FLEXTRONICS INTERNATIONAL LTD.
Form 10-Q
February 07, 2007

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

(Mark One)

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

For the quarterly period ended December 31, 2006

or

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

For the transition period from to

Commission file number 0-23354

FLEXTRONICS INTERNATIONAL LTD.
(Exact name of registrant as specified in its charter)

Singapore	**Not Applicable**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
One Marina Boulevard, #28-00 Singapore	**018989**
(Address of registrant s principal executive offices)	*(Zip Code)*

Registrant s telephone number, including area code
(65) 6890 7188

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 þ No o

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 þ Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

As of February 2, 2007, there were 607,187,628 shares of the Registrant s ordinary shares outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. ***FINANCIAL STATEMENTS***

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Flextronics International Ltd.:

We have reviewed the accompanying condensed consolidated balance sheet of Flextronics International Ltd. and subsidiaries (the Company) as of December 31, 2006, the related condensed consolidated statements of operations for the three-month and nine-month periods ended December 31, 2006 and 2005, and the related condensed consolidated statements of cash flows for the nine-month periods ended December 31, 2006 and 2005. These interim financial statements are the responsibility of the Company s management.

We conducted our reviews in accordance with standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of the Company as of March 31, 2006 and the related consolidated statements of operations, shareholders equity, and cash flows for the year then ended (not presented herein); and in our report dated May 30, 2006, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of March 31, 2006 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ DELOITTE & TOUCHE LLP
San Jose, California
February 7, 2007

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FLEXTRONICS INTERNATIONAL LTD.
CONDENSED CONSOLIDATED BALANCE SHEETS

	December 31, 2006	March 31, 2006
	(In thousands, except share amounts) (Unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 909,195	$ 942,859
Accounts receivable, net of allowance for doubtful accounts of $18,418 and $17,749 as of December 31, 2006 and March 31, 2006, respectively	1,907,123	1,496,520
Inventories	2,535,151	1,738,310
Deferred income taxes	13,095	9,643
Current assets of discontinued operations		89,509
Other current assets	622,176	620,095
Total current assets	5,986,740	4,896,936
Property and equipment, net of accumulated depreciation of $1,382,500 and $1,234,341 as of December 31, 2006 and March 31, 2006, respectively	1,922,660	1,586,486
Deferred income taxes	656,576	646,431
Goodwill	3,057,756	2,676,727
Other intangible assets, net	201,902	115,064
Long-term assets of discontinued operations		574,384
Other assets	862,258	462,379
Total assets	$ 12,687,892	$ 10,958,407
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Bank borrowings, current portion of long-term debt and capital lease obligations	$ 8,224	$ 106,099
Accounts payable	3,747,138	2,758,019
Accrued payroll	215,672	184,483
Current liabilities of discontinued operations		57,213
Other current liabilities	940,743	852,490
Total current liabilities	4,911,777	3,958,304
Long-term debt and capital lease obligations, net of current portion	1,492,499	1,488,975
Long-term liabilities of discontinued operations		30,578
Other liabilities	160,192	125,903
Commitments and contingencies (Note L)		
Shareholders equity:		
Ordinary shares, no par value; 606,944,332 and 578,141,566 shares issued and outstanding as of December 31, 2006 and March 31, 2006,	5,911,935	5,572,574

respectively		
Retained earnings (accumulated deficit)	146,526	(241,438)
Accumulated other comprehensive income	64,963	27,565
Deferred compensation		(4,054)
Total shareholders equity	6,123,424	5,354,647
Total liabilities and shareholders equity	$ 12,687,892	$ 10,958,407

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

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FLEXTRONICS INTERNATIONAL LTD.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three-Month Periods Ended December 31,		Nine-Month Periods Ended December 31,	
	2006	2005	2006	2005
	(In thousands, except per share amounts) (Unaudited)			
Net sales	$ 5,415,460	$ 4,125,957	$ 14,176,936	$ 11,757,087
Cost of sales (including $1,708 and $3,559 of stock-based compensation expense for the three-and nine-month periods ended December 31, 2006, respectively)	5,126,311	3,889,325	13,377,737	11,036,913
Restructuring charges		63,115	95,683	129,150
Gross profit	289,149	173,517	703,516	591,024
Selling, general and administrative expenses (including $6,346 and $589 of stock-based compensation expense for the three-month periods ended December 31, 2006 and 2005, respectively, and $19,759 and $1,745 for the nine-month periods ended December 31, 2006 and 2005, respectively)	135,884	96,198	403,366	354,587
Intangible amortization	7,794	8,910	23,520	28,890
Restructuring charges		5,442	565	22,442
Other charges, net		7,705		7,705
Interest and other expense, net	16,791	21,885	77,063	67,692
Loss (gain) on divestitures of operations		3,126		(23,819)
Income from continuing operations before income taxes	128,680	30,251	199,002	133,527
Provision for (benefit from) income taxes	10,089	(7,368)	(1,224)	59,912
Income from continuing operations	118,591	37,619	200,226	73,615
Discontinued operations:				
Income from discontinued operations, net of tax		4,335	187,738	24,599
Net income	$ 118,591	$ 41,954	$ 387,964	$ 98,214
Earnings per share:				
Income from continuing operations:				
Basic	$ 0.20	$ 0.07	$ 0.34	$ 0.13
Diluted	$ 0.20	$ 0.06	$ 0.34	$ 0.12

Income from discontinued operations:								
Basic	$		$	0.01	$	0.32	$	0.04
Diluted	$		$	0.01	$	0.32	$	0.04
Net income:								
Basic	$	0.20	$	0.07	$	0.67	$	0.17
Diluted	$	0.20	$	0.07	$	0.66	$	0.16
Weighted-average shares used in computing per share amounts:								
Basic		589,414		574,635		582,353		572,112
Diluted		598,534		599,761		590,658		600,068

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

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FLEXTRONICS INTERNATIONAL LTD.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine-Month Periods Ended December 31,	
	2006	2005
	(In thousands) (Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 387,964	$ 98,214
Depreciation and amortization	241,473	246,789
Gain on divestitures of operations	(181,228)	(67,569)
Change in working capital and other, net of effect of acquisitions	(147,551)	369,531
Net cash provided by operating activities	300,658	646,965
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment, net of dispositions	(436,741)	(151,880)
Acquisitions of businesses, net of cash acquired	(353,608)	(622,961)
Proceeds from divestitures of operations, net of cash held in divested operations of $108,624 and $33,064 for the nine-month periods ended December 31, 2006 and 2005, respectively	579,850	518,505
Other investments and notes receivable	(15,430)	4,426
Net cash used in investing activities	(225,929)	(251,910)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from bank borrowings and long-term debt	6,037,506	2,180,689
Repayments of bank borrowings, long-term debt and capital lease obligations	(6,180,269)	(2,436,289)
Net proceeds from issuance of ordinary shares	17,607	47,132
Net cash used in financing activities	(125,156)	(208,468)
Effect of exchange rate changes on cash	16,763	27,792
Net increase (decrease) in cash and cash equivalents	(33,664)	214,379
Cash and cash equivalents at beginning of period	942,859	869,258
Cash and cash equivalents at end of period	$ 909,195	$ 1,083,637
Supplemental disclosures of cash flow information:		
Non-cash investing and financing activities:		
Fair value of seller notes received from sale of divested operations	$ 204,920	$ 38,278
Issuance of ordinary shares upon conversion of debt	$	$ 5,000
Issuance of ordinary shares for acquisition of businesses	$ 299,608	$ 24,914

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

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE A ORGANIZATION OF THE COMPANY

Flextronics International Ltd. (Flextronics or the Company) was incorporated in the Republic of Singapore in May 1990. The Company is a leading provider of advanced design and electronics manufacturing services (EMS) to original equipment manufacturers (OEMs) of a broad range of products in the following markets: computing; mobile communications; consumer digital; infrastructure; industrial, semiconductor and white goods; automotive, marine and aerospace; and medical. The Company s strategy is to provide customers with a full range of vertically-integrated global supply chain services through which the Company designs, builds and ships a complete packaged product for its OEM customers. OEM customers leverage the Company s services to meet their product requirements throughout the entire product life cycle. The Company also provides after-market services such as logistics, repair and warranty services.

The Company s service offerings include, rigid printed circuit board and flexible circuit fabrication, systems assembly and manufacturing (including enclosures, testing services, materials procurement and inventory management), logistics, after-sales services (including product repair, re-manufacturing and maintenance) and multiple component product offerings. Additionally, the Company provides market-specific design and engineering services ranging from contract design services, where the customer purchases services on a time and materials basis, to original product design and manufacturing services, where the customer purchases a product that was designed, developed and manufactured by the Company (commonly referred to as original design manufacturing, or ODM). ODM products are sold by the Company s OEM customers under the OEMs brand names. The Company s contract design and ODM services include user interface and industrial design, mechanical engineering and tooling design, electronic system design and printed circuit board design.

In November 2006, the Company completed its acquisition of International DisplayWorks, Inc. (IDW) in a stock-for-stock merger. In September 2006, the Company completed the sale of its software development and solutions business to an affiliate of Kohlberg Kravis Roberts & Co. (KKR). In August 2005, the Company sold its semiconductor division to AMIS Holdings, Inc., the parent company of AMI Semiconductor, Inc. The results of operations and balance sheet for the software development and solutions business and the semiconductor division are included in discontinued operations in the condensed consolidated financial statements. Refer to the discussion of the Company s acquisition and divestitures in Note M, Acquisitions and Divestitures. Refer also to Note N, Discontinued Operations.

NOTE B SUMMARY OF ACCOUNTING POLICIES

Basis of Presentation and Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP or GAAP) for interim financial information and in accordance with the requirements of Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements, and should be read in conjunction with the Company s audited consolidated financial statements as of and for the fiscal year ended March 31, 2006 contained in the Company s Annual Report on Form 10-K. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three- and nine-month periods ended December 31, 2006 are not necessarily indicative of the results that may be expected for the fiscal year ended March 31, 2007.

The Company s fiscal year ends on March 31 of each year. The first and second fiscal quarters end on the Friday closest to the last day of each respective calendar quarter. The third and fourth fiscal quarters end on December 31 and March 31, respectively.

Amounts included in the condensed consolidated financial statements are expressed in U.S. dollars.

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The accompanying unaudited condensed consolidated financial statements include the accounts of Flextronics and its majority-owned subsidiaries, after elimination of intercompany accounts and transactions. The Company consolidates all majority-owned subsidiaries and investments in entities in which the Company has a controlling interest. For consolidated majority-owned subsidiaries in which the Company owns less than 100%, the Company recognizes a minority interest for the ownership interest of the minority owner. As of December 31, 2006, minority interest was not material. As of March 31, 2006, minority interest was $23.4 million, of which $10.8 million is included in other liabilities and $12.6 million is included in long-term liabilities of discontinued operations in the condensed consolidated balance sheet. The associated minority interest expense has not been material to the Company s results of operations for the three- and nine-month periods ended December 31, 2006 and 2005, and has been classified, as applicable, within income from discontinued operations or as interest and other expense, net, in the condensed consolidated statements of operations.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Estimates are used in accounting for, among other things, allowances for doubtful accounts, inventory write-downs, valuation allowances for deferred tax assets, useful lives of property, equipment and intangible assets, asset impairments, fair values of derivative instruments and the related hedged items, restructuring charges, contingencies, capital leases, and the fair values of options granted under the Company s stock-based compensation plans. Actual results may differ from previously estimated amounts, and such differences may be material to the condensed consolidated financial statements. Estimates and assumptions are reviewed periodically, and the effects of revisions are reflected in the period they occur.

Translation of Foreign Currencies

The financial position and results of operations for certain of the Company s subsidiaries are measured using a currency other than the U.S. dollar as their functional currency. Accordingly, all assets and liabilities for these subsidiaries are translated into U.S. dollars at the current exchange rates as of the respective balance sheet date. Revenue and expense items are translated at the average exchange rates prevailing during the period. Cumulative gains and losses from the translation of these subsidiaries financial statements are reported as a separate component of shareholders equity. Foreign exchange gains and losses arising from transactions denominated in a currency other than the functional currency of the entity involved, and remeasurement adjustments for foreign operations where the U.S. dollar is the functional currency, are included in operating results.

Revenue Recognition

The Company recognizes manufacturing revenue when it ships goods or the goods are received by its customer, title and risk of ownership have passed, the price to the buyer is fixed or determinable and recoverability is reasonably assured. Generally, there are no formal customer acceptance requirements or further obligations related to manufacturing services. If such requirements or obligations exist, then the Company recognizes the related revenues at the time when such requirements are completed and the obligations are fulfilled. The Company makes provisions for estimated sales returns and other adjustments at the time revenue is recognized based upon contractual terms and an analysis of historical returns. These provisions were not material to the condensed consolidated financial statements for the three- and nine-month periods ended December 31, 2006 and 2005.

The Company provides a comprehensive suite of services for its customers that range from contract design to original product design to repair services. The Company recognizes service revenue when the services have been performed and the related costs are expensed as incurred. Net sales for services from continuing operations were less than 10% of the Company s total sales from continuing operations during the three- and nine-month periods ended December 31, 2006 and 2005, and accordingly, are included in net sales in the condensed consolidated statements of operations.

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Allowance for Doubtful Accounts

The Company performs ongoing credit evaluations of its customers financial condition and makes provisions for doubtful accounts based on the outcome of those credit evaluations. The Company evaluates the collectibility of its accounts receivable based on specific customer circumstances, current economic trends, historical experience with collections and the age of past due receivables. Unanticipated changes in the liquidity or financial position of the Company s customers may require additional provisions for doubtful accounts.

On October 8, 2005, Delphi Corporation (Delphi), a customer of the Company, filed for Chapter 11 bankruptcy, which resulted in the Company providing a bad debt provision of $15.0 million as a charge to selling, general and administrative expenses during the three-month period ended September 30, 2005. The Company reversed this $15.0 million bad debt reserve as a credit to selling, general and administrative expenses during the three-month period ended December 31, 2005, as the related accounts receivable were substantially collected.

Other Assets

The Company has certain investments in, and notes receivable from, non-publicly traded companies, which are included within other assets in the Company s condensed consolidated balance sheets. As of December 31, 2006 and March 31, 2006, the Company s investments in non-publicly traded companies totaled $250.9 million and $173.9 million, respectively, and notes receivable from certain of these non-majority owned investments totaled $334.8 million and $62.8 million, respectively. The increases in these investments and notes receivable during the nine-month period ended December 31, 2006 is primarily attributable to the divestiture of the Company s software development and solutions business as further discussed in Note M, Acquisitions and Divestitures. Non-majority-owned investments are accounted for using the equity method when the Company has an ownership percentage equal to or greater than 20%, or has the ability to significantly influence the operating decisions of the issuer; otherwise, the cost method is used. The Company monitors these investments for impairment and makes appropriate reductions in carrying values as required.

Other assets also include the Company s own investment participation in its trade receivables securitization program as further discussed in Note H, Trade Receivables Securitization.

Inventories

Inventories are stated at the lower of cost (on a first-in, first-out basis) or market value. The stated cost is comprised of direct materials, labor and overhead. The components of inventories related to continuing operations, net of applicable lower of cost or market write-downs, were as follows:

	As of	
	December 31, 2006	**March 31, 2006**
	(In thousands)	
Raw materials	$ 1,303,252	$ 884,940
Work-in-progress	521,511	335,061
Finished goods	710,388	518,309
Total	$ 2,535,151	$ 1,738,310

Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization is recognized on a straight-line basis over the estimated useful lives of the related assets (three to thirty years), with the exception of building leasehold improvements, which are amortized over the term of the lease, if shorter.

The Company reviews property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of property and equipment is measured by comparing its carrying amount to the projected undiscounted cash flows the property and equipment are expected to generate. An impairment loss is recognized when the carrying amount of a long-lived asset exceeds its fair

value.

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Deferred Income Taxes

The Company provides for income taxes in accordance with the asset and liability method of accounting for income taxes. Under this method, deferred income taxes are recognized for the tax consequences of temporary differences between the carrying amount and the tax basis of existing assets and liabilities by applying the applicable statutory tax rate to such differences.

Goodwill and Other Intangibles

Goodwill of our reporting units is tested for impairment each year as of January 31st and whenever events or changes in circumstances indicate that the carrying amount of goodwill may not be recoverable. Goodwill is tested for impairment at the reporting unit level by comparing the reporting unit s carrying amount, including goodwill, to the fair value of the reporting unit. Reporting units represent components of the Company for which discrete financial information is available that is regularly reviewed by management. For purposes of the annual goodwill impairment evaluation during fiscal year 2006, the Company identified three separate reporting units: Electronics Manufacturing Services, its Printed Circuit Board division and its Software Development and Solutions business. If the carrying amount of any reporting unit exceeds its fair value, the amount of impairment loss recognized, if any, is measured using a discounted cash flow analysis. Further, to the extent the carrying amount of the Company as a whole is greater than its market capitalization, all, or a significant portion of its goodwill may be considered impaired.

The following table summarizes the activity in the Company s goodwill account relating to continuing operations during the nine-month period ended December 31, 2006:

	Amount (In thousands)
Balance, beginning of the period	$ 2,676,727
Additions (1)	339,790
Reclassification to other intangibles (2)	(9,000)
Foreign currency translation adjustments	50,239
Balance, end of the period	$ 3,057,756

(1) Additions include approximately $198.2 million attributable to its November 2006 acquisition of International DisplayWorks, Inc., $94.3 million attributable to the May 2006 completion of the closing of Nortel s manufacturing system house in Calgary, Canada

and $47.3 million attributable to certain acquisitions that were not individually significant to the Company. Refer to the discussion of the Company s acquisitions in Note M, Acquisitions and Divestitures.

(2) Reclassification resulting from final allocation of the Company s intangible assets acquired through certain business combinations completed in a period subsequent to the respective period of acquisition, based on third-party valuations.

The Company s acquired intangible assets are subject to amortization over their estimated useful lives and are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an intangible may not be recoverable. An impairment loss is recognized when the carrying amount of an intangible asset exceeds its fair value. Intangible assets are primarily comprised of customer-related intangibles, which include contractual agreements and customer relationships, and licenses and other intangibles, which is primarily comprised of licenses and also includes patents and trademarks, and developed technologies. Customer-related intangibles are amortized on a straight-line basis generally over a period of up to eight years, and licenses and other intangibles over a period of up to five years. No residual value is estimated for any intangible assets. During the nine-month period ended December 31, 2006, there were approximately $61.8 million of additions to intangible assets related to customer-related intangibles and approximately $48.1 million related to acquired licenses. The fair value of the Company s intangible assets purchased through business combinations is principally determined based on management s estimates

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of cash flow and recoverability. The Company is in the process of determining the fair value of its intangible assets acquired from certain acquisitions. Such valuations are completed within one year of purchase. The components of acquired intangible assets relating to continuing operations are as follows:

	As of					
	December 31, 2006			March 31, 2006		
	Gross Carrying Amount	Accumulated Amortization (In thousands)	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization (In thousands)	Net Carrying Amount
Intangible assets:						
Customer-related intangibles	$ 211,338	$ (57,208)	$ 154,130	$ 150,471	$ (36,086)	$ 114,385
Licenses and other intangibles	74,804	(27,032)	47,772	26,521	(25,842)	679
Total	$ 286,142	$ (84,240)	$ 201,902	$ 176,992	$ (61,928)	$ 115,064

Total intangible amortization expense recognized from continuing operations was $7.8 million and $23.5 million during the three- and nine-month periods ended December 31, 2006, respectively, and $8.9 million and $28.9 million during the three- and nine-month periods ended December 31, 2005, respectively. The estimated future annual amortization expense related to acquired intangible assets from continuing operations is as follows:

Fiscal Years Ending March 31,	Amount (In thousands)
2007	$ 8,403(1)
2008	46,329
2009	41,365
2010	36,915
2011	31,306
Thereafter	37,584
Total amortization expense	$ 201,902

(1) Represents estimated amortization for the three-month period ending March 31, 2007.

Derivative Instruments and Hedging Activities

All derivative instruments are recognized on the balance sheet at fair value. If the derivative instrument is designated as a cash flow hedge, effectiveness is measured on a quarterly basis by calculating the ratio of the cumulative change in the fair value of the derivative instrument to the cumulative change in the hedged item. The effective portion of changes in the fair value of the derivative instrument is recognized in shareholders equity as a separate component of accumulated other comprehensive income (loss), and recognized in the condensed consolidated statements of operations when the hedged item affects earnings. Ineffective portions of changes in the fair value of

cash flow hedges are recognized in earnings immediately. If the derivative instrument is designated as a fair value hedge, the changes in the fair value of the derivative instrument and of the hedged item attributable to the hedged risk are recognized in earnings in the current period.

Restructuring Charges

The Company recognizes restructuring charges related to its plans to close or consolidate duplicate manufacturing and administrative facilities. In connection with these activities, the Company records restructuring charges for employee termination costs, long-lived asset impairment and other exit-related costs.

The recognition of restructuring charges requires the Company to make certain judgments and estimates regarding the nature, timing and amount of costs associated with the planned exit activity. To the extent the Company s actual results differ from its estimates and assumptions, the Company may be required to revise the estimates of future liabilities, requiring the recognition of additional restructuring charges or the reduction of liabilities already recognized. Such changes to previously estimated amounts may be material to the condensed consolidated financial statements. At the end of each reporting period, the Company evaluates the remaining accrued balances to ensure that no excess accruals are retained and the utilization of the provisions are for their intended purpose in accordance with developed exit plans.

Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS 157), which defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands the requisite disclosures for fair value measurements. SFAS 157 is effective in fiscal years beginning after November 15, 2007 and is required to be adopted by the Company in the first quarter of fiscal year 2009. The Company is currently assessing the impact of adopting SFAS 157 on its consolidated results of operations and financial condition.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 158, *Employer s Accounting for Defined Benefit Pension and Other Post-retirement Plans*, *an amendment of FASB Statements No. 87, 88, 106, and 132R* (SFAS 158). This statement requires recognition of the over-funded or under-funded status of defined benefit post-retirement plans as an asset or liability, respectively, in the statement of financial position and to recognize changes in that funded status in comprehensive income in the year in which changes occur. SFAS 158 also requires measurement of the funded status of a plan as of the date of the statement of financial position. SFAS 158 is effective for recognition of the funded status of benefit plans for fiscal years ending after December 15, 2006 and is required to be adopted by the Company in the current fiscal year. The measurement date provisions of SFAS 158 are effective for fiscal years ending after December 15, 2008 and is required to be adopted by the Company beginning in fiscal year 2009. The Company is currently evaluating the effect of adopting SFAS 158 on its consolidated results of operations and financial condition.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48) as an interpretation of FASB Statement No. 109, *Accounting for Income Taxes* (SFAS 109). This Interpretation clarifies the accounting for uncertainty in income taxes recognized by prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on de-recognition of tax benefits previously recognized and additional disclosures for unrecognized tax benefits, interest and penalties. The evaluation of a tax position in accordance with this Interpretation begins with a determination as to whether it is more likely than not that a tax position will be sustained upon examination based on the technical merits of the position. A tax position that meets the more-likely-than-not recognition threshold is then measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement for recognition in the financial statements. FIN 48 is effective no later than fiscal years beginning after December 15, 2006, and is required to be adopted by the Company in the first quarter of fiscal year 2008. The Company is currently assessing the impact of adopting FIN 48 on its consolidated results of operations and financial condition.

In September 2006, the FASB published FASB Staff Position (FSP) No. AUG AIR-1, *Accounting for Planned Maintenance Activities*, which eliminates the accrue-in-advance method of accounting for planned major maintenance activities. The FSP is effective for fiscal years beginning after December 15, 2006 and is required to be adopted by the Company beginning in the first quarter of fiscal year 2008. Any changes resulting from adoption is to be considered a change in accounting principle with retrospective application as prescribed in SFAS 154, *Accounting Changes and Error Corrections*, if practical. The adoption of the FSP is not expected to have a material effect on the Company s consolidated results of operations, financial condition and cash flows.

In September 2006, the SEC released Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements*, (SAB 108), which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. Pursuant to SAB 108, registrants are required to quantify errors using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. SAB 108 is effective for fiscal years ending after November 15, 2006 and is required to be applied by the Company in the current fiscal year. The Company does not believe that the application of SAB 108 will have a material effect on the Company s consolidated results of operations or financial condition.

NOTE C STOCK-BASED COMPENSATION

Equity Compensation Plans

As of December 31, 2006, the Company grants equity compensation awards from three plans: the 2001 Equity Incentive Plan (the 2001 Plan), the 2002 Interim Incentive Plan (the 2002 Plan), and the 2004 Award Plan for New Employees (the 2004 Plan).

The 2001 Plan provides for grants of up to 32,000,000 ordinary shares (plus shares available under prior Company plans and assumed plans consolidated into the 2001 Plan). The 2001 Plan provides for grants of incentive and nonqualified stock options and share bonus awards to employees, officers and non-employee directors, and also contains an automatic option grant program for non-employee directors. Options issued under the 2001 Plan generally vest over four years and generally expire ten years from the date of grant, except that options granted to non-employee directors expire five years from the date of grant.

The 2002 Plan provides for grants of up to 20,000,000 ordinary shares. The 2002 Plan provides for grants of nonqualified stock options and share bonus awards to employees and officers. Options issued under the 2002 Plan generally vest over four years and generally expire ten years from the date of grant.