compared to the year ended March 31, 2004.

*Equity in profit of affiliates.* Equity in the profit of affiliates was Rs.50.8 million (\$1.2 million) for the year ended March 31, 2005, compared to Rs.17.1 million for the year ended March 31, 2004, representing an increase of Rs.33.7 million, or 197.1%. The increase is on account of sale of our stake in Wisden Cricinfo in February 2004. Our share of the loss of Wisden CricInfo for the year ended March 31, 2004 was Rs.21.6 million. The increase is also on account of better performance of our affiliate Refco-Sify during the year ended March 31, 2005. During the year ended March 31, 2005, Refco-Sify completed a rights issue. The Company chose not to participate in the rights issue. As a result, our equity ownership in Refco-Sify has been reduced from 40% to 30%. Due to additional issuance of shares, we recorded Rs.1.1 million as gain on dilution through shareholders equity as per Staff Accounting Bulletin 51, *Accounting For Sales Of Stock By A Subsidiary ( SAB 51 )*. We do not have any intention of further investment or dilution of our investment in Refco-Sify.

*Foreign exchange (gain)/loss.* Foreign exchange gain for the year ended March 31, 2005 was Rs.2.6 million (\$0.1 million), compared to a foreign exchange loss of Rs.52.1 million for the year ended March 31, 2004, representing an increase in gain of Rs.54.7 million, or 105.0%. This is as a result of the appreciation of U.S. Dollar to

the Indian Rupee as compared to March 31, 2004, which impacted the value of our U.S. Dollar denominated cash deposits.

*Other income (net).* Other income was Rs.93.3 million (\$2.1 million) for the year ended March 31, 2005, compared to Rs.144.1 million for the year ended March 31, 2004, representing a decrease of Rs.50.8 million, or 35.2%. The decrease in other income is on account of the profit on the sale of investment in Dr Reddy's Bio-Sciences Limited (formerly Satyam Institute of E Business Limited) of Rs.75.6 million and the Rs.3.7 million profit on the sale of substantially all of the

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assets of Indiaplaza, which were both recognised during the year ended March 31, 2004. During the year ended March 31, 2005, the balance of Rs.15.7 million on the sale of investment in Dr. Reddy's Bio-Sciences Limited was recognised consequent to a court verdict that was settled in favour of the company after an injunction order was vacated.

*Net Loss.* Our net loss was Rs.307.6 million (\$7.1 million) for the year ended March 31, 2005, compared to a net loss of Rs.371.3 million for the year ended March 31, 2004. Excluding the impact of the one time profit pertaining to profit on sale of our investment in Dr Reddy's Biosciences Limited for both the relevant periods, our net loss for the year ended March 31, 2005 would have been Rs.323.3 million (\$7.4 million) compared to a net loss of Rs.446.9 million for the year ended March 31, 2004.

**Liquidity and Capital Resources**

Prior to 1998, we financed our operations through funding from Satyam Computer Services, our former parent company. No further funding is expected from Satyam Computer Services in the future. Since 1998, we have financed our operations through equity sales and borrowings from institutions and banks. During fiscal years 1998, 1999 and 2000, we received Rs.38.5 million, Rs.307.5 million and Rs.10,220.0 million, respectively, in net cash proceeds from the sale of equity securities. We did not issue any equity shares in financing transactions in fiscal year 2001 or fiscal year 2002. During the fiscal years 2003 and 2004, we received Rs.792.0 million and Rs.166.9 million, respectively, in net cash proceeds from the issuance of equity securities. During fiscal year 2005, we received Rs.78.8 million in net cash proceeds from the issuance of shares to employees upon exercise of their stock options. During fiscal year 2006, we received Rs. 1,643.0 million in net cash proceeds towards issuance of shares to Infinity Capital Ventures and Rs. 49.4 million from issuance of shares to employees upon exercise of their stock options.

In July 2003, we sold our investment in one of our subsidiaries for consideration of Rs.277.5 million (\$6.4 million). In February 2004, we sold our entire investment in Wisden CricInfo for a total consideration of Rs.61.2 million (\$1.4 million) (GBP 0.74 million) which included repayment of loans made to Wisden Cricinfo of Rs.22.9 million (\$0.5 million) (GBP 0.3 million).

The following table summarizes our statements of cash flows for the periods presented:

	<b>Fiscal year ended, and as of March 31,</b>			
	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2006 U.S. Dollars</b>
	<b>Indian Rupees (in thousands)</b>			
Net loss	(371,284)	(307,576)	(149,245)	(3,355)
Net decrease (increase) in working capital	57,288	198,707	(128,119)	(2,880)
Other adjustments for non-cash items	587,981	559,821	500,478	11,251
Net cash provided by (used in) operating activities	273,985	450,952	223,114	5,016
Net cash provided by (used in) investing activities	11,327	(523,504)	(429,138)	(9,648)
Net cash provided by (used in) financing activities	189,958	69,182	1,684,055	37,861
Effect of exchange rate changes on cash and cash equivalents	(47,063)	1,479	20,558	463
Net increase (decrease) in cash and cash equivalents	428,207	(1,891)	1,498,589	33,692

Our principal capital and liquidity needs historically have related to developing our network infrastructure and our corporate network and electronic commerce services, establishing our customer service and support operations, developing our sales and marketing activities and for general working capital needs. We have also expended significant funds on acquisitions and investments.

A significant part of the development of our points of presence in India and our related network and infrastructure was completed during fiscal year 2001. During fiscal year 2001, we invested approximately Rs.500.0 million in moving to new owned office space in Chennai and Mumbai. Since the expansion into additional points of presence in India was not a priority and since the network had sufficient capacity to handle the traffic during

2003 and 2004, there were no significant sums expended on plant and equipment during those years, other than equipment required to provide broadband access through wireless technologies on the last mile. As a result, we incurred Rs.284.3 million and Rs.342.6 million for capital expenditures for the fiscal years ending March 31, 2003 and 2004, respectively. During the course of fiscal 2005 and 2006, we increased our capital expenditures to expand our network reach to cover 171 points of presence, to meet the needs of our growing client base. We incurred Rs.533.2 million and Rs. 587.5 million for capital expenditures during fiscal 2005 and 2006 respectively.

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Although we have 171 points of presence in India, a need for expansion into smaller towns would arise as our corporate and data network services grow, especially as we increase the connectivity for some of our existing clients.. There are many ISP s and data/network service providers exiting the business and, depending on pricing and other terms, we may acquire one or more of these third parties. In that event, we will need to invest in technologies to increase the speed of the backbone and edge networks. We will also have to invest in wireless and wire line methods of last mile Internet access delivery.

During fiscal years 2003 through 2005, our highest operational priority was to reduce cash burn incurred to build our organization and infrastructure to support our rapid growth, which has now stabilized. We pursued several initiatives to reduce our cash burn. The first focus was toward reducing the working capital required by our business. This was done by enhanced focus on collecting receivables and advancing the billing for the customers of our corporate data/network services division to the beginning of the quarter from the end of the quarter. Our improved collection efforts and change in policy to collect fees for certain services in advance resulted in a decrease in net receivables in recent periods. The second focus was toward reducing bandwidth costs. This was achieved by leveraging on the demonopolization of VSNL, negotiation with a range of suppliers, including VSNL, availability of national bandwidth (both intercity and intracity) from private telecom providers at lower rates and increasing the role of fixed wireless mode of delivery in the last mile. As a result of these initiatives, we have significantly reduced our cash burn over the last three years. We believe that the reductions achieved on account of the above are permanent reductions.

We intend to continue to focus on generation of cash surpluses in fiscal year 2007. Nevertheless, we expect to incur continued losses in the near future. Based upon our present business and funding plans, we believe that our cash and cash equivalents of Rs.2,822.5 million (\$63.5 million) as of March 31, 2006, excluding restricted cash included in current assets of Rs.1.0 million (\$0.02 million), is sufficient to meet our currently known requirements for at least the next 18 months beginning April, 2006. In light of the highly dynamic nature of our business, however, we cannot assure you that our capital requirements and sources will not change significantly in the future.

Cash balances held in foreign currency were Rs.555.7 million, Rs.293.2 million and Rs.1,956.39 million as of March 31, 2004, 2005 and 2006, respectively. Cash balances held in Indian currency were Rs.881.8 million, Rs.1,062.9 million and Rs.867.1 million as of March 31, 2004, 2005 and 2006, respectively. These amounts include cash and cash equivalents and restricted cash. Foreign exchange loss during fiscal 2004 was Rs.52.2 million and foreign exchange gain during fiscal 2005 and 2006 were Rs.2.6 million and Rs.23.2 million, respectively. This foreign exchange gain or loss is on account of cash held in foreign currency impacted by appreciation or depreciation of the U.S. Dollar against the Indian Rupee.

Cash provided by operating activities during fiscal year 2006 was Rs.223.1 million. This is mainly attributable to non-cash depreciation charge of Rs.476.5 million, provision for doubtful receivables of Rs.90.7 million, increase in trade accounts payable by Rs.177.2 million, increase in advances received from customers by Rs.43.1 million, increase in deferred revenues by Rs.35.1 million, offset by net loss from operations of Rs.149.2 million, increase in accounts receivable by Rs.279.9 million, increase in other assets by Rs.69.3 million, increase in prepaid expenses by Rs.4.0 million, increase in inventories by Rs.1.3 million, translation gain on cash and cash equivalents of Rs.20.6 million and decrease in other liabilities by 12.6 million. Cash provided by operating activities during fiscal year 2005 was Rs.451.0 million. This is mainly attributable to non-cash depreciation charge of Rs.567.4 million, provision for doubtful receivables of Rs.57.6 million, increase in trade accounts payable by Rs.310.6 million, increase in other liabilities by Rs.74.2 million, decrease in prepaid expenses by Rs.19.8 million and loss on sale of plant and equipment of Rs.2.8 million, offset by net loss from operations of Rs.307.6 million, increase in accounts receivable by Rs.178.9 million, increase in inventories by Rs.8.4 million, decrease in advances received from customers by Rs.14.2 million, increase in other assets by Rs.26.2 million and gain on sale of investments of Rs.15.7 million. Cash provided by operating activities during fiscal year 2004 was Rs.274.0 million. This is mainly attributable to a Rs.582.5 million non-cash depreciation charge, Rs.76.5 million provision for doubtful receivables, increase in trade accounts payable by Rs.120.6 million, an increase in advances received from customers by Rs.57.5 million, a decrease in other assets by Rs.43.0 million, a Rs.17.8 million decrease in prepaid expenses, and a Rs.22.9 million decrease in inventories, offset by a Rs.371.3 million net loss from operations, an increase in accounts receivable by

Rs.223.1 million, a decrease in other liabilities by Rs.42.0 million, gain on sale of plant and equipment of Rs.2.0 million and gain on sale of investments of Rs.99.0 million.

Cash used in investing activities during fiscal year 2006 was Rs.429.1 million, principally as a result of expenditure on purchase of routers, modems, ports, servers and other capital equipment in connection with the expansion of our network of Rs.587.4 million and purchase of intangible assets of software licenses of Rs.17.6 million, partially offset by proceeds from advances received towards sale of investments of Rs.139.8 million, movement in restricted cash by Rs.31.2 million and proceeds from sale of plant and equipment for Rs.4.9 million. Cash used in investing activities during fiscal year 2005 was Rs.523.5 million, principally as a result of expenditure on purchase of routers, modems, ports, servers and other capital equipment in connection with the expansion of our network of Rs.533.2 million and purchase of intangible assets of IPVPN License fee of Rs.100.0 million, partially offset by proceeds from sale of investments of Rs.15.0 million, movement in restricted cash by Rs.79.5 million and proceeds from sale of plant and equipment for Rs.15.2 million. Cash provided by investing activities of operations during fiscal year 2004 was Rs.11.3 million principally as a result of proceeds from sale of investments for

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Rs.257.4 million, movement in restricted cash by Rs.62.9 million, proceeds from sale of investment in affiliates for Rs.56.7 million and proceeds from sale of plant and equipment for Rs.13.0 million, offset by expenditure of Rs.342.6 million on purchase of routers, modems, ports, servers and other capital equipment in connection with the expansion of our network, purchase of intangible assets of Rs.2.3 million and purchase consideration for the acquisition of Sify Networks Private Limited (formerly E Alcatraz Consulting Private Limited) for Rs.32.8 million.

Cash provided by financing activities for fiscal year 2006 was Rs.1,684.1 million, which consisted of net proceeds from issuance of common stock of Rs.1,692.4 million, partly offset by repayment of principal under capital lease obligations of Rs.8.3 million. Cash provided by financing activities for fiscal year 2005 was Rs.69.2 million, which consisted of net proceeds from issuance of common stock to employees on exercise of stock options of Rs.78.8 million, partly offset by repayment of principal under capital lease obligations of Rs.9.6 million. Cash provided by financing activities for fiscal year 2004 was Rs.190.0 million and consisted of net proceeds from issuance of common stock of Rs.166.9 million and acquisition related debts of Rs.30.4 million, offset by repayment of principal under capital lease obligations of Rs.7.3 million.

In the ordinary course of our business we regularly engage in discussions and negotiations relating to potential investments, strategic partnerships and acquisitions. We will continue to be aggressive in our efforts to identify one or more investment or acquisition opportunities. However, we cannot assure you that we will be able to identify or complete any such transaction on favorable terms, or at all.

Government of India policies previously limited the total foreign equity in an Internet service provider to 49%. In May 2001, the Department of Commerce and Industry increased the limit on foreign direct investment for Internet companies from 49% to 74%. Our license was reissued in April 2002, increasing the maximum permitted level of foreign equity investment in our company to 74% and also permitting us to provide VoIP, subject to the terms of operation as detailed in the license. This limit of 74% is the maximum foreign equity investment that was permitted for ISPs that operate their own international gateways. Since we do not operate our own international gateways we were allowed to increase our foreign equity participation to 100%. If additional funds are raised through the issuance of equity or convertible debt securities, the percentage ownership of our shareholders and the holders of our ADSs will be reduced and these securities may have rights, preferences or privileges senior to those of our shareholders and the holders of our ADSs. We cannot assure you that additional financing will be available on terms favorable to us, or at all. If adequate funds are not available or are not available on acceptable terms, our ability to fund and expand our operations, take advantage of unanticipated opportunities, develop or enhance Internet content, features or services, or otherwise respond to competitive pressures will be significantly limited. Our business, results of operations and financial condition could be materially adversely affected by any such limitation. Please see Item 3. Key Information Risk Factors Forward-looking statements contained in this annual report may not be realized.

As of March 31, 2006, we had spent approximately Rs.2,649.38 million (\$59.6 million) to develop and deploy our network infrastructure. As of March 31, 2006, our future contractual obligations and commercial commitments were as follows:

	Payments Due by Period			Rs.Million	
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Contractual Obligations	5.6	2.9	2.7		
Capital Lease Obligations	5.6	2.9	2.7		

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	Amount of Commitment Expiration			Rs.million	
	Total Amounts	Per Period Less than 1	1-3 years	4-5 years	Over 5 years
Other Commercial Commitments	Committed	year	1-3 years	years	years
Standby Letters of Credit	247.9	247.9			
Guarantees	174.7	24.5	148.7	1.5	
Other Commercial Commitments	162.3	162.3			
Total Commercial Commitments	584.9	434.7	148.7	1.5	

**Recent Accounting Pronouncements****SFAS No. 123(R)**

Recently, the Financial Accounting Standards Board (FASB) issued Statement No. 123 (revised 2004), *Share Based Payment* (SFAS No. 123R), requiring companies to change their accounting policies to record the fair value of stock option issued to employees as an expense. Currently, we do not deduct the expense of employee stock option grants from its income statement based on the fair value method as we have adopted the pro forma disclosure provisions of SFAS No. 123. We are required to adopt SFAS No. 123R on April 1, 2006. The unamortized stock compensation expense as of March 31, 2006, determined under the fair value method is approximately Rs. 178,209 (\$4,006). We are evaluating the impact of the standard on the existing grants of employee stock options and future grants, if any. We are required to adopt SFAS No. 123R on April 1, 2006. The unamortized stock compensation expense as of March 31, 2006, determined under the fair value method is approximately Rs. 178,209 (\$4,006). We are required to adopt SFAS No.123(R) on April 1, 2006. Our management expects compensation costs to be recognized in accordance with SFAS No.123(R) to be significantly higher than that would have been recognized under APB 25.

**SFAS No. 154**

In June 2005, the FASB issued Statement No. 154, *Accounting Changes and Error Corrections*, a replacement of APB Opinion No. 20 and FASB Statement No. 3. Statement 154 applies to all voluntary changes in accounting principle, and changes the requirements for accounting for and reporting of a change in accounting principle. Statement 154 requires retrospective application to prior periods financial statements of a voluntary change in accounting principle unless it is impracticable. Opinion 20 previously required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. Statement 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. Statement 154 does not change the transition provisions of any existing accounting pronouncements, including those that are in a transition phase as of the effective date of this Statement. We are evaluating the impact of Statement No. 154.

**Critical Accounting Policies**

Critical accounting policies are defined as those that, in our view, are most important to the portrayal of our financial condition and results and that place the most significant demands on our management's judgment. We believe that the accounting policies discussed below are the most critical accounting policies.

**Revenue recognition**

Effective July 1, 2003, we adopted EITF Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables* for all revenue arrangements entered into on or after that date. Based on this guidance, we recognize revenues on the delivered products or services only if:

the revenue recognition criteria applicable to the unit of accounting is met;

the delivered element has value to the customer on a standalone basis (the delivered unit will have value on a standalone basis if it is being sold separately by other vendors or the customer could resell the deliverable on a standalone basis);

there is objective and reliable evidence of the fair value of the undelivered item(s); and

if the arrangement includes a general right of return relative to the delivered item, delivery or performance of the undelivered item(s) is considered probable and substantially in our control.

The arrangement consideration is allocated to the units of accounting based on their fair values. The revenue recognized for the delivered items is limited to the amount that is not contingent upon the delivery or performance of the

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undelivered items. In certain cases, the application of the contingent revenue provisions of EITF Issue No. 00-21 could result in recognizing a loss on the delivered element. In such cases, the cost recognized is limited to the amount of non-contingent revenues recognized and the balance of costs are recorded as an asset and are reviewed for impairment based on the estimated net cash flows to be received for future deliverables under the contract. These costs are subsequently recognized on recognition of the revenue allocable to the balance of deliverables.

Assessments about whether the delivered units have a value to the customer on a standalone basis, impact of forfeiture and similar contractual provisions, and determination of fair value of each unit would affect the timing of revenue recognition and would impact our results of operations.

We recognize revenue only on collectibility being probable and hence credit losses do not have an impact on our revenue recognition policy. Our provisions are based on the age of our receivables. No one client has contributed significantly to credit losses. We have had no significant changes in our collection policies or payment terms.

*Corporate network/data services*

We provide connectivity for a fixed period of time at a fixed rate regardless of usage. Connectivity is the last element that is provided in the case of a bundled contract. The connectivity charges are the same when sold alone or as part of a package. The revenue attributable to connectivity services is recognized ratably over the period of the contract. The hardware and software are standard products that are being freely traded in and purchased from the market, have standard specifications and are not otherwise customized for the specific needs of a customer. The software sold by us is off-the-shelf software, such as antivirus utilities and firewalls. The fair value for the hardware and software is available from the market, and the revenue attributable to hardware and software is recognized on delivery. Installation consists of commissioning of the last mile connectivity to the customer premises either through our wireless mode of broadband delivery or through the carrier exchange (primarily Bharat Sanchar Nigam Limited, or BSNL, a Government of India entity), and usually takes 4-6 weeks. However, once commissioned, this last mile connectivity can be used by the customer to access any other service provider. When the customer has such last mile connectivity, we do not charge any installation fee. The revenue attributable to the installation of the link is recognized on completion of the installation work. Revenue from ancillary services such as e-mail, fax and domain registration are recognized over the period such facilities are provided. All revenues are shown exclusive of sales tax and service tax and net of applicable discounts and allowances.

Web hosting service revenues primarily include co-location services and connectivity services. On occasion, we also sell related hardware and software to our web-hosting customers. At all times, such hardware and software belongs to the customer. This hardware and software is purchased from outside vendors and is freely traded in the market. We treat each element of the arrangement as a separate earnings process. The value of the hosting service is determined based on vendor specific objective evidence from similar services sold separately by us. When hardware and/or software is also included with hosting services and sold as a package the vendor specific objective evidence of the undelivered element is considered to arrive at the residual value of the delivered element. Revenue from hosting services is recognized over the period during which the service is provided.

Security services are provided on either a time-and-materials or fixed-price, fixed-timeframe basis. Revenues from services provided on a time-and-materials basis are recognized as the related services are performed. Revenues from services provided on a fixed-price, fixed-timeframe basis are recognized pursuant to the percentage of completion method, in accordance with SOP81-1, Accounting For Performance of Construction-Type and Certain Production-Type Contracts.

*Internet access services*

Dial-up Internet access is sold to customers either for a specified number of hours or for an unlimited usage within a specified period of time. Customers purchase a CD that allows them to access the Internet. The amounts received from customers on the sale of these CDs are not refundable. We recognize revenue from sale of CDs based on usage by the customer. At the end of the specified period, the remaining unutilized hours, if any, are recognized as revenue. Revenue from unlimited Internet access and electronic mail access is recognized over the specified period.

Public Internet access is provided to customers through a chain of franchisee cybercafé outlets and, to a lesser extent, Sify-owned cybercafés. We enter into an arrangement with franchisees that provides for the payment of an initial non-refundable franchisee fee in consideration for establishing the franchisee relationship and providing certain

initial services. These initial services consist of a number of activities, including installing the broadband receiver equipment at the cybercafé and connecting it to one of our broadcasting towers, obtaining regulatory approvals for clearance of the site for wireless transmission at the allotted frequency range and other ancillary services. Initial franchisee fee revenue is recognized at the time of commencement of operations by the franchisee, in accordance with SFAS No. 45, *Accounting for Franchisee Fee Revenue*, because we believe that substantial performance for which these non-refundable payments are received is completed at the time of commencement of operations and no uncertainty exists with regard to the collection of such fees. The amount of initial franchisee fee revenue recognized during the fiscal years ended March 31, 2005 and 2006

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were Rs.108.0 million and Rs.104.0 million, respectively. As of March 31, 2006, we owned 34 of the 3,307 cybercafés. Internet access revenue is recognized based on usage by the customer.

VoIP revenues are recognized on the basis of usage.

*Online portal services*

We enter into contracts with customers to serve advertisements in the portal, and we are paid on the basis of impressions, click-throughs or leads. Revenue is recognized based on actual impressions, click-throughs and leads delivered. There are no performance obligations or minimum guarantees. Revenues from electronic commerce transactions are recognized when the transactions are completed.

*Other services*

We provide e-learning software development services to facilitate web-based learning in various organizations. These customized services vary in size from customer to customer and relate to computer based and web based training in accordance with the customer specification. These services include information presentation, structured, content delivery, content digitization and simulation based training. These services are generally provided on a fixed price basis. We believe that the deliverables provided by us to our customers in connection with e-learning software development services are of the same nature as the services provided in an arrangement to deliver software that entail significant production, modification or customization of software. Our fixed price contracts to provide these services are also similar to contracts for services performed by architects, engineers or architectural engineering design firms as stated in paragraph 13 of SOP 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*. Accordingly, we recognize revenue based on the percentage of completion method from fixed price contracts relating to e-learning software development services.

*Impairment of long-lived assets*

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, long-lived assets, such as property, plant, and equipment, and purchased intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposal group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

*Deferred stock compensation*

We apply the intrinsic-value-based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations, including FASB Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation*, an interpretation of APB Opinion No. 25, issued in March 2000, to account for our fixed-plan stock options. Under this method, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. SFAS No. 123, *Accounting for Stock-Based Compensation*, established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, we have elected to continue to apply the intrinsic-value-based method of accounting described above, and have adopted only the disclosure requirements of SFAS No. 123 as amended by SFAS No. 148, *Accounting for Stock-Based Compensation - Transition and Disclosure*.

*Accounting estimates*

We prepare financial statements in conformity with US GAAP, which requires us to make a number of estimates and assumptions relating to the reporting of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements. Some of the more significant estimates include allowances for doubtful accounts, depreciation and amortization of long-lived assets and the valuation allowance for deferred tax assets. Actual results could differ from those estimates.

We continually evaluate these estimates and assumptions based on the most recently available information, our own historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Since the use of estimates are an integral component of the financial reporting process, actual results could differ from those estimates.

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**Board of Directors and Senior Management Executives**

The following table sets forth the name, age and position of each director and senior management executive of our company as of March 31, 2006:

<b>Name</b>	<b>Age</b>	<b>Designation</b>
R. Ramaraj	56	Chief Executive Officer and Managing Director
Durgesh Mehta	53	Chief Financial Officer
Shrikant Joshi	49	President - Access Media
Rahul Swarup	46	President, Enterprise Solutions
Rustom Irani	43	Chief Technology Officer
Ajit Abraham	46	Chief Human Resources Officer
Surya Mantha	43	Senior Vice President - Interactive Services
Raju Vegesna (4)	46	Chairman of the Board of Directors
C.B.Mouli (1)	59	Director & Financial Expert of Audit Committee
S.K.Rao (1) (2) (3)	62	Director & Chairman of Audit Committee
T.H. Chowdary (2) (3)	73	Director & Chairman of Compensation & Nomination Committees
R.D.Thulasiraj (1) (2) (3)	54	Director
P.S.Raju (4)	52	Director

(1) Member of the Audit Committee.

(2) Member of the Compensation Committee.

(3) Member of the Nominating Committee.

(4) Appointed as Directors and Mr. Vegesna as Chairman pursuant to Subscription Agreement dated November 10, 2005 between Sify and Infinity Capital Ventures, LP.

R. Ramaraj has served as Chief Executive Officer of our company since April 1998. Mr. Ramaraj has served as a Director since August 1996, prior to which he served as an advisor to our company since June 1996. From 1992 to 1996, Mr. Ramaraj served as a Director of Sterling Cellular Limited, a mobile telephone company based in India. Mr. Ramaraj is a Director of Universal Print Systems Ltd., a publicly held printing company based in India. He is also

a Director of IndiaWorld Communications Limited, a wholly owned subsidiary of Sify. Mr. Ramaraj received a B.Tech in Chemical Engineering from the University of Madras and a MBA from the Indian Institute of Management, Kolkata (Calcutta).

Durgesh Mehta has served as Chief Financial Officer since December 2005. Durgesh is a member of the Institute of Chartered Accountants of India. Prior to joining Sify, Mr. Mehta was the Finance Director of Unilever Arabia, Dubai, where he was responsible for the Finance, IT and Legal functions of the six GCC Countries, Iran and Yemen. Between 2000 and 2002, Mr. Mehta was the Financial Controller of Hindustan Lever Ltd. He is a Director of Sify Communications Limited and IndiaWorld Communications Limited, both subsidiaries of Sify.

Shrikant Joshi has served as President Access Media since December 2001. Mr. Joshi served as Head of Sales of Heinz from July 2000 to November 2001. From 1996 to 2000, Mr. Joshi served as Head of Domestic appliances and Personal Care Business of Phillips India Ltd. Mr. Joshi started his career with WIPRO in 1983 and held various senior positions across different businesses of WIPRO. Mr. Joshi received a Bachelors degree from IIT Delhi and a MBA from IIM Ahmedabad.

Rahul Swarup has served as President, Enterprise Solutions of our company since April 2001. From September 1999 to March 2001, Mr. Swarup served as Chief Technology Officer of our company. From 1989 to 1999, he was Vice President of Citicorp Global Technology Infrastructure. Mr. Swarup received a B.E. in Electrical Engineering from IIT Kanpur. Rahul Swarup is the Managing Director of Sify Communications Limited, a subsidiary of Sify. He is also a Director of Sify Networks Private Limited, a wholly owned subsidiary of Sify.

Rustom Irani has served as Chief Technology Officer of our company since April 2001. From December 1999 to March 2001, Mr. Irani served as our Vice President, Technology. From August 1999 to December 1999, he was Vice President, Technology and Chief Information Officer of GE Capital International Services, Hyderabad. From 1987 to August 1999, Mr. Irani was Vice President, Technology of Citibank N.A. Mr. Irani received a B.Sc. in Chemistry from the Arts & Sciences College, Secunderabad and a diploma in Computer Programming from Data Network Consultants, Mumbai.

Ajit Abraham has served as Chief Human Resources Officer of our company since May 1999. From 1998 to 1999, Mr. Ajit was Vice President, Human Resources of Mobil India, an oil company. From 1996 to 1998, he was General

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Manager, Human Resources, of Mahindra Holidays and Resorts. From 1994 to 1996, Mr. Ajit was Deputy General Manager, BioProducts Division of E.I.D. Parry, a manufacturing company. Ajit received a Master of Arts (Social Work) from University of Madras and a Diploma in Advanced Study in Human Resource Development. He is also a Director of Sify Communications Limited and IndiaWorld Communications Limited, subsidiaries of Sify.

Surya Mantha has served as Senior Vice President Interactive Services since August 2001. Mr Surya received B Tech Degree from IIT, Kanpur, MS from Virginia, MBA Degree from the University of Rochester and is also a Doctorate in Computer Science from the University of Utah. From 2001 to 2005, Mr Surya was the General Manager, (Industry & Solutions, Marketing, Business Product & Services), Realnetwork Inc., Seattle, WA.

Raju Vegesna has served as a Director of our company since November 2005. Mr. Vegesna is a Silicon Valley entrepreneur who founded several leading edge technology companies, including ServerWorks Corporation, acquired by Broadcom in 2001. After that acquisition, and post a brief stint with Broadcom, Mr. Vegesna founded and currently serves as CEO and Chairman of ServerEngines, LLC, a rapidly growing Silicon Valley-based company engaged in the development of innovative enterprise computing products. He holds a BS in Electrical Engineering from the University of Bangalore and holds an MS in Computer Engineering from Wayne State University, USA, and holds several patents in Microprocessor and Multiprocessor technology. He is also a Director of Server Engines LLC and Nulife Corp.

C.B. Mouli has served as a Director of our company since July 2005. Mr. Mouli is a member of the Institute of Chartered Accountants of India and also holds a Bachelor of Law Degree. Mr Mouli, a partner of C.B. Mouli & Associates, a Chartered Accountants firm and he is currently, the Chairman of the Audit Committee of GVK Jaipur Kishangarh Expressway Limited, a major infrastructure company. He is a Director of Taj GVK Hotels & Resorts Limited, GVK Jaipur Kishangarh Expressway Limited, Ammana Bio Pharma Limited and Ammana Equity Fund Private Limited.

S.K. Rao has served as a Director of our company since July 2005. Mr Rao, currently is the Director General, Administrative Staff College of India, Hyderabad. Mr Rao previously worked at the Commonwealth Secretariat in London in various diplomatic capacities. He also acted as the Consultant for the United Nations and represented the Commonwealth Secretariat as an Observer at the meetings of the UN General Assembly. Mr. Rao holds a MA and a Ph.D in Economics from Trinity College, Cambridge, U.K.

T.H. Chowdary has served as a Director of our company since February 1996. Dr. Chowdary retired as the Chief Executive Officer of VSNL. He has held key positions in the ITU, Intelsat and other international telecommunications organizations during the course of his career. He has since pioneered the cause of telecommunications education in India by setting up the Centre for Telecommunications Management Studies (CTMS) at Hyderabad. He has published several papers and is highly regarded in telecommunications circles in India and abroad for his command over technology and policy issues. Dr. Chowdary is also a director in Softsol India Limited and Tera Software Limited.

R. D. Thulasiraj has served as a Director of our company since July 2005. Mr Thulasiraj serves as the Executive Director of the Lions Aravind Institute of Community Ophthalmology (LAICO), which runs one of the world's biggest rural eye care programs, and is one of the large public health institutions in India. Mr Thulasiraj is also the Chairman of International Agency for Prevention of Blindness South East Asia Region (IAPB SEAR) and is a third world authority on hospital management for eye care. Mr. Thulasiraj received a MBA in Management from Indian Institute of Management, Kolkata(Calcutta).

P. S. Raju has served as a Director of our company since February 2006. Mr P S Raju is a member of the Institute of Chartered Accountants of India. Mr Raju is an independent practicing accountant. He has been the financial advisor to several ventures and knows the Indian business culture and accounting. He is also a Director of ServerEngines (India) Private Limited.

**Director Compensation**

Our Articles of Association provide that each of our directors may receive a sitting fee not exceeding the maximum limits prescribed under the provisions of the Indian Companies Act, 1956. Accordingly, our Directors, other than the Chairman and the Managing Director have been receiving Rs.20,000 for each Board and Committee meeting attended by them, effective October 2005. Mr. Ramaraj, who is employed as our Chief Executive Officer,

does not receive any additional compensation for his service on our Board of Directors. Directors are reimbursed for travel and out-of-pocket expenses in connection with their attendance at Board and Committee meetings. T. H. Chowdary, a Director of our company, has been receiving Rs.20,000 per month effective February 1, 2004 for the technical services rendered by him to us, after obtaining requisite Governmental permission for the same. Other than Mr. Ramaraj, none of our directors is a party to a service contract providing for benefits upon termination of employment with us.

**Table of Contents****Officer Compensation**

The following table sets forth all compensation paid by us during the fiscal year ended March 31, 2006 to our executive officers.

Name	Summary Compensation Table (Rs. Million)		
	Salary	Bonus	Stock Compensation
R. Ramaraj	7.50	Nil	3.45
Shrikant Joshi	5.10	1.35	0.48
Rahul Swarup	4.75	2.15	0.51
J. Avinash	2.24	Nil	0.03
Rustom Irani	4.58	1.9	0.45
Ajit Abraham	4.33	1.85	0.45

**Part of the year**

Anil Ahuja	4.17	Nil	(0.28)
George Zacharias	5.42	1.5	(0.02)
John Devasahayam	2.53	Nil	(0.002)
Surya Mantha	3.03	Nil	0.24
Durgesh Mehta	2.39	Nil	0.70

The following table sets forth all stock options granted by us during the fiscal year ended March 31, 2006 to our executive officers.

Name	Equity Shares Underlying Option Grant	Exercise Price (Rs.)	Expiration Date
R. Ramaraj	450,000*	238.32	February 24, 2009
Durgesh Mehta	100,000	481.74	May 9, 2009
Shrikant Joshi	55,000	238.32	February 24, 2009
Rahul Swarup	55,000	238.32	February 24, 2009
Rustom Irani	50,000	238.32	February 24, 2009
Ajit Abraham	50,000	238.32	February 24, 2009
Surya Mantha	35,000	238.32	February 24, 2009
C. B. Mouli	5,000	238.32	February 24, 2009
S. K. Rao	5,000	238.32	February 24, 2009
T. H. Chowdary	5,000	238.32	February 24, 2009
R. D. Thulasiraj	5,000	238.32	February 24, 2009

February 24,  
2009

\* In addition to the above, Mr Ramaraj holds another 50 equity shares and hence effectively holds 450,050 equity shares on the total share capital of the company.

The following table sets forth all stock options exercised by our executive officers during the fiscal year ended March 31, 2006.

Name	No. of shares	Exercise Price Rs.
1. R. Ramaraj		
2. George Zacharias	78,125	163.4
3. Anil Ahuja	20,313	228.74
4. Rahul Swarup	16,000	163.4
5. Ajit Abraham	15,000	163.4
6. Shrikant Joshi	12,550	140.35
7. J. Avinash	7,813	163.4
8. Rustom Irani	16,000	163.4
9. John Devasahayam	10,416	163.4

Mr Ramaraj's term of office as Managing Director has a term of five years and expires on March 31, 2008.

We paid retention bonuses amounting to Rs.20 million during the quarter ended December 31, 2005 to our key employees. The amount is being amortized over the retention period of 36 months and will be recovered from the employees

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in the event of termination of service before the end of the retention period. Our Compensation Committee in its meeting dated April 20, 2006 approved an amendment to this retention bonus scheme wherein the retention period has been reduced to 18 months.

Since this is an event subsequent to the balance sheet date, the charge on account of reduction in the retention period pertaining to the year ended March 31, 2006, amounting to Rs. 29,336, will be accounted in the next financial year in accordance with Para No.40 of Statement of Financial Accounting Concept No.6.

### **Board Composition**

Our Articles of Association set the minimum number of directors at three and the maximum number of directors at twelve. We currently have seven directors. The Indian Companies Act and our Articles of Association require the following:

at least two-thirds of our directors shall be subject to re-election by our shareholders; and

at least one-third of our directors who are subject to re-election shall be up for re-election at each annual meeting of our shareholders.

On July 15, 2005, we appointed Messrs. S.K. Rao, C.B. Mouli and R.D. Thulasiraj as independent Directors of the Board to comply with the requirements of NASDAQ Rule 4350(c).

Consequent to the divestment of their entire holding by Venture Tech and Satyam Computer Services during the year, Messrs. Sandeep Reddy, Srinivasa C. Raju, B. Rama Raju and V. Srinivas, their nominees resigned from the Board of Sify Limited.

Infinity Capital Ventures, LP, acquired the entire holding from Satyam Computer Services. In addition, in terms of the Subscription Agreement dated November 10, 2005 executed by the company with them, they have acquired an additional 6,720,260 shares of the company on a private transaction. At the conclusion of this transaction, their ownership in the company was at 42%. Messrs. Raju Vegesna and P.S. Raju are the nominees of Infinity Capital Ventures, LP.

The terms of Messrs. T.H. Chowdary and S.K. Rao will expire at our Annual General Meeting to be held in 2006 and they are eligible for reelection. The terms of Messrs. C.B. Mouli and R.D. Thulasiraj will expire at our Annual General Meeting to be held in 2007 and they are eligible for reelection. The terms of Messrs. Raju Vegesna and P.S. Raju will expire at our Annual General Meeting to be held in 2008 and they are eligible for reelection.

### **Board Committees**

The Audit Committee of the Board of Directors reviews, acts on and reports to the Board of Directors with respect to various auditing and accounting matters, including the recommendation of our independent auditors, the scope of the annual audits, fees to be paid to the independent auditors, the performance of our independent auditors and our accounting practices. Effective July 15, 2005, the members of our Audit Committee were Messrs. S.K. Rao, C.B. Mouli and R.D. Thulasiraj. This is in line with the SEC and NASDAQ regulations of having an independent Audit Committee.

The Compensation Committee of the Board of Directors determines the salaries, benefits and stock option grants for our employees, consultants, directors and other individuals compensated by our company. The Compensation Committee also administers our compensation plans. Effective July 15, 2005, the members of our Compensation Committee were Messrs. T.H. Chowdary, S.K. Rao and R.D. Thulasiraj. This is in line with the NASDAQ regulations on corporate governance.

The Nominating Committee of the Board of Directors evaluates and recommends the appointment of Directors to Board Committees, determines Board qualifications, evaluate their performance and determines the future requirements. The Committee was constituted on July 15, 2005 and the members of the Committee were Messrs. T.H. Chowdary, S.K. Rao and R.D. Thulasiraj. This is in line with the NASDAQ regulations on corporate governance.

**Table of Contents****Employees**

As of March 31, 2006, we had 1,910 employees, compared with 1,663 and 1,210 employees as of March 31, 2005 and March 31, 2004, respectively. Of our current employees, 107 are administrative, 578 from our sales and marketing staffs, 224 are in product and content development, 927 are dedicated to technology and technical support, and 74 are in business process and customer care. None of our employees are represented by a union. We believe that our relationship with our employees is good.

**Stock Ownership**

The following table sets forth information with respect to the beneficial ownership of our equity shares as of June 1, 2006 by each director and our senior management executives. The table gives effect to equity shares issuable within 60 days of June 1, 2006 upon the exercise of all options and other rights beneficially owned by the indicated shareholders on that date. Beneficial ownership is determined in accordance with the rules of the SEC and includes voting and investment power with respect to equity shares. Unless otherwise indicated, the persons named in the table have sole voting and sole investment control with respect to all equity shares beneficially owned.

<b>Beneficial Owner</b>	<b>Equity Shares Beneficially Owned</b>	
	<b>Number</b>	<b>Percent</b>
R. Ramaraj	50	0 -
Raju Vegesna	17,902,860	42.23
T. H. Chowdary		
C B Mouli		
P S Raju		
S K Rao		
R D Thulasiraj		
Durgesh Mehta		
Rahul Swarup		
Rustom Irani		
Ajit Abraham		
Surya Mantha		

**Employee Stock Option Plan**

We have an Associate Stock Option Plan, or ASOP, which provides for the grant of options to employees of our company. The ASOP 2005 was approved by our Board of Directors and our shareholders in October 2005. A total of 3.2 million equity shares are reserved for issuance under our Associate Stock Option Plans (ASOP). As of March 31, 2006, we had outstanding an aggregate of 2,055,297 options (net of 1,020,112 options that have been forfeited by employees or expired) under our ASOP with a weighted average exercise price equal to approximately Rs.265.31 (\$5.96) per equity share.

The ASOP is administered by the Compensation Committee of our Board of Directors. On the recommendation of the Compensation Committee, we will issue option letters to identified employees, with the right to convert the issued options into our equity shares at the rates indicated in the options. The consideration for transfer of the options will be Rs.1 per option to be paid by the employee before transfer of the options.

An employee holding options may apply for conversion of the options on a date specified therein which is referred to as the conversion date. The options are not transferable by an employee. The options lapse in the event of cessation of employment due to reasons of non-performance or otherwise. The equity shares transferred to the employee after conversion from options is the absolute property of the employee and will be held by the employee. A registration statement on Form S-8 covering the shares to be issued under the ASOP has been filed and the participants in the ASOP will be able to receive ADSs upon exercise of their options.

**Item 7. Major Shareholders and Related Party Transactions****Principal Shareholders**

The following table sets forth information with respect to the beneficial ownership of our equity shares as of June 1, 2006 by each person or group of affiliated persons who is known by us based on our review of public filings to beneficially own 5% or more of our equity shares. The table gives effect to equity shares issuable within 60 days of June 1, 2006 upon the exercise of all options and other rights beneficially owned by the indicated shareholders on that date.

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Beneficial ownership is determined in accordance with the rules of the SEC and includes voting and investment power with respect to equity shares. Unless otherwise indicated, the persons named in the table have sole voting and sole investment control with respect to all equity shares beneficially owned. The information below is based on a review of filings made by such persons with the SEC.

Mr Raju Vegesna, the Co-Trustee of the Vegesna Family Trust, which is the owner of Infinity Capital Management LLC, which is the general partner of Infinity Capital Ventures, LP, exercise voting control and dispositive power over the equity shares owned by Infinity Capital Ventures, LP. Mr Raju Vegesna, Director of our company, is affiliated with Infinity Capital Ventures, LP.

<b>Beneficial Owner</b>	<b>Equity Shares Beneficially owned</b>	
	<b>Number</b>	<b>Percent</b>
Infinity Capital Ventures, LP, 11601 Wilshire Boulevard, Suite 1900, Los Angeles, CA 90025	17,902,860	42.23

**Details of significant change in the percentage ownership held by the major shareholders:**

<b>Name of the shareholder</b>	<b>2003-04</b>		<b>2004-05</b>		<b>2005-06</b>	
	<b>No. of shares</b>	<b>%</b>	<b>No. of shares</b>	<b>%</b>	<b>No. of shares</b>	<b>%</b>
Satyam Computer Services Ltd.	11,182,600	32.0	11,182,600	31.61		
Venture Tech Solutions Pvt. Ltd.	3,533,326	10.1	2,750,000	7.77		
SAIF Investment Company Ltd.	2,808,140	8.0	2,008,140	5.68		
Infinity Capital Ventures, LP					17,902,860	42.23

The company has not issued any shares having different voting rights and hence the company's major shareholders do not have different voting rights.

**United States Shareholders**

As of March 31, 2006, 41,731,741 of our ADSs were held in the United States and we had approximately 29,000 shareholders in the United States. Each ADS represents one equity share.

**Host country Shareholders**

As on March 31, 2006, 657,773 of our equity shares were held in India and we had 18 shareholders of record in India. Each equity share has a par value of Rs.10/- each.

**Control of Registrant**

Based on our review of filings made with the SEC, we believe Infinity Capital Ventures, LP beneficially owned approximately 42% of our equity shares as of March 31, 2006. This shareholder is a party to the Subscription Agreement dated November 10, 2005 with our company. The Subscription Agreement provides that, among other things, the company shall appoint Mr Raju Vegesna as the Chairman of the Board of Directors, Infinity Capital shall also nominate another person to the Board of Directors and for so long as Infinity Capital continues to own at least 10% of the Company's outstanding Equity Shares, the Company shall not enter into any agreement pursuant to which it would provide a third party with registration rights for Company securities, without the consent of Infinity Capital. In November 2005, Mr Raju Vegesna, a nominee of Infinity Capital Ventures, LP, was appointed as Chairman of our Board of Directors. In February 2006, the company also appointed Mr.P.S.Raju as the second nominee of Infinity Capital to the Board of Directors.

These shareholders are presently able to exercise significant influence over many matters requiring approval by our shareholders, including the election of directors and approval of significant corporate transactions. Under Indian law, a simple majority is sufficient to control all shareholder action except for those items, which require approval by a special resolution. If a special resolution is required, the number of votes cast in favor of the resolution must be not less than three times the number of votes cast against it. Examples of actions that require a special resolution include:

altering our Articles of Association;

issuing additional shares of capital stock, except for *pro rata* issuances to existing shareholders;

commencing any new line of business; and

commencing a liquidation.

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Circumstances may arise in which the interests of Infinity Capital Ventures, LP or a subsequent purchaser of their shares could conflict with the interest of our other shareholders or holders of our ADSs. These shareholders could prevent or delay a change in control of our company even if a transaction of that sort would be beneficial to our other shareholders, including the holders of our ADSs.

**Related Party Transactions**

Our company has a stated policy on related party transactions, which states whenever Sify enters into any transaction with a related party the Company shall perform these transactions on terms no less favorable to the Company than could have been obtained from independent third parties.

Until December 2002, Satyam Computer Services was our parent company. In fiscal year 2006, we billed an aggregate of Rs.121.1 million (\$2.72 million) in services to Satyam Computer Services and its affiliates. For fiscal years 2004 and 2005 the corresponding figures were Rs.51.5 million and Rs.48.7 million, respectively. We believe that these transactions with Satyam Computer Services and its affiliates were on terms no less favorable to our company than could have been obtained from independent third parties.

On December 20, 2005, the Company divested 26% of its holding in Sify Communications Limited, or 4,680,000 shares, to M/s Infinity Satcom Universal (P) Ltd for a sale consideration of Rs.139,810. This was a related party transaction because Mr. Raju Vegesna, a member of Our Board of Directors, is the brother of Mr Ananda Raju, the owner of Infinity Satcom Universal (P) Ltd. We will be transferring our IP-VPN business from Sify Limited to Sify Communications Limited on receipt of the ILD/NLD license. Pending transfer of this business, we will recognize a gain of Rs.2,548 on the sale of 266 shares in Sify Communications Limited.

T. H. Chowdary, a Director of our company, has been receiving Rs.20,000 per month effective February 1, 2004 for the technical services rendered by him to the company, after obtaining requisite Governmental permission for the same.

**Item 8. Financial Information****Financial Statements**

We have elected to provide financial statements pursuant to Item 18 of Form 20-F. No significant change has occurred since the date of our annual financial statements for fiscal 2006.

**Legal Proceedings**

Our company and certain of our officers and directors are named as defendants in a securities class action lawsuit filed in the United States District Court for the Southern District of New York. This action, which is captioned *In re Satyam Infoway Ltd.* Initial Public Offering Securities Litigation, also names several of the underwriters involved in our initial public offering of American Depositary Shares as defendants. This class action is brought on behalf of a purported class of purchasers of our ADSs from the time of our Initial Public Offering ( IPO ) in October 1999 through December 2000. The central allegation in this action is that the underwriters in our IPO solicited and received undisclosed commissions from, and entered into undisclosed arrangements with, certain investors who purchased our ADSs in the IPO and the aftermarket. The complaint also alleges that we violated the United States federal securities laws by failing to disclose in the IPO prospectus that the underwriters had engaged in these allegedly undisclosed arrangements. More than 300 issuers have been named in similar lawsuits. On June 26, 2003, the plaintiffs in the consolidated IPO class action lawsuits currently pending against us and over 300 other issuers who went public between 1998 and 2000, announced a proposed settlement with us and the other issuer defendants. The proposed settlement provides that the insurers of all settling issuers will guarantee that the plaintiffs recover \$1 billion from non-settling defendants, including the investment banks who acted as underwriters in those offerings. In the event that the plaintiffs do not recover \$1 billion, the insurers for the settling issuers will make up the difference. We believe that we have sufficient insurance coverage to cover the maximum amount that it may be responsible for under the proposed settlement. Although the Federal District Court has preliminarily approved the settlement, it is possible that the Court may not finally approve the settlement in whole or part. We believe the maximum financial exposure under this settlement, in the event that the plaintiffs recover nothing from the non-settling defendants, is approximately U.S. \$3.9 million, an amount we believe is fully recoverable from Sify's insurer.

We are party to additional legal actions arising in the ordinary course of business. Based on the available information, as at March 31, 2006, we believe that we have adequate legal defenses for these actions and that the ultimate outcome of these actions will not have a material adverse effect on our company.

**Dividends**

We have not declared or paid any cash dividends on our equity shares since inception and do not expect to pay any cash dividends for the foreseeable future. We currently intend to retain future earnings, if any, to finance the expansion of our business. Investors seeking cash dividends should not purchase our ADSs.

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Under Indian law, a corporation may pay dividends upon a recommendation by its Board of Directors and approval by a majority of its shareholders. Any future cash dividends on our equity shares represented by ADSs will be paid to the depositary in rupees and will generally be converted into dollars by the depositary and distributed to holders of ADSs, net of the depositary's fees and expenses.

**Item 9. The Offer and Listing****Trading Markets**

There is no public market for our equity shares in India, the United States or any other market. Our ADSs evidenced by American Depositary Receipts, or ADRs, are traded in the United States only on the Nasdaq National Market. Each ADS represents one equity share. The ADRs evidencing ADSs were issued by our depositary, Citibank, N.A., pursuant to a Deposit Agreement.

**Price History**

Our ADSs commenced trading on the Nasdaq National Market on October 19, 1999. The tables below set forth, for the periods indicated, high and low trading prices for our ADSs:

**Prior Fiscal Years**

	<b>Fiscal year ended</b>	<b>High</b> \$	<b>Low</b> \$
March 31, 2002		17.60	2.88
March 31, 2003		6.44	0.88
March 31, 2004		9.25	3.75
March 31, 2005		8.62	3.82
March 31, 2006		14.58	3.81

**Quarters of Prior Fiscal Years**

	<b>Fiscal year ended March 31, 2005</b>	<b>High</b> \$	<b>Low</b> \$
First Quarter		8.62	5.61
Second Quarter		6.23	3.82
Third Quarter		7.13	5.48
Fourth Quarter		6.10	4.34

	<b>Fiscal year ended March 31, 2006</b>	<b>High</b> \$	<b>Low</b> \$
First Quarter		5.78	3.81
Second Quarter		5.95	4.35
Third Quarter		11.85	4.75
Fourth Quarter		14.58	8.77

**Prior Six months**

		<b>Price range</b>	
	<b>Month</b>	<b>High</b> \$	<b>Low</b> \$
December 2005		11.85	7.22
January 2006		12.35	8.77
February 2006		14.50	10.02
March 2006		13.97	12.08
April 2006		14.99	10.75
May 2006		13.20	9.50

The initial public offering of our ADSs was priced on October 18, 1999 at a price of \$18.00 per ADS.



**Table of Contents****Item 10. Additional Information**

Sify Limited was organized as a limited liability company under the laws of the Republic of India pursuant to the provisions of the Indian Companies Act on December 12, 1995. Our authorized share capital is 50,000,000 shares, par value Rs.10 per share. The number of equity shares outstanding as of March 31, 2005 and March 31, 2006 were 35,380,278 and 42,389,514 respectively. During the fiscal year ended March 31, 2006, the company had issued 6,720,260 equity shares, par value Rs.10 per share to Infinity Capital Ventures, LP, and another 288,976 equity shares, par value Rs.10 per share to the employees in respect of the exercise of the grants under Associate Stock Option Plan 2002. The total number of shares issued during the year amounts to 7,009,236 equity shares, par value Rs.10 per share.

The equity shares are our only class of share capital. Some of the share capital is represented by American Depository Receipts issued by our company in accordance with applicable laws and regulations. Our Articles of Association and the Indian Companies Act permit us to issue classes of securities in addition to the equity shares. For the purposes of this annual report, shareholder means a shareholder who is registered as a member in the register of members of our company. The term shareholders and shareholders have the same meaning in this annual report since the Indian Companies Act only defines a shareholder.

A total of 3.2 million equity shares are reserved for issuance under our Associate Stock Option Plan, or ASOP. As of March 31, 2006, we had outstanding an aggregate of 2,055,297 options (net of 1,020,112 options that have been forfeited by employees or expired) under our ASOP with a weighted average exercise price equal to approximately Rs.265.31 (\$5.96) per equity share. The unamortized deferred compensation expense related to these grants amounted to Rs.41.9 million (\$0.9 million) as of March 31, 2006.

During the fiscal year ended March 31, 2004, Venture Tech, who had subscribed for the shares of our company in terms of an Investor Rights Agreement, sold 2,017,641 shares reducing their holding from 15.9% to 10.1% and SAIF sold 4,750,000 shares reducing their holding from 21.6% to 8%.

During the fiscal year ended March 31, 2005, Venture Tech sold an additional 783,326 shares reducing their holding from 10.1% to 7.7% and SAIF sold an additional 800,000 shares reducing their holding from 8% to 5.68%.

During the fiscal year ended March 31, 2006,, Venture Tech sold the remaining 2,750,000 shares of our company and SAIF sold the remaining 2,008,140 shares of our company. Satyam Computer Services had divested their entire holding of 11,182,600 shares in the company to Infinity Capital Ventures, LP through a sponsored ADR programme arranged by us. Further, Infinity Capital, pursuant to the Subscription Agreement dated November 10, 2005 acquired another 6,720,260 shares of the company in a private transaction. On conclusion of this transaction, the issued and outstanding share capital of our company was 42,389,514 equity shares, with a par value of Rs.10/- per share.

Our company has not issued any other class of shares or having different voting rights. The company had also not issued any shares for consideration other than cash. There is also no reduction of issued share capital of the company.

At the Extraordinary General Meeting of our shareholders held on December 23, 2005, the shareholders had approved by a Special Resolution the issue and allotment of 4.97 million equity shares of the par value of Rs.10/- per share at such price as may be determined to the public in India as the initial public offer to comply with the statutory requirement of domestic listing of the shares of our company, as and when announced by the Government of India.

In June, 2006, Rustom Irani and Ajit Abraham each announced that they will be stepping down as officers of our Company and will be leaving the employment of our Company. Mr. Irani is our Chief Technology Officer and Mr. Abraham is our Chief Human Resources Officer. Our management has begun searching for their replacements.

**Memorandum and Articles of Association**

A copy of the revised Memorandum and Articles of Association is annexed as Exhibit No. 1.1

Under our Memorandum of Association, the main objectives of our company include:

- developing, servicing and selling or leasing data through direct or electronic media, developing a wide area of communications network and providing value-added services on the network for the development, service, purchase or sale of computers, software and related products in order to provide marketing services; and

designing and developing systems and application software for sale in and outside of India, and designing and developing systems and applications software for or on behalf of manufacturers, owners and users of computer systems and digital or electronic equipment.

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*Board of Directors*

In terms of the provisions of the Articles of Association of the Company and the Indian Companies Act, 1956:

- (a) no director of the company can vote on a proposal, arrangement or contract in which he is materially interested;
- (b) the directors of the company can not vote on a proposal in the absence of an independent quorum for compensation to themselves or their body;
- (c) each of our directors is entitled to receive a sitting fee not exceeding Rs.20,000 for every meeting of the Board of Directors and each meeting of a Committee of the Board of Directors, as well as all traveling and out-of-pocket expenses incurred in attending such meetings;
- (d) the directors are empowered to borrow moneys through board meetings up to the prescribed limit and beyond that with the approval of the shareholders through a General Meeting;
- (e) retirement of directors are determined by rotation and not based on age limit; and
- (f) no director is required to hold any qualification shares.

**For additional information, please see Item 6. Director, Senior Management and Employees Board Composition, -Board Committees and -Director Compensation, and -Officer Compensation.**

*Dividends*

Under the Indian Companies Act, unless our Board of Directors recommends the payment of a dividend, we may not declare a dividend. Similarly, under our Articles, although the shareholders may, at the annual general meeting, approve a dividend in an amount less than that recommended by the Board of Directors, they cannot increase the amount of the dividend. In India, dividends generally are declared as a percentage of the par value of a company's equity shares. The dividend recommended by the Board of Directors, and thereafter approved by the shareholders in general meeting, if any, and subject to the limitations described above, is distributed and paid to shareholders in proportion to the paid up value of their shares within 30 days of the approval by the shareholders at the annual general meeting. Pursuant to our Articles, our Board of Directors has discretion to declare and pay interim dividends without shareholder approval. With respect to equity shares issued during a particular fiscal year (including any equity shares underlying ADSs issued to the depository), cash dividends declared and paid for such fiscal year generally will be prorated from the date of issuance to the end of such fiscal year.

Under the Indian Companies Act, dividends may be paid out of profits of a company in the year in which the dividend is declared or out of the undistributed profits of previous fiscal years. Before declaring a dividend greater than 10% of the par value of its equity shares, a company is required under the Indian Companies Act to transfer to its reserves a minimum percentage of its profits for that year, ranging from 2.5% to 10% depending upon the dividend percentage to be declared in such year. The Indian Companies Act further provides that, in the event of an inadequacy or absence of profits in any year, a dividend may be declared for such year out of the company's accumulated profits, subject to the following conditions:

the rate of dividend to be declared may not exceed 10% of its paid up capital or the average of the rate at which dividends were declared by the company in the prior five years, whichever is less;

the total amount to be drawn from the accumulated profits earned in the previous years and transferred to the reserves may not exceed an amount equivalent to 10% of its paid up capital and free reserves, and the amount so drawn is to be used first to set off the losses incurred in the fiscal year before any dividends in respect of preference or equity shares are declared; and

the balance of reserves after withdrawals shall not fall below 15% of its paid up capital.

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**For additional information, please see Item 8. Financial Information Dividends.**

*Voting Rights*

At any general meeting, voting is by show of hands unless a poll is demanded by a shareholder or shareholders present in person or by proxy holding at least 10% of the total shares entitled to vote on the resolution or by those holding shares with an aggregate paid up capital of at least Rs.50,000. Upon a show of hands, every shareholder entitled to vote and present in person has one vote and, on a poll, every shareholder entitled to vote and present in person or by proxy has voting rights in proportion to the paid up capital held by such shareholders.

Any shareholder may appoint a proxy. The instrument appointing a proxy must be delivered to us at least 48 hours prior to the meeting. A proxy does not participate at the time of show of hands but the proxy is entitled to vote on a poll being taken. A corporate shareholder may appoint an authorized representative who can vote on behalf of the shareholder, both upon a show of hands and upon a poll.

Ordinary resolutions may be passed by simple majority of those present and voting at any general meeting for which the required period of notice has been given. However, specified resolutions such as amendments to our Articles and the Memorandum of Association, commencement of a new line of business, the waiver of preemptive rights for the issuance of any new shares and a reduction of share capital, require that votes cast in favor of the resolution (whether by show of hands or poll) are not less than three times the number of votes, if any, cast against the resolution.

*Bonus Shares*

In addition to permitting dividends to be paid out of current or retained earnings as described above, the Indian Companies Act permits us to distribute an amount transferred from the general reserve or surplus in our profit and loss account to our shareholders in the form of bonus shares, which are similar to a stock dividend. The Indian Companies Act also permits the issuance of bonus shares from a share premium account. Bonus shares are distributed to shareholders in the proportion recommended by the Board. Shareholders of record on a fixed record date are entitled to receive such bonus shares.

*Preemptive Rights and Issue of Additional Shares*

The Indian Companies Act gives shareholders the right to subscribe for new shares in proportion to their respective existing shareholdings unless otherwise determined by a special resolution passed by a general meeting of the shareholders. For approval, a special resolution must be approved by a number of votes, which is not less than three times the number of votes against the special resolution. At our 2000 Annual General Meeting, our shareholders approved a special resolution pursuant to which we may issue up to one million equity shares (equivalent to one million ADSs) in connection with acquisitions, 268,500 of which we issued in connection with our acquisition of IndiaWorld Communications, 551,180 of which we issued in connection with our acquisition of a 25% stake in CricInfo Limited and 113,798 of which we issued in connection with our acquisition of IndiaPlaza.com. At our 2001 Annual General Meeting, our shareholders approved a special resolution permitting us to issue up to four million additional equity shares in connection with acquisitions or capital raising transactions, and ADS holders are deemed to have waived their preemptive rights with respect to these shares. At our December 2002 Extraordinary General Meeting, our shareholders approved a special resolution permitting us to issue up to 12.5 million additional equity shares (equivalent to 12.5 million ADSs) in connection with the sale of equity shares to SAIF and VentureTech, and our ADS holders are deemed to have waived their preemptive rights with respect to these shares and our Board of Directors may approve the issuance of these shares without further action of our shareholders. At our Extraordinary General Meeting held in December 2005, our shareholders approved a special resolution permitting us to issue up to 6,720,260 additional equity shares (equivalent to 6.72 million ADSs) in connection with the acquisition of additional shares by Infinity Capital, as per the Subscription Agreement dated November 10, 2005 executed by the company with them.

*Annual General Meetings of Shareholders*

We must convene an annual general meeting of shareholders within six months after the end of each fiscal year and may convene an extraordinary general meeting of shareholders when necessary or at the request of a shareholder or shareholders holding at least 10% of our paid up capital carrying voting rights. The annual general meeting of the shareholders is generally convened by our Secretary pursuant to a resolution of the Board. Written notice setting out

the agenda of the meeting must be given at least 21 days (excluding the days of mailing and receipt) prior to the date of the general meeting to the shareholders on record. Shareholders who are registered as shareholders in the company's register on the record date are entitled to attend or vote at such meeting.

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The annual general meeting of shareholders must be held at our registered office or at such other place within the city in which the registered office is located. Meetings other than the annual general meeting may be held at any other place if so determined by the Board. Our registered office is located at 2<sup>nd</sup> Floor, Tidel Park, 4, Canal Bank Road, Taramani, Chennai 600 113, India.

Our Articles provide that a quorum for a general meeting is the presence of at least five shareholders in person.

*2006 Annual General Meeting*

Our Annual General Meeting for the fiscal year 2006 will be held at the registered office of our company, 2<sup>nd</sup> Floor, Tidel Park, 4 Canal Bank Road, Taramani, Chennai 600 113, India. The matters to be brought in front of our shareholders at this meeting shall be described in the Notice of the Tenth Annual General Meeting, which will be mailed to the shareholders and shall also be filed with the Commission on Form 6-K. Please see that filing for a description of the matters to be considered by our shareholders at the meeting. At the Annual General Meeting, each of the proposals shall be put up for approval by our shareholders.

*Limitations on the Rights to Own Securities*

The limitations on the rights to own securities of Indian companies, including the rights of non-resident or foreign shareholders to hold securities, are discussed in the section entitled *Risk Factors – Risks Related to the ADSs and Our Trading Market* in this Annual Report.

*Register of Shareholders; Record Dates; Transfer of Shares*

We maintain a register of shareholders as required under the Indian Companies Act, 1956. For the purpose of determining the shares entitled to annual dividends, the register is closed for a specified period prior to the annual general meeting. The date on which this period begins is the record date.

To determine which shareholders are entitled to specified shareholder rights, we may close the register of shareholders. The Indian Companies Act requires us to give at least seven days' prior notice to the public before such closure. We may not close the register of shareholders for more than thirty consecutive days, and in no event for more than forty-five days in a year.

Following the introduction of the Depositories Act, 1996, and the repeal of Section 22A of the Securities Contracts (Regulation) Act, 1956, which enabled companies to refuse to register transfers of shares in some circumstances, the equity shares of a public company are freely transferable, subject only to the provisions of Section 111A of the Indian Companies Act. Since we are a public company under Indian law, the provisions of Section 111A will apply to us. Our Articles currently contain provisions, that give our directors discretion to refuse to register a transfer of shares in some circumstances. According to our Articles, our directors are required to exercise this right in the best interests of our company. While our directors are not required to provide a reason for any such refusal in writing, they must give notice of the refusal to the transferee within two months after receipt of the application for registration of transfer by our company. In accordance with the provisions of Section 111A(2) of the Indian Companies Act, our directors may exercise this discretion if they have sufficient cause to do so. If our directors refuse to register a transfer of shares, the shareholder wishing to transfer his, her or its shares may file a civil suit or an appeal with the Company Law Board, or CLB. Pursuant to Section 111A(3), if a transfer of shares contravenes any of the provisions of the Securities and Exchange Board of India Act, 1992 or the regulations issued thereunder or the Sick Industrial Companies (Special Provisions) Act, 1985 or any other Indian laws, the CLB may, on application made by the company, a depository incorporated in India, an investor, the Securities and Exchange Board of India or other parties, direct the rectification of the register of records. The CLB may, in its discretion, issue an interim order suspending the voting rights attached to the relevant shares before making or completing its investigation into the alleged contravention. Notwithstanding such investigation, the rights of a shareholder to transfer the shares will not be restricted.

Under the Indian Companies Act, unless the shares of a company are held in a dematerialized form, a transfer of shares is effected by an instrument of transfer in the form prescribed by the Indian Companies Act and the rules thereunder together with delivery of the share certificates. Our transfer agent is Citibank, N.A. – Mumbai branch.

*Audit and Annual Report*

At least 21 days before the annual general meeting of shareholders excluding the days of mailing and receipt, we must distribute to our shareholders a detailed version of our audited balance sheet and profit and loss account and

the related reports of the Board and the auditors, together with a notice convening the annual general meeting. These materials are also generally made available at our corporate website, [www.sifycorp.com](http://www.sifycorp.com). Under the Indian Companies Act, we must file the

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balance sheet and annual profit and loss account presented to the shareholders within 30 days of the conclusion of the annual general meeting with the Registrar of Companies in Tamil Nadu, India, which is the state in which our registered office is located. We must also file an annual return containing a list of our shareholders and other information within 60 days of the conclusion of the meeting.

*Company Acquisition of Equity Shares*

Under the Indian Companies Act, approval of at least 75% votes in favor, of a company's shareholders present in person or by proxy as the case may be, voting on the matter and approval of the High Court of the State in which the registered office of the company is situated is required to reduce a company's share capital. A company may, under some circumstances, acquire its own equity shares without seeking the approval of the High Court. However, a company would have to extinguish the shares it has so acquired within the prescribed time period. Generally, a company is not permitted to acquire its own shares for treasury operations. An acquisition by a company of its own shares (without having to obtain the approval of the High Court) must comply with prescribed rules, regulations and conditions as laid down in the Indian Companies Act and the Securities and Exchange Board of India (Buy-back of Securities) Regulations, 1998, or Buy-back Regulations.

*Liquidation Rights*

Subject to the rights of creditors, employees and the holders of any shares entitled by their terms to preferential repayment over the equity shares, if any, in the event of our winding-up the holders of the equity shares are entitled to be repaid the amounts of paid up capital or credited as paid up on those equity shares. All surplus assets after payments due to the holders of any preference shares at the commencement of the winding-up shall be paid to holders of equity shares in proportion to their shareholdings.

*Redemption of Equity Shares*

Under the Indian Indian Companies Act, equity shares are not redeemable.

**Material Contracts**

*You should read the following description of our material contracts in conjunction with the descriptions of our acquisitions and investments and our relationships with strategic partners as described under Item 4. Information on the Company.*

*Internet Service Provider License.*

We entered into a license agreement with the DOT on November 12, 1998 with effect on the same day, under which we were granted a license to provide national Internet services on a non-exclusive basis. The terms and conditions of our license are generally consistent with the policy for licensing Internet service providers. The term of our license is 15 years. Our license can be revoked by the DOT if we breach the terms and conditions of the license. The DOT retains the right to take over our network and to modify, revoke, terminate or suspend the terms and conditions of the license at any time if, in its opinion, it is necessary or expedient to do so in the interest of general public, or for the proper operation of the telecommunications sector or for security considerations. The DOT also retains the right to review the terms of our license based on changes in national telecommunications policy. We are not allowed to assign or transfer our rights under our license without the prior written consent of the DOT.

Government of India policies permit a maximum level of foreign equity investment of 74% in Internet service providers having their own gateways. Our license was reissued in April 2002, allowing us a maximum level of foreign equity investment of 74% and also permitting us to provide VoIP, subject to the terms of operation as detailed in the license. We currently do not own any international gateways and are technically permitted to have a 100% foreign holding in our company, subject to government regulations.

Our license also requires us to ensure that objectionable, obscene and unauthorized content, or any other content, messages or communications infringing copyrights, intellectual property rights and domestic and international cyber laws or which is inconsistent with the laws of India, is not carried on our network. Although under the terms of our license we are free to fix the prices we charge our subscribers, the TRAI may set prices for the provision of Internet access services generally. We are permitted to use encryption to safeguard information transmitted over our network. However, if we use a higher level of encryption than that specified by the Government of India, our license requires us to deposit a set of keys with the Government of India. License fees were waived through October 31, 2003, and a nominal license fee of Re.1 per annum is payable from November 1, 2003. Our

obligations under the license are secured by a performance bank guarantee in the amount of Rs.10 million (\$0.2 million) as of March 31, 2006.

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In December 2004, the Government of India through DOT imposed new requirements on Internet Service Providers wishing to offer Virtual Private Network services. Consequently, we applied for permission to offer VPN services, and the DOT, Government of India issued a letter of intent to us on December 30, 2004 regarding amendment of our existing ISP license to include provision of VPN services. In January 2005, we paid a Rs.100 million one time entry fee and submitted a financial bank guarantee of Rs.10 million as required by the letter of intent.

On January 11, 2005, we received provisional permission from the DOT, Government of India to offer VPN service in accordance with the new requirements. Final permission to offer VPN service shall be effective only after we sign the amendment to the license agreement. However the provisional permission does not carry any terms and conditions relating to the license.

The Indian Department of Telecommunications, or DOT, also requires ISP licensees to pay an annual fee of 8% of the adjusted gross revenues generated under the ISP license. To date, the DOT has not issued any guidelines or procedures for implementing this decision. However, it is our understanding that the license fee provisions will become effective only after amendments to the license. The Internet Service Provider Association of India, or ISPAI, had filed an appeal against this license with the Telecom Disputes Settlement and Arbitration Tribunal, or TDSAT. TDSAT directed GOI to consult with TRAI before finalizing the license conditions.

We have reserved Rs.24.6 million for the period April 1, 2005 to December 31, 2005 towards the 8% annual fee on VPN revenue as per the provisional IP VPN license and Rs.12.7 million for the period January 1, 2006 to March 31, 2006 towards the 6% annual fee on AGR as per the ILD/NLD license requirement.

*Sponsored ADR Program*

On November 10, 2004, we entered into an agreement with Satyam Computer Services, SAIF and Venture Tech in which we agreed, in part, to facilitate the conversion of our outstanding Indian equity shares into ADSs and to register the ADSs for resale under the U.S. federal securities laws. Pursuant to this agreement, Satyam Computer Services, SAIF, Venture Tech and other holders of our equity shares may dispose of some or all of their equity shares in one or more transactions. A registration statement in Form F-3 had been filed by us on December 7, 2004 which covered 4,538,200 ADSs. The company may file such additional registration statements in the future.

Based on the above, the company had completed four tranches of Sponsored ADR Program and converted 1,130,526, 2,750,000, 11,182,600 and 657,121 shares aggregating to 15,720,247 shares into ADS.

*Subscription Agreement*

Infinity Capital Ventures, LP beneficially owned approximately 42% of our equity shares as of March 31, 2006. This shareholder is a party to the Subscription Agreement with our company dated November 10, 2005. The Subscription Agreement provides for, among other things, the company shall appoint Mr Raju Vegesna as the Chairman of the Board of Directors, Infinity Capital shall also nominate another person in the Board of Sify Limited and so long as Infinity Capital continues to own at least 10% of the Company's outstanding Equity Shares, the Company shall not enter into any agreement pursuant to which it would provide a third party with registration rights for Company securities, without the consent of Infinity Capital.

*Standstill Agreement*

On November 10, 2005, Infinity Capital and Raju Vegesna entered into a Standstill Agreement with us, pursuant to which, upon the terms and subject to the conditions set forth therein, Infinity Capital agreed not to purchase more than 45% of our outstanding fully diluted equity.

*Shareholders Agreement*

On December 20, 2005, Infinity Satcom Universal (P) Limited, or Universal Satcom and Sify Communications Limited, or Sify Communications, the company's subsidiary, entered into an agreement with the company. The agreement provides for, among other things, the company shall transfer 26% of its holding in Sify Communications to Universal Satcom in order to facilitate Sify Communications to comply with the Government of India regulations of having not more than 74% non-resident holding to apply for the licence and provide for the National Long Distance, or NLD and International Long Distance, or ILD services in Telecom sector and also to comply with other regulations.

**Exchange Controls**

*General*

Prior to June 1, 2000, investment in Indian securities was regulated by the Indian Foreign Exchange Regulation Act, 1973. Under Section 29(1)(b) of the Indian Foreign Exchange Regulation Act, 1973, no person or company resident outside India that is not incorporated in India (other than a banking company) could purchase the shares of any company carrying on any trading, commercial or industrial activity in India without the permission of the Reserve Bank of India. Also, under Section 19(1)(d) of the Indian Foreign Exchange Regulation Act, 1973, the transfer and issuance of any security

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of any Indian company to a person resident outside India required the permission of the Reserve Bank of India. Under Section 19(5) of the Indian Foreign Exchange Regulation Act, 1973, no transfer of shares in a company registered in India by a non-resident to a resident of India was valid unless the transfer was confirmed by the Reserve Bank of India upon application filed by the transferor or the transferee. Furthermore, the issuance of rights and other distributions of securities to a non-resident also requires the prior consent of the Reserve Bank of India. However, the Reserve Bank of India has issued notifications over the past few years relaxing the restrictions on foreign investment in Indian companies.

As of June 1, 2000, the Indian Foreign Exchange Regulation Act, 1973 was replaced by the Indian Foreign Exchange Management Act, 1999, or FEMA. The Indian Foreign Exchange Management Act, 1999 contains provisions regarding current account convertibility and amendments to the definition of a resident of India. However, some of the preexisting controls and restrictions on capital account transactions remain in force. While many of the restrictions imposed by the Indian Foreign Exchange Regulation Act, 1973 have been relaxed under this new legislation, the RBI continues to exercise control over capital account transactions, which alter the assets or liabilities, including contingent liabilities, of persons. The RBI has issued regulations under FEMA to regulate various kinds of capital account transactions, including aspects of the purchase and issuance of shares of Indian companies. Therefore, transaction involving foreign investment in Indian securities is regulated by the provisions of the Indian Foreign Exchange Management Act, 1999 and continues to be regulated by the Reserve Bank of India.

*ADR Guidelines*

Shares of Indian companies represented by ADSs, subject to sectoral limits and the guidelines issued thereunder, are no longer required to be approved for issuance to foreign investors by the either Ministry of Finance or the Reserve Bank of India under the Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993, as modified from time to time, notified by the Government of India. This change was effected through the guidelines for ADR and GDR issues by Indian companies issued by the Ministry of Finance on January 19, 2000 and a notification issued by the Reserve Bank of India. Hence, we do not require the approval of the Ministry of Finance and the Reserve Bank of India under the Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993. However, we will be required to furnish full particulars of the issue, including the underlying equity shares representing the ADRs, to the Ministry of Finance and the Reserve Bank of India within 30 days of the completion of an offering.

Further, pending utilization of foreign exchange resources raised by issue of ADRs, Indian companies may invest the proceeds in foreign exchange in:

- (a) deposits with or certificates of deposit or other instruments of banks who have been rated not less than A1+ by Standard and Poor or B1 by Moody's for short term obligations;
- (b) deposits with branches outside India of an authorized dealer in India; and
- (c) treasury bill and other monetary instruments with a maturity or unexpired maturity of the instrument of one year or less.

The Issue of Foreign Currency Convertible Bonds and Ordinary Shares Scheme is distinct from other policies or facilities, as described below, relating to investments in Indian companies by foreign investors. The issuance of ADSs pursuant to the Issue of Foreign Currency Convertible Bonds and Ordinary Shares Scheme also affords to owners of ADSs the benefits of Section 115AC of the Indian Income-tax Act, 1961 for purposes of the application of Indian tax law. For additional information, please see [Taxation](#) [Indian Taxation](#).

*Foreign Direct Investment*

Currently, subject to certain exceptions, foreign direct investment and investment by individuals of Indian nationality or origin residing outside India, or non-resident Indians, and overseas corporate bodies at least 60% owned by such persons, or overseas corporate bodies, in Indian companies do not require the specific prior approval of the Foreign Investment Promotion Board, or FIPB, a body formed by the Government of India to negotiate with large foreign companies interested in making long-term investments in India. Furthermore, henceforth no prior approval of the Reserve Bank of India is required although a post-investment declaration in giving details of the foreign investment in the company pursuant to the ADR issue must be filed with the Reserve Bank of India within thirty days of our ADR offering. However, the waiver of approval by the FIPB and the RBI is unavailable in certain industries,

which have been identified by the Government of India. The waiver of approval would not apply in the following cases:

foreign investment in industries that require an industrial license;

foreign investment being more than 24% in the equity capital of manufacturing items reserved for small scale industries;

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all proposals in which the foreign collaboration has a previous venture/tie-up in India in the relevant sector;

all proposals relating to acquisition of shares in an existing company by a foreign investor;

all proposals for investment in the industries specified by the Government of India; and

all proposals for investment in specified industries where the proposed investment is in excess of the sectoral caps specified therein.

In cases where FIPB approval is obtained, no prior approval of the Reserve Bank of India is required, although a declaration in the prescribed form as mentioned above must be filed with the Reserve Bank of India once the foreign investment is made in the Indian company. In cases where no prior approval of the FIPB is required, prior approval of the Reserve Bank of India would also not be required. However, a declaration in the prescribed form giving details of the foreign investment must be filed with the Reserve Bank of India once the foreign investment is made in the Indian company.

In May 1994, the Government of India announced that purchases by foreign investors of ADSs and foreign currency convertible bonds of Indian companies would be treated as foreign direct investment in the equity issued by Indian companies for such offerings.

In November 1998, the Reserve Bank of India issued a notification to the effect that foreign investment in preferred shares will be considered as part of the share capital of a company and the provisions relating to foreign direct investment in the equity shares of a company discussed above would apply. Investments in preferred shares are included as foreign direct investment for the purposes of sectoral caps on foreign equity, if such preferred shares carry a conversion option. If the preferred shares are structured without a conversion option, they would fall outside the foreign direct investment limit.

The discussion on the foreign direct investment regime in India set forth above applies only to a new issuance of shares made by Indian companies, not to a transfer of shares.

Notwithstanding the foregoing, Government of India policies permit a maximum level of foreign equity investment of 74% in Internet service providers having their own international gateways. Our license was reissued in April 2002, allowing us a maximum level of foreign equity investment of 74% and also permitting us to provide VoIP, subject to the terms of operation as detailed in the license. We currently do not own any international gateways and are technically permitted to have 100% foreign holding in our company, subject to government regulations.

*Investment by Non-Resident Indians and Overseas Corporate Bodies*

A variety of special facilities for making investments in India in shares of Indian companies are available to individuals of Indian nationality or origin residing outside India, or non-resident Indians, and to overseas corporate bodies, or OCBs, at least 60% owned by such persons. These facilities permit non-resident Indians and overseas corporate bodies to make portfolio investments in shares and other securities of Indian companies on a basis not generally available to other foreign investors. These facilities are different and distinct from investments by foreign direct investors described above.

Apart from portfolio investments in Indian companies, non-resident Indians and overseas corporate bodies may also invest in Indian companies through foreign direct investments. For additional information, please see

Foreign Direct Investment. Under the foreign direct investment rules, non-resident Indians and overseas corporate bodies may invest up to 100% in high-priority industries in which other foreign investors are permitted to invest only up to 50%, 51%, 74% or 100%, depending on the industry category.

*Investment by Foreign Institutional Investors*

In September 1992, the Government of India issued guidelines which enable foreign institutional investors, including institutions such as pension funds, investment trusts, asset management companies, nominee companies and incorporated/institutional portfolio managers, to make portfolio investments in the securities of listed and unlisted companies in India. Under the guidelines, foreign institutional investors must obtain an initial registration from the Securities and Exchange Board of India to make these investments. Foreign institutional investors must also comply with the provisions of the Securities Exchange Board of India Foreign Institutional Investors Regulations, 1995. When

it receives the initial registration, the foreign institutional investor also obtains general permission from the Reserve Bank of India to engage in transactions regulated under the Indian Foreign Exchange Regulation Act. Together, the initial

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registration and the Reserve Bank of India's general permission enable the registered foreign institutional investor to buy, subject to the ownership restrictions discussed below, and freely sell securities issued by Indian companies whether or not they are listed, to realize capital gains on investments made through the initial amount invested in India, to subscribe or renounce rights offerings for shares, to appoint a domestic custodian for custody of investments held and to repatriate the capital, capital gains, dividends, income received by way of interest and any compensation received towards sale or renunciation of rights offerings of shares. The foreign institutional investor regulations also set out the general obligations and responsibilities and investment conditions and restrictions applicable to foreign institutional investors. One such restriction is that unless the foreign Institutional Investor is registered as a debt fund with the Securities Exchange Board of India, the total investment in equity and equity-related instruments should not be less than 70% of the aggregate of all investments of a foreign institutional investor in India.

Apart from making portfolio investments in Indian companies as described above, foreign institutional investors may direct foreign investments in Indian companies. For additional information, please see Foreign Direct Investment.

*Ownership Restrictions*

The Securities and Exchange Board of India and Reserve Bank of India regulations restrict portfolio investments in Indian companies by foreign institutional investors, non-resident Indians and overseas corporate bodies, all of which we refer to as foreign portfolio investors. The Reserve Bank of India issued a circular in August 1998 stating that foreign institutional investors in aggregate may hold no more than 30% of the equity shares of an Indian company and non-resident Indians and overseas corporate bodies in aggregate may hold no more than 10% of the shares of an Indian company through portfolio investments. Under current Indian law, foreign institutional investors in the aggregate may hold no more than 24% of the equity shares of an Indian company, and non-resident Indians and overseas corporate bodies in aggregate may hold no more than 10% of the shares of an Indian company through portfolio investments. The 24% limit referred to above may be increased to 49% if the shareholders of the company pass a special resolution to that effect. The Reserve Bank of India circular also states that no single foreign institutional investor may hold more than 10% of the shares of an Indian company and no single non-resident Indian or overseas corporate body may hold more than 5% of the shares of an Indian company.

Foreign institutional investors are urged to consult with their Indian legal and tax advisers about the relationship between the foreign institutional investor regulations and the ADSs and any equity shares withdrawn upon surrender of ADSs.

Under the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 approved by the Securities and Exchange Board of India in January 1997 and notified by the Government of India in February 1997, which replaced the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Resolutions, upon the acquisition (directly or indirectly) of more than 5% of the outstanding shares (the aggregate of the existing shares and the newly acquired shares) of a listed public Indian company, a purchaser is required to notify the company, and the company is required to notify all the stock exchanges on which the shares of the company are listed, of the purchaser's shareholdings or voting rights in that company within four working days of (a) the receipt of allotment information or (b) the acquisition of shares or voting rights, as the case may be. Before the acquisition of 15% or more of such shares or a change in control of the company, either by himself or with others acting in concert the purchaser is required to make annual disclosures of the purchaser's holdings in the company and to make an open offer to the other shareholders offering to purchase at least 20% of all the outstanding shares of the company at a minimum offer price as determined pursuant to the new regulations. A purchaser who holds between 15.0% and 75.0% of a company's shares cannot acquire additional shares or voting rights that would entitle the purchaser to exercise an additional 5.0% of the voting rights in any 12 month period unless such purchaser makes a public announcement offering to acquire an additional 20% of the company's shares. Upon conversion of ADSs into equity shares, an ADS holder will be subject to the Takeover Code. The Takeover Code does not apply to purchases involving the acquisition of shares (i) by allotment in a public, rights and preferential issue, (ii) pursuant to an underwriting agreement, (iii) by registered stockbrokers in the ordinary course of business on behalf of customers, (iv) in unlisted companies, (v) pursuant to a scheme of reconstruction or amalgamation or (vi) pursuant to a scheme under Section 18 of the Sick Industrial Companies (Special Provisions) Act, 1985. The Takeover Code does not apply to purchases in the ordinary course of business by public financial

institutions either on their own account or as a pledgee. In addition, the Takeover Code does not apply to the purchase of ADSs so long as they are not converted into equity shares. However, since we are an unlisted company, the provisions of the new regulations will not apply to us. If our shares are listed on an Indian stock exchange in the future, the new regulations will apply to the holders of our ADSs.

Open market purchases of securities of Indian companies in India by foreign direct investors or investments by non-resident Indians, overseas corporate bodies and foreign institutional investors above the ownership levels set forth above require Government of India approval on a case-by-case basis.

**Table of Contents***Voting Rights of Deposited Equity Shares Represented by ADSs*

Holders of ADSs generally have the right under the deposit agreement to instruct the depository bank to exercise the voting rights for the equity shares represented by the related ADSs. At our request, the depository bank will mail to the holders of ADSs any notice of shareholders' meeting received from us together with information explaining how to instruct the depository bank to exercise the voting rights of the securities represented by ADSs.

If the depository bank timely receives voting instructions from a holder of ADSs, it will endeavor to vote the securities represented by the holder's ADSs in accordance with such voting instructions. In the event that voting takes place by a show of hands, the depository bank will cause the custodian to vote all deposited securities in accordance with the instructions received by holders of a majority of the ADSs for which the depository bank receives voting instructions.

Please note that the ability of the depository bank to carry out voting instructions may be limited by practical and legal limitations and the terms of the securities on deposit. We cannot assure you that ADS holders will receive voting materials in time to enable them to return voting instructions to the depository bank in a timely manner. Securities for which no voting instructions have been received will not be voted except as discussed above.

Under Indian law, subject to the presence in person at a shareholder meeting of persons holding equity shares representing a quorum, all resolutions proposed to be approved at that meeting are voted on by a show of hands unless a shareholder present in person at the meeting demands that a poll be taken. Equity shares not represented in person at the meeting, including equity shares underlying ADSs for which a holder has provided voting instructions to the depository bank, are not counted in a vote by show of hands. As a result, only in the event that a shareholder present at the meeting demands that a poll be taken will the votes of ADSs holders be counted. Securities for which no voting instructions have been received will not be voted on a poll.

As a foreign private issuer, we are not subject to the SEC's proxy rules, which regulate the form and content of solicitations by United States-based issuers of proxies from their shareholders. To date, our practice has been to provide advance notice to our ADS holders of all shareholder meetings and to solicit their vote on such matters, through the depository, and we expect to continue this practice. The form of notice and proxy statement that we have been using does not include all of the information that would be provided under the SEC's proxy rules.

**Taxation***Indian Taxation*

*General.* The following relates to the principal Indian tax consequences for holders of ADSs and equity shares received upon withdrawal of such equity shares who are not resident in India, whether of Indian origin or not. We refer to these persons as non-resident holders. The following is based on the provisions of the Income-tax Act, 1961, including the special tax regime contained in Section 115AC and the Issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993. The Income-tax Act is generally amended or changed by amendments carried out through the Finance Act enacted every year as a part of the budget approvals.

This section is not intended to constitute a complete analysis of the individual tax consequences to non-resident holders under Indian law for the acquisition, ownership and sale of ADSs and equity shares. Personal tax consequences of an investment may vary for non-resident holders in various circumstances, and potential investors should therefore consult their own tax advisers on the tax consequences of such acquisition, ownership and sale, including specifically the tax consequences under the law of the jurisdiction of their residence and any tax treaty between India and their country of residence.

*Residence.* For purposes of the Income-tax Act, an individual is considered to be a resident of India during any fiscal year if he or she is in India in that year for:

a period or periods amounting to 182 days or more; or

60 days or more and, in case of a citizen of India or a person of Indian origin, who, being outside India, comes on a visit to India, is in India for 182 days or more effective April 1, 1995 and in each case within the four preceding years has been in India for a period or periods amounting to 365 days or more.

A company is a resident of India if it is registered in India or the control and the management of its affairs is situated wholly in India. A firm or other association of persons is resident in India except where the control and management of its affairs is situated wholly outside India. Individuals, companies, firms and other associations of persons that are not residents of India would be treated as non-residents for purposes of the Income-tax Act.

Fringe Benefit Tax: The Finance Minister of India has recently introduced the FBT that will be levied on employers. Under the FBT, employers will be required to pay a tax of 30% exclusive of applicable surcharge and cess on the taxable value of the fringe benefits or privileges that are provided or deemed to be provided to employees on a collective, rather than individual, basis.. The impact of FBT for the fiscal year ended March 31, 2006 was Rs 20 million.

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*Taxation of Distributions.* The Finance Act, 2003 states that after April 1, 2003, dividend income will be exempt from tax for shareholders and that domestic companies will be liable to pay a dividend distribution tax at the rate of 12.5% plus a surcharge at the time of the distribution. Any distributions of additional ADSs, equity shares or rights to subscribe for equity shares made to non-resident holders with respect to ADSs or equity shares will not be subject to Indian tax. Similarly, the acquisition by a non-resident holder of equity shares upon redemption of ADSs will not constitute a taxable event for Indian income tax purposes. Such acquisition will, however, give rise to a stamp duty as described below under Stamp Duty and Transfer Tax.

*Taxation of Capital Gains.* Any gain realized on the sale of ADSs or equity shares by a non-resident holder to any non-resident outside India is not subject to Indian capital gains tax.

Since our ADS offerings were approved by the Government of India under the Issue of Foreign Currency Convertible Bonds and Ordinary Shares Scheme, non-resident holders of the ADSs have the benefit of tax concessions available under Section 115AC. As a result, gains realized on the sale of ADSs will not be subject to Indian taxation. The effect of the Scheme in the context of Section 115AC is unclear as to whether such tax treatment is available to a non-resident who acquires equity shares outside India from a non-resident holder of equity shares after receipt of the equity shares upon surrender of the ADSs. If concessional tax treatment is not available, gains realized on the sale of such equity shares will be subject to customary Indian taxation on capital gains as discussed below. The Issue of Foreign Currency Convertible Bonds and Ordinary Shares Scheme provides that if the equity shares are sold on a recognized stock exchange in India against payment in Indian rupees, they will no longer be eligible for such concessional tax treatment.

Subject to any relief provided pursuant to an applicable tax treaty, any gain realized on the sale of equity shares to an Indian resident or inside India generally will be subject to Indian capital gains tax. However, the acquisition by non-resident holders of equity shares in exchange for ADSs will not be subject to Indian capital gains tax. Under the Issue of Foreign Currency Convertible Bonds and Ordinary Shares Scheme, the cost of acquisition of equity shares received in exchange for ADSs will be the cost of the underlying shares on the date that the depository gives notice to the custodian of the delivery of the equity shares in exchange for the corresponding ADSs. In the case of companies listed in India, the cost of acquisition of the equity shares would be the price of the equity shares prevailing on the Stock Exchange, Mumbai or the National Stock Exchange on the date the depository gives notice to the custodian of the delivery of the equity shares in exchange for the corresponding ADSs. However, the Issue of Foreign Currency Convertible Bonds and Ordinary Shares Scheme and Section 115AC do not provide for determination of the cost of acquisition for the purposes of computing capital gains tax where the shares of the Indian company are not listed on the Stock Exchange, Mumbai or the National Stock Exchange in India. Therefore, in the case of our company, which is not listed on either the Stock Exchange, Mumbai or the National Stock Exchange, the mode of determination of the cost of acquisition of equity shares is unclear. Therefore, the original cost of acquisition of the ADSs may be treated as the cost of acquisition for the purposes of determining the capital gains tax. According to the Issue of Foreign Currency Convertible Bonds and Ordinary Shares Scheme, a non-resident holder's holding period for purposes of determining the applicable Indian capital gains tax rate in respect of equity shares received in exchange for ADSs commences on the date of the notice of the redemption by the depository to the custodian. The India-U.S. Treaty does not provide an exemption from the imposition of Indian capital gains tax.

Under Section 115AC, taxable gain realized in respect of equity shares held for more than 12 months, or long-term gain, is subject to tax at the rate of 10%. Taxable gain realized in respect of equity shares held for 12 months or less, or short-term gain, is subject to tax at variable rates with a maximum rate of 48%. In addition, non-corporate foreign assesses are subject to a surcharge of 5.0%. The actual rate of tax on short-term gain depends on a number of factors, including the residential status of the non-resident holder and the type of income chargeable in India.

*Buy-back of Securities.* Currently, Indian companies are not subject to any tax in respect of the buy-back of their shares. However, the shareholders will be taxed on any gain at the long-term or short-term, as applicable, capital gains rates. For additional information, please see Taxation of Capital Gains.

*Stamp Duty and Transfer Tax.* Upon issuance of the equity shares underlying our ADSs, we are required to pay a stamp duty of 0.1% of the aggregate value of the shares issued, provided that the issue of dematerialized shares is

not subject to Indian stamp duty. A transfer of ADSs is not subject to Indian stamp duty. However, upon the acquisition of equity shares from the depository in exchange for ADSs, the non-resident holder will be liable for Indian stamp duty at the rate of 0.5% of the market value of the equity shares on the redemption date. Similarly upon a sale of shares in physical form, stamp duty at the rate of 0.5% of the market value of the equity shares on the trade date is payable, although customarily such duty is borne by the purchaser. Our equity shares, if and when issued and traded in dematerialized form, are not subject to Indian stamp duty.

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*Wealth Tax.* The holding of the ADSs in the hands of non-resident holders and the holding of the underlying equity shares by the depository as a fiduciary will be exempt from Indian wealth tax. Non-resident holders are advised to consult their own tax advisers in this context.

*Gift Tax and Estate Duty.* Indian gift tax was abolished in October 1998. In India, there is no estate duty law. As a result, no estate duty would be applicable in India. Non-resident holders are advised to consult their own tax advisors in this context.

*Service Tax.* Brokerage or commissions paid to stockbrokers in connection with the sale or purchase of shares is subject to a service tax of 12.24%.

**Income Tax Matters**

As of March 31, 2006, we had a business loss carry forward of approximately Rs.4,535.5 million (\$102.0 million) for financial reporting purposes. Under Indian law, loss carry forwards from a particular year may be used to offset taxable income over the next eight years.

The statutory corporate income tax rate and the surcharge thereon are subject to change in line with the changes announced in the Union Budget each year. For the fiscal ended 2005, the rate of corporate income tax was 35% plus a surcharge of 2.5% and 2% education cess thereon, resulting in an effective tax rate of 36.6%. For fiscal year 2006, the corporate income tax rate has been reduced to 30%, subject to a surcharge of 10% and education cess of 2%, resulting in an effective tax rate of 33.7%. We cannot assure you that the current income tax rate will remain unchanged in the future. We also cannot assure you that the surcharge will be in effect for a limited period of time or that additional surcharges will not be levied by the Government of India. Until April 1, 2002, dividends declared, distributed or paid by an Indian corporation were subject to a dividend tax of 10.2%, including the applicable surcharge for fiscal 2002, of the total amount of the dividend declared, distributed or paid. This tax is not paid by shareholders nor is it a withholding requirement, but rather it is a direct tax payable by the corporation before distribution of a dividend. Effective April 1, 2002, Indian companies were no longer to be taxed on declared dividends. The Finance Act, 2003 proposed that after April 1, 2003, dividend income will be exempt from tax for shareholders and that domestic companies will be liable to pay a dividend distribution tax at the rate of 12.5% plus a surcharge at the time of the distribution.

*United States Federal Taxation*

The following is a summary of the material U.S. federal income and estate tax consequences that may be relevant with respect to the acquisition, ownership and disposition of equity shares or ADSs. This summary addresses the U.S. federal income and estate tax considerations of holders that are U.S. persons, *i.e.*, citizens or residents of the United States, partnerships or corporations created in or under the laws of the United States or any political subdivision thereof or therein, estates, the income of which is subject to U.S. federal income taxation regardless of its source and trusts for which a U.S. court exercises primary supervision and a U.S. person has the authority to control all substantial decisions and that will hold equity shares or ADSs as capital assets. We refer to these persons as U.S. holders. This summary does not address tax considerations applicable to holders that may be subject to special tax rules, such as banks, insurance companies, dealers in securities or currencies, tax-exempt entities, persons that hold equity shares or ADSs as a position in a straddle or as part of a hedging or conversion transaction for tax purposes, persons that have a functional currency other than the U.S. dollar or holders of 10% or more, by voting power or value, of the stock of our company. This summary is based on the tax laws of the United States as in effect on the date of this annual report and on United States Treasury Regulations in effect or, in some cases, proposed, as of the date of this annual report, as well as judicial and administrative interpretations thereof available on or before such date and is based in part on representations of the depository and the assumption that each obligation in the deposit agreement and any related agreement will be performed in accordance with its terms. All of the foregoing are subject to change, which change could apply retroactively and could affect the tax consequences described below.

Each prospective investor should consult his, her or its own tax advisor with respect to the U.S. Federal, state, local and foreign tax consequences of acquiring, owning or disposing of equity shares or ADSs.

*Ownership of ADSs.* For U.S. federal income tax purposes, holders of ADSs should be treated as the owners of equity shares represented by such ADSs. However, the United States Treasury had expressed concerns that parties to whom ADSs are pre-released may be taking actions inconsistent with the claiming of the reduced rate of tax

applicable to dividends received by certain non-corporate holders, as described below. Accordingly, the availability of the lower rate of tax applicable to dividends could be affected by actions that may be taken by the United States Treasury.

*Dividends.* Subject to special rules discussed below governing passive foreign investment companies, distributions of cash or property (other than equity shares, if any, that are distributed pro rata to all shareholders of our company, including holders of ADSs, and also meet certain conditions) with respect to equity shares will be includible in income by a U.S. holder as foreign source dividend income at the time of receipt, which in the case of a U.S. holder of ADSs generally will be the date of receipt by the depositary, to the extent such distributions are made from the current or

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accumulated earnings and profits of our company as determined under U.S. federal income tax principles. Such dividends will not be eligible for the dividends received deduction generally allowed to corporate U.S. holders. To the extent, if any, that the amount of any distribution by our company exceeds our company's current and accumulated earnings and profits, it will be treated first as a tax-free return of the U.S. holder's tax basis in the equity shares or ADSs and thereafter as capital gain. With respect to non-corporate taxpayers for taxable years beginning before January 1, 2009, dividends may be taxed at the lower applicable capital gains rate provided that (1) ADSs or equity shares are readily tradable on an established securities market in the United States, (2) we are not a passive foreign investment company (as discussed below) for either our taxable year in which the dividend is paid or the preceding taxable year, and (3) certain holding period requirements are met.

It is not clear if any Indian tax imposed upon distributions paid to a U.S. holder with respect to ADSs or equity shares would be eligible for credit against the U.S. holder's federal income tax liability (or alternatively, a deduction in computing taxable income). Dividends paid by our company generally will constitute passive income for purposes of the foreign tax credit (or, in the case of certain holders, financial services income).

If dividends are paid in Indian rupees, the amount of the dividend distribution includible in the income of a U.S. holder will be in the U.S. dollar value of the payments made in Indian rupees, determined at a spot exchange rate between Indian rupees and U.S. dollars applicable to the date of distribution, regardless of whether the payment is in fact converted into U.S. dollars. Generally, gain or loss, if any, resulting from currency exchange fluctuations during the period from the date the dividend is paid to the date such payment is converted into U.S. dollars will be treated as ordinary income or loss.

*Sale or Exchange of equity shares or ADSs.* A U.S. holder generally will recognize gain or loss on the sale or exchange of equity shares or ADSs equal to the difference between the amount realized on such sale or exchange and the U.S. holder's tax basis in the equity shares or ADSs. Subject to special rules described below governing passive foreign investment companies, such gain or loss will be capital gain or loss, and will be long-term capital gain or loss if the equity shares or ADSs were held for more than one year. Gain or loss, if any, recognized by a U.S. holder generally will be treated as U.S. source gain or loss for U.S. foreign tax credit purposes. The deductibility of capital losses may be subject to limitation.

*Estate Taxes.* An individual shareholder who is a citizen or resident of the United States for U.S. federal estate tax purposes will have the value of the equity shares or ADSs owned by such holder included in his or her gross estate for U.S. federal estate tax purposes.

*Passive Foreign Investment Company.* A non-U.S. corporation will be classified as a passive foreign investment company for U.S. Federal income tax purposes if either:

75% or more of its gross income for the taxable year is passive income; or

on a quarterly average for the taxable year by value (or, if it is not a publicly traded corporation and so elects, by adjusted basis) 50% or more of its assets produce or are held for the production of passive income.

We do not believe that we satisfy either of the tests for passive foreign investment company status. If we were to be a passive foreign investment company for any taxable year, U.S. holders would be required to either:

pay an interest charge together with tax calculated at maximum ordinary income rates on excess distributions, which is defined to include gain on a sale or other disposition of equity shares;

if a qualified electing fund election is made, include in their taxable income their pro rata share of undistributed amounts of our income; or

if the equity shares are marketable and a mark-to-market election is made, mark-to-market the equity shares each taxable year and recognize ordinary gain and, to the extent of prior ordinary gain, ordinary loss for the increase or decrease in market value for such taxable year.

*Backup Withholding Tax and Information Reporting Requirements.* Dividends paid on equity shares to a holder who is not an exempt recipient, if any, may be subject to information reporting and, unless a holder either furnishes its

taxpayer identification number or otherwise establishes an exemption, may also be subject to U.S. backup withholding tax. In addition, information reporting will apply to payments of proceeds from the sale or redemption of equity shares or ADSs by a paying agent, including a broker, within the United States to a U.S. holder, other than an exempt recipient. An exempt recipient includes a corporation. In addition, a paying agent within the United States will be required to withhold 31% of any payments of the proceeds from the sale or redemption of equity shares or ADSs within the United States to a holder, other than an exempt recipient, if such holder fails to furnish its correct taxpayer identification number or otherwise fails to comply with such backup withholding requirements.

The above summary is not intended to constitute a complete analysis of all tax consequences relating to ownership of equity shares or ADSs. You should consult your own tax advisor concerning the tax consequences of your particular situation.

**Table of Contents****Item 11. Quantitative and Qualitative Disclosures About Market Risk**

Fair value estimates are made at a specific point in time and are based on relevant market information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

We also face market risk relating to foreign exchange rate fluctuations, principally relating to the fluctuation of U.S. dollar to Indian rupee exchange rate. Our foreign exchange risk principally arises from accounts payable to overseas vendors. This risk is partially mitigated as we hold balances in foreign currency with overseas banks. Our foreign exchange gain/(loss) was Rs.(52.1) million, Rs.2.6 million and Rs.23.2 million for fiscal years 2004, 2005 and 2006, respectively.

**Item 12. Description of Securities Other Than Equity Securities**

Not applicable.

**PART II****Item 13. Defaults, Dividend Arrearages and Delinquencies**

Not applicable.

**Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds**

Under the Indian Companies Act, 1956 of India, or Indian Companies Act, a company incorporated in India must offer its holders of equity shares preemptive rights to subscribe and pay for a proportionate number of shares to maintain their existing ownership percentages prior to the issuance of any new equity shares, unless the preemptive rights have been waived by adopting a special resolution by holders of three-fourths of the company's shares which are voted on the resolution. At our 2000 Annual General Meeting, our shareholders approved a special resolution permitting us to issue up to one million equity shares in connection with acquisitions. We issued virtually all of these equity shares in connection with our acquisitions of IndiaWorld Communications and Indiaplaza.com and our investment in CricInfo Limited. At our 2001 Annual General Meeting, our shareholders approved a special resolution permitting us to issue up to four million additional equity shares in connection with acquisitions or capital raising transactions, and ADS holders are deemed to have waived their preemptive rights with respect to these shares. At our December 2002 Extraordinary General Meeting, our shareholders approved a special resolution permitting us to issue up to 12.5 million additional equity shares in connection with the sale of equity shares to SAIF and VentureTech, and our ADS holders are deemed to have waived their preemptive rights with respect to these shares. Our Board approved the issue of 11.6 million shares out of the 12.5 million approved by the shareholders. Out of this, 8.6 million was issued as ADSs and 3.0 million as Indian equity shares. We raised \$14.7 million and Rs.253.4 million through the ADS issue and Indian equity share issue respectively. Of the \$14.7 million in proceeds from the ADS issue, \$12.3 million is available as cash, \$1.2 million was used for investments in affiliates, \$0.5 million was expended on U.S. branch operations and \$0.7 million was expended on other operating expenses. The total amount of Rs.253.4 million raised by way of issue of Indian equity shares is available as cash. At our Extraordinary General Meeting held in December 2005, our shareholders approved a special resolution permitting us to issue up to 6,720,260 additional equity shares (equivalent to 6.72 million ADSs) in connection with the acquisition of additional shares by Infinity Capital, as per the Subscription Agreement dated November 10, 2005 executed by the company with them. We raised \$37.20 million from the ADS issue.

**Item 15. Controls and procedures***Evaluation of disclosure controls and procedures*

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the U.S. Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, to allow timely decisions regarding required disclosures. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and, in reaching a reasonable level of assurance, management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Also, we have investments in certain

unconsolidated entities. As we do not control or manage these entities, our disclosure controls and procedures with respect to such entities are necessarily substantially more limited than those we maintain with respect to our consolidated subsidiaries.

**Table of Contents****Management's annual report on internal control over financial reporting**

We have carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer, Chief Financial Officer and other senior management personnel, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, our management, including our Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of March 31, 2006, in order to provide reasonable assurance that the information required to be disclosed in filings and submissions under the Securities Exchange Act of 1934, as amended, were recorded, processed, summarized, and reported within the time periods specified by the U.S. Securities and Exchange Commission's rules and forms, and that material information related to us and our consolidated subsidiaries was accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions about required disclosure.

**Changes in internal controls**

There were no changes in our internal controls over financial reporting that occurred during the fiscal year ended March 31, 2006, the period covered by this Annual Report on Form 20-F, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Item 16A. Audit Committee financial expert**

Mr. C. B. Mouli, a member of our audit committee, is independent as per the SEC and NASDAQ rules, conforms to the requirements to be an audit committee financial expert under the SEC's definition and he was appointed by the Board as the Audit Committee Financial Expert effective July 15, 2005.

**Item 16B. Code of Ethics**

The Company has adopted a Code of Conduct and Conflict of Interest Policy that is applicable to all officers, directors and employees. The text of the policy was filed as an Exhibit under Item 19 to the Annual Report for the year ended March 31, 2005. This policy is available on our website, [www.sifycorp.com](http://www.sifycorp.com).

**Item 16C. Principal Accountant Fees and Services**

The following table sets forth for the fiscal years indicated the fees paid to our principal accountant and its associated entities for various services provided us in these periods.

Type of Service	Fiscal year ended	
	march 31, 2005	march 31, 2006
(a) Audit Fees	Rs.7.4 million	Rs.7.8 million
(b) Audit Related Fees	Nil	Nil
(c) Tax Fees	Nil	Nil
(d) All Other Fees	Nil	Nil

Fees include out of pocket expenses and applicable taxes.

Our Audit Committee requires pre-approval of all audit and permissible non-audit services to be performed for the company by its independent auditors, subject to the de-minimus exception for non-audit services described in Section 10A(i)(1)(B) of the Securities Exchange act of 1934.

**Item 16D. Exemptions from the Listing Standards for Audit Committees**

Not applicable.

**Item 16E. Purchase of Equity Securities by the Issuer and Affiliated Purchasers**

None.

**PART III****Item 17. Financial Statements**

Not applicable.

**Item 18. Financial Statements**

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**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders Sify Limited

We have audited the accompanying consolidated balance sheets of Sify Limited and subsidiaries as of March 31, 2006 and 2005, and the related consolidated statements of operations, stockholders' equity and comprehensive income, and cash flows, for each of the years in the three-year period ended March 31, 2006. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sify Limited and subsidiaries as of March 31, 2006 and 2005, and the results of their operations and their cash flows for each of the years in the three-year period ended March 31, 2006, in conformity with U.S. generally accepted accounting principles.

The accompanying consolidated financial statements as of and for the year ended March 31, 2006 have been translated into United States dollars solely for the convenience of the reader. We have audited the translation and, in our opinion, the consolidated financial statements expressed in Indian Rupees have been translated into dollars on the basis set forth in Note 2 of the notes to the consolidated financial statements.

/s/ KPMG

KPMG

India

April 20, 2006

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**SIFY LIMITED and Subsidiaries**  
**CONSOLIDATED BALANCE SHEETS**  
(in thousands, except share data and as otherwise stated)

	As at March 31, 2005 Rs.	As at March 31, 2006 Rs.	2006 \$
<b>ASSETS</b>			
<b>Current assets:</b>			
		Rs.	
Cash and cash equivalents	Rs. 1,323,912	2,822,501	\$ 63,456
Cash restricted	24,904		
Accounts receivable	615,286	838,433	18,850
Due from employees	2,063	23,818	535
Due from related parties	33,524		
Inventories	29,194	30,462	685
Prepaid expenses	87,162	91,158	2,049
Net investment in sales-type leases, current portion	9,430	10,776	242
Other current assets	140,285	212,696	4,782
<b>Total current assets</b>	<b>2,265,760</b>	<b>4,029,844</b>	<b>90,599</b>
Cash restricted	7,336	1,000	22
Net investment in sales-type leases	19,735	10,842	244
Property, plant and equipment-net	1,233,628	1,423,246	31,997
Goodwill and other intangible assets	208,725	62,436	1,404
Investments in affiliated companies	192,357	233,060	5,240
Other assets	93,241	191,343	4,302
		Rs.	
<b>Total assets</b>	<b>Rs. 4,020,782</b>	<b>5,951,771</b>	<b>\$ 133,808</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>			
<b>Current liabilities:</b>			
Current installments of capital lease obligations	6,089	2,759	62
Trade accounts payable	454,466	440,841	9,911
Accrued liabilities	393,727	584,264	13,136
Deferred revenue	409,244	444,333	9,990
Due to employees	2,326	1,300	29
Advances from customers	69,429	112,512	2,529
Other current liabilities	117,876	74,174	1,668
<b>Total current liabilities</b>	<b>1,453,157</b>	<b>1,660,183</b>	<b>37,325</b>
Capital lease obligations, excluding current installments	3,814	2,546	57
Other liabilities	63,627	234,533	5,273
<b>Total liabilities</b>	<b>1,520,598</b>	<b>1,897,262</b>	<b>42,655</b>

**Minority interest** 1,595

**Shareholders equity**

Common stock, Rs 10 par value; 50,000,000 equity shares authorized (2005 37,500,000); Issued and outstanding: 42,389,514 shares as of March 31, 2006 and 35,380,278

shares as of March 31, 2005	353,803	423,895	9,530
Additional paid-in capital	14,564,831	16,238,413	365,073
Deferred compensation employee stock offer plan	(3,416)	(41,925)	(944)
Accumulated deficit	(12,416,624)	(12,565,874)	(282,506)
<b>Total shareholders equity</b>	<b>2,498,589</b>	<b>4,054,509</b>	<b>91,153</b>

<b>Total liabilities and shareholders equity</b>	<b>Rs. 4,020,782</b>	<b>Rs. 5,951,771</b>	<b>\$ 133,808</b>
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See accompanying notes to consolidated financial statements

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**SIFY LIMITED and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in thousands, except share data and as otherwise stated)

	<b>Year ended March 31,</b>			
	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2006</b>
	<b>Rs.</b>	<b>Rs.</b>	<b>Rs.</b>	<b>\$</b>
Revenue				
Products	Rs. 238,226	Rs. 402,391	Rs. 343,712	\$ 7,727
Services	2,513,397	3,151,846	4,262,697	95,834
	Rs.	Rs.	Rs.	
	2,751,623	3,554,237	4,606,409	\$ 103,561
Revenue from related parties				
Products	6,175	8,532	43,879	986
Services	43,386	50,688	31,519	709
	49,561	59,220	75,398	1,695
<b>Total Revenue</b>	<b>2,801,184</b>	<b>3,613,457</b>	<b>4,681,807</b>	<b>105,256</b>
Cost of revenue				
Products	213,957	357,753	324,411	7,293
Services	1,262,757	1,666,189	2,210,312	49,692
	1,476,714	2,023,942	2,534,723	56,985
Selling, general and administrative expenses	1,208,884	1,418,757	1,852,296	41,643
Provision for doubtful receivables and advances	76,487	57,579	90,670	2,038
Impairment of assets	22,551			
Depreciation	432,684	472,400	395,018	8,881
Amortisation of intangible assets	99,350	84,387	68,759	1,546
Amortisation of deferred stock compensation expense	27,946	10,639	12,749	287
Foreign exchange (gain) / loss	52,148	(2,595)	(23,221)	(522)
<b>Total operating expenses</b>	<b>3,396,764</b>	<b>4,065,109</b>	<b>4,930,994</b>	<b>110,858</b>
Operating loss	(595,580)	(451,652)	(249,187)	(5,602)
Other income, net	144,147	93,324	59,239	1,332
Loss before taxes and equity in profits of affiliates	(451,433)	(358,328)	(189,948)	(4,270)
Equity in profit of affiliate	17,083	50,752	40,703	915
Gain on sale of investment in affiliates	63,059			

Minority interest	79			
Loss before income taxes	(371,212)	(307,576)	(149,245)	(3,355)
Income taxes	(72)			
<b>Net loss</b>	<b>Rs.(371,284)</b>	<b>Rs.(307,576)</b>	<b>Rs.(149,245)</b>	<b>\$ (3,355)</b>
<b>Net loss per equity share (basic and diluted)</b>	(10.76)	(8.75)	(4.05)	(0.09)
<b>Basic and diluted weighted average equity shares used in computing loss per equity share</b>	34,519,545	35,156,120	36,811,476	36,811,476

See accompanying notes to consolidated financial statements

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**SIFY LIMITED and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME**  
(in thousands, except share data and as stated otherwise)

	Common Stock		Additional	Accumulated	Deferred Compensation	-	Accumulated	Total
	Shares	Par Value	Paid Capital	Comprehensive Income	Comprehensive Income	Other Employee Stock Offer Plan	Deficit	Stockholders Equity
	Nos.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
<b>Balance as of March 31, 2003</b>	32,795,200	327,952	14,326,742		(3,390)	(24,839)	(11,737,769)	2,888,696
Issue of common stock	2,105,793	21,058	145,862					166,920
Compensation related to stock option grants			21,497			(21,497)		
Amortization of compensation related to stock option grants			(4,064)			32,010		27,946
Comprehensive income								
Net loss				(371,284)			(371,284)	(371,284)
Other comprehensive income								
Unrealized loss on investments, net				2,129	2,129			2,129
Foreign exchange translation adjustment				1,261	1,261			1,261
Comprehensive income				(367,894)				
<b>Balance as of March 31, 2004</b>	34,900,993	349,010	14,490,037			(14,326)	(12,109,053)	2,715,668
	479,285	4,793	73,968					78,761

Issue of common stock							
Compensation related to stock option grants			2,287		(2,287)		
Amortization of compensation related to stock option grants			(2,558)		13,197		10,639
SAB 51 gain			1,097				1,097
Comprehensive income							
Net loss			(307,576)		(307,576)		(307,576)
Comprehensive income			(307,576)				
<b>Balance as of March 31, 2005</b>	35,380,278	353,803	14,564,831		(3,416)	(12,416,629)	2,498,589
Issue of common stock	7,009,236	70,092	1,622,324				1,692,416
Compensation related to stock option grants			55,143		(55,143)		
Amortization of compensation related to stock option grants			(3,885)		16,634		12,749
Comprehensive income							
Net loss			(149,245)		(149,245)		(149,245)
Comprehensive income			(149,245)				
<b>Balance as of March 31, 2006</b>	42,389,514	423,895	16,238,413		(41,925)	(12,565,874)	4,054,509
<b>Balance as of March 31, 2006 (in US\$)</b>	42,389,514	9,530	365,073		(944)	(282,506)	91,153

See accompanying notes to consolidated financial statements.

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**SIFY LIMITED and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands, except share data and as otherwise stated)

	Year ended March 31,			
	2004	2005	2006	2006
	Rs.	Rs.	Rs.	\$
<b>Cash Flows from operating activities:</b>				
<b>Net loss</b>	<b>Rs. (371,284)</b>	<b>Rs. (307,576)</b>	<b>Rs. (149,245)</b>	<b>\$ (3,355)</b>
Adjustments to reconcile net loss to net cash provided by operating activities:				
Depreciation, impairment and amortization of intangible assets and deferred stock compensation	582,531	567,426	471,711	10,608
Equity in profit of affiliate	(17,083)	(50,752)	(40,703)	(915)
Gain on sale of investment	(98,948)	(15,710)		
Gain on sale of investment in affiliates	(63,059)			
Loss / (gain) on sale of property, plant and equipment	(1,990)	2,757	1,662	37
Provision for doubtful receivables and advances	76,487	57,579	90,670	2,038
Minority interest	(79)			
Unrealized (gain) / loss on account of exchange differences		)	(709)	(16)
Translation (gain) / loss on cash and cash equivalents	47,063	(1,479)	(20,558)	(462)
Gain on disposal of subsidiary			(1,595)	(36)
<i>Changes in assets and liabilities:</i>				
Accounts receivable	(223,074)	(178,885)	(279,853)	(6,292)
Due from employees	4,870	4,250	(23,952)	(537)
Due from related parties	2,986	(20,494)		
Inventories	22,894	(8,435)	(1,268)	(29)
Prepaid expenses	17,828	19,795	(3,996)	(90)
Other assets	43,034	(26,246)	(69,335)	(1,559)
Net investment in sales-type leases		(29,165)	7,547	170
Trade accounts payable and accrued liabilities	120,621	310,643	177,185	3,983
Deferred revenue	52,656	67,291	35,089	789
Advances from customers	57,499	(14,241)	43,070	968
Other liabilities	(42,026)	74,194	(12,606)	(283)
<b>Net cash provided by operating activities</b>	<b>Rs. 210,926</b>	<b>Rs. 450,952</b>	<b>Rs. 223,114</b>	<b>\$ 5,016</b>
<b>Cash flows from investing activities:</b>				
Expenditure on property, plant and equipment	(342,584)	(533,197)	(587,455)	(13,207)
Proceeds from sale of property, plant and equipment	12,955	15,200	4,922	111
Expenditure on intangible assets	(2,331)	(100,000)	(17,655)	(397)

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Proceeds from sale of investment in affiliates	56,737			
Expenditure on acquisition of minority interest	(940)			
Net movement in cash restricted	62,889	79,493	31,240	702
Purchase consideration for acquisition, net of cash acquired	(32,755)			
Proceeds from sale of investments	320,415	15,000		
Advances towards sale of investments			139,810	3,143
<b>Net cash provided by / (used in) investing activities</b>	<b>Rs. 74,386</b>	<b>Rs. (523,504)</b>	<b>Rs. (429,138)</b>	<b>\$ (9,648)</b>
<b>Cash flows from financing activities:</b>				
Acquisition related debt	30,355			
Principal payments under capital lease obligations	(7,317)	(9,579)	(8,361)	(188)
Net proceeds from issuance of common stock	166,920	78,761	1,692,416	38,049
<b>Net cash provided by financing activities</b>	<b>Rs. 189,958</b>	<b>Rs. 69,182</b>	<b>Rs. 1,684,055</b>	<b>\$ 37,861</b>
Effect of exchange rate changes on cash and cash equivalents	(47,063)	1,479	20,558	462
<b>Net increase / (decrease) in cash and cash equivalents</b>	<b>428,207</b>	<b>(1,891)</b>	<b>1,498,589</b>	<b>33,692</b>
<b>Cash and cash equivalents at the beginning of the year</b>	<b>897,596</b>	<b>1,325,803</b>	<b>1,323,912</b>	<b>29,764</b>
<b>Cash and cash equivalents at the end of the year</b>	<b>Rs. 1,325,803</b>	<b>Rs. 1,323,912</b>	<b>Rs. 2,822,501</b>	<b>\$ 63,456</b>
<b>Supplementary Information</b>				
Cash paid towards interest	2,126	832	11,090	249
Cash paid / (refund received) towards income taxes	(29,468)	12,698	(11,643)	(262)
Additions to property, plant and equipment represented by capital lease obligations	9,737	7,272	3,637	82
Reversal of minority interest pursuant to disposal of subsidiary.			1,595	

See accompanying notes to consolidated financial statements

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**SIFY LIMITED and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(In thousands, except share data and as as stated otherwise)**

**1. Description of business**

Sify Limited (Sify) together with its subsidiaries (the Company) and its affiliates is engaged in providing various services, such as Corporate Network and Data Services, Internet Access Services, Online Portal and Content Offerings and selling products related to such services.

**2. Summary of significant accounting policies**

*Basis of preparation of financials statements*

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) in Indian Rupees (Rs.), the national currency of India. Solely for the convenience of the reader, the financial statements as of and for the year ended March 31, 2006 have been translated into United States dollars at the noon buying rate in New York City on March 31, 2006 for cable transfers in Indian rupees, as certified for customs purposes by the Federal Reserve Bank of New York of U.S. \$1 = Rs.44.48. No representation is made that the Indian rupee amounts have been, could have been or could be converted into United States dollars at such a rate or at any other rate on March 31, 2006 or at any other date.

*Use of estimates*

In conformity with U.S. GAAP, management of the Company has made a number of estimates and assumptions relating to the reporting of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements. Some of the more significant estimates include allowances for doubtful accounts, depreciation and amortization of long-lived assets and the valuation allowance for deferred tax assets. Actual results could differ from those estimates.

*Principles of consolidation*

The consolidated financial statements of Sify include financial statements of its majority-owned subsidiaries, which are more than 50% owned and where Sify is able to exercise control over the operating and financial policies of the investees. All inter-company accounts and transactions are eliminated on consolidation.

*Investments in affiliates*

The Company accounts for investments between 20% and 50% or where it would be otherwise able to exercise significant influence over the operating and financial policies of the investees under the equity method. In accordance with Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets* (SFAS No. 142), the excess of cost of the stock of those affiliates over the Company's share of their net assets at the acquisition date is recognized as goodwill, which is tested for impairment periodically and diminution in value, if any, is provided for through a charge in the statement of operations. In accordance with Accounting Principles Board (APB) Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*, the Company recognizes a loss when there is a loss in value in the equity method investment, which is other than a temporary decline.

*Cash and cash equivalents*

Cash and cash equivalents currently consist of cash and cash on deposit with banks, which are unrestricted as to its use.

*Revenue recognition*

The operating segments of the Company are:

Corporate network/data services, which provides Internet,connectivity,security and consulting,hosting and managed service solutions;

Internet access services, from homes and through cybercafes;

Online portal services and content offerings; and

Other services, such as development of e-learning software.

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These segments recognize revenues on the following basis:

**Corporate network/data services**

Corporate network service revenues primarily include connectivity services and, to a lesser extent, the revenues from the sale of hardware and software purchased from third party vendors, installation of the link, and other ancillary services such as e-mail, fax and domain registration. Generally, these elements are sold as a package consisting of all or some of the elements. These multiple element arrangements are recognized as separable elements because each element constitutes a separate earnings process, each element has a fair value that is reliable, verifiable and objectively determinable, and the undelivered element is not essential to functionality of the delivered elements. In this arrangement involving delivery of multiple elements, in accordance with EITF Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables* (EITF 00-21), the units of accounting are determined based on whether the delivered items have a value to the customer on a stand alone basis, whether there is objective and reliable evidence of fair value of the undelivered elements and if the arrangement includes a general right of return relative to the delivered item, whether delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the Company. The arrangement consideration is allocated to the units of accounting based on their fair values. Revenue on delivered items is recognized when the revenue recognition criteria applicable to that unit of accounting are met.

The Company provides connectivity for a fixed period of time at a fixed rate regardless of usage. Connectivity is the last element that is provided in the case of a bundled contract. The connectivity charges are the same when sold alone or as part of a package. The revenue attributable to connectivity services is recognized ratably over the period of the contract. The hardware and software are standard products that are being freely traded in and purchased from the market, have standard specifications and are not otherwise customized for the specific needs of a customer. The software sold by the Company is off-the-shelf software, such as antivirus utilities and firewalls. The fair value for the hardware and software is available from the market. The revenue attributable to hardware/software is recognized on delivery. Installation consists of commissioning of the last mile connectivity to the customer premises either through the Company's wireless mode of broadband delivery or through the carrier exchange (primarily Bharat Sanchar Nigam Limited, or BSNL, a Government of India entity). However, once commissioned this last mile connectivity can be used by the customer to access any other service provider. The installation normally takes 4-6 weeks. When the customer has such last mile connectivity, the Company does not charge any installation fee. The revenue attributable to the installation of the link is recognized on completion of the installation work. Revenue from ancillary services such as e-mail, fax and domain registration are recognized over the period such facilities are provided. All revenues are shown exclusive of sales tax and service tax and net of applicable discounts and allowances.

Web hosting service revenues primarily include co-location services and connectivity services. On occasion, the Company also sells related hardware/software to its web hosting customers. At all times, such hardware and software belongs to the customer. This hardware and software is purchased from outside vendors and is freely traded in the market. The Company treats each element of the arrangement as a separate earnings process. The value of the hosting service is determined based on vendor specific objective evidence from similar services sold separately by the Company. When hardware and/or software is also included with hosting services and sold as a package the vendor specific objective evidence of the undelivered element is considered to arrive at the residual value of the delivered element. Revenue from hosting services is recognized over the period during which the service is provided.

The Company remotely manages the IT infrastructure of global enterprises from India. The contracts are on time and material basis and revenues are recognized accordingly.

**Internet access services**

Internet access services include Internet access at homes and businesses through dial-up or cable operator and internet access through a network of cybercafés. It also includes revenues from VoIP.

Dial-up Internet access is sold to customers either for a specified number of hours or for an unlimited usage within a specified period of time. Customers purchase user accounts or top-ups that enable them to access the Internet for a specified quantum of usage or for a specified period of time all within a contracted period. The amounts received from customers on the sale of these user accounts or top-ups are not refundable. We recognize revenue from sale of user accounts or top-ups based on usage by the customer (where access is for a specified quantum of usage) and based on time (where access is for a specified period of time). Any unused hours at the end of the contracted period are

recognized as revenue.

VoIP services are mainly provided through VoIP Booths at *iway* cybercafés and to a smaller extent through Cable TV operators, or CTOs, and through multi-dwelling units, or MDUs. The user purchases the packs that enables them to use the Internet telephone facility through CTO and MDUs. Revenue is recognized on the basis of usage by the customer. The customer uses VoIP facilities at the *iway* cybercafés and makes the payment to the extent of usage of the facility. Revenue is recognized on the basis of usage.

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Internet access at homes and businesses through cable networks is provided through a franchised network of cable operators in India. Customers buy user accounts for a specified usage or volume of data transfer or for a specified period of time all within a contracted period. Revenues is recognized on actual usage by customer (where access is for a specified quantum of usage) or based on time (where access is for a specified period of time). Any unused hours at the end of the contracted period are recognized as revenue.

In the case of franchised cybercafé operators, the Company enters into an agreement with the franchisee that establishes the rights and obligations of each party and grants each franchisee a non-exclusive license to operate the cybercafés using the Company's logo, brand and trade names. The cybercafés are owned and operated by the franchisees. The franchisee procures the retail space, invests in furniture, interior decor, personal computers and point of sale signage and employs and trains the franchisee staff. The franchisee is responsible for the maintenance of the premises and interface with customers. The Company provides the complete backend support, including bandwidth, the authentication/usage engine and the billing and collection system.

In the case of franchised cable network operators and franchised cybercafé operators, the Company enters into a standard arrangement with franchisees that provides for the payment of an initial non-refundable franchisee fee in consideration for establishing the franchisee relationship and providing certain initial services. The fee covers the following upfront services rendered by the Company:

- o conducting a market survey and deciding on the best location for the cybercafé or cable head end;
- o installing the broadband receiver equipment on the roof top of the cybercafé or the cable head end and connecting it to one of Sify's broadcasting towers;
- o obtaining the regulatory approvals for clearance of the site for wireless transmission at the allotted frequency range;
- o installing the wiring from the receiver unit to the individual personal computers in the cybercafé or the transmitting equipment in the cable head end;
- o assisting in obtaining facilities, including computers and interiors for the cybercafés; and
- o providing the operations manual with instructions and guidelines for running the cybercafé or distributing Internet access through cable network.

The initial franchisee fee revenue is recognized at the time of commencement of operations by the franchisee, in accordance with SFAS 45, *Accounting for Franchisee Fee Revenue*. Internet access revenue and VoIP revenues are recognized based on usage by the customer

As of March 31, 2006, Sify owned 34 of the 3,307 cybercafés.

The amount of initial franchise fee revenue recognized during the years ended March 31, 2004, March 31, 2005 and March 31, 2006 were Rs.102,130, Rs.107,960 and Rs.104,085, respectively.

### **Online portal services**

The Company enters into contracts with customers to serve advertisements in the portal and the Company is paid on the basis of impressions, click-throughs or leads and in each case the revenue is recognized based on actual impressions/click-throughs/leads delivered. There are no performance obligations or minimum guarantees.

Revenues from commissions earned on electronic commerce transactions are recognized when the transactions are

completed. Revenues from value-added services that are rendered using Sify's mobile telephone short code, 4545 are recognized upon delivery of the content/ring tones to the end subscriber and confirmation by the mobile phone service provider.

### **Other services**

The Company provides e-learning software development services to facilitate web-based learning in various organizations. These customized services vary in size from customer to customer and relate to computer based and web based training in accordance with the customer specification. These services include information presentation, structured, content delivery, content digitization and simulation based training. These services are generally provided on a fixed price basis. The Company believes that the deliverables provided by the Company to its customers in connection with e-learning software development services are of the same nature as the services provided in an arrangement to deliver software that entail significant production, modification or customization of software. The Company's fixed price contracts to provide these services are also similar to contracts for services performed by architects, engineers or architectural engineering design firms as stated in paragraph 13 of SOP 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*. Accordingly, the Company recognizes revenue based on the percentage of completion method from fixed price contracts relating to e-learning software development services.

### *Cost of revenues*

Cost of revenues represents direct operating expenses incurred in earning the revenues consisting of bandwidth cost, salaries, and other direct expenses but excludes depreciation and amortization.

**Table of Contents***Inventories*

Inventories, which comprise of communication hardware, application software and others, are generally stated at the lower of cost as determined using the first-in-first-out method (FIFO), and net realisable value. The Company makes a provision for the slow moving inventory on the basis of age of inventory.

*Sales-type leases*

From time to time, the Company leases certain products sold by the Company to its customers under sales-type lease arrangements. Revenue from sales-type leases is recognized at the inception of the lease. At the time a sales-type lease is consummated, the Company records the gross finance receivable, unearned finance income and the estimated residual value of the leased equipment. Unearned finance income represents the excess of the gross minimum lease payments receivable plus the estimated residual value over the fair value of the equipment. Unearned finance income is recognized as financing income using the interest method over the term of the transaction.

*Property, plant and equipment*

Property, plant and equipment are stated at cost. Plant and equipment under capital leases are stated at the present value of minimum lease payments. In respect of imported capital goods, duty credits receivable from the Government of India ( GOI ) under the Served From India Scheme can be utilized to decrease the Customs duty payable upon import of Capital goods acquired for own use. Such credits are not eligible for refund, transfer or sale to third parties. Accordingly, the fixed assets when imported are capitalized net of such duty credits. The Company computes depreciation for all plant and equipment using the straight-line method. Leasehold improvements are amortized on a straight-line basis over the shorter of the lease term or estimated useful life of the asset. Routine repairs and maintenance costs are expensed as incurred. The estimated useful lives of assets are as follows:

Buildings	28 years
Plant and machinery	5 years
Computer equipment	5 years
Office equipment	5 years
Furniture and fixtures	5 years
Vehicles	5 years

The Company assessed the actual and the expected benefits from use of computers and servers as compared to previous estimates. Based on its assessment, the Company has revised the estimated life for computer equipment from 2 years to 5 years.

Software for internal use is acquired primarily from third-party vendors and is in ready-to-use condition. Costs for acquiring such software are capitalized. Capitalized software costs are amortized on a straight-line basis over the estimated useful life of the software. Software acquired for internal use with estimated useful life of less than one year is expensed upon acquisition. Deposits paid towards the acquisition of plant and equipment outstanding at each balance sheet date and the cost of property, plant and equipment not ready to be put to use are disclosed under Construction-in-progress.

*Goodwill and intangible assets*

Intangible assets with estimable useful lives are amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS Statement No. 144, *Accounting for Impairment or Disposal of Long-Lived Assets*.

In accordance with SFAS No. 142, Goodwill and Other Intangible Assets, all assets and liabilities of the acquired business including goodwill are assigned to the reporting units. The Company does not amortize goodwill but instead tests goodwill for impairment at least annually, using a two step impairment process. The fair value of the reporting unit is first compared to its carrying value. The fair value of reporting units is determined using the income approach based on measurement techniques such as discounted cash flow analyses. If the fair value of the reporting unit exceeds the carrying value of the net assets assigned to that unit, goodwill is not impaired. If the carrying value of the net assets assigned to the reporting unit exceeds the fair value of the reporting unit, then the implied fair value of the reporting unit's goodwill is compared with the carrying value of the reporting unit's goodwill. The implied fair value of goodwill is determined in the same manner as the amount of goodwill recognized in a business combination. If the carrying value of a reporting unit's goodwill exceeds its implied fair value, then an impairment loss equal to the

difference is recorded.

*Foreign currency translations*

The functional and reporting currency of the Company is the Indian Rupee, except that of the United States subsidiary whose functional currency is the U.S. Dollar. The translation of the U.S. Dollar into Indian Rupee is performed for balance sheet accounts using the exchange rate in effect at the balance sheet date and for revenue and expense accounts using a monthly average of the exchange rates for the respective periods. The gains or losses resulting from such translation are reported in other comprehensive income, a separate component of shareholders' equity.

*Foreign currency transactions*

Assets and liabilities denominated in foreign currencies are expressed in the functional currency at the rates of exchange as of the balance sheet date. The unrealized gain or loss resulting from this translation is reflected in the statements of operations. Income and expenses in foreign currencies are expressed in the functional currency at exchange rates prevailing when income is earned or expenses are incurred.

*Earnings per share*

In accordance with SFAS No. 128, *Earnings per Share*, basic earnings per share are computed using the weighted average number of common shares outstanding during the period. Disclosure of diluted earnings per share is not applicable as the potential equity shares are anti-dilutive. The Company's outstanding shares includes shares held with a depositary to represent equity shares underlying the Company's ADSs.

**Table of Contents***Income taxes*

Income taxes are accounted for using the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances are established when necessary to reduce deferred tax assets to the amount considered more likely than not to be realized.

*Retirement benefits to employees**Provident fund*

In accordance with Indian law, all employees receive benefits from a provident fund, which is a defined contribution plan. Both the employee and employer make monthly contributions to the plan, each equal to a specified percentage of employee's basic salary. The Company has no further obligations under the plan beyond its monthly contributions.

*Gratuity*

The Company provides for gratuity, a defined benefit retirement plan (the Gratuity Plan) covering all employees. The Gratuity Plan commenced on April 1, 1997. The plan provides a lump sum payment to vested employees at retirement or termination of employment of an amount based on the respective employee's salary and the years of employment with the Company. The Company provides the gratuity benefit through annual contributions to a fund managed by the Life Insurance Corporation of India (LIC). Under this scheme, the settlement obligation remains with the Company, although the LIC administers the scheme and determines the contribution premium required to be paid by the Company. The Gratuity Plan is accounted for in accordance with SFAS No. 87, *Employers' Accounting for Pensions*.

*Stock-based compensation*

The Company applies the intrinsic-value-based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations including FASB Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation, an interpretation of APB Opinion No. 25*, issued in March 2000, to account for its fixed-plan stock options. Under this method, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. SFAS No. 123 established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic-value-based method of accounting described above, and has adopted only the disclosure requirements of SFAS No. 123 as amended by SFAS No. 148, *Accounting for Stock-Based Compensation - Transition and Disclosure*.

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock based employee compensation.

	<b>Year ended March 31,</b>		
	<b>2004</b>	<b>2005</b>	<b>2006</b>
Net Loss - As reported	Rs. (371,284)	Rs. (307,576)	Rs. (149,245)
Add: Stock based compensation expense included in reported net loss	27,946	10,639	12,749
Less: Total stock based employee compensation expense determined under fair value based method for all awards	65,461	55,025	66,538
Pro forma net loss	(408,799)	(351,962)	(203,034)
Loss Per Share:			
Basic and Diluted - as reported	(10.76)	(8.75)	(4.05)
Basic and Diluted - pro forma	(11.84)	(10.01)	(5.52)

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

	Year ended March 31,		
	2004	2005	2006
Dividend yield	131%		
	to	103.4% to	58.13% to
Expected volatility	157.3%	116.6 %	116.6 %
	4.5%		
	to		
Risk-free interest rate	5.25 %	4.5% to 7.50 %	4.5% to 7.5%
	12-36		
Expected term	months	12-36 months	12-40 months

*Impairment of long-lived assets and long-lived assets to be disposed of*

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, long-lived assets, such as property, plant, and equipment, and purchased intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposal group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

*Gain / Loss on sale of investments*

The gain or loss on sale / disposal of investments in equity for affiliates and subsidiaries are considered as capital in nature and therefore are included directly in the statement of shareholders' equity in accordance with SEC Staff Accounting Bulletin 51.

*Fair value of financial instruments*

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

**Recent Accounting Pronouncements****SFAS No. 123(R)**

In December 2004, the Financial Accounting Standard Board (FASB) issued SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS No. 123R), requiring companies to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. The compensation costs arising out of such awards are required to be recognized over the period during which an employee provides service in exchange for the award. SFAS No.123R provides two alternative adoption methods. The first method is a modified prospective transition method whereby a company would recognize share based employee costs from the beginning of the fiscal period in which the recognition provisions are first applied as if the fair value-based accounting method had been used to account for all employee awards granted, modified, or settled after the effective date and to any awards that were not fully vested as of the effective date. Measurement and attribution of compensation cost for awards that are unvested as of the effective date of SFAS No.123R would be based on the same estimate of the grant-date fair value and the same attribution method used previously under SFAS No.123, *Accounting for Stock Based Compensation* (SFAS No. 123). The second adoption method is a modified retrospective transition method whereby a company would recognize employee compensation cost for periods presented prior to the adoption of SFAS No. 123R in accordance with the original provisions of SFAS No. 123; that is, an entity would recognize employee compensation costs in the amounts reported in the pro forma disclosures provided in accordance with SFAS No. 123;

a company would not be permitted to make any changes to those amounts upon adoption of SFAS No. 123R unless those changes represent a correction of an error. For periods after the date of adoption of SFAS No.123R, the modified prospective transition method described above would be applied. SFAS No.123R does not change the accounting guidance for share-based payment transaction with parties other than employees provided in SFAS No. 123 as originally issued and EITF Issue No 96-18. Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling Goods or Services . SFAS No. 123R is effective for fiscal years beginning after June 15, 2005. SFAS No. 123R applies to all awards granted and to awards modified, repurchased, or cancelled in the fiscal year beginning after June 15, 2005. Pursuant to the Securities and Exchange Commission Release No. 33-8568, the Company is required to adopt SFAS No. 123R and related guidance in the implementation of SFAS No. 123R under Staff Accounting Bulletin (SAB) 107 on Share based payments from April 1, 2006. Upon adoption of SFAS No. 123R the Company will record a cumulative catch-up adjustment to recognize the impact of adjusting compensation charge for estimated forfeitures.

**Table of Contents***Reclassifications*

Certain prior-years amounts have been reclassified to conform to the current year's presentation.

**3. Change in Accounting Estimate**

During the year, the Company assessed the actual and expected benefits from the use of computers and servers as compared to previous estimates. Based on this assessment, the Company revised the estimated life for these assets from 2 years to 5 years. In accordance with Accounting Principles Board Opinion 20, Accounting Changes, the revisions to the estimated life of these fixed assets are considered to be a change in the accounting estimate and, accordingly, are accounted for during the current period. The change in estimated life has resulted in a decrease in depreciation charge and net loss for the year ended March 31, 2006 by Rs. 32,715. Consequently, the net loss per share for the year ended March 31, 2006 is lower by Re.0.89

**4. IP / VPN License**

In December 2004, the Government of India ( GOI ) issued guidelines on offering Virtual Private Network( IP-VPN ) services by Internet Service Providers ( ISPs ). As per the guidelines, the Company paid Rs.100,000 as a one-time entry fee and submitted a financial bank guarantee of Rs.10,000. In addition, the ISP licensees were required to pay an annual fee of 8% of the adjusted gross revenues generated under the ISP license for IP-VPN services. The Company amortized the one-time entry fee over a period of 15 years, up to September 30, 2005 and provided for the annual fee up to December 31, 2005.

On November 10, 2005, the GOI issued guidelines for obtaining National Long Distance ( NLD ) and International Long Distance ( ILD ) licenses including the terms and conditions for the licenses. These guidelines eliminated the IP-VPN license entitling the Company to a full refund of the \$100,000 entry fee, and permitting existing IP-VPN license holders to migrate to the NLD and ILD service licenses effective January 1, 2006. The Company has applied for these licenses and discontinued amortization of the IP-VPN licenses effective November 10, 2005. The Company has accounted for the gain arising from the refund of the IP-VPN license fee as an offset to the amortization charge recorded previously.

As per the ILD and NLD license guidelines, the Company will be required to pay Rs. 50,000 as an entry fee for the ILD and NLD licenses when approval is obtained and submit a bank guarantee of Rs. 25,000 for the ILD license and Rs. 20,000 for the NLD license. This entry fee will be evenly amortized over the license period of 20 years. In addition to the one time entry fee, the Company has to pay an annual license fee of 6% on the Adjusted Gross Revenue generated (AGR) as defined under the ILD and NLD licenses for IP-VPN services effective January 1, 2006.

**Table of Contents****5. Sale of 26% holding in Sify Communications Limited**

The new guidelines issued by the GOI for ILD/NLD licenses limit foreign direct investment ( FDI ) for the telecom sector to 74% of the equity shares outstanding. As the foreign shareholding in Sify is more than the threshold limit, Sify would not be eligible for the NLD/ILD licenses. Accordingly, the Company determined to provide the IP-VPN services through Sify Communications Limited (formerly Safescrypt Limited), a subsidiary of Sify. On December 19, 2005 Sify infused Rs.700,000 as additional equity in Sify Communication Limited to make positive the net worth of Sify Communications Limited. On December 20, 2005, the Company divested 26% of its holding in Sify Communications Limited, or 4,680,000 shares, to M/s Infinity Satcom Universal (P) Ltd for a sale consideration of Rs.139,810. This was a related party transaction because Mr. Raju Vegesna, a member of the Company's Board of Directors, is the brother of Mr Ananda Raju, the owner of Infinity Satcom Universal (P) Ltd. Sify Communications Limited has applied for the ILD/NLD license to provide IP-VPN services.

The Company would be transferring the IP VPN business from Sify Limited to Sify Communications Limited on receipt of ILD / NLD license. Pending transfer of business the Company has not recognized share of profit / loss incurred by Sify Communications Limited attributable to the minority share holders and gain on sale of 26% holding. The amount received against the sale proceeds has been disclosed under the other liabilities. Further, Sify will carry on the IP-VPN business, until the business is transferred to Sify Communications, Limited.

**6. Cash and cash equivalents**

Cash and cash equivalents as on March 31, 2006 amounted to Rs. 2,822,501 (Rs. 1,323,912 as on March 31, 2005). This excludes cash-restricted included in current assets of Rs.Nil (Rs. 24,904 as on March 31, 2005) and cash-restricted included in non-current assets of Rs.1,000 (Rs. 7,336 as on March 31, 2005), representing deposits held under lien against bank guarantees given by the Company towards future performance obligations and letters of credit given to suppliers of the Company against purchase obligations.

**Cash Restricted - Current**

	As at March 31,	
	<b>2005</b>	<b>2006</b>
Against Letter of Credit	Rs.12,409	
Against future performance obligation	12,495	
	Rs.24,904	

**Cash Restricted - Non current**

	As at March 31,	
	<b>2005</b>	<b>2006</b>
Against future performance obligation	Rs.7,336	Rs.1,000
	Rs.7,336	Rs.1,000

The fair values of cash and cash equivalents approximate their carrying values.

**7. Accounts receivable**

Accounts receivable as of March 31, 2005 and 2006 are stated net of allowance for doubtful receivables. The Company maintains an allowance for doubtful receivables based on its age and collectability. Accounts receivable

are not collateralised except to the extent of refundable deposits received from cybercafe s franchisees and from cable television operators (CTO).

Accounts receivables consist of:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Due from customers	724,663	1,038,480
Less: Allowance for doubtful debts	109,377	200,047
Balance at the end of the year	615,286	838,433

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The activity in the allowance for doubtful accounts receivable is given below:

	<b>Years ended March 31,</b>		
	<b>2004</b>	<b>2005</b>	<b>2006</b>
	Rs.	Rs.	Rs.
Balance at the beginning of the year	165,879	52,533	109,377
Add : Additional provision	76,487	57,579	90,670
Less : Bad debts written off	189,833	735	
Balance at the end of the year	52,533	109,377	200,047

**8. Inventories**

Inventories consist of:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Communication hardware	26,600	18,454
Application software	1,696	2,041
Others	898	9,967
	29,194	30,462

**9. Sales-Type Leases**

The Company's leasing arrangement consist of leasing various types of routers, modems and other equipment for establishing virtual private networks and providing bandwidth to its customers in its corporate connectivity business. The leases are classified as sales-type leases and expire after a period of three years.

The following lists the components of the net investment in sales-type leases:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Minimum lease payments receivable	31,930	22,987
Less: Unearned income	2,765	1,339
Net investment in sales-type leases	29,165	21,618

The minimum lease payments receivable for each of the fiscal years are as follows:

For the year ending

March 31,

2007	Rs.11,805
2008	10,851
2009	331
Total	22,987

**Table of Contents****10. Other current assets**

Other current assets consist of:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Vendor advances and deposits	40,898	98,008
Advances for expenses	26,040	2,744
Accrued income	2,284	29,284
Accrued interest	12,491	35,731
Tax deposits	58,572	46,929
	<b>140,285</b>	<b>212,696</b>

Tax deposits represent taxes deducted at source by the customer and paid to the Government of India, which is refundable to the Company.

**11. Investments in affiliates***Man Financial-Sify Securities India Private Limited(Formerly Refco-Sify Securities India Private Limited)*

Prior to the fiscal year ended March 31, 2004, the Company held 40% of the outstanding equity share capital of Refco-Sify Securities India Private Limited (Refco-Sify). During the year ended March 31, 2005, Refco-Sify completed a rights issue, in which the Company chose not to participate. As a result, the Company's equity ownership in Refco-Sify was reduced from 40% to 29.85%. In accordance with the Company's accounting policy, during the year ended March 31, 2005 the Company accounted for a gain on dilution through shareholders' equity amounting to Rs.1,097. The Company accounted its proportionate share of profit in accordance with its applicable equity ownership in Refco-Sify.

In October 2005, Refco Group US ( Refco ), the 70.15% shareholder of Refco-Sify Securities India Private Limited ( Refco-Sify ), sought bankruptcy protection through a Chapter 11 filing at the New York Courts. Consequent to this, the businesses of Refco were under auction process and the auction bid was won by M/s Man Financial Inc. ( Man Financial ). As per the bid, Refco-Sify shares are to be held by Refco. In connection with the purchase of Refco-Sify shares by Man Financial, Man Financial and the Company executed a Shareholders Agreement on November 25, 2005 (the Shareholders Agreement ), pursuant to which, the name of Refco-Sify was changed to Man-Sify Securities India Private Limited ( Man-Sify ).

The carrying value of the investment in Man-Sify as of March 31, 2005 and 2006 was Rs. 192,357 and Rs. 233,060 respectively. Sify's equity in the profit of Man-Sify for the years ended March 31, 2005 and March 31, 2006 was Rs.50,752 and Rs. 40,703 respectively.

The summarised unaudited financial information as to assets, liabilities and results of operations of Man-Sify and its subsidiaries is presented below:

**Balance Sheet**

	As at March 31,	
	2005	2006
	Rs.	Rs.
Current assets	1,760,432	3,431,296
Non-current assets	69,847	82,656
<i>Total assets</i>	<i>1,830,279</i>	<i>3,513,952</i>
Current liabilities	1,185,618	2,733,183
Other liabilities	3,471	
Shareholders' equity	641,190	780,769
<i>Total liabilities and Shareholders' equity</i>	<i>1,830,279</i>	<i>3,415,952</i>

**Table of Contents****Statement of Operations**

	<b>For the year ended March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Revenues	507,105	806,198
Net Profit	99,785	140,683

*Cricinfo Limited and Wisden Cricinfo Limited*

During the year ended March 31, 2004, the Company sold its entire investments in Wisden Cricinfo Limited and recognized a gain of Rs.63,059, representing the aggregate of the difference between the proceeds received of Rs.61,218 and the net carrying value of the investment of Rs.21,110 and the reversal of an allowance of Rs.22,951 (relating to an advance to Wisden Cricinfo that had been fully provided for). The Company's equity in the losses of Wisden Cricinfo Limited for the year ended March 31, 2004 was Rs.21,632.

**12. Property, plant and equipment**

Property, plant and equipment consist of:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Land	5,132	5,132
Building	485,156	485,156
Leasehold improvements	133,937	162,139
Plant and machinery	2,433,759	2,835,478
Computer equipment	194,266	286,170
Office equipment	80,606	95,104
Furniture and fixtures	127,690	152,059
Vehicles	20,487	14,214
Construction-in-progress	20,809	19,368
	3,501,842	4,054,820
Accumulated depreciation	(2,268,214)	(2,631,574)
	<b>1,223,628</b>	<b>1,423,246</b>

**Table of Contents****13. Goodwill and other intangible assets, net**

Goodwill and other intangible assets consist of:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Goodwill	14,596	14,596
<i>Other Intangible assets</i>		
Technical know-how	85,633	82,753
Portals and web content	100,360	52,730
Customer contracts and others	56,084	56,084
Software	204,464	222,119
IPVPN Licence fee	100,000	
<b>Total</b>	<b>546,541</b>	<b>413,686</b>
Less: Accumulated amortization and impairment	352,412	365,846
<b>Other Intangible assets, net</b>	<b>194,129</b>	<b>47,840</b>
<b>Total</b>	<b>208,725</b>	<b>62,436</b>

The Company has adopted the provisions of SFAS No. 141, *Business Combinations* and 142, *Goodwill and Other Intangible Assets*, and has accordingly assessed the remaining useful lives of identified intangibles with definite useful lives and provides for amortization over the determined useful life of the asset. The Company does not have any intangible assets with indefinite useful life.

The Company periodically assessed the carrying value of intangible assets in the books and recorded an impairment charge of Rs. 22,551 during the year ended March 31, 2004

**Acquired and amortized intangible assets**

	<b>As at March 31, 2006</b>		
	<b>Weighted average life</b>	<b>Gross carrying amount</b>	<b>Accumulated amortization</b>
Technical know-how	5.00	Rs.82,753	Rs.79,240
Portals and web content	4.91	52,730	50,065
Customer contracts and others	4.04	56,084	39,119
Systems Software	2.90	222,119	197,422
		<b>Rs.</b>	
		<b>413,686</b>	<b>Rs. 365,846</b>

Estimated amortization expense in future years for the carrying value of other intangible assets as at March 31, 2006:

For the year ended March 31, 2007	Rs.29,686
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2008		11,973
2009		6,181
	85	

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**Table of Contents****14. Other assets**

Other assets consist of:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Deposits	92,843	89,768
Staff advances recoverable	398	1,575
Deposit with Department of Telecommunication towards License Fees		100,000
	<b>93,241</b>	<b>191,343</b>

The IP-VPN license fee will be adjusted against the one-time entry fee payable for the ILD and NLD licenses (see note 4) and for 2006 such amount has been reclassified under other assets.

**15. Deferred revenue**

Deferred revenue includes the amount of unearned income for the following segments:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Corporate network/data services	234,496	305,028
Internet access services	161,765	133,613
Online portal services	1,073	623
Other services	11,910	5,069
	<b>409,244</b>	<b>444,333</b>

**16. Capital lease obligations**

The gross amounts and related accumulated depreciation recorded for assets acquired under capital leases are as follows:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
Vehicles	20,485	14,212
Less: Accumulated depreciation	6,396	8,168
	<b>14,089</b>	<b>6,044</b>

The following is a schedule of future minimum capital lease commitments as at March 31, 2006:

Due for the year ended March 31, 2007	Rs. 2,994
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2008	1,775
2009	903
<b>Total minimum lease payments</b>	<b>5,672</b>
Less: Interest	367
<b>Present value of net minimum capital leases payments</b>	<b>5,305</b>
Less: Current installments of obligations under capital leases	2,759
<b>Obligations under capital leases, excluding current installments</b>	<b>2,546</b>

**Table of Contents****17. Accrued Liabilities and Other liabilities**

Accrued liabilities principally comprise of provisions for expenses amounting to Rs. 311,247 and Rs.507,006 as at March 31, 2005 and 2006, respectively. Other liabilities primarily comprise of advances received towards net sale consideration of Rs.139,460 received during the year on account of sale of 26% stake in Sify Communications Limited and deposits received from sales partners amounting to Rs. 63,376 and Rs. 94,822 as at March 31, 2005 and 2006, respectively.

**18. Income tax**

The provision for income taxes consists of:

	Year ended March 31,		
	2004	2005	2006
	Rs.	Rs.	Rs.
Current tax	(72)		
Deferred tax			
	(72)		

Income taxes are substantially from domestic operations. An amount considered insignificant is from foreign operations. For the years ended March 31, 2004, 2005 and 2006 the reported income tax expense differed from amounts computed by applying the enacted tax rates to income from continuing operations before income taxes as set out below:

	Year ended March 31,		
	2004	2005	2006
	Rs.	Rs.	Rs.
Net loss from operations before taxes	(371,212)	(307,576)	(149,245)
Enacted tax rates in India	35.88%	36.59%	33.66%
Computed expected tax benefit	(133,191)	(112,550)	(50,236)
Differences not deductible for tax purposes	11,225	15,357	55,519
Change in valuation allowance	(152,719)	142,777	(165,488)
Tax rate change of investment in affiliates	201,170	7,310	15,652
Others	24,230	(5,440)	4,478
Effect of tax rate change	49,357	(47,454)	140,075
Total income tax expense	<b>72</b>		

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. Valuation allowances are established where necessary to reduce deferred tax assets to the amount considered more likely than not to be realized.



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The carry forward losses as of March 31, 2006 amount to Rs. 2,116,284 and expire as follows:

<b>Year ending March 31,</b>	<b>Rs.</b>
2007	101,237
2008	139,002
2009	119,927
2010	528,158
2011	616,024
2012	255,815
2013 and thereafter	356,121

Significant components of deferred tax assets and liabilities included in the balance sheet are as follows:

	<b>As at March 31,</b>	
	<b>2005</b>	<b>2006</b>
	<b>Rs.</b>	<b>Rs.</b>
<b>Deferred tax assets:</b>		
Carry forward business loss	1,637,693	1,470,841
Property, plant and equipment	22,736	35,447
Accruals and expenses currently not allowed for tax purposes	14,161	
Investment in affiliates	343,985	335,474
Carry forward capital loss	15,279	31,169
Provision for doubtful accounts receivables	40,108	30,416
Total deferred tax assets	2,073,962	1,908,473
Less: valuation allowance	(2,073,962)	(1,908,473)
Net deferred tax assets		

**19. Shareholders equity**

The Company has only one class of capital stock referred to as equity shares. All references in these financial statements to the number of shares and per share amounts of the Company's equity shares have been retroactively restated to reflect stock splits made by the Company.

The shareholders of the Company, in the annual general meeting held on October 25, 2005, approved an increase in authorized share capital of the Company from 37,500,000 Equity Shares of Rs.10/- each to 38,100,000 Equity Shares of Rs.10/- each. Further, the shareholders of the Company in an extraordinary general meeting held on December 23, 2005 approved the increase in the authorized share capital of the Company from 38,100,000 Equity Shares of Rs.10/- each to 50,000,000 Equity Shares of Rs.10/-.

**20. Common stock***Voting*

Each holder of equity shares is entitled to one vote per share. The equity shares represented by American Depository Shares ( ADS ) carry similar rights to voting and dividends as the other equity shares. One ADS

represents one underlying equity share.

*Share holding agreement*

Sify, Satyam Computers Services Limited (Satyam), SAIF Investment Company Limited (SAIF) and Venture Tech entered into a subscription agreement dated October 7, 2002 and entered into an investor rights agreement dated October 7, 2002 reserving certain rights of consultation and veto for SAIF Investment Company Limited and Venture Tech.

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Effective July 7, 2005 Sify entered into a Termination and Amendment Agreement with Satyam Computer Services Limited , SAIF Investment Company Limited and Venture Tech Solutions Private Limited ,pursuant to which SAIF irrevocably terminated all of its rights and obligations pursuant to the Investor Rights Agreement.

Effective July 21, 2005 Sify entered into a Termination and Amendment Agreement with Satyam Computer Services Limited and Venture Tech Solutions Private Limited ,pursuant to which Venture Tech irrevocably terminated all of its rights and obligations pursuant to the Investor Rights Agreement.

Effective September 20, 2005 Sify entered into a Termination and Amendment Agreement with Satyam Computer Services Limited ,pursuant to which Satyam irrevocably terminated all of its rights and obligations pursuant to the Investor Rights Agreement.

On November 10, 2005, Infinity Capital Ventures, LP ( Infinity Capital ), a Delaware limited partnership, acquired 11,182,600 Sify American Depositary Shares ( ADSs ) from Satyam Computer Services Limited ( Satyam ) for US \$5.60 per share representing the market price of the share on such date. The total purchase price for the Satyam shares was US \$62,623. Upon this acquisition, the entire holding of Satyam in Sify has been divested.

On November 10, 2005, Sify and Infinity Capital entered into a Subscription Agreement pursuant to which Infinity Capital agreed to purchase from Sify 6,720,260 newly-issued equity shares (ADSs) at a price of US \$5.60 per share. The total issue price for the newly issued shares was Rs. 1,691,624 (equivalent of US \$37,633). The closing of this transaction occurred in January 2006.

*Dividends*

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

*Liquidation*

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

*Stock Options*

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

**21. Other income, net**

Other income consists of:

	<b>For the year ended March 31,</b>		
	<b>2004</b>	<b>2005</b>	<b>2006</b>
	Rs.	Rs.	Rs.
Interest expense	(2,126)	(1,938)	(11,090)

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Other finance charges	(8,882)	(11,281)	(13,773)
Interest income	48,187	52,759	70,314
Gain on sale of investments	82,758	15,710	
Others	24,210	38,074	13,788
<b>Other (expense)/income, net</b>	<b>144,147</b>	<b>93,324</b>	<b>59,239</b>

**Table of Contents****22. Employee benefit****Gratuity**

The following table sets out the funded status of the Gratuity Plan and the amounts recognized in the Company's balance sheet.

	<b>As of March 31,</b>	
	<b>2005</b>	<b>2006</b>
	Rs.	Rs.
<b>Accumulated benefit obligation</b>	10,600	12,799
<b>Change in projected benefit obligation</b>		
Projected benefit obligation at the beginning of the year	16,093	18,140
Service cost	5,688	6,806
Interest cost	1,100	1,392
Actuarial (gain)/loss	(4,057)	(2,217)
Benefits paid	(684)	(2,506)
<b>Projected benefit obligation at the end of the year</b>	<b>18,140</b>	<b>21,615</b>
<b>Change in plan assets</b>		
Fair value of plan assets at the beginning of the year	4,436	4,716
Actual return on plan assets	267	(492)
Employer contributions	697	
Benefits paid	(684)	(2,506)
<b>Fair value of plan assets at the end of the year</b>	<b>4,716</b>	<b>1,718</b>
Funded status of the plans	13,424	19,897
Unrecognized net actuarial gain/(loss)	6,698	7,395
<b>Accrued benefit cost</b>	<b>20,122</b>	<b>27,292</b>

	<b>As of March 31,</b>		
	<b>2004</b>	<b>2005</b>	<b>2006</b>
	Rs.	Rs.	Rs.
<b>The components of net gratuity costs are reflected below:</b>			
Service cost	4,593	5,688	6,806
Interest cost	929	1,100	1,392
Expected returns on plan assets	(351)	(543)	(538)
Recognized net actuarial (gain)/ loss	(57)	(130)	(490)
<b>Net gratuity costs</b>	<b>5,114</b>	<b>6,115</b>	<b>7,170</b>

**Principal weighted average actuarial assumptions:**

Discount rate		7%	8%	8%
Long-term rate of compensation increase		6%	6%	6%
Rate of return on plan assets		6%	6%	7.50%
	90			

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The Company assesses these assumptions with the projected long-term plans of growth and prevalent industry standards. Unrecognised actuarial loss is amortised over the average remaining service period of the active employees to receive benefits under the plans.

The Company provides the gratuity benefit through annual contributions to a fund managed by the Life Insurance Corporation of India (LIC). The Company estimates the long-term return on plan assets at 7.5% based on the average long-term rate of return expected to prevail over the next 15 to 20 years on the types of investments held with LIC. The Trustees administer contributions made to the trust and contributions are invested in specific designated instruments as permitted by Indian law and investments are also made in mutual funds that invest in the specific designated instruments. As of March 31, 2006, all of the plan assets are invested in debt securities.

The employer's best estimate of contributions expected to be paid to the plan during the year 2006-2007 amounts to Rs.2,500. Further, the benefits expected to be paid in each of the next five fiscal years, and in the aggregate for the five fiscal years thereafter are as follows:

For the year ended	
March 31,	
2007	Rs. 1,584
2008	1,955
2009	2,527
2010	3,847
2011	6,075
2012 to 2016	35,950

The expected benefits are based on the same assumptions need to measure the Company's benefit obligations as of March 31, 2006.

**24. Related Party Transactions**

The Company has entered into transactions with the following related parties:

Satyam Computer Services Limited (formerly the Company's parent company), where the Company provided connectivity services and software development services for certain e-learning projects until November 10, 2005;

Affiliated companies; and

Employees of the Company.

Directors of the Company

Given below is an analysis of transactions with Satyam Computer Services Limited:

	As at March 31,		April 01,
	2004	2005	2005 to
	Rs.	Rs.	November
			10, 2005
			Rs.
Due (to)/from Satyam Computer Services Limited at beginning of the year	16,016	13,030	33,524
Allocation of facilities costs	(4,408)	(1,647)	

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Capital expenses incurred on behalf of the Company	(5,376)		
Billings to Satyam Computer Services Limited	51,455	48,713	121,132
Collections from Satyam Computer Services Limited	(44,657)	(36,005)	(101,958)
Payment to Satyam Computer Services Limited		9,433	
<b>Due (to)/from Satyam Computer Services Limited</b>	<b>13,030</b>	<b>33,524</b>	<b>52,698</b>

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The following is a summary of significant transactions with other related parties:

	Year ended March 31,		
	2004	2005	2006
	Rs.	Rs.	Rs.
Interest on loans	1,411		
Sale of equity in Sify Communications Limited			139,810
<i>Employee loans</i>			

The Company has the following amounts due with respect to employee loans:

	As at March 31,	
	2005	2006
	Rs.	Rs.
Due from employees	2,461	25,393

The estimated fair value amounts of other employee loans were Rs.2,235 and Rs. 23,519 as of March 31, 2005 and 2006, respectively. Considerable judgment is required to develop the estimates of fair value. Thus, the estimates provided herein are not necessarily indicative of the amounts the Company could realize in the market.

Repayable in the year ending March 31:

	Fair value	Gross value
2007	Rs. 22,156	Rs.23,818
2008	1,363	1,575

**25. Stock based compensation plans****Employee Stock Offer Plan 1999**

Under the Employee Stock Offer Plan, 1999, the Company provided for the issuance of 825,000 warrants to eligible employees. The warrants were issued to an employee welfare trust (the Trust) at Re.1 each on September 28, 1999. The Trust holds the warrants and transfers them to eligible employees over a period of three years. The warrants, which are to be transferred to eligible employees at Re. 1 each, entitles the holder to purchase one equity share at an exercise price determined by the Compensation Committee. The warrants and the equity shares received upon the exercise of warrants are subject to progressive vesting over a three-year period from the date of issue of warrants to employees. Deferred compensation is recorded in the event that the exercise price of the warrant is determined to be less than the fair market value of the underlying shares on the date of the grant. Deferred compensation is amortized over the vesting period of the warrants. The warrants allotted and the underlying equity shares are not subject to any repurchase obligations by the Company.

The warrants are to be exercised within a period of one month from the date of the last vesting.

Shares arising out of option			Weighted average exercise price		
			(in Rupees)		
Year ended March 31,			Year ended March 31,		
2004	2005	2006	2004	2005	2006

Outstanding at beginning of the year	2,700	350.00
Granted		
Forfeited		
Expired	2,700	350.00
Exercised		
Outstanding at the end of the year		
Exercisable at the end of the year		
Weighted-average fair value of grants during the year		

**Table of Contents****Associate Stock Option Plan 2000**

In fiscal 2000, the Company established the Associate Stock Option Plan 2000 (the ASOP 2000 Plan), which provides for the issuance of warrants to eligible employees. The warrants were issued to an employee welfare trust on May 22, 2000. The Trust transfers these warrants to the eligible employees at Re. 1 each and each warrant entitles the holder to purchase one ADS at an exercise price determined by the Compensation committee.

The warrants vest in a graded manner over a period of 3 years as follows:

One sixth of the warrants:	At the end of one year from the date of the grant
Two sixths of the warrants:	At the end of two years from the date of the grant
Three sixths of the warrants:	At the end of three years from the date of the grant.

The warrants are to be exercised within a period of one month from the date of the last vesting.

As the number of warrants that an individual employee is entitled to receive and the price of the warrants are known at the grant date, the ASOP 2000 Plan is considered as a fixed grant. Deferred compensation is recorded in the event that exercise price of the warrant is determined to be less than the fair market value of the underlying shares on the date of the grant. Deferred compensation is amortized over the vesting period of the warrants.

The terms of 5,080 stock options with a weighted average exercise price of Rs.169.30 have been modified. These options are accounted in accordance with EITF Issue 00-23, *Issues Related to the Accounting for Stock Compensation under APB Opinion No. 25 and FASB Interpretation No. 44*, as a variable plan. The Company has not recorded any additional compensation charge under variable accounting, as the exercise price has been higher than the market price.

Stock option activity under the ASOP 2000 Plan is as follows:

	Shares arising out of option			Weighted average exercise price (in Rupees)		
	Year ended March 31,			Year ended March 31,		
	2004	2005	2006	2004	2005	2006
Outstanding at beginning of the year	396,500	151,500	7,770	1,385.88	214.20	105.91
Granted	8,520			182.47		
Forfeited	29,320	10,391	720	386.23	171.40	165.91
Expired	153,290	19,396	1090	3,265.89	281.26	107.11
Exercised	70,910	113,943	3920	93.83	167.36	54.71
Outstanding at the end of the year	151,500	7,770	2040	214.20	105.91	182.47
Exercisable at the end of the year	37,270	990	960	224.01	107.52	182.47
Weighted-average grant date fair value of grants during the year				122.95		

**Associate Stock Option Plan 2002**

In fiscal 2002, the Company established the Associate Stock Option Plan 2002 (the ASOP 2002 Plan), which provides for the issuance of warrants to eligible employees. On December 9, 2002, the Company issued warrants to the eligible employees at Re. 1 each and each warrant entitles the holder to purchase one ADS at an exercise price determined by the Compensation Committee.

The warrants vest in a graded manner over a period of 3 years as follows:

One sixth of the warrant quantity:	At the end of one year from the date of the grant
Five sixths of the warrant quantity:	At the end of each quarter during the second and third year from the date of the grant in eight equal installments.

The warrants are to be exercised within a period of one month from the date of the last vesting.

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As the number of warrants that an individual employee is entitled to receive and the price of the warrants are known at the grant date, the ASOP 2002 Plan is considered as a fixed grant. Deferred compensation is recorded in the event that exercise price of the warrant is determined to be less than the fair market value of the underlying shares on the date of the grant. Deferred compensation is amortized over the vesting period of the warrants.

Stock option activity under the ASOP 2002 Plan is as follows:

	Shares arising out of option			Weighted average exercise price		
				(in Rupees)		
	Year ended March 31,			Year ended March 31,		
2004	2005	2006	2004	2005	2006	
Outstanding at beginning of the year		1,108,000	757,473		170.25	178.35
Granted	1,128,060	90,000		170.13	254.16	
Forfeited	20,060	69,458	85,479	163.69	189.66	214.74
Expired		5,727	10,081		281.26	239.35
Exercised		365,342	285,056		163.39	172.60
Outstanding at the end of the year	1,108,000	757,473	376,857	170.25	178.35	172.83
Exercisable at the end of the year		131,589	357,482		174.61	168.58
Weighted-average grant date fair value of grants during the year				79.79	157.78	

**Associate Stock Option Plan 2005**

In October 2005, the Company established the Associate Stock Option Plan 2005 (the ASOP 2005 Plan), which provides for the issuance of 1,900,000 ADR s/shares to eligible employees. The Company cancelled any balance available for issue under previous plans. Accordingly, any unissued options available under previous plans or any options surrendered or lapsed are cancelled. During the period October 2005 to March 2006, the Company granted options to the eligible employees at a weighted average exercise price of Rs 285.98 per option.

The options vest in a graded manner over a period of 3 years as follows:

One sixth of the option quantity:	At the end of one year from the date of the grant
Five sixths of the option quantity:	At the end of each quarter during the second and third year from the date of the grant in eight equal installments.

The options can be exercised only after they vest but before the expiry date of forty months from the date of the grant.

As the number of ADR s/shares that an individual employee is entitled to receive and the price of the option are known at the grant date, the ASOP 2005 Plan is considered as a fixed grant. Deferred compensation is recorded in the event that exercise price of the option is determined to be less than the fair market value of the underlying shares on the date of the grant. Deferred compensation is amortized over the vesting period of the options.

Stock option activity under the ASOP 2005 Plan is as follows:

	<b>Shares arising out of option</b>	<b>Weighted average exercise price (in Rupees)</b>
	<b>Year ended March 31, 2006</b>	<b>Year ended March 31, 2006</b>
Outstanding at beginning of the year		
Granted	1,735,400	285.98
Forfeited	59,000	279.57
Expired		
Exercised		
Outstanding at the end of the year	1,676,400	286.20
Exercisable at the end of the year		
Weighted-average grant date fair value of grants during the year		126.37

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The following table summarizes information about fixed price options outstanding at March 31, 2006:

	Range of exercise price	Number outstanding at March 31, 2006	Weighted average exercise price	Weighted average remaining contractual life	Number exercisable at March 31, 2006	Weighted average exercise price
ASOP 2000	Rs. 163-265	2,040	Rs.182.47	0.13 years	960	Rs.182.47
ASOP 2002	Rs.163-265	376,857	172.83	0.16	357,482	168.58
ASOP 2005	Rs.163-265	1,346,600	238.32	2.90		
ASOP 2005	Rs.266-482	329,800	481.74	3.11		
	Rs. 163-482	2,055,297	265.31		358,442	168.62

**26. Commitments and contingencies**

a) During the year Sify has received a notice from the Income-Tax Department of India for the financial years 2002 and 2003 for a sum of Rs.103,000 stating that no withholding tax has been deducted in respect of international bandwidth and leased line payments made by the Company to international bandwidth / lease line service providers.

Based on the opinion of our counsel, withholding taxes need not be deducted if the service provider did not have any permanent establishment in India and has not installed any equipment at the Company's premises. The Company is able to demonstrate that international service providers have neither had a permanent establishment in India nor has installed any equipment at the Company's premises. Accordingly, the likelihood of the loss contingency is remote and no provision for the loss contingency is considered necessary.

b) The company has outstanding financial and performance guarantees for various statutory purposes and letters of credit totalling Rs. 279,865 and Rs. 422,683 as of March 31, 2005 and 2006, respectively. These guarantees are generally provided to governmental agencies

c) Provident Fund contribution not provided for on leave encashment in respect of periods prior to April 01, 2005 is estimated at Rs.4,326.

**27. Products and services**

Breakup of revenues against products and services are as follows:

	Year ended March 31,		
	2004	2005	2006
	Rs.	Rs.	Rs.
Service revenue	2,323,033	2,858,070	3,928,072
Initial franchise fee	102,138	107,956	104,085
Installation service revenue	131,612	236,508	262,059
	2,556,783	3,202,534	4,294,216

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Product revenue	244,401	410,923	387,591
	<b>2,801,184</b>	<b>3,613,457</b>	<b>4,681,807</b>

**Table of Contents****28. Segment reporting**

SFAS No 131, *Disclosures about Segments of an Enterprise and Related Information*, establishes standards for the way that public business enterprises report information about operating segments and related disclosures about products and services, geographic areas and major customers. The Company's operations predominantly relate to connectivity to enterprises and providing Internet access to retail subscribers (both home access and public access). The Company also operates portals, Sify.com., Samachar.com and SifyMax.in, that provide a variety of India-related content to audiences both in India and abroad, and which generates revenue from advertisements and other value added services.

The primary operating segments of the Company are:

Corporate network/data services, which provides Internet, connectivity, security and consulting, hosting and managed service solutions;

Retail Internet access services, from homes and through cybercafés;

Online portal and content offerings; and

Other services, such as development of e-learning software.

The Chief Operating Decision Maker ( CODM ) evaluates the Company's performance and allocates resources to various strategic business units that are identified based on the products and services that they offer and on the basis of the market served. The measure of loss reviewed by the CODM was Earnings/loss before interest, taxes, depreciation and amortization.

Revenue in relation to segments is categorized based on items that are individually identifiable to that segment. Bandwidth costs, which form a significant part of the total expenses, are allocated primarily between the corporate network/data services and Internet access services businesses as described below:

International bandwidth refers to bandwidth that is required for access to sites and offices outside the country. For all these businesses, bandwidth is allocated based on actual utilization captured by monitoring traffic per IP pool assigned at the egress points. The Company has packet shapers in the main locations to monitor bandwidth use by each of the above categories of users. This information is used in determining norms like bandwidth per port and bandwidth per personal computer. The actual utilization is cross validated against assumptions / norms for each business.

National bandwidth refers to the inter-city link bandwidth implemented within the country. Inter-city link bandwidth was allocated based on the number of subscribers or iway cybercafés at non gateway points and the bandwidth sold to and used by business enterprises (determined using packet shapers). However, in order to strengthen its corporate business, the Company enhanced its national backbone to carry Internet traffic to the international fibre gateways, shifting from hybrid satellite and fibre gateways to fibre only gateways for international bandwidth. National bandwidth costs are now allocated based on international bandwidth allocation ratios because most of the traffic carried on the national backbone is directed towards the international gateways. The Company believes that the resulting allocations are reasonable.

Last mile costs related to dial-up access (E1/R2 costs) that can be directly identified to businesses are allocated directly. Spectrum charges that are paid to the WPERSONAL COMPUTER for the license that has been provided to enable Sify to operate on the 5.7 ghz wireless spectrum are allocated based on the bandwidth that is used by the various businesses that use this spectrum. Certain expenses, such as depreciation, technology and administrative overheads, which form a significant component of total expenses, are not allocable to specific segments as the

underlying services are used interchangeably. Management believes that it is not practical to provide segment disclosure of these expenses and, accordingly, they are separately disclosed as unallocated and adjusted only against the total income of the Company.

A significant part of the fixed assets used in the Company's business are not identifiable to any of the reportable segments and can be used interchangeably between segments. Management believes that it is not practicable to provide segment disclosures relating to total assets since a meaningful segregation of the available data is onerous.

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The Company's operating segment information for the years ended March 31, 2004, 2005 and 2006 are presented below:

<b>Year ended March 31, 2006</b>					(all in Rupees)
	Corporate Network / Data Services	Retail Internet Access Services	Online Portal Services	Other Services	Total
				Rs.	
Revenues	Rs.2,531,094	Rs.1,814,115	Rs.178,986	157,612	Rs.4,681,807
Allocated expenses	(1,512,832)	(1,798,963)	(187,941)	(141,567)	(3,641,303)
Equity in profit of affiliates			40,703		40,703
Segment operating income	Rs.1,018,262	Rs.15,152	Rs.31,748	Rs.16,045	Rs.1,081,207
Unallocated corporate expenses					(843,599)
Foreign exchange gain, net					23,221
Other income / (expense), net					11,835
Depreciation and amortization					(476,526)
Interest income, net					54,617
Net loss					Rs.(149,245)

<b>Year ended March 31, 2005</b>					(all in Rupees)
	<b>Corporate Network/Data Services</b>	<b>Retail Internet Access Services</b>	<b>Online Portal Services</b>	<b>Other Services</b>	<b>Total</b>
Revenues	2,023,412	1,404,876	103,053	82,116	3,613,457
Allocated expenses	(1,345,254)	(1,361,140)	(99,303)	(74,346)	(2,880,043)
Equity in profit of affiliates			50,752		50,752
Segment operating income	678,158	43,736	54,502	7,770	784,166
Unallocated corporate expenses					(620,235)
Foreign exchange gain					2,595
Other income/(expense), net					42,503
Depreciation and amortization					(567,426)
Interest income, net					50,821
Net (loss)					(307,576)

**Year ended March 31, 2004** (all in Rupees)

	<b>Corporate</b>	<b>Retail Internet</b>	<b>Online Portal Services</b>	<b>Other Services</b>	<b>Total</b>
	<b>Network/Data Services</b>	<b>Access Services</b>			
Revenues	1,395,498	1,088,440	84,233	233,013	2,801,184
Allocated expenses	(846,526)	(1,188,366)	(100,935)	(85,277)	(2,221,104)
Equity in profit of affiliates			17,083		17,083
Minority interest			79		79
Segment operating income/(loss)	548,972	(99,926)	460	147,736	597,242
Unallocated corporate expenses					(540,981)
Foreign exchange loss, net					(52,148)
Other income/(expense), net					97,541
Profit from sale of business					63,059
Depreciation and amortization					(559,980)
Impairment of assets					(22,551)
Interest income, net					46,606
Income taxes					(72)
Net (loss)					(371,284)

**Table of Contents****29. Legal proceedings**

The Company and certain of its officers and directors are named as defendants in a securities class action lawsuit filed in the United States District Court for the Southern District of New York. This action, which is captioned *In re Satyam Infoway Ltd. Initial Public Offering Securities Litigation*, also names several of the underwriters involved in Sify's initial public offering of American Depositary Shares as defendants. This class action is brought on behalf of a purported class of purchasers of Sify's ADSs from the time of Sify's Initial Public Offering (IPO) in October 1999 through December 2000. The central allegation in this action is that the underwriters in Sify's IPO solicited and received undisclosed commissions from, and entered into undisclosed arrangements with, certain investors who purchased Sify's ADSs in the IPO and the aftermarket. The complaint also alleges that Sify violated the United States federal securities laws by failing to disclose in the IPO prospectus that the underwriters had engaged in these allegedly undisclosed arrangements. More than 300 issuers have been named in similar lawsuits.

In July 2002, an omnibus motion to dismiss all complaints against issuers and individual defendants affiliated with issuers was filed by the entire group of issuer defendants in these similar actions. In October 2002, the cases against the Company's executive officers who were named as defendants in this action were dismissed without prejudice. In February 2003, the court in this action issued its decision on defendants' omnibus motion to dismiss. This decision denied the motion to dismiss the Section 11 claim as to the Company and virtually all of the other issuer defendants. The decision also denied the motion to dismiss the Section 10(b) claim as to numerous issuer defendants, including the Company. On June 26, 2003, the plaintiffs in the consolidated IPO class action lawsuits currently pending against Sify and over 300 other issuers who went public between 1998 and 2000, announced a proposed settlement with Sify and the other issuer defendants. The proposed settlement provides that the insurers of all settling issuers will guarantee that the plaintiffs recover \$1 billion from non-settling defendants, including the investment banks who acted as underwriters in those offerings. In the event that the plaintiffs do not recover \$1 billion, the insurers for the settling issuers will make up the difference.

The Company believes that it has sufficient insurance coverage to cover the maximum amount that it may be responsible for under the proposed settlement. Although the Federal District Court has preliminarily approved the settlement, it is possible that the Federal District Court may not finally approve the settlement in whole or part. The Company believes the maximum exposure under this settlement, in the event that the plaintiffs recover nothing from the non-settling defendants, is approximately U.S. \$3.9 million, an amount which the Company believes is fully recoverable from the Company's insurer.

The Company is party to additional legal actions arising in the ordinary course of business. Based on the available information, as of March 31, 2006 Sify believes that it has adequate legal defenses for these actions and that the ultimate outcome of these actions will not have a material adverse effect on Sify.

**30. Subsequent Events**

The Company has paid retention bonuses amounting to Rs.20 million during the quarter ended December 31, 2005 to its key employees. The amount is being amortized over the retention period of 36 months and will be recovered from the employees in the event of termination of service before the end of the retention period. The Compensation Committee of the Company in its meeting dated April 20, 2006 approved an amendment to this retention bonus scheme wherein the retention period has been reduced to 18 months.

In June, 2006, Rustom Irani and Ajit Abraham each announced that they will be stepping down as officers of our Company and will be leaving the employment of our Company. Mr. Irani is our Chief Technology Officer and Mr. Abraham is our Chief Human Resources Officer. Our management has begun searching for their replacements.

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**Item 19. Exhibits**

Number	Description
1.1	Amended Articles of Association of Sify Limited. (1)
1.2	Memorandum of Association of Sify Limited. (2)
1.3	Amendment of Memorandum of Association. (3)
2.1	Deposit Agreement, dated as of October 18, 1999, among Sify Limited, Citibank, N.A. and holders from time to time of American Depositary Receipts issued thereunder (including, as an exhibit, the form of American Depositary Receipt). (4)
2.2	Amendment No. 1 to Deposit Agreement among Sify Limited, Citibank, N.A. and holders from time to time of American Depositary Receipts issued thereunder (including, as an exhibit, the form of American Depositary Receipt). (4)
2.3	Amendment No. 2 to Deposit Agreement among Sify Limited, Citibank, N.A. and holders from time to time of American Depositary Receipts issued thereunder (including, as an exhibit, the form of American Depositary Receipt). (5)
2.4	Subscription Agreement dated November 10, 2005 between Sify Limited and Infinity Capital Ventures, LP. (9)
2.5	Standstill Agreement dated November 10, 2005 by and among Sify Limited, Infinity Capital Ventures, LP and Mr Raju Vegesna. (9)
2.6	Shareholders Agreement dated December 20, 2005 between Sify Limited, Infinity Satcom Universal (P) Limited, and Sify Communications Limited. (10)
2.7	Shareholders Agreement dated November 25, 2005 between Sify Limited and Man Financial. (11)
4.1	Associate Stock Option Plan 2000 (6)
4.2	Associate Stock Option Plan 2002 (6)
4.3	Associate Stock Option Plan 2005
4.4	Form of Indemnification Agreement. (7)
4.5	License Agreement for Provision of Internet Service, including Internet Telephony dated as of April 1, 2002 by and between Sify Limited and the Government of India, Ministry of Communications and Information Technology, Department of Telecommunications, Telecom Commission. (3)
4.6	Bank Guarantee, dated as of November 4, 1998. (2)
4.7	

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Agreement, dated November 10, 2004, between Sify Limited, Satyam Computer Services Limited, SAIF Investment Company Limited and Venture Tech Solutions Pvt. Ltd. (8)

- 8.1 List of Subsidiaries.
- 11.1 Code of Conduct and Conflict of Interest Policy (6)
- 12.1 Rule 13a-14(a) Certification of Chief Executive Officer
- 12.2 Rule 13a-14(a) Certification of Chief Financial Officer
- 13.1 Section 1350 Certification of Chief Executive Officer
- 13.2 Section 1350 Certification of Chief Financial Officer
- 15.1 Consent of KPMG

(1) Previously filed as an exhibit to the Report on Form 6-K filed with the Commission on February 17, 2005 and incorporated herein by reference.

(2) Previously filed as an exhibit to Amendment No. 1 to the Registration Statement on Form F-1 filed with the Commission on October 4, 1999 and incorporated herein by reference.

(3) Previously filed as an exhibit to the Annual Report on Form 20-F filed with the Commission on July 1, 2002

and  
incorporated  
herein by  
reference.

- (4) Previously filed as an exhibit to the Post-Effective Amendment No. 1 to Form F-6 filed with the Commission on January 5, 2000 and incorporated herein by reference.
  
- (5) Previously filed as an exhibit to the Registration Statement on Form S-8 (File No. 333-101322) filed with Commission on November 20, 2002 and incorporated herein by reference.
  
- (6) Previously filed as an exhibit to the Annual Report on Form 20-F filed with the Commission on June 29, 2004 and incorporated herein by reference.
  
- (7) Previously filed as an exhibit to Amendment No. 2 to the Registration

Statement on  
Form F-2 filed  
with the  
Commission on  
October 13,  
1999 and  
incorporated  
herein by  
reference.

(8) Previously filed  
as an exhibit to  
the Report on  
Form 6-K filed  
with the  
Commission on  
November 30,  
2004 and  
incorporated  
herein by  
reference.

(9) Previously filed  
as an exhibit to  
the Report on  
Form 6-K filed  
with the  
Commission on  
November 21,  
2005 and  
incorporated  
herein by  
reference.

(10) Previously filed  
as an exhibit to  
the Report on  
Form 6-K filed  
with the  
Commission on  
December 7,  
2005 and  
incorporated  
herein by  
reference.

(11) Previously filed  
as an exhibit to  
the Report on  
Form 6-K filed  
with the

Commission on  
December 23,  
2005 and  
incorporated  
herein by  
reference.

**Table of Contents**

**SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

**SIFY LIMITED**

By: /s/ R. Ramaraj

Name: R. Ramaraj  
Title: Chief Executive Officer & Managing  
Director

By: /s/ Durgesh Mehta

Name: Durgesh Mehta  
Title: Chief Financial Officer

Date: June 30, 2006

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**Exhibit Index**

Number	Description
1.1	Amended Articles of Association of Sify Limited. (1)
1.2	Memorandum of Association of Sify Limited. (2)
1.3	Amendment of Memorandum of Association. (3)
2.1	Deposit Agreement, dated as of October 18, 1999, among Sify Limited, Citibank, N.A. and holders from time to time of American Depositary Receipts issued thereunder (including, as an exhibit, the form of American Depositary Receipt). (4)
2.2	Amendment No. 1 to Deposit Agreement among Sify Limited, Citibank, N.A. and holders from time to time of American Depositary Receipts issued thereunder (including, as an exhibit, the form of American Depositary Receipt). (4)
2.3	Amendment No. 2 to Deposit Agreement among Sify Limited, Citibank, N.A. and holders from time to time of American Depositary Receipts issued thereunder (including, as an exhibit, the form of American Depositary Receipt). (5)
2.4	Subscription Agreement dated November 10, 2005 between Sify Limited and Infinity Capital Ventures, LP. (9)
2.5	Standstill Agreement dated November 10, 2005 by and among Sify Limited, Infinity Capital Ventures, LP and Mr Raju Vegesna. (9)
2.6	Shareholders Agreement dated December 20, 2005 between Sify Limited, Infinity Satcom Universal (P) Limited, and Sify Communications Limited. (10)
2.7	Shareholders Agreement dated November 25, 2005 between Sify Limited and Man Financial. (11)
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- (3) Previously filed as an exhibit to the Annual Report on Form 20-F filed with the Commission

on July 1, 2002  
and  
incorporated  
herein by  
reference.

- (4) Previously filed as an exhibit to the Post-Effective Amendment No. 1 to Form F-6 filed with the Commission on January 5, 2000 and incorporated herein by reference.
- (5) Previously filed as an exhibit to the Registration Statement on Form S-8 (File No. 333-101322) filed with Commission on November 20, 2002 and incorporated herein by reference.
- (6) Previously filed as an exhibit to the Annual Report on Form 20-F filed with the Commission on June 29, 2004 and incorporated herein by reference.
- (7) Previously filed as an exhibit to Amendment No. 2 to the

Registration Statement on Form F-2 filed with the Commission on October 13, 1999 and incorporated herein by reference.

(8) Previously filed as an exhibit to the Report on Form 6-K filed with the Commission on November 30, 2004 and incorporated herein by reference.

(9) Previously filed as an exhibit to the Report on Form 6-K filed with the Commission on November 21, 2005 at incorporated herein by reference.

(10) Previously filed as an exhibit to the Report on Form 6-K filed with the Commission on December 7, 2005 and incorporated herein by reference.

(11) Previously filed as an exhibit to the Report on Form 6-K filed

with the  
Commission on  
December 23,  
2005 and  
incorporated  
herein by  
reference.