

EASTMAN KODAK CO  
Form 10-Q  
November 01, 2007

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

**FORM 10-Q**

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

For the quarterly period ended September 30, 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**  
(State of incorporation)

**16-0417150**  
(IRS Employer Identification No.)

**343 STATE STREET, ROCHESTER, NEW YORK**  
(Address of principal executive offices)

**14650**  
(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  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    Accelerated filer     Non-accelerated filer

[X] [ ]

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.

**Number of Shares Outstanding at  
October 26, 2007  
287,976,505**

**Class  
Common Stock, \$2.50 par value**

PAGE 2

**Eastman Kodak Company  
Form 10-Q  
September 30, 2007**

**Table of Contents**

	<b>Page</b>
<b><u>Part I.</u></b>	
	<b><u>Financial Information</u></b>
Item 1.	<u>Financial Statements</u> 3
	<u>Consolidated Statement of Operations (Unaudited)</u> 3
	<u>Consolidated Statement of Retained Earnings (Unaudited)</u> 4
	<u>Consolidated Statement of Financial Position (Unaudited)</u> 5
	<u>Consolidated Statement of Cash Flows (Unaudited)</u> 6
	<u>Notes to Financial Statements (Unaudited)</u> 7
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> 25
	<u>Liquidity and Capital Resources</u> 46
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u> 53
Item 4.	<u>Controls and Procedures</u> 54
<b><u>Part II.</u></b>	
	<b><u>Other Information</u></b>
Item 1.	<u>Legal Proceedings</u> 54
Item 6.	<u>Exhibits</u> 54
	<u>Signatures</u> 55
	<u>Index to Exhibits</u> 56

PAGE 3

**Part I. Financial Information**

**Item 1. Financial Statements**

**EASTMAN KODAK COMPANY**  
**CONSOLIDATED STATEMENT OF OPERATIONS (Unaudited)**

(in millions, except per share data)	Three Months Ended September 30		Nine Months Ended September 30	
	2007	2006	2007	2006
Net sales	\$ 2,581	\$ 2,595	\$ 7,210	
Cost of goods sold	1,899	1,944	5,453	
Gross profit	682	651	1,757	
Selling, general and administrative expenses	427	464	1,259	
Research and development costs	129	138	398	
Restructuring costs and other	100	108	480	
Other operating expenses (income), net	6	(48)	(33)	
Earnings (loss) from continuing operations before interest, other income (charges), net and income taxes	20	(11)	(347)	
Interest expense	28	51	84	
Other income (charges), net	37	9	75	
Earnings (loss) from continuing operations before income taxes	29	(53)	(356)	
(Benefit) provision for income taxes	(5)	30	(64)	
Earnings (loss) from continuing operations	34	(83)	(292)	
Earnings from discontinued operations, net of income taxes	3	46	753	
<b>NET EARNINGS (LOSS)</b>	<b>\$ 37</b>	<b>\$ (37)</b>	<b>\$ 461</b>	
Basic and diluted net earnings (loss) per share:				
Continuing operations	\$ 0.12	\$ (0.29)	\$ (1.02)	
Discontinued operations	0.01	0.16	2.62	
Total	\$ 0.13	\$ (0.13)	\$ 1.60	
Number of common shares used in basic net earnings (loss) per share	287.8	287.2	287.6	
Incremental shares from assumed conversion of options	0.8	□	□	
Number of common shares used in diluted net earnings (loss) per share	288.6	287.2	287.6	

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

PAGE 4

**EASTMAN KODAK COMPANY**  
**CONSOLIDATED STATEMENT OF RETAINED EARNINGS (Unaudited)**

(in millions)	Three Months Ended September 30		Nine Months Ended September 30	
	2007	2006	2007	2006
Retained earnings at beginning of period	\$ 6,305	\$ 6,062	\$ 5,967	\$ 6,717
Net earnings (loss)	37	(37)	461	(617)
Cash dividends	□	□	(72)	(72)
Loss from issuance of treasury stock	(9)	(3)	(23)	(6)
Retained earnings at end of period	\$ 6,333	\$ 6,022	\$ 6,333	\$ 6,022

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

**EASTMAN KODAK COMPANY**  
**CONSOLIDATED STATEMENT OF FINANCIAL POSITION (Unaudited)**

(in millions)	September 30, 2007	December 31, 2006
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 1,847	\$ 1,469
Receivables, net	2,130	2,072
Inventories, net	1,230	1,001
Deferred income taxes	114	108
Other current assets	123	96
Assets of discontinued operations		811
Total current assets	5,444	5,557
Property, plant and equipment, net	1,906	2,602
Goodwill	1,636	1,584
Other long-term assets	3,945	3,509
Assets of discontinued operations		1,068
<b>TOTAL ASSETS</b>	<b>\$ 12,931</b>	<b>\$ 14,320</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable and other current liabilities	\$ 3,387	\$ 3,712
Short-term borrowings	330	64
Accrued income and other taxes	303	347
Liabilities of discontinued operations		431
Total current liabilities	4,020	4,554
Long-term debt, net of current portion	1,296	2,714
Pension and other postretirement liabilities	3,428	3,934
Other long-term liabilities	1,529	1,690
Liabilities of discontinued operations		40
Total liabilities	10,273	12,932
Commitments and Contingencies (Note 7)		
<b>SHAREHOLDERS' EQUITY</b>		
Common stock, \$2.50 par value	978	978
Additional paid in capital	884	881
Retained earnings	6,333	5,967
Accumulated other comprehensive income (loss)	229	(635)
	8,424	7,191
Less: Treasury stock, at cost	5,766	5,803
Total shareholders' equity	2,658	1,388
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b>\$ 12,931</b>	<b>\$ 14,320</b>

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

**EASTMAN KODAK COMPANY**  
**CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)**

(in millions)	Nine Months Ended	
	2007	September 30, 2006
Cash flows from operating activities:		
Net earnings (loss)	\$ 461	\$ (617)
Adjustments to reconcile to net cash used in operating activities:		
Earnings from discontinued operations, net of income taxes	(753)	(167)
Depreciation and amortization	609	910
Gain on sales of businesses/assets	(39)	(49)
Non-cash restructuring costs, asset impairments and other charges	286	116
Benefit for deferred income taxes	(78)	(126)
(Increase) decrease in receivables	(30)	215
(Increase) decrease in inventories	(183)	31
Decrease in liabilities excluding borrowings	(846)	(490)
Other items, net	(121)	(140)
Total adjustments	(1,155)	300
Net cash used in continuing operations	(694)	(317)
Net cash (used in) provided by discontinued operations	(30)	245
Net cash used in operating activities	(724)	(72)
Cash flows from investing activities:		
Additions to properties	(179)	(253)
Net proceeds from sales of businesses/assets	146	112
Acquisitions, net of cash acquired	(2)	(3)
Investments in unconsolidated affiliates	□	(10)
Marketable securities - sales	123	89
Marketable securities - purchases	(131)	(88)
Net cash used in continuing operations	(43)	(153)
Net cash provided by (used in) discontinued operations	2,335	(29)
Net cash provided by (used in) investing activities	2,292	(182)
Cash flows from financing activities:		
Proceeds from other borrowings	65	580
Repayment of other borrowings	(1,213)	(827)
Dividends to shareholders	(72)	(72)
Exercise of employee stock options	5	□
Net cash used in financing activities	(1,215)	(319)
Effect of exchange rate changes on cash	25	10
Net increase (decrease) in cash and cash equivalents	378	(563)
Cash and cash equivalents, beginning of period	1,469	1,665
Cash and cash equivalents, end of period	\$ 1,847	\$ 1,102

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 disclosures 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:

- Gains and losses on sales of capital assets and certain asset impairment charges that were previously presented in other income (charges), net have been reclassified to other operating (income) expenses, net. Amounts reclassified for the three months and nine months ended September 30, 2006 were \$48 million of income and \$37 million of income, respectively.
- 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.

In preparing the financial statements for the three- and nine-month periods ended September 30, 2007, the Company recorded adjustments for items that should have been recorded in prior periods, the largest of which is a \$20 million tax provision for a valuation allowance recorded in the second quarter of 2007 that should have been recorded in 2006. This item is discussed further in Note 5, "Goodwill and Other Intangibles," and Note 6, "Income Taxes." Each correction recorded in the three- and nine-month periods ended September 30, 2007 is individually no greater than \$6 million, other than the item noted above. The Company has determined that these corrections, individually and in the aggregate, are not material to the financial statements as of and for the three- and nine-month periods ended September 30, 2007, to any prior period financial statements, or to its expected full year results for 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). 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, classification of interest and penalties, and disclosure. Further information regarding the adoption of FIN 48 is disclosed in Note 6, "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)	September 30, 2007	December 31, 2006
Trade receivables	\$ 1,729	\$ 1,737
Miscellaneous receivables	401	335
Total (net of allowances of \$117 and \$134 as of September 30, 2007 and December 31, 2006, respectively)	\$ 2,130	\$ 2,072

Of the total trade receivable amounts of \$1,729 million and \$1,737 million as of September 30, 2007 and December 31, 2006, respectively, approximately \$215 million and \$272 million, respectively, 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.

PAGE 9

**NOTE 3: INVENTORIES, NET**

(in millions)	September 30, 2007	December 31, 2006
Finished goods	\$ 762	\$ 606
Work in process	272	192
Raw materials	196	203

Total \$ 1,230 \$ 1,001

**NOTE 4: PROPERTY, PLANT AND EQUIPMENT, NET**

(in millions)	September 30, 2007	December 31, 2006
Land	\$ 92	\$ 91
Buildings and building improvements	1,857	2,319
Machinery and equipment	5,875	7,153
Construction in progress	34	86
	7,858	9,649
Accumulated depreciation	(5,952)	(7,047)
Net properties	\$ 1,906	\$ 2,602

Depreciation expense for the three months ended September 30, 2007 and 2006 was \$136 million and \$243 million, respectively, of which approximately \$23 million and \$73 million, respectively, represented accelerated depreciation in connection with restructuring actions. Depreciation expense for the nine months ended September 30, 2007 and 2006 was \$526 million and \$820 million, respectively, of which approximately \$103 million and \$213 million, respectively, represented accelerated depreciation in connection with restructuring actions.

In April 2007, the Company entered into an agreement to sell its manufacturing site in Xiamen, China. This sale closed in the second quarter of 2007 and resulted in a reduction to net properties of approximately \$278 million. This action is part of the 2004-2007 Restructuring Program.

**NOTE 5: GOODWILL AND OTHER INTANGIBLE ASSETS**

Goodwill was \$1,636 million and \$1,584 million at September 30, 2007 and December 31, 2006, respectively. The changes in the carrying amount of goodwill by reportable segment for the nine months ended September 30, 2007 were as follows:

(in millions)	As of September 30, 2007			
	Consumer			
	Digital	Film	Graphic	Consolidated
	Imaging	Products	Communications	Total
	Group	Group	Group	Total
Balance at December 31, 2006	\$ 217	\$ 544	\$ 823	\$ 1,584
Additions	□	□	2	2
Purchase accounting adjustment	□	□	24	24
Currency translation adjustments	7	14	5	26
Balance at September 30, 2007	\$ 224	\$ 558	\$ 854	\$ 1,636

PAGE 10

During the second quarter of 2007, the Company identified a deferred tax asset in a recently acquired non-U.S. subsidiary that was overstated at the date of acquisition. Therefore, the Company recorded an increase in the value of goodwill of \$24 million in the second quarter to appropriately reflect the proper goodwill balance. This \$24 million is presented as a purchase accounting adjustment in the table above. The Company also recorded a valuation allowance of \$20 million, which should have been recorded in 2006, in order to properly reflect the value of the net deferred tax asset. The Company has determined that this correction is not material to the current period or to any prior period financial statement amounts.



Edgar Filing: EASTMAN KODAK CO - Form 10-Q

Due to the realignment of the Kodak operating model and change in reporting structure, as described in Note 14, "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 September 30, 2007 and December 31, 2006 were as follows:

<b>As of September 30, 2007</b>				
(in millions)	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>	<b>Net</b>	<b>Weighted-Average Amortization Period</b>
Technology-based	\$ 326	\$ 154	\$ 172	7 years
Customer-related	279	119	160	10 years
Other	216	116	100	7 years
<b>Total</b>	<b>\$ 821</b>	<b>\$ 389</b>	<b>\$ 432</b>	<b>8 years</b>

  

<b>As of December 31, 2006</b>				
(in millions)	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>	<b>Net</b>	<b>Weighted-Average Amortization Period</b>
Technology-based	\$ 324	\$ 119	\$ 205	7 years
Customer-related	274	95	179	10 years
Other	214	88	126	8 years
<b>Total</b>	<b>\$ 812</b>	<b>\$ 302</b>	<b>\$ 510</b>	<b>8 years</b>

Amortization expense related to purchased intangible assets for the three months ended September 30, 2007 and 2006 was \$27 million and \$30 million, respectively. Amortization expense related to purchased intangible assets for the nine months ended September 30, 2007 and 2006 was \$83 million and \$90 million, respectively.

Estimated future amortization expense related to purchased intangible assets at September 30, 2007 is as follows (in millions):

2007	\$ 28
2008	107
2009	102
2010	80
2011	40
2012 and thereafter	75
<b>Total</b>	<b>\$ 432</b>

PAGE 11

**NOTE 6: INCOME TAXES**

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

(dollars in millions)	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Earnings (loss) from continuing operations before income taxes	\$29	(\$53)	(\$356)	(\$685)

Edgar Filing: EASTMAN KODAK CO - Form 10-Q

(Benefit) provision for income taxes	(5)	30	(64)	99
Effective tax rate	(17.2)%	(56.6)%	18.0%	(14.5)%

For the three months ended September 30, 2007, the Company recorded a benefit of \$5 million on pre-tax earnings of \$29 million, representing an effective rate of (17.2)%. The difference between the effective tax rate and the U.S. statutory rate of 35.0% is primarily attributable to: (1) losses generated in certain jurisdictions outside the U.S., which were not benefited, (2) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S., (3) non-U.S. tax benefits of \$6 million associated with restructuring costs and asset impairments, (4) a net benefit of \$16 million associated with adjustments related to uncertain tax positions, and (5) a tax provision of \$13 million associated with the impact of foreign legislative tax rate changes.

In accordance with SFAS No. 109, "Accounting for Income Taxes," the Company recorded a tax benefit in continuing operations associated with the realization of current year losses in certain jurisdictions where it has historically had a valuation allowance due to the recognition of the pre-tax gain in discontinued operations.

For the three months ended September 30, 2006, the Company recorded a provision of \$30 million on a pre-tax loss of \$53 million, representing an effective rate of (56.6)%. 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, (2) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S., (3) non-U.S. tax benefits of \$8 million associated with restructuring costs and asset impairments, and (4) discrete tax benefits of \$9 million relating primarily to tax rate changes, impacts from ongoing tax audits with respect to open tax years, and other property sales gains/losses.

For the nine months ended September 30, 2007, the Company recorded a benefit of \$64 million on a pre-tax loss of \$356 million, representing an effective rate of 18.0%. The difference between the effective tax rate and the U.S. statutory rate of 35.0% is primarily attributable to: (1) losses generated in certain jurisdictions outside the U.S., which were not benefited, (2) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S., (3) non-U.S. tax benefits of \$42 million associated with restructuring costs and asset impairments, (4) a net benefit of \$75 million associated with adjustments related to uncertain tax positions, and (5) a tax provision of \$13 million associated with the impact of foreign legislative tax rate changes.

For the nine months ended September 30, 2006, the Company recorded a provision of \$99 million on a pre-tax loss of \$685 million, representing an effective rate of (14.5)%. 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 earnings from operations in certain lower-taxed jurisdictions outside the U.S., (3) non-U.S. tax benefits of \$64 million associated with restructuring costs and asset impairments, and (4) discrete tax charges of \$44 million relating primarily to purchase accounting for the Creo and KPG acquisitions, tax rate changes, impacts from ongoing tax audits with respect to open tax years, and other property sales gains/losses.

During the second quarter of 2007 the Company identified a deferred tax asset in a recently acquired non-U.S. subsidiary that was overstated at the date of acquisition. Therefore, the Company recorded an increase in the value of goodwill of \$24 million in the second quarter of 2007 to appropriately reflect the proper goodwill balance. The Company also recorded a valuation allowance of \$20 million, which should have been recorded in 2006, in order to properly reflect the value of the net deferred tax asset. This amount is included in the \$64 million benefit for the nine months ended September 30, 2007. The Company has determined that this correction is not material to the three- or nine-month periods ended September 30, 2007 or to any prior period financial statement amounts.

PAGE 12

The Company adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48) in the first quarter of 2007. As a result of the implementation of FIN 48, there was no cumulative effect adjustment for unrecognized tax benefits, which would have been accounted for as an adjustment to the January 1, 2007 balance of retained earnings. The Company had a liability for income taxes associated with uncertain tax benefits, including interest and penalties, of \$301 million, \$324 million and \$323 million as of September 30, 2007, June 30, 2007 and March 31, 2007, respectively. For the third quarter of 2007, the decline in the liability for income taxes associated with uncertain tax benefits of \$23 million relates to a \$20 million decrease as the result of the

closure of a foreign jurisdiction audit for tax years 1999 through 2001, and a net decrease of \$3 million related to various worldwide tax positions, including interest and payments.

If the unrecognized tax benefits were recognized, they would favorably affect the effective income tax rate for the remainder of 2007 or in any future periods. Consistent with the provisions of FIN 48, the Company has classified certain income tax liabilities as current or non-current based on management's estimate of when these liabilities will be settled and has reclassified these items in the Consolidated Statement of Financial Position as of December 31, 2006 to conform to the current period presentation. These non-current income tax liabilities are recorded in Other long-term liabilities in the Consolidated Statement of Financial Position.

It is reasonably possible that the liability associated with our unrecognized tax benefits will increase or decrease within the next twelve months. These changes may be the result of ongoing audits or the expiration of statutes of limitations. At this time, an estimate of the range of the reasonably possible outcomes cannot be made.

The Company files numerous consolidated and separate income tax returns in the U.S. federal jurisdiction and in many state and foreign jurisdictions. The Company has substantially concluded all U.S. federal income tax matters for years through 2000. The Company's U.S. tax matters for the years 2001 through 2006 remain subject to examination by the Internal Revenue Service. Substantially all material state, local, and foreign income tax matters have been concluded for years through 1998. The Company's tax matters for the years 1999 through 2006 remain subject to examination by the respective state, local, and foreign tax jurisdiction authorities.

As previously reported, on October 3, 2006, the Company filed a claim for a federal tax refund related to a 1994 loss recognized on the sale of a subsidiary's stock that was disallowed at that time under Internal Revenue Service regulations. Since that time, the IRS has issued new regulations that serve as the basis for this refund claim. At September 30, 2007, the Company anticipates that this claim will be brought to the Joint Committee of Taxation for review during the fourth quarter of 2007. Based on information available at this time, and in accordance with FIN 48, the Company has not recorded a tax benefit due to the uncertainty of the resolution and the amount associated with the claim.

The Company's policy regarding interest and/or penalties related to income tax matters is to recognize such items as a component of income tax expense. As of the adoption of FIN 48, the Company had \$58 million accrued for income tax-related interest and penalties.

## **NOTE 7: COMMITMENTS AND CONTINGENCIES**

### **Environmental**

At September 30, 2007, the Company's undiscounted accrued liabilities for environmental remediation costs amounted to \$140 million and are reported in other long-term liabilities in the accompanying Consolidated Statement of Financial Position. Included in this amount are the items described below.

The Company is currently implementing a Corrective Action Program required by the Resource Conservation and Recovery Act (RCRA) at the Kodak Park site in Rochester, NY. The Company is currently in the process of completing, and in many cases has completed, RCRA Facility Investigations (RFI), Corrective Measures Studies (CMS) and Corrective Measures Implementation (CMI) for areas at the site. At September 30, 2007, estimated future investigation and remediation costs of \$64 million are accrued for this site, the majority of which relates to long-term operation, maintenance of remediation systems and monitoring costs.

PAGE 13

The Company has accrued for obligations relating to other operating sites with estimated future investigation, remediation and monitoring costs of \$19 million.

The Company has obligations relating to plant closures and former operations. The Company has accrued for obligations with estimated future investigation, remediation and monitoring costs of \$37 million at sites of former operations.

The Company has retained certain obligations for environmental remediation and Superfund matters related to certain sites associated with the non-imaging health businesses sold in 1994. The Company has accrued for

obligations with estimated future remediation costs of \$20 million for these sites.

Cash expenditures for the aforementioned investigation, remediation and monitoring activities are expected to be incurred over the next twenty-eight years for many of the sites. For these known environmental liabilities, the accrual reflects the Company's best estimate of the amount it will incur under the agreed-upon or proposed work plans. The Company's cost estimates were determined using the ASTM Standard E 2137-01, "Standard Guide for Estimating Monetary Costs and Liabilities for Environmental Matters," and have not been reduced by possible recoveries from third parties. The overall method includes the use of a probabilistic model which forecasts a range of cost estimates for the remediation required at individual sites. The projects are closely monitored and the models are reviewed as significant events occur or at least once per year. The Company's estimate includes investigations, equipment and operating costs for remediation and long-term monitoring of the sites. The Company does not believe it is reasonably possible that the losses for the known exposures could exceed the current accruals by material amounts.

A Consent Decree was signed in 1994 in settlement of a civil complaint brought by the U.S. Environmental Protection Agency and the U.S. Department of Justice. In connection with the Consent Decree, the Company is subject to a Compliance Schedule, under which the Company has improved its waste characterization procedures, upgraded one of its incinerators, and is evaluating and upgrading its industrial sewer system. The total expenditures required to complete this program are currently estimated to be approximately \$1 million over the next year. These expenditures are incurred as part of plant operations and, therefore, are not included in the environmental accrual at September 30, 2007.

The Company is presently designated as a potentially responsible party (PRP) under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended (the Superfund Law), or under similar state laws, for environmental assessment and cleanup costs as the result of the Company's alleged arrangements for disposal of hazardous substances at nine Superfund sites. With respect to each of these sites, the Company's liability is minimal. In addition, the Company has been identified as a PRP in connection with the non-imaging health businesses in two active Superfund sites. Numerous other PRPs have also been designated at these sites. Although the law imposes joint and several liability on PRPs, the Company's historical experience demonstrates that these costs are shared with other PRPs. Settlements and costs paid by the Company in Superfund matters to date have not been material. Future costs are also not expected to be material to the Company's financial position, results of operations or cash flows.

Uncertainties associated with environmental remediation contingencies are pervasive and often result in wide ranges of outcomes. Estimates developed in the early stages of remediation can vary significantly. A finite estimate of costs does not normally become fixed and determinable at a specific time. Rather, the costs associated with environmental remediation become estimable over a continuum of events and activities that help to frame and define a liability, and the Company continually updates its cost estimates. The Company has an ongoing monitoring and identification process to assess how the activities, with respect to the known exposures, are progressing against the accrued cost estimates, as well as to identify other potential remediation issues.

Estimates of the amount and timing of future costs of environmental remediation requirements are by their nature imprecise because of the continuing evolution of environmental laws and regulatory requirements, the availability and application of technology, the identification of presently unknown remediation sites and the allocation of costs among the potentially responsible parties. Based upon information presently available, such future costs are not expected to have a material effect on the Company's competitive or financial position. However, such costs could be material to results of operations in a particular future quarter or year.

PAGE 14

### **Asset Retirement Obligations**

As of September 30, 2007, the Company has recorded \$71 million of asset retirement obligations within Other long-term liabilities in the accompanying Consolidated Statement of Financial Position.

The Company's asset retirement obligations primarily relate to asbestos contained in buildings that the Company owns. In many of the countries in which the Company operates, environmental regulations exist that require the Company to handle and dispose of asbestos in a special manner if a building undergoes major renovations or is demolished. Otherwise, the Company is not required to remove the asbestos from its buildings. The Company records a liability equal to the estimated fair value of its obligation to perform asset retirement activities related

to the asbestos, computed using an expected present value technique, when sufficient information exists to calculate the fair value. The Company does not have a liability recorded related to each building that contains asbestos because the Company cannot estimate the fair value of its obligation for certain buildings due to a lack of sufficient information about the range of time over which the obligation may be settled through demolition, renovation or sale of the building.

The change in the Company's asset retirement obligations from December 31, 2006 to September 30, 2007 was as follows:

<b>(in millions)</b>	
Asset retirement obligations as of December 31, 2006	\$ 92
Liabilities incurred in the current period	3
Liabilities settled in the current period	(36)
Accretion expense	3
Revisions in estimated cash flows	7
Foreign exchange	2
Asset retirement obligations as of September 30, 2007	\$ 71

### Other Commitments and Contingencies

At September 30, 2007, the Company had outstanding letters of credit totaling \$143 million and surety bonds in the amount of \$85 million primarily to ensure the payment of possible casualty and workers' compensation claims.

The Company and its subsidiary companies are involved in various lawsuits, claims, investigations and proceedings, including product liability, commercial, employment, environmental, and health and safety matters, which are being handled and defended in the ordinary course of business. In addition, the Company is subject to various claims and legal proceedings concerning intellectual property matters, including patent infringement suits in which the Company is a defendant, and suits in which the Company is the plaintiff. There are no such matters pending representing contingent losses that the Company and its General Counsel expect to be material in relation to the Company's business, financial position, results of operations or cash flows.

PAGE 15

### NOTE 8: GUARANTEES

The Company guarantees debt and other obligations of certain customers. The debt and other obligations are primarily due to banks and leasing companies in connection with financing of customers' purchases of product and equipment from the Company. At September 30, 2007, the following customer guarantees were in place:

<b>(dollars in millions)</b>	<b>As of September 30, 2007</b>	
	<b>Maximum Amount</b>	<b>Amount Outstanding</b>
Customer amounts due to banks and leasing companies	\$ 151	\$ 110
Other third-parties	2	□
Total guarantees of customer debt and other obligations	\$ 153	\$ 110

The guarantees for the third party debt mature between 2007 and 2011. The customer financing agreements and related guarantees typically have a term of 90 days for product and short-term equipment financing arrangements, and up to five years for long-term equipment financing arrangements. These guarantees would require payment from the Company only in the event of default on payment by the respective debtor. In some cases, particularly for guarantees related to equipment financing, the Company has collateral or recourse provisions to recover and sell the equipment to reduce any losses that might be incurred in connection with the guarantees.

Management believes the likelihood is remote that material payments will be required under any of the guarantees disclosed above. With respect to the guarantees that the Company issued in the quarter ended September 30, 2007, the Company assessed the fair value of its obligation to stand ready to perform under these guarantees by considering the likelihood of occurrence of the specified triggering events or conditions requiring performance as well as other assumptions and factors.

The Company also guarantees debt owed to banks and other third parties for some of its consolidated subsidiaries. The maximum amount guaranteed is \$666 million, and the outstanding debt under those guarantees, which is recorded within the short-term borrowings and long-term debt, net of current portion components in the accompanying Consolidated Statement of Financial Position, is \$239 million. These guarantees expire in 2007 through 2013. Pursuant to the terms of the Company's \$2.7 billion Senior Secured Credit Agreement dated October 18, 2005, obligations under the \$2.7 billion Secured Credit Facilities and other obligations of the Company and its subsidiaries to the \$2.7 billion Secured Credit Facilities lenders are guaranteed.

### Indemnifications

The Company issues indemnifications in certain instances when it sells businesses and real estate, and in the ordinary course of business with its customers, suppliers, service providers and business partners. Further, the Company indemnifies its directors and officers who are, or were, serving at the Company's request in such capacities. Historically, costs incurred to settle claims related to these indemnifications have not been material to the Company's financial position, results of operations or cash flows. Additionally, the fair value of the indemnifications that the Company issued during the quarter ended September 30, 2007 was not material to the Company's financial position, results of operations or cash flows.

PAGE 16

### Warranty Costs

The Company has warranty obligations in connection with the sale of its products and equipment. The original warranty period is generally one year or less. The costs incurred to provide for these warranty obligations are estimated and recorded as an accrued liability at the time of sale. The Company estimates its warranty cost at the point of sale for a given product based on historical failure rates and related costs to repair. The change in the Company's accrued warranty obligations balance, which is reflected in accounts payable and other current liabilities in the accompanying Consolidated Statement of Financial Position, was as follows:

<b>(in millions)</b>	
Accrued warranty obligations at December 31, 2006	\$ 39
Actual warranty experience during 2007	(35)
2007 warranty provisions	31
Accrued warranty obligations at September 30, 2007	\$ 35

The Company also offers its customers extended warranty arrangements that are generally one year, but may range from three months to three years after the original warranty period. The Company provides repair services and routine maintenance under these arrangements. The Company has not separated the extended warranty revenues and costs from the routine maintenance service revenues and costs, as it is not practicable to do so. Therefore, these revenues and costs have been aggregated in the presentation below. Costs incurred under these arrangements for the nine months ended September 30, 2007 amounted to \$131 million. The change in the Company's deferred revenue balance in relation to these extended warranty arrangements from December 31, 2006 to September 30, 2007, which is reflected in accounts payable and other current liabilities in the accompanying Consolidated Statement of Financial Position, was as follows:

<b>(in millions)</b>	
Deferred revenue at December 31, 2006	\$ 143
New extended warranty arrangements in 2007	292
Recognition of extended warranty arrangement revenue in 2007	(280)

Adjustments for changes in estimate in 2007	(1)
Deferred revenue at September 30, 2007	\$ 154

**NOTE 9: RESTRUCTURING COSTS AND OTHER**

The Company has undertaken a cost reduction program that was initially announced in January 2004. This program is referred to as the "2004-2007 Restructuring Program." This program was expected to result in total charges of \$1.3 billion to \$1.7 billion over a three-year period ending in 2006, of which \$700 million to \$900 million related to severance, with the remainder relating to the disposal of buildings and equipment. Overall, Kodak's worldwide facility square footage was expected to be reduced by approximately one-third. Approximately 12,000 to 15,000 positions worldwide were expected to be eliminated through these actions primarily in global manufacturing, selected traditional businesses and corporate administration.

The Company subsequently expanded the program to extend into 2007 and increased the expected employment reductions to 28,000 to 30,000 positions and total charges to \$3.6 billion to \$3.8 billion. The Company now expects that the total employment reductions will be in the range of 27,000 to 28,000 positions and total charges will be in the range of \$3.4 billion to \$3.6 billion. These new estimates reflect greater efficiencies in manufacturing infrastructure projects as well as the Company's ability to outsource or sell certain operations, which reduces involuntary severance charges.

The aforementioned 2004-2007 Restructuring Program underpins a dramatic transformation of the Company focused on two primary elements of cost restructuring: manufacturing infrastructure and operating expense rationalization. As this four-year effort has progressed, the underlying business model necessarily has evolved, requiring broader and more costly manufacturing infrastructure reductions (primarily non-cash charges) than originally anticipated, as well as similarly broader rationalization of selling, administrative and other business resources (primarily severance charges). In addition, the recent divestiture of the Health Group has further increased the amount of reductions necessary to appropriately scale the Corporate infrastructure.

The actual charges for initiatives under this program are recorded in the period in which the Company commits to formalized restructuring plans or executes the specific actions contemplated by the program and all criteria for restructuring charge recognition under the applicable accounting guidance have been met.

PAGE 17

**Restructuring Programs Summary**

The activity in the accrued restructuring balances and the non-cash charges incurred in relation to all of the Company's restructuring programs were as follows for the third quarter of 2007:

(in millions)	Balance		Reversals	Cash Payments	Non-cash Settlements	Other Adjustments and Reclasses	Balance Sept. 30, 2007
	June 30, 2007	Costs Incurred (1)					
<b>2004-2007 Restructuring Program:</b>							
Severance reserve	\$ 173	\$ 59	\$ (1)	\$ (62)	\$ 0	\$ (6)	\$ 163
Exit costs reserve	24	38	0	(40)	0	2	24
Total reserve	\$ 197	\$ 97	\$ (1)	\$ (102)	\$ 0	\$ (4)	\$ 187
Long-lived asset impairments and inventory write-downs	\$ 0	\$ 10	\$ 0	\$ 0	\$ (10)	\$ 0	\$ 0
Accelerated depreciation	\$ 0	\$ 23	\$ 0	\$ 0	\$ (23)	\$ 0	\$ 0
<b>Pre-2004 Restructuring Programs:</b>							
Severance reserve	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Exit costs reserve	6	0	0	(1)	0	1	6

Total reserve	\$ 6	\$ □	\$ □	\$ (1)	\$ □	\$ 1	\$ 6
Total of all restructuring programs	\$ 203	\$ 130	\$ (1)	\$ (103)	\$ (33)	\$ (3)	\$ 193

- (1) The costs incurred include both continuing operations of \$128 million and discontinued operations of \$2 million.
- (2) During the three months ended September 30, 2007, the Company paid approximately \$110 million related to restructuring. Of this total amount, \$103 million was recorded against restructuring reserves, while \$7 million was recorded against pension and other postretirement liabilities.
- (3) The total restructuring charges of \$130 million include pension and other postretirement charges and credits for curtailments, settlements and special termination benefits. However, because the impact of these charges and credits relate to the accounting for pensions and other postretirement benefits, the related impacts on the Consolidated Statement of Financial Position are reflected in their respective components as opposed to within the accrued restructuring balances at September 30, 2007. Accordingly, the Other Adjustments and Reclasses column of the table above includes (1) reclassifications to Other long-term assets and Pension and other postretirement liabilities for the position elimination-related impacts on the Company's pension and other postretirement employee benefit plan arrangements, including net curtailment, settlement and special termination charges of (\$11) million, and (2) reclassifications to Other long-term liabilities for the restructuring-related impacts on the Company's environmental remediation liabilities of \$1 million. Additionally, the Other Adjustments and Reclasses column of the table above includes foreign currency translation of \$7 million.

The costs incurred, net of reversals, which total \$129 million for the three months ended September 30, 2007, include \$23 million and \$4 million of charges related to accelerated depreciation and inventory write-downs that were reported in cost of goods sold in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007. Of the remaining costs incurred, net of reversals, \$2 million was included in discontinued operations and \$100 million was reported as restructuring costs and other in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007. The severance costs and exit costs require the outlay of cash, while long-lived asset impairments, accelerated depreciation and inventory write-downs represent non-cash items.

PAGE 18

### 2004-2007 Restructuring Program Activity

The Company implemented certain actions under the program during the third quarter of 2007. As a result of these actions, the Company recorded charges, net of reversals, of \$129 million in the third quarter of 2007, which were composed of severance, long-lived asset impairments, exit costs, inventory write-downs, and accelerated depreciation of \$58 million, \$6 million, \$38 million, \$4 million, and \$23 million, respectively. Included in these amounts, \$2 million of exit costs are presented as discontinued operations. The severance costs related to the elimination of approximately 1,425 positions, including approximately 100 photofinishing, 1,025 manufacturing, 50 research and development and 250 administrative positions. The geographic composition of the positions to be eliminated includes approximately 775 in the United States and Canada and 650 throughout the rest of the world. The reduction of the 1,425 positions and the \$129 million charges, net of reversals, are reflected in the 2004-2007 Restructuring Program table below. The \$6 million charge in the third quarter for long-lived asset impairments was included in restructuring costs and other in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007. The charges taken for inventory write-downs of \$4 million were reported in cost of goods sold in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007.



Edgar Filing: EASTMAN KODAK CO - Form 10-Q

As a result of initiatives implemented under the 2004-2007 Restructuring Program, the Company also recorded \$23 million of accelerated depreciation on long-lived assets in cost of goods sold in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007. The accelerated depreciation relates to long-lived assets accounted for under the held and used model of SFAS No. 144. The total amount of \$23 million relates to \$22 million of manufacturing facilities and equipment, and \$1 million of photofinishing facilities that will be used until their abandonment. The Company will incur approximately \$2 million of accelerated depreciation in the fourth quarter of 2007 as a result of the initiatives already implemented under the 2004-2007 Restructuring Program.

In April 2007, the Company entered into an agreement to sell its manufacturing site in Xiamen, China. This sale closed in the second quarter of 2007 and resulted in a non-cash charge of approximately \$238 million. This action is part of the 2004-2007 Restructuring Program.

Under this program, on a life-to-date basis as of September 30, 2007, the Company has recorded charges of \$3,329 million, which was composed of severance, long-lived asset impairments, exit costs, inventory write-downs and accelerated depreciation of \$1,381 million, \$617 million, \$342 million, \$79 million and \$931 million, respectively, less reversals of \$21 million. The severance costs related to the elimination of approximately 27,025 positions, including approximately 6,525 photofinishing, 12,975 manufacturing, 1,500 research and development and 6,025 administrative positions.

PAGE 19

The following table summarizes the activity with respect to the charges recorded in connection with the focused cost reduction actions that the Company has committed to under the 2004-2007 Restructuring Program and the remaining balances in the related reserves at September 30, 2007:

(dollars in millions)	Number of Employees	Severance Reserve	Exit Costs Reserve	Total	Long-lived Asset Impairments and Inventory Accelerated	
					Write-down	Depreciation
2004 charges - continuing operations	8,975	\$ 405	\$ 95	\$ 500	\$ 156	\$ 152
2004 charges - discontinued operations	650	13	4	17	1	□
2004 reversals - continuing operations	□	(6)	(1)	(7)	□	□
2004 utilization	(5,175)	(169)	(47)	(216)	(157)	(152)
2004 other adj. & reclasses	□	24	(15)	9	□	□
Balance at 12/31/04	4,450	267	36	303	□	□
2005 charges - continuing operations	7,850	472	82	554	160	391
2005 charges - discontinued operations	275	25	2	27	1	□
2005 reversals - continuing operations	□	(3)	(6)	(9)	□	□
2005 utilization	(10,225)	(377)	(95)	(472)	(161)	(391)
2005 other adj. & reclasses	□	(113)	4	(109)	□	□
Balance at 12/31/05	2,350	271	23	294	□	□
2006 charges - continuing operations	5,150	266	66	332	97	273
2006 charges - discontinued operations	475	52	3	55	3	12
2006 reversals - continuing operations	□	(3)	(1)	(4)	□	□
2006 utilization	(5,700)	(416)	(67)	(483)	(100)	(285)
2006 other adj. & reclasses	□	58	□	58	□	□
Balance at 12/31/06	2,275	228	24	252	□	□
Q1 2007 charges - continuing operations	1,075	53	22	75	11	65
Q1 2007 charges - discontinued operations	50	17	□	17	□	□
Q1 2007 utilization	(1,000)	(84)	(20)	(104)	(11)	(65)
Q1 2007 other adj. & reclasses	□	(18)	□	(18)	□	□
Balance at 3/31/07	2,400	196	26	222	□	□

Edgar Filing: EASTMAN KODAK CO - Form 10-Q

Q2 2007 charges - continuing operations	1,100	16	28	44	257	15
Q2 2007 charges - discontinued operations	□	3	2	5	□	□
Q2 2007 utilization	(1,250)	(83)	(32)	(115)	(257)	(15)
Q2 2007 other adj. & reclasses	□	41	□	41	□	□
Balance at 6/30/07	2,250	173	24	197	□	□
Q3 2007 charges - continuing operations	1,425	59	36	95	10	23
Q3 2007 charges - discontinued operations	□	□	2	2	□	□
Q3 2007 reversals - continuing operations	□	(1)	□	(1)	□	□
Q3 2007 utilization	(1,000)	(62)	(40)	(102)	(10)	(23)
Q3 2007 other adj. & reclasses	□	(6)	2	(4)	□	□
Balance at 9/30/07	2,675	\$ 163	\$ 24	\$ 187	\$ □	\$ □

As a result of the initiatives already implemented under the 2004-2007 Restructuring Program, severance payments will be paid during periods through 2008 since, in many instances, the employees whose positions were eliminated can elect or are required to receive their payments over an extended period of time. Most exit costs have been paid or will be paid during 2007. However, certain costs, such as long-term lease payments, will be paid over periods after 2007.

PAGE 20

The charges of \$130 million recorded in the third quarter of 2007 included \$28 million applicable to FPG, \$19 million applicable to CDG, \$7 million applicable to GCG, and \$74 million that was applicable to manufacturing, research and development, and administrative functions, which are shared across all segments. The remaining \$2 million was applicable to discontinued operations.

**Pre-2004 Restructuring Programs Activity**

At September 30, 2007, the Company had remaining exit costs reserves of \$6 million, relating to restructuring plans committed to or executed prior to 2004. Most of these remaining exit costs reserves represent long-term lease payments, which will continue to be paid over periods throughout and after 2007.

**NOTE 10: RETIREMENT PLANS AND OTHER POSTRETIREMENT BENEFITS**

Components of the net periodic benefit cost for all major funded and unfunded U.S. and Non-U.S. defined benefit plans for the three and nine months ended September 30 are as follows:

(in millions)	Three Months Ended September 30,				Nine Months Ended September 30,			
	2007		2006		2007		2006	
	U.S.	Non-U.S.	U.S.	Non-U.S.	U.S.	Non-U.S.	U.S.	Non-U.S.
Service cost	\$ 16	\$ 6	\$ 22	\$ 8	\$ 55	\$ 20	\$ 68	\$
Interest cost	74	52	82	46	232	150	246	
Expected return on plan assets	(133)	(65)	(131)	(57)	(405)	(187)	(391)	(
Amortization of:								
Prior service cost	□	□	□	2	□	□	□	□
Recognized net actuarial loss	2	14	2	17	5	48	8	
Pension (income) expense before special termination benefits, curtailments and settlements	(41)	7	(25)	16	(113)	31	(69)	
Special termination benefits	17	□	□	8	45	7	□	
Curtailement (gains) losses	□	□	(13)	(6)	(15)	(3)	(20)	
Settlement (gains) losses	(7)	□	5	□	(45)	(4)	13	
Net pension (income) expense	(31)	7	(33)	18	(128)	31	(76)	
Other plans including unfunded plans	□	5	□	5	□	8	□	

Total net pension (income) expense from continuing operations	\$ (31)	\$ 12	\$ (33)	\$ 23	\$ (128)	\$ 39	\$ (76)	\$
---	---------	-------	---------	-------	----------	-------	---------	----

For the quarters ended September 30, 2007 and 2006, \$17 million and \$8 million, respectively, of special termination benefits charges were incurred as a result of the Company's restructuring actions and, therefore, have been included in restructuring costs and other in the Consolidated Statement of Operations. Additionally, as a result of the Company's restructuring actions, the Company recognized net curtailment and settlement gains of \$7 million that have been included in restructuring costs and other in the Consolidated Statement of Operations for the quarter ended September 30, 2007.

The Company made contributions (funded plans) or paid benefits (unfunded plans) totaling approximately \$30 million relating to its major U.S. and non-U.S. defined benefit pension plans in the third quarter of 2007. The Company expects its contribution (funded plans) and benefit payment (unfunded plans) requirements for its major U.S. and non-U.S. defined benefit pension plans for the balance of 2007 to be approximately \$39 million.

PAGE 21

Postretirement benefit cost for the Company's U.S., United Kingdom and Canada postretirement benefit plans, which represent the Company's major postretirement plans, includes:

(in millions)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2007	2006	2007	2006
Service cost	\$ 2	\$ 2	\$ 6	\$ 8
Interest cost	41	43	123	125
Amortization of:				
Prior service cost	(8)	(11)	(28)	(35)
Actuarial loss	11	10	38	38
Other postretirement benefit cost before curtailment and settlement (gains) losses	46	44	139	136
Curtailment gain		(4)	(5)	(8)
Total net postretirement benefit cost	\$ 46	\$ 40	\$ 134	\$ 128

The Company paid benefits totaling approximately \$42 million relating to its U.S., United Kingdom and Canada postretirement benefit plans in the third quarter of 2007. The Company expects to pay benefits of \$51 million for these postretirement plans for the balance of 2007.

As a result of the cumulative impact of the ongoing position eliminations under its Pre-2004 and 2004-2007 Restructuring Programs, as disclosed in Note 9, certain of the Company's retirement plans experienced curtailment events in the third quarter of 2007. These curtailment events resulted in the remeasurement of the plans' obligations during the quarter, which decreased the Company's recognized retirement and other postretirement benefit plan obligation by \$133 million.

#### NOTE 11: EARNINGS PER SHARE

For the three months ended September 30, 2007, the Company calculated diluted net earnings per share excluding the assumed conversion of outstanding options to purchase 25.7 million shares of common stock at weighted average per share prices of \$42.91. These options were excluded in the computation of diluted net earnings per share because the options' exercise prices were greater than the average market price of the common shares for the period.

As a result of the net loss from continuing operations presented for the nine months ended September 30, 2007, the Company calculated diluted net earnings (loss) per share using weighted average basic shares outstanding for the period, as utilizing diluted shares would be anti-dilutive to net earnings (loss) per share. Therefore, outstanding options to purchase 29.8 million shares of the Company's common stock were excluded in the computation of diluted net earnings (loss) per share for the nine months ended September 30, 2007.

As a result of the net loss from continuing operations presented for the three and nine months ended September 30, 2006, the Company calculated diluted net earnings (loss) per share using weighted average basic shares outstanding for the period, as utilizing diluted shares would be anti-dilutive to loss per share. Therefore, outstanding options to purchase 33.8 million shares of the Company's common stock were not included in the computation of diluted net earnings (loss) per share for the three and nine months ended September 30, 2006.

The Company currently has approximately \$575 million in contingent convertible notes (the Convertible Securities) outstanding that were issued in October 2003. Interest on the Convertible Securities accrues at a rate of 3.375% and is payable semi-annually. The Convertible Securities are convertible at an initial conversion rate of 32.2373 shares of the Company's common stock for each \$1,000 principal of the Convertible Securities. The Company's diluted net earnings (loss) per share exclude the effect of the Convertible Securities, as they were anti-dilutive for all periods presented.

PAGE 22

**NOTE 12: SHAREHOLDERS' EQUITY**

The Company has 950 million shares of authorized common stock with a par value of \$2.50 per share, of which 391 million shares had been issued as of September 30, 2007 and December 31, 2006. Treasury stock at cost consists of approximately 103 million shares at September 30, 2007 and 104 million shares at December 31, 2006.

**NOTE 13: COMPREHENSIVE INCOME (LOSS)**

(in millions)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2007	2006	2007	2006
Net earnings (loss)	\$ 37	\$ (37)	\$ 461	\$ (617)
Unrealized gains on available-for-sale securities, net of tax	□	4		6
Realized and unrealized gains from hedging activity, net of tax	7		7	1
Currency translation adjustments	53	30	87	54
Pension and other postretirement benefit plan obligation activity	81	(60)	770	146
Total comprehensive income (loss), net of tax	\$ 178	\$ (63)	\$ 1,325	\$ (410)

**NOTE 14: SEGMENT INFORMATION****Kodak Operating Model and Reporting Structure**

The Company has three reportable segments: Consumer Digital Imaging Group (CDG), Film Products Group (FPG), and Graphic Communications Group (GCG). The balance of the Company's continuing operations, which individually and in the aggregate do not meet the criteria of a reportable segment, are reported in All Other. A description of the segments is as follows:

**Consumer Digital Imaging Group Segment (CDG):** CDG encompasses digital capture, kiosks, snapshot printing, consumer imaging services, photographic paper, photofinishing services, consumer inkjet printing and imaging sensors. This segment provides consumers and professionals with a full range of products and services

for capturing, storing, printing and sharing images. CDG also includes the licensing activities related to the Company's intellectual property in digital capture products.

**Film Products Group Segment (FPG):** FPG encompasses consumer and professional film, one-time-use cameras, aerial and industrial film, and entertainment imaging products and services. This segment provides consumers, professionals, cinematographers, and other entertainment imaging customers with film-related products and services.

**Graphic Communications Group Segment (GCG):** GCG serves a variety of customers in the creative, in-plant, data center, commercial printing, packaging, newspaper and digital service bureau market segments with a range of software, media and hardware products that provide customers with a variety of solutions for prepress equipment, workflow software, digital and traditional printing, document scanning and multi-vendor IT services. Products and related services include workflow software and digital controller development; continuous inkjet and electrophotographic products, including equipment, consumables and service; prepress consumables; output devices; proofing hardware, media and software; and document scanners.

**All Other:** All Other is composed of Kodak's display business and other small, miscellaneous businesses.

PAGE 23

Prior period segment results have been revised to conform to the current period segment reporting structure.

Segment financial information is shown below:

(in millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
<b>Net sales from continuing operations:</b>				
Consumer Digital Imaging Group	\$ 1,123	\$ 1,109	\$ 2,901	\$ 2,853
Film Products Group	488	593	1,505	1,505
Graphic Communications Group	928	880	2,721	2,721
All Other	42	13	83	83
Consolidated total	\$ 2,581	\$ 2,595	\$ 7,210	\$ 7,162
<b>Earnings (loss) from continuing operations before interest, other income (charges), net and income taxes:</b>				
Consumer Digital Imaging Group	\$ 10	\$ (3)	\$ (168)	\$ (168)
Film Products Group	122	115	329	329
Graphic Communications Group	42	26	95	95
All Other	(9)	(16)	(30)	(30)
Total of segments	165	122	226	226
Restructuring costs and other	(127)	(181)	(594)	(594)
Other operating income (expenses), net	(6)	48	33	33
Legal reserve/settlement	(12)	□	(12)	□
Interest expense	(28)	(51)	(84)	(84)
Other income (charges), net	37	9	75	75
Consolidated earnings (loss) from continuing operations before income taxes	\$ 29	\$ (53)	\$ (356)	\$ (356)
			At September 30, 2007	At December 31, 2006
(in millions)				

<b>Segment total assets:</b>					
Consumer Digital Imaging Group		\$	3,465	\$	3
Film Products Group			2,845		3
Graphic Communications Group			4,024		3
All Other			72		
Total of segments			10,406		10
Cash and marketable securities			1,876		1
Deferred income tax assets			650		
Other corporate assets/reserves			(1)		
Assets held for sale			□		1
Consolidated total assets		\$	12,931	\$	14

PAGE 24

**NOTE 15: DISCONTINUED OPERATIONS**

On April 30, 2007, the Company sold all of the assets and business operations of its Health Group segment to Onex Healthcare Holdings, Inc. (□Onex□) (now known as Carestream Health, Inc.), a subsidiary of Onex Corporation, for up to \$2.55 billion. The price was composed of \$2.35 billion in cash at closing and \$200 million in additional future payments if Onex achieves certain returns with respect to its investment. If Onex investors realize an internal rate of return in excess of 25% on their investment, the Company will receive payment equal to 25% of the excess return, up to \$200 million.

The Company recognized a pre-tax gain of \$980 million on the sale in the second quarter of 2007, and recorded pre-tax true-up adjustments to the gain on sale totaling \$6 million in the third quarter of 2007, primarily related to gains from pension settlements. The pre-tax gain excludes the following: up to \$200 million of potential future payments related to Onex's return on its investment as noted above; potential charges related to settling pension obligations with Onex in future periods; and any adjustments that may be made in the future that are currently under review.

The Company used a portion of the initial \$2.35 billion cash proceeds to fully repay its approximately \$1.15 billion of Secured Term Debt. About 8,100 employees of the Company associated with the Health Group transitioned to Carestream Health, Inc. as part of the transaction. Also included in the sale were manufacturing operations focused on the production of health imaging products, as well as an office building in Rochester, NY.

The following is a summary of the composition of Earnings from discontinued operations, net of income taxes, included in the Consolidated Statement of Operations:

(in millions)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2007	2006	2007	2006
Revenues from Health Group operations (1)	\$ □	\$ 609	\$ 754	\$ 1,878
Pre-tax income from Health Group operations	\$ □	\$ 35	\$ 34	\$ 141
Pre-tax gain on sale of Health Group segment	6	□	986	□
Provision (benefit) for income taxes	3	(11)	267	(26)
Earnings from discontinued operations, net of income taxes	\$ 3	\$ 46	\$ 753	\$ 167

(1) Due to the April 30, 2007 close date, 2007 amounts include four months of revenue in the nine months ended September 30, 2007.

Upon authorization of the Company's Board of Directors on January 8, 2007, the Company met all the requirements of SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," for accounting for the Health Group segment as a discontinued operation. As such, the Health Group business ceased depreciation and amortization of long-lived assets. In accordance with EITF No. 87-24, "Allocation of Interest to

Discontinued Operations," the Company allocated certain interest expense on debt that was required to be repaid as a result of the sale. Interest expense allocated to discontinued operations totaled \$23 million for the three months ended September 30, 2006, and \$30 million and \$67 million for the nine months ended September 30, 2007 and 2006, respectively.

In accordance with SFAS No. 109, "Accounting for Income Taxes," the Company recorded a tax benefit in continuing operations associated with the realization of current year losses in certain jurisdictions where it has historically had a valuation allowance due to the recognition of the pre-tax gain in discontinued operations.

The following assets and liabilities, related to the Health Group business, were segregated and included in current and non-current Assets of discontinued operations and Liabilities of discontinued operations, as appropriate, in the Consolidated Statement of Financial Position at December 31, 2006.

PAGE 25

(in millions)	December 31, 2006
Receivables, net	\$ 598
Inventories, net	201
Other current assets	12
Current assets of discontinued operations	\$ 811
Property, plant and equipment, net	\$ 240
Goodwill	612
Other long-term assets	216
Noncurrent assets of discontinued operations	\$ 1,068
Current liabilities of discontinued operations	\$ 431
Pension and other postretirement liabilities	\$ 30
Other long-term liabilities	10
Noncurrent liabilities of discontinued operations	\$ 40

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Kodak Operating Model and Reporting Structure

The Company has three reportable segments: Consumer Digital Imaging Group (CDG), Film Products Group (FPG), and Graphic Communications Group (GCG). Within each of the Company's reportable segments are various components, or Strategic Product Groups (SPGs). Throughout the remainder of this document, references to the segments' SPGs are indicated in italics. The balance of the Company's continuing operations, which individually and in the aggregate do not meet the criteria of a reportable segment, are reported in All Other. A description of the segments is as follows:

**Consumer Digital Imaging Group Segment (CDG):** CDG encompasses digital capture, kiosks, snapshot printing, consumer imaging services, photographic paper, photofinishing services, consumer inkjet printing and imaging sensors. This segment provides consumers and professionals with a full range of products and services for capturing, storing, printing and sharing images. CDG also includes the licensing activities related to the Company's intellectual property in digital capture products.

**Film Products Group Segment (FPG):** FPG encompasses consumer and professional film, one-time-use cameras, aerial and industrial film, and entertainment imaging products and services. This segment provides consumers, professionals, cinematographers, and other entertainment imaging customers with film-related products and services.

**Graphic Communications Group Segment (GCG):** GCG serves a variety of customers in the creative, in-plant, data center, commercial printing, packaging, newspaper and digital service bureau market segments with a range of software, media and hardware products that provide customers with a variety of solutions for prepress equipment, workflow software, digital and traditional printing, document scanning and multi-vendor IT services. Products and related services include workflow software and digital controller development; continuous inkjet and electrophotographic products, including equipment, consumables and service; prepress consumables; output devices; proofing hardware, media and software; and document scanners.

**All Other:** All Other is composed of Kodak's display business and other small, miscellaneous businesses.

Prior period segment results have been revised to conform to the current period segment reporting structure.

PAGE 26

### Net Sales from Continuing Operations by Reportable Segment and All Other

(in millions)	Three Months Ended September 30,				Nine Months Ended September 30,		
	2007	2006	Change	Foreign Currency Impact*	2007	2006	Change
<b>Consumer Digital Imaging Group</b>							
Inside the U.S.	\$ 597	\$ 579	3%	0%	\$ 1,498	\$ 1,569	-5%
Outside the U.S.	526	530	-1	+5	1,403	1,547	-9%
<b>Total Consumer Digital Imaging Group</b>	<b>1,123</b>	<b>1,109</b>	<b>+1</b>	<b>+2</b>	<b>2,901</b>	<b>3,116</b>	<b>-7%</b>
<b>Film Products Group</b>							
Inside the U.S.	115	170	-32	0	365	502	-28%
Outside the U.S.	373	423	-12	+4	1,140	1,251	-9%
<b>Total Film Products Group</b>	<b>488</b>	<b>593</b>	<b>-18</b>	<b>+3</b>	<b>1,505</b>	<b>1,753</b>	<b>-13%</b>
<b>Graphic Communications Group</b>							
Inside the U.S.	301	314	-4	0	887	941	-6%
Outside the U.S.	627	566	+11	+3	1,834	1,717	+7%
<b>Total Graphic Communications Group</b>	<b>928</b>	<b>880</b>	<b>+5</b>	<b>+2</b>	<b>2,721</b>	<b>2,658</b>	<b>+2%</b>
<b>All Other</b>							
Inside the U.S.	30	7	+329	0	59	37	+62%
Outside the U.S.	12	6	+100	0	24	11	+118%
<b>Total All Other</b>	<b>42</b>	<b>13</b>	<b>+223</b>	<b>0</b>	<b>83</b>	<b>48</b>	<b>+73%</b>
<b>Consolidated</b>							
Inside the U.S.	1,043	1,070	-3	0	2,809	3,049	-8%
Outside the U.S.	1,538	1,525	+1	+4	4,401	4,526	-3%
<b>Consolidated Total</b>	<b>\$ 2,581</b>	<b>\$ 2,595</b>	<b>-1%</b>	<b>+2%</b>	<b>\$ 7,210</b>	<b>\$ 7,575</b>	<b>-5%</b>

\* Represents the percentage point change in segment net sales for the period that is attributable to foreign currency fluctuations

### Earnings (Loss) from Continuing Operations Before Interest, Other Income (Charges), Net and Income Taxes by Reportable Segment and All Other

(in millions)	Three Months Ended September 30,			Nine Months Ended September 30,	
	2007	2006	Change	2007	2006
Consumer Digital Imaging Group	\$ 10	\$ (3)	+433%	\$ (168)	\$ (168)
Film Products Group	122	115	+6%	329	329
Graphic Communications Group	42	26	+62%	95	95
All Other	(9)	(16)	+44%	(30)	(30)



Total of segments	\$ 165	\$ 122	+35%	\$ 226	\$
Restructuring costs and other	(127)	(181)		(594)	
Other operating income (expenses), net	(6)	48		33	
Legal reserve/settlement	(12)			(12)	
Interest expense	(28)	(51)		(84)	
Other income (charges), net	37	9		75	
Consolidated earnings (loss) from continuing operations before income taxes	\$ 29	\$ (53)	+155%	\$ (356)	\$

PAGE 27

**2007 COMPARED WITH 2006**

**Third Quarter**

**RESULTS OF OPERATIONS □ CONTINUING OPERATIONS**

**CONSOLIDATED**

(in millions, except per share data)	Three Months Ended		% of Sales	Three Months Ended		Increase / (Decrease)
	2007	September 30		2006	September 30	
Digital net sales	\$ 1,589			\$ 1,417		\$ 172
Traditional net sales	986			1,169		(183)
New technologies	6			9		(3)
Net sales	2,581			2,595		(14)
Cost of goods sold	1,899			1,944		(45)
Gross profit	682	26.4%		651	25.1%	31
Selling, general and administrative expenses	427	17%		464	18%	(37)
Research and development costs	129	5%		138	5%	(9)
Restructuring costs and other	100	4%		108	4%	(8)
Other operating expenses (income), net	6			(48)		54
Earnings (loss) from continuing operations before interest, other income (charges), net and income taxes	20	1%		(11)	0%	31
Interest expense	28			51		(23)
Other income (charges), net	37			9		28
Earnings (loss) from continuing operations before income taxes	29			(53)		82
(Benefit) provision for income taxes	(5)			30		(35)
Earnings (loss) from continuing operations	34	1%		(83)	-3%	117
Earnings from discontinued operations, net of income taxes	3	0%		46	2%	(43)
NET EARNINGS (LOSS)	\$ 37			\$ (37)		\$ 74

**Three Months Ended**  
**September 30**  
**2007**      **Change vs.**

**Percent Change vs. 2006**  
**Foreign**      **Manufacturing**

	Amount	2006	Volume	Price/Mix	Exchange	and Other Costs
Total net sales	\$ 2,581	-0.5%	-0.1%	-2.7%	2.3%	0.0%
Gross profit margin	26.4%	1.3pp	0.0pp	-3.9pp	1.3pp	3.9pp

### Worldwide Revenues

For the three months ended September 30, 2007, net sales were virtually unchanged compared with the same period in 2006, as significant increases in digital revenues in both CDG and GCG were offset by industry-related volume declines in the traditional businesses within all three segments. In addition, foreign exchange resulted in a positive impact to net sales during the quarter. Specifically, unfavorable price/mix was primarily driven by product portfolio shifts in *Digital Capture and Devices* and by price declines in the kiosk and related media portion of *Retail Printing* within CDG. Volume did not have a significant impact on consolidated net sales, as declines within traditional SPGs were generally offset by volume increases within digital SPGs.

PAGE 28

The increase in digital product sales was primarily due to increased revenues from *Digital Capture and Devices*, and the digital portion of *Retail Printing*, both within CDG. Within GCG, growth in *Digital Printing Solutions* and in the digital prepress consumables portion of *Prepress Solutions* also contributed to this increase.

The decrease in net sales of the Company's traditional products was primarily driven by declines in *Film Capture* within FPG, and the traditional portion of *Retail Printing* within CDG.

### Gross Profit

Gross profit improved in the third quarter of 2007 in both dollars and as a percentage of sales, due largely to reduced manufacturing and other costs as a result of a number of factors, as well as increased intellectual property royalties within CDG. In addition, foreign exchange was a positive contributor to gross profit as a result of the weak U.S. dollar. The decreases in manufacturing and other costs were driven by a combination of the impact of the Company's cost reduction initiatives, strategic manufacturing and supply chain initiatives within CDG, lower restructuring-related charges, and lower depreciation expense, partially offset by increased silver and aluminum costs. These increases to gross profit margins were also partially offset by unfavorable price/mix, which was primarily driven by *Digital Capture and Devices* within CDG, *Film Capture* within FPG, and *Prepress Solutions* within GCG.

Included in gross profit for the quarter is a non-recurring extension and amendment of an existing license arrangement within *Digital Capture and Devices*. This licensing arrangement contributed approximately 2.6% of revenue to consolidated gross profit dollars in the current quarter, as compared with 2.2% of revenue to consolidated gross profit dollars for a similar arrangement in the prior year quarter.

### Selling, General and Administrative Expenses

The year-over-year decrease in consolidated SG&A was primarily attributable to significant Company-wide cost reduction actions, partially offset by increased advertising costs related to *Consumer Inkjet Systems*.

### Research and Development Costs

The decrease in research and development costs (R&D) was primarily driven by the continuing realignment of resources, as well as the timing of development of new products.

### Restructuring Costs and Other

These costs, as well as the restructuring-related costs reported in cost of goods sold, are discussed under "RESTRUCTURING COSTS AND OTHER" below.

**Other Operating Expenses (Income), Net**

The other operating expenses (income), net category includes gains and losses on sales of capital assets and certain asset impairment charges. The year-over-year change in other operating expenses (income), net was largely driven by significant one-time gains on sales of capital assets in the prior year quarter.

**Interest Expense**

Lower interest expense was primarily due to lower debt levels resulting from the full payoff of the Company's Secured Term Debt in the second quarter of 2007.

PAGE 29

**Other Income (Charges), Net**

The other income (charges), net category includes interest income, income and losses from equity investments, and foreign exchange gains and losses. The increase in other income (charges), net was primarily attributable to higher interest income due to higher year-over-year cash balances resulting from the proceeds on the sale of the Health Group, and was also impacted by higher gains on foreign exchange transactions than in the prior year.

**Income Tax (Benefit) Provision**

(dollars in millions)	Three Months Ended September 30	
	2007	2006
Earnings (loss) from continuing operations before income taxes	\$29	(\$53)
(Benefit) provision for income taxes	(5)	30
Effective tax rate	(17.2)%	(56.6)%
(Benefit) provision for income taxes @ 35%	\$10	(\$19)
Difference between tax at effective vs statutory rate	(\$15)	\$49

For the three months ended September 30, 2007, the difference between the Company's recorded benefit and the provision that would result from applying the U.S. statutory rate of 35.0% is primarily attributable to: (1) losses generated in certain jurisdictions outside the U.S., which were not benefited, (2) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S., (3) non-U.S. tax benefits of \$6 million associated with restructuring costs and asset impairments, (4) a net benefit of \$16 million associated with adjustments related to uncertain tax positions, and (5) a tax provision of \$13 million associated with the impact of foreign legislative tax rate changes.

In accordance with SFAS No. 109, "Accounting for Income Taxes," the Company recorded a tax benefit in continuing operations associated with the realization of current year losses in certain jurisdictions where it has historically had a valuation allowance due to the recognition of the pre-tax gain in discontinued operations.

For the three months ended September 30, 2006, the difference between the recorded provision and the benefit that would result from applying 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, (2) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S., (3) non-U.S. tax benefits of \$8 million associated with restructuring costs and asset impairments, and (4) discrete tax benefits of \$9 million relating primarily to tax rate changes, impacts from ongoing tax audits with respect to open tax years, and other property sales gains/losses.

PAGE 30

**CONSUMER DIGITAL IMAGING GROUP**

(dollars in millions)	Three Months Ended				
	September 30		September 30		Increase / (Decrease)
	2007	% of Sales	2006	% of Sales	
Digital net sales	\$ 765		\$ 660		\$ 105
Traditional net sales	358		449		(91)
Total net sales	1,123		1,109		14
Cost of goods sold	863		864		(1)
Gross profit	260	23.2%	245	22.1%	15
Selling, general and administrative expenses	188	17%	180	16%	8
Research and development costs	62	6%	68	6%	(6)
Earnings (loss) from continuing operations before interest, other income (charges), net and income taxes	\$ 10	1%	\$ (3)	0%	\$ 13

	Three Months Ended		Percent Change vs. 2006			
	September 30		Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs
	2007	Change vs. 2006				
	Amount					
Total net sales	\$ 1,123	1.3%	3.8%	-4.7%	2.2%	0.0%
Gross profit margin	23.2%	1.1pp	0.1pp	-4.7pp	1.2pp	4.5pp

## Worldwide Revenues

Net sales in CDG increased 1% due to increases in digital products, significantly offset by decreases in the traditional portion of the business. Volume increases were primarily attributable to digital cameras, kiosks and related media, and the new digital picture frames, partially offset by declines in the traditional portion of *Retail Printing* and snapshot printing. Negative price/mix was largely driven by digital camera product portfolio shifts within *Digital Capture and Devices*, and kiosks and related media within *Retail Printing*.

Net worldwide sales of *Digital Capture and Devices*, which includes consumer digital cameras, accessories, memory products, snapshot printers and related media, and intellectual property royalties, increased 18% in the third quarter of 2007 as compared with the prior year quarter, primarily reflecting higher digital camera volumes, sales of new digital picture frames, increased intellectual property royalties and favorable exchange, partially offset by negative price/mix and lower snapshot printing volumes. For digital still cameras, Kodak remains in the top three market position on a worldwide basis year-to-date through August.

*Retail Printing* includes color negative paper, photochemicals, service and support, photofinishing services, and retail kiosks and related media. Net worldwide sales of *Retail Printing* decreased 13% in the third quarter of 2007 as compared with the prior year quarter, reflecting volume declines in the traditional portion of the business and negative price/mix in kiosks and related media, partially offset by favorable foreign exchange. Paper, photochemicals, and output systems revenues declined 16% and sales of photofinishing services declined 32% from the third quarter of 2006, reflecting continuing industry volume declines. These declines were partially offset by increased sales of kiosks and related media, which increased 13% from the prior year quarter. The change in kiosks and related media sales reflects strong consumables sales at retail locations, as well as higher kiosk equipment sales.

PAGE 31

CDG digital product sales are comprised of digital capture and devices, kiosks/media, online printing, consumer inkjet systems, and imaging sensors. The 16% increase was primarily driven by higher sales of digital cameras, higher kiosk and related media sales, increased intellectual property royalties and sales of new digital picture frames, partially offset by declines in snapshot printing.

CDG traditional product sales are comprised of consumer and professional photographic paper, photochemicals and photofinishing services. The 20% decrease in traditional product sales for CDG was primarily driven by declines in photofinishing services and photographic paper.

**Gross Profit**

The increase in gross profit margin for CDG was primarily attributable to reductions in cost, increases in intellectual property royalties, and favorable foreign exchange. The reductions in manufacturing and other costs were primarily driven by strategic manufacturing and supply chain initiatives to respond to continuous unfavorable price in *Digital Capture and Devices*. In addition, cost reductions were driven by the benefits of previous restructuring activities and lower depreciation expense, partially offset by adverse silver costs, and costs associated with the scaling of manufacturing and new product introduction activities in the *Consumer Inkjet Systems* business. The gross profit margin improvement was partially offset by unfavorable mix in *Digital Capture and Devices*, excluding intellectual property royalties.

Included in gross profit for the quarter is a non-recurring extension and amendment to an existing license arrangement. The impact of this licensing arrangement contributed approximately 6.0% of revenue to segment gross profit dollars in the current quarter, as compared with 5.1% of revenue to segment gross profit dollars for a similar arrangement in the prior year quarter. These types of arrangements provide the Company with a return on portions of historical R&D investments and similar opportunities are expected to have a continuing impact on the results of operations.

**Selling, General and Administrative Expenses**

The increase in SG&A expenses for CDG was primarily driven by increased advertising expenses associated with *Consumer Inkjet Systems*, partially offset by focused cost reduction initiatives and improved go-to-market structure.

**Research and Development Costs**

The decrease in R&D costs for CDG was attributable to spending incurred in 2006 related to the development of *Consumer Inkjet Systems*, which were introduced in the first quarter of 2007.

**FILM PRODUCTS GROUP**

(dollars in millions)	Three Months Ended				
	September 30		September 30		Increase / (Decrease)
	2007	% of Sales	2006	% of Sales	
Total net sales	\$ 488		\$ 593		\$ (105)
Cost of goods sold	284		361		(77)
Gross profit	204	41.8%	232	39.1%	(28)
Selling, general and administrative expenses	75	15%	109	18%	(34)
Research and development costs	7	1%	8	1%	(1)
Earnings from continuing operations before interest, other income (charges), net and income taxes	\$ 122	25%	\$ 115	19%	\$ 7

PAGE 32

Three Months Ended		Percent Change vs. 2006			
September 30		Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs
2007	Change vs. 2006				
Amount					

net sales	\$	488	-17.7%	-17.6%	-2.6%	2.5%	0
profit margin		41.8%	2.7pp	-0.5pp	-2.6pp	1.6pp	4

### Worldwide Revenues

The decrease in FPG worldwide net sales was comprised of: (1) lower volumes, which were primarily attributable to *Film Capture* and *Entertainment Imaging* films, and (2) declines related to negative price/mix, which were primarily attributable to *Film Capture*. These decreases were partially offset by favorable foreign exchange.

Net worldwide sales of *Film Capture*, including consumer roll film (35mm and APS film), one-time-use cameras (OTUC), professional films, and reloadable traditional film cameras, decreased 32% in the third quarter of 2007 as compared with the third quarter of 2006, primarily reflecting continuing industry volume declines and negative price/mix, partially offset by favorable exchange.

Net worldwide sales for *Entertainment Imaging* films, which includes origination, intermediate, and print films for the entertainment industry, decreased 5% compared with the prior year, primarily reflecting volume declines in color print films and negative price/mix in origination films, partially offset by favorable exchange across all product lines.

### Gross Profit

The increase in FPG gross profit margin was primarily attributable to decreased manufacturing and other costs, which were driven by the impact of the Company's cost reduction initiatives, and lower depreciation expense, partially offset by increased silver costs. Favorable foreign exchange also increased gross profit margins. Negative price/mix effects were driven by both *Film Capture* and *Entertainment Imaging* films.

### Selling, General and Administrative Expenses

The decline in SG&A expenses for FPG was attributable to the concentrated efforts of the business to achieve target cost models.

PAGE 33

### GRAPHIC COMMUNICATIONS GROUP

(dollars in millions)	Three Months Ended September 30					
	2007	% of Sales	2006	% of Sales	Increase / (Decrease)	Chan %
Digital net sales	\$ 824		\$ 757		\$ 67	
Traditional net sales	104		123		(19)	-
Total net sales	928		880		48	
Cost of goods sold	674		635		39	
Gross profit	254	27.4%	245	27.8%	9	
Selling, general and administrative expenses	162	17%	169	19%	(7)	
Research and development costs	50	5%	50	6%		
Earnings from continuing operations before interest, other income (charges), net and income taxes	\$ 42	5%	\$ 26	3%	\$ 16	

	Three Months Ended		Percent Change vs. 2006			
	September 30		Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs
	2007 Amount	Change vs. 2006				
Total net sales	\$ 928	5.5%	3.5%	-0.2%	2.2%	0.0%
Gross profit margin	27.4%	-0.4pp	0.3pp	-1.3pp	1.1pp	-0.5pp

### Worldwide Revenues

Volume increases and favorable foreign exchange combined to drive the growth in GCG net sales during the quarter. Specifically, volume growth was primarily driven by *Prepress Solutions*, *Digital Printing Solutions*, and *Enterprise Solutions*. Within *Prepress Solutions*, volume growth in digital prepress consumables was partially offset by volume declines in traditional prepress consumables.

Net worldwide sales of *Prepress Solutions* increased 5%, primarily driven by increased sales of digital plates, partially offset by declines in sales of analog plates.

Net worldwide sales of *Document Imaging* increased 2% compared with prior year, driven by increased revenue in business process services and scanners.

Net worldwide sales of *Digital Printing Solutions* increased 10%, primarily driven by electrophotographic solutions.

Net worldwide sales of *Enterprise Solutions* increased 5%, primarily attributable to revenue growth from workflow software products.

GCG digital product sales are comprised of *Enterprise Solutions*, *Digital Printing Solutions*, portions of *Prepress Solutions* and portions of *Document Imaging*. The 9% increase in digital products and services revenue was primarily attributable to increased sales from *Digital Printing Solutions* and the digital portions of *Prepress Solutions*.

GCG traditional product sales are comprised of sales of traditional prepress consumables, including analog plates and graphics film, and traditional document imaging equipment and media. The 15% decrease in traditional product sales was primarily attributable to lower volumes of analog plates.

PAGE 34

### Gross Profit

While gross profit dollars increased due to sales volume, the decline in gross profit margin was primarily driven by unfavorable price/mix, largely related to *Prepress Solutions* and *Enterprise Solutions*. The increased manufacturing costs were mainly due to higher aluminum and silver costs. These unfavorable items were partially offset by favorable foreign exchange and volume increases.

### Selling, General and Administrative Expenses

The decrease in SG&A expenses for GCG is largely attributable to concentrated efforts to achieve targeted cost reductions.

### ALL OTHER

### Worldwide Revenues

Net worldwide sales for All Other were \$42 million for the third quarter of 2007 as compared with \$13 million for the third quarter of 2006, representing an increase of \$29 million, or 223%. This increase is attributable to ongoing manufacturing supply and cost-recovery arrangements with Carestream Health, Inc.

### Loss From Continuing Operations Before Interest, Other Income (Charges), Net and Income Taxes

The loss from continuing operations before interest, other income (charges), net and income taxes for All Other was \$9 million in the current quarter as compared with a loss of \$16 million in the third quarter of 2006. This \$7 million improvement in earnings was largely driven by cost reduction actions within the display business.

### RESULTS OF OPERATIONS - DISCONTINUED OPERATIONS

On April 30, 2007, the Company sold all of the assets and business operations of its Health Group segment to Onex Healthcare Holdings, Inc. (["Onex"]) (now known as Carestream Health, Inc.), a subsidiary of Onex Corporation, for up to \$2.55 billion. The price was composed of \$2.35 billion in cash at closing and \$200 million in additional future payments if Onex achieves certain returns with respect to its investment. If Onex investors realize an internal rate of return in excess of 25% on their investment, the Company will receive payment equal to 25% of the excess return, up to \$200 million.

The Company recognized a pre-tax gain of \$980 million on the sale in the second quarter of 2007, and recorded pre-tax true-up adjustments to the gain on sale totaling \$6 million in the third quarter of 2007, primarily related to gains from pension settlements. The pre-tax gain excludes the following: up to \$200 million of potential future payments related to Onex's return on its investment as noted above; potential charges related to settling pension obligations with Onex in future periods; and any adjustments that may be made in the future that are currently under review.

The Company used a portion of the initial \$2.35 billion cash proceeds to fully repay its approximately \$1.15 billion of Secured Term Debt. About 8,100 employees of the Company associated with the Health Group transitioned to Carestream Health, Inc. as part of the transaction. Also included in the sale were manufacturing operations focused on the production of health imaging products, as well as an office building in Rochester, NY.

Upon authorization of the Company's Board of Directors on January 8, 2007, the Company met all the requirements of SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," for accounting for the Health Group segment as a discontinued operation. As such, the Health Group business ceased depreciation and amortization of long-lived assets. In accordance with EITF No. 87-24, "Allocation of Interest to Discontinued Operations," the Company allocated certain interest expense on debt that was required to be repaid as a result of the sale. Interest expense allocated to discontinued operations totaled \$23 million for the three months ended September 30, 2006.

PAGE 35

Total Company earnings from discontinued operations for the three months ended September 30, 2007 and 2006 of \$3 million and \$46 million, respectively, were net of a provision for income taxes of \$3 million, and a benefit for income taxes of \$10 million, respectively.

### Year to date

### RESULTS OF OPERATIONS □ CONTINUING OPERATIONS

#### CONSOLIDATED

(in millions, except per share data)	Nine Months Ended		% of Sales	% of Sales	Increase (Decrease)
	2007	September 30			
Digital net sales	\$ 4,259	% of Sales	\$ 4,084		\$ 175
Traditional net sales	2,926		3,457		(531)



Edgar Filing: EASTMAN KODAK CO - Form 10-Q

New technologies	25		34		
Net sales	7,210		7,575		(3)
Cost of goods sold	5,453		5,880		(4)
Gross profit	1,757	24.4%	1,695	22.4%	
Selling, general and administrative expenses	1,259	17%	1,489	20%	(2)
Research and development costs	398	6%	438	6%	
Restructuring costs and other	480	7%	402	5%	
Other operating expenses (income), net	(33)		(37)		
Loss from continuing operations before interest, other income (charges), net and income taxes	(347)	-5%	(597)	-8%	
Interest expense	84		135		
Other income (charges), net	75		47		
Loss from continuing operations before income taxes	(356)		(685)		
(Benefit) provision for income taxes	(64)		99		(1)
Loss from continuing operations	(292)	-4%	(784)	-10%	4
Earnings from discontinued operations, net of income taxes	753	10%	167	2%	5
NET EARNINGS (LOSS)	\$ 461		\$ (617)		\$ 1,0

	Nine Months Ended		Percent Change vs. 2006			
	2007	Change vs. 2006	Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs
	Amount					
Net sales	\$ 7,210	-4.8%	-4.1%	-3.3%	2.6%	0.0%
Gross profit margin	24.4%	2.0pp	-0.3pp	-3.5pp	1.1pp	4.7%

### Worldwide Revenues

For the nine months ended September 30, 2007, net sales declined as significant industry-related volume declines in the traditional businesses within all three segments were partially offset by growth in digital revenues in CDG and GCG. However, foreign exchange resulted in a positive impact to net sales during the period. The decrease in volumes was primarily driven by *Film Capture* within FPG, and the traditional portion of *Retail Printing* within CDG. Negative price/mix was primarily driven by the product portfolio shifts within *Digital Capture and Devices* and by *Retail Printing* within CDG.

PAGE 36

The increase in digital product sales was primarily due to revenue growth in the digital prepress consumables portion of *Prepress Solutions* and *Enterprise Solutions* within GCG, and kiosks and related media within CDG. Revenues from *Digital Capture and Devices* within CDG were essentially flat year-over-year.

The decrease in net sales of traditional products was primarily driven by declines in *Film Capture* within FPG, the traditional portion of *Retail Printing* within CDG, and the traditional consumables portion of *Prepress Solutions* within GCG.

### Gross Profit

Gross profit improved in the nine months ended September 30, 2007 in both dollars and as a percentage of sales, due largely to reduced manufacturing and other costs as a result of a number of factors, as well as increased intellectual property royalties within CDG. In addition, foreign exchange was a positive contributor to gross profit as a result of the weak U.S. dollar. The decreases in manufacturing and other costs were due to a combination of the impact of the Company's cost reduction initiatives, strategic manufacturing and supply chain initiatives within CDG, lower restructuring-related charges, and lower depreciation expense, partially offset by increased silver and aluminum costs. The unfavorable price/mix was driven by *Digital Capture and Devices* and *Retail Printing* within CDG, and *Film Capture* within FPG.

Included in gross profit is a non-recurring extension and amendment to an existing license arrangement during the current period. The impact of this licensing arrangement contributed approximately 0.9% of revenue to consolidated gross profit dollars in the current period, as compared with 0.8% of revenue to consolidated gross profit dollars for a similar arrangement in the prior year period. These types of arrangements provide the Company with a return on portions of historical R&D investments and similar opportunities are expected to have a continuing impact on the results of operations.

### **Selling, General and Administrative Expenses**

The year-over-year decrease in consolidated SG&A was primarily attributable to significant Company-wide cost reduction actions, partially offset by increased advertising costs related to *Consumer Inkjet Systems*.

### **Research and Development Costs**

The decrease in R&D costs was primarily driven by the continuing realignment of resources, as well as the timing of development of new products.

### **Restructuring Costs and Other**

The most significant portion of the year-to-date restructuring costs was a \$238 million impairment charge related to the sale of the Company's Xiamen, China facility in the second quarter. These costs, as well as the restructuring-related costs reported in cost of goods sold, are discussed in further detail under "RESTRUCTURING COSTS AND OTHER" below.

### **Interest Expense**

Lower interest expense was primarily due to lower debt levels resulting from the full payoff of the Company's Secured Term Debt in the second quarter of 2007.

PAGE 37

### **Other Income (Charges), Net**

The Other income (charges), net category includes interest income, income and losses from equity investments, and foreign exchange gains and losses. The increase in other income (charges), net as compared with the prior year period was primarily attributable to increased interest income due to higher cash balances.

### **Income Tax (Benefit) Provision**

(dollars in millions)	Nine Months Ended September 30	
	2007	2006
Loss from continuing operations before income taxes	(\$356)	(\$685)
(Benefit) provision for income taxes	(64)	99
Effective tax rate	18.0%	(14.5)%
(Benefit) provision for income taxes @ 35%	(\$125)	(\$240)
Difference between tax at effective vs statutory rate	\$61	\$339

For the nine months ended September 30, 2007, the difference between the Company's recorded benefit and the benefit that would result from applying the U.S. statutory rate of 35.0% is primarily attributable to: (1) losses generated in certain jurisdictions outside the U.S., which were not benefited, (2) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S., (3) non-U.S. tax benefits of \$42 million associated with restructuring costs and asset impairments, (4) a net benefit of \$75 million associated with adjustments related to uncertain tax positions, and (5) a tax provision of \$13 million associated with the impact of foreign legislative tax rate changes.

During the second quarter of 2007 the Company identified a deferred tax asset in a recently acquired non-U.S. subsidiary, which should have been appropriately reserved with a valuation allowance in a prior period. Therefore, the Company recorded a valuation allowance of \$20 million in the second quarter of 2007. This amount is included in the \$64 million benefit discussed above.

In accordance with SFAS No. 109, "Accounting for Income Taxes," the Company recorded a tax benefit in continuing operations associated with the realization of current year losses in certain jurisdictions where it has historically had a valuation allowance due to the recognition of the pre-tax gain in discontinued operations.

For the nine months ended September 30, 2006, the difference between the Company's recorded provision and the benefit that would result from applying 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, (2) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S., (3) non-U.S. tax benefits of \$64 million associated with restructuring costs and asset impairments, and (4) discrete tax charges of \$44 million relating primarily to purchase accounting for the Creo and KPG acquisitions, tax rate changes, impacts from ongoing tax audits with respect to open tax years, and other property sales gains/losses.

PAGE 38

**CONSUMER DIGITAL IMAGING GROUP**

	2007		2006		Increase / (Decrease)
	Amount	% of Sales	Amount	% of Sales	
(dollars in millions)					
Digital net sales	\$ 1,871		\$ 1,820		\$ 51
Traditional net sales	1,030		1,296		(266)
Total net sales	2,901		3,116		(215)
Cost of goods sold	2,367		2,617		(250)
Gross profit	534	18.4%	499	16.0%	35
Selling, general and administrative expenses	518	18%	589	19%	(71)
Research and development costs	184	6%	213	7%	(29)
Loss from continuing operations before interest, other income (charges), net and income taxes	\$ (168)	-6%	\$ (303)	-10%	\$ 135

	2007		Percent Change vs. 2006			
	Amount	Change vs. 2006	Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs
Net sales	\$ 2,901	-6.9%	-2.6%	-6.0%	1.7%	
Gross profit margin	18.4%	2.4pp	-0.1pp	-5.6pp	1.1pp	

## Worldwide Revenues

Net sales in CDG declined 7% due to significant declines in the traditional portion of the business, partially offset by increases in digital products. The negative price/mix was primarily driven by digital camera product portfolio shifts within *Digital Capture and Devices* and by *Retail Printing*. The decrease in volumes was largely attributable to snapshot printing, the traditional portion of *Retail Printing*, and inkjet media, partially offset by sales of the new digital picture frames and inkjet printers.

Net worldwide sales of *Digital Capture and Devices*, which includes consumer digital cameras, accessories, memory products, snapshot printers and related media, and intellectual property royalties, were essentially flat in the nine months ended September 30, 2007 as compared with the prior year period, primarily reflecting negative price/mix on digital cameras and lower snapshot printing volumes, largely offset by increased intellectual property royalties, sales of new digital picture frames, and favorable foreign exchange. For digital still cameras, Kodak remains in the top three market position on a worldwide basis year-to-date through August.

*Retail Printing* includes color negative paper, photochemicals, service and support, photofinishing services, and retail kiosks and related media. Net worldwide sales of *Retail Printing* decreased 14% in the nine months ended September 30, 2007 as compared with the prior year period, reflecting volume declines in the traditional portion of the business, and negative price/mix, partially offset by favorable foreign exchange. Paper, photochemicals, and output systems revenues declined 14% and sales of photofinishing services declined 39% as compared with the prior year period, reflecting continuing industry volume declines. These declines were partially offset by increased sales of kiosks and related media, which increased 9% from the prior year period.

CDG digital product sales are comprised of digital capture and devices, kiosks/media, online printing, consumer inkjet systems, and imaging sensors. The 3% increase in digital product sales for CDG was primarily driven by intellectual property royalty revenues, new digital picture frames, kiosks and related media, and new inkjet printers, partially offset by declines in sales of snapshot printing, digital cameras, and inkjet media.

PAGE 39

CDG traditional product sales are comprised of consumer and professional photographic paper, photochemicals and photofinishing services. The 21% decrease in traditional product sales was primarily driven by declines in photofinishing services and photographic paper.

## Gross Profit

The increase in gross profit margin for CDG was primarily attributable to reductions in cost, increases in intellectual property royalties, and favorable foreign exchange. The reductions in manufacturing and other costs were primarily driven by strategic manufacturing and supply chain initiatives to respond to continuous unfavorable price in *Digital Capture and Devices*. In addition, cost reductions were driven by the benefits of previous restructuring activities and lower depreciation expense, partially offset by adverse silver costs, and costs associated with the scaling of manufacturing and new product introduction activities in the *Consumer Inkjet Systems* business. The gross profit margin improvement was partially offset by unfavorable price/mix in *Retail Printing*.

Included in gross profit is a non-recurring extension and amendment to an existing license arrangement during the current period. The impact of this licensing arrangement contributed approximately 2.3% of revenue to segment gross profit dollars in the current period, as compared with 1.8% of revenue to segment gross profit dollars for a similar arrangement in the prior year period. These types of arrangements provide the Company with a return on portions of historical R&D investments and similar opportunities are expected to have a continuing impact on the results of operations.

## Selling, General and Administrative Expenses

The decrease in SG&A expenses for CDG was primarily driven by focused cost reduction initiatives and improved go-to-market structure, partially offset by increased advertising expenses associated with *Consumer Inkjet Systems*.

## Research and Development Costs

The decrease in R&D costs for CDG is largely attributable to spending incurred in 2006 related to the development of *Consumer Inkjet Systems*, which were introduced in the first quarter of 2007, and was also impacted by cost reduction actions.

## FILM PRODUCTS GROUP

(dollars in millions)	2007		Nine Months Ended September 30		2006		Increase (Decrease)
			% of Sales		% of Sales		
Total net sales	\$	1,505		\$	1,753		\$ (248)
Cost of goods sold		916			1,099		(183)
Gross profit		589	39.1%		654	37.3%	(65)
Selling, general and administrative expenses		238	16%		345	20%	(107)
Research and development costs		22	1%		24	1%	(2)
Earnings from continuing operations before interest, other income (charges), net and income taxes	\$	329	22%	\$	285	16%	\$ 44

PAGE 40

	2007		Change vs. 2006		Percent Change vs. 2006		
	Amount		2006	Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs
Total net sales	\$	1,505	-14.1%	-14.4%	-2.2%	2.5%	0.0%
Gross profit margin		39.1%	1.8pp	-0.5pp	-2.6pp	1.7pp	3.2pp

## Worldwide Revenues

The decrease in FPG worldwide net sales was comprised of: (1) lower volumes, which were primarily attributable to *Film Capture*, and (2) declines related to negative price/mix, which were primarily attributable to *Film Capture* and *Entertainment Imaging* films. These decreases were partially offset by favorable foreign exchange.

Net worldwide sales of *Film Capture*, including consumer roll film (35mm and APS film), one-time-use cameras (OTUC), professional films, and reloadable traditional film cameras, decreased 30% in the nine months ended September 30, 2007 as compared with the prior year period, primarily reflecting continuing industry volume declines and negative price/mix, partially offset by favorable exchange.

Net worldwide sales for *Entertainment Imaging* films, which include origination, intermediate, and print films for the entertainment industry, increased 1%, primarily reflecting favorable foreign exchange, partially offset by unfavorable price/mix and volume declines.

## Gross Profit

Reduced manufacturing and other costs were driven by cost reduction initiatives and lower depreciation expense, partially offset by higher silver costs. These improvements in gross profit margins were partially offset by negative price/mix within both *Film Capture* and *Entertainment Imaging* films.

**Selling, General and Administrative Expenses**

The decline in SG&A expenses for FPG was attributable to the concentrated efforts of the business to reduce costs.

PAGE 41

**GRAPHIC COMMUNICATIONS GROUP**

	2007		2006		Increase
	Amount	% of Sales	Amount	% of Sales	
(dollars in millions)					
Digital net sales	\$ 2,388		\$ 2,264		\$ 124
Traditional net sales	333		394		(61)
Total net sales	2,721		2,658		63
Cost of goods sold	1,977		1,906		71
Gross profit	744	27.3%	752	28.3%	(8)
Selling, general and administrative expenses	497	18%	536	20%	(39)
Research and development costs	152	6%	150	6%	2
Earnings from continuing operations before interest, other income (charges), net and income taxes	\$ 95	3%	\$ 66	2%	\$ 29

	2007		2006		Percent Change vs. 2006		
	Amount	Change vs. 2006	Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs	
Net sales	\$ 2,721	2.4%	-0.4%	-0.9%	3.7%	0.0pp	
Profit margin	27.3%	-1.0pp	0.0pp	-0.4pp	0.4pp	-1.0pp	

**Worldwide Revenues**

The increase in net sales was primarily attributable to favorable foreign exchange. The volume declines were primarily driven by the traditional prepress consumables portion of *Prepress Solutions*, largely offset by increases in the digital prepress consumables portion of *Prepress Solutions*. Unfavorable price/mix was primarily attributable to *Prepress Solutions* and *Enterprise Solutions*.

Net worldwide sales of *Prepress Solutions* increased 2%, primarily driven by increased sales of digital plates, partially offset by declines in sales of analog plates and prepress equipment sales.

Net worldwide sales of *Document Imaging* increased 1%, primarily driven by increased business process service revenues, partially offset by traditional document imaging media.

Net worldwide sales of *Digital Printing Solutions* increased 1%, primarily driven by growth in consumables and service, partially offset by declines in equipment.

Net worldwide sales of *Enterprise Solutions* increased 11%, primarily driven by growth from workflow software products.

GCG digital product sales are comprised of *Enterprise Solutions*, *Digital Printing Solutions*, portions of *Prepress Solutions*, and portions of *Document Imaging*. The 5% increase in digital product sales for GCG was primarily attributable to the digital portion of *Prepress Solutions*, *Enterprise Solutions*, and favorable exchange.

The 15% decrease in GCG traditional product sales was primarily attributable to lower volumes of analog plates.

PAGE 42

### **Gross Profit**

Gross profit deteriorated slightly compared with the prior year period, largely as a result of the increased manufacturing and other costs, driven by adverse aluminum and silver pricing. The negative price/mix was largely driven by *Prepress Solutions*, *Digital Printing Solutions*, and *Enterprise Solutions*. These negative impacts on gross profit margin were partially offset by favorable foreign exchange.

### **Selling, General and Administrative Expenses**

The decrease in SG&A expenses for GCG was largely attributable to concentrated efforts of the business to achieve targeted cost reductions.

### **ALL OTHER**

#### **Worldwide Revenues**

Net worldwide sales for All Other were \$83 million for the nine months ended September 30, 2007 as compared with \$48 million for the nine months ended September 30, 2006, representing an increase of \$35 million, or 73%. This increase is attributable to ongoing manufacturing supply and cost-recovery arrangements with Carestream Health, Inc.

#### **Loss From Continuing Operations Before Interest, Other Income (Charges), Net and Income Taxes**

The loss from continuing operations before interest, other income (charges), net and income taxes for All Other was \$30 million in the current period as compared with a loss of \$57 million in the nine months ended September 30, 2006. This \$27 million improvement in earnings is largely driven by cost reduction actions within the display business.

### **RESULTS OF OPERATIONS - DISCONTINUED OPERATIONS**

On April 30, 2007, the Company sold all of the assets and business operations of its Health Group segment to Onex Healthcare Holdings, Inc. Refer to "Results of Operations - Discontinued Operations" for the third quarter on page 34.

Interest expense allocated to discontinued operations totaled \$30 million and \$67 million for the nine months ended September 30, 2007 and 2006, respectively.

Total Company earnings from discontinued operations for the nine months ended September 30, 2007 and 2006 of \$753 million (including a pre-tax gain on sale of \$986 million) and \$167 million, respectively, were net of a provision for income taxes of \$267 million, and a benefit for income taxes of \$26 million, respectively.

### **RESTRUCTURING COSTS AND OTHER**

The Company has undertaken a cost reduction program that was initially announced in January 2004. This program is referred to as the "2004-2007 Restructuring Program." This program was expected to result in total charges of \$1.3 billion to \$1.7 billion over a three-year period ending in 2006, of which \$700 million to \$900 million related to severance, with the remainder relating to the disposal of buildings and equipment. Overall, Kodak's worldwide facility square footage was expected to be reduced by approximately one-third. Approximately 12,000 to 15,000 positions worldwide were expected to be eliminated through these actions primarily in global

manufacturing, selected traditional businesses and corporate administration.

The Company subsequently expanded the program to extend into 2007 and increased the expected employment reductions to 28,000 to 30,000 positions and total charges to \$3.6 billion to \$3.8 billion. The Company now expects that the total employment reductions will be in the range of 27,000 to 28,000 positions and total charges will be in the range of \$3.4 billion to \$3.6 billion. These new estimates reflect greater efficiencies in manufacturing infrastructure projects as well as the Company's ability to outsource or sell certain operations, which reduces involuntary severance charges.

PAGE 43

The aforementioned 2004-2007 Restructuring Program underpins a dramatic transformation of the Company focused on two primary elements of cost restructuring: manufacturing infrastructure and operating expense rationalization. As this four-year effort has progressed, the underlying business model necessarily has evolved, requiring broader and more costly manufacturing infrastructure reductions (primarily non-cash charges) than originally anticipated, as well as similarly broader rationalization of selling, administrative and other business resources (primarily severance charges). In addition, the recent divestiture of the Health Group has further increased the amount of reductions necessary to appropriately scale the Corporate infrastructure.

The actual charges for initiatives under this program are recorded in the period in which the Company commits to formalized restructuring plans or executes the specific actions contemplated by the program and all criteria for restructuring charge recognition under the applicable accounting guidance have been met.

### Restructuring Programs Summary

The activity in the accrued restructuring balances and the non-cash charges incurred in relation to all of the Company's restructuring programs were as follows for the third quarter of 2007:

(in millions)	Balance	Costs Incurred	Reversals	Cash Payments	Non-cash Settlements	Other	Balance
	June 30, 2007					Adjustments and Reclasses	
<b>2004-2007 Restructuring Program:</b>		(1)		(2)		(3)	
Severance reserve	\$ 173	\$ 59	\$ (1)	\$ (62)	\$ □	\$ (6)	\$ 163
Exit costs reserve	24	38	□	(40)	□	2	24
Total reserve	\$ 197	\$ 97	\$ (1)	\$ (102)	\$ □	\$ (4)	\$ 187
Long-lived asset impairments and inventory write-downs	\$ □	\$ 10	\$ □	\$ □	\$ (10)	\$ □	\$ □
Accelerated depreciation	\$ □	\$ 23	\$ □	\$ □	\$ (23)	\$ □	\$ □
<b>Pre-2004 Restructuring Programs:</b>							
Severance reserve	\$ □	\$ □	\$ □	\$ □	\$ □	\$ □	\$ □
Exit costs reserve	6	□	□	(1)	□	1	6
Total reserve	\$ 6	\$ □	\$ □	\$ (1)	\$ □	\$ 1	\$ 6
<b>Total of all restructuring programs</b>	<b>\$ 203</b>	<b>\$ 130</b>	<b>\$ (1)</b>	<b>\$ (103)</b>	<b>\$ (33)</b>	<b>\$ (3)</b>	<b>\$ 193</b>

(1) The costs incurred include both continuing operations of \$128 million and discontinued operations of \$2 million.

(2) During the three months ended September 30, 2007, the Company paid approximately \$110 million related to restructuring. Of this total amount, \$103 million was recorded against restructuring reserves,



while \$7 million was recorded against pension and other postretirement liabilities.

- (3) The total restructuring charges of \$130 million include pension and other postretirement charges and credits for curtailments, settlements and special termination benefits. However, because the impact of these charges and credits relate to the accounting for pensions and other postretirement benefits, the related impacts on the Consolidated Statement of Financial Position are reflected in their respective components as opposed to within the accrued restructuring balances at September 30, 2007. Accordingly, the Other Adjustments and Reclasses column of the table above includes (1) reclassifications to Other long-term assets and Pension and other postretirement liabilities for the position elimination-related impacts on the Company's pension and other postretirement employee benefit plan arrangements, including net curtailment, settlement and special termination charges of (\$11) million, and (2) reclassifications to Other long-term liabilities for the restructuring-related impacts on the Company's environmental remediation liabilities of \$1 million. Additionally, the Other Adjustments and Reclasses column of the table above includes foreign currency translation of \$7 million.

PAGE 44

The costs incurred, net of reversals, which total \$129 million for the three months ended September 30, 2007, include \$23 million and \$4 million of charges related to accelerated depreciation and inventory write-downs that were reported in cost of goods sold in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007. Of the remaining costs incurred, net of reversals, \$2 million was included in discontinued operations and \$100 million was reported as restructuring costs and other in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007. The severance costs and exit costs require the outlay of cash, while long-lived asset impairments, accelerated depreciation and inventory write-downs represent non-cash items.

#### **2004-2007 Restructuring Program Activity**

The Company implemented certain actions under the program during the third quarter of 2007. As a result of these actions, the Company recorded charges, net of reversals, of \$129 million in the third quarter of 2007, which were composed of severance, long-lived asset impairments, exit costs, inventory write-downs, and accelerated depreciation of \$58 million, \$6 million, \$36 million, \$4 million, and \$23 million, respectively. Included in these amounts, \$2 million of exit costs are presented as discontinued operations. The severance costs related to the elimination of approximately 1,425 positions, including approximately 100 photofinishing, 1,025 manufacturing, 50 research and development and 250 administrative positions. The geographic composition of the positions to be eliminated includes approximately 775 in the United States and Canada and 650 throughout the rest of the world. The reduction of the 1,425 positions and the \$129 million charges, net of reversals, are reflected in the 2004-2007 Restructuring Program table below. The \$6 million charge in the third quarter for long-lived asset impairments was included in restructuring costs and other in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007, respectively. The charges taken for inventory write-downs of \$4 million were reported in cost of goods sold in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007.

As a result of initiatives implemented under the 2004-2007 Restructuring Program, the Company also recorded \$23 million of accelerated depreciation on long-lived assets in cost of goods sold in the accompanying Consolidated Statement of Operations for the three months ended September 30, 2007. The accelerated depreciation relates to long-lived assets accounted for under the held and used model of SFAS No. 144. The total amount of \$23 million relates to \$22 million of manufacturing facilities and equipment, and \$1 million of photofinishing facilities that will be used until their abandonment. The Company will incur approximately \$2 million of accelerated depreciation in the fourth quarter of 2007 as a result of the initiatives already implemented under the 2004-2007 Restructuring Program.

Edgar Filing: EASTMAN KODAK CO - Form 10-Q

In April 2007, the Company entered into an agreement to sell its manufacturing site in Xiamen, China. This sale closed in the second quarter of 2007 and resulted in a non-cash charge of approximately \$238 million. This action is part of the 2004-2007 Restructuring Program.

Under this program, on a life-to-date basis as of September 30, 2007, the Company has recorded charges of \$3,329 million, which was composed of severance, long-lived asset impairments, exit costs, inventory write-downs and accelerated depreciation of \$1,381 million, \$617 million, \$342 million, \$79 million and \$931 million, respectively, less reversals of \$21 million. The severance costs related to the elimination of approximately 27,025 positions, including approximately 6,525 photofinishing, 12,975 manufacturing, 1,500 research and development and 6,025 administrative positions.

The following table summarizes the activity with respect to the charges recorded in connection with the focused cost reduction actions that the Company has committed to under the 2004-2007 Restructuring Program and the remaining balances in the related reserves at September 30, 2007:

PAGE 45

(dollars in millions)	Number of Employees	Severance Reserve	Exit Costs Reserve	Total	Long-lived Asset Impairments and Inventory Accelerated Depreciation	
					Write-downs	Depreciation
2004 charges - continuing operations	8,975	\$ 405	\$ 95	\$ 500	\$ 156	\$ 152
2004 charges - discontinued operations	650	13	4	17	1	□
2004 reversals - continuing operations	□	(6)	(1)	(7)	□	□
2004 utilization	(5,175)	(169)	(47)	(216)	(157)	(152)
2004 other adj. & reclasses		24	(15)	9	□	□
Balance at 12/31/04	4,450	267	36	303	□	□
2005 charges - continuing operations	7,850	472	82	554	160	391
2005 charges - discontinued operations	275	25	2	27	1	□
2005 reversals - continuing operations	□	(3)	(6)	(9)	□	□
2005 utilization	(10,225)	(377)	(95)	(472)	(161)	(391)
2005 other adj. & reclasses		(113)	4	(109)	□	□
Balance at 12/31/05	2,350	271	23	294	□	□
2006 charges - continuing operations	5,150	266	66	332	97	273
2006 charges - discontinued operations	475	52	3	55	3	12
2006 reversals - continuing operations	□	(3)	(1)	(4)	□	□
2006 utilization	(5,700)	(416)	(67)	(483)	(100)	(285)
2006 other adj. & reclasses		58	□	58	□	□
Balance at 12/31/06	2,275	228	24	252	□	□
Q1 2007 charges - continuing operations	1,075	53	22	75	11	65
Q1 2007 charges - discontinued operations	50	17	□	17	□	□
Q1 2007 utilization	(1,000)	(84)	(20)	(104)	(11)	(65)
Q1 2007 other adj. & reclasses		(18)	□	(18)	□	□
Balance at 3/31/07	2,400	196	26	222	□	□
Q2 2007 charges - continuing operations	1,100	16	28	44	257	15
Q2 2007 charges - discontinued operations		3	2	5	□	□
Q2 2007 utilization	(1,250)	(83)	(32)	(115)	(257)	(15)
Q2 2007 other adj. & reclasses		41	□	41	□	□
Balance at 6/30/07	2,250	173	24	197	□	□
Q3 2007 charges - continuing operations	1,425	59	36	95	10	23
Q3 2007 charges - discontinued operations			2	2	□	□

Q3 2007 reversals - continuing operations		(1)	□	(1)		
Q3 2007 utilization	(1,000)	(62)	(40)	(102)	(10)	(23)
Q3 2007 other adj. & reclasses		(6)	2	(4)	□	□
Balance at 9/30/07	2,675	\$ 163	\$ 24	\$ 187	\$ □	\$ □

As a result of the initiatives already implemented under the 2004-2007 Restructuring Program, severance payments will be paid during periods through 2008 since, in many instances, the employees whose positions were eliminated can elect or are required to receive their payments over an extended period of time. Most exit costs have been paid or will be paid during 2007. However, certain costs, such as long-term lease payments, will be paid over periods after 2007.

PAGE 46

The charges of \$130 million recorded in the third quarter of 2007 included \$28 million applicable to FPG, \$19 million applicable to CDG, \$7 million applicable to GCG, and \$74 million that was applicable to manufacturing, research and development, and administrative functions, which are shared across all segments. The remaining \$2 million is applicable to discontinued operations.

The restructuring actions implemented during the third quarter of 2007 under the 2004-2007 Restructuring Program are expected to generate future annual cost savings of approximately \$83 million, all of which are expected to be future annual cash savings. These cost savings began to be realized by the Company beginning in the third quarter of 2007, and are expected to be fully realized by the end of 2008 as most of the actions and severance payouts are completed. These total cost savings are expected to reduce future cost of goods sold, SG&A, and R&D expenses by approximately \$53 million, \$25 million, and \$5 million, respectively.

Based on all of the actions taken to date under the 2004-2007 Restructuring Program, the program is expected to generate annual cost savings of approximately \$1,618 million, including annual cash savings of \$1,544 million, as compared with pre-program levels. The Company began realizing these savings in the second quarter of 2004, and expects the savings to be fully realized by the end of 2008 as most of the actions and severance payouts are completed. These total cost savings are expected to reduce cost of goods sold, SG&A, and R&D expenses by approximately \$1,026 million, \$444 million, and \$148 million, respectively.

The above savings estimates are based primarily on objective data related to the Company's severance actions. Savings resulting from facility closures and other non-severance actions that are more difficult to quantify are not included. The Company reaffirms its estimate of total annual cost savings including both employee-related costs and facility-related costs under the extended 2004-2007 Restructuring Program of \$1.6 billion to \$1.8 billion, as announced in July 2005, and does not expect the final annual cost savings to differ materially from this estimate.

### Pre-2004 Restructuring Programs Activity

At September 30, 2007, the Company had remaining exit costs reserves of \$6 million, relating to restructuring plans committed to or executed prior to 2004. Most of these remaining exit costs reserves represent long-term lease payments, which will continue to be paid over periods throughout and after 2007.

## LIQUIDITY AND CAPITAL RESOURCES

### Cash Flow Activity

The Company's primary sources and uses of cash for the nine month period ended September 30, 2007 included proceeds on the sale of the Health Group, earnings from continuing operations, adjusted for non-cash items of income and expense, debt payments, restructuring payments, capital additions, working capital needs, dividend payments and employee benefit plan payments/contributions.

Net cash used in continuing operations from operating activities was \$694 million for the nine months ended September 30, 2007. The Company's primary sources of cash from operating activities for the period are earnings from continuing operations, as adjusted for non-cash items of income and expense, which provided \$486 million

of operating cash. The Company's primary uses of cash in operating activities include:

- Increases in inventories, driven by seasonal build in anticipation of the fourth quarter demand, the introduction of new products, and increased raw material prices;
- Net decrease in liabilities resulting from payment of trade payables and other accruals from year-end 2006 levels;
- Recognition of deferred income on intellectual property arrangements; and
- Decrease in restructuring liabilities driven by cash payments for severance benefits, partially offset by restructuring charges within the current year.

PAGE 47

Included in the uses of cash in operating activities discussed above were:

- Cash expenditures of \$345 million against restructuring reserves and pension and other postretirement liabilities, primarily for the payment of severance benefits. Employees whose positions were eliminated could elect to receive severance payments for up to two years following their date of termination.
- Contributions (funded plans) or benefit payments (unfunded plans) totaling approximately \$83 million relating to major U.S. and non-U.S. defined benefit pension plans. The Company expects its contribution (funded plans) and benefit payment (unfunded plans) requirements for its major U.S. and non-U.S. defined benefit pension plans for the balance of 2007 to be approximately \$39 million.
- Benefit payments totaling approximately \$164 million relating to U.S., United Kingdom and Canada postretirement benefit plans. The Company expects to pay benefits of \$51 million for its U.S., United Kingdom and Canada postretirement plans for the balance of 2007.

Net cash used in continuing operations in investing activities for the nine months ended September 30, 2007 of \$43 million includes capital additions of \$179 million. The majority of the spending supports new products, manufacturing productivity and quality improvements, infrastructure improvements, equipment placements with customers, and ongoing environmental and safety initiatives. Proceeds from sales of businesses and assets in the period provided cash of \$146 million.

Net cash provided by discontinued operations from investing activities was \$2,335 million largely due to the proceeds received in connection with the sale of the Health Group business. The Company utilized a portion of this cash for the full repayment of the Secured Term Debt, as reflected in net cash used in financing activities in the period.

Net cash used in financing activities was \$1,215 million, including the repayment of debt discussed above and dividends of \$72 million. The Company has a dividend policy whereby it makes semi-annual payments which, when declared, will be paid on the Company's 10th business day each July and December to shareholders of record on the close of the first business day of the preceding month. On May 9, 2007, the Board of Directors declared a semi-annual cash dividend of \$.25 per share payable to shareholders of record at the close of business on June 1, 2007. This dividend was paid on July 16, 2007. On October 16, 2007, the Board of Directors declared a semi-annual cash dividend of \$.25 per share payable to shareholders of record at the close of business on November 1, 2007 and payable on December 14, 2007.

The Company believes that its cash flow from operations, in addition to asset sales, will be sufficient to cover its working capital and capital investment needs and the funds required for future debt reduction, restructuring payments, dividend payments, employee benefit plan payments/contributions, and potential acquisitions. The Company's cash balances and its financing arrangements will be used to bridge timing differences between expenditures and cash generated from operations.

### **Short-Term Borrowings**

As of September 30, 2007, the Company and its subsidiaries, on a consolidated basis, maintained \$1,086 million in committed bank lines of credit and \$484 million in uncommitted bank lines of credit to ensure continued access to short-term borrowing capacity.

### **Secured Credit Facilities**

On October 18, 2005 the Company closed on \$2.7 billion of Senior Secured Credit Facilities (Secured Credit Facilities) under a new Secured Credit Agreement (Secured Credit Agreement) and associated Security Agreement and Canadian Security Agreement. The Secured Credit Facilities consist of a \$1.0 billion 5-Year Committed Revolving Credit Facility (5-Year Revolving Credit Facility) expiring October 18, 2010 and \$1.7 billion of Term Loan Facilities (Term Facilities) expiring October 18, 2012.

The 5-Year Revolving Credit Facility can be used by Eastman Kodak Company (U.S. Borrower) for general corporate purposes including the issuance of letters of credit. Amounts available under the facility can be borrowed, repaid and re-borrowed throughout the term of the facility provided the Company remains in compliance with covenants contained in the Secured Credit Agreement. As of September 30, 2007, there was no debt outstanding and \$141 million of letters of credit issued under this facility.

PAGE 48

Under the Term Facilities, \$1.2 billion was borrowed at closing primarily to refinance debt originally issued under the Company's previous \$1.225 billion 5-Year Facility to finance the acquisition of Creo Inc. on June 15, 2005. The \$1.2 billion consisted of a \$920 million 7-Year Term Loan to the U.S. Borrower and \$280 million 7-Year Term Loan to Kodak Graphic Communications Canada Company (KGCCC or, the Canadian Borrower). Pursuant to the terms of the Secured Credit Agreement, an additional \$500 million was available to the U.S. Borrower under the seven-year term loan facility for advance at any time through June 15, 2006. On June 15, 2006, the Company used this \$500 million to refinance \$500 million 6.375% Medium Term Notes, Series A, due June 15, 2006.

On January 10, 2007, the Company announced that it had entered into an agreement to sell its Health Group to Onex Healthcare Holdings, Inc., a subsidiary of Onex Corporation. Under terms of the agreement, the Company agreed to sell its Health Group to Onex for up to \$2.55 billion. The price was composed of \$2.35 billion in cash at closing, plus up to \$200 million in additional future payments if Onex achieves certain returns with respect to its investment. If Onex Healthcare investors realize an internal rate of return in excess of 25% on their investment, the Company will receive payment equal to 25% of the excess return, up to \$200 million. The sale closed on April 30, 2007. Because of tax-loss carryforwards and other tax attributes, the Company retained the vast majority of the initial \$2.35 billion cash proceeds. Consistent with the terms of the Secured Credit Agreement, on May 3, 2007 the Company used a portion of the proceeds to fully repay its approximately \$1.15 billion of secured term debt.

At September 30, 2007, there were no borrowings outstanding for these secured credit facilities. Debt issue costs incurred of approximately \$57 million associated with the Secured Credit Facilities were recorded as an asset and are being amortized over the life of the borrowings. As a result of the payment of secured debt in connection with the sale of the Health Group, approximately \$19 million of unamortized costs were written off in the second quarter of 2007 to the gain on sale within discontinued operations. The term facilities are no longer available for new borrowings.

Pursuant to the Secured Credit Agreement and associated Security Agreement, each subsidiary organized in the U.S. jointly and severally guarantees the obligations under the Secured Credit Agreement and all other obligations of the Company and its subsidiaries to the Lenders. The guaranty is supported by the pledge of certain U.S. assets of the U.S. Borrower and the Company's U.S. subsidiaries including, but not limited to, receivables, inventory, equipment, deposit accounts, investments, intellectual property, including patents, trademarks and copyrights, and the capital stock of "Material Subsidiaries." Excluded from pledged assets are real property, "Principal Properties" and equity interests in "Restricted Subsidiaries," as defined in the Company's 1988 Indenture.

"Material Subsidiaries" are defined as those subsidiaries with revenues or assets constituting 5 percent or more of the consolidated revenues or assets of the corresponding borrower. "Material Subsidiaries" are determined on an annual basis under the Secured Credit Agreement.

Pursuant to the Secured Credit Agreement and associated Canadian Security Agreement, Eastman Kodak Company and Kodak Graphic Communications Company (KGCC, formerly Creo Americas, Inc.), jointly and severally guarantee the obligations of the Canadian Borrower, to the Lenders. Subsequently, KGCC has been merged into Eastman Kodak Company. Certain assets of the Canadian Borrower in Canada were also pledged, including, but not limited to, receivables, inventory, equipment, deposit accounts, investments, intellectual property, including patents, trademarks and copyrights, and the capital stock of the Canadian Borrower's Material Subsidiaries.

Interest rates for borrowings under the Secured Credit Agreement are dependent on the Company's Long Term Senior Secured Credit Rating. The Secured Credit Agreement contains various affirmative and negative covenants customary in a facility of this type, including two quarterly financial covenants: (1) a consolidated debt for borrowed money to consolidated earnings before interest, taxes, depreciation and amortization (EBITDA) (subject to adjustments to exclude any extraordinary income or losses, as defined by the Secured Credit Agreement, interest income and certain non-cash items of income and expense) ratio on a rolling four-quarter basis of not greater than 3.50 to 1 as of December 31, 2006 and thereafter, and (2) a consolidated EBITDA to consolidated interest expense (subject to adjustments to exclude interest expense not related to borrowed money) ratio, on a rolling four-quarter basis, of no less than 3.00 to 1. As of September 30, 2007, the Company was in compliance with all covenants under the Secured Credit Agreement.

PAGE 49

In addition, subject to various conditions and exceptions in the Secured Credit Agreement, in the event the Company sells assets for net proceeds totaling \$75 million or more in any year, except for proceeds used within 12 months for reinvestments in the business of up to \$300 million, proceeds from sales of assets used in the Company's non-digital products and services businesses to prepay or repay debt or pay cash restructuring charges within 12 months from the date of sale of the assets, or proceeds from the sale of inventory in the ordinary course of business, the amount in excess of \$75 million must be applied to prepay loans under the Secured Credit Agreement.

The Company pays a commitment fee at an annual rate of 37.5 basis points on the undrawn balance of the 5-Year Revolving Credit Facility at the Company's current Senior Secured credit rating of Ba1 and BB from Moody's Investor Services, Inc. (Moody's) and Standard & Poor's Rating Services (S&P), respectively. This fee amounts to \$3.75 million annually, and is reported as interest expense in the Company's Consolidated Statement of Operations.

In addition to the 5-Year Revolving Credit Facility, the Company has other committed and uncommitted lines of credit at September 30, 2007 totaling \$86 million and \$484 million, respectively. These lines primarily support borrowing needs of the Company's subsidiaries, which include term loans, overdraft coverage, letters of credit and revolving credit lines. Interest rates and other terms of borrowing under these lines of credit vary from country to country, depending on local market conditions. Total outstanding borrowings against these other committed and uncommitted lines of credit at September 30, 2007 were \$10 million and \$24 million, respectively. These outstanding borrowings are reflected in the short-term borrowings in the accompanying Consolidated Statement of Financial Position at September 30, 2007.

At September 30, 2007, the Company had outstanding letters of credit totaling \$143 million and surety bonds in the amount of \$85 million primarily to ensure the payment of possible casualty and workers' compensation claims, environmental liabilities, and to support various customs and trade activities.

#### ***Debt Shelf Registration and Convertible Securities***

On September 5, 2003, the Company filed a shelf registration statement on Form S-3 (the primary debt shelf registration) for the issuance of up to \$2.0 billion of new debt securities. Pursuant to Rule 429 under the Securities Act of 1933, \$650 million of remaining unsold debt securities under a prior shelf registration statement were included in the primary debt shelf registration, thus giving the Company the ability to issue up to \$2.65 billion in public debt. After issuance of \$500 million in notes in October 2003, the remaining availability under the primary debt shelf registration was \$2.15 billion.

The Company has \$575 million aggregate principal amount of Convertible Senior Notes due 2033 (the Convertible Securities) on which interest accrues at the rate of 3.375% per annum and is payable semiannually. The Convertible Securities are unsecured and rank equally with all of the Company's other unsecured and

unsubordinated indebtedness. The Convertible Securities may be converted, at the option of the holders, to shares of the Company's common stock if the Company's Senior Unsecured credit rating assigned to the Convertible Securities by either Moody's or S&P is lower than Ba2 or BB, respectively. At the Company's current Senior Unsecured credit rating, the Convertible Securities may be converted by their holders.

The Company's \$1.0 billion 5-year Committed Revolving Credit Facility, along with other committed and uncommitted credit lines, and cash balances, provide the Company with adequate liquidity to meet its working capital and investing needs.

**Credit Quality**

Moody's and S&P's ratings for the Company, including their outlooks, as of the filing date of this Form 10-Q are as follows:

PAGE 50

	<b>Senior Secured Rating</b>	<b>Corporate Rating</b>	<b>Senior Unsecured Rating</b>	<b>Outlook</b>
Moody's	Ba1	B1	B2	Stable
S&P	BB	B+	B	Negative

On September 11, 2007, Standard & Poor's (S&P) concluded a review on Kodak. The conclusion of this work has resulted in an affirmation of the Company's Corporate Rating at B+, and an unchanged outlook of negative. However, S&P has removed the Company from credit watch, where it had been placed with negative implications on August 2, 2006. The Company's Senior Secured rating has improved two levels to BB.

S&P's ratings reflect their concerns regarding the continued decline in the Company's traditional business, the Company's uncertain profitability and cash flow generation of its digital business, and the potential for additional restructuring charges.

On May 7, 2007, Moody's concluded a review for possible downgrade, which was initiated in May 2006 after the Company announced its intention to explore strategic alternatives for its Health business. As a result, the Company's Corporate and Senior Unsecured ratings were confirmed at B1 and B2, respectively, and the Senior Secured rating, reflecting the remaining 5-Year Revolving Credit Facility, was upgraded from Ba3 to Ba1. The rating outlook was changed from negative to stable.

Moody's ratings reflect their views regarding the Company's significant challenges to replace revenue and cash flow from declining legacy film businesses as well as the Company's market position, operating profit margin and free cash flow volatility, asset returns (net of cash), financial leverage, and liquidity.

The stable rating outlook reflects Moody's expectation that the Company will continue to maintain liquidity and generate earnings sufficient to withstand further secular declines of its legacy film businesses, lack of substantial profitability in certain of its digital businesses and its sizable new business start up costs.

The Company is in compliance with all covenants or other requirements set forth in its credit agreements and indentures. Further, the Company does not have any rating downgrade triggers that would accelerate the maturity dates of its debt. However, the Company could be required to increase the dollar amount of its letters of credit or provide other financial support up to an additional \$71 million at the current credit ratings. As of the filing date of this Form 10-Q, the Company has not been requested to materially increase its letters of credit or other financial support. Downgrades in the Company's credit rating or disruptions in the capital markets could impact borrowing costs and the nature of its funding alternatives.

**Off-Balance Sheet Arrangements**

## Edgar Filing: EASTMAN KODAK CO - Form 10-Q

The Company guarantees debt and other obligations of certain customers. The debt and other obligations are primarily due to banks and leasing companies in connection with financing of customers' purchases of product and equipment from the Company. At September 30, 2007, the following customer guarantees were in place:

(dollars in millions)	As of September 30, 2007	
	Maximum Amount	Amount Outstanding
Customer amounts due to banks and leasing companies	\$ 151	\$ 110
Other third-parties	2	□
Total guarantees of customer debt and other obligations	\$ 153	\$ 110

PAGE 51

The guarantees for the third party debt mature between 2007 and 2011. The customer financing agreements and related guarantees typically have a term of 90 days for product and short-term equipment financing arrangements, and up to five years for long-term equipment financing arrangements. These guarantees would require payment from the Company only in the event of default on payment by the respective debtor. In some cases, particularly for guarantees related to equipment financing, the Company has collateral or recourse provisions to recover and sell the equipment to reduce any losses that might be incurred in connection with the guarantees.

Management believes the likelihood is remote that material payments will be required under any of the guarantees disclosed above. With respect to the guarantees that the Company issued in the quarter ended September 30, 2007, the Company assessed the fair value of its obligation to stand ready to perform under these guarantees by considering the likelihood of occurrence of the specified triggering events or conditions requiring performance as well as other assumptions and factors.

The Company also guarantees debt owed to banks and other third parties for some of its consolidated subsidiaries. The maximum amount guaranteed is \$666 million, and the outstanding debt under those guarantees, which is recorded within the short-term borrowings and long-term debt, net of current portion components in the accompanying Consolidated Statement of Financial Position, is \$239 million. These guarantees expire in 2007 through 2013. Pursuant to the terms of the Company's \$2.7 billion Senior Secured Credit Agreement dated October 18, 2005, obligations under the \$2.7 billion Secured Credit Facilities and other obligations of the Company and its subsidiaries to the \$2.7 billion Secured Credit Facilities lenders are guaranteed.

The Company issues indemnifications in certain instances when it sells businesses and real estate, and in the ordinary course of business with its customers, suppliers, service providers and business partners. Further, the Company indemnifies its directors and officers who are, or were, serving at the Company's request in such capacities. Historically, costs incurred to settle claims related to these indemnifications have not been material to the Company's financial position, results of operations or cash flows. Additionally, the fair value of the indemnifications that the Company issued during the quarter ended September 30, 2007 was not material to the Company's financial position, results of operations or cash flows.

### **Other**

As of September 30, 2007, there has been no material change in the Company's environmental liability exposure and, therefore, no material change in the undiscounted accrued liabilities for environmental remediation costs relative to December 31, 2006 or September 30, 2006.

### **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 (year ending December 31, 2007 for the Company). 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, classification of interest and penalties, and disclosure. The adoption of FIN 48 in the first quarter of 2007 did not have a material impact on the Company's Consolidated Financial Statements. Further information regarding the adoption of FIN 48 is disclosed in Note 6, "Income Taxes."

PAGE 52

**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 expects to adopt SFAS No. 159 in the first quarter of 2008.

**CAUTIONARY STATEMENT PURSUANT TO SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995**

Certain statements in this report may be forward-looking in nature, or "forward-looking statements" as defined in the United States Private Securities Litigation Reform Act of 1995. For example, references to the Company's expectations for cash flow, taxes, receivables, guarantees, results of litigation, environmental remediation costs, employment reductions, cost of postretirement benefits, and restructuring costs, charges and savings are forward-looking statements.

Actual results may differ from those expressed or implied in forward-looking statements. In addition, any forward-looking statements represent the Company's estimates only as of the date they are made, and should not be relied upon as representing the Company's estimates as of any subsequent date. While the Company may elect to update forward-looking statements at some point in the future, the Company specifically disclaims any obligation to do so, even if its estimates change. The forward-looking statements contained in this report are subject to a number of factors and uncertainties, including the successful:

- execution of the digital growth and profitability strategies, business model and cash plan;
- implementation of the cost reduction programs;
- transition of certain financial processes and administrative functions to a global shared services model and the outsourcing of certain functions to third parties;

## Edgar Filing: EASTMAN KODAK CO - Form 10-Q

- implementation of, and performance under, the debt management program, including compliance with the Company's debt covenants;
- development and implementation of product go-to-market and e-commerce strategies;
- protection, enforcement and defense of the Company's intellectual property, including defense of its products against the intellectual property challenges of others;
- execution of intellectual property licensing programs and other strategies;
- integration of the Company's businesses to SAP, the Company's enterprise system software;
- completion of various portfolio actions;
- reduction of inventories;
- integration of acquired businesses and consolidation of the Company's subsidiary structure;
- improvement in manufacturing productivity and techniques;
- improvement in working capital management and cash conversion cycle;
- continued availability of essential components and services from concentrated sources of supply;
- improvement in supply chain efficiency and dependability; and
- implementation of the strategies designed to address the decline in the Company's traditional businesses.

PAGE 53

The forward-looking statements contained in this report are subject to the following additional risk factors:

- inherent unpredictability of currency fluctuations, commodity prices and raw material costs;
- competitive actions, including pricing;
- the Company's ability to access capital markets;
- the nature and pace of technology evolution;
- changes to accounting rules and tax laws, as well as other factors which could impact the Company's reported financial position or effective tax rate;
- pension and other postretirement benefit cost factors such as actuarial assumptions, market performance, and employee retirement decisions;
- general economic, business, geo-political and regulatory conditions or unanticipated environmental liabilities or costs;
- changes in market growth;
- continued effectiveness of internal controls; and
- other factors and uncertainties disclosed from time to time in the Company's filings with the Securities and Exchange Commission.

Any forward-looking statements in this report should be evaluated in light of these important factors and uncertainties.

### **Item 3. Quantitative And Qualitative Disclosures About Market Risk**

The Company, as a result of its global operating and financing activities, is exposed to changes in foreign currency exchange rates, commodity prices, and interest rates, which may adversely affect its results of operations and financial position. In seeking to minimize the risks associated with such activities, the Company may enter into derivative contracts.

Foreign currency forward contracts are used to hedge existing foreign currency denominated assets and liabilities, especially those of the Company's International Treasury Center, and may be used to hedge foreign currency denominated intercompany sales. Silver forward contracts are used to mitigate the Company's risk to fluctuating silver prices.

The Company's exposure to changes in interest rates results from its investing and borrowing activities used to meet its liquidity needs. Long-term debt is generally used to finance long-term investments, while short-term debt is used to meet working capital requirements. The Company does not utilize financial instruments for trading or other speculative purposes.

Using a sensitivity analysis based on estimated fair value of open foreign currency forward contracts using available forward rates, if the U.S. dollar had been 10% stronger at September 30, 2007 and 2006, the fair value of open forward contracts would have decreased \$59 million and increased \$22 million, respectively. Such gains or losses would be substantially offset by losses or gains from the revaluation or settlement of the underlying positions hedged.

Using a sensitivity analysis based on estimated fair value of open silver forward contracts using available forward prices, if available forward silver prices had been 10% lower at September 30, 2007, the fair value of open forward contracts would have decreased \$5 million. Such losses in fair value, if realized, would be offset by lower costs of manufacturing silver-containing products. There were no open forward contracts hedging silver at September 30, 2006.

The Company is exposed to interest rate risk primarily through its borrowing activities and, to a lesser extent, through investments in marketable securities. The Company may utilize borrowings to fund its working capital and investment needs. The majority of short-term and long-term borrowings are in fixed-rate instruments. There is inherent roll-over risk for borrowings and marketable securities as they mature and are renewed at current market rates. The extent of this risk is not predictable because of the variability of future interest rates and business financing requirements.

PAGE 54

Using a sensitivity analysis based on estimated fair value of short-term and long-term borrowings, if available market interest rates had been 10% (about 57 basis points) higher at September 30, 2007, the fair value of short-term and long-term borrowings would have decreased \$1 million and \$55 million, respectively. Using a sensitivity analysis based on estimated fair value of short-term and long-term borrowings, if available market interest rates had been 10% (about 68 basis points) higher at September 30, 2006, the fair value of short-term and long-term borrowings would have decreased less than \$1 million and \$63 million, respectively.

The Company's financial instrument counterparties are high-quality investment or commercial banks with significant experience with such instruments. The Company manages exposure to counterparty credit risk by requiring specific minimum credit standards and diversification of counterparties. The Company has procedures to monitor the credit exposure amounts. The maximum credit exposure at September 30, 2007 was not significant to the Company.

#### **Item 4. Controls and Procedures**

##### **Evaluation of Disclosure Controls and Procedures**

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. The Company's management, with participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness

of the Company's disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. The Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) were effective.

### **Changes in Internal Control over Financial Reporting**

There have been no changes in the Company's internal control over financial reporting during the most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **Part II. Other Information**

### **Item 1. Legal Proceedings**

During March 2005, the Company was contacted by members of the Division of Enforcement of the SEC concerning the announced restatement of the Company's financial statements for the full year and quarters of 2003 and the first three unaudited quarters of 2004. An informal inquiry by the staff of the SEC into the substance of that restatement is continuing. The Company continues to fully cooperate with this inquiry, and the staff has indicated that the inquiry should not be construed as an indication by the SEC or its staff that any violations of law have occurred.

The Company is one of several Potentially Responsible Parties named in connection with the closure of the LWD, Inc. site; a former permitted hazardous waste treatment facility in Calvert City, Kentucky. The Company has entered into a Consent Order with the EPA based upon evidence that the Company sent waste to the facility for incineration. The Company's expected cost in connection with this matter is estimated to be \$150,000, of which the Company has paid \$87,200.

### **Item 6. Exhibits**

(a) Exhibits required as part of this report are listed in the index appearing on page 56.

PAGE 55

## **SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**EASTMAN KODAK COMPANY**

(Registrant)

Date: November 1, 2007

/s/ Diane E. Wilfong

**Diane E. Wilfong**

**Chief Accounting Officer and Controller**

PAGE 56

**Eastman Kodak Company and Subsidiary Companies  
Index to Exhibits**

**Exhibit**

## Edgar Filing: EASTMAN KODAK CO - Form 10-Q

### Number

- (10) F. Eastman Kodak Company 2005 Omnibus Long-Term Compensation Plan, effective January 1, 2005.  
(Incorporated by reference to the Eastman Kodak Company Current Report on Form 8-K, filed on May 11, 2005.)
- Form of Notice of Award of Non-Qualified Stock Options pursuant to the 2005 Omnibus Long-Term Compensation Plan.  
(Incorporated by reference to the Eastman Kodak Company Current Report on Form 8-K, filed on May 11, 2005.)
- Form of Notice of Award of Restricted Stock, pursuant to the 2005 Omnibus Long-Term Compensation Plan.  
(Incorporated by reference to the Eastman Kodak Company Current Report on Form 8-K, filed on May 11, 2005.)
- Form of Notice of Award of Restricted Stock with a Deferral Feature, pursuant to the 2005 Omnibus Long-Term Compensation Plan.  
(Incorporated by reference to the Eastman Kodak Company Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005, Exhibit 10.)
- Form of Administrative Guide for Annual Officer Stock Options Grant under the 2005 Omnibus Long-Term Compensation Plan.  
(Incorporated by reference to the Eastman Kodak Company Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2005, Exhibit 10.)
- Form of Award Notice for Annual Director Stock Option Grant under the 2005 Omnibus Long-Term Compensation Plan.  
(Incorporated by reference to the Eastman Kodak Company Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2005, Exhibit 10.)
- Form of Award Notice for Annual Director Restricted Stock Grant under the 2005 Omnibus Long-Term Compensation Plan.  
(Incorporated by reference to the Eastman Kodak Company Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2005, Exhibit 10.)
- Amendment to the Eastman Kodak Company 2005 Omnibus Long-Term Compensation Plan, effective July 17, 2007.
- (12) Statement Re Computation of Ratio of Earnings to Fixed Charges.
- (31.1) Certification.
- (31.2) Certification.
- (32.1) Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- (32.2) Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.