UNIVERSAL ELECTRONICS INC
Form 10-Q
August 09, 2007

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2007

o **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: 0-21044

UNIVERSAL ELECTRONICS INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**33-0204817**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
6101 Gateway Drive Cypress, California	**90630**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant s Telephone Number, Including Area Code: (714) 820-1000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No o

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 o Accelerated filer þ Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act)

Yes o No þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 14,548,719 shares of Common Stock, par value $.01 per share, of the registrant were outstanding on August 7, 2007.

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PART I. FINANCIAL INFORMATION
ITEM 1. Consolidated Financial Statements

UNIVERSAL ELECTRONICS INC.
CONSOLIDATED BALANCE SHEETS
(In thousands, except share-related data)
(Unaudited)

	June 30, 2007		December 31, 2006	
ASSETS				
Current assets:				
Cash and cash equivalents	$	76,439	$	66,075
Accounts receivable, net		59,634		51,867
Inventories, net		27,272		26,459
Prepaid expenses and other current assets		3,295		2,722
Prepaid income taxes		5,338		
Deferred income taxes		3,047		3,069
Total current assets		175,025		150,192
Equipment, furniture and fixtures, net		6,519		5,899
Goodwill		10,697		10,644
Intangible assets, net		5,570		5,587
Other assets		281		221
Deferred income taxes		5,265		6,065
Total assets	$	203,357	$	178,608
LIABILITIES AND STOCKHOLDERS EQUITY				
Current liabilities:				
Accounts payable	$	26,953	$	20,153
Accrued sales discounts/rebates		3,562		4,498
Accrued income taxes				4,483
Accrued compensation		3,541		7,430
Other accrued expenses		6,955		7,449
Total current liabilities		41,011		44,013
Long term liabilities:				
Deferred income taxes		116		103
Accrued income taxes		6,860		
Other long term liabilities		741		275
Total liabilities		48,728		44,391
Commitments and Contingencies				

Stockholders equity:		
Preferred stock, $.01 par value, 5,000,000 shares authorized; none issued or outstanding		
Common stock, $.01 par value, 50,000,000 shares authorized; 18,119,675 and 17,543,235 shares issued at June 30, 2007 and December 31, 2006, respectively	181	175
Paid-in capital	106,417	94,733
Accumulated other comprehensive income	4,699	2,759
Retained earnings	77,527	68,514
	188,824	166,181
Less cost of common stock in treasury, 3,587,939 and 3,528,827 shares at June 30, 2007 and December 31, 2006, respectively	(34,195)	(31,964)
Total stockholders equity	154,629	134,217
Total liabilities and stockholders equity	$ 203,357	$ 178,608

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

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UNIVERSAL ELECTRONICS INC.
CONSOLIDATED INCOME STATEMENTS
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	**2006**	**2007**	**2006**
Net sales	$ 71,478	$ 52,370	$ 137,497	$ 106,543
Cost of sales	46,852	32,788	88,530	68,473
Gross profit	24,626	19,582	48,967	38,070
Research and development expenses	2,269	1,919	4,591	3,765
Selling, general and administrative expenses	16,385	13,620	32,218	27,132
Operating income	5,972	4,043	12,158	7,173
Interest income, net	732	349	1,320	621
Other income (expense), net	27	(411)	121	(572)
Income before provision for income taxes	6,731	3,981	13,599	7,222
Provision for income taxes	(2,185)	(1,562)	(4,416)	(2,667)
Net income	$ 4,546	$ 2,419	$ 9,183	$ 4,555
Earnings per share:				
Basic	$ 0.31	$ 0.18	$ 0.64	$ 0.33
Diluted	$ 0.30	$ 0.17	$ 0.61	$ 0.32
Shares used in computing earnings per share:				
Basic	14,437	13,802	14,282	13,722
Diluted	15,262	14,356	15,084	14,297

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

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UNIVERSAL ELECTRONICS INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Cash provided by operating activities:		
Net income	$ 9,183	$ 4,555
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,160	1,915
Provision (recovery) for doubtful accounts	10	(14)
Provision for inventory write-downs	952	562
Provision for deferred income taxes	853	(315)
Tax benefit from exercise of stock options	1,960	507
Excess tax benefit from stock-based compensation	(1,091)	
Shares issued for employee benefit plan	394	271
Stock-based compensation	1,481	1,604
Changes in operating assets and liabilities:		
Accounts receivable	(7,103)	1,413
Inventory	(1,419)	(1,957)
Prepaid expenses and other assets	(586)	493
Accounts payable and accrued expenses	1,566	429
Accrued income taxes	(3,476)	1,835
Net cash provided by operating activities	4,884	11,298
Cash used for investing activities:		
Acquisition of equipment, furniture and fixtures	(2,050)	(2,115)
Acquisition of intangible assets	(635)	(587)
Net cash used for investing activities	(2,685)	(2,702)
Cash provided by financing activities:		
Proceeds from stock options exercised	8,037	3,072
Treasury stock purchases	(2,413)	(222)
Excess tax benefit from stock-based compensation	1,091	
Net cash provided by financing activities	6,715	2,850
Effect of exchange rate changes on cash	1,450	3,689
Net increase in cash and cash equivalents	10,364	15,135

Cash and cash equivalents at beginning of period	66,075	43,641
Cash and cash equivalents at end of period	$ 76,439	$ 58,776

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

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UNIVERSAL ELECTRONICS INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1: Basis of Presentation and Significant Accounting Policies

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements. Certain information and footnote disclosures normally included in financial statements, which are prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission.

The results of operations for the three and six months ended June 30, 2007 are not necessarily indicative of the results to be expected for the full year. These financial statements should be read in conjunction with the consolidated financial statements and related notes contained in our Annual Report on Form 10-K for our fiscal year ended December 31, 2006. The financial information presented in the accompanying statements reflects all adjustments that are, in the opinion of management, necessary for a fair presentation of financial position, operations and cash flows for the periods presented. All such adjustments are of a normal recurring nature. As used herein, the terms Company , we , us and our refer to Universal Electronics Inc. and its subsidiaries, unless the context indicates to the contrary.

Segment Realignment

In the third quarter of 2006, we integrated the SimpleDevices business segment into our Core Business segment in order to more closely align our financial reporting with our business structure. The segment integration did not impact previously reported consolidated net revenue, income from operations, net income or net earnings per share.

Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and judgments that affect the amounts reported in our consolidated financial statements and accompanying notes. Actual results may differ from these estimates and judgments.

Recent Accounting Pronouncements

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 Including an amendment of FASB Statement No. 115* (SFAS 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities 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. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings (or another performance indicator if the business entity does not report earnings) at each subsequent reporting date. SFAS 159 is effective for the Company beginning January 1, 2008. We are currently evaluating the effect that the adoption of SFAS 159 will have on our consolidated results of operations and financial condition.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS 157), which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP) and expands disclosures about fair value measurements for assets and liabilities. SFAS 157 applies when other accounting pronouncements require or permit assets or liabilities to be measured at fair value. Accordingly, SFAS 157 does not require new fair value measurements. SFAS 157 is effective for the Company beginning January 1, 2008. We are currently evaluating the effect that the adoption of SFAS 157 will have on our consolidated results of operations and financial condition.

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Effective January 1, 2007, we applied the opinion reached by the FASB s Emerging Issues Task Force (EITF) on EITF Issue 06-3, *How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation).* The consensus in EITF Issue 06-3 does not require us to reevaluate our existing accounting policies for income statement presentation. Application of EITF 06-3 resulted in additional disclosure, but did not change the method in which we account for taxes collected. We present all non-income government-assessed taxes (sales, use and value added taxes) collected from our customers and remitted to governmental agencies on a net basis (excluded from revenue) in our financial statements. The government-assessed taxes are recorded in other accrued expenses until they are remitted to the government agency.

Effective January 1, 2007, we adopted FASB Interpretation 48 (FIN 48), *Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109* (SFAS 109). Additionally, in May 2007, the FASB published FASB Staff Position No. FIN 48-1, *Definition of Settlement in FASB Interpretation No. 48* (FSP FIN 48-1). FSP FIN 48-1 is an amendment to FIN 48. It clarifies how an enterprise should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. FSP FIN 48-1 is effective upon the initial adoption of FIN 48. Accordingly, we adopted FSP FIN 48-1 on January 1, 2007. Refer to Note 6 below for further discussion regarding the financial effects of adopting FIN 48.

Note 2: Stock-Based Compensation

Effective January 1, 2006, we adopted the fair value recognition provisions of SFAS No. 123R, *Share Based Payment* (SFAS 123R) using the modified-prospective transition method. Stock-based compensation expense is presented in the same income statement line as cash compensation paid to the same employees or directors. During the three months ended June 30, 2007 and 2006, we recorded $0.8 million and $0.8 million, respectively in pre-tax stock-based compensation expense. Included in SG&A stock-based compensation expense is $117 thousand and $82 thousand in pre-tax compensation expense related to stock awards granted to outside directors for the three months ended June 30, 2007 and 2006, respectively. The income tax benefit as a result of implementation of SFAS 123R was $0.2 million and $0.2 million for the three months ended June 30, 2007 and 2006, respectively.

During the six months ended June 30, 2007 and 2006, we recorded $1.5 million and $1.6 million, respectively, in pre-tax stock-based compensation expense. Included in SG&A stock-based compensation expense is $234 thousand and $163 thousand in pre-tax compensation expense related to stock awards granted to outside directors for the six months ended June 30, 2007 and 2006, respectively. The income tax benefit as a result of implementation of SFAS 123R was $0.4 million and $0.5 million for the six months ended June 30, 2007 and 2006, respectively.

Stock-based compensation expense was attributable to the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	**2007**	**2006**	**2007**	**2006**
Cost of sales	$ 7	$ 6	$ 13	$ 13
Research and development	106	94	185	199
Selling, general and administrative	692	653	1,283	1,392
Stock-based compensation expense before income taxes	$ 805	$ 753	$ 1,481	$ 1,604

We estimate the fair value of share-based payment awards using the Black-Scholes option pricing model with the following assumptions and weighted average fair values:

Three Months Ended June 30,		Six Months Ended June 30,	
2007 (1)	**2006**	**2007 (1)**	**2006**

Weighted average fair value of grants	$11.86	$ 8.07	$11.73	$ 8.09
Risk-free interest rate	4.58%	4.96%	4.58%	4.75%
Expected volatility	38.83%	42.12%	39.06%	42.89%
Expected life in years	5.24	5.35	5.24	5.35

(1) The fair value calculation was based on stock options granted during the period.

UNIVERSAL ELECTRONICS INC.
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(Unaudited)

Stock option activity as of June 30, 2007 and changes during the six months ended June 30, 2007 were as follows:

	Number of Options (in thousands)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2006	2,480	$ 13.73		
Granted	324	27.68		
Exercised	(561)	14.32		
Forfeited/cancelled/ expired	(72)	13.50		
Outstanding at June 30, 2007	2,171	$ 15.66	5.65	$ 44,840
Vested and expected to vest at June 30, 2007	2,071	$ 15.27	5.49	$ 43,597
Exercisable at June 30, 2007	1,450	$ 12.78	4.22	$ 34,126

The aggregate intrinsic value in the table above represents total pre-tax intrinsic value (difference between Universal Electronics Inc. s average of the high and low trades of the last trading day of the second quarter of 2007 (June 29, 2007) and the option exercise price, multiplied by the number of the in-the-money options) that option holders would have received had all option holders exercised their options on June 29, 2007. This amount changes based on the fair market value of our common stock. The total intrinsic value of options exercised for the three and six months ended June 30, 2007 was $4.7 million and $7.9 million, respectively. The total intrinsic value of options exercised for the three and six months ended June 30, 2006 was $0.7 million and $1.9 million, respectively.

As of June 30, 2007, we expect to recognize $5.9 million of total unrecognized compensation expense related to non-vested employee stock options over a weighted-average life of 2.6 years.

Nonvested restricted stock awards as of June 30, 2007 and changes during the six months ended June 30, 2007 were as follows:

	Shares Granted	Weighted-Average Grant Date Fair Value
Nonvested at December 31, 2006	12,500	$ 18.74
Granted		
Vested	(12,500)	18.74
Forfeited		
Nonvested at June 30, 2007		$

Note 3: Cash and Cash Equivalents

Cash and cash equivalents include cash accounts and all investments purchased with initial maturities of three months or less. We maintain cash and cash equivalents with various financial institutions. These financial institutions are located in many different geographic regions. We mitigate our exposure to credit risk by placing our cash and cash equivalents with high quality financial institutions.

At June 30, 2007, we had approximately $12.5 million and $63.9 million of cash and cash equivalents in the United States and Europe, respectively. At December 31, 2006, we had approximately $6.1 million and $60.0 million of cash and cash equivalents in the United States and Europe, respectively.

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Note 4: Accounts Receivable and Revenue Concentrations

Accounts receivable consisted of the following at June 30, 2007 and December 31, 2006:

(In thousands)	June 30, 2007	December 31, 2006
Trade receivable, gross	$ 62,555	$ 55,726
Allowance for doubtful accounts	(2,228)	(2,602)
Allowance for sales returns	(1,307)	(1,894)
Net trade receivable	59,020	51,230
Other receivables:		
Note receivable [1]	205	200
Other [2]	409	437
Accounts receivable, net	$ 59,634	$ 51,867

[1] In April 1999, we provided a $200 thousand non-recourse interest bearing secured loan to our chief executive officer, which is due by December 15, 2007. The note and related interest are classified as a current asset.

[2] Other receivables as of June 30, 2007 and December 31, 2006 consisted primarily of a tenant improvement allowance provided by our

landlord for the renovation and expansion of our corporate headquarters in Cypress, California. Construction is expected to be complete by the end of 2007. The tenant improvement allowance will be paid upon completion of construction.

Significant Customers

We had sales to one significant customer that contributed more than 10% of total net sales. Sales made to this customer were $12.4 million and $7.0 million, representing 17.4% and 13.3% of our total net sales for the three months ended June 30, 2007 and 2006, respectively. Sales made to this customer during the six months ended June 30, 2007 and 2006 amounted to $22.5 million and $14.0 million, representing 16.4% and 13.1% of total net sales, respectively. Trade receivables with this customer amounted to $9.2 million and $3.1 million, or 15.6% and 6.0% of our net trade receivable at June 30, 2007 and December 31, 2006, respectively.

In addition, we had sales to another customer and its sub-contractors that, when combined, totaled $12.1 million and $7.0 million, representing 17.0% and 12.7% of total net sales for the three months ended June 30, 2007 and 2006, respectively. Sales made to this customer and its sub-contractors during the six months ended June 30, 2007 and 2006 amounted to $23.0 million and $18.7 million, representing 16.7% and 17.5% of total net sales, respectively. Trade receivables with this customer and its sub-contractors amounted to $9.0 million and $6.2 million, or 15.2% and 12.2% of our net trade receivable at June 30, 2007 and December 31, 2006, respectively.

The future loss of either of these customers or of any other key customer (in the United States or abroad, for any reason, including the financial weakness or bankruptcy of the customer or our inability to obtain orders or our inability to maintain order volume) would have an adverse effect on our financial condition, results of operations and cash flows.

Note 5: Inventories and Significant Suppliers

Inventories

Inventories, which consist of wireless control devices, including universal remote controls, antennas and related component parts, are valued at the lower of cost or market. Cost, which is determined using the first-in, first-out method includes the purchase of integrated circuits, sub-contractor costs and freight-in. We carry inventory in amounts necessary to satisfy our customers inventory requirements on a timely basis.

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Product innovations and technological advances may shorten a given product s life cycle. We continually monitor inventory to control inventory levels and dispose of any excess or obsolete inventories on hand. We write down our inventory for estimated obsolescence or unmarketable inventory, in an amount equal to the difference between the cost of the inventory and its estimated market value based upon our best estimates about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional inventory write-downs may be required.

Net inventories consisted of the following at June 30, 2007 and December 31, 2006:

(In thousands)		**June 30, 2007**		**December 31, 2006**
Components	$	7,168	$	6,101
Finished goods		22,264		22,537
Reserve for inventory scrap		(2,160)		(2,179)
Inventory, net	$	27,272	$	26,459

During the three months ended June 30, 2007 and 2006 inventory write-downs totaled $0.5 million and $0.5 million, respectively. During the six months ended June 30, 2007 and 2006 inventory write-downs totaled $1.0 million and $0.6 million, respectively. Inventory write-downs are a normal part of our business and result primarily from product life cycle estimation variances.

Significant Suppliers

Most of the components used in our products are available from multiple sources. We have elected to purchase integrated circuits (IC), used principally in our wireless control products, from two main sources. Purchases from one supplier amounted to more than 10% of total inventory purchases. Purchases from this major supplier amounted to $5.5 million and $3.2 million, representing 13.3% and 8.5% of total inventory purchases for the three months ended June 30, 2007 and 2006, respectively. Purchases made from this supplier during the six months ended June 30, 2007 and 2006 amounted to $10.7 million and $5.6 million, representing 14.0% and 8.9% of total inventory purchases, respectively. Accounts payable with that supplier amounted to $2.4 million and $0.8 million, representing 8.9% and 3.9% of total accounts payable at June 30, 2007 and December 31, 2006, respectively. For the three and six months ended June 30, 2006, a different IC supplier provided more than 10% of total inventory purchases. Purchases from that supplier amounted to $4.2 million and $7.1 million, representing 11.4% and 11.2% of total inventory purchases for the three and six months ended June 30, 2006, respectively.

In addition, during the three months ended June 30, 2007, we purchased component and finished good products from three major suppliers. Purchases from these three major suppliers amounted to $11.5 million, $9.1 million and $4.6 million, representing 27.9%, 21.8% and 11.1%, respectively, of total inventory purchases for the three months ended June 30, 2007. During the three months ended June 30, 2006 purchases from the same three suppliers amounted to $10.3 million, $2.2 million and $2.9 million, representing 27.7%, 5.8% and 7.7%, respectively, of total inventory purchases. During the six months ended June 30, 2007 purchases from these three suppliers amounted to $21.3 million, $14.3 million and $8.4 million, representing 27.7%, 18.7% and 11.0%, respectively, of total inventory purchases. During the same period last year, purchases from these three suppliers amounted to $18.7 million, $3.6 million and $3.4 million, representing 29.4%, 5.6% and 5.4% of total inventory purchases. For the three and six months ended June 30, 2006, one other supplier provided more than 10% of total inventory purchases. Purchases from this supplier amounted to $4.6 million and $7.5 million, representing 12.3% and 11.8%, of total inventory purchases for the three and six months ended June 30, 2006, respectively.

Accounts payable with the aforementioned three suppliers of component and finished good products amounted to $8.6 million, $4.8 million and $3.5 million, representing 31.7%, 17.7% and 12.8%, respectively, of total accounts payable at June 30, 2007. At December 31, 2006, accounts payable with the same three suppliers amounted to $8.2 million, $2.0 million and $3.4 million, representing 40.4%, 9.8% and 17.1%, respectively, of total accounts payable. No other component and finished goods supplier accounted for inventory purchases exceeding ten percent of the total inventory purchases for the three and six months ended June 30, 2007 or 2006.

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We have identified alternative sources of supply for these integrated circuits, components, and finished goods; however, there can be no assurance that we will be able to continue to purchase inventory on a timely basis from any of these sources. We generally maintain inventories of our integrated chips, which could be used in part to mitigate, but not eliminate, delays resulting from supply interruptions. An extended interruption, a shortage or termination in the supply of any of the components used in our products, a reduction in their quality or reliability, or a significant increase in prices of components, would have an adverse effect on our business, results of operations and cash flows.

Note 6: Income Taxes

We use the estimated annual effective tax rate to determine our provision for income taxes for interim periods. We recorded income tax expense of $2.2 million for the three months ended June 30, 2007 compared to $1.6 million for the same period last year. Our estimated effective tax rate was 32.5% and 39.2% during the three months ended June 30, 2007 and 2006, respectively. We recorded income tax expense of $4.4 million for the six months ended June 30, 2007 compared to $2.7 million for the same period last year. Our estimated effective tax rate was 32.5% and 36.9% during the six months ended June 30, 2007 and 2006, respectively. The decrease in our effective tax rate is due primarily to the re-enactment of the federal research and development tax credit statute which was passed by Congress in the fourth quarter of 2006 as well as the Netherlands statutory tax rate decreasing from 31.5% in 2006 to 25.5% in 2007, offset partially by increased pre-tax income in higher tax rate jurisdictions.

We adopted the provisions of FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes- an interpretation of FASB Statement No. 109* (FIN 48) effective January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*, and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

In accordance with the adoption of FIN 48 effective January 1, 2007, we evaluate our tax positions to determine if it is more likely than not that a tax position is sustainable, based on its technical merits. If a tax position does not meet the more likely than not standard, a full reserve is established against the tax asset or a liability is recorded. Additionally, for a position that is determined to, more likely than not, be sustainable, we measure the benefit at the greatest cumulative probability of being realized and establish a reserve or liability for the balance. A material change in our tax reserves could have a significant impact on our results.

As a result of implementing FIN 48, we recognized a $0.2 million increase in our liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007 balance of retained earnings. We recorded an increase in our unrecognized tax benefits of approximately $0.1 million and $0.2 million for the three and six months ended June 30, 2007, respectively. We had unrecognized tax benefits of approximately $6.8 million as of January 1, 2007, of which $6.3 million, if recognized, would result in the reduction of our effective tax rate. The open statute of limitations for our significant tax jurisdiction are as follows: federal and state for 2002 through 2006 and non-U.S. for 2001 through 2006. In accordance with FIN 48, we have elected to classify interest and penalties as components of tax expense. Interest and penalties are $0.6 million at the date of adoption and as of June 30, 2007 and are included in the unrecognized tax benefits. All unrecognized tax benefits at June 30, 2007 are classified as long term a