

BEST BUY CO INC
Form 10-Q
October 11, 2007

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 1, 2007

OR

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

For the transition period from to

Commission File Number: 1-9595

BEST BUY CO., INC.

(Exact name of registrant as specified in its charter)

Minnesota

(State or other jurisdiction of incorporation or
organization)

41-0907483

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

**7601 Penn Avenue South
Richfield, Minnesota**

(Address of principal executive offices)

55423

(Zip Code)

(612) 291-1000

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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 such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. **Yes x No o**

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

Large accelerated filer x

Accelerated filer 0

Non-accelerated filer 0

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). **Yes** 0 **No** x

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. **Yes** 0 **No** 0

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common Stock, \$.10 Par Value 417,777,000 shares outstanding as of September 1, 2007.

BEST BUY CO., INC.

FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 1, 2007

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PART I FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

BEST BUY CO., INC.CONDENSED CONSOLIDATED BALANCE SHEETSASSETS

(\$ in millions, except per share amounts)

(Unaudited)

	September 1, 2007	March 3, 2007	August 26, 2006
CURRENT ASSETS			
Cash and cash equivalents	\$ 1,390	\$ 1,205	\$ 1,104
Short-term investments	121	2,588	1,534
Receivables	554	548	513
Merchandise inventories	4,650	4,028	4,049
Other current assets	733	712	687
Total current assets	7,448	9,081	7,887
PROPERTY AND EQUIPMENT			
Property and equipment	5,328	4,904	5,151
Less accumulated depreciation	2,210	1,966	2,364
Net property and equipment	3,118	2,938	2,787
GOODWILL	1,053	919	1,010
TRADENAMES	93	81	83
EQUITY AND OTHER INVESTMENTS	200	338	306
OTHER ASSETS	325	213	334
TOTAL ASSETS	\$ 12,237	\$ 13,570	\$ 12,407

NOTE: The consolidated balance sheet as of March 3, 2007, has been condensed from the audited consolidated financial statements.

See Notes to Condensed Consolidated Financial Statements.

BEST BUY CO., INC.CONDENSED CONSOLIDATED BALANCE SHEETSLIABILITIES AND SHAREHOLDERS' EQUITY

(\$ in millions, except per share amounts)

(Unaudited)

	September 1, 2007	March 3, 2007	August 26, 2006
CURRENT LIABILITIES			
Accounts payable	\$ 4,312	\$ 3,934	\$ 3,858
Unredeemed gift card liabilities	422	496	392
Accrued compensation and related expenses	287	332	263
Accrued liabilities	970	990	958
Accrued income taxes	99	489	399
Short-term debt	1,357	41	77
Current portion of long-term debt	20	19	419
Total current liabilities	7,467	6,301	6,366
LONG-TERM LIABILITIES	751	443	392
LONG-TERM DEBT	600	590	184
MINORITY INTERESTS	38	35	31
SHAREHOLDERS' EQUITY			
Preferred stock, \$1.00 par value: Authorized 400,000 shares; Issued and outstanding none			
Common stock, \$.10 par value: Authorized 1.5 billion shares; Issued and outstanding 417,777,000, 480,655,000 and 480,250,000 shares, respectively	42	48	48
Additional paid-in capital		430	389
Prepaid stock repurchase	(200)		
Retained earnings	3,147	5,507	4,690
Accumulated other comprehensive income	392	216	307
Total shareholders' equity	3,381	6,201	5,434
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 12,237	\$ 13,570	\$ 12,407

NOTE: The consolidated balance sheet as of March 3, 2007, has been condensed from the audited consolidated financial statements.

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See Notes to Condensed Consolidated Financial Statements.

BEST BUY CO., INC.CONSOLIDATED STATEMENTS OF EARNINGS

(\$ in millions, except per share amounts)

(Unaudited)

	Three Months Ended		Six Months Ended	
	September 1, 2007	August 26, 2006	September 1, 2007	August 26, 2006
Revenue	\$ 8,750	\$ 7,603	\$ 16,677	\$ 14,562
Cost of goods sold	6,611	5,701	12,646	10,895
Gross profit	2,139	1,902	4,031	3,667
Selling, general and administrative expenses	1,738	1,572	3,364	3,000
Operating income	401	330	667	667
Other income (expense)				
Investment income and other	22	29	66	60
Interest expense	(23)	(8)	(30)	(16)
Earnings before income tax expense, minority interest and equity in loss of affiliates	400	351	703	711
Income tax expense	144	121	257	247
Minority interest	(5)		(3)	
Equity in loss of affiliates	(1)		(1)	
Net earnings	\$ 250	\$ 230	\$ 442	\$ 464
Earnings per share				
Basic	\$ 0.56	\$ 0.48	\$ 0.96	\$ 0.96
Diluted	\$ 0.55	\$ 0.47	\$ 0.94	\$ 0.94
Dividends declared per common share	\$ 0.10	\$ 0.08	\$ 0.20	\$ 0.16
Weighted average common shares outstanding (in millions)				
Basic	444.1	482.0	461.5	483.3
Diluted	456.2	496.5	473.8	498.4

See Notes to Condensed Consolidated Financial Statements.

BEST BUY CO., INC.CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITYFOR THE SIX MONTHS ENDED SEPTEMBER 1, 2007

(\$ and shares in millions, except per share amounts)

(Unaudited)

	Common Shares	Common Stock	Additional Paid-In Capital	Prepaid Stock Repurchase	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balances at March 3, 2007	481	\$ 48	\$ 430	\$	\$ 5,507	\$ 216	\$ 6,201
Net earnings, six months ended September 1, 2007					442		442
Foreign currency translation adjustments						178	178
Unrealized loss on available-for-sale securities						(2)	(2)
Total comprehensive income							618
Cumulative effect of adopting a new accounting standard					(13)		(13)
Stock-based compensation			58				58
Stock options exercised	1		32				32
Issuance of common stock under employee stock purchase plan	1		27				27
Tax benefit from stock options exercised and employee stock purchase plan			12				12
Payment for accelerated share repurchase program				(3,000)			(3,000)
Repurchase of common stock	(65)	(6)	(559)	2,800	(2,696)		(461)
Common stock dividends, \$0.20 per share					(93)		(93)
Balances at September 1, 2007	418	\$ 42	\$	\$ (200)	\$ 3,147	\$ 392	\$ 3,381

See Notes to Condensed Consolidated Financial Statements.

BEST BUY CO., INC.CONSOLIDATED STATEMENTS OF CASH FLOWS

(\$ in millions)

(Unaudited)

	Six Months Ended	
	September 1, 2007	August 26, 2006
OPERATING ACTIVITIES		
Net earnings	\$ 442	\$ 464
Adjustments to reconcile net earnings to total cash provided by (used in) operating activities		
Depreciation	279	246
Asset impairment charges	1	21
Stock-based compensation	58	59
Deferred income taxes	(18)	(28)
Excess tax benefits from stock-based compensation	(12)	(31)
Other, net	2	14
Changes in operating assets and liabilities, net of acquired assets and liabilities		
Receivables	4	(15)
Merchandise inventories	(555)	(548)
Other assets	(2)	(5)
Accounts payable	278	231
Other liabilities	(142)	(185)
Accrued income taxes	(204)	(263)
Total cash provided by (used in) operating activities	131	(40)
INVESTING ACTIVITIES		
Additions to property and equipment, net of \$35 non-cash capital expenditures in the six months ended September 1, 2007	(376)	(299)
Purchases of investments	(3,739)	(1,635)
Sales of investments	6,345	3,060
Acquisition of businesses, net of cash acquired	(89)	(421)
Change in restricted assets	2	(16)
Other, net		12
Total cash provided by investing activities	2,143	701
FINANCING ACTIVITIES		
Repurchase of common stock	(3,461)	(462)
Issuance of common stock under employee stock purchase plan and for the exercise of stock options	59	117
Excess tax benefits from stock-based compensation	12	31
Dividends paid	(93)	(78)
Proceeds from issuance of debt	2,861	38
Repayments of debt	(1,538)	(7)
Other, net		37
Total cash used in financing activities	(2,160)	(324)

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EFFECT OF EXCHANGE RATE CHANGES ON CASH	71	19
INCREASE IN CASH AND CASH EQUIVALENTS	185	356
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	1,205	748
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 1,390	\$ 1,104

See Notes to Condensed Consolidated Financial Statements.

BEST BUY CO., INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(\$ in millions, except per share amounts)

(Unaudited)

1. Basis of Presentation

In the opinion of management, the accompanying condensed consolidated financial statements contain all adjustments necessary for a fair presentation as prescribed by accounting principles generally accepted in the U.S. All adjustments were comprised of normal recurring adjustments, except as noted in these Notes to Condensed Consolidated Financial Statements. Historically, we have realized more of our revenue and earnings in the fiscal fourth quarter, which includes the majority of the holiday shopping season in the U.S. and Canada, than in any other fiscal quarter. The timing of new store openings, costs associated with the development of new businesses, as well as general economic conditions may also affect our future quarterly results. Consequently, interim results are not necessarily indicative of results for the entire fiscal year. These interim financial statements and the related notes should be read in conjunction with the consolidated financial statements and notes included in our Annual Report on Form 10-K for the fiscal year ended March 3, 2007.

Consistent with China's statutory requirements, our China operations' fiscal year ends on December 31. Therefore, we have elected to consolidate our China financial results on a two-month lag. There was no significant intervening event that would have materially affected our consolidated financial statements had it been recorded during the fiscal quarter.

Reclassifications

To maintain consistency and comparability, we reclassified certain prior-year amounts to conform to the current-year presentation as described in Note 1, *Summary of Significant Accounting Policies*, of the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended March 3, 2007. In addition, to conform to the current-year presentation, we reclassified:

to the International segment, \$2 and \$3 of selling, general and administrative (SG&A) support costs for the three and six months ended August 26, 2006, respectively, which were previously reported as part of the Domestic segment;

to short-term debt, \$77 of liabilities at August 26, 2006 which were previously reported in current portion of long-term debt; and

to equity and other investments, \$20 and \$29 of investments at March 3, 2007 and August 26, 2006, respectively, which were previously reported in other assets.

These reclassifications had no effect on previously reported consolidated operating income, net earnings, shareholders' equity or cash flows.

New Accounting Standards

In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS No. 159 permits companies to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing companies with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. Companies are not allowed to adopt SFAS No. 159 on a retrospective basis unless they choose early adoption. We plan to adopt SFAS No. 159 beginning in the first quarter of fiscal 2009. We are evaluating the impact, if any, the adoption of SFAS No. 159 will have on our consolidated operating income or net earnings.

\$ in millions, except per share amounts

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, SFAS No. 157 does not require any new fair value measurement. SFAS No. 157 is effective for fiscal years beginning after December 15, 2007. We plan to adopt SFAS No. 157 beginning in the first quarter of fiscal 2009. We are evaluating the impact, if any, the adoption of SFAS No. 157 will have on our consolidated operating income or net earnings.

2. Acquisitions

Speakeasy, Inc.

On May 1, 2007, we acquired Speakeasy, Inc. (Speakeasy) for \$103 in cash, or \$89 net of cash acquired, including transaction costs and the repayment of \$5 of Speakeasy's debt. We acquired Speakeasy, an independent U.S. broadband voice, data and IT services provider, to strengthen our portfolio of technology solutions. We accounted for the acquisition using the purchase method in accordance with SFAS No. 141, *Business Combinations*. Accordingly, we recorded the net assets at their estimated fair values, and included operating results in our Domestic segment from the date of acquisition. We allocated the purchase price on a preliminary basis using information currently available. The allocation of the purchase price to the assets and liabilities acquired will be finalized no later than the first quarter of fiscal 2009, as we obtain more information regarding asset valuations, liabilities assumed and revisions of preliminary estimates of fair values made at the date of purchase. The premium we paid in excess of the fair value of the net assets acquired was primarily for the expected synergies we believe Speakeasy will generate by providing new technology solutions for our existing and future customers, as well as to obtain Speakeasy's skilled, established workforce. None of the goodwill is deductible for tax purposes.

The preliminary purchase price allocation, net of cash acquired, was as follows:

Receivables	\$ 8
Property and equipment	8
Other assets	21
Tradename	6
Goodwill	76
Current liabilities	(30)
Total	\$ 89

Jiangsu Five Star Appliance Co., Ltd.

On June 8, 2006, we acquired a 75% interest in Jiangsu Five Star Appliance Co., Ltd. (Five Star) for \$184, including a working capital injection of \$122 and transaction costs. Five Star is an appliance and consumer electronics retailer and had 131 stores located in eight of China's 34 provinces on the date of acquisition. We made the investment in Five Star to further our international growth plans, to increase our knowledge of

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Chinese customers and to obtain an immediate retail presence in China. We accounted for the acquisition using the purchase method in accordance with SFAS No. 141. Accordingly, we recorded the net assets at their estimated fair values, and included operating results in our International segment from the date of acquisition. We allocated the purchase price on a preliminary basis using information then available. The allocation of the purchase price to the assets and liabilities acquired was finalized in the first quarter of fiscal 2008. There was no significant adjustment to the preliminary purchase price allocation. None of the goodwill is deductible for tax purposes.

\$ in millions, except per share amounts

The final purchase price allocation, net of cash acquired, was as follows:

Restricted cash	\$ 204
Merchandise inventories	109
Property and equipment	78
Other assets	78
Tradenname	21
Goodwill	24
Accounts payable	(368)
Other current liabilities	(35)
Debt	(64)
Long-term liabilities	(1)
Minority interests ¹	(33)
Total	\$ 13

1 The minority interests proportionate ownership of assets and liabilities were recorded at historical carrying values.

3. Investments

Investments were comprised of the following:

	September 1, 2007	March 3, 2007	August 26, 2006
Short-term investments			
Debt securities	\$ 121	\$ 2,588	\$ 1,534
Equity and other investments			
Debt securities	\$	\$ 318	\$ 277
Marketable equity securities	184	4	20
Other investments	16	16	9
Total equity and other investments	\$ 200	\$ 338	\$ 306

Debt Securities

Short-term and long-term investments in debt securities are comprised of auction-rate securities, variable-rate demand notes, asset-backed securities, municipal debt securities, and commercial paper. In accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and based on our ability to market and to sell these instruments, we classify auction-rate securities, variable-rate demand notes and other investments in debt securities as available-for-sale and carry them at amortized cost, which approximates fair value. Auction-rate securities and variable-rate demand notes are similar to short-term debt instruments because their interest rates are reset periodically. Investments in these securities can be sold for cash on the auction date. We classify auction-rate securities and variable-rate demand notes as

short-term or long-term investments based on the reset dates.

In accordance with our investment policy, we place our investments in debt securities with issuers who have high-quality credit and limit the amount of investment exposure to any one issuer. We seek to preserve principal and minimize exposure to interest-rate fluctuations by limiting default risk, market risk and reinvestment risk.

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The following table presents the amortized principal amounts, related weighted-average interest rates (taxable equivalent), maturities and major security types for our investments in debt securities:

	September 1, 2007		March 3, 2007		August 26, 2006	
	Amortized Principal Amount	Weighted- Average Interest Rate	Amortized Principal Amount	Weighted- Average Interest Rate	Amortized Principal Amount	Weighted- Average Interest Rate
Short-term investments (less than one year)	\$ 121	6.23%	\$ 2,588	5.68%	\$ 1,534	5.62%
Long-term investments (one to three years)		N/A	318	5.68%	277	5.74%
Total	\$ 121		\$ 2,906		\$ 1,811	
Auction-rate securities, variable-rate demand notes, and asset-backed securities	\$ 108		\$ 66		\$ 75	
Municipal debt securities			2,840		1,736	
Commercial paper	13					
Total	\$ 121		\$ 2,906		\$ 1,811	

The carrying values of our investments in debt securities approximated fair value at September 1, 2007; March 3, 2007; and August 26, 2006, due to the rapid turnover of our portfolio and the highly liquid nature of these investments. Therefore, there was no significant unrealized holding gain or loss. Realized gains and losses are included in investment income and other in the consolidated statements of earnings and were not significant for any period presented. The decrease in the balance of investments in debt securities compared with the balances at March 3, 2007 and at August 26, 2006, was due to the liquidation of a substantial portion of our investments portfolio to repay our bridge loan facility and to fund our accelerated share repurchase (ASR) program. See Note 4, *Credit Facilities*, for further information on the bridge loan facility, and Note 7, *Common Stock Repurchases*, for further information on the ASR program.

Marketable Equity Securities

We also invest in marketable equity securities and classify them as available-for-sale. Investments in marketable equity securities are included in equity and other investments in our consolidated balance sheets, and are reported at fair value based on quoted market prices. All unrealized holding gains and losses are reflected net of tax in accumulated other comprehensive income in shareholders' equity.

The carrying values of our investments in marketable equity securities at September 1, 2007; March 3, 2007; and August 26, 2006, were \$184, \$4 and \$20, respectively. The increase in marketable equity securities since March 3, 2007, was primarily due to our investment in The Carphone Warehouse Group PLC (CPW), a leading European mobile communications retailer. During the second quarter of fiscal 2008, we acquired 26.1 million shares of common stock of CPW in the open market for \$183, representing nearly 3% of CPW's outstanding shares. The decrease in marketable equity securities from August 26, 2006 to March 3, 2007, was primarily due to the sale of our investment in Golf Galaxy, Inc. (Golf Galaxy) in February 2007. At August 26, 2006, the carrying value of our investment in Golf Galaxy was \$16.

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Net unrealized (loss)/gain, net of tax, included in accumulated other comprehensive income were \$(3), \$(1) and \$7 at September 1, 2007; March 3, 2007; and August 26, 2006, respectively.

Other Investments

We also have investments that are accounted for on either the cost method or the equity method that we include in equity and other investments in our consolidated balance sheets. The aggregate carrying values of these investments at September 1, 2007; March 3, 2007; and August 26, 2006, were \$16, \$16 and \$9, respectively.

4. Credit Facilities

On June 26, 2007, we entered into a \$3,000 bridge loan facility with Goldman Sachs Credit Partners L.P. (the Bridge Facility), simultaneously with the execution of agreements to purchase \$3,000 of shares of our common stock in the aggregate pursuant to our ASR program. We initially borrowed \$2,500 under the Bridge Facility and used \$500 of our existing cash

\$ in millions, except per share amounts

and investments to fund the ASR program. Effective July 11, 2007, we reduced the amount we could borrow under the Bridge Facility to \$2,500. At September 1, 2007, \$1,298 was outstanding under the Bridge Facility. See Note 7, *Common Stock Repurchases*, for further information on the ASR program.

Effective July 2, 2007, we terminated our previous \$200 revolving credit facility that was scheduled to expire on December 22, 2009.

On September 19, 2007, we entered into a \$2,500 five-year unsecured revolving credit agreement with JPMorgan Chase Bank, N.A. (JPMorgan), as administrative agent, and a syndication of banks. On the same date, we repaid the outstanding balance and terminated the Bridge Facility. See Note 11, *Subsequent Event*, for further information regarding these transactions.

5. Income Taxes

We adopted the provisions of FASB Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109*, effective March 4, 2007. FIN No. 48 provides guidance regarding the recognition, measurement, presentation and disclosure in the financial statements of tax positions taken or expected to be taken on a tax return, including the decision whether to file or not to file in a particular jurisdiction. The adoption of FIN No. 48 resulted in the reclassification of \$201 of tax liabilities from current to long-term and a \$13 increase in our liability for unrecognized tax benefits, which was accounted for as a reduction to the March 4, 2007 retained earnings balance.

At March 4, 2007, our total liability for unrecognized tax benefits, after the adoption of FIN No. 48, was \$201, of which \$68 represented tax benefits that, if recognized, would favorably impact the effective tax rate. Our liability for unrecognized tax benefits was \$229 at September 1, 2007.

We recognize interest and penalties in income tax expense in our consolidated statements of earnings. At March 4, 2007, we had accrued interest and penalties of \$30. There has been no significant change in our accrued interest and penalties since March 4, 2007.

We file a consolidated U.S. federal income tax return, as well as income tax returns in various states and foreign jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before fiscal 2003. In April 2007, the Internal Revenue Service completed its examination of our U.S. federal income tax returns for fiscal 2003 and fiscal 2004 and resolution of the issues pertaining to those years is expected in fiscal 2009. However, we do not expect that the resolution of these issues will have a significant effect on our consolidated financial condition or results of operations.

6. Earnings per Share

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Our basic earnings per share calculation is computed based on the weighted-average number of common shares outstanding. Our diluted earnings per share calculation is computed based on the weighted-average number of common shares outstanding adjusted by the number of additional shares that would have been outstanding had the potentially dilutive common shares been issued. Potentially dilutive shares of common stock include stock options, nonvested share awards and shares issuable under our employee stock purchase plan, as well as common shares that would have resulted from the assumed conversion of our convertible debentures. Since the potentially dilutive shares related to the convertible debentures are included in the calculation, the related interest expense, net of tax, is added back to net earnings, as the interest would not have been paid if the convertible debentures had been converted to common stock. Nonvested market-based awards and nonvested performance-based awards are included in the average diluted shares outstanding each period if established market or performance criteria have been met at the end of the respective periods.

\$ in millions, except per share amounts

The following table presents a reconciliation of the numerators and denominators of basic and diluted earnings per share (shares in millions):

	Three Months Ended		Six Months Ended	
	September 1, 2007	August 26, 2006	September 1, 2007	August 26, 2006
Numerator				
Net earnings, basic	\$ 250	\$ 230	\$ 442	\$ 464
Adjustment for assumed dilution				
Interest on convertible debentures, net of tax	1	1	3	3
Net earnings, diluted	\$ 251	\$ 231	\$ 445	\$ 467
Denominator				
Weighted-average common shares outstanding	444.1	482.0	461.5	483.3
Effect of potentially dilutive securities				
Shares from assumed conversion of convertible debentures	8.8	8.8	8.8	8.8
Stock options and other	3.3	5.7	3.5	6.3
Weighted-average common shares outstanding, assuming dilution	456.2	496.5	473.8	498.4
Earnings per share				
Basic	\$ 0.56	\$ 0.48	\$ 0.96	\$ 0.96
Diluted	\$ 0.55	\$ 0.47	\$ 0.94	\$ 0.94

The computation of average dilutive shares outstanding excluded stock options to purchase 8.7 million and 0.4 million shares of common stock for the three months ended September 1, 2007, and August 26, 2006, respectively, and 8.7 million and 0.4 million shares of common stock for the six months ended September 1, 2007, and August 26, 2006, respectively. These amounts were excluded because the options' exercise prices were greater than the average market price of our common stock for the periods presented and, therefore, their effect would be antidilutive (i.e., including such options would result in higher earnings per share).

7. Common Stock Repurchases

On June 26, 2007, our Board of Directors (Board) authorized a new \$5,500 share repurchase program. The new program has no stated expiration date. The new program terminated and replaced our prior \$1,500 share repurchase program authorized by our Board in June 2006. The June 2006 share repurchase program terminated and replaced our prior \$1,500 share repurchase program authorized by our Board in April 2005.

Open Market Repurchases

The following table presents open market share repurchases (shares in millions):

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	Three Months Ended		Six Months Ended	
	September 1, 2007	August 26, 2006	September 1, 2007	August 26, 2006
Total number of shares repurchased	1.1	4.6	9.8	9.0
Total cost of shares repurchased	\$ 49	\$ 224	\$ 461	\$ 462

In the three and six months ended September 1, 2007, we purchased and retired 1.1 and 9.8 million shares, respectively, at a cost of \$49 and \$461 under our June 2006 share repurchase program. We made no open market purchases during the three months ended September 1, 2007, under our June 2007 share repurchase program.

\$ in millions, except per share amounts

In the three and six months ended August 26, 2006, we purchased and retired 2.8 million shares at a cost of \$130 under our June 2006 share repurchase program. For the three months ended August 26, 2006, we also purchased and retired 1.8 million shares at a cost of \$94 under our April 2005 share repurchase program. In the six months ended August 26, 2006, we purchased and retired 6.2 million shares at a cost of \$332 under our April 2005 share repurchase program. Retired shares constitute authorized but unissued shares.

Accelerated Share Repurchase Program

In accordance with the new \$5,500 share repurchase program, on June 26, 2007, we entered into an ASR program authorized by our Board. The ASR program consists of two agreements to purchase shares of our common stock from Goldman, Sachs & Co. (Goldman) for an aggregate purchase price of \$3,000. Goldman borrowed the shares that were delivered to us as described below, and is expected to purchase sufficient shares of our common stock in the open market to return to lenders over the terms of the agreements. The ASR program will conclude in February 2008, although in certain circumstances the termination date may be accelerated at Goldman's option. The actual number of shares repurchased will be determined at the completion of the ASR program. We do not expect to make significant additional share repurchases prior to the conclusion of the ASR program. Repurchased shares have been retired and constitute authorized but unissued shares.

Collared ASR

Under the first agreement (the Collared ASR), the number of shares to be repurchased is based generally on the volume-weighted average price (VWAP) of our common stock during the term of the Collared ASR, subject to collar provisions that established minimum and maximum numbers of shares based on the VWAP of our common stock over the specified hedge period. On July 2, 2007, we paid \$2,000 to Goldman in exchange for an initial delivery of 28.3 million shares to us on July 2-6, 2007, under the terms of the Collared ASR.

Pursuant to the terms of the Collared ASR, the hedge period for determining the minimum and maximum numbers of shares to be purchased ended on July 24, 2007. The minimum has been set at 38.7 million shares and the maximum has been set at 44.8 million shares. Goldman delivered 10.4 million additional shares to us on July 27, 2007. Accordingly, we have received a total of 38.7 million shares from Goldman at September 1, 2007, equivalent to the minimum number of shares to be delivered under the terms of the Collared ASR. At the conclusion of the Collared ASR, we may receive additional shares based on the VWAP of our common stock during the agreement term, up to the maximum 44.8 million shares.

Uncollared ASR

Under the second agreement (the Uncollared ASR), the number of shares to be repurchased is based generally on the VWAP of our common stock during the term of the Uncollared ASR. On July 2, 2007, we paid \$1,000 to Goldman under the terms of the Uncollared ASR in exchange for an initial delivery of 17.0 million shares to us on July 30-31, 2007, subject to a 20%, or \$200, holdback. At the conclusion of the Uncollared ASR, we may receive additional shares, or we may be required to pay additional cash or shares (at our option), based on the VWAP of our common stock during the agreement term. At September 1, 2007, the \$200 holdback was shown on our condensed consolidated balance sheet as prepaid stock repurchase in shareholders' equity.

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The following table presents share repurchases under the ASR program (shares in millions):

	Three Months Ended September 1, 2007	Six Months Ended September 1, 2007
Collared ASR		
Shares received	38.7	38.7
Payments made	\$ 2,000	\$ 2,000
Uncollared ASR		
Shares received	17.0	17.0
Payments made	\$ 1,000	\$ 1,000
Total shares received	55.7	55.7
Total payments made	\$ 3,000	\$ 3,000

\$ in millions, except per share amounts

8. Comprehensive Income

Comprehensive income is computed as net earnings plus other items that are recorded directly to shareholders' equity. In addition to net earnings, the components of comprehensive income are foreign currency translation adjustments and unrealized gains or losses, net of tax, on available-for-sale marketable equity securities. Foreign currency translation adjustments do not include a provision for income tax expense when earnings from foreign operations are considered to be indefinitely reinvested outside the U.S. Comprehensive income was \$258 and \$222 in the three months ended September 1, 2007, and August 26, 2006, respectively, and \$618 and \$510 in the six months ended September 1, 2007, and August 26, 2006, respectively.

9. Segments

We operate two reportable segments: Domestic and International. The Domestic segment is comprised of all U.S. store and online operations. The International segment is comprised of all store and online operations outside the U.S. We have included Speakeasy, which we acquired on May 1, 2007, in the Domestic segment. Our segments are evaluated on an operating income basis, and a stand-alone tax provision is not calculated for each segment. To conform to the current-year presentation, we reclassified to the International segment \$2 and \$3 of SG&A support costs for the three and six months ended August 26, 2006, respectively, which were reported as part of the Domestic segment in fiscal 2007. The other accounting policies of the segments are the same as those described in Note 1, *Summary of Significant Accounting Policies*, in the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended March 3, 2007.

Revenue by reportable segment was as follows:

	Three Months Ended		Six Months Ended	
	September 1, 2007	August 26, 2006	September 1, 2007	August 26, 2006
Domestic	\$ 7,234	\$ 6,621	\$ 13,938	\$ 12,783
International	1,516	982	2,739	1,779
Total revenue	\$ 8,750	\$ 7,603	\$ 16,677	\$ 14,562

Operating income by reportable segment and the reconciliation to earnings before income tax expense, minority interest and equity in loss of affiliates were as follows:

	Three Months Ended		Six Months Ended	
	September 1, 2007	August 26, 2006	September 1, 2007	August 26, 2006
Domestic	\$ 358	\$ 330	\$ 628	\$ 664
International	43		39	3
Total operating income	401	330	667	667
Other income (expense)				

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Investment income and other	22	29	66	60
Interest expense	(23)	(8)	(30)	(16)
Earnings before income tax expense, minority interest and equity in loss of affiliates	\$ 400	\$ 351	\$ 703	\$ 711

Assets by reportable segment were as follows:

	September 1, 2007	March 3, 2007	August 26, 2006
Domestic	\$ 8,658	\$ 10,614	\$ 9,315
International	3,579	2,956	3,092
Total assets	\$ 12,237	\$ 13,570	\$ 12,407

\$ in millions, except per share amounts

Goodwill by reportable segment was as follows:

	September 1, 2007	March 3, 2007	August 26,
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