EMC CORP
Form 10-Q/A
August 10, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q/A

Amendment No. 1

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended June 30, 2006

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For transition period from ______ to ______

Commission File Number 1-9853

EMC CORPORATION

(Exact name of registrant as specified in its charter)

Massachusetts	**04-2680009**
(State or other jurisdiction of	(I.R.S. Employer
incorporation or organization)	Identification Number)
176 South Street	**01748**

Hopkinton, Massachusetts
(Address of principal executive offices) (Zip Code)

(508) 435-1000

(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 x No ¨

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

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

The number of shares of common stock, par value $.01 per share, of the registrant outstanding as of June 30, 2006 was 2,298,487,844.

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Amendment No. 1 to the Quarterly Report on Form 10-Q for the

Quarterly Period Ended June 30, 2006

EXPLANATORY NOTE

We are filing this Amendment No. 1 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006, as filed with the Securities and Exchange Commission on August 4, 2006, to correct the following typographical errors: p. 12 Amounts charged to the accrual for the Six Months Ended June 30, 2006 should read (58,707), p. 14 end of last sentence under *Employee Stock Purchase Plan* should read $52.6 million and $49.2 million, respectively, p. 17 Total Stock-Based Compensation for the Six Months Ended June 30, 2006 in Cost of product sales should read 22,964, p. 23 Consolidated Cost of Sales for the Six Months Ended June 30, 2006 should read 2,433,875, p. 24 last sentence in the third paragraph under *Defined Benefit Pension Plans* should read At June 30, 2006, the Pension Plan held $0.3 million of our common stock, p. 30 % Change for the Three Months Ended June 30, 2006 and June 30, 2005 for the Total cost of revenue should read 11.8, p. 31 $ Change for the Six Months Ended June 30, 2006 and June 30, 2005 for Net income should read $(11.7), p. 36 the next to last sentence in the second paragraph under *Financial Condition* should read Net purchases and maturities of investments were $266.1 and $115.0 for the six months ended June 30, 2006 and 2005, respectively and p. 37 next to last sentence in the first paragraph should read Under the terms of the agreement, we will pay $28.00 per share in cash in exchange for each share of RSA for an aggregate purchase price of approximately $2,100.0, net of RSA s existing cash balance. In addition, in Management s Discussion and Analysis of Financial Condition and Results of Operations, we have adjusted various numbers due to rounding and clarified in two instances that a period over period percentage change was not measurable.

Other than the changes referred to above, all other information in our Form 10-Q described above remains unchanged. This amendment does not reflect events occurring after the original filing of such Form 10-Q and does not modify or update the disclosures in any way other than to correct the typographical errors described above.

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EMC CORPORATION

FACTORS THAT MAY AFFECT FUTURE RESULTS

This Quarterly Report on Form 10-Q contains forward-looking statements, within the meaning of the Federal securities laws, about our business and prospects. The forward-looking statements do not include the impact of the definitive agreement to acquire all of the outstanding capital stock of RSA Security Inc., which we announced on June 29, 2006, or of any other potential mergers, acquisitions, divestitures or business combinations that may be announced or closed after the date hereof. Any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words believes, plans, intends, expects, goals and sim expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these words. Our future results may differ materially from our past results and from those projected in the forward-looking statements due to various uncertainties and risks, including those described in Item 1A of Part II (Risk Factors). We disclaim any obligation to update any forward-looking statements contained herein after the date of this Quarterly Report.

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PART I

FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

EMC CORPORATION

CONSOLIDATED BALANCE SHEETS

(in thousands, except per share amounts)

(unaudited)

ASSETS	June 30, 2006	December 31, 2005
Current assets:		
Cash and cash equivalents	$ 1,560,384	$ 2,322,370
Short-term investments	1,237,614	1,615,495
Accounts and notes receivable, less allowance for doubtful accounts of $36,109 and $38,126	1,264,519	1,405,564
Inventories	763,771	724,751
Deferred income taxes	348,122	326,318
Other current assets	239,963	179,478
Total current assets	5,414,373	6,573,976
Long-term investments	3,487,049	3,417,589
Property, plant and equipment, net	1,836,399	1,754,035
Intangible assets, net	555,726	563,024
Other assets, net	649,389	598,252
Goodwill, net	4,114,928	3,883,507
Total assets	$ 16,057,864	$ 16,790,383
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 616,686	$ 583,756
Accrued expenses	1,245,708	1,279,857
Income taxes payable	420,334	645,694
Deferred revenue	1,269,613	1,164,551
Total current liabilities	3,552,341	3,673,858
Deferred revenue	690,773	640,598
Deferred income taxes	122,335	175,192
Long-term convertible debt		126,963
Other liabilities	116,740	108,342
Commitments and contingencies		
Stockholders equity:		
Series preferred stock, par value $0.01; authorized 25,000 shares; none outstanding		
Common stock, par value $0.01; authorized 6,000,000 shares; issued and outstanding 2,298,488 and 2,384,147 shares	22,985	23,841
Additional paid-in capital	4,506,133	5,867,076
Deferred compensation		(332,311)
Retained earnings	7,122,060	6,570,511
Accumulated other comprehensive loss, net	(75,503)	(63,687)

Total stockholders equity	11,575,675	12,065,430
Total liabilities and stockholders equity	$ 16,057,864	$ 16,790,383

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

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EMC CORPORATION

CONSOLIDATED INCOME STATEMENTS

(in thousands, except per share amounts)

(unaudited)

	For the Three Months Ended June 30, 2006	For the Three Months Ended June 30, 2005	For the Six Months Ended June 30, 2006	For the Six Months Ended June 30, 2005
Revenues:				
Product sales	$ 1,833,598	$ 1,688,330	$ 3,682,128	$ 3,308,833
Services	740,925	656,485	1,443,082	1,279,113
	2,574,523	2,344,815	5,125,210	4,587,946
Costs and expenses:				
Cost of product sales	884,741	813,080	1,802,638	1,611,619
Cost of services	331,790	275,093	631,237	545,464
Research and development	299,429	253,342	582,918	487,639
Selling, general and administrative	782,016	642,654	1,530,240	1,258,400
Restructuring and other special charges	12,024		10,830	968
Operating income	264,523	360,646	567,347	683,856
Investment income	61,713	43,494	123,516	86,489
Interest expense	(621)	(1,983)	(2,631)	(4,016)
Other income (expense), net	479	(1,069)	3,195	(3,373)
Income before taxes	326,094	401,088	691,427	762,956
Income tax provision	47,001	107,724	136,506	199,758
Income before cumulative effect of a change in accounting principle	279,093	293,364	554,921	563,198
Cumulative effect of a change in accounting principle, net of tax benefit of $0, $0, $808 and $0			(3,372)	
Net income	$ 279,093	$ 293,364	$ 551,549	$ 563,198
Net income per weighted average share, basic:				
Income before cumulative effect of a change in accounting principle	$ 0.12	$ 0.12	$ 0.24	$ 0.24
Cumulative effect of a change in accounting principle				
Net income	$ 0.12	$ 0.12	$ 0.24	$ 0.24
Net income per weighted average share, diluted:				
Income before cumulative effect of a change in accounting principle	$ 0.12	$ 0.12	$ 0.23	$ 0.23
Cumulative effect of a change in accounting principle				
Net income	$ 0.12	$ 0.12	$ 0.23	$ 0.23
Weighted average shares, basic	2,306,457	2,391,826	2,328,360	2,393,658

Weighted average shares, diluted	2,341,785	2,442,359	2,371,301	2,442,897

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

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EMC CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	For the Six Months Ended	
	June 30, 2006	June 30, 2005
Cash flows from operating activities:		
Cash received from customers	$ 5,423,035	$ 4,722,463
Cash paid to suppliers and employees	(4,124,686)	(3,761,901)
Dividends and interest received	134,906	111,090
Interest paid	(2,696)	(5,107)
Income taxes paid	(401,357)	(37,721)
Net cash provided by operating activities	1,029,202	1,028,824
Cash flows from investing activities:		
Additions to property, plant and equipment	(316,120)	(253,652)
Capitalized software development costs	(96,074)	(82,536)
Purchases of short and long-term available for sale securities	(3,486,712)	(4,822,195)
Sales and maturities of short and long-term available for sale securities	3,752,790	4,937,156
Business acquisitions, net of cash acquired	(296,730)	(262,125)
Other	(13,910)	(2,100)
Net cash used in investing activities	(456,756)	(485,452)
Cash flows from financing activities:		
Issuance of common stock	129,897	136,845
Purchase of treasury stock	(1,375,608)	(270,906)
Excess tax benefits from stock-based compensation	9,727	
Payment of long-term and short-term obligations	(127,396)	(88)
Proceeds from long-term and short-term obligations	85	192
Net cash used in financing activities	(1,363,295)	(133,957)
Effect of exchange rate changes on cash and cash equivalents	28,863	(33,775)
Net (decrease) increase in cash and cash equivalents	(761,986)	375,640
Cash and cash equivalents at beginning of period	2,322,370	1,476,803
Cash and cash equivalents at end of period	$ 1,560,384	$ 1,852,443
Reconciliation of net income to net cash provided by operating activities:		
Net income	$ 551,549	$ 563,198
Adjustments to reconcile net income to net cash provided by operating activities:		
Cumulative effect of a change in accounting principle	3,372	
Depreciation and amortization	364,641	316,516
Non-cash restructuring and other special charges	12,410	3,100

Stock-based compensation expense	201,938	34,393
Provision for doubtful accounts	866	3,748
Deferred income taxes, net	(67,065)	24,312
Tax benefit from stock options exercised		30,659
Excess tax benefits from stock-based compensation	(9,727)	
Other	14,977	24,618
Changes in assets and liabilities, net of acquisitions:		
Accounts and notes receivable	147,483	22,750
Inventories	(19,999)	(167,209)
Other assets	(72,514)	(10,630)
Accounts payable	22,884	(62,700)
Accrued expenses	(76,886)	37,416
Income taxes payable	(198,018)	107,756
Deferred revenue	149,476	108,019
Other liabilities	3,815	(7,122)
Net cash provided by operating activities	$ 1,029,202	$ 1,028,824
Non-cash activity:		
Issuance of stock options exchanged in business combinations	$ 7,500	$ 37,360

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

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EMC CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

(unaudited)

	For the Three Months Ended June 30, 2006	For the Three Months Ended June 30, 2005	For the Six Months Ended June 30, 2006	For the Six Months Ended June 30, 2005
Net income	$ 279,093	$ 293,364	$ 551,549	$ 563,198
Other comprehensive income (loss), net of taxes:				
Foreign currency translation adjustments, net of taxes (benefit) of $0, $(8,797), $0 and $(10,716)	12,551	(9,857)	13,339	(14,114)
Changes in market value of derivatives, net of taxes (benefit) of $(3), $259, $(63) and $278	(24)	2,335	(568)	2,535
Changes in market value of investments, net of taxes (benefit) of $(2,512), $8,844, $(2,408) and $395	(11,132)	26,178	(24,587)	(4,689)
Other comprehensive income (loss)	1,395	18,656	(11,816)	(16,268)
Comprehensive income	$ 280,488	$ 312,020	$ 539,733	$ 546,930

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

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EMC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

Company

EMC Corporation (EMC) and its subsidiaries develop and deliver open, flexible information infrastructures, offering a wide range of systems, software, services and solutions that help organizations extract greater value from their information and get the most out of their IT assets.

EMC develops solutions for customers to manage information intelligently based on its changing value to an organization over time. With a strategy known as *information lifecycle management*, we help individuals and organizations store, manage, protect, secure, move and share information to collaborate, solve problems, save money, exploit new opportunities, comply with regulations and policies and improve operational results. Information lifecycle management simultaneously lowers the cost and reduces the risk of managing information, no matter what format it is in documents, images or e-mail as well as the data that resides in databases.

We also provide specialized *virtual infrastructure* and *resource management* software. Virtual infrastructure helps organizations respond to changing IT requirements by dynamically altering their computing and storage environments with flexible virtualization technologies. Resource management allows organizations to better understand, manage and automate the operation of their information infrastructure.

General

The accompanying interim consolidated financial statements are unaudited and have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. These statements include the accounts of EMC and its wholly-owned subsidiaries. All intercompany transactions have been eliminated in consolidation. Certain information and footnote disclosures normally included in our annual consolidated financial statements have been condensed or omitted. Accordingly, these interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2005 which are contained in our Annual Report on Form 10-K filed with the Securities and Exchange Commission (the SEC) on March 6, 2006.

The results of operations for the interim periods are not necessarily indicative of the results of operations to be expected for any future period or the entire fiscal year. The interim consolidated financial statements, in the opinion of management, reflect all adjustments (consisting of normal recurring accruals) necessary to fairly state the results as of and for the three and six month periods ended June 30, 2006 and 2005.

New Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109 (FIN No. 48). FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FAS No. 109, Accounting for Income Taxes. FIN No. 48 prescribes a two-step process to determine the amount of tax benefit to be recognized. First, the tax position must be evaluated to determine the likelihood that it will be sustained upon external examination. If the tax position is deemed more-likely-than-not to be sustained, the tax position is then assessed to determine the amount of benefit to recognize in the financial statements. The amount of the benefit that may be recognized is the largest amount that has a greater than 50 percent likelihood of being realized upon ultimate settlement. FIN No. 48 will be effective for us beginning in 2007. We are currently evaluating the potential impact of FIN No. 48 on our financial position and results of operations.

2. Business Acquisitions and Goodwill

Definitive Agreement to Acquire RSA Security Inc.

As of June 29, 2006, we entered into a definitive agreement to acquire all of the outstanding capital stock of RSA Security Inc. (RSA). Under the terms of the agreement, we will pay $28.00 per share in cash in exchange for each share of RSA for an aggregate purchase price of approximately $2.1 billion, net of RSA s existing cash balance. RSA provides technologies to secure

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EMC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

information no matter where it resides or travels inside or outside of an organization and throughout its lifecycle. With industry-leading authentication, access control, and encryption solutions, RSA helps organizations of all sizes ensure the authenticity and protection of people, information and transactions. The acquisition will add industry-leading identity and access management solutions and encryption and key management software to our product offerings. The acquisition is expected to be completed late in the third quarter or early in the fourth quarter of 2006, subject to customary closing conditions and regulatory approvals.

Acquisitions

In May 2006, we acquired all of the outstanding capital stock of Kashya, Inc. (Kashya), a provider of enterprise-class data replication and data protection software. Kashya will allow us to expand our software portfolio for replication across heterogeneous environments.

In May 2006, we acquired all of the outstanding capital stock of Interlink Group, Inc. (Interlink), an IT professional services firm that specializes in application development, IT infrastructure, enterprise integration, enterprise content management and customer relationship management for Microsoft environments. The acquisition of Interlink strengthens and expands our growing Microsoft solutions practice.

In June 2006, we acquired all of the outstanding capital stock of nLayers Ltd. (nLayers), a leader in application discovery and mapping software. The acquisition further expands our resource management portfolio, enabling automated comprehensive root-cause and impact analysis across all technology domains, including networks, applications and storage.

In June 2006, we acquired the assets of ProActivity Software Solutions Ltd. (ProActivity), a provider of content management software for business process management. ProActivity provides tools to monitor, analyze and optimize business processes. The acquisition further expands the EMC Documentum product suite s process modeling, process execution and process integration capabilities.

In June 2006, our VMware subsidiary acquired all of the outstanding capital stock of Akimbi Systems, Inc. (Akimbi), a developer of software that builds upon and leverages virtualization technology to improve the efficiency and effectiveness of enterprise application development operations and the IT organizations that support them. Through the acquisition of Akimbi, we intend to enhance our capabilities for virtualizing information by providing virtualization solutions to the development and test environments.

The aggregate purchase price, net of cash received for these acquisitions was $287.8 million, which consisted of $274.8 million of cash, $7.5 million in fair value of our vested stock options issued in exchange for the acquirees stock options and $5.5 million of transaction costs, which primarily consisted of fees paid for legal and financial advisory services.

The following represents the aggregate allocation of the purchase price for the aforementioned companies to intangible assets (table in thousands):

Developed technology (weighted-average useful life of 5.1 years)	$ 47,747
Customer/service relationships (weighted-average useful life of 6.6 years)	3,200
Tradenames and trademarks (weighted-average useful life of 0.5 years)	26
Non-competition agreements (weighted-average useful life of 3.0 years)	200
Backlog (weighted-average useful life of 2.0 years)	919
Acquired IPR&D	12,410
Total intangible assets	$ 64,502

The fair value of intangible assets was primarily based upon the income approach. The rates used to discount the net cash flows to their present values for each acquisition were based upon weighted average costs of capital that ranged from 5.3% - 25.0%. The discount rates were determined after consideration of market rates of return on debt and equity capital, the weighted average returns on invested capital and the risk associated with achieving forecasted sales related to the technology and assets acquired. The total weighted average amortization period for the intangible assets is 5.1 years. The intangible assets are being amortized based upon the pattern in which the economic benefits of the intangible assets are being utilized.

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EMC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Of the $64.5 million of acquired intangible assets, $12.4 million was allocated to IPR&D which was written off at the respective date of acquisition because the IPR&D had no alternative uses and had not reached technological feasibility. The write-off is included in restructuring and other special charges in our income statement. The value assigned to IPR&D was determined utilizing the income approach by determining cash flow projections relating to identified IPR&D projects. The stage of completion of each in-process project was estimated to determine the discount rates to be applied to the valuation of the in-process technology. Based upon the level of completion and the risk associated with in-process technology, we applied discount rates that ranged from 22.0% - 35.0% to value the IPR&D projects acquired.

The combined effect of the above transactions to EMC s revenue, net income and basic and diluted net income per weighted average share as if the acquisitions occurred on January 1, 2005 is immaterial for the three and six months ended June 30, 2006 and 2005, respectively. As a result, pro forma information for these acquisitions is not presented.

Goodwill recognized in these transactions totaled $234.4 million, of which $6.3 million is deductible for income tax purposes. Changes in the carrying amount of goodwill, net, on a consolidated basis and by segment for the three and six months ended June 30, 2006 consist of the following (table in thousands):

	EMC Information Storage Products	EMC Multi-Platform Software	EMC Services	VMware	Other Businesses	Total
Balance, April 1, 2006	$ 552,766	$ 2,786,528	$ 20,548	$ 522,334	$	$ 3,882,176
Goodwill acquired	45,482	93,676	18,772	76,504		234,434
Tax deduction from exercise of stock options		(659)		(69)		(728)
Finalization of purchase price allocations		(13)	(659)	(282)		(954)
Balance, June 30, 2006	$ 598,248	$ 2,879,532	$ 38,661	$ 598,487	$	$ 4,114,928

	EMC Information Storage Products	EMC Multi-Platform Software	EMC Services	VMware	Other Businesses	Total
Balance, January 1, 2006	$ 552,766	$ 2,789,126	$ 19,098	$ 522,517	$	$ 3,883,507
Goodwill acquired	45,482	103,432	18,772	76,504		244,190
Tax deduction from exercise of stock options		(7,792)		(225)		(8,017)
Finalization of purchase price allocations		(5,234)	791	(309)		(4,752)
Balance, June 30, 2006	$ 598,248	$ 2,879,532	$ 38,661	$ 598,487	$	$ 4,114,928

3. Investments

Our investments are comprised primarily of debt securities that are classified as available for sale and recorded at their fair market values. Investments with remaining maturities of less than 12 months from the consolidated balance sheet date are classified as short-term investments. Investments with remaining maturities of more than 12 months from the consolidated balance sheet date are classified as long-term investments.

Unrealized gains and temporary losses on investments classified as available for sale are included as a separate component of stockholders equity, net of any related tax effect. Realized gains and losses are reflected in the income statement in investment income. As of June 30, 2006, we had total short and long-term investments of $4.7 billion.

EMC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Unrealized losses on investments at June 30, 2006 by investment category and length of time the investment has been in a continuous unrealized loss position are as follows (table in thousands):

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. government and agency obligations	$ 1,016,609	$ (11,556)	$ 367,570	$ (9,652)	$ 1,384,179	$ (21,208)
U.S. corporate debt securities	571,322	(6,767)	212,675	(5,277)	783,997	(12,044)
Asset and mortgage-backed securities	566,555	(7,492)	391,356	(10,208)	957,911	(17,700)
Bank loans	192,505	(892)	2,193	(23)	194,698	(915)
Municipal obligations	766,601	(8,871)	9,603	(411)	776,204	(9,282)
Foreign debt securities	5,893	(102)	36,629	(605)	42,522	(707)
Total	$ 3,119,485	$ (35,680)	$ 1,020,026	$ (26,176)	$ 4,139,511	$ (61,856)

We evaluate investments with unrealized losses to determine if the losses are other-than-temporary. The gross unrealized losses related to bank loans were due to changes in credit spreads. All other gross unrealized losses were due to changes in interest rates. We have determined that the gross unrealized losses at June 30, 2006 are temporary. In making this determination, we considered the loss as a percentage of the investments cost, the financial condition and near-term prospects of the issuers, the magnitude of the losses compared to the investments cost, the length of time the investments have been in an unrealized loss position and our ability to hold the investments to maturity.

4. Inventories

Inventories consist of (table in thousands):

	June 30, 2006	December 31, 2005
Purchased parts	$ 72,556	$ 56,803
Work-in-process	396,717	491,474
Finished goods	294,498	176,474
	$ 763,771	$ 724,751

5. Property, Plant and Equipment

Property, plant and equipment consists of (table in thousands):

	June 30, 2006	December 31, 2005
Furniture and fixtures	$ 160,592	$ 168,495
Equipment	2,489,946	2,249,054
Buildings and improvements	925,356	908,559
Land	108,533	105,906
Building construction in progress	118,251	108,524
	3,802,678	3,540,538
Accumulated depreciation	(1,966,279)	(1,786,503)
	$ 1,836,399	$ 1,754,035

Building construction in progress and land owned at June 30, 2006 include $93.1 million and $6.0 million, respectively, of facilities not yet placed in service that we are holding for future use.

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EMC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

6. Accrued Expenses

Accrued expenses consist of (table in thousands):

	June 30, 2006	December 31, 2005
Salaries and benefits	$ 486,110	$ 477,361
Product warranties	235,544	206,608
Restructuring (See Note 10)	106,195	154,613
Other	417,859	441,275
	$ 1,245,708	$ 1,279,857

Product Warranties

Systems sales include a standard product warranty. At the time of the sale, we accrue for systems warranty costs. The initial systems warranty accrual is based upon our historical experience and specific identification of systems requirements. Upon expiration of the initial warranty, we may sell additional maintenance contracts to our customers. Revenue from these additional maintenance contracts is deferred and recognized ratably over the service period. The following represents the activity in our warranty accrual for our standard product warranty (table in thousands):

	For the Three Months Ended		For the Six Months Ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
Balance, beginning of the period	$ 234,549	$ 209,595	$ 206,608	$ 180,758
Current year accrual	32,695	35,382	87,643	85,042
Amounts charged to the accrual	(31,700)	(27,185)	(58,707)	(48,008)
Balance, end of the period	$ 235,544	$ 217,792	$ 235,544	$ 217,792

The current quarter provision includes amounts accrued for systems at the time of shipment, adjustments within the quarter for changes in estimated costs for warranties on systems shipped in the quarter and changes in estimated costs for warranties on systems shipped in prior years. It is not practicable to determine the amounts applicable to each of the components. The provision for the three and six months ended June 30, 2006 includes $1.1 million and $23.1 million respectively associated with stock-based compensation expense as a result of the adoption of Financial Accounting Standard No. 123R, Share-Based Payment (FAS No. 123R). Included in the provision for the six months ended June 30, 2006 is $22.0 million which represents the cumulative effect adjustment recorded in connection with the adoption of FAS No. 123R.

7. Convertible Debt

On April 3, 2006, we redeemed the outstanding $125.0 million 4.5% Senior Convertible Notes due April 1, 2007 (the Notes) that we assumed in connection with the acquisition of Documentum in December 2003 for $126.1 million, based on a contractual redemption price of 100.9%.

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EMC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

8. Net Income Per Share

The reconciliation from basic to diluted earnings per share for both the numerators and denominators is as follows (table in thousands, except per share amounts):

	For the Three Months Ended June 30, 2006	June 30, 2005	For the Six Months Ended June 30, 2006	June 30, 2005
Numerator:				
Net income, as reported, basic	$ 279,093	$ 293,364	$ 551,549	$ 563,198
Adjustment for interest expense on convertible debt, net of taxes		643	643	1,286
Net income - diluted	$ 279,093	$ 294,007	$ 552,192	$ 564,484
Denominator:				
Basic weighted average common shares outstanding	2,306,457	2,391,826	2,328,360	2,393,658
Weighted common stock equivalents	35,328	41,477	33,885	40,183
Assumed conversion of convertible debt		9,056	9,056	9,056
Diluted weighted average shares outstanding	2,341,785	2,442,359	2,371,301	2,442,897

Options to acquire 194.9 million and 188.6 million shares of our common stock for the three and six months ended June 30, 2006, respectively, and options to acquire 64.1 and 81.8 million shares of our common stock for the three and six months ended June 30, 2005, respectively were excluded from the calculation of diluted earnings per share because of their antidilutive effect. The effect of our senior convertible debt assumed in connection with our acquisition of Documentum on the calculation of diluted net income per weighted average share for the three and six months ended June 30, 2006 and 2005 was calculated using the if converted method. We redeemed all of the outstanding senior convertible debt on April 3, 2006. See Note 7 for further information.

9. Stock-Based Compensation

Equity Plans

The EMC Corporation 2003 Stock Plan (the 2003 Plan) provides for the grant of stock options, stock appreciation rights, restricted stock and restricted stock units. The exercise price for a stock option shall not be less than 100% of the fair market value of our common stock on the date of grant. Options generally become exercisable in annual installments over a period of three to five years after the date of grant and expire ten years after the date of grant. Incentive stock options will expire no later than ten years after the date of grant. Restricted stock is common stock that is subject to a risk of forfeiture or other restrictions that will lapse upon satisfaction of specified conditions. Restricted stock units represent the right to receive shares of common stock in the future, with the right to future delivery of the shares subject to a risk of forfeiture or other restrictions that will lapse upon satisfaction of specified conditions. Awards of restricted stock or restricted stock units that vest only by the passage of time will not vest fully in less than three years after the date of grant. The 2003 Plan allows us to grant up to 200.0 million shares of common stock, no more than 60.0 million shares of which may be issued pursuant to awards of restricted stock or restricted stock units.

In addition to the 2003 Plan, we have three employee stock option plans (the 1985 Plan , the 1993 Plan , and the 2001 Plan). Under the terms of each of the three plans, the exercise price of incentive stock options issued must be equal to at least the fair market value of our common stock on the date of grant. In the event that non-qualified stock options are granted under the 1985 Plan, the exercise price may be less than the fair market value at the time of grant, but in the case of employees not subject to Section 16 of the Securities Exchange Act of 1934, not less than par value (which is $0.01 per share), and in the case of employees subject to Section 16, not less than 50% of the fair market value on the date of grant. In the event that non-qualified stock options are granted under the 1993 Plan or the 2001 Plan, the exercise price may be less than the fair market value at the time of grant but not less than par value.

A total of 748.0 million shares of common stock have been reserved for issuance under the above four plans.

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We have a stock option plan that provides for the grant of stock options to members of our Board of Directors (the Directors Plan). A total of 14.4 million shares of common stock have been reserved for issuance under the Directors Plan. The exercise price for each option granted under the Directors Plan will be at a price per share determined at the time the option is granted, but not less than 50% of the fair market value of common stock on the date of grant.

At June 30, 2006, there was an aggregate of approximately 86.1 million shares of common stock available for issuance pursuant to future grants under the 1985 Plan, the 1993 Plan, the 2001 Plan, the 2003 Plan and the Directors Plan.

We have, in connection with the acquisition of various companies, assumed the stock option plans of these companies. We do not intend to make future grants under any of such plans.

We utilize both authorized and unissued shares and treasury shares to satisfy all shares issued under our equity plans. Our Board of Directors has authorized the repurchase of 500.0 million shares of our common stock. For the three and six months ended June 30, 2006, we repurchased 78.3 million and 106.0 million shares of our common stock, respectively. Cumulatively, we have repurchased 238.5 million shares at a cost of $3.1 billion, leaving a remaining balance of 261.5 million shares authorized for future repurchases.

We plan to spend $3.0 billion in 2006 on common stock repurchases and the redemption of the Notes (see Note 7). Through the six months ended June 30, 2006, we have repurchased approximately $1.375 billion of our common stock and redeemed the Notes for $126.1 million.

Employee Stock Purchase Plan

Under our 1989 Employee Stock Purchase Plan (the 1989 Plan), eligible employees may purchase shares of common stock through payroll deductions at the lower of 85% of the fair market value of the stock at the time of grant or 85% of the fair market value at the time of exercise. Options to purchase shares are granted twice yearly, on January 1 and July 1, and are exercisable on the succeeding June 30 or December 31. There are 98.0 million shares approved to be issued under the 1989 Plan. For the six months ended June 30, 2006 and 2005, 5.6 million shares and 4.2 million shares, respectively, were purchased under the 1989 Plan at a purchase price per share of $9.32 and $11.65 respectively. Total cash proceeds from the purchase of shares under the 1989 Plan for the six months ended June 30, 2006 and 2005 were $52.6 million and $49.2 million, respectively.

Stock Options

The following tables summarize our option activity under all equity plans for the three and six months ended June 30, 2006 and 2005 as follows (shares in thousands):

	Number of Shares	Wtd. Avg. Exercise Price
Outstanding, January 1, 2006	296,250	$ 17.78
Granted	3,171	13.56
Forfeited	(2,730)	12.69
Expired	(1,519)	33.11
Exercised	(8,938)	7.02
Outstanding, March 31, 2006	286,234	18.04
Options granted relating to business acquisitions	1,190	0.53
Granted	3,028	13.37
Forfeited	(1,907)	12.58

Expired	(1,105)		35.14
Exercised	(2,410)		6.26
Outstanding, June 30, 2006	285,030	$	18.00

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	Number of Shares	Wtd. Avg. Exercise Price
Outstanding, January 1, 2005	275,341	$ 18.02
Options granted relating to business acquisitions	3,938	5.17
Granted	2,186	12.88
Forfeited	(3,061)	15.70
Expired	(2,004)	37.34
Exercised	(6,281)	5.90
Outstanding, March 31, 2005	270,119	17.96
Granted	1,201	12.72
Forfeited	(1,694)	14.74
Expired	(934)	35.79
Exercised	(7,792)	6.82
Outstanding, June 30, 2005	260,900	$ 18.26

The total pre-tax intrinsic value of options exercised during the three months ended June 30, 2006 and 2005 was $16.2 million and $53.4 million, respectively, and was $78.2 million and $98.1 million for the six months ended June 30, 2006 and 2005, respectively. Cash proceeds from the exercise of stock options were $14.7 million and $53.1 million for the three months ended June 30, 2006 and June 30, 2005, respectively. Cash proceeds from the exercise of stock options were $77.3 million and $87.6 million for the six months ended June 30, 2006 and June 30, 2005, respectively. Income tax benefits realized from the exercise of stock options during the three months ended June 30, 2006 and 2005 were $8.5 million and $16.6 million, respectively, and were $27.3 million and $30.9 million for the six months ended June 30, 2006 and 2005, respectively.

Summarized information about stock options outstanding that are expected to vest and stock options exercisable at June 30, 2006 is as follows (shares and intrinsic values in thousands):

	Options Outstanding and Expected to Vest				Options Exercisable			
Range of Exercise Price	Number of Options	Weighted Avg. Remaining Contractual Life	Weighted Avg. Exercise Price	Aggregate Intrinsic Value	Number of Options	Weighted Avg. Remaining Contractual Life	Weighted Avg. Exercise Price	Aggregate Intrinsic Value
$ 0.01-$ 4.12	7,793	4.4	$ 1.81	$ 71,384	6,935	4.3	$ 1.96	$ 62,484
$ 4.13-$ 9.27	45,139	5.1	6.04	222,535	31,596	4.8	6.27	148,501
$ 9.28-$13.91	118,612	6.6	12.26	3,415	58,498	5.5	12.10	2,662
$13.92-$20.87	52,984	7.5	14.06		10,304	4.8	16.92	
$20.88-$31.31	1,792	2.8	26.69		1,792	2.8	26.69	
$31.32-$46.97	24,612	4.2	35.07		24,612	4.2	35.07	
$46.98-$70.46	5,460	3.7	60.04		5,460	3.7	60.04	
$70.47-$90.00	13,797	4.2	83.36		13,797	4.2	83.36	
	270,189	6.0	$ 18.04	$ 297,334	152,994	4.8	$ 22.76	$ 213,647
Expected forfeitures	14,841							

Total options outstanding	285,030

The aggregate intrinsic values in the preceding table represent the total pre-tax intrinsic values based on our closing stock price of $10.97 as of June 30, 2006 which would have been received by the option holders had all options been exercised as of that date.

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Restricted Stock and Restricted Stock Units

The following tables summarize our restricted stock and restricted stock unit activity for the three and six months ended June 30, 2006 and 2005 (shares in thousands):

	Number of Shares	Weighted Average Grant Date Fair Value
Restricted stock and restricted stock units at January 1, 2006	25,291	$ 13.74
Granted	353	13.43
Vested	(2,853)	12.98
Forfeited	(127)	13.72
Restricted stock and restricted stock units at March 31, 2006	22,664	13.83
Granted	3,681	12.56
Vested	(1,461)	13.37
Forfeited	(69)	13.57
Restricted stock and restricted stock units at June 30, 2006	24,815	$ 13.71

	Number of Shares	Weighted Average Grant Date Fair Value
Restricted stock and restricted stock units at January 1, 2005	6,903	$ 12.76
Granted	1,488	12.89
Vested	(763)	12.92
Restricted stock and restricted stock units at March 31, 2005	7,628	12.77
Granted	6,943	13.98
Vested	(349)	11.21
Forfeited	(84)	13.00
Restricted stock and restricted stock units at June 30, 2005	14,138	$ 13.40

The total fair value of restricted stock and restricted stock units that vested during the three and six months ended June 30, 2006 was $19.5 million and $56.6 million, respectively. The total fair value of restricted stock and restricted stock units that vested during the three and six months ended June 30, 2005 was $3.9 million and $13.8 million, respectively.

Our restricted stock awards have various vesting terms, including pro rata vesting over three years, cliff vesting at the end of three or five years from the date of grant with acceleration for achieving specified performance criteria and cliff vesting on various dates contingent on achieving specified performance criteria.

As of June 30, 2006, 24.8 million shares of restricted stock and restricted stock units were outstanding and unvested, with an aggregate intrinsic value of $340.1 million and a weighted average remaining contractual life of approximately 3.4 years. These shares and units are expected to vest through 2011. Of the total shares of restricted stock and restricted stock units outstanding, 17.9 million shares and units will vest upon fulfilling service conditions. Of this amount, vesting for 15.9 million shares and units will accelerate upon achieving performance conditions. The remaining 6.9 million shares and units will vest only if certain performance conditions are achieved.

Impact of Adopting FAS No. 123R

On January 1, 2006, we adopted FAS No. 123R. The standard requires recognizing compensation costs for all share-based payment awards made to employees and directors based upon the awards estimated grant date fair value. The standard covers employee stock options, restricted stock, restricted stock units and employee stock purchases related to our employee stock

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purchase plan. Additionally, we applied the provisions of the SEC s Staff Accounting Bulletin No. 107 on Share-Based Payment to our adoption of FAS No. 123R. Previously, we elected to account for these share-based payment awards under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB No. 25) and elected to only disclose the impact of expensing the fair value of stock options in the notes to the financial statements.

We adopted FAS No. 123R using the modified prospective transition method which requires applying the standard as of January 1, 2006 (the adoption date). The modified prospective transition method does not result in the restatement of results from prior periods and accordingly, the results of operations for the three and six months ended June 30, 2006 and future periods will not be comparable to our historical results of operations.

Under the modified prospective transition method, FAS No. 123R applies to new equity awards and to equity awards modified, repurchased or canceled after the adoption date. Additionally, compensation cost for the portion of awards granted prior to the adoption date for which the requisite service has not been rendered as of the adoption date shall be recognized as the requisite service is rendered. The compensation cost for that portion of awards shall be based on the grant-date fair value of those awards as calculated in the prior period pro forma disclosures under FAS No. 123, Accounting for Stock-Based Compensation (FAS No. 123). Changes to the grant-date fair value of equity awards granted before the effective date are precluded. The compensation cost for those earlier awards shall be attributed to periods beginning on or after the adoption date using the attribution method that was used under FAS No. 123, which was the straight-line method. Instead of recognizing forfeitures only as they occur, we now estimate an expected forfeiture rate which is factored in to determine our quarterly expense. Deferred compensation which related to those earlier awards has been eliminated against additional paid-in capital. FAS No. 123R also changes the reporting of tax-related amounts within the statement of cash flows. The gross amount of windfall tax benefits resulting from stock-based compensation will be reported as financing inflows.

For stock options, we have selected the Black-Scholes option-pricing model to determine the fair value of our stock option awards. For stock options, restricted stock and restricted stock units, we recognize compensation cost on a straight-line basis over the awards vesting periods for those awards which contain only a service vesting feature. For awards with a performance condition vesting feature, we recognize compensation cost on a graded vesting basis over the awards vesting periods.

The following table summarizes the components of total stock-based compensation expense included in our consolidated income statement for the three and six months ended June 30, 2006 (in thousands):

	Three Months Ended June, 30 2006			Six Months Ended June 30, 2006		
	Stock Options	**Restricted Stock**	**Total Stock-Based Compensation**	**Stock Options**	**Restricted Stock**	**Total Stock-Based Compensation**
Cost of product sales	$ 9,289	$ 1,507	$ 10,796	$ 20,293	$ 2,671	$ 22,964
Cost of services	4,936	707	5,643	11,327	1,451	12,778
Research and development	13,839	11,996	25,835	30,724	20,373	51,097
Selling, general and administrative	37,114	18,935	56,049	78,078	37,022	115,100
Stock-based compensation expense before income taxes	65,178	33,145	98,323	140,422	61,517	201,939
Income tax benefit	10,133	9,355	19,488	24,363	17,219	41,582
Total stock-based compensation, net of tax	$ 55,045	$ 23,790	$ 78,835	$ 116,059	$ 44,298	$ 160,357

Stock option expense includes $6.2 million and $13.9 million of expense for the three and six months ended June 30, 2006 associated with our employee stock purchase plan.

In connection with the adoption of FAS No. 123R, we recorded a cumulative effect adjustment of $3.4 million for the six months ended June 30, 2006 to recognize compensation costs recorded in our pro forma equity compensation disclosures that would have been capitalized in our consolidated balance sheet as of January 1, 2006. Additionally, included in the cumulative effect adjustment was the application of an estimated forfeiture rate on our previously recognized expense on unvested restricted stock and restricted stock units.

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The table below presents the net change in amounts capitalized or accrued on the consolidated balance sheet for the three and six months ended June 30, 2006 in the following line items (in thousands):

	Increased (Decreased) during the three months ended June 30, 2006	Increased (Decreased) during the six months ended June 30, 2006
Inventory	$ (796)	$ 2,396
Other assets (capitalized software development costs)	880	15,113
Accrued expenses (accrued warranty expenses)	1,071	23,120

As of June 30, 2006, the total unrecognized after-tax compensation cost for stock options, restricted stock, restricted stock units and options under our employee stock purchase plan was $580.2 million. Approximately 82% of our employees have received grants through these equity compensation programs. This non-cash expense will be recognized through 2011 with a weighted average remaining period of 1.7 years.

As a result of adopting FAS No. 123R, our income before taxes and net income for the three months ended June 30, 2006 were $59.5 million and $51.5 million lower, respectively, and our income before taxes and net income for the six months ended June 30, 2006 were $128.4 million and $108.4 million lower, respectively, than if we had continued to account for share-based compensation under APB No. 25. Basic and diluted earnings per share for the three months ended June 30, 2006 would have each been $0.14 if we had not adopted FAS No. 123R, compared to reported basic and diluted earnings per share which were each $0.12. Basic and diluted earnings per share for the six months ended June 30, 2006 would have each been $0.28 if we had not adopted FAS No. 123R, compared to reported basic and diluted earnings per share of $0.24 and $0.23, respectively.

Prior to the adoption of FAS No. 123R, we presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the consolidated statement of cash flows. FAS No. 123R requires the cash flows resulting from excess tax benefits to be classified as financing cash flows, rather than as operating cash flows. The $9.7 million excess tax benefit classified as a financing cash inflow would have been classified as an operating cash inflow had we not adopted FAS No. 123R.

For the periods prior to 2006, we elected to apply APB No. 25 and related interpretations in accounting for our stock-based compensation plans. The following is a reconciliation of net income per weighted average share had we adopted the fair value recognition provisions of FAS No. 123 for the three and six months ended June 30, 2005 (table in thousands, except per share amounts):

	Three Months Ended June 30, 2005	Six Months Ended June 30, 2005
Net income	$ 293,364	$ 563,198
Add back: Stock compensation costs, net of tax, on stock-based awards	13,111	22,130
Less: Stock compensation costs, net of taxes, had stock compensation expense been measured at fair value	(99,477)	(196,133)
Incremental stock compensation expense per FAS No. 123, net of taxes	(86,366)	(174,003)
Adjusted net income	$ 206,998	$ 389,195
Net income per weighted average share, basic as reported	$ 0.12	$ 0.24

Net income per weighted average share, diluted as reported	$	0.12	$	0.23
Adjusted net income per weighted average share, basic	$	0.09	$	0.16
Adjusted net income per weighted average share, diluted	$	0.08	$	0.16