VEECO INSTRUMENTS INC
Form 10-Q
November 06, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 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 0-16244

VEECO INSTRUMENTS INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**11-2989601** (I.R.S. Employer Identification Number)
100 Sunnyside Boulevard, Suite B **Woodbury, New York** (Address of Principal Executive Offices)	**11797-2902** (Zip Code)

Registrant s telephone number, including area code: **(516) 677-0200**

Website: **www.veeco.com**

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 x 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 o Accelerated filer x 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 x

31,076,375 shares of common stock, $0.01 par value per share, were outstanding as of the close of business on October 30, 2006.

SAFE HARBOR STATEMENT

This Quarterly Report on Form 10-Q (the 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. Discussions containing such forward-looking statements may be found in Items 2 and 3 hereof, as well as within this Report generally. In addition, when used in this Report, the words believes, anticipates, expects, estimates, plans, intends, and similar expressions are intended to identify forward-looking statements. All forward-looking statements are subject to a number of risks and uncertainties that could cause actual results to differ materially from projected results. These risks and uncertainties include, without limitation, the following:

- The cyclicality of the microelectronics industries we serve directly affects our business.
- We operate in an industry characterized by rapid technological change.
- We face significant competition.
- We depend on a limited number of customers that operate in highly concentrated industries.
- Our quarterly operating results fluctuate significantly.
- We face securities class action and shareholder derivative lawsuits which could result in substantial costs, diversion of management s attention and resources and negative publicity.
- Our acquisition strategy subjects us to risks associated with evaluating and pursuing these opportunities and integrating these businesses.
- Any difficulty or inability to attract, retain and motivate key employees could have a material adverse effect on our business.
- We are exposed to the risks of operating a global business and the requirement to comply with laws and regulations of various jurisdictions such as import/export controls, which may not apply to our non-U.S. competitors.
- We are subject to foreign currency exchange risks.
- Our success depends on protection of our intellectual property rights.
- We may be subject to claims of intellectual property infringement by others.
- We rely on a limited number of suppliers.
- Our outsourcing strategy could adversely affect our results of operations.
- Changes in accounting standards for stock-based compensation may adversely affect our stock price and our ability to attract, motivate and retain key employees.
- The implementation of a new information technology system may disrupt our operations.
- We may not obtain sufficient affordable funds to finance our future needs.

- We are subject to risks of non-compliance with environmental and safety regulations.

- We have adopted certain measures that may have anti-takeover effects which may make an acquisition of our company by another company more difficult.

- The other matters discussed under the heading Management s Discussion and Analysis of Financial Condition and Results of Operations contained in this Report and in the Annual Report on Form 10-K for the year ended December 31, 2005 of Veeco Instruments Inc. (Veeco or the Company).

Consequently, such forward-looking statements should be regarded solely as the Company s current plans, estimates and beliefs. The Company does not undertake any obligation to update any forward-looking statements to reflect future events or circumstances after the date of such statements.

Available Information

We file annual, quarterly and current reports, information statements and other information with the Securities and Exchange Commission (the SEC). The public may read and copy any materials we file with the SEC at the SEC s Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of that site is http://www.sec.gov.

Internet Address

We maintain a website where additional information concerning our business and various upcoming events can be found. The address of our website is www.veeco.com. We provide a link on our website, under Investors Financial Information SEC Filings, through which investors can access our filings with the SEC, including our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and all amendments to those reports. These filings are posted to our Internet site, as soon as reasonably practicable after we electronically file such material with the SEC.

VEECO INSTRUMENTS INC.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

Veeco Instruments Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
(In thousands, except per share data)
(Unaudited)

	Three Months Ended September 30, 2006	**2005**
Net sales	$ 112,369	$ 100,078
Cost of sales	64,513	55,816
Gross profit	47,856	44,262
Costs and expenses:		
Selling, general and administrative expense	22,296	21,210
Research and development expense	15,716	14,388
Amortization expense	4,025	4,038
Write-off of purchased in-process technology	1,160	
Other (income) expense, net	(310)	413
Total operating expenses	42,887	40,049
Operating income	4,969	4,213
Interest expense, net	1,056	1,815
Income before income taxes and noncontrolling interest	3,913	2,398
Income tax provision	612	832
Noncontrolling interest	(1,207)	
Net income	$ 4,508	$ 1,566
Net income per common share	$ 0.15	$ 0.05
Diluted net income per common share	$ 0.14	$ 0.05
Weighted average shares outstanding	30,693	29,965
Diluted weighted average shares outstanding	31,393	30,360

See accompanying notes.

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Veeco Instruments Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
(In thousands, except per share data)
(Unaudited)

	Nine Months Ended September 30, 2006	2005
Net sales	$ 317,922	$ 297,343
Cost of sales	178,585	172,123
Gross profit	139,337	125,220
Costs and expenses:		
Selling, general and administrative expense	68,622	62,816
Research and development expense	45,554	45,075
Amortization expense	12,029	12,554
Write-off of purchased in-process technology	1,160	
Other (income) expense, net	(243)	385
Total operating expenses	127,122	120,830
Operating income	12,215	4,390
Interest expense, net	3,583	5,920
Gain on extinguishment of debt	(330)	
Income (loss) before income taxes and noncontrolling interest	8,962	(1,530)
Income tax provision	2,878	2,055
Noncontrolling interest	(1,207)	
Net income (loss)	$ 7,291	$ (3,585)
Net income (loss) per common share	$ 0.24	$ (0.12)
Diluted net income (loss) per common share	$ 0.23	$ (0.12)
Weighted average shares outstanding	30,369	29,894
Diluted weighted average shares outstanding	31,100	29,894

See accompanying notes.

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Veeco Instruments Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(In thousands)

	September 30, 2006 (Unaudited)	December 31, 2005
Assets		
Current assets:		
Cash and cash equivalents	$ 126,565	$ 124,499
Accounts receivable, less allowance for doubtful accounts of $2,331 in 2006 and $1,860 in 2005	87,049	89,230
Inventories	104,689	88,904
Prepaid expenses and other current assets	13,107	9,640
Deferred income taxes	3,531	2,870
Total current assets	334,941	315,143
Property, plant and equipment at cost, less accumulated depreciation of $84,857 in 2006 and $77,954 in 2005	71,684	69,806
Goodwill	100,898	99,622
Purchased technology, less accumulated amortization of $61,548 in 2006 and $51,992 in 2005	47,045	55,776
Other intangible assets, less accumulated amortization of $25,539 in 2006 and $22,274 in 2005	25,543	26,899
Other assets	428	614
Total assets	$ 580,539	$ 567,860
Liabilities and shareholders equity		
Current liabilities:		
Accounts payable	$ 36,429	$ 31,289
Accrued expenses	51,617	51,169
Deferred profit	758	537
Income taxes payable	2,054	2,123
Current portion of long-term debt	393	375
Total current liabilities	91,251	85,493
Deferred income taxes	2,418	1,048
Long-term debt	208,907	229,205
Other non-current liabilities	3,097	3,527
Noncontrolling interest	1,793	
Shareholders equity	273,073	248,587
Total liabilities and shareholders equity	$ 580,539	$ 567,860

See accompanying notes.

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Veeco Instruments Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Nine Months Ended September 30, 2006	2005
Operating activities		
Net income (loss)	$ 7,291	$ (3,585)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	22,426	22,403
Deferred income taxes	291	(254)
Gain on extinguishment of debt	(330)	
Non-cash compensation expense for share-based payments	1,443	72
Noncontrolling interest in net loss of subsidiary	(1,207)	
Write-off of purchased in-process technology	1,160	
(Gain) loss on sale of property plant and equipment	(27)	346
Changes in operating assets and liabilities:		
Accounts receivable	3,103	(4,876)
Inventories	(14,691)	10,177
Accounts payable	5,025	7,642
Accrued expenses, deferred profit and other current liabilities	3,159	1,179
Other, net	(5,119)	(3,645)
Net cash provided by operating activities	22,524	29,459
Investing activities		
Capital expenditures	(12,473)	(8,553)
Payments for net assets of businesses acquired	(3,068)	(15,038)
Proceeds from sale of property, plant and equipment and assets held for sale	35	2,260
Net maturities of investments	(128)	(70)
Net cash used in investing activities	(15,634)	(21,401)
Financing activities		
Proceeds from stock issuance	15,082	1,820
Repayments of long-term debt	(19,680)	(264)
Net cash (used in) provided by financing activities	(4,598)	1,556
Effect of exchange rates on cash and cash equivalents	(226)	1,813
Net change in cash and cash equivalents	2,066	11,427
Cash and cash equivalents at beginning of period	124,499	100,276
Cash and cash equivalents at end of period	$ 126,565	$ 111,703

Non-Cash Items

During the nine months ended September 30, 2006, the Company had non-cash items excluded from the Condensed Consolidated Statements of Cash Flows of approximately $6.3 million. This amount consisted of (1) $1.5 million reflecting the transfer of demonstration and lab equipment from property, plant and equipment to inventory; (2) $0.7 million for the transfer of inventory to property, plant and equipment; and (3) $3.5 million fair value of assets acquired and $0.6 million of liabilities assumed in connection with the consolidation of a variable interest entity (See Note 7   Business Acquisition and Related Party Transaction).

During the nine months ended September 30, 2005, the Company had non-cash items excluded from the Condensed Consolidated Statements of Cash Flows of approximately $4.2 million. This amount consists of (1) $1.8 million of additional purchase price relating to the acquisition of Manufacturing Technology Inc., which resulted in a corresponding increase to goodwill; (2) $1.3 million for the transfer of property, plant and equipment to inventory; and (3) $1.1 million for the accrual of a contingent earn-out payment to the former shareholders of Nanodevices Inc. related to the achievement of certain revenue targets during the third quarter of 2005, which was paid in the second quarter of 2006, and has been reflected as additional goodwill.

See accompanying notes.

VEECO INSTRUMENTS INC. AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1 Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation (consisting of normal recurring accruals) have been included. Operating results for the three and nine months ended September 30, 2006, are not necessarily indicative of the results that may be expected for the year ending December 31, 2006. For further information, refer to the financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005.

Earnings (Loss) Per Share

The following table sets forth the reconciliation of weighted average shares outstanding and diluted weighted average shares outstanding:

	Three months ended September 30,		Nine months ended September 30,	
	2006	**2005**	**2006**	**2005**
	(In thousands)			
Weighted average shares outstanding	30,693	29,965	30,369	29,894
Dilutive effect of stock options and restricted stock awards and units	700	395	731	
Diluted weighted average shares outstanding	31,393	30,360	31,100	29,894

Net income and diluted net income per common share are computed using the weighted average number of common and common equivalent shares outstanding during the period. The effect of approximately 212,000 common equivalent shares for the nine months ended September 30, 2005, were anti-dilutive and therefore, are not included in the weighted average shares outstanding.

In addition, the effect of the assumed conversion of convertible subordinated notes into approximately 5.2 million and 5.3 million common equivalent shares is antidilutive and therefore, is not included in the weighted shares outstanding for the three and nine months ended September 30, 2006, respectively. The effect of the assumed conversion of convertible subordinated notes into approximately 5.7 million common equivalent shares is antidilutive and therefore, is not included in the weighted average shares outstanding for the comparable prior year periods.

Share-Based Compensation

As of September 30, 2006, the Company has stock option and restricted stock plans, which are described more fully in Note 2. The Company also assumed certain stock option plans and agreements in connection with various acquisitions, as also discussed in Note 2. Prior to 2006, the Company accounted for these stock option plans under the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees,* and related interpretations and generally, no compensation expense was reflected in net income as options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), *Share-Based Payment*, which is a revision of SFAS No. 123, *Accounting for Stock-Based Compensation*, supersedes APB No. 25 and amends SFAS No. 95, *Statement of Cash Flows*. SFAS No. 123(R) requires all share-based payments to employees and non-employee directors, including grants of stock options, to be recognized in the income statement based on their fair values. Pro forma disclosure is no longer an alternative. SFAS No. 123(R) was adopted using the modified prospective method of application, which requires Veeco to recognize compensation expense on a prospective basis. Therefore, prior period financial statements have not been restated. Under this method, in addition to reflecting compensation expense for new share-based awards, expense

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is also recognized to reflect the remaining service period of awards that had been included in the pro forma disclosures in prior periods. SFAS No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under previous accounting literature, which has the effect of reducing consolidated cash flows from operations and increasing cash flows from financing activities in periods after adoption. For the three and nine months ended September 30, 2006, the Company did not recognize any amount of consolidated financing cash flows for such excess tax deductions.

Total share-based compensation expense is attributable to the remaining requisite service periods of stock options and restricted common stock awards and units. For the three months ended September 30, 2006, the Company granted 9,900 restricted common stock awards and units to its employees. For the nine months ended September 30, 2006, the Company granted 146,200 stock options and 208,150 restricted common stock awards and units to its directors, officers and employees. As a result of adopting SFAS No. 123(R), the Company s net income for the three and nine months ended September 30, 2006 was $0.1 million and $0.4 million lower, respectively, than if it had continued to account for share-based compensation under APB No. 25. Net income per common share and diluted net income per common share for the three and nine months ended September 30, 2006, are approximately $0.01 lower for both periods, than if the Company had continued to account for share-based compensation under APB No. 25. As of September 30, 2006, the total unrecognized compensation cost related to nonvested stock awards and option awards is $4.2 million and $1.4 million, respectively, and the related weighted average period over which it is expected that such unrecognized compensation costs will be recognized is approximately 2.3 years for the nonvested stock awards and 2.2 years for option awards. Future share-based compensation expense will depend on levels of share-based awards granted in the future and, therefore, cannot be predicted at this time.

Prior to the Company s adoption of SFAS No. 123(R), SFAS No. 123 required that the Company provide pro forma information regarding net loss and loss per share as if compensation cost for the Company s stock-based awards had been determined in accordance with the fair value method prescribed therein. In accordance with SFAS No. 123, the following table illustrates the effect on net loss and net loss per share if the Company had applied the fair value recognition provisions, under which compensation expense would be recognized as incurred, to stock-based employee compensation.

	Three months ended September 30, 2005			**Nine months ended September 30, 2005**		
	(In thousands, except per share amounts)					
Net income (loss), as reported	$	1,566		$	(3,585	)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(3,904		)	(29,121		)
Pro forma net loss	$	(2,338	)	$	(32,706	)
Net income (loss) per common share:						
Net income (loss) and diluted net income (loss) per common share, as reported	$	0.05		$	(0.12	)
Net loss and diluted net loss per common share, pro forma	$	(0.08	)	$	(1.09	)

Recent Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. (FIN) 48, *Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, Accounting for Income Taxes.* FIN 48 clarifies the accounting and disclosure for income taxes by defining the threshold for recognizing the benefits of tax return positions in the financial statements as more-likely-than-not to be sustained by the taxing authority. It also provides guidance on derecognition, measurement and classification of income tax uncertainties, along with any related interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently assessing the impact of FIN 48 on its consolidated financial position and results of operations.

In September 2006, the FASB issued FASB Statement No. 157, *Fair Value Measurements*. Statement No. 157 establishes a common definition for fair value to be applied to U.S. generally accepted accounting principles requiring use of fair value, establishes a framework for measuring fair value, and expands disclosure about such fair value measurements. Statement No. 157 is effective for fiscal years beginning after November 15, 2007. The adoption of this statement is not expected to have a material impact on the Company s consolidated financial position and results of operations.

In September 2006, the FASB issued FASB Statement No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans*. Statement No. 158 improves financial reporting by requiring an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. This Statement also improves financial reporting by requiring an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. The recognition and disclosure provisions of Statement No. 158 are effective for fiscal years ending after December 15, 2006. The requirement to measure plan assets and benefit obligations as of the date of the employer s fiscal year-end statement of financial position is effective for fiscal years ending after December 15, 2008. The adoption of this statement is not expected to have a material impact on the Company s consolidated financial position and results of operations.

Reclassifications

Certain amounts in the 2005 condensed consolidated financial statements have been reclassified to conform to the 2006 presentation.

Note 2 Share-Based Payments

Stock Option and Restricted Stock Plans

The Company has several stock option and restricted stock plans. The Veeco Instruments Inc. 2000 Stock Incentive Plan, as amended, (the 2000 Plan), was approved by the Board of Directors and shareholders in May 2000. The 2000 Plan provides for the grant to officers and key employees of up to 8,530,000 options (2,114,174 options are available for future grants as of September 30, 2006) to purchase shares of common stock of the Company. Stock options granted pursuant to the 2000 Plan expire after seven years and generally become exercisable over a three-year period following the grant date. However, grants made under the 2000 Plan between June 17, 2005 and December 23, 2005 became exercisable on or before December 31, 2005, and are subject to a resale restriction which provides that the shares issuable upon exercise of the option may not be transferred prior to the second anniversary of the option grant date. In addition, the 2000 Plan provides for automatic annual grants of 5,000 shares of restricted stock to each member of the Board of Directors of the Company who is not an employee of the Company. Up to 1,700,000 of the awards authorized under the 2000 Plan may be issued in the form of restricted stock (1,471,650 shares are available for future grants as of September 30, 2006). For the nine months ended September 30, 2006, the Company granted 164,650 shares of restricted common stock and 3,500 restricted stock units to key employees, which vest over three years, and in May 2006, granted 40,000 shares of restricted common stock to the non-employee members of the Board of Directors, which vest over a period of one year.

A summary of the Company s restricted stock awards including restricted stock units as of September 30, 2006, is presented below:

	Shares (000 s)		Weighted-Average Grant-Date Fair Value	
Nonvested at beginning of year	45		$	15.60
Granted	208		24.22	
Vested				
Forfeited	(25	)	23.61	
Nonvested at September 30, 2006	228		$	22.60

The Veeco Instruments Inc. 2000 Stock Option Plan for Non-Officer Employees (the Non-Officer Plan) was approved by the Board of Directors in October 2000. The Non-Officer Plan provided for the grant of stock options to non-officer employees to purchase shares of common stock of the Company. Stock options granted pursuant to the Non-Officer Plan become exercisable over a three-year period following the grant date and expire after seven years.

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The Veeco Instruments Inc. Amended and Restated 1992 Employees Stock Option Plan (the 1992 Plan) provided for the grant to officers and key employees of stock options to purchase shares of common stock of the Company. Stock options granted pursuant to the 1992 Plan become exercisable over a three-year period following the grant date and expire after ten years.

The Veeco Instruments Inc. 1994 Stock Option Plan for Outside Directors, as amended, (the Directors Option Plan), provided for automatic annual grants of stock options to each member of the Board of Directors of the Company who is not an employee of the Company. Such options are exercisable immediately and expire after ten years.

The Non-Officer Plan, the 1992 Plan and the Directors Option Plan have been frozen; and, thus, there are no options available for future grant as of September 30, 2006 under these plans.

In addition to the plans described above, the Company assumed certain stock option plans and agreements relating to the merger in September 2001 with Applied Epi, Inc. (Applied Epi). These stock option plans do not have options available for future grants and expire after ten years from the date of grant. Options granted under two of the plans vested over three years and options granted under one of the plans vested immediately. As of September 30, 2006, there are 197,192 options outstanding under the various Applied Epi plans. In addition, Veeco assumed certain warrants related to Applied Epi, which were in effect prior to the merger with Veeco. These warrants expired in February 2006.

In May 2000, the Company assumed certain stock option plans and agreements related to CVC, Inc. and Commonwealth Scientific Corporation, a subsidiary of CVC, Inc., which were in effect prior to the merger with Veeco. These plans do not have options available for future grants, the options granted thereunder generally vested over a three to five year period and expire five to ten years from the date of grant. As of September 30, 2006, there are 6,965 options outstanding under the various CVC, Inc. and Commonwealth Scientific Corporation plans.

With the adoption of SFAS No. 123(R) on January 1, 2006, the Company is required to record the fair value of stock-based compensation awards as an expense. In order to determine the fair value of stock options on the date of grant, the Company applies the Black-Scholes option-pricing model. Inherent in the model are assumptions related to expected stock-price volatility, option life, risk-free interest rate and dividend yield. While the risk-free interest rate and dividend yield are less subjective assumptions, typically based on factual data derived from public sources, the expected stock-price volatility and option life assumptions require a level of judgment which make them critical accounting estimates.

Beginning in the fourth quarter of 2005, the Company used an expected stock-price volatility assumption that is a combination of both historical and implied volatilities of the underlying stock, which are obtained from public data sources. Prior to that time, the Company based this assumption solely on historical volatility.

With regard to the weighted-average option life assumption, the Company considers the exercise behavior of past grants and models the pattern of aggregate exercises.

The fair value of each option granted during the nine months ended September 30, 2006, was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

Weighted-average expected stock-price volatility	40	%
Weighted-average expected option life	3 years	
Average risk-free interest rate	4.99	%
Average dividend yield	0	%

No options were granted in the third quarter of 2006.

The fair value of each option grant that was unvested as of January 1, 2006, was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

Weighted-average expected stock-price volatility	60	%
Weighted-average expected option life	4 years	
Average risk-free interest rate	3.64	%
Average dividend yield	0	%

A summary of the Company s stock option plans as of and for the nine months ended September 30, 2006, is presented below:

	Shares (000 s)		Weighted-Average Exercise Price		Aggregate Intrinsic Value (000s)		Weighted-Average Remaining Contractual Life (in years)
Outstanding at beginning of year	7,834		$	24.81			
Granted	146		23.61				
Exercised	(822	)	18.23				
Forfeited (including cancelled options)	(639	)	24.98				
Outstanding at September 30, 2006	6,519		$	25.59	$	7,868	3.3
Options exercisable at September 30, 2006	6,312		$	25.73	$	7,655	–––––3.2

The weighted-average grant date fair value of stock options granted for the nine months ended September 30, 2006 was $7.61 per option. The weighted-average grant date fair value of stock options granted for the three and nine months ended September 30, 2005 was $9.54 and $8.08 per option, respectively. The total intrinsic value of stock options exercised during the three and nine months ended September 30, 2006 was $1.2 million and $4.4 million, respectively. The total intrinsic value of stock options exercised during the three and nine months ended September 30, 2005 was $0.5 million and $0.6 million, respectively.

The following table summarizes information about stock options outstanding at September 30, 2006:

	Options Outstanding					Options Exercisable			
Range of Exercise Prices	Number Outstanding at September 30, 2006 (000 s)	Weighted-Average Remaining Contractual Life (in years)		Weighted-Average Exercise Price		Number Outstanding at September 30, 2006 (000 s)		Weighted-Average Exercise Price	
$0.27	93	4.3		$	0.27	93		$	0.27
10.26-15.35									