NCR CORP
Form 10-Q
May 12, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2008

Commission File Number 001-00395

NCR CORPORATION

(Exact name of registrant as specified in its charter)

Maryland	**31-0387920**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1700 South Patterson Blvd.

Dayton, Ohio 45479

(Address of principal executive offices) (Zip Code)

Registrant s telephone number, including area code: (937) 445-5000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

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

Number of shares of common stock, $0.01 par value per share, outstanding as of April 30, 2008, was approximately 167.5 million.

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Part I. Financial Information

Item 1. Financial Statements
Condensed Consolidated Statements of Operations (Unaudited)

In millions, except per share amounts

	Three Months Ended March 31	
	2008	2007
Product revenue	$ 603	$ 486
Service revenue	580	506
Total revenue	1,183	992
Cost of products	441	411
Cost of services	483	424
Selling, general and administrative expenses	159	145
Research and development expenses	35	29
Total operating expenses	1,118	1,009
Income (loss) from operations	65	(17)
Interest expense	6	6
Other income, net	(7)	(9)
Income (loss) from continuing operations before income taxes	66	(14)
Income tax expense (benefit)	17	(5)
Income (loss) from continuing operations	49	(9)
(Loss) income from discontinued operations, net of tax	(1)	43
Net income	$ 48	$ 34
Income (loss) per common share from continuing operations		
Basic	$ 0.28	$ (0.05)
Diluted	$ 0.28	$ (0.05)
Net income per common share		
Basic	$ 0.28	$ 0.19
Diluted	$ 0.27	$ 0.19
Weighted average common shares outstanding		
Basic	173.0	179.3

Diluted	175.7	179.3

See Notes to Condensed Consolidated Financial Statements.

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Condensed Consolidated Balance Sheets (Unaudited)

In millions, except per share amounts

	March 31, 2008	December 31, 2007
Assets		
Current assets		
Cash and cash equivalents	$ 851	$ 952
Accounts receivable, net	1,048	1,167
Inventories, net	752	717
Other current assets	260	252
Total current assets	2,911	3,088
Property, plant and equipment, net	309	313
Goodwill	66	64
Prepaid pension cost	831	776
Deferred income taxes	208	210
Other assets	331	329
Total assets	$ 4,656	$ 4,780
Liabilities and stockholders equity		
Current liabilities		
Short-term borrowings	$ 1	$ 1
Accounts payable	481	516
Payroll and benefits liabilities	163	231
Deferred service revenue and customer deposits	432	359
Other current liabilities	380	423
Total current liabilities	1,457	1,530
Long-term debt	308	307
Pension and indemnity plan liabilities	450	433
Postretirement and postemployment benefits liabilities	362	359
Deferred income taxes	53	45
Income tax accruals	179	165
Other liabilities	158	165
Minority interests	22	19
Total liabilities	2,989	3,023
Commitments and contingencies (Note 8)		
Stockholders equity		
Preferred stock: par value $0.01 per share, 100.0 shares authorized, no shares issued and outstanding at March 31, 2008 and December 31, 2007		
Common stock: par value $0.01 per share, 500.0 shares authorized, 169.8 and 178.2 shares issued and outstanding at March 31, 2008 and December 31, 2007, respectively	2	2
Paid-in capital	503	683
Retained earnings	1,656	1,608
Accumulated other comprehensive loss	(494)	(536)

Total stockholders equity		1,667		1,757
Total liabilities and stockholders equity	$	4,656	$	4,780

See Notes to Condensed Consolidated Financial Statements.

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Condensed Consolidated Statements of Cash Flows (Unaudited)

In millions

	Three Months Ended March 31 2008	2007
Operating activities		
Net Income	$ 48	$ 34
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss (income) from discontinued operations	1	(43)
Depreciation and amortization	29	27
Stock-based compensation expense	10	5
Excess tax benefit from stock-based compensation		(2)
Deferred income taxes	7	5
Gains on sale of property, plant and equipment	(17)	(4)
Changes in operating assets and liabilities:		
Receivables	119	67
Inventories	(35)	(37)
Current payables and accrued expenses	(94)	(74)
Deferred service revenue and customer deposits	73	41
Employee severance and pension	(21)	26
Other assets and liabilities	(39)	(2)
Net cash provided by operating activities	81	43
Investing activities		
Expenditures for property, plant and equipment	(17)	(22)
Proceeds from sales of property, plant and equipment	38	11
Additions to capitalized software	(15)	(12)
Net cash provided by (used in) investing activities	6	(23)
Financing activities		
Repurchases of Company common stock	(193)	
Excess tax benefit from stock-based compensation		2
Proceeds from employee stock plans	4	18
Net cash (used in) provided by financing activities	(189)	20
Cash flows from discontinued operations		
Net cash (used in) provided by operating activities	(13)	108
Net cash used in investing activities		(19)
Net cash provided by financing activities		2
Net cash (used in) provided by discontinued operations	(13)	91
Effect of exchange rate changes on cash and cash equivalents	14	2
(Decrease) increase in cash and cash equivalents	(101)	133
Cash and cash equivalents at beginning of period	952	947

Cash and cash equivalents at end of period	$ 851	$ 1,080

See Notes to Condensed Consolidated Financial Statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The accompanying Condensed Consolidated Financial Statements have been prepared by NCR Corporation (NCR, the Company, we or us) without audit pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC) and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments) necessary for a fair statement of the consolidated results of operations, financial position, and cash flows for each period presented. The consolidated results for the interim periods are not necessarily indicative of results to be expected for the full year. These financial statements should be read in conjunction with NCR s Form 10-K for the year ended December 31, 2007.

As a result of the spin-off of Teradata in 2007, the results of operations and cash flows of Teradata have been presented as a discontinued operation for all periods presented in this Form 10-Q. Unless otherwise noted, disclosures herein refer only to continuing operations.

As discussed in Note 10, effective January 1, 2008, NCR reorganized its businesses and the management thereof to a functional geographic model, changing from the previous model of global business units organized by product and service offering. We have reclassified prior period segment information to conform to the current period presentation of our segment information.

Use of Estimates The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and judgments that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the period reported. Actual results could differ from those estimates.

Revenue Recognition NCR s revenue recognition policy is consistent with the requirements of Statement of Position 97-2 (SOP 97-2), *Software Revenue Recognition*, Staff Accounting Bulletin No. 104 (SAB 104), *Revenue Recognition*, Emerging Issues Task Force Issue No. 00-21 (Issue 00-21), *Revenue Arrangements with Multiple Deliverables*, and other applicable revenue recognition guidance and interpretations. The Company records revenue, net of taxes, when it is realized, or realizable, and earned. The Company considers these requirements met when persuasive evidence of an arrangement exists, the products or services have been provided to the customer, the sales price is fixed or determinable, and collectibility is reasonably assured. For product sales, revenue is recognized when the customer has assumed risk of loss of the goods sold and all performance requirements are complete. For service sales, revenue is recognized as the services are provided or ratably over the service period.

NCR frequently enters into multiple-element arrangements with its customers involving hardware, software, professional consulting and maintenance support services. For arrangements involving multiple deliverables, where deliverables include software and non-software products and services, NCR applies the provisions of Issue 00-21 to separate the deliverables and allocate the total arrangement consideration. Each unit of accounting is then accounted for under the applicable revenue recognition guidance.

A majority of NCR s solutions contain software that is more than incidental to the hardware and services. Revenue related to software and software-related elements is recognized in accordance with SOP 97-2. In situations where there is appropriate evidence of fair value for all undelivered elements, but not for delivered elements, the residual method is used to allocate the arrangement s consideration. Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is allocated to the delivered elements and is recognized as revenue. Fair value of software and software-related elements is based on vendor specific objective evidence (VSOE). VSOE of fair value is determined based on the price charged when each element is sold separately.

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NCR s customers may request that certain transactions be on a bill and hold basis. For these transactions, the Company recognizes revenue in accordance with SAB 104. For the quarter ended March 31, 2008, the amount from bill and hold transactions approximated 1% of consolidated revenue.

Warranty and Sales Returns Provisions for product warranties and sales returns and allowances are recorded in the period in which the related revenue is recognized. The Company accrues warranty reserves and sales returns and allowances using percentages of revenue to reflect the Company s historical average warranty and sales return claims.

In addition to the standard product warranty, the Company periodically offers extended warranties to its customers in the form of product maintenance services. For contracts that are not separately priced but include product maintenance, the Company defers revenue at an amount equal to its objective and reliable fair value (VSOE for transactions subject to the provisions of SOP 97-2) of the product maintenance and recognizes the deferred revenue over the service term. For separately priced product maintenance contracts, not subject to the provisions of SOP 97-2, NCR applies the provisions of FASB Technical Bulletin No. 90-1, *Accounting for Separately Priced Extended Warranty and Product Maintenance Contracts* (FTB 90-1). In conformity with FTB 90-1, NCR defers the stated amount of the separately priced contract and recognizes the deferred revenue ratably over the service term.

2. SUPPLEMENTAL FINANCIAL INFORMATION

In millions	Three Months Ended March 31 2008	Three Months Ended March 31 2007
Comprehensive Income		
Income (loss) from continuing operations	**$ 49**	$ (9)
Other comprehensive (loss) income, net of tax:		
Unrealized loss on securities	**(2)**	(1)
Unrealized loss on derivatives accounted for as hedges		(1)
Amortization of costs associated with pension, postemployment and postretirement benefits	**15**	22
Currency translation adjustments	**29**	5
Total comprehensive income from continuing operations	**91**	16
Total comprehensive (loss) income from discontinued operations	**(1)**	45
Total comprehensive income	**$ 90**	$ 61

Total comprehensive income from discontinued operations for the three months ended March 31, 2007 includes $43 million of income from discontinued operations, net of tax, as well as $2 million of other components of other comprehensive income related to the discontinued operation.

In millions	March 31, 2008	December 31, 2007
Inventories, net		
Work in process and raw materials	**$ 133**	$ 138
Finished goods	**226**	194
Service parts	**393**	385
Total inventories, net	**$ 752**	$ 717

3. NEW ACCOUNTING PRONOUNCEMENTS

Statement of Financial Accounting Standards No. 157 In September 2006, the FASB issued SFAS No. 157 (SFAS 157), *Fair Value Measurements*. This statement defines fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. On February 12, 2008, the FASB issued FASB Staff Position No. FAS 157-2 (FSP 157-2), which delays the effective date of SFAS 157 for nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Where the measurement objective specifically requires the use of fair value, the Company adopted the provisions of SFAS 157 related to financial assets and liabilities as well as those nonfinancial assets and liabilities with recurring fair value measurements, on January 1, 2008. See Note 11, Fair Value of Assets and Liabilities, for further discussion of the adoption of SFAS 157. The Company is currently assessing the impact of SFAS 157 related to those nonfinancial assets and liabilities for which the effective date has been delayed until fiscal years beginning after November 15, 2008.

Statement of Financial Accounting Standards No. 159 In February 2007, the FASB issued SFAS No. 159 (SFAS 159), *The Fair Value Option for Financial Assets and Financial Liabilities*. This statement permits entities to choose to measure financial instruments and certain other items at fair value for recognition or disclosure purposes. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company did not elect to measure financial instruments and other items at fair value and therefore, the adoption of SFAS 159 did not have an impact on its Condensed Consolidated Financial Statements.

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Statement of Financial Accounting Standards No. 141 (revised 2007) In December 2007, the FASB issued SFAS No. 141 (revised 2007) (SFAS 141R), *Business Combinations.* SFAS 141R provides revised guidance on how acquirers recognize and measure the consideration transferred, intangible assets acquired, liabilities assumed, noncontrolling interests, and goodwill acquired in a business combination. SFAS 141R also expands required disclosures surrounding the nature and financial effects of business combinations. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The adoption of SFAS 141R is not expected to have a material impact on the Company s financial position, results of operations or liquidity; however, our accounting for all business combinations after adoption will comply with the new standard.

Statement of Financial Accounting Standards No. 160 In December 2007, the FASB issued SFAS No. 160 (SFAS 160), *Noncontrolling Interests in Consolidated Financial Statements, an Amendment to ARB No. 51.* SFAS 160 applies to all entities that have an outstanding noncontrolling interest in one or more subsidiaries or that deconsolidate a subsidiary. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. The adoption of SFAS 160 is not expected to have a material impact on the Company s financial position, results of operations or liquidity.

Statement of Financial Accounting Standards No. 161 In March 2008, the FASB issued SFAS No. 161 (SFAS 161), *Disclosures about Derivative Instruments and Hedging Activities*. The new standard is intended to help investors better understand how derivative instruments and hedging activities affect an entity s financial position, financial performance and cash flows through enhanced disclosure requirements. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The adoption of SFAS 161 is not expected to have a material impact on the Company s financial position, results of operations or liquidity; however, our disclosures after adoption will comply with the new standard.

4. RESTRUCTURING AND REAL ESTATE TRANSACTIONS

In the first quarter of 2007, the Company initiated a manufacturing realignment primarily related to its ATM products, which included outsourcing certain manufacturing activities in the Americas region and shifting other manufacturing activities from high cost to low cost geographies in the Europe, Middle East and Africa as well as the Asia Pacific and Japan regions. As expected, this realignment has improved productivity and freed capital to invest in revenue-generating programs in sales, engineering and market development. As a result of this realignment, in the first quarter of 2007, the Company recorded $46 million for employee severance and other termination benefits. Of the $46 million initially recorded for this realignment, $37 million was recorded as a discrete cost in accordance with Statement of Financial Accounting Standards No. 112 (SFAS 112), *Employers Accounting for Postemployment Benefits,* and the remainder was recorded in accordance with Statement of Financial Accounting Standards No. 146 (SFAS 146), *Accounting for Costs Associated with Exit or Disposal Activities*. As of December 31, 2007, $11 million of the initial reserve for this initiative remained, of which the Company made $8 million in severance payments during the three months ended March 31, 2008. The reserve balance of $3 million is expected to be utilized during the remainder of 2008.

In the third quarter of 2007, NCR commenced a realignment program in Japan, which was primarily focused on its customer services. The realignment program included actions which were designed to improve operating efficiency and to strengthen the Company s competitive position in Japan and has resulted in reductions in employment. As a result of this realignment program, in the third quarter of 2007, the Company recorded $27 million as a discrete cost for employee severance in accordance with SFAS 112. As of December 31, 2007, $7 million of the initial reserve for this initiative remained, which was fully utilized in the three months ended March 31, 2008.

The following table summarizes the remaining reserve for these activities as of December 31, 2007 and the remaining reserve as of March 31, 2008, which is included on the Condensed Consolidated Balance Sheets in other current liabilities. The cash expenditures necessary to satisfy the remaining obligations will be paid during the remainder of 2008.

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In millions	Employee Severance and Other Benefits
Restructuring reserve	
Balance as of December 31, 2007	$ 18
Payments during the three months ended March 31, 2008	(15)
Ending balance as of March 31, 2008	$ 3

During the first quarter of 2008, the Company recognized a $16 million gain in selling, general and administrative expenses in the Condensed Consolidated Statement of Operations from the sale of a manufacturing facility in Canada, which had a net book value of $4 million.

5. IDENTIFIABLE INTANGIBLE ASSETS

NCR s identifiable intangible assets, reported in Other Assets in the Condensed Consolidated Balance Sheets, were specifically identified when acquired, and are deemed to have finite lives. These intangible assets are being amortized over original periods ranging from four to five years. The gross carrying amount and accumulated amortization for NCR s identifiable intangible assets were as follows:

	Original	March 31, 2008		December 31, 2007	
In millions	Amortization Life (in Years)	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Identifiable intangible assets					
Non-compete arrangements	4 - 5	**$ 5**	**$ (3)**	$ 5	$ (3)
Intellectual property	4 - 5	**46**	**(29)**	45	(27)
Total identifiable intangible assets		**$ 51**	**$ (32)**	$ 50	$ (30)

The aggregate amortization expense (actual and estimated) for identifiable intangible assets for the following periods is:

	Three months ended March 31,	For the year ended (estimated)				
In millions	2008	2008	2009	2010	2011	2012
Amortization expense	**$ 2**	$ 9	$ 7	$ 3	$ 1	$ 1

6. STOCK COMPENSATION PLANS

As of March 31, 2008, the Company s primary types of share-based compensation were stock options and restricted stock. The Company recorded stock-based compensation expense for the three months ended March 31 as follows:

In millions	2008	2007
Stock options	**$ 4**	$ 3
Restricted stock	**6**	2
Total stock-based compensation (pre-tax)	**10**	5
Tax benefit	**(3)**	(1)
Total stock-based compensation, net of tax	**$ 7**	$ 4

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Stock-based compensation expense is recognized in the financial statements based upon fair value. Stock-based compensation expense increased compared to the first quarter of 2007, primarily due to expected performance against targets, higher grant activity and the modifications of stock awards for NCR employees in connection with the spin-off of Teradata on September 30, 2007. The modifications resulted in the establishment of new service and performance-based measures for a portion of the awards outstanding at the time of the spin-off. As these adjustments were modifications of awards in accordance with SFAS 123R, the Company compared the fair value of the awards immediately prior to the modification to the fair value immediately after the modification to measure the incremental stock-based compensation cost. These modifications resulted in approximately $2 million of incremental expense for the three months ended March 31, 2008 compared to the three months ended March 31, 2007.

The weighted average fair value of option grants was estimated based on the below weighted average assumptions and was $7.30 for the three months ended March 31, 2008 and $7.82 for the three months ended March 31, 2007.

	Three Months Ended March 31	
	2008	**2007**
Dividend yield		
Risk-free interest rate	**2.55%**	**4.51%**
Expected volatility	**31.8%**	**32.6%**
Expected holding period (years)	**5.1**	**5.0**

Expected volatility incorporates a blend of both historical volatility of the Company s stock over a period equal to the expected term of the options and implied volatility from traded options on the Company s stock, as management believes this is more representative of prospective trends. The Company uses historical data to estimate option exercise and employee termination within the valuation model. The expected holding period represents the period of time that options are expected to be outstanding. The risk-free interest rate for periods within the contractual life of the option is based on the five-year U.S. Treasury yield curve in effect at the time of grant.

7. EMPLOYEE BENEFIT PLANS

Components of net periodic benefit (income) cost of the Company s pension plans for the three months ended March 31 are as follows:

	U.S. Pension Benefits		**International Pension Benefits**		**Total Pension Benefits**	
In millions	**2008**	**2007**	**2008**	**2007**	**2008**	**2007**
Net service cost	$	$	**$ 8**	$ 10	**$ 8**	$ 10
Interest cost	48	46	**27**	22	**75**	68
Expected return on plan assets	(62)	(61)	**(33)**	(31)	**(95)**	(92)
Amortization of:						
Prior service cost			**2**	3	**2**	3
Actuarial loss		1	**16**	21	**16**	22
Net benefit (income) cost	$ (14)	$ (14)	**$ 20**	$ 25	**$ 6**	$ 11

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Of the total net benefit cost presented above for the three months ended March 31, 2007, $2 million was related to discontinued operations.

The net periodic benefit cost of the postretirement plan for the three months ended March 31 was:

	Postretirement Benefits	
In millions	**2008**	**2007**
Interest cost	**$ 2**	$ 2
Amortization of:		
Prior service cost	**(3)**	(3)
Actuarial loss	**1**	1
Net benefit cost	**$**	$

The net periodic benefit cost of the postemployment plan for the three months ended March 31 was:

	Postemployment Benefits	
In millions	**2008**	**2007**
Net service cost	**$ 6**	$ 8
Interest cost	**4**	5
Amortization of:		
Actuarial loss	**3**	6
Net benefit cost	**$ 13**	$ 19
Restructuring severance cost (Note 4)		37
Total postemployment cost	**$ 13**	$ 56

Of the total postemployment cost presented above for the three months ended March 31, 2007, $4 million was related to discontinued operations.

Employer Contributions

Pension For the three months ended March 31, 2008, NCR contributed approximately $15 million to its international pension plans and $2 million to its executive pension plan. NCR anticipates contributing an additional $65 million to its international pension plans in 2008 for a total of $80 million, and an additional $8 million to its executive pension plan in 2008 for a total of $10 million. NCR does not anticipate making cash contributions to its U.S. qualified pension plan in 2008.

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Postretirement For the three months ended March 31, 2008, the Company made $4 million in contributions to its U.S. postretirement plan. NCR anticipates contributing an additional $14 million to its U.S. postretirement plan for a total of $18 million in 2008.

Postemployment For the three months ended March 31, 2008, NCR contributed approximately $19 million to its postemployment plans, of which $15 million was for benefit payments relating to the realignment initiatives described in Note 4. NCR anticipates contributing an additional $41 million to its postemployment plans in 2008 for a total of $60 million.

8. COMMITMENTS AND CONTINGENCIES

In the normal course of business, NCR is subject to various regulations, proceedings, lawsuits, claims and other matters, including actions under laws and regulations related to the environment and health and safety, among others. NCR believes the amounts provided in its Condensed Consolidated Financial Statements, as prescribed by GAAP, are adequate in light of the probable and estimable liabilities. The Company does not currently expect to incur material capital expenditures related to compliance with such laws and regulations. However, there can be no assurances that the actual amounts required to satisfy alleged liabilities from various lawsuits, claims, legal proceedings and other matters, including the Fox River environmental matter discussed below, and to comply with applicable laws and regulations, will not exceed the amounts reflected in NCR s Condensed Consolidated Financial Statements or will not have a material adverse effect on its consolidated results of operations, capital expenditures, competitive position, financial condition or cash flows. Any costs that may be incurred in excess of those amounts provided as of March 31, 2008 cannot currently be reasonably determined.

The United States Department of Justice is conducting an investigation regarding the propriety of the Company s former Teradata Data Warehousing business s arrangements and understandings with others in connection with certain federal contracts. In connection with the spin-off of Teradata on September 30, 2007, the responsibility for this matter, together with the related reserve, was distributed to Teradata Corporation. While the Company may be subject to ostensible exposure inasmuch as it was the contracting party in the matter at issue, Teradata Corporation is generally obligated to indemnify the Company for any losses arising out of this matter.

A separate portion of the government s investigation relates to the adequacy of pricing disclosures made to the government in connection with negotiation of the Company s General Services Administration Federal Supply Schedule and to whether certain subsequent price reductions were properly passed on to the government. Both Teradata Corporation and the Company are participating in this aspect of the investigation, with respect to certain products and services of each, and each will assume financial responsibility for its own exposures, if any, without indemnification from the other. At this time, the Company is unable to determine whether it has probable liability with respect to this aspect of the investigation.

Environmental Matters NCR s facilities and operations are subject to a wide range of environmental protection laws, and NCR has investigatory and remedial activities underway at a number of facilities that it currently owns or operates, or formerly owned or operated, to comply, or to determine compliance, with such laws. Also, NCR has been identified, either by a government agency or by a private party seeking contribution to site clean-up costs, as a potentially responsible party (PRP) at a number of sites pursuant to various state and federal laws, including the Federal Water Pollution Control Act, the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) and comparable state statutes.

NCR is one of eight entities that have been formally notified by governmental and other entities (such as local Native American tribes) that they are PRPs for environmental claims under CERCLA and other statutes arising out of the presence of polychlorinated biphenyls (PCBs) in sediments in the lower Fox River and in the Bay of Green Bay, in Wisconsin. NCR was identified as a PRP because of alleged PCB discharges from two carbonless copy paper manufacturing facilities it previously owned, which are located along the Fox River. Some parties contend that NCR is also responsible for PCB discharges from paper mills owned by other companies because carbonless paper manufactured by NCR was allegedly purchased by those mills as a raw material for their paper making processes. NCR sold the facilities in 1978 to Appleton Papers Inc. (API), which has also been identified as a PRP. The other Fox River PRPs that received notices are P.H. Glatfelter Company, Georgia-Pacific Consumer Products LP (G-P, successor to Fort James Operating Company), WTM I Co. (formerly Wisconsin Tissue Mills, now owned by Chesapeake Corporation), CBC Corporation (formerly Riverside Paper Corporation), U.S. Paper Mills Corp. (owned by Sonoco Products Company), and Menasha Corporation.

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As of March 31, 2008, the reserve for the Fox River matter was approximately $81 million compared to $85 million as of December 31, 2007. The change in the reserve was due primarily to utilizations for clean-up activities and legal fees. NCR regularly re-evaluates the assumptions used in determining the appropriate reserve for the Fox River matter as additional information becomes available and, when warranted, makes appropriate adjustments.

In July 2003, the United States Environmental Protection Agency (USEPA) and Wisconsin Department of Natural Resources (WDNR) issued their final clean-up plan (known as a Record of Decision, or ROD) for the largest portion of the Fox River. The ROD addressed the lower part of the Fox River and portions of Green Bay, where USEPA and WDNR (the Governments) estimate the bulk of the sediments that need to be remediated are located. In two portions of the lower part of the Fox River covered by the ROD Operable Units (OUs) 3 and 4 the Governments selected large-scale dredging as the clean-up approach. In the ROD, the Governments estimated that approximately 6.5 million cubic yards of sediment would be removed from these portions at an estimated cost of approximately $284 million. The Governments also identified capping the river bed with appropriate materials as a contingent remedy to be evaluated during the remedial design process. For Green Bay, or OU 5, the Governments selected monitored natural attenuation as the clean-up approach at an estimated cost of approximately $40 million. Earlier, in January 2003, the Governments had issued their ROD for the upper portions of the Fox River projecting the cost of that work to be approximately $65 million for OU 1 and $10 million for OU 2. Combining the cost estimates from both RODs issued in 2003, the Governments expected the selected remedies for all five OUs to cost approximately $400 million, exclusive of contingencies.

By letter dated September 30, 2003, the Governments notified NCR and the seven other PRPs of their potential liability for remediation of the lower portions of the Fox River and requested that one or more of the PRPs enter into an agreement with the Governments to perform the engineering design work for the clean-up of OUs 2 through 5. In response, in 2004, NCR and G-P entered into an Administrative Order on Consent (AOC) with the Governments to perform this design work, which is not expected to be completed until late 2008 at the earliest. In November 2006, the Governments issued for public comment a proposal to amend the RODs for the lower river. The proposal called for a combination of dredging and capping to remediate the PCB-containing sediments, as opposed to using dredging throughout the lower river.

In April 2006, NCR and U.S. Paper Mills entered into a consent decree with the Governments to undertake a removal action involving an area of elevated PCBs downriver of the De Pere Dam (Phase 1 work). The consent decree was approved in November 2006 by the federal court in Wisconsin, and most of the work was performed during 2007. The remaining work is expected to be completed in 2008. The estimated costs of this project are included in the estimates discussed below. In June 2007, the Governments issued their amendment to the 2003 RODs (Amended ROD), adopting the proposal to use a combination of dredging and capping to remediate the sediments in OUs 2 through 5 (the Amended ROD did not address OU 1). The Amended ROD stated that the cost of this work will be $390 million.

By letter received February 14, 2007, the Governments again notified NCR and the seven other PRPs of their potential liability for remediation and requested that the parties enter into negotiations with the Governments over a consent decree for implementing the remedy for the lower river. In October 2007, certain of the PRPs issued a request for proposals (RFP), seeking bids from contractors for the type of contractual arrangement for the lower river clean-up work consistent with the then ongoing settlement discussions. Initial responses to the RFP were received in mid-December, and subsequent modified responses, reflecting alternative contracting approaches, were received in the first quarter of 2008. Further negotiations with one of the contractors are ongoing and may culminate in the execution of a contract in the second or third quarter of 2008. At the same time, certain PRPs and the Governments are exploring value engineering concepts intended to reduce the costs of the remediation, though these efforts are in their early stages. In light of the cost information obtained through the RFP responses and the subsequent proposal refinement, there can be no assurance that the estimated total clean-up costs for the site, and thus the Company s reserve, will not be significantly higher, but the contractor negotiations must be completed and the referenced value engineering analysis must progress further, before NCR is in a position to determine whether better estimates can be made.

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On November 13, 2007, the Governments issued a unilateral administrative order (Order) under Section 106 of CERCLA to all eight of the PRPs. The Order requires the PRPs to implement the remedial work in the lower river in accordance with the requirements of the Amended ROD. Under the Order, full-scale remediation is to begin in 2009. NCR, API and the other PRPs are working with the Governments to implement certain provisions of the Order.

On January 7, 2008, NCR and API filed a lawsuit in federal court, which is currently pending in Green Bay, Wisconsin, seeking a judicial ruling determining each PRP s allocable responsibility for the cost of performing the remedial work at the Fox River. The suit was initially filed against the George A. Whiting Paper Company, and several defendants, including the Glatfelter and Menasha companies, two of the eight PRPs receiving the Order, have been added to the suit in the following months. As of May 6, 2008, two counterclaims seeking contribution under CERCLA had been filed against NCR and API. Absent settlements, additional parties are likely to be joined to the lawsuit by July 2008, and additional counterclaims may be filed. No trial date or other schedule has been set for this lawsuit.

The extent of NCR s potential liability remains subject to many uncertainties. NCR s eventual liability which is expected to be paid out over a period extending through at least approximately 2019 will depend on a number of factors. In general, the most significant factors include: (1) the total of the clean-up costs for each of the segments of the river; (2) the total natural resource damages for the site; (3) the shares NCR and API will jointly bear of future clean-up costs and natural resource damages as former and current owners of paper manufacturing facilities located along the Fox River; (4) the share NCR will bear of the joint NCR/API payments for such clean-up costs and natural resource damages; and (5) NCR s transaction and litigation costs to defend itself in this matter, including participation in allocation litigation. In establishing the reserve, NCR attempts to estimate a range of reasonably possible outcomes for each of these factors, although each range is itself highly uncertain. NCR uses its best estimate within the range, if that is possible. Where there is a range of equally possible outcomes, and there is no amount within that range that is considered to be a better estimate than any other amount, NCR uses the low end of the range. These factors are discussed below:

For the first factor described above, the total of the clean-up costs for each of the segments of the river, NCR uses a best estimate of $613 million. This $613 million estimate uses the $390 million cost for the lower river work set forth in the Amended ROD and increases it to $403 million to account for the cost of certain work required by the Amended ROD but not included in the Amended ROD s official cost estimate. The total cost also includes estimates for the OU 1 work, the Phase I work and the remedial design work. Finally, it adds to these estimates a 20% contingency for possible cost overruns and future Government oversight costs, and an amount for Government past costs. The range of reasonably possible outcomes is estimated to be between $537 million (assuming no cost-overrun contingency) and $664 million (assuming a 30% contingency). However, there can be no assurances that these amounts will not be significantly higher. The cost information obtained through the RFP responses, and the subsequent proposal refinement and negotiations, suggest these amounts may increase but the contractor negotiations must be completed and the referenced value engineering analysis must progress further, before NCR is in a position to determine whether better estimates can be made.

Second, for total natural resource damages (NRD), NCR uses a best estimate of $76 million. Previously, NCR used a best estimate of $131 million. This reduction is based on new information NCR recently obtained. NCR believes the range of reasonably possible outcomes for NRD, if it were to be litigated, is between zero and $176 million.

Third, for the NCR/API shares of future clean-up costs, NCR has determined that there are ranges of equally possible outcomes for the different segments of the river, and that no estimates within these ranges are better than the other estimates. Accordingly, NCR uses the low ends of the ranges, which are based primarily on the proximity of the areas to be remediated to the locations at which PCBs from the NCR/API plants were discharged to the river. The extensive data that has been collected over the last few years, along with various recent analyses of this data, have allowed NCR to move away from its prior discharge analysis and use this proximity approach. There are other estimates that are significantly higher; however, NCR believes there is such uncertainty surrounding these estimates that it cannot quantify the high end of the range, although NCR does not believe the joint NCR/API percentage of direct discharges is near 100%. As for the NCR/API share of NRD, which is discussed above, NCR uses a best estimate.

Fourth, for the NCR share of the joint NCR/API payments, NCR uses 45 percent for the first $75 million in total costs attributable to the joint NCR/API share, and uses 40 percent for costs in excess of $75 million. These percentages are set by an agreement between NCR and API and an arbitration award. NCR s analysis of this factor assumes that API is able to pay its share of the NCR/API joint share.

Finally, NCR estimated the transaction costs it is likely to incur to defend this matter through 2019, the time period NCR s engineering consultants believe it will take to complete the design work and implement the remedy for the river. This estimate is based on an analysis of NCR s costs since this matter first arose in 1995 and estimates of what NCR s defense and transaction costs will be in the future. NCR expects that the bulk of these transaction costs will be incurred in the earlier years of this time period, when the design work is completed and the initial clean-up activities begin. NCR believes that once clean-up is underway, its transaction costs will decrease on an annual basis.

In light of the ongoing remedial design work being conducted by NCR and G-P, the ongoing settlement discussions (including the prospects not only of group settlements but also of individual settlements for some corporate or municipal entities), the efforts to implement the Government Order for clean-up of the lower river, the advent of the allocation litigation referenced above, the initial bids received in response to the RFP, the subsequent value engineering efforts designed to render the clean-up more efficient and less costly, efforts by NCR and API to identify other parties with potential responsibility for the clean-up (some of which have had little or no involvement with the site activities and Government discussions of recent years), and ongoing negotiations with contractors about the cost of implementing the work required under the Order, calculation of the reserve has become subject to added layers of complexities, and it is possible there could be additional changes to some elements of the reserve over the upcoming periods, although we are unable to predict or estimate such changes at this time. However, there can be no assurance that the clean-up and related expenditures will not have a material effect on NCR s capital expenditures, earnings and competitive position.

AT&T and Alcatel-Lucent are jointly responsible for indemnifying NCR for a portion of the amounts incurred by NCR for the Fox River matter over a certain threshold. NCR s estimate of what AT&T and Alcatel-Lucent will pay under the indemnity is recorded as a long-term receivable of approximately $30 million as of March 31, 2008, and is deducted in determining the net reserve discussed above.

In addition, NCR previously reached settlement agreements with certain of its principal insurance carriers in a combined total of approximately $29 million. Of this amount, $9 million is subject to competing claims by another party, and NCR and the other party have agreed that these funds will be used for Fox River costs and will be shared on an agreed upon basis (subject to reallocation at a later date). NCR s agreed upon share of the $9 million is estimated to be $4 million.

It is difficult to estimate the future financial impact of environmental laws, including potential liabilities. NCR records environmental provisions when it is probable that a liability has been incurred and the amount or range of the liability is reasonably estimable. Provisions for estimated losses from environmental restoration and remediation are, depending on the site, based primarily on internal and third-party environmental studies (except for the Fox River site, where the estimated clean-up costs and natural resource damages are estimated as described above), estimates as to the number and participation level of any other PRPs, the extent of the contamination, and the nature of required clean-up and restoration actions. Reserves are adjusted as further information develops or circumstances change. Management expects that the amounts reserved from time to time will be paid out over the

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period of investigation, negotiation, remediation and restoration for the applicable sites. The amounts provided for environmental matters in NCR s Condensed Consolidated Financial Statements are the estimated gross undiscounted amounts of such liabilities, without deductions for insurance or third-party indemnity claims, except as qualified in the following sentences. Except for the sharing agreement with API described above with respect to the Fox River site, in those cases where insurance carriers or third-party indemnitors have agreed to pay any amounts and management believes that collectibility of such amounts is probable, the amounts are reflected as receivables in the Condensed Consolidated Financial Statements. For the Fox River site, a receivable relating to the AT&T and Alcatel-Lucent indemnity is recorded as of March 31, 2008, because payment is considered probable and is supported by contractual agreements.

Guarantees and Product Warranties Guarantees associated with NCR s business activities are reviewed for appropriateness and impact to the Company s financial statements.

NCR provides its customers a standard manufacturer s warranty and records, at the time of the sale, a corresponding estimated liability for potential warranty costs. Estimated future obligations due to warranty claims are based upon historical factors such as labor rates, average repair time, travel time, number of service calls per machine and cost of replacement parts. When a sale is consummated, the total customer revenue is recognized and the associated warranty liability is recorded using pre-established warranty percentages for the respective product classes. From time to time, product design or quality corrections are accomplished through modification programs. When identified, associated costs of labor and parts for such programs are estimated and accrued as part of the warranty reserve.

The Company recorded the activity related to the warranty reserve for the three months ended March 31 as follows:

In millions	**2008**	**2007**
Warranty reserve		
Beginning balance as of January 1	**$ 13**	$ 13
Accruals for warranties issued	**12**	6
Settlements (in cash or in kind)	**(12)**	(10)
Ending balance as of March 31	**$ 13**	$ 9

The accruals for warranties issued increased for the three months ended March 31, 2008 compared to the three months ended March 31, 2007 due to higher product revenue and the increase of the standard warranty period for some products in certain geographies. NCR also periodically offers extended warranties in the form of product maintenance services to its customers. Refer to Warranty and Sales Returns under Note 1, Basis of Presentation, for further description of the Company s accounting policy for extended warranties. Amounts associated with these extended warranties are not included in the table above.

In addition, NCR provides its customers with certain indemnification rights. In general, NCR agrees to indemnify the customer if a third party asserts patent or other infringement on the part of the customer for its use of the Company s products. From time to time, NCR also enters into agreements in connection with its acquisition and divestiture activities that include indemnification obligations by the Company. The fair value of these indemnification obligations is not readily determinable due to the conditional nature of the Company s potential obligations and the specific facts and circumstances involved with each particular agreement. The Company has not recorded a liability in connection with these indemnifications. Historically, payments made by the Company under these types of agreements have not had a material effect on the Company s condensed consolidated financial condition, results of operations or cash flows.

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9. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing net income by the weighted average number of shares outstanding during the reported period. The calculation of diluted earnings per share is similar to basic earnings per share, except that the weighted average number of shares outstanding includes the dilution from potential shares added from stock options and unvested restricted stock awards.

The components of basic and diluted earnings per share are as follows:

In millions, except per share amounts	Three Months Ended March 31 2008	2007
Income (loss) from continuing operations	**$ 49**	$ (9)
(Loss) income from discontinued operations	**(1)**	43
Net Income applicable to common shares	**48**	34
Weighted average outstanding shares of common stock	**173.0**	179.3
Dilutive effect of employee stock options and restricted stock	**2.7**	*
Common stock and common stock equivalents	**175.7**	179.3
Basic earnings (loss) per share:		
From continuing operations	**$ 0.28**	$ (0.05)
From discontinued operations	**$**	$ 0.24
Net earnings per share (Basic)	**$ 0.28**	$ 0.19
Diluted earnings (loss) per share:		
From continuing operations	**$ 0.28**	$ (0.05)
From discontinued operations	**$ (0.01)**	$ 0.24