EASTMAN KODAK CO
Form 10-Q
May 09, 2007

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2007

or

[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from ___ to ___

Commission File Number 1-87

EASTMAN KODAK COMPANY
(Exact name of registrant as specified in its charter)

NEW JERSEY	**16-0417150**
(State of incorporation)	**(IRS Employer Identification No.)**
343 STATE STREET, ROCHESTER, NEW YORK	**14650**
(Address of principal executive offices)	**(Zip Code)**

Registrant's telephone number, including area code: 585-724-4000

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, and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] 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.

Large accelerated filer [X] Accelerated filer [ ] Non-accelerated filer [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [X]

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Number of Shares Outstanding at April 30, 2007
Common Stock, $2.50 par value	**287,690,661**

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Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

EASTMAN KODAK COMPANY
CONSOLIDATED STATEMENT OF OPERATIONS (Unaudited)

	Three Months Ended March 31	
(in millions, except per share data)	2007	2006
Net sales	$ 2,119	$ 2,292
Cost of goods sold	1,690	1,823
Gross profit	429	469
Selling, general and administrative expenses	395	507
Research and development costs	137	148
Restructuring costs and other	85	138

Loss from continuing operations before interest, other income (charges), net and income taxes	(188)	(324)
Interest expense	25	41
Other income (charges), net	23	27
Loss from continuing operations before income taxes	(190)	(338)
(Benefit) provision for income taxes	(16)	8
Loss from continuing operations	(174)	(346)
Earnings from discontinued operations, net of income taxes	23	48
NET LOSS	$ (151)	$ (298)
Basic and diluted net (loss) earnings per share:		
Continuing operations	$ (0.61)	$ (1.21)
Discontinued operations	0.08	0.17
Total	$ (0.53)	$ (1.04)
Number of common shares used in basic net loss per share	287.3	287.2
Incremental shares from assumed conversion of options		—
Number of common shares used in diluted net loss per share	287.3	287.2

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

EASTMAN KODAK COMPANY
CONSOLIDATED STATEMENT OF RETAINED EARNINGS (Unaudited)

(in millions)	Three Months Ended March 31 2007	2006
Retained earnings at beginning of period	$ 5,967	$ 6,717
Net loss	(151)	(298)
Loss from issuance of treasury stock	(6)	(2)
Retained earnings at end of period	$ 5,810	$ 6,417

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

EASTMAN KODAK COMPANY
CONSOLIDATED STATEMENT OF FINANCIAL POSITION (Unaudited)

(in millions)	March 31, 2007	December 31, 2006
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 1,026	$ 1,469
Receivables, net	1,801	2,072
Inventories, net	1,157	1,001
Deferred income taxes	121	108
Other current assets	102	96
Assets of discontinued operations	780	811
Total current assets	4,987	5,557
Property, plant and equipment, net	2,404	2,602

Goodwill	1,589	1,584
Other long-term assets	3,640	3,509
Assets of discontinued operations	1,081	1,068
TOTAL ASSETS	$ 13,701	$ 14,320
LIABILITIES AND SHAREHOLDERS’ EQUITY		
CURRENT LIABILITIES		
Accounts payable and other current liabilities	$ 3,263	$ 3,712
Short-term borrowings	44	64
Accrued income and other taxes	307	347
Liabilities of discontinued operations	410	431
Total current liabilities	4,024	4,554
Long-term debt, net of current portion	2,710	2,714
Pension and other postretirement liabilities	3,725	3,934
Other long-term liabilities	1,609	1,690
Liabilities of discontinued operations	43	40
Total liabilities	12,111	12,932
Commitments and Contingencies (Note 6)		
SHAREHOLDERS’ EQUITY		
Common stock, $2.50 par value	978	978
Additional paid in capital	879	881
Retained earnings	5,810	5,967
Accumulated other comprehensive loss	(284)	(635)
	7,383	7,191
Less: Treasury stock, at cost	5,793	5,803
Total shareholders’ equity	1,590	1,388
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	$ 13,701	$ 14,320

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

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EASTMAN KODAK COMPANY
CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)

	Three Months Ended March 31,	
(in millions)	**2007**	**2006**
Cash flows from operating activities:		
Net loss	$ (151)	$ (298)
Adjustments to reconcile to net cash provided by operating activities:		
Earnings from discontinued operations, net of income taxes	(23)	(48)
Depreciation and amortization	248	336
(Gain) loss on sales of businesses/assets	(8)	9
Non-cash restructuring costs, asset impairments and other charges	11	41
Provision (Benefit) for deferred income taxes	14	(45)
Decrease in receivables	274	242
Increase in inventories	(152)	(162)
Decrease in liabilities excluding borrowings	(609)	(504)
Other items, net	(1)	(108)
Total adjustments	(246)	(239)

Net cash used in continuing operations	(397)	(537)
Net cash provided by discontinued operations	43	56
Net cash used in operating activities	(354)	(481)
Cash flows from investing activities:		
Additions to properties	(66)	(78)
Net proceeds from sales of businesses/assets	10	6
Acquisitions, net of cash acquired	(2)	—
Investments in unconsolidated affiliates	—	(8)
Marketable securities - sales	36	23
Marketable securities - purchases	(41)	(24)
Net cash used in continuing operations	(63)	(81)
Net cash used in discontinued operations	(11)	(15)
Net cash used in investing activities	(74)	(96)
Cash flows from financing activities:		
Net decrease in borrowings with maturities of 90 days or less	(17)	(22)
Proceeds from other borrowings	6	55
Repayment of other borrowings	(8)	(52)
Net cash used in financing activities	(19)	(19)
Effect of exchange rate changes on cash	4	8
Net decrease in cash and cash equivalents	(443)	(588)
Cash and cash equivalents, beginning of year	1,469	1,665
Cash and cash equivalents, end of quarter	$ 1,026	$ 1,077

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

EASTMAN KODAK COMPANY
NOTES TO FINANCIAL STATEMENTS (Unaudited)

NOTE 1: BASIS OF PRESENTATION

BASIS OF PRESENTATION

The consolidated interim financial statements are unaudited, and certain information and footnote disclosure related thereto normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted in accordance with Rule 10-01 of Regulation S-X. In the opinion of management, the accompanying unaudited consolidated financial statements were prepared following the same policies and procedures used in the preparation of the audited financial statements and reflect all adjustments (consisting of normal recurring adjustments) necessary to present fairly the results of operations, financial position and cash flows of Eastman Kodak Company and its subsidiaries (the Company). The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year. These consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

Certain amounts for prior periods have been reclassified to conform to the current period classification. Prior period reclassifications include the following:

- The presentation of discontinued operations and related assets and liabilities held for sale, as a result of the divestiture of the Health Group segment.
- The adoption of FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes," which requires reclassification of liabilities related to uncertain tax positions.
- Prior period segment results have been revised to conform to the new segment reporting structure, which was effective January 1, 2007.

RECENT ACCOUNTING PRONOUNCEMENTS

FASB Statement No. 155

In February 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments (an amendment of FASB Statements No. 133 and 140)." This Statement permits fair value measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation. SFAS No. 155 is effective for all financial instruments acquired, issued, or subject to a remeasurement event occurring after the beginning of an entity's first fiscal year that begins after September 15, 2006 (January 1, 2007 for the Company). Additionally, the fair value option may also be applied upon adoption of this Statement for hybrid financial instruments that had been bifurcated under previous accounting guidance prior to the adoption of this Statement. The adoption of SFAS No. 155 in the first quarter of 2007 did not have a material impact on the Company's Consolidated Financial Statements.

FASB Interpretation No. 48

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48). FIN 48 clarifies the accounting and reporting for uncertainty in income taxes recognized in accordance with SFAS No. 109, "Accounting for Income Taxes." This Interpretation prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, and also provides guidance on various related matters such as derecognition, interest and penalties, and disclosure. Further information regarding the adoption of FIN 48 is disclosed in Note 5, "Income Taxes."

FASB Statement No. 157

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements," which establishes a comprehensive framework for measuring fair value in GAAP and expands disclosures about fair value measurements. Specifically, this Statement sets forth a definition of fair value, and establishes a hierarchy prioritizing the inputs to valuation techniques, giving the highest priority to quoted prices in active markets for identical assets and liabilities and the lowest priority to unobservable inputs. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The provisions of SFAS No. 157 are generally required to be applied on a prospective basis, except to certain financial instruments accounted for under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," for which the provisions of SFAS No. 157 should be applied retrospectively. The Company will adopt SFAS No. 157 in the first quarter of 2008.

FASB Statement No. 159

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities," which permits entities to choose to measure, on an item-by-item basis, specified financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected are required to be reported in earnings at each reporting date. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The provisions of this statement are required to be applied prospectively. The Company will adopt SFAS No. 159 in the first quarter of 2008.

NOTE 2: RECEIVABLES, NET

(in millions)	**March 31, 2007**	**December 31, 2006**
Trade receivables	$ 1,463	$ 1,737
Miscellaneous receivables	338	335
Total (net of allowances of $120 and $134 as of March 31, 2007 and December 31, 2006, respectively)	$ 1,801	$ 2,072

Of the total trade receivable amounts of $1,463 million and $1,737 million as of March 31, 2007 and December 31, 2006, respectively, approximately $194 million and $272 million are expected to be settled through customer deductions in lieu of cash payments. Such deductions represent rebates owed to the customer and are included in accounts payable and other current liabilities in the accompanying Consolidated Statement of Financial Position at each respective balance sheet date.

NOTE 3: INVENTORIES, NET

(in millions)	March 31, 2007	December 31, 2006
Finished goods	$ 684	$ 606
Work in process	236	192
Raw materials	237	203
Total	$ 1,157	$ 1,001

NOTE 4: GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill was $1,589 million and $1,584 million at March 31, 2007 and December 31, 2006, respectively. The changes in the carrying amount of goodwill by reportable segment for the three months ended March 31, 2007 were as follows:

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	As of March 31, 2007			
(in millions)	Consumer Digital Imaging Group	Film Products Group	Graphic Communications Group	Consolidated Total
Balance at December 31, 2006	$ 217	$ 544	$ 823	$ 1,584
Additions			2	2
Currency translation adjustments	1	3	(1)	3
Balance at March 31, 2007	$ 218	$ 547	$ 824	$ 1,589

Due to the realignment of the Kodak operating model and change in reporting structure, as described in Note 13, Segment Information, effective January 1, 2007, the Company reassigned goodwill to its reportable segments using a relative fair value approach as required under SFAS No. 142, "Goodwill and Other Intangible Assets." Additionally, the Company reassessed its goodwill for impairment during the first quarter of 2007, and determined that no reporting units carrying values exceeded their respective estimated fair values based on the realigned reporting structure and, therefore, there was no impairment.

The gross carrying amount and accumulated amortization by major intangible asset category as of March 31, 2007 and December 31, 2006 were as follows:

	As of March 31, 2007			
(in millions)	Gross Carrying Amount	Accumulated Amortization	Net	Weighted-Average Amortization Period
Technology-based	$ 324	$ 130	$ 194	7 years
Customer-related	275	103	172	10 years
Other	217	98	119	8 years
Total	$ 816	$ 331	$ 485	8 years

	As of December 31, 2006			
(in millions)	Gross Carrying Amount	Accumulated Amortization	Net	Weighted-Average Amortization Period
Technology-based	$ 324	$ 119	$ 205	7 years
Customer-related	274	95	179	10 years
Other	214	88	126	8 years

Total	$	812	$	302	$	510	8 years

Amortization expense related to purchased intangible assets for the three months ended March 31, 2007 and 2006 was $28 million and $30 million, respectively.

Estimated future amortization expense related to purchased intangible assets at March 31, 2007 is as follows (in millions):

2007	$	83
2008		105
2009		101
2010		77
2011		39
2012 and thereafter		80
Total	$	485

NOTE 5: INCOME TAXES

The Company□s income tax (benefit) provision and effective tax rate were as follows:

	Three Months Ended March 31	
(dollars in millions):	**2007**	**2006**
Loss from continuing operations before income taxes	($190)	($338)
(Benefit) provision for income taxes	(16)	8
Effective tax rate	8.4%	(2.4)%

For the first quarter of 2007, the Company recorded a benefit of $16 million on a pre-tax loss of $190 million, representing an effective rate of 8.4%. The difference between the effective tax rate and the U.S. statutory rate of 35.0% is primarily attributable to: (1) losses generated within the U.S. and in certain jurisdictions outside the U.S., which were not benefited, and (2) the mix of the earnings from operations in certain lower-taxed jurisdictions outside the U.S. Other significant items that caused the difference from the statutory tax rate include non-U.S. tax benefits of $10 million associated with total worldwide restructuring costs; and a benefit of