

DELPHI CORP
Form 10-Q
May 09, 2008

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**UNITED STATES
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 March 31, 2008

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: 1-14787

DELPHI CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

38-3430473

(I.R.S. Employer
Identification No.)

5725 Delphi Drive, Troy, Michigan
(Address of principal executive offices)

48098
(Zip Code)

(248) 813-2000

(Registrant's telephone number, including area code)

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 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 definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-Accelerated filer Smaller reporting company .

(Do not check if a 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 .

As of March 31, 2008 there were 564,176,022 outstanding shares of the registrant's \$0.01 par value common stock.

WEBSITE ACCESS TO COMPANY S REPORTS

Delphi s internet website address is www.delphi.com. Our Annual Reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to section 13(a) or 15(d) of the Exchange Act are available free of charge through our website as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission.

DELPHI CORPORATION

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(DEBTOR-IN-POSSESSION)****CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)**

	Three Months Ended March 31,	
	2008	2007
	(in millions, except per share amounts)	
Net sales:		
General Motors and affiliates	\$ 1,641	\$ 2,163
Other customers	3,611	3,519
Total net sales	5,252	5,682
Operating expenses:		
Cost of sales, excluding items listed below	4,897	5,306
U.S. employee workforce transition program charges (credit)	36	(6)
Depreciation and amortization	222	233
Selling, general and administrative	364	364
Total operating expenses	5,519	5,897
Operating loss	(267)	(215)
Interest expense (contractual interest expense for the three months ended March 31, 2008 and 2007 was \$129 million and \$124 million, respectively)	(110)	(90)
Loss on extinguishment of debt		(23)
Other income, net	19	20
Reorganization items	(109)	(39)
Loss from continuing operations before income taxes, minority interest and equity income	(467)	(347)
Income tax expense	(63)	(46)
Loss from continuing operations before minority interest and equity income	(530)	(393)
Minority interest, net of tax	(11)	(12)
Equity income, net of tax	11	14
Loss from continuing operations	(530)	(391)
Loss from discontinued operations, net of tax	(59)	(142)

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Net loss	\$	(589)	\$	(533)
Basic and diluted loss per share:				
Continuing operations	\$	(0.94)	\$	(0.70)
Discontinued operations		(0.10)		(0.25)
Basic and diluted loss per share	\$	(1.04)	\$	(0.95)

See notes to consolidated financial statements.

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**DELPHI CORPORATION
(DEBTOR-IN-POSSESSION)**

CONSOLIDATED BALANCE SHEETS

	March 31, 2008 (Unaudited)	December 31, 2007
	(in millions)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 1,310	\$ 1,036
Restricted cash	175	173
Accounts receivable, net:		
General Motors and affiliates	1,226	1,257
Other	2,991	2,637
Inventories, net:		
Productive material, work-in-process and supplies	1,341	1,312
Finished goods	503	496
Other current assets	592	588
Assets held for sale (Note 4)	655	720
Total current assets	8,793	8,219
Long-term assets:		
Property, net	3,820	3,863
Investments in affiliates	387	387
Goodwill	406	397
Other	798	801
Total long-term assets	5,411	5,448
Total assets	\$ 14,204	\$ 13,667
LIABILITIES AND STOCKHOLDERS DEFICIT		
Current liabilities:		
Short-term debt (Note 11)	\$ 4,212	\$ 3,495
Accounts payable	2,960	2,904
Accrued liabilities (Note 8)	2,401	2,281
Liabilities held for sale (Note 4)	426	412
Total current liabilities	9,999	9,092
Long-Term liabilities:		
Other long-term debt (Note 11)	62	59
Employee benefit plan obligations (Note 13)	475	443
Other (Note 8)	1,201	1,185
Total long-term liabilities	1,738	1,687

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Liabilities subject to compromise (Note 10)	16,363	16,197
Total liabilities	28,100	26,976
Commitments and contingencies (Note 18)		
Minority interest	164	163
Stockholders' deficit:		
Common stock, \$0.01 par value, 1,350 million shares authorized, 565 million shares issued in 2008 and 2007	6	6
Additional paid-in capital	2,748	2,756
Accumulated deficit	(15,690)	(14,976)
Accumulated other comprehensive loss:		
Employee benefit plans (Note 13)	(1,721)	(1,679)
Other	611	446
Total accumulated other comprehensive loss	(1,110)	(1,233)
Treasury stock, at cost (850 thousand and 1.5 million shares in 2008 and 2007, respectively)	(14)	(25)
Total stockholders' deficit	(14,060)	(13,472)
Total liabilities and stockholders' deficit	\$ 14,204	\$ 13,667

See notes to consolidated financial statements.

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**DELPHI CORPORATION
(DEBTOR-IN-POSSESSION)**

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Three Months Ended	
	March 31,	
	2008	2007
	(in millions)	
Cash flows from operating activities:		
Net loss	\$ (589)	\$ (533)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	222	233
Deferred income taxes	(4)	3
Pension and other postretirement benefit expenses	185	249
Equity income	(11)	(14)
Reorganization items	109	39
U.S. employee workforce transition program charges (credit)	36	(6)
Loss on extinguishment of debt		23
Loss on assets held for sale	30	
Changes in operating assets and liabilities:		
Accounts receivable, net	(395)	(574)
Inventories, net	(50)	(3)
Other assets	18	(55)
Accounts payable	176	304
Accrued and other long-term liabilities	108	131
Other, net	37	(21)
U.S. employee workforce transition program payments	(71)	(481)
U.S. employee workforce transition program reimbursement by GM		264
Pension contributions	(68)	(92)
Other postretirement benefit payments	(66)	(40)
Net payments for reorganization items	(16)	(30)
Dividends from equity investments	5	
Discontinued operations (Note 4)	54	189
Net cash used in operating activities	(290)	(414)
Cash flows from investing activities:		
Capital expenditures	(255)	(178)
Proceeds from sale of property	21	10
Proceeds from sale of non-U.S. trade bank notes	62	36
Proceeds from divestitures, net	87	
Increase in restricted cash	(2)	
Other, net	3	(10)
Discontinued operations	(70)	(14)
Net cash used in investing activities	(154)	(156)

Cash flows from financing activities:		
Proceeds from refinanced debtor-in-possession facility, net of issuance cost		2,739
Repayments of borrowings under debtor-in-possession facility		(250)
Repayments of borrowings under prepetition term loan facility		(988)
Repayments of borrowings under prepetition revolving credit facility		(1,508)
Net borrowings under refinanced debtor-in-possession facility	452	327
Net borrowings under other debt agreements	210	62
Dividend payments of consolidated affiliates to minority shareholders	(7)	(7)
Discontinued operations	11	
Net cash provided by financing activities	666	375
Effect of exchange rate fluctuations on cash and cash equivalents	52	12
Increase (decrease) in cash and cash equivalents	274	(183)
Cash and cash equivalents at beginning of period	1,036	1,608
Cash and cash equivalents at end of period	\$ 1,310	\$ 1,425

See notes to consolidated financial statements.

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**DELPHI CORPORATION
(DEBTOR-IN-POSSESSION)**

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS (Unaudited)

	Three Months Ended March 31,	
	2008	2007
	(in millions)	
Net loss	\$ (589)	\$ (533)
Other comprehensive income:		
Currency translation adjustments, net of tax	69	26
Net change in unrecognized gain on derivative instruments, net of tax	96	3
Employee benefit plans adjustment, net of tax	(30)	
Other comprehensive income	135	29
Comprehensive loss	\$ (454)	\$ (504)

See notes to consolidated financial statements.

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**DELPHI CORPORATION
(DEBTOR-IN-POSSESSION)**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. BASIS OF PRESENTATION

General Delphi Corporation, together with its subsidiaries and affiliates (Delphi or the Company), is a supplier of vehicle electronics, transportation components, integrated systems and modules, and other electronic technology. Delphi's most significant customer is General Motors Corporation (GM) and North America and Europe are its most significant markets. Delphi is continuing to diversify its customer base and geographic markets. The consolidated financial statements and notes thereto included in this report should be read in conjunction with Delphi's consolidated financial statements and notes thereto included in Delphi's Annual Report on Form 10-K for the year ended December 31, 2007 filed with the United States (U.S.) Securities and Exchange Commission (SEC).

Consolidation The consolidated financial statements include the accounts of Delphi and domestic and non-U.S. subsidiaries in which Delphi holds a controlling financial or management interest and variable interest entities of which Delphi has determined that it is the primary beneficiary. Delphi's share of the earnings or losses of non-controlled affiliates, over which Delphi exercises significant influence (generally a 20% to 50% ownership interest), is included in the consolidated operating results using the equity method of accounting. All significant intercompany transactions and balances between consolidated Delphi businesses have been eliminated. All adjustments, consisting of only normal recurring items, which are necessary for a fair presentation, have been included. The results for interim periods are not necessarily indicative of results that may be expected from any other interim period or for the full year and may not necessarily reflect the consolidated results of operations, financial position and cash flows of Delphi in the future.

Bankruptcy Filing On October 8, 2005 (the Petition Date), Delphi and certain of its U.S. subsidiaries (the Initial Filers) filed voluntary petitions for reorganization relief under chapter 11 of the United States Bankruptcy Code (the Bankruptcy Code) in the United States Bankruptcy Court for the Southern District of New York (the Court), and on October 14, 2005, three additional U.S. subsidiaries of Delphi (together with the Initial Filers, collectively, the Debtors) filed voluntary petitions for reorganization relief under chapter 11 of the Bankruptcy Code (collectively the Debtors October 8, 2005 and October 14, 2005 filings are referred to herein as the Chapter 11 Filings). The reorganization cases are being jointly administered under the caption In re Delphi Corporation, et al., Case No. 05-44481 (RDD). The Debtors will continue to operate their businesses as debtors-in-possession under the jurisdiction of the Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Court. Delphi's non-U.S. subsidiaries were not included in the filings, will continue their business operations without supervision from the U.S. Courts and are not subject to the requirements of the Bankruptcy Code.

American Institute of Certified Public Accountants Statement of Position 90-7, *Financial Reporting by Entities in Reorganization under the Bankruptcy Code* (SOP 90-7), which is applicable to companies in chapter 11 of the Bankruptcy Code, generally does not change the manner in which financial statements are prepared. However, it does require, among other disclosures, that the financial statements for periods subsequent to the filing of the chapter 11 petition distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Revenues, expenses, realized gains and losses, and provisions for losses that can be directly associated with the reorganization and restructuring of the business must be reported separately as reorganization items in the statements of operations. The balance sheet must distinguish prepetition liabilities subject to compromise from both those prepetition liabilities that are not subject to compromise and from postpetition liabilities. Liabilities that may be affected by a plan of reorganization must be reported at the amounts expected to be allowed, even if they may be settled for lesser amounts. In addition, reorganization items must be disclosed separately in the statement of

cash flows. Delphi has segregated those items as outlined above for all reporting periods subsequent to October 8, 2005.

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Going Concern The Debtors are operating pursuant to chapter 11 of the Bankruptcy Code and continuation of the Company as a going concern is contingent upon, among other things, the Debtors' ability (i) to comply with the terms and conditions of their debtor-in-possession ("DIP") financing agreement; (ii) to reduce wage and benefit costs and liabilities during the bankruptcy process; (iii) to return to profitability; (iv) to generate sufficient cash flow from operations; and (v) to obtain financing sources to meet the Company's future obligations. These matters create substantial uncertainty relating to the Company's ability to continue as a going concern. The accompanying consolidated financial statements do not reflect any adjustments relating to the recoverability of assets and classification of liabilities that might result from the outcome of these uncertainties. In addition, the Company filed its proposed plan of reorganization with the Court in September 2007. The Court confirmed Delphi's plan of reorganization, as amended, on January 25, 2008; however, Delphi has not yet consummated its confirmed plan of reorganization and is continuing to work with its stakeholders to further amend the plan. Depending on the extent and nature of any further proposed amendments, the plan of reorganization may not be consummated necessitating Delphi and certain of its U.S. subsidiaries to continue as debtors-in-possession in chapter 11 longer than initially anticipated. Consummation of a confirmed plan of reorganization often materially changes the amounts reported in a company's consolidated financial statements, which do not give effect to any adjustments to the carrying value of assets or amounts of liabilities that might be necessary as a consequence of consummation of a confirmed plan of reorganization.

Contractual Interest Expense and Interest Expense on Unsecured Claims Contractual interest expense represents amounts due under the contractual terms of outstanding debt, including debt subject to compromise for which interest expense is not recognized in accordance with the provisions of SOP 90-7. Delphi did not record contractual interest expense on certain unsecured prepetition debt during the quarter ended March 31, 2007. In September 2007, Delphi began recording prior contractual interest expense related to certain prepetition debt because it became probable that the interest would become an allowed claim based on the provisions of the plan of reorganization filed with the Court in September 2007. The plan of reorganization also provides that certain holders of allowed unsecured claims against Delphi will be paid postpetition interest on their claims, calculated at the contractual non-default rate from the petition date through January 25, 2008. Delphi recorded interest related to prepetition debt and allowed unsecured claims of \$14 million during the quarter ended March 31, 2008. This interest expense was calculated through January 25, 2008, the confirmation date of the plan of reorganization. This estimate is based on numerous factual and legal assumptions. At March 31, 2008, Delphi had accrued interest of \$425 million in accrued liabilities in the accompanying balance sheet for prepetition claims. Upon consummation of the confirmed plan of reorganization discussed in Note 2. Transformation Plan and Chapter 11 Bankruptcy, the interest accrued for prepetition claims will be discharged at the emergence date; however, as noted above, Delphi has not yet consummated its confirmed plan and is continuing to work with its stakeholders to further amend the plan accordingly, and there can be no assurances that these estimates will not change as a result of changes to the plan.

Use of Estimates Preparation of consolidated financial statements in conformity with generally accepted accounting principles in the United States of America ("U.S. GAAP") requires Delphi to make estimates and assumptions that affect amounts reported therein. During the first quarter of 2008, there were no material changes in the methods or policies used to establish accounting estimates. Generally, matters subject to Delphi's estimation and judgment include amounts related to accounts receivable realization, inventory obsolescence, asset impairments, useful lives of intangible and fixed assets, deferred tax asset valuation allowances, income taxes, pension and other postretirement benefit plan assumptions, accruals related to litigation, warranty costs, environmental remediation costs, workers compensation accruals and healthcare accruals. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be based upon amounts that differ from those estimates.

Valuation of Long-Lived Assets Delphi periodically evaluates the carrying value of long-lived assets held for use including intangible assets when events or circumstances warrant such a review. The carrying value of a long-lived asset held for use is considered impaired when the anticipated separately identifiable undiscounted cash flows from

the asset are less than the carrying value of the asset. In that event, a loss is

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recognized based on the amount by which the carrying value exceeds the fair value of the long-lived asset. Fair value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involved or Delphi's review of appraisals. Impairment losses on long-lived assets held for sale are determined in a similar manner, except that fair values are reduced for the cost to dispose of the assets. During the first quarter of 2008 and 2007, Delphi recorded asset impairment charges of \$3 million and \$160 million, respectively, of which \$3 million and \$6 million, respectively, were recorded in depreciation and amortization and included in loss from continuing operations and \$154 million was recorded in loss from discontinued operations for the first quarter of 2007. Refer to Note 4. Discontinued Operations for more information.

Discontinued Operations In accordance with Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, (SFAS 144), a business component that is disposed of or classified as held for sale is reported as discontinued operations if the cash flows of the component have been or will be eliminated from the ongoing operations of the Company and the Company will no longer have any significant continuing involvement in the business component. The results of discontinued operations are aggregated and presented separately in the consolidated statements of operations and consolidated statements of cash flows. Assets and liabilities of the discontinued operations are aggregated and reported separately as assets and liabilities held for sale in the consolidated balance sheet. SFAS 144 requires the reclassification of amounts presented for prior years to effect their classification as discontinued operations.

Amounts have been derived from the consolidated financial statements and accounting records of Delphi using the historical basis of assets and liabilities to be disposed of and historical results of operations related to Delphi's global steering and halfshaft businesses (the Steering Business) and its interiors and closures product line (the Interiors and Closures Business). The sale of the U.S. operations and certain of the non-U.S. operations of the Steering Business will be sales of assets and will include (i) all assets, except for cash, deferred tax assets, and intercompany accounts, and (ii) all liabilities, except for debt, deferred tax liabilities, intercompany accounts, U.S. pension and other postretirement benefit liabilities, accrued payroll, and certain employee benefit accounts. The sale of certain non-U.S. operations of the Steering Business will be stock sales and will include all assets and liabilities for the sites with purchase price adjustments for cash, debt, and certain other accounts. The sale of the Interiors and Closures Business closed on February 29, 2008. The majority of the Interiors and Closures Business sale were asset sales and the buyer assumed inventory, fixed assets, non-U.S. pension liabilities and an investment in a joint venture in Korea.

While the historical results of operations of the Steering Business and the Interiors and Closures Business include general corporate allocations of certain functions historically provided by Delphi, such as accounting, treasury, tax, human resources, facility maintenance, and other services, no amounts for these general corporate retained functions have been allocated to the loss from discontinued operations in the statements of operations. Delphi expects to retain certain employee pension and other postretirement benefit liabilities for the Steering Business and these liabilities were not allocated to liabilities held for sale in the balance sheets. Expenses related to the service cost of employee pension and other postretirement benefit plans, however, were allocated to discontinued operations in the statements of operations, because Delphi will not continue to incur such related expense subsequent to the divestiture of these businesses. Allocations have been made based upon a reasonable allocation method.

Recently Issued Accounting Pronouncements In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 (SFAS 157), *Fair Value Measurements*. SFAS 157 defines fair value, establishes a framework for measuring fair value in U.S. GAAP, and expands the disclosure requirements regarding fair value measurements. The rule does not introduce new requirements mandating the use of fair value. SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The definition is based on an exit price rather than an entry price, regardless of whether the entity plans to hold or sell the asset. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company utilized

the fair value measures of SFAS 157 in accounting for its marketable securities and derivative net assets. The adoption of the new definition of fair value pursuant to SFAS 157 did not have a significant impact on Delphi's financial statements. Refer to Note 15. Fair Value Measurements for the disclosures required by SFAS 157.

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In September 2006, the FASB issued Statement of Financial Accounting Standards No. 158 (SFAS 158), *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans-an amendment of FASB Statements No. 87, 88, 106, and 132(R)*. SFAS 158 requires, among other things, an employer to measure the funded status of its defined benefit pension and other postretirement benefits plans as of the date of its year-end statement of financial position, with limited exceptions, effective for fiscal years ending after December 15, 2008. Historically, Delphi has measured the funded status of its U.S. retiree health care benefit plans and certain international pension plans as of September 30 of each year. Delphi adopted the measurement date provisions of SFAS 158 as of January 1, 2008, which resulted in adjustments that increased pension and other postretirement benefit liabilities by \$139 million, the accumulated deficit by \$129 million and increased accumulated other comprehensive loss by \$10 million.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 (SFAS 159), *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*. SFAS 159 permits entities to choose, at specified election dates, to measure many financial instruments and certain other items at fair value that are not currently measured at fair value. Unrealized gains and losses on items for which the fair value option has been elected would be reported in earnings at each subsequent reporting date. SFAS 159 also establishes presentation and disclosure requirements in order to facilitate comparisons between entities choosing different measurement attributes for similar types of assets and liabilities. SFAS 159 does not affect existing accounting requirements for certain assets and liabilities to be carried at fair value. SFAS 159 is effective as of the beginning of a reporting entity's first fiscal year that begins after November 15, 2007. Delphi adopted SFAS 159 as of January 1, 2008 and did not elect the fair value option for any financial instruments upon adoption of SFAS 159.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 (Revised 2007) (SFAS 141R), *Business Combinations*. SFAS 141R requires an acquiring entity to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. 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. Earlier adoption is prohibited. Accordingly, Delphi is required to record and disclose business combinations following existing U.S. GAAP until January 1, 2009. Delphi is currently evaluating the requirements of SFAS 141R, and has not yet determined the impact on its financial statements.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160 (SFAS 160), *Noncontrolling Interests in Consolidated Financial Statements An Amendment of ARB No. 51*. SFAS 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. Delphi is currently evaluating the requirements of SFAS 160, and has not yet determined the impact on its financial statements.

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 161 (SFAS 161), *Disclosures about Derivative Instruments and Hedging Activities an Amendment of FASB Statement 133*. SFAS 161 enhances required disclosures regarding derivatives and hedging activities, including enhanced disclosures regarding how: (a) an entity uses derivative instruments; (b) derivative instruments and related hedged items are accounted for under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*; and (c) derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS 161 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after November 15, 2008. Earlier adoption is encouraged. Delphi is currently evaluating the requirements of SFAS 161, and has not yet determined the impact on its financial statements.

In April 2008, the FASB issued FASB Staff Position SOP 90-7-1 (FSP SOP 90-7-1), *An Amendment of AICPA Statement of Position 90-7*. FSP SOP 90-7-1 resolves the conflict between the guidance requiring early adoption of

new accounting standards for entities required to follow fresh-start reporting under American Institute of Certified Public Accountants Statement of Position 90-7, *Financial Reporting by Entities in Reorganization under the Bankruptcy Code*, and other authoritative accounting standards that expressly prohibit early adoption. Specifically, FSP SOP 90-7-1 will require an entity emerging from bankruptcy that

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applies fresh-start reporting to follow only the accounting standards in effect at the date fresh-start reporting is adopted, which include those standards eligible for early adoption if an election is made to adopt early.

2. TRANSFORMATION PLAN AND CHAPTER 11 BANKRUPTCY

On September 6, 2007, Delphi filed a proposed plan of reorganization (the Plan) and related disclosure statement (the Disclosure Statement) with the Court. The Plan and Disclosure Statement outlined Delphi's transformation centering around five core areas, as detailed below, including agreements reached with each of Delphi's principal U.S. labor unions and GM. Through November 2007, the Court granted additional requests by Delphi to further continue the hearing on the adequacy of the Disclosure Statement to allow Delphi to negotiate potential amendments to the Plan and the related agreements with its stakeholders, including the comprehensive agreements reached with GM and the Equity Purchase and Commitment Agreement (July EPCA) between Delphi and certain affiliates of lead investor Appaloosa Management L.P. (Appaloosa), Harbinger Capital Partners Master Fund I, Ltd. (Harbinger), Pardus Capital Management, L.P. (Pardus) and Merrill Lynch, Pierce, Fenner & Smith, Incorporated (Merrill), UBS Securities LLC (UBS), and Goldman Sachs & Co. (Goldman) (collectively the Investors). On December 3, 2007, Delphi filed further potential amendments to the Plan, the comprehensive agreements reached with GM, the July EPCA, and the related Disclosure Statement and on December 4, 2007 Delphi announced that it had reached agreement in principle on these amendments with the Creditors' Committee, the Equity Committee, GM, and the Investors. After a hearing on the adequacy of the proposed Disclosure Statement in December of 2007, Delphi filed its first amended joint Plan of Reorganization (the Amended Plan) and its first amended Disclosure Statement with respect to the Amended Plan (the Amended Disclosure Statement). The Court entered an order approving the adequacy of the Amended Disclosure Statement on December 10, 2007. On December 10, 2007, Delphi and the Investors entered into an amendment to the July EPCA (the EPCA Amendment) and together with the July EPCA and all schedules and exhibits thereto, the EPCA). After entry of the order approving the Amended Disclosure Statement, Delphi began solicitation of votes on the Amended Plan. On January 16, 2008, Delphi filed further modifications to the Amended Plan. Additional modifications are set forth in Exhibit A to the Confirmation Order which was entered on January 25, 2008 and that order became final on February 4, 2008.

Plan of Reorganization and Transformation Plan**Elements of Transformation Plan**

On March 31, 2006, Delphi announced its transformation plan centered around five key elements, each of which is also addressed in its Amended Plan and the series of settlement agreements it embodies. The progress on each element is discussed below.

Labor Modify Delphi's labor agreements to create a more competitive arena in which to conduct business.

During the second quarter of 2007, Delphi signed an agreement with the International Union, United Automobile, Aerospace and Agricultural Implement Workers of America (UAW), and during the third quarter of 2007, Delphi signed agreements with the remainder of its principal U.S. labor unions, which were ratified by the respective unions and approved by the Court in the third quarter of 2007. Among other things, as approved and confirmed by the Court, this series of settlement agreements or memoranda of understanding among Delphi, its unions, and GM settled the Debtors' motion under sections 1113 and 1114 of the Bankruptcy Code seeking authority to reject their U.S. labor agreements and to modify retiree benefits (the 1113/1114 Motion). As applicable, these agreements also, among other things, modify, extend or terminate provisions of the existing collective bargaining agreements among Delphi and its unions and cover issues such as site plans, workforce transition and legacy pension and other postretirement benefits obligations as well as other comprehensive transformational issues. Portions of these agreements have already become effective, and the remaining portions will not become effective until the effectiveness of the Global Settlement

Agreement, as amended (the GSA), and the Master Restructuring Agreement, as amended (the MRA), with GM and upon substantial consummation of the Amended Plan as confirmed by the Court. The Amended Plan incorporates, approves, and is consistent with the terms of each agreement.

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Among other things, these agreements generally provided certain members of the union labor workforce options to either retire, accept a voluntary severance package or accept lump sum payments in return for lower hourly wages. Refer to Note 12. U.S. Employee Workforce Transition Programs for more information.

On September 4, 2007, the Court confirmed that the 1113/1114 Motion was withdrawn without prejudice, subject to the Court's prior settlement approval orders pertaining to each of Delphi's U.S. labor unions, as it relates to all parties and the intervening respondents, by entry of an Order Withdrawing Without Prejudice Debtors' Motion For Order Under 11 U.S.C. § 1113(c) Authorizing Rejection Of Collective Bargaining Agreements And Authorizing Modification Of Retiree Welfare Benefits Under 11 U.S.C. § 1114(g).

GM Conclude negotiations with GM to finalize financial support for certain of Delphi's legacy and labor costs and to ascertain GM's business commitment to Delphi going forward.

Delphi and GM have entered into comprehensive settlement agreements consisting of the GSA and the MRA. The GSA and the MRA comprised part of the Amended Plan and were approved in the order confirming the Amended Plan on January 25, 2008. The GSA and MRA are not effective until and unless Delphi emerges from chapter 11. Accordingly, the accompanying consolidated financial statements do not include any adjustments related to the GSA or the MRA. These agreements will result in a material reduction in Delphi's liabilities related to the workforce transition programs. Delphi will account for the impact of the GSA or the MRA when the conditions of the agreements are satisfied, which will likely occur upon emergence from chapter 11.

Most obligations set forth in the GSA are to be performed upon the occurrence of the effective date of the Amended Plan or as soon as reasonably possible thereafter. By contrast, resolution of most of the matters addressed in the MRA will require a significantly longer period that will extend for a number of years after confirmation of the Amended Plan.

GM's obligations under the GSA and MRA are conditioned upon, among other things, Delphi's consummation of the Amended Plan, including payment of amounts to settle GM claims as outlined below.

The GSA is intended to resolve outstanding issues between Delphi and GM that have arisen or may arise before Delphi's emergence from chapter 11, and will be implemented by Delphi and GM in the short term. On November 14, 2007 and again on December 3, 2007, Delphi entered into amendments to both the GSA and the MRA. These agreements, as amended, provide for a comprehensive settlement of all outstanding issues between Delphi and GM, including (other than ordinary course matters): litigation commenced in March 2006 by Delphi to terminate certain supply agreements with GM; all potential claims and disputes with GM arising out of the separation of Delphi from GM in 1999; certain post-separation claims and disputes between Delphi and GM; the proofs of claim filed by GM against Delphi in Delphi's chapter 11 cases; GM's treatment under Delphi's Amended Plan; and various other legacy issues.

In addition to establishing claims treatment, including specifying which claims survive and the consideration to be paid by Delphi to GM in satisfaction of certain claims, the GSA addresses, among other things, commitments by Delphi and GM regarding other postretirement benefit and pension obligations, and other GM contributions with respect to labor matters and releases.

GM will assume approximately \$7 billion of certain post-retirement benefits for certain of the Company's active and retired hourly employees, including health care and life insurance;

Delphi will freeze its Delphi Hourly-Rate Employees Pension Plan as soon as practicable following the effective date of the Amended Plan, as provided in the union settlement agreements, and GM's Hourly Pension

Plan will become responsible for certain future costs related to the Delphi Hourly-Rate Employees Pension Plan;

Delphi will transfer certain assets and liabilities of its Delphi Hourly-Rate Employees Pension Plan to the GM Hourly-Rate Employee Pension Plan, as set forth in the union settlement agreements;

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Shortly after the effectiveness of the Amended Plan, GM will receive an interest bearing note from Delphi in the amount of \$1.5 billion which is expected to be paid promptly following effectiveness;

GM will make significant contributions to Delphi to fund various special attrition programs, consistent with the provisions of the U.S. labor agreements; and

GM and certain related parties and Delphi and certain related parties will exchange broad, global releases (which will not apply to certain surviving claims as set forth in the GSA).

The MRA is intended to govern certain aspects of Delphi and GM's commercial relationship following Delphi's emergence from chapter 11. The MRA addresses, among other things, the scope of GM's existing and future business awards to Delphi and related pricing agreements and sourcing arrangements, GM commitments with respect to reimbursement of specified ongoing labor costs, the disposition of certain Delphi facilities, and the treatment of existing agreements between Delphi and GM. Through the MRA, Delphi and GM have agreed to certain terms and conditions governing, among other things:

The scope of existing business awards, related pricing agreements, and extensions of certain existing supply agreements, including GM's ability to move production to alternative suppliers, and reorganized Delphi's rights to bid and qualify for new business awards;

GM will make significant, ongoing contributions to Delphi and reorganized Delphi to reimburse the Company for labor costs in excess of \$26 per hour, excluding certain costs, including hourly pension and other postretirement benefit contributions provided under the Supplemental Wage Agreement, at specified UAW manufacturing facilities retained by Delphi;

GM and Delphi have agreed to certain terms and conditions concerning the sale of certain of Delphi's non-core businesses;

GM and Delphi have agreed to certain additional terms and conditions if certain of Delphi's businesses and facilities are not sold or wound down by certain future dates (as defined in the MRA); and

GM and Delphi have agreed to the treatment of certain contracts between Delphi and GM arising from Delphi's separation from GM and other contracts between Delphi and GM.

The GSA and MRA may be terminated by the Company or GM because the effective date of the Amended Plan did not occur by March 31, 2008 and the EPCA was terminated. As of the date hereof, neither Delphi nor GM has terminated the GSA or the MRA.

Portfolio Streamline Delphi's product portfolio to capitalize on world-class technology and market strengths and make the necessary manufacturing alignment with Delphi's new focus.

In March 2006, Delphi identified non-core product lines and manufacturing sites that do not fit into Delphi's future strategic framework, including brake and chassis systems, catalysts, cockpits and instrument panels, door modules and latches, ride dynamics, steering, halfshafts, and wheel bearings. Effective November 1, 2006, in connection with the Company's continuous evaluation of its product portfolio, it decided that the power products business no longer fit within the Company's future product portfolio and that business line was moved to Delphi's Automotive Holdings Group. With the exception of the catalyst product line (included in the Powertrain Systems segment), and the steering and halfshaft product lines and interiors and closures product lines (included in discontinued operations), the

Company's non-core product lines are included in the Automotive Holdings Group segment, refer to Note 17. Segment Reporting.

Delphi has continued sale and wind-down efforts with respect to non-core product lines and manufacturing sites. The sale and wind-down process is being conducted in consultation with the Company's customers, unions and other stakeholders to carefully manage the transition of affected product lines and manufacturing sites. The disposition of any U.S. operation is also being accomplished in accordance with the requirements of the Bankruptcy Code and union labor contracts as applicable. The Company also has begun consultations with the works councils in accordance with applicable laws regarding any sale or wind-down of affected manufacturing sites in Europe.

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During the first quarter of 2008, Delphi obtained Court approval of bidding procedures and sales agreements for the steering and halfshaft product line, the global bearings business and the U.S. suspensions business and closed on the sales of the interiors and closures product line and the North American brake components machining and assembly assets. Refer to Note 4. Discontinued Operations and Note 5. Divestitures for more information.

Costs recorded in the first quarter of 2008 and 2007 related to the transformation plan for non-core product lines include impairments of long-lived assets and employee termination benefits and other exit costs as further described in Note 4. Discontinued Operations and Note 6. Employee Termination Benefits and Other Exit Costs.

Cost Structure Transform the salaried workforce and reduce general and administrative expenses to ensure that its organizational and cost structure is competitive and aligned with Delphi's product portfolio and manufacturing footprint.

Delphi is continuing to implement restructuring initiatives in furtherance of the transformation of its salaried workforce to reduce selling, general and administrative expenses to support its realigned portfolio. These initiatives include financial services and information technology outsourcing activities, reduction in its global salaried workforce by taking advantage of attrition and using salaried separation plans, and realignment of certain salaried benefit programs to bring them in line with more competitive industry levels. Given the investment required to implement these initiatives, Delphi does not expect to fully realize substantial savings until 2009 and beyond.

Pensions Devise a workable solution to the current pension funding situation, whether by extending contributions to the pension trusts or otherwise.

Delphi's discussions with the Internal Revenue Service (IRS) and the Pension Benefit Guaranty Corporation (PBGC) regarding the funding of the Delphi Hourly-Rate Employees Pension Plan (the Hourly Plan) and the Delphi Retirement Program for Salaried Employees (the Salaried Plan) upon emergence from chapter 11 culminated in a funding plan that would enable the Company to satisfy its pension funding obligations upon emergence from chapter 11 through a combination of emergence contributions and a transfer of certain unfunded liabilities to a pension plan sponsored by GM.

On May 1, 2007, the IRS issued conditional waivers for the Hourly Plan and Salaried Plan with respect to the plan year ended September 30, 2006 (the 2006 Waivers). On May 31, 2007, the Court authorized Delphi to perform under the terms of those funding waivers. The IRS modified the 2006 Waivers by extending the dates by which Delphi is required to file its Amended Plan and emerge from chapter 11. On September 28, 2007, the IRS issued a second conditional waiver for the Hourly Plan for the plan year ended September 30, 2007 (the 2007 Hourly Plan Waiver). The waivers were required, at that time, to facilitate the Debtors' option to effectuate the transfer of certain hourly pension obligations to GM in an economically efficient manner, and to remove uncertainty as to whether excise taxes would be assessed as a result of accumulated funding deficiencies relating to prepetition service. Absent the waivers, the transfer to GM could have triggered an obligation on the part of the Debtors to make cash contributions to the Hourly Plan which would result in a projected overfunding of the Hourly Plan. On October 26, 2007, the Court authorized Delphi to perform under the 2007 Hourly Plan Waiver, which would have expired if Delphi did not emerge from chapter 11 by February 29, 2008. The Court authorized two additional funding waivers which authorized Delphi to defer funding contributions due under the Employee Retirement Income Security Act (ERISA) and the U.S. Internal Revenue Code (the Code) until May 9, 2008. On April 4, 2008, the IRS and the PBGC modified the 2006 Waivers and the 2007 Hourly Plan Waiver by extending the date by which Delphi must emerge from chapter 11 to May 9, 2008.

Delphi did not seek extension past May 9, 2008 of the 2006 Waivers or the 2007 Hourly Plan Waiver. Delphi believes that ERISA and the Code will still, under most circumstances, post June 15, 2008, permit the Company to be able to

effect the planned transfer of hourly pension obligations to GM in an economically efficient manner. However, by permitting the waivers to lapse Delphi is exposed to excise taxes as a result of accumulated funding deficiencies for the plan years ended September 30, 2005 and 2006 of approximately

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\$170 million and \$1.2 billion, respectively. Accordingly, the IRS may assert against Delphi excise taxes in the approximate amounts of \$17 million and \$122 million for plan years ended September 30, 2005 and 2006, respectively. Also, should Delphi not meet its minimum funding requirements on or before June 15, 2008, the accumulated funding deficiency would be approximately \$2.4 billion for the plan year ended September 30, 2007, which could lead to the IRS further asserting additional excise taxes of approximately \$244 million. If the accumulated funding deficiency is not corrected after Delphi receives the assessments, an excise tax of up to 100% may be assessed at the discretion of the IRS. Assuming Delphi is assessed an excise tax for all plan years through 2007, the total range of exposure would approximate between \$380 million and \$3.8 billion.

Delphi believes that under the Bankruptcy Code, the Company is not obligated to make contributions for pension benefits attributable to prepetition service while in chapter 11 and that it has made all required payments for postpetition service. Delphi further believes that as a result, it is not liable for any penalty excise taxes that may be assessed by the IRS. Delphi believes that its ultimate emergence from chapter 11 will result in a consensual resolution of its pension funding obligations, and given the significant uncertainty surrounding the outcome of the excise tax assessment and the potential for Delphi to litigate this matter, if necessary, management has concluded that an unfavorable outcome is not currently probable. Accordingly, as of March 31, 2008, no amounts have been recorded for any excise tax assessment.

Pursuant to the pertinent terms of the waivers, as modified, Delphi provided to the PBGC letters of credit, effective June 16, 2007, in favor of the Hourly and Salaried Plans in the amount of \$100 million to support funding obligations under the Hourly Plan (increased to \$112.5 million pursuant to the waiver extension granted March 28, 2008) and \$50 million to support funding obligations under the Salaried Plan. In exchange for extension of the waivers on April 4, 2008, the Company extended the term of the previously issued letters of credit to May 23, 2008, and increased the face amount of the letter of credit in favor of the Hourly Plan by \$10 million to \$122.5 million effective April 16, 2008. Due to the expiration of the waivers, the PBGC has informed Delphi that it intends to draw against the \$172.5 million of letters of credit in favor of the Hourly and Salaried Plans. The cash proceeds from the letters of credit will be recognized as Delphi funding contributions to the plans.

The Company has represented that it currently intends to meet the minimum funding standard under IRC section 412 for the plan years ended September 30, 2006 and 2007 upon emergence from chapter 11. Assuming a consensual funding plan is achieved, the Company currently expects that its pension contributions due upon emergence from chapter 11 will approximate \$1 billion under current legislation and plan design, after giving effect to an anticipated transfer of at least a net of \$1.5 billion of unfunded benefit liabilities from the Hourly Plan to a pension plan sponsored by GM.

In addition to the funding strategy discussed above and the changes to the Hourly Plan discussed in the Labor section, Delphi committed to freeze the Hourly and Salaried Plans effective at the end of the month following emergence from chapter 11. Refer to Note 13. Pension and Other Postretirement Benefits for more information.

The Amended Plan of Reorganization

On April 4, 2008, Delphi announced that although the Debtors had met the conditions required to substantially consummate the Amended Plan (as modified by the Court's final confirmation order), including obtaining \$6.1 billion of exit financing, the Investors refused to participate in a closing that was commenced but not completed and refused to fund the EPCA. The Debtors are prepared to pursue any and all available equitable and legal remedies with respect to the Investors that are in the best interests of the Debtors and their stakeholders, and are working with their stakeholders to achieve their goal of emergence from chapter 11 as soon as practicable.

Pursuant to an order entered by the Court on April 30, 2008, the Debtors' exclusivity period under the Bankruptcy Code for filing a plan of reorganization is extended until 30 days after substantial consummation of the Amended Plan (as modified) or any modified plan and the Debtors' exclusivity period for soliciting acceptance of the Amended Plan (as modified) is extended until 90 days after substantial consummation of the

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Amended Plan (as modified) or any modified plan. Notwithstanding the foregoing, the Debtors' exclusive period for filing a plan of reorganization, as between the Debtors and the Creditors' Committee and the Equity Committee, collectively, is extended through and including August 31, 2008 and the Debtors' exclusive period for soliciting acceptance of a plan of reorganization, as between the Debtors and the Creditors' Committee and the Equity Committee, collectively, is extended through and including October 31, 2008.

Equity Purchase and Commitment Agreement

Under the terms and subject to the conditions of the EPCA, the Investors committed to purchase \$800 million of convertible preferred stock and approximately \$175 million of common stock in the reorganized Company. Additionally, subject to satisfaction of other terms and conditions, the Investors committed to purchase any unsubscribed shares of common stock in connection with an approximately \$1.6 billion rights offering that was made available to unsecured creditors. The rights offering commenced on March 11, 2008 and expired on March 31, 2008. In light of the Investors' refusal to fund the EPCA, in April 2008, the Company cancelled the rights offering and returned all funds submitted.

The EPCA also included certain corporate governance provisions for the reorganized Company, each of which was incorporated into Delphi's Amended Plan. The EPCA also incorporated Delphi's earlier commitment to preserve its salaried and hourly defined benefit U.S. pension plans and to fund required contributions to the plans that were not made in full as permitted under the Bankruptcy Code.

The EPCA was subject to the satisfaction or waiver of numerous conditions, including the condition that an affiliate of Appaloosa was reasonably satisfied with the terms of certain material transaction documents (evidenced by an affiliate of Appaloosa not delivering a deficiency notice), to the extent the terms thereof would have an impact on the Investors proposed investment in the Company and receipt of proceeds from the sale of preferred stock, exit financing and the discount rights offering sufficient to fund the transaction contemplated by the EPCA and certain related transactions. Other conditions to closing included release and exculpation of each Investor as set forth in the EPCA Amendment; that the Company would have undrawn availability of \$1.4 billion including a letter of credit carve out and reductions under a borrowing base formula; that the Company's pro forma interest expense during 2008 on the Company's indebtedness, as defined in the EPCA, would not exceed \$585 million; that scheduled Pension Benefit Guarantee Corporation liens were withdrawn; and that the aggregate amount of trade and unsecured claims could be no more than \$1.45 billion (subject to certain waivers and exclusions).

An affiliate of Appaloosa could terminate the EPCA, including, at any time on or after April 5, 2008, if the Amended Plan had not become effective; if the Company had changed its recommendation or approval of the transactions contemplated by the EPCA, the Amended Plan terms or the settlement with GM in a manner adverse to the Investors or approved or recommended an alternative transaction; or if the Company had entered into any agreement, or taken any action to seek Court approval relating to any plan, proposal, offer or transaction, that was inconsistent with the EPCA, the settlement with GM or the Amended Plan. In the event of certain terminations of the EPCA pursuant to the terms thereof, the Company could be obligated to pay the Investors \$83 million plus certain transaction expenses as described in the immediately following paragraph.

The Company would be required to pay the Investors \$83 million plus certain transaction expenses if (a) the EPCA was terminated as a result of the Company's agreeing to pursue an alternative investment transaction with a third party or (b) either the Company's Board of Directors withdrew its recommendation of the transaction or the Company willfully breached the EPCA, and within the next 24 months thereafter, the Company then agreed to an alternative investment transaction.

On April 4, 2008, Delphi announced that although it had met the conditions required to substantially consummate its First Amended Joint Plan of Reorganization, including obtaining \$6.1 billion of exit financing, the Investors refused to participate in a closing that was commenced but not completed on that date. Several hours prior to the scheduled closing on April 4, 2008, Appaloosa delivered to Delphi a letter dated April 4, 2008, stating that such letter constitutes a notice of immediate termination of the EPCA. Appaloosa's April 4 letter alleged that Delphi had breached certain provisions of the EPCA, that Appaloosa is entitled to terminate the EPCA and that the Investors are entitled to be paid the fee of \$83 million plus certain

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expenses and other amounts. At the time Appaloosa delivered its letter, other than the Investors, all the required parties for a successful closing and emergence from chapter 11, including representatives of Delphi's exit financing lenders, GM, and the Unsecured Creditors and Equity Committees in Delphi's chapter 11 cases were present, were prepared to move forward, and all actions necessary to consummate the plan of reorganization were taken other than the concurrent closing and funding of the EPCA.

On April 5, 2008, Appaloosa delivered to Delphi a letter described as a supplement to the April 4 Termination Notice, stating this letter constitutes a notice of an additional ground for termination of the EPCA. The April 5 letter stated that because the EPCA had not become effective on or before April 4, 2008 it was grounds for its termination.

Delphi believes that Appaloosa wrongfully terminated the EPCA and disputes the allegations that Delphi breached the EPCA or failed to satisfy any condition to the Investors' obligations thereunder as asserted by Appaloosa in its April 4 letter. Delphi's Board of Directors formed a special litigation committee and engaged independent legal counsel to consider and pursue any and all available equitable and legal remedies, including the commencement of legal action in the Court to seek all appropriate relief, including specific performance by the Investors of their obligations under the EPCA.

In exchange for the Investors' commitment to purchase common stock and the unsubscribed shares in the rights offering, the Company paid an aggregate commitment fee of \$39 million and certain transaction expenses and in exchange for the Investors' commitment to purchase preferred stock the Company paid an aggregate commitment fee of \$18 million. In addition, the Company paid an arrangement fee of \$6 million to Appaloosa to compensate Appaloosa for arranging the transactions contemplated by the EPCA. The Company has also paid certain out-of-pocket costs and expenses reasonably incurred by the Investors or their affiliates subject to certain terms, conditions and limitations set forth in the EPCA. Delphi had deferred the recognition of these amounts in other current assets as they were to be netted against the proceeds from the EPCA upon issuance of the new shares. However, as a result of the events relating to the termination of the EPCA as described above, Delphi recognized \$79 million of expense related to these fees and other expenses during the first quarter of 2008.

The cost related to the transformation plan will be recognized in the Company's consolidated financial statements as elements of the Amended Plan (as modified), as the terms of any future confirmed plan of reorganization, as the U.S. labor agreements, and as the GSA, and the MRA become effective. In the event the Debtors are unable to consummate the Amended Plan (as modified), the cost will be recognized as the aforementioned agreements become effective as elements of any future confirmed plan of reorganization. The Amended Plan and agreements will significantly impact Delphi's accounting for its pension plans, post-retirement benefit plans, other employee related benefits, long-lived asset impairments and exit costs related to the sites planned for closure or consolidation, compensation costs for labor recognized over the term of the U.S. labor agreements, and the fair values assigned to assets and liabilities upon Delphi's emergence from chapter 11, among others. Such adjustments will have a material impact on Delphi's financial statements.

There are a number of risks and uncertainties inherent in the chapter 11 process, including those detailed in Delphi's Annual Report on Form 10-K for the year ended December 31, 2007, Part I, Item 1A. Risk Factors and Part II, Item 1A. Risk Factors in this Quarterly Report on Form 10-Q. In addition, Delphi cannot assure that potential adverse publicity associated with the Chapter 11 Filings and the resulting uncertainty regarding its future prospects will not materially hinder Delphi's ongoing business activities and its ability to operate, fund and execute Delphi's business plan by impairing relations with existing and potential customers; negatively impacting its ability to attract, retain and compensate key executives and associates and to retain employees generally; limiting its ability to obtain trade credit; and impairing present and future relationships with vendors and service providers.

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The financial statements of the Debtors are presented as follows:

Basis of Presentation

Condensed Combined Debtors-in-Possession Financial Statements The financial statements contained within this note represent the condensed combined financial statements for the Debtors only. Delphi's non-Debtor subsidiaries are treated as non-consolidated affiliates in these financial statements and as such their net income is included as Equity income (loss) income from non-Debtor affiliates, net of tax in the statement of operations and their net assets are included as Investments in non-Debtor affiliates in the balance sheet. The Debtors' financial statements contained herein have been prepared in accordance with the guidance in SOP 90-7.

Intercompany Transactions Intercompany transactions between Debtors have been eliminated in the financial statements contained herein. Intercompany transactions between the Debtors and non-Debtor affiliates have not been eliminated in the Debtors' financial statements. Therefore, reorganization items, net included in the Debtors' Statement of Operations, liabilities subject to compromise included in the Debtors' Balance Sheet, and reorganization items and payments for reorganization items, net included in the Debtors' Statement of Cash Flows are different than Delphi Corporation's consolidated financial statements. As approved by the Court on January 25, 2008, the Debtors sold investments in non-Debtor affiliates in the amount of \$1.4 billion to a non-Debtor affiliate and received a note receivable from non-Debtor affiliates, of which \$0.2 billion is included in current assets and \$1.2 billion is included in long-term assets.

Contractual Interest Expense and Interest Expense on Unsecured Claims Contractual interest expense represents amounts due under the contractual terms of outstanding debt, including debt subject to compromise for which interest expense is not recognized in accordance with the provisions of SOP 90-7. Delphi did not record contractual interest expense on certain unsecured prepetition debt during the quarter ended March 31, 2007. In September 2007, Delphi began recording prior contractual interest expense related to certain prepetition debt because it became probable that the interest would become an allowed claim based on the provisions of the plan of reorganization filed with the Court in September 2007. The plan of reorganization also provides that certain holders of allowed unsecured claims against Delphi will be paid postpetition interest on their claims, calculated at the contractual non-default rate from the petition date through January 25, 2008. Delphi recorded interest related to prepetition debt and allowed unsecured claims of \$14 million during the quarter ended March 31, 2008. This interest expense was calculated through January 25, 2008, the confirmation date of the plan of reorganization. This estimate is based on numerous factual and legal assumptions. At March 31, 2008, Delphi had accrued interest of \$425 million in accrued liabilities in the accompanying balance sheet for prepetition claims.

U.S. Employee Workforce Transition Programs The workforce transition programs offer buy-down payments for eligible traditional employees who do not elect the attrition or flowback options and continue to work for Delphi. The estimated payments to be made under the buy-down arrangements within the UAW and IUE-CWA Workforce Transition Programs totaled \$323 million and were recorded as a wage asset and liability in 2007. In the first quarter of 2008, the wage asset and liability were increased by \$3 million to reflect the final terms of certain divestitures. At March 31, 2008, \$84 million was recorded in other current assets and \$199 million was recorded in other long-term assets in the accompanying balance sheet, net of \$21 million of amortization expense recorded in the first quarter of 2008, of which \$1 million was recorded in loss from discontinued operations. In addition, \$16 million was recorded in U.S. employee workforce transition program charges to reflect costs under the workforce transition programs in excess of amounts previously estimated. Refer to Note 12. U.S. Employee Workforce Transition Programs for more information.

Assets Held for Sale The assets held for sale by the Debtors include the net assets held for sale of the Non-debtor affiliates of \$335 million which was reclassified from investments in non-Debtor affiliates.

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(Non-filed entities, principally non-U.S. subsidiaries, excluded from consolidated Debtor group)

	Three Months Ended	
	March 31	
	2008	2007
	(in millions)	
Net sales	\$ 2,328	\$ 3,287
Operating expenses:		
Cost of sales, excluding items listed below	2,453	3,322
U.S. employee workforce transition program charges (credit)	36	(6)
Depreciation and amortization	115	137
Selling, general and administrative	225	236
Total operating expenses	2,829	3,689
Operating loss	(501)	(402)
Interest expense (contractual interest expense for the three months ended March 31, 2008 and 2007 was \$113 million and \$112 million, respectively)	(95)	(79)
Loss on extinguishment of debt		(23)
Other income, net		12
Reorganization items, net	(100)	(31)
Loss from continuing operations before income tax expense and equity income	(696)	(523)
Income tax expense	(3)	(4)
Loss from continuing operations before equity income	(699)	(527)
Equity income from non-consolidated affiliates, net of tax	7	14
Loss from continuing operations before discontinued operations and equity income from non-Debtor affiliates	(692)	(513)
Loss from discontinued operations, net of tax	(82)	(123)
Equity income from non-Debtor affiliates, net of tax	185	103
Net loss	\$ (589)	\$ (533)

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CONDENSED COMBINED DEBTORS-IN-POSSESSION BALANCE SHEET
(Non-filed entities, principally non-U.S. subsidiaries, excluded from consolidated Debtor group)

	March 31,		December 31,
	2008		2007
	(Unaudited)		(in millions)
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 47	\$	113
Restricted cash	125		125
Accounts receivable, net:			
General Motors and affiliates	900		972
Other third parties	708		623
Non-Debtor affiliates	245		250
Notes receivable from non-Debtor affiliates	449		278
Inventories, net:			
Productive material, work-in-process and supplies	639		652
Finished goods	156		171
Other current assets	342		385
Assets held for sale	422		475
Total current assets	4,033		4,044
Long-term assets:			
Property, net	1,347		1,446
Investments in affiliates	329		331
Investments in non-Debtor affiliates	2,067		3,267
Goodwill	152		152
Notes receivable from non-Debtor affiliates	1,172		
Other	487		512
Total long-term assets	5,554		5,708
Total assets	\$ 9,587	\$	9,752
LIABILITIES AND STOCKHOLDERS DEFICIT			
Current liabilities not subject to compromise:			
Notes payable and secured debt in default	\$ 3,231	\$	2,782
Accounts payable	898		1,007
Accounts payable to non-Debtor affiliates	654		689
Accrued liabilities	1,275		1,328
Liabilities held for sale	193		167
Total current liabilities	6,251		5,973
Debtor-in-possession financing	23		24
Employee benefit plan obligations and other	932		951

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Total long-term liabilities	955	975
Liabilities subject to compromise	16,441	16,276
Total liabilities	23,647	23,224
Stockholders' deficit:		
Total stockholders' deficit	(14,060)	(13,472)
Total liabilities and stockholders' deficit	\$ 9,587	\$ 9,752

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(93) (93) \$(93)				
Net earnings	351	351	351	
Comprehensive income				\$258
Balance, July 31, 2000	3,547,123	35	10,327	1,460 (130) 11,692
Issuance of stock for legal settlement	32,812	1	50	51
Foreign currency translation adjustment net of tax				(294) (294) \$(294)
Net loss	(7,128)	(7,128)	(7,128)	
Comprehensive loss				\$(7,422)
Balance, July 31, 2001	3,579,935	36	10,377	(5,668) (424) 4,321
Foreign currency translation adjustment net of tax				199 199 \$199
Net earnings	1,673	1,673	1,673	
Comprehensive income				\$1,872
Balance, July 31, 2002	3,579,935	\$36	\$10,377	\$(3,995) \$(225) \$6,193

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

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(93) (93) \$(93) Net earnings 351 351 351 Comprehensive income

SI TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

Year ended July 31,
(In Thousands Except Share Data)

	<u>2002</u>	<u>2001</u>	<u>2000</u>
Cash flows from operating activities:			
Net earnings (loss)	\$ 1,673	\$ (7,128)	\$ 351
Adjustments to reconcile net earnings (loss) to net cash provided by operating activities:			
Depreciation and amortization	1,017	1,530	1,860
Restructuring charges		3,844	
Goodwill impairment loss		2,000	
Deferred lease costs	(209)	(248)	(205)
Deferred income taxes	(557)	810	212
Non-cash common stock and options expenses		51	33
Changes in operating assets and liabilities:			
Trade accounts receivable	410	1,177	1,605
Inventories	(1,081)	142	1,220
Income taxes receivable/payable	404	(255)	145
Other current assets	(29)	54	(215)
Accounts payable	58	(76)	(235)
Accrued liabilities and customer advances	(776)	(869)	(1,776)
Net cash provided by operating activities	910	1,032	2,995
Cash flows from investing activities:			
Acquisition of intangibles and other assets		(296)	115
Purchase of property and equipment	(118)	(306)	(484)
Net cash used in investing activities	(118)	(602)	(369)
Cash flows from financing activities:			
Net borrowings (payments) on line of credit	258	1,404	(1,142)
Payments on long-term debt	(1,285)	(1,504)	(1,226)
Foreign currency translation adjustment	93	(62)	(178)
Net increase (decrease) in cash	(142)	268	80
Cash at beginning of year	380	112	32
Cash at end of year	\$ 238	\$ 380	\$ 112
Cash paid during the year for:			
Interest	\$ 904	\$ 1,405	\$ 1,823
Income taxes	\$	\$ 23	\$

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

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

July 31, 2002 and 2001

(In Thousands Except Share Data)

NOTE A SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

SI Technologies, Inc. (SI or Company) designs, manufactures and markets high performance industrial sensors, weighing and factory automation equipment, and related products. SI products incorporate devices, equipment and systems for the handling, inspection and measurement of goods and materials. Key markets served by SI include aerospace/aviation, food, forestry, manufacturing, mining, transportation/distribution and waste management. Additional disclosure regarding components of the Company's businesses is in Note N-Industry and Geographic Area Segment Information.

1. Principles of Consolidation

The consolidated financial statements include the accounts of SI Technologies, Inc. and its subsidiaries; AeroGo, Inc., Allegany Technology, Inc., Evergreen Weigh, Inc., NV Technology, Inc., Revere Transducers, Inc., Revere Transducers Europe B.V., AeroGo Export, Inc., and IDEAutomation International, Inc. All significant intercompany accounts and transactions have been eliminated in consolidation.

2. Revenue Recognition and Accounts Receivable

The Company recognizes revenue only when all of the four following criteria are met: 1) Persuasive evidence of an arrangement exists, usually in the form of a written purchase order; 2) Delivery has occurred (or a shipment has been made, depending upon the terms of the purchase order) or services have been rendered; 3) The Company's price to the buyer is fixed or determinable, usually evidenced by a written purchase order; and 4) Collectability is reasonably assured, based on credit evaluation and history with the customer.

Additionally, on long-term contracts, sales are recorded based on the percentage that incurred costs bear to the total estimated costs at completion. Estimated cost to complete is based on the budget, incurred cost, risk assessment of the cost, and is then adjusted for normal/historical variance of project actual versus budget. Estimated losses are recorded in total when they become evident. Such billings are generally made and collected in the subsequent year.

Accounts receivables are reviewed regularly by management and written off against the uncollectable reserve when it is determined that the account can not reasonably be expected to be collected. Reserve balances are determined by management through analysis on past payment history, and current financial status of the customers.

3. Inventories

Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out method. Uncompleted contracts are included in inventory at the accumulated cost of each contract not in excess of realizable value. Quantities on hand are evaluated compared to recent usage and recent changes in sales trends. Reserves for obsolescence and excess quantities are established based upon this evaluation.

4. Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Depreciation is provided in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives, principally on a straight-line basis. Leasehold improvements are amortized over the lives of the respective leases

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

or the service lives of the improvements, whichever is shorter. Estimated service lives of property and equipment are as follows:

Machinery and equipment	2 to 10 years
Buildings	35 years
Leasehold improvements	2 to 10 years

The straight-line method of depreciation is followed for substantially all assets for financial reporting purposes, while accelerated methods are used for tax purposes.

5. Intangible Assets

Intangible assets primarily represent the excess costs of acquiring subsidiaries over the fair value of net assets acquired at the date of acquisition, which are amortized using the straight-line method primarily over periods of 25 to 40 years. In accordance with Statement of Financial Accounting Standards No. 121 Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of, the Company periodically reviews goodwill to assess recoverability. Impairment is recognized in operating results if expected future operating discounted cash flows of the acquired business are less than the carrying value of goodwill. Accumulated amortization totaled \$1,506 and \$1,179 at July 31, 2002 and 2001, respectively.

As a result of the evaluation of its Allegany Technology subsidiary in connection with the 2001 restructuring plan, the Company recorded an impairment loss of \$2,000 in 2001. The impairment loss was determined based upon management's estimate of discounted cash flows from products acquired and incorporated in the Allegany Technology operation.

6. Product Warranty

Product warranty costs are estimated and accrued at the time sales are recorded and are based upon actual operating history and changes in product mix.

7. Comprehensive Income

Foreign currency assets and liabilities are translated into their U.S. dollar equivalents based on yearend exchange rates. Revenue and expense accounts are translated at average exchange rates for the appropriate fiscal year. Aggregate exchange gains and losses arising from the translation of foreign assets and liabilities are included in stockholders' equity. Transaction gains and losses are included in income and have not been significant in amount.

8. Use of Estimates

In preparing the Company's financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

9. Recent Accounting Pronouncements

On July 20, 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) 141, Business Combinations, and SFAS 142, Goodwill and Intangible Assets. SFAS 141 is effective for all business combinations completed after June 30, 2001. Major provisions of these Statements and their effective dates for the Company are as follows:

All business combinations initiated after June 30, 2001 must use the purchase method of accounting. The pooling of interests method of accounting is prohibited except for transactions initiated before July 1, 2001.

Intangible assets acquired in a business combination must be recorded separately from goodwill if they arise from contractual or other legal rights or are separable from the acquired entity and can be sold, transferred, licensed, rented or exchanged, either individually or as part of a related contract, asset or liability.

Goodwill, as well as intangible assets with indefinite lives, acquired after June 30, 2001, will not be amortized. Effective August 1, 2002, all previously recognized goodwill and intangible assets with indefinite lives would no longer be subject to amortization.

Effective August 1, 2002, goodwill and intangible assets with indefinite lives will be tested for impairment annually and whenever there is an impairment indicator.

All acquired goodwill must be assigned to reporting units for purposes of impairment testing and segment reporting.

The Company has continued to amortize goodwill and intangible assets recognized prior to July 1, 2001, under its current method until July 31, 2002, at which time annual and quarterly goodwill amortization of \$327 and \$82, respectively, and annual and quarterly amortization of \$39 and \$10, respectively, relating to intangible assets with indefinite lives will no longer be recognized. By July 31, 2003 the Company will have completed a transitional fair value based impairment test of goodwill as of August 1, 2002. By October 31, 2002 the Company will have completed a transitional impairment test of all intangible assets with indefinite lives. Impairment losses, if any, resulting from the transitional testing will be recognized in the quarter ended October 31, 2002, as a cumulative effect of a change in accounting principle.

In June 2001, the FASB issued SFAS 143, *Accounting for Asset Retirement Obligations*. SFAS 143 applies to all entities, including rate-regulated entities that have legal obligations associated with the retirement of a tangible long-lived asset that result from acquisition, construction, or development and (or) normal operations of the long-lived asset. The application of this Statement is not limited to certain specialized industries, such as the extractive or nuclear industries. This Statement also applies, for example, to a company that operates a manufacturing facility and has a legal obligation to dismantle its manufacturing plant and restore the underlying land when it ceases operation of that plant. Statement 143 is effective for financial statements issued for fiscal years beginning after June 15, 2002. Management believes the implementation of this standard will not have a material effect upon the Company's financial statements.

In August 2001, the FASB issued SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, to address significant implementation issues related to SFAS No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*, and to develop a single accounting model to account for long-lived assets to be disposed of. SFAS No. 144 supersedes SFAS No. 121, as well as the provisions of Opinion 30, *Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*, that address the

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

disposal of a segment of a business. SFAS 144 also amends ARB 51, *Consolidated Financial Statements*, to eliminate the exception to consolidate a subsidiary for which control is likely to be temporary. Management believes the implementation of this standard will not have a material effect upon the Company's financial statements.

In April 2002, the FASB issued SFAS 145, *Rescission of FASB Statements 4, 44, and 64, Amendment of FASB Statement 13, and Technical Corrections*. As described in the last paragraph of this Summary and in Section D, SFAS 145 has a May 15, 2002, effective date. SFAS 145 rescinds SFAS 4, *Reporting Gains and Losses from Extinguishment of Debt*, and SFAS 64, *Extinguishment of Debt Made to Satisfy Sinking-Fund Requirements*. Accordingly, a gain or loss from a debt extinguishment should not be classified as an extraordinary item unless it meets the criteria for extraordinary item classification in APB Opinion 30, *Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual, and Infrequently Occurring Events and Transactions*. SFAS 145 also rescinds SFAS 44, *Accounting for Intangible Assets of Motor Carriers*, because transition to the Motor Carrier Act of 1980 is complete and intrastate operating rights have been deregulated. Management believes the implementation of this standard will not have a material effect upon the Company's financial statements.

In June 2002, the FASB approved for issuance SFAS 146, *Accounting for Costs Associated with Exit or Disposal Activities*. This Statement provides financial accounting and reporting guidance for costs associated with exit or disposal activities and nullifies EITF Issue 94-3, *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)*. Statement 146 is effective for exit or disposal activities initiated after December 31, 2002. Early application is encouraged. Previously issued financial statements should not be restated. The provisions of EITF Issue 94-3 continue to apply for an exit activity initiated under an exit plan that met the criteria in EITF Issue 94-3 before the Statement's initial application. Management believes the implementation of this standard will not have a material effect upon the Company's financial statements.

NOTE B BUSINESS COMBINATIONS

1. *Revere Transducers*

Effective July 1, 1998, the Company purchased 100% of the common stock of Revere Transducers, Inc. and Revere Transducers Europe B.V. (jointly Revere) for \$8,282 in cash. Revere is engaged in the manufacture of industrial sensors and weighing equipment. The combination is accounted for under the purchase method of accounting. The fair value of net assets acquired exceeded the acquisition cost by \$250, which was adjusted in 1999 from \$552 for additional acquisition costs. This amount has been applied to reduce the fair value of recorded property and equipment. The purchase of Revere was funded by the issuance of notes payable to a bank as described in Note F. The net unamortized goodwill at July 31, 2002 was \$347.

2. *Allegany Technology, Inc.*

Effective July 1, 1998, the Company purchased 100% of the common stock of Allegany Technology, Inc. (Allegany) for \$2,888 in cash and SI common stock. Allegany is engaged in the manufacture of industrial sensors and weighing equipment and systems. The combination is accounted for under the purchase method of accounting. The excess of the total acquisition cost over the fair value of net assets acquired in the amount of \$3,000 which was adjusted in 1999 from \$2,811. The purchase of Allegany was funded by borrowings under the Company's line of credit and from the issuance of 142,219 shares of common stock. In 2001 the Company recorded a \$2,000 charge for goodwill impairment (see Note A). The remaining goodwill is being amortized on a straight-line basis over twenty-five years. The net unamortized goodwill at July 31, 2002 was \$3,052.

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. *AeroGo, Inc.*

Effective July 1, 1997, the Company purchased 100% of the common stock of AeroGo, Inc. (AeroGo) for \$6,000 in cash. AeroGo is engaged in the manufacture of load handling and factory automation equipment and systems. The combination is accounted for under the purchase method of accounting. The excess of the total acquisition cost over the fair value of net assets acquired in the amount of \$4,376 is being amortized on a straight-line basis over twenty-five years. The net unamortized goodwill at July 31, 2002 was \$3,486.

NOTE C INVENTORIES

Inventories consist of the following at July 31:

	<u>2002</u>	<u>2001</u>
Raw materials	\$ 4,767	\$ 4,354
Work in process	1,162	977
Finished goods	4,349	4,427
	<u>10,278</u>	<u>9,758</u>
Less reserve for excess and obsolete inventories	(613)	(1,174)
Inventories, net	<u>\$ 9,665</u>	<u>\$ 8,584</u>

During 2002, approximately \$293,000 of excess and obsolete inventory was disposed of during the year.

NOTE D PROPERTY AND EQUIPMENT

Property and equipment consists of the following at July 31:

	<u>2002</u>	<u>2001</u>
Machinery and equipment	\$ 4,301	\$ 5,851
Buildings	281	259
Leasehold improvements	244	221
	<u>4,826</u>	<u>6,331</u>
Less accumulated depreciation	(2,858)	(3,676)
Property and equipment, net	<u>\$ 1,968</u>	<u>\$ 2,655</u>

The Company abandoned certain assets having a cost of \$1,623 and \$2,950 and accumulated depreciation of \$1,470 and \$1,242 as of July 31, 2002 and 2001, respectively in connection with its restructuring plan (see Note P).

NOTE E ACCRUED LIABILITIES

Accrued liabilities consist of the following at July 31:

	<u>2002</u>	<u>2001</u>
Accrued salaries, wages and other compensation	\$ 767	\$ 1,001
Warranty reserve	271	224
Restructuring charges (see Note P)	360	1,281

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Deferred lease and rent cost - current	205	205
Other	832	546
	<u> </u>	<u> </u>
	\$ 2,435	\$ 3,257
	<u> </u>	<u> </u>

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE F DEBT

Debt consists of the following at July 31:

	<u>2002</u>	<u>2001</u>
1) Revolving line of credit with a bank for up to \$6,500 (\$8,000 in 2001) interest at the prime rate plus 2.75% (at July 31, 2002, totaling 7.5%), secured by the Company's trade accounts receivable, inventories and certain equipment. Principal and interest due November 2002. Utilized for U.S. operations	\$ 5,344	\$ 6,911
2) Revolving line of credit with a bank for up to \$2,212 (Euro 2,250), interest at the rate of 6.75%, secured by certain of the Company's trade accounts receivable, inventories and equipment. Interest only due quarterly. Utilized for European operations	1,956	1,631
3) Note payable to bank in monthly installments of \$56 plus interest at the prime rate plus 1.75% (totaling 6.5% at July 31, 2002), secured by substantially all of the Company's assets, due November 2005	4,712	5,972
4) Note payable to bank in monthly installments of \$25 plus interest at the prime rate plus 3.25%, secured by substantially all of the Company's assets, due November 2002	1,475	
	<u>13,487</u>	<u>14,514</u>
Less current maturities of debt	(9,448)	(14,514)
Long term debt	<u>\$ 4,039</u>	<u>\$</u>

As of July 31, 2002 the Company was not in default of any of its debt covenants.

In June 2002, the Company amended its principal credit agreement with its bank. The terms provide for a revolving line of credit up to a maximum of \$6,500 with interest at prime plus 2.75%, which had a balance of \$5,344 as of July 31, 2002. Monthly payments on the line are interest only with principal due November 30, 2002. The credit agreement provides a new term note for \$1,500 with interest at prime plus 3.25%, which has a balance outstanding as of July 31, 2002 of \$1,475. Monthly payments on the new term note are \$25 plus interest with principal due November 30, 2002. Monthly payments on the existing note payable of \$4,712 at July 31, 2002 are reduced to \$56 plus interest at prime plus 1.75%, with the remaining terms of the existing note unchanged. The line and both notes are secured by substantially all of the Company's assets and are cross-collateralized and cross-defaulted. The Company is required to maintain certain levels of earnings before interest, taxes, depreciation and amortization, tangible net worth and fixed charge coverage and may not pay any cash dividends under terms of the agreement.

Management believes the \$6,500 line of credit will be renewed in November 2002 at terms similar to the existing financing arrangements. Management also believes that the \$1,475 term loan will be extended with principal payments continuing at \$25 per month.

The maturities on long-term debt are as follows:

<u>Year ending July 31,</u>	
2003	\$ 2,148
2004	673
2005	673
2006	2,693
	<u>\$ 6,187</u>

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE G OTHER LIABILITIES

Other liabilities consist of the following at July 31:

	2002	2001
Deferred lease costs	\$ 186	\$ 345
Deferred rent	174	224
	<u>\$ 360</u>	<u>\$ 569</u>

Deferred lease costs arising from an acquisition represent the discounted operating lease costs for excess plant capacity acquired at the acquisition date totaling \$995. The deferred lease cost is amortized over 40 months, the remaining life of the lease. The deferred rent is attributable to escalating rental payments on the Tustin facility lease, which is accounted for using the straight line method of the total lease cost.

NOTE H FOREIGN CURRENCY TRANSLATION LOSS

In 2002 and 2001, respectively, the Company incurred a foreign currency translation gain (loss) of \$199 and (\$294) due to differences in the exchange rate between the US dollar and the Euro (Dutch Guilder-2001).

NOTE I COMMITMENTS AND CONTINGENCIES

1. Leases

The Company conducts a portion of its operations in leased facilities under noncancelable operating leases expiring at various dates through 2008. A portion of one manufacturing facility is subleased under a lease, which expires in 2004. At July 31, 2002, total future minimum sublease rentals for 2003 through 2005 amount to \$257.

The minimum rental commitments, excluding sublease income, under operating leases are as follows:

Year ending July 31,	
2003	\$ 1,166
2004	1,100
2005	421
2006	269
2007	108
	<u>\$ 3,064</u>

Rent expense under noncancelable operating leases was approximately \$713, \$726, and \$1,245 for the years ended July 31, 2002, 2001 and 2000, respectively. Sublease income was approximately \$119, \$113 and \$119 for the years ended July 31, 2002, 2001 and 2000, respectively. Portions of the rent expense for 2002 and 2001 were reduced by charges to the restructuring reserve.

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2. Consulting and Non-compete Agreements

Certain former executives of acquired companies entered into consulting and non-compete agreements with the Company. The consulting agreements have a term of five years and the non-compete agreements have terms ranging from two to ten years. The following table summarizes remaining obligations under these agreements:

Year ending July 31,		
2003	\$	63
2004		63
2005		63
2006		47
	\$	236

The expense associated with these agreements totaled \$123, \$288, and \$123 for the years ended July 31, 2002, 2001 and 2000, respectively.

3. Litigation

The Company is engaged in various legal actions as of July 31, 2002. In the opinion of management, based upon the advice of counsel, the ultimate outcome of these actions will not have a material impact on the Company's consolidated financial statements.

NOTE J INCOME TAXES

The Company accounts for income taxes on the liability method as prescribed by Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes (SFAS 109).

Income tax benefit (expense) consists of the following for the year ended July 31:

	2002	2001	2000
Current (expense) benefit	\$ (17)	\$ 255	\$ (132)
Deferred (expense) benefit	557	(917)	(212)
	\$ 540	\$ (662)	\$ (344)

The income tax benefit (expense) reconciled to the tax computed at the statutory federal rate was as follows for the year ended July 31:

	2002	2001	2000
Tax at statutory rate	\$ (391)	\$ 2,198	\$ (231)
Valuation allowance	875	(1,915)	
Nondeductible goodwill	(134)	(975)	(191)
Credits and net operating losses utilized	156		
State and foreign taxes		137	47
State tax benefit from restructuring			41
Other	34	(107)	(10)
	\$ 540	\$ (662)	\$ (344)

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The components of deferred taxes included in the balance sheet are as follows at July 31:

	<u>2002</u>	<u>2001</u>
Deferred tax asset:		
Net operating loss carryforwards	\$ 222	\$ 222
Accrued vacation and warranty	440	198
Provision for bad debts	95	105
Inventory reserve and capitalized overhead	218	428
Asset write-downs	902	771
Abandoned facility costs	245	366
Employee termination costs		99
Deferred lease costs		79
Other	15	
	<u>1,915</u>	<u>2,268</u>
Valuation allowance	(1,040)	(1,915)
	<u>875</u>	<u>353</u>
Deferred tax liability:		
Excess of tax over book depreciation	(389)	(353)
Deferred state taxes	(40)	
	<u>(429)</u>	<u>(353)</u>
Net Deferred Tax Asset	<u>\$ 446</u>	<u>\$</u>

The valuation allowance was reduced by \$875 in 2002. The reduction of the valuation allowance was a result of the Company's profitability in the current year and estimated profitability in the future year. However, management continues to provide a valuation allowance due to the uncertainty of future taxable results and recoverability of the remaining deferred tax assets.

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE K STOCK OPTION PLAN

The Company implemented a stock option plan in 1995 (the Plan) and has authorized a total of 600,000 shares of common stock to be granted under the Plan. The Company had 147,500 shares available to grant under the Plan at July 31, 2002. Additionally, options to purchase 115,000 shares are outstanding under the old stock option plan that expired July 31, 1994. The vesting period and expiration dates of the stock options are at the discretion of the Board of Directors, and range up to five years.

The Company has adopted only the disclosure provisions of Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation (SFAS 123). In accounting for its plans the Company applies APB Opinion No. 25, Accounting for Stock Issued to Employees, which does not require recognition of compensation expense due to options being granted at fair value on the date of grant. If the Company had elected to recognize compensation expense based upon the fair value at the grant date for awards under these plans consistent with the methodology prescribed by SFAS 123, the Company's net earnings (loss) and earnings (loss) per share would be adjusted to the pro forma amounts indicated below:

	<u>2002</u>	<u>2001</u>	<u>2000</u>
Net earnings (loss):			
As reported	\$ 1,673	\$ (7,128)	\$ 351
Pro forma	1,600	(7,279)	225
Earnings per common share:			
As reported basic	\$.47	\$ (2.00)	\$.10
Pro forma	\$.45	\$ (2.04)	\$.06
As reported diluted	\$.47	\$ (2.00)	\$.09
Pro forma	\$.45	\$ (2.04)	\$.06

These pro forma amounts may not be representative of future disclosures because they do not take into effect pro forma compensation expense related to grants made before 1996.

The fair value of these options was estimated at the date of grant using the Black-Scholes option-pricing model with the following assumptions for the periods ending July 31, 2002, 2001 and 2000, respectively: dividend yields are nil, expected volatility of 69%, 64% and 61% percent; risk-free interest rate of 4.05%, 4.84% and 5.83%; and an expected option life of 5 years. The weighted-average fair value of options granted during the periods ending July 31, 2002, 2001 and 2000, for which the weighted average exercise price equals the market price on the grant date was \$.88, \$1.47, and \$1.34, respectively.

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables summarize information concerning currently outstanding and exercisable stock options:

	Stock Options Outstanding	Weighted-Average Exercise Price
Balance, July 31, 1999	428,500	\$ 3.00
Granted	70,000	\$ 2.34
Exercised		\$
Expired/canceled	(31,000)	\$ 3.49
Balance, July 31, 2000	467,500	\$ 2.89
Granted	100,000	\$ 1.94
Exercised		\$
Expired/canceled		\$
Balance, July 31, 2001	567,500	\$ 2.72
Granted	170,000	\$ 1.13
Exercised		\$
Expired/canceled	(75,000)	\$ 1.81
Balance, July 31, 2002	662,500	\$ 2.42

Range of Exercise Prices	Number of Shares Outstanding As of July 31, 2002	Weighted-Average Remaining Contractual Life in Years	Weighted-Average Exercise Price
\$1-\$2	340,000	5.2	\$ 1.44
\$2-\$3	165,000	6.7	\$ 2.41
\$3-\$4	500	3.3	\$ 3.25
\$4-\$5	157,000	4.5	\$ 4.53
	662,500		

Range of Exercise Prices	Number of Shares Exercisable as of July 31, 2002	Weighted-Average Exercise Price
\$1-\$2	190,000	\$ 1.69
\$2-\$3	157,000	\$ 2.41
\$3-\$4	500	\$ 3.25
\$4-\$5	147,000	\$ 4.52
	494,500	

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE L EARNINGS PER SHARE

The Company uses Statement of Financial Accounting Standards (SFAS) No. 128, Earnings per Share which established standards for computing and presenting earnings per share (EPS). Earnings per share are based on the average number of shares outstanding during each period and income available to common shareholders. Earnings per share assuming dilution is based on the assumption that outstanding stock options and warrants were exercised. Anti-dilutive options are excluded from the computation of diluted earnings per share.

The table below presents the information used to compute earnings (loss) per common share, with and without dilution:

	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
For the Year Ended July 31, 2002			
Earnings available to common stockholders	\$ 1,673	3,579,935	\$.47
Effect of dilutive securities			
Stock options		4,636	
Earnings per common share assuming dilution			
Earnings available to common stockholders and effect of assumed conversions	\$ 1,673	3,584,571	\$.47
For the Year Ended July 31, 2001			
Loss available to common stockholders	\$ (7,128)	3,563,529	\$ (2.00)
For the Year Ended July 31, 2000			
Earnings available to common stockholders	\$ 351	3,547,123	\$.10
Effect of dilutive securities			
Stock options		160,318	
Earnings per common share assuming dilution			
Earnings available to common stockholders and effect of assumed conversions	\$ 351	3,707,441	\$.09

The computation of loss per share assuming dilution for the year ended July 31, 2001 was anti-dilutive and excluded 567,500 outstanding stock options.

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE M INDUSTRY AND GEOGRAPHIC AREA SEGMENT INFORMATION

The Company applies the principles of SFAS No. 131, Disclosure about Segments of an Enterprise and Related Information. The Company operates in two reportable business segments (1) industrial measurement, and (2) industrial automation. The Company's reportable segments are strategic business units that offer different products. They are managed separately based on the fundamental differences in their operations. The accounting policies of the segments are the same as those described in Note A Summary of Significant Accounting Policies.

For 2002, approximately 76% of the American sales are within the United States, and 6% are within Canada. European sales are primarily United Kingdom, and France. No single customer or control group represents more the 10% of total sales.

Included in the industrial measurement segment are industrial sensors and controls products consisting of a wide range of NTEP and OIML approved, EX, Factory Mutual and IP rated load cells, transducers, translators and sensors. When matched with microprocessor-controlled digital electronics, they measure forces such as pressure, weight, mass and torque. Weighing Systems products constitute the combination of load cells and microprocessor-controlled digital electronics that in combination provide for an integrated system providing weight data in both dynamic and static industrial weighing applications

The industrial automation segment consists of load handling, moving and positioning equipment and systems for applications in manufacturing, construction and other environments in which heavy bulky materials are being transported and positioned.

Foreign Operations

	<u>2002</u>	<u>2001</u>	<u>2000</u>
Identifiable Assets:			
Americas	\$ 21,102	\$ 21,812	\$ 28,649
Europe	4,680	4,098	4,369
Sales:			
Americas	23,946	27,566	31,549
Europe	8,667	8,725	9,780
Operating Profit (Loss):			
Americas	1,416	(5,578)	1,897
Europe	527	665	602

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Segment Information 2002

	<u>Industrial Measurement</u>	<u>Industrial Automation</u>	<u>SI Consolidated</u>
Year ended July 31, 2002:			
Sales	\$ 25,407	\$ 7,206	\$ 32,613
Cost of goods sold	16,827	4,067	20,894
Gross profit	8,580	3,139	11,719
Gross profit %	34%	44%	36%
Operating expenses	7,247	2,529	9,776
Operating profit	1,333	610	1,943
Interest expense			(904)
Other income, net			94
Earnings before income taxes			1,133
Income tax benefit			540
Net earnings			\$ 1,673
Assets	\$ 21,147	\$ 4,635	\$ 25,782

Segment Information 2001

	<u>Industrial Measurement</u>	<u>Industrial Automation</u>	<u>SI Consolidated</u>
Year ended July 31, 2001:			
Sales	\$ 28,289	\$ 8,002	\$ 36,291
Cost of goods sold	19,994	4,348	24,342
Gross profit	8,295	3,654	11,949
Gross profit %	29%	46%	33%
Operating expenses	8,363	2,655	11,018
Restructuring charges	3,844		3,844
Goodwill impairment	2,000		2,000
Total expense	14,207	2,655	16,862
Operating profit (loss)	(5,912)	999	(4,913)
Interest expense			(1,564)
Other income, net			11
Loss before income taxes			(6,466)
Income tax expense			(662)
Net loss			\$ (7,128)
Assets	\$ 20,542	\$ 5,368	\$ 25,910

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Segment Information 2000

	<u>Industrial Measurement</u>	<u>Industrial Automation</u>	<u>SI Consolidated</u>
Year ended July 31, 2000:			
Sales	\$ 31,947	\$ 9,382	\$ 41,329
Cost of goods sold	21,678	5,048	26,726
Gross profit	10,269	4,334	14,603
Gross profit %	32%	46%	35%
Operating expenses	8,599	3,505	12,104
Operating profit	1,670	829	2,499
Interest expense			(1,860)
Other income, net			56
Loss before income taxes			695
Income tax expense			(344)
Net loss			\$ 351
Assets	\$ 26,863	\$ 6,155	\$ 33,018

NOTE N BENEFIT PLANS

The Company has defined contribution 401(k) plans for each subsidiary. All employees are eligible for participation upon completion of a waiting period. The contribution expense associated with these plans totaled approximately \$26, \$162, and \$142 for the years ended July 31, 2002, 2001 and 2000, respectively. The Company's matching contribution was decreased in 2002.

NOTE O FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company's financial instruments include cash, accounts receivable, accounts payable, customer advances, accrued liabilities, and short and long-term debt. Management has determined that the fair value of cash, accounts receivable, accounts payable, customer advances, accrued liabilities, and short-term debt approximate the carrying values due to the short-term nature of these instruments.

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE P RESTRUCTURING CHARGE

During the quarter ended April 30, 2001, the Company began implementing a restructuring plan involving consolidation of two of its subsidiaries, Allegany Technology and Revere Transducers. Approved by the Company's Board of Directors on May 7, 2001, this plan to consolidate operations was necessitated by worsening revenue trends in some of the Company's key markets and consists of several elements, including: (1) reduction of manufacturing capacity by abandoning and/or downsizing facilities, (2) disposing of redundant assets, (3) termination of approximately 50 employees, and (4) outsourcing a significant portion of the combined operation's higher volume products. A charge for restructuring of \$3,480 was recorded as of April 30, 2001. The restructuring charge was increased by \$364 in the fourth quarter ended July 31, 2001 to accrue for additional disposition of fixed assets and employee severance costs arising from management's decision to further utilize offshore manufacturing sources. The components of the restructuring charge are as follows:

<u>Restructuring Category:</u>	<u>Year ended July 31, 2001</u>
Write-down of redundant and abandoned assets	\$ 2,168
Abandoned facilities costs, primarily lease payments	1,225
Employee termination costs	379
Other	72
Total estimated restructuring charge	\$ 3,844

Through the end of 2002, the Company's restructuring costs have approximated the Plan above. The Company has readied the Maryland facility for sale or sublet, and is currently actively marketing it. The Company has accrued \$360,000 for lease costs on Maryland through May 2006, and on Tustin through September 2004. The Company has completed implementation of the restructuring plan with the exception of relocating the Tustin operations to a new facility. The relocation will occur in September 2004 unless suitable sub-tenant arrangements can be negotiated before the termination of the lease at that time.

SI TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE Q Selected Quarterly Financial Data (unaudited)

The following table sets forth selected quarterly financial data for the eight quarters ended July 31:

	Quarter Ended			
	October 31, 2001	January 31, 2002	April 30, 2002	July 31, 2002
Revenue	\$ 8,536	\$ 8,014	\$ 7,759	\$ 8,304
Gross Profit	2,978	2,783	2,691	3,267
Earnings from operations	570	441	393	539
Net earnings	353	166	197	957
Net income per share, basic	\$.10	\$.05	\$.05	\$.27
Net income per share, diluted	\$.10	\$.05	\$.05	\$.27

Fourth quarter results reflect recognition of deferred tax benefits of \$557.

	October 31, 2000	January 31, 2001	April 30, 2001	July 31, 2001
Revenue	\$ 9,893	\$ 9,622	\$ 8,377	\$ 8,399
Gross Profit	3,250	3,388	2,649	2,662
Earnings (loss) from operations	428	556	(5,647)	(250)
Net income (loss)	(59)	19	(5,490)	(1,598)
Net income (loss) per share, basic	\$ (.02)	\$.01	\$ (1.55)	\$ (.44)
Net income (loss) per share, diluted	\$ (.02)	\$.01	\$ (1.55)	\$ (.44)

CERTIFICATES

I, Rick A. Beets, certify that:

- 1) I have reviewed this annual report on Form 10-K of SI Technologies;
- 2) Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
- 3) Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

Date: October 31, 2002

/s/ RICK A. BEETS

Rick A. Beets
President, CEO and CFO

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
(SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002)**

In connection with the Annual Report of SI Technologies, Inc. (the Company) on Form 10-K for the period ending July 31, 2002 as filed with the Securities and Exchange Commission on the date hereof (the Report), I, Rick A. Beets, President, Chief Executive Officer and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, that:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ RICK A. BEETS

Rick A. Beets
President, Chief Executive Officer, CFO

October 31, 2002