L 3 COMMUNICATIONS CORP
Form 10-Q
November 04, 2009

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

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

For the quarterly period ended September 25, 2009

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 numbers 001-14141 and 333-46983

L-3 COMMUNICATIONS HOLDINGS, INC.
L-3 COMMUNICATIONS CORPORATION
(Exact names of registrants as specified in their charters)

Delaware (State or other jurisdiction of incorporation or organization)	**13-3937434 and 13-3937436** (I.R.S. Employer Identification Nos.)
600 Third Avenue, New York, NY (Address of principal executive offices)	**10016** (Zip Code)

(212) 697-1111
(Telephone number)

Indicate by check mark whether the registrants (1) have 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 registrants were required to file such reports), and (2) have been subject to such filing requirements for the past 90 days. x Yes o No

Indicate by check mark whether the registrants have submitted electronically and posted on their corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrants were required to submit and post such files). x Yes o No

Indicate by check mark whether the registrants are large accelerated filers, accelerated filers, non-accelerated filers, or smaller reporting companies. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrants are shell companies (as defined in Rule 12b-2 of the Act). o Yes x No

There were 116,225,477 shares of L-3 Communications Holdings, Inc. common stock with a par value of $0.01 outstanding as of the close of business on October 30, 2009.

L-3 COMMUNICATIONS HOLDINGS, INC.
AND L-3 COMMUNICATIONS CORPORATION

INDEX TO QUARTERLY REPORT ON FORM 10-Q
For the quarterly period ended September 25, 2009

PART I FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

L-3 COMMUNICATIONS HOLDINGS, INC.
AND L-3 COMMUNICATIONS CORPORATION

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(in millions, except share data)

	September 25, 2009	December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,191	$ 867
Billed receivables, net of allowances, of $33 in 2009 and $26 in 2008	1,270	1,226
Contracts in process	2,398	2,267
Inventories	258	259
Deferred income taxes	169	211
Other current assets	127	131
Total current assets	5,413	4,961
Property, plant and equipment, net	838	821
Goodwill	8,188	8,029
Identifiable intangible assets	390	417
Deferred debt issue costs	35	44
Other assets	204	212
Total assets	$ 15,068	$ 14,484
LIABILITIES AND EQUITY		
Current liabilities:		
Current portion of long-term debt	$ 650	$
Accounts payable, trade	593	602
Accrued employment costs	674	700
Accrued expenses	525	479
Advance payments and billings in excess of costs incurred	499	530
Income taxes	30	45
Other current liabilities	336	351
Total current liabilities	3,307	2,707
Pension and postretirement benefits	844	802
Deferred income taxes	179	127
Other liabilities	424	414

Long-term debt		3,860		4,493
Total liabilities		8,614		8,543
Commitments and contingencies (see Note 16)				
Equity:				
L-3 shareholders equity:				
L-3 Communications Holdings, Inc. s common stock: $.01 par value; 300,000,000 shares authorized, 116,136,178 shares outstanding at September 25, 2009 and 118,633,746 shares outstanding at December 31, 2008 (L-3 Communications Corporation s common stock: $.01 par value, 100 shares authorized, issued and outstanding)		4,345		4,136
L-3 Communications Holdings, Inc. s treasury stock at cost, 19,633,649 shares at September 25, 2009 and 13,995,450 shares at December 31, 2008		(1,715)		(1,319)
Retained earnings		3,922		3,373
Accumulated other comprehensive loss		(190)		(332)
Total L-3 shareholders equity		6,362		5,858
Noncontrolling interests		92		83
Total equity		6,454		5,941
Total liabilities and equity	$	15,068	$	14,484

See notes to unaudited condensed consolidated financial statements.

L-3 COMMUNICATIONS HOLDINGS, INC.
AND L-3 COMMUNICATIONS CORPORATION

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in millions, except per share data)

	Third Quarter Ended	
	September 25, 2009	September 26, 2008
Net sales:		
Products	$ 1,810	$ 1,752
Services	2,032	1,910
Total net sales	3,842	3,662
Cost of sales:		
Products	1,586	1,561
Services	1,838	1,701
Total cost of sales	3,424	3,262
Operating income	418	400
Interest and other income, net	3	7
Interest expense	68	72
Income before income taxes	353	335
Provision for income taxes	100	123
Net income	$ 253	$ 212
Less: Net income attributable to noncontrolling interests	3	2
Net income attributable to L-3	$ 250	$ 210
Less: Net income allocable to participating securities	2	3
Net income allocable to L-3 Communications Holdings, Inc. s common shareholders	$ 248	$ 207
L-3 Communications Holdings, Inc. s earnings per common share:		
Basic	$ 2.13	$ 1.71
Diluted	$ 2.12	$ 1.70
L-3 Communications Holdings, Inc. s weighted average common shares outstanding:		
Basic	116.4	121.0

Diluted	117.0	122.0

See notes to unaudited condensed consolidated financial statements.

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L-3 COMMUNICATIONS HOLDINGS, INC.
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UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in millions, except per share data)

	Year-to-Date Ended September 25, 2009	Year-to-Date Ended September 26, 2008
Net sales:		
Products	$ 5,456	$ 5,120
Services	5,951	5,770
Total net sales	11,407	10,890
Cost of sales:		
Products	4,842	4,588
Services	5,354	5,159
Total cost of sales	10,196	9,747
Litigation Gain		126
Operating income	1,211	1,269
Interest and other income, net	12	22
Interest expense	203	214
Income before income taxes	1,020	1,077
Provision for income taxes	339	395
Net income	$ 681	$ 682
Less: Net income attributable to noncontrolling interests	7	8
Net income attributable to L-3	$ 674	$ 674
Less: Net income allocable to participating securities	6	6
Net income allocable to L-3 Communications Holdings, Inc. s common shareholders	$ 668	$ 668
L-3 Communications Holdings, Inc. s earnings per common share:		
Basic	$ 5.70	$ 5.48
Diluted	$ 5.68	$ 5.42

L-3 Communications Holdings, Inc. s weighted average common shares outstanding:		
Basic	117.1	121.8
Diluted	117.6	123.2

See notes to unaudited condensed consolidated financial statements.

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L-3 COMMUNICATIONS HOLDINGS, INC.
AND L-3 COMMUNICATIONS CORPORATION

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF EQUITY
(in millions, except per share data)

	L-3 Communications Holdings, Inc. s Common Stock							
	Shares Issued	Par Value	Additional Paid-in Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Noncontrolling Interests	Total Equity
For the Year-to-Date ended September 25, 2009:								
Balance at December 31, 2008	118.6	$ 1	$ 4,135	$ (1,319)	$ 3,373	$ (332)	$ 83	$ 5,941
Comprehensive income:								
Net income					674		7	681
Pension and postretirement benefit plans:								
Amortization of net loss and prior service cost previously recognized, net of income taxes of $16						23		23
Unrealized gain on hedging instruments, net of income taxes of $1						3		3
Foreign currency translation adjustment						116		116
Total comprehensive income								823
Distributions to noncontrolling interests							(6)	(6)
Cash dividends paid on common stock ($1.05 per share)					(124)			(124)
Recognition of non-controlling interest in consolidated subsidiary							8	8
Shares issued:								
Employee savings plans	1.6		110					110

Exercise of stock options	0.3		14					14
Employee stock purchase plan	1.1		34					34
Stock-based compensation expense			53					53
Treasury stock purchased	(5.6)			(396)				(396)
Other	0.1		(2)		(1)			(3)
Balance at September 25, 2009	116.1	$ 1	$ 4,344	$ (1,715)	$ 3,922	$ (190)	$ 92	$ 6,454
For the Year-to-Date ended September 26, 2008:								
Balance at December 31, 2007	124.2	$ 1	$ 3,816	$ (525)	$ 2,582	$ 153	$ 87	$ 6,114
Comprehensive income:								
Net income					674		8	682
Pension and postretirement benefit plans:								
Amortization of net loss and prior service cost previously recognized, net of income taxes of $1						2		2
Unrealized gain on hedging instruments, net of income taxes of $2						4		4
Foreign currency translation adjustment						(54)		(54)
Total comprehensive income								634
Distributions to noncontrolling interests							(8)	(8)
Cash dividends paid on common stock ($0.90 per share)					(111)			(111)
Shares issued:								
Employee savings plans	1.0		108					108
Exercise of stock options	0.7		50					50
Employee stock purchase plan	0.8		35					35
Stock-based compensation expense			48					48
Treasury stock purchased	(5.6)			(573)				(573)
Other			(5)					(5)
	121.1	$ 1	$ 4,052	$ (1,098)	$ 3,145	$ 105	$ 87	$ 6,292

Balance at
September 26, 2008

See notes to unaudited condensed consolidated financial statements.

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L-3 COMMUNICATIONS HOLDINGS, INC.
AND L-3 COMMUNICATIONS CORPORATION

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions)

	Year-to-Date Ended	
	September 25, 2009	September 26, 2008
Operating activities:		
Net income	$ 681	$ 682
Depreciation of property, plant and equipment	117	114
Amortization of intangibles and other assets	45	41
Deferred income tax provision	36	143
Stock-based employee compensation expense	53	48
Contributions to employee savings plans in L-3 Communications Holdings, Inc. s common stock	110	108
Amortization of pension and postretirement benefit plans net loss and prior service cost	39	3
Amortization of bond discounts (included in interest expense)	17	15
Amortization of deferred debt issue costs (included in interest expense)	8	8
Impairment charge		28
Gain on sale of a product line		(12)
Other non-cash items	(2)	(6)
Subtotal	1,104	1,172
Changes in operating assets and liabilities, excluding acquired amounts:		
Billed receivables	(18)	(2)
Contracts in process	(98)	(161)
Inventories	(3)	(32)
Other assets		(31)
Accounts payable, trade	10	171
Accrued employment costs	(44)	(23)
Accrued expenses	1	30
Advance payments and billings in excess of costs incurred	(35)	71
Income taxes	32	(10)
Excess income tax benefits related to share-based payment arrangements	(3)	(10)
Other current liabilities	(20)	(143)
Pension and postretirement benefits	40	17
All other operating activities	12	(18)
Subtotal	(126)	(141)
Net cash from operating activities	978	1,031
Investing activities:		

Business acquisitions, net of cash acquired	(86)	(224)
Proceeds from sale of product lines		12
Capital expenditures	(128)	(139)
Dispositions of property, plant and equipment	3	5
Other investing activities		(6)
Net cash used in investing activities	(211)	(352)
Financing activities:		
Common stock repurchased	(396)	(573)
Dividends paid on L-3 Communications Holdings, Inc. s common stock	(124)	(111)
Proceeds from exercise of stock options	11	38
Proceeds from employee stock purchase plan	51	52
Excess income tax benefits related to share-based payment arrangements	3	10
Other financing activities	(9)	(11)
Net cash used in financing activities	(464)	(595)
Effect of foreign currency exchange rate changes on cash and cash equivalents	21	(7)
Net increase in cash and cash equivalents	324	77
Cash and cash equivalents, beginning of the period	867	780
Cash and cash equivalents, end of the period	$ 1,191	$ 857

See notes to unaudited condensed consolidated financial statements.

L-3 COMMUNICATIONS HOLDINGS, INC.
AND L-3 COMMUNICATIONS CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS

1. Description of Business

L-3 Communications Holdings, Inc. derives all of its operating income and cash flows from its wholly-owned subsidiary, L-3 Communications Corporation (L-3 Communications). L-3 Communications Holdings, Inc. (L-3 Holdings and, together with its subsidiaries, referred to herein as L-3 or the Company) is a prime system contractor in aircraft modernization and maintenance, Command, Control, Communications, Intelligence, Surveillance and Reconnaissance (C^3ISR) systems, and government services. L-3 is also a leading provider of high technology products, subsystems and systems. The Company s customers include the U.S. Department of Defense (DoD) and its prime contractors, U.S. Government intelligence agencies, the U.S. Department of Homeland Security (DHS), U.S. Department of State (DoS), U.S. Department of Justice (DoJ), allied foreign governments, domestic and foreign commercial customers and select other U.S. federal, state and local government agencies.

The Company has the following four reportable segments: (1) C^3ISR, (2) Government Services, (3) Aircraft Modernization and Maintenance (AM&M), and (4) Specialized Products. Financial information with respect to each of the Company s reportable segments is included in Note 20. C^3ISR provides products and services for the global ISR market, C^3 systems, networked communications systems and secure communications products. The Company believes that these products and services are critical elements for a substantial number of major command, control and communication, intelligence gathering and space systems. These products and services are used to connect a variety of airborne, space, ground and sea-based communication systems and are used in the transmission, processing, recording, monitoring, and dissemination functions of these communication systems. Government Services provides a full range of engineering, technical, information technology (IT), advisory, training and support services to the DoD, DoS, DoJ, and U.S. Government intelligence agencies and allied foreign governments. AM&M provides modernization, upgrades and sustainment, maintenance and logistics support services for military and various government aircraft and other platforms. The Company sells these services primarily to the DoD, the Canadian Department of Defense (DND) and other allied foreign governments. Specialized Products provides a broad range of products, including components, products, subsystems, systems, and related services to military and commercial customers in several niche markets across several business areas, including power & control systems, electro-optic/infrared (EO/IR), microwave, simulation & training, precision engagement, aviation products, security & detection, propulsion systems, displays, telemetry & advanced technology, undersea warfare, and marine services.

2. Basis of Presentation

These unaudited condensed consolidated financial statements for the quarterly period and year-to-date period ended September 25, 2009 should be read in conjunction with the audited consolidated financial statements of L-3 Holdings and L-3 Communications included in their Annual Report on Form 10-K for the fiscal year ended December 31, 2008.

The Company adopted eight new accounting standards during the year-to-date period ended September 25, 2009, six of which were effective January 1, 2009. In accordance with the transition and disclosure provisions of three of these standards, the Company retrospectively applied those provisions and adjusted the prior period financial statements accordingly. See Note 3 for the standards adopted and their impact to the Company s financial position and results of operations.

The accompanying financial statements comprise the consolidated financial statements of L-3 Holdings and L-3 Communications. L-3 Holdings only asset is its investment in the common stock of L-3 Communications, its wholly-owned subsidiary, and its only obligations are: (1) the 3% Convertible Contingent Debt Securities (CODES) due 2035, which were issued by L-3 Holdings on July 29, 2005, (2) its guarantee of borrowings under the senior credit facility of L-3 Communications and (3) its guarantee of other contractual obligations of L-3 Communications and its subsidiaries. L-3 Holdings obligations relating to the CODES have been jointly, severally, fully and

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**L-3 COMMUNICATIONS HOLDINGS, INC.
AND L-3 COMMUNICATIONS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS (Continued)**

unconditionally guaranteed by L-3 Communications and certain of its wholly-owned domestic subsidiaries. Accordingly, such debt has been reflected as debt of L-3 Communications in its consolidated financial statements in accordance with the U.S. Securities and Exchange Commission s (SEC) Staff Accounting Bulletin (SAB) No. 54. All issuances of and conversions into L-3 Holdings equity securities, including grants of stock options, restricted stock, restricted stock units and performance units by L-3 Holdings to employees and directors of L-3 Communications and its subsidiaries, have been reflected in the consolidated financial statements of L-3 Communications. As a result, the consolidated financial positions, results of operations and cash flows of L-3 Holdings and L-3 Communications are substantially the same. See Note 22 for additional information regarding the unaudited financial information of L-3 Communications and its subsidiaries.

The unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X of the SEC. Accordingly, they do not include all of the disclosures required by U.S. GAAP for a complete set of annual audited financial statements. In the opinion of management, all adjustments (consisting of normal and recurring adjustments) considered necessary for a fair presentation of the results for the interim periods presented have been included. The results of operations for the interim periods are not necessarily indicative of results for the full year.

Certain reclassifications have been made to conform prior year amounts to the current year presentation.

It is the Company s established practice to close its books for the quarters ending March, June and September on the Friday nearest to the end of the calendar quarter. The interim unaudited condensed consolidated financial statements included herein have been prepared and are labeled based on that convention. The Company closes its annual books on December 31 regardless of what day it falls on.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of sales and costs of sales during the reporting period. The most significant of these estimates and assumptions relate to contract revenue, profit and loss recognition, fair values of assets acquired and liabilities assumed in business combinations, market values for inventories reported at lower of cost or market, pension and post-retirement benefit obligations, stock-based employee compensation expense, income taxes, including the valuations of deferred tax assets, litigation reserves and environmental obligations, accrued product warranty costs, and the recoverability, useful lives and valuation of recorded amounts of long-lived assets, identifiable intangible assets and goodwill. Changes in estimates are reflected in the periods during which they become known. Actual amounts will differ from these estimates and could differ materially. For a more complete discussion of these estimates and assumptions, see the Annual Report of L-3 Holdings and L-3 Communications on Form 10-K for the fiscal year ended December 31, 2008.

During the quarter ended March 27, 2009, the Company revised its reportable segment presentations to conform to certain re-alignments in the Company s management and organization structure. Consequently, the Company made certain reclassifications between its C^3ISR, Government Services, and AM&M reportable segments. See Note 20 for the prior period amounts reclassified between reportable segments.

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**L-3 COMMUNICATIONS HOLDINGS, INC.
AND L-3 COMMUNICATIONS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS (Continued)**

3. New Accounting Standards Implemented

In June 2009, the Financial Accounting Standards Board (FASB) issued the FASB Accounting Standards Codifications (Codification). The Codification has become the single source for all authoritative U.S. GAAP recognized by the FASB, does not change U.S. GAAP and did not impact the Company s financial position, results of operations and cash flows. All references to U.S. GAAP in this report are in accordance with the Codification.

The Company adopted eight newly issued accounting standards during the year-to-date period ended September 25, 2009. The following six standards were effective January 1, 2009:

Accounting for convertible debt instruments that may be settled in cash upon conversion (Convertible Debt). The new standard is contained in FASB Accounting Standards Codification (ASC) Topic 470, *Debt*;

Determining whether instruments granted in share-based payment transactions are participating securities (Participating Securities). The new standard is contained in FASB ASC Topic 260, *Earnings Per Share;*

Noncontrolling interests in consolidated financial statements (Noncontrolling Interests). The new standard is contained in FASB ASC Topic 810, *Consolidation*;

Disclosures about derivative instruments and hedging activities (Derivative Disclosures). The new standard is contained in FASB ASC Topic 815, *Derivatives and Hedging*;

Business combinations (Business Combinations). The new standard is contained in FASB ASC Topic 805, *Business Combinations;* and

Fair value measurements and disclosures (Fair Value Measurements). The new standard is contained in FASB ASC Topic 820, *Fair Value Measurements and Disclosures.*

For the impact of the adoption of the newly issued standards for Convertible Debt, Participating Securities and Noncontrolling Interests on the Company s: (1) Condensed Consolidated Balance Sheet, at December 31, 2008, (2) Consolidated Equity Account Balances, at December 31, 2007, and (3) Condensed Consolidated Statements of Operations for the quarter and year-to-date periods ended September 26, 2008, see pages 11-13. The adoption of the new accounting standards for Derivative Disclosures, Business Combinations and Fair Value Measurements did not have a material impact on the Company s prior period financial statements.

Convertible Debt: In accordance with the provisions of the newly issued standard for convertible debt, the Company is separately accounting for the liability and equity (conversion option) components of the CODES in a manner that reflects the Company s non-convertible debt borrowing rate when interest expense is recognized. Previously, the CODES were recorded at maturity value. The Convertible Debt standard does not apply to the Company s other outstanding debt instruments because they are not convertible debt instruments within its scope. The Company has retrospectively applied the provisions of this standard and adjusted the prior period financial statements accordingly.

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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS (Continued)**

The following table presents the impact of the provisions of the Convertible Debt standard on the Statements of Operations for the quarter and year-to-date period ended September 25, 2009.

	Third Quarter Ended September 25, 2009	Year-to-Date Ended September 25, 2009
	(in millions, except per share data)	
Interest expense	$ 5	$ 15
Provision for income taxes	(2)	(6)
Net income attributable to L-3	(3)	(9)
L-3 Holdings earnings per common share:		
Basic	$ (0.03)	$ (0.08)
Diluted	$ (0.02)	$ (0.08)

Participating Securities: In accordance with the provisions of the newly issued standard for participating securities, the Company is including the impact of restricted stock and restricted stock units that are entitled to receive non-forfeitable dividends when calculating both basic EPS and diluted EPS. The Company has retrospectively applied the provisions of this standard and adjusted the prior period financial statements accordingly. The adoption of the provisions of this standard decreased basic EPS by $0.02 and diluted EPS by $0.01 for the quarter ended September 25, 2009 and decreased basic EPS by $0.05 and diluted EPS by $0.02 for the year-to-date period ended September 25, 2009.

Noncontrolling Interests: The Company retrospectively applied the presentation requirements of the newly issued standard for noncontrolling interest by: (1) reclassifying noncontrolling interests (minority interests) to equity on the Company s balance sheets, and (2) including net income attributable to noncontrolling interests in net income on the Company s statements of operations.

Derivative Disclosures: The enhanced disclosures for derivative instruments and related hedging activities required in accordance with the provisions of this standard can be found in Note 15.

Business Combinations: The Company adopted the provisions of the newly issued standard for business combinations to its acquisition of Chesapeake Sciences Corporation (CSC), which was completed on January 30, 2009. See Note 4 for additional information regarding the CSC acquisition. There were no other material business acquisitions completed during the year-to-date period ended September 25, 2009. In accordance with the provisions of this standard, the Company is: (1) expensing transaction and restructuring costs, (2) recognizing and measuring contingent consideration at fair value, (3) measuring contingent assets and liabilities at fair value, or in accordance with FASB ASC Topic 450, *Contingencies,* as appropriate, and (4) capitalizing in-process research and development. In addition, the difference between the ultimate resolution and the amount recorded on the balance sheet for acquired uncertain tax positions is recorded through earnings. Previously, the difference would have been recorded through goodwill. Other than the net reversal of amounts previously accrued of $26 million disclosed in Note 11, the adoption of this standard did not have a material impact on the Company s financial position, results of operations and cash flows for the quarter and year-to-date period ended September 25, 2009.

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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS (Continued)**

Fair Value Measurements: The Company applied the provisions of the standard for fair value measurements to non-financial assets and non-financial liabilities not recognized or disclosed at fair value in the financial statements on a recurring basis. The effective date for application of the provisions of this standard to all non-financial assets and non-financial liabilities not recognized or disclosed at fair value on a recurring basis was previously delayed until January 1, 2009. The application of the provisions of the fair value measurement standard had no impact on the Company s financial position, results of operations and cash flows as the Company did not have any non-financial assets and non-financial liabilities that were recognized or disclosed at fair value on a non-recurring basis at September 25, 2009.

Effective June 26, 2009, the Company adopted the following two new accounting standards:

Subsequent Events (Subsequent Events). The new standard is contained in FASB ASC Topic 855, *Subsequent Events*; and

Interim Disclosures about Fair Value of Financial Instruments (Financial Instruments). The new standard is contained in FASB ASC Topic 825, *Financial Instruments*.

Subsequent Events: The adoption of the provisions of the newly issued standard for subsequent events requires the Company to evaluate events after the balance sheet date and disclose the date through which the evaluation is performed. The Company has evaluated subsequent events through the time of filing this Form 10-Q with the SEC on November 4, 2009.

Financial Instruments: The adoption of the provisions of the newly issued standard for financial instruments requires: (1) the fair value disclosures of an entity s financial instruments for interim financial statements, and (2) disclosures about the methods and significant assumptions used to estimate the fair value of financial instruments. See Note 15 for the disclosures required by the provisions of the Financial Instruments standard.

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L-3 COMMUNICATIONS HOLDINGS, INC.
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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below present the Company s As Previously Reported and As Currently Reported: (1) Condensed Consolidated Balance Sheet, at December 31, 2008, (2) Consolidated Equity Account Balances, at December 31, 2007, and (3) Condensed Consolidated Statement of Operations, for the quarter and year-to-date period ended September 26, 2008, in each case to reflect the adjustments made to adopt the provisions of the newly issued standards for Noncontrolling Interests, Convertible Debt and Participating Securities, as applicable.

		Adjustments for:		
	As Previously Reported	Noncontrolling Interests	Convertible Debt	As Currently Reported
		(in millions)		
Condensed Consolidated Balance Sheet, at December 31, 2008:				
ASSETS				
Total current assets	$ 4,961	$	$	$ 4,961
Property, plant and equipment, net	821			821
Goodwill	8,029			8,029
Identifiable intangible assets	417			417
Deferred debt issue costs	45		(1)	44
Other assets	212			212
Total assets	$ 14,485	$	$ (1)	$ 14,484
LIABILITIES AND EQUITY				
Total current liabilities	$ 2,707	$	$	$ 2,707
Pension and postretirement benefits	802			802
Deferred income taxes	110		17	127
Other liabilities	414			414
Long-term debt	4,538		(45)	4,493
Total liabilities	8,571		(28)	8,543
Minority interests	83	(83)		
Equity:				
L-3 shareholders equity:				
L-3 Communications Holdings Inc. s common stock	4,072		64	4,136
L-3 Communications Holdings Inc. s treasury stock at cost	(1,319)			(1,319)

Retained earnings		3,410				(37)		3,373
Accumulated other comprehensive loss		(332)						(332)
Total L-3 shareholders equity		5,831				27		5,858
Noncontrolling interests				83				83
Total equity		5,831		83		27		5,941
Total liabilities and equity	$	14,485	$		$	(1)	$	14,484
Consolidated Equity Account Balances, at December 31, 2007:								
L-3 Communications Holdings Inc. s common stock, net of treasury stock	$	3,228	$		$	64	$	3,292
Retained earnings		2,608				(26)		2,582
Accumulated other comprehensive income		153						153
Noncontrolling interests				87				87
Total equity	$	5,989	$	87	$	38	$	6,114

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	As Previously Reported	Adjustments for: Noncontrolling Interests	Participating Securities	Convertible Debt	As Currently Reported
	(in millions, except per share data)				
Condensed Consolidated Statement of Operations, for the quarter ended September 26, 2008:					
Net sales	$ 3,662	$	$	$	$ 3,662
Cost of sales	3,262				3,262
Operating income	400				400
Interest and other income, net	7				7
Interest expense	68			4	72
Minority interests in net income of consolidated subsidiaries	2	(2)			
Income before income taxes	337	2		(4)	335
Provision for income taxes	125			(2)	123
Net income	$ 212	$ 2	$	$ (2)	$ 212
Less: Net income attributable to noncontrolling interests		2			2
Net income attributable to L-3	$ 212	$	$	$ (2)	$ 210
Less: Net income allocable to participating securities			3		3
Net income allocable to L-3 Communications Holdings, Inc. s common shareholders	$ 212	$	$ (3)	$ (2)	$ 207
L-3 Communications Holdings, Inc. s earnings per common share:					
Basic	$ 1.75	$	$ (0.02)	$ (0.02)	$ 1.71
Diluted	$ 1.73	$	$ (0.01)	$ (0.02)	$ 1.70
L-3 Communications Holdings, Inc. s weighted average common shares					

outstanding:			
Basic	121.0		121.0
Diluted	122.6	(0.6)	122.0

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			Adjustments for:		
	As Previously Reported	Noncontrolling Interests	Participating Securities	Convertible Debt	As Currently Reported
		(in millions, except per share data)			
Condensed Consolidated Statement of Operations, for the year-to-date period ended September 26, 2008:					
Net sales	$ 10,890	$	$	$	$ 10,890
Cost of sales	9,747				9,747
Litigation Gain	126				126
Operating income	1,269				1,269
Interest and other income, net	22				22
Interest expense	200			14	214
Minority interests in net income of consolidated subsidiaries	8	(8)			
Income before income taxes	1,083	8		(14)	1,077
Provision for income taxes	401			(6)	395
Net income	$ 682	$ 8	$	$ (8)	$ 682
Less: Net income attributable to noncontrolling interests		8			8
Net income attributable to L-3	$ 682	$	$	$ (8)	$ 674
Less: Net income allocable to participating securities			6		6
Net income allocable to L-3 Communications Holdings, Inc. s common shareholders	$ 682	$	$ (6)	$ (8)	$ 668
L-3 Communications Holdings, Inc. s earnings per common share:					
Basic	$ 5.60	$	$ (0.05)	$ (0.07)	$ 5.48
Diluted	$ 5.51	$	$ (0.02)	$ (0.07)	$ 5.42

L-3 Communications Holdings, Inc. s weighted average common shares outstanding:			
Basic	121.8		121.8
Diluted	123.7	(0.5)	123.2

4. Acquisitions and Dispositions

All of the business acquisitions are included in the Company s results of operations from their respective dates of acquisition.

2009 Business Acquisitions

On January 30, 2009, the Company acquired all of the outstanding stock of CSC for a preliminary purchase price of $92 million, consisting of: (1) $87 million in cash, including a $7 million net working capital adjustment, of which $6 million was for cash acquired, and (2) a purchase price payable of $5 million related to certain tax benefits acquired. CSC is a developer and manufacturer of anti-submarine warfare systems for use onboard submarines and surface ship combatants. Based on the preliminary purchase price allocation, the amount of goodwill recognized was $57 million, which was assigned to the Specialized Products reportable segment, and is not expected to be deductible for income tax purposes. The final purchase price allocation is expected to be completed during the

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fourth quarter of 2009, and will be based on final appraisals and other analyses of fair values for acquired assets and assumed liabilities. The Company does not expect any of the differences between the preliminary and final purchase price allocations to have a material impact on its results of operations and financial position. The acquisition was financed with cash on hand.

2008 Business Acquisitions

During the year-to-date period ended September 25, 2009, the Company completed the purchase price allocations for G.A. International (GAI) and International Resources Group, Ltd. (IRG), subject to the finalization of the purchase price for GAI. The purchase price for GAI is subject to additional consideration not to exceed $1 million that is contingent upon GAI s post-acquisition financial performance through July 25, 2011. Any additional consideration paid that is contingent upon post-acquisition performance will be accounted for as goodwill. The final purchase price allocations for these business acquisitions compared to the preliminary purchase price allocations did not have a material impact on the Company s results of operations or financial position.

Unaudited Pro Forma Statements of Operations Data

The following unaudited pro forma Statements of Operations data presents the combined results of the Company and its business acquisitions completed during the year-to-date period ended September 25, 2009 and the year ended December 31, 2008, in each case assuming that the business acquisitions that were completed during these periods had occurred on January 1, 2008.

	Third Quarter Ended		Year-to-Date Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
	(in millions, except per share data)			
Pro forma net sales	$ 3,842	$ 3,694	$ 11,413	$ 11,034
Pro forma net income attributable to L-3	$ 250	$ 212	$ 674	$ 676
Pro forma diluted EPS	$ 2.12	$ 1.71	$ 5.68	$ 5.43

The unaudited pro forma results disclosed in the table above are based on various assumptions and are not necessarily indicative of the results of operations that would have occurred had the Company completed these acquisitions on January 1, 2008.

2008 Business and Product Line Dispositions

On October 8, 2008, the Company divested its 85% ownership interest in Medical Education Technologies, Inc. (METI), which was within the Specialized Products reportable segment. The sale resulted in a fourth quarter 2008 after-tax gain of $20 million (pre-tax gain of $33 million). The gain was excluded from income from continuing operations for the 2008 fourth quarter in accordance with U.S. GAAP for impairment or disposal of long-lived assets (contained in FASB ASC Topic 360, *Property, Plant, and Equipment* and FASB ASC Topic 205, *Presentation of Financial Statements*).The revenues, operating results and net assets of METI for all periods presented were not material and, therefore, are not presented as discontinued operations. METI generated $17 million of sales and $2 million of operating income for the quarter ended September 26, 2008, $47 million of sales and $4 million of operating income for the year-to-date period ended September 26, 2008, and $48 million of sales and $4 million of operating income for the year ended December 31, 2008.

On May 9, 2008, the Company sold the Electron Technologies Passive Microwave Devices (PMD) product line, which was within the Specialized Products reportable segment. The sale resulted in a second quarter 2008 after-tax gain of approximately $7 million (pre-tax gain of $12 million), which was recorded as a reduction of cost

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of sales for products in the Unaudited Condensed Consolidated Statement of Operations. The net proceeds from the sale are included in investing activities on the Unaudited Condensed Consolidated Statement of Cash Flows. The PMD product line generated $8 million of sales for both the year-to-date period ended September 26, 2008 and the year ended December 31, 2008.

5. Contracts in Process

The components of contracts in process are presented in the table below.

	September 25, 2009	December 31, 2008
	(in millions)	
Unbilled contract receivables, gross	$ 2,318	$ 2,079
Less: unliquidated progress payments	(629)	(462)
Unbilled contract receivables, net	1,689	1,617
Inventoried contract costs, gross	846	754
Less: unliquidated progress payments	(137)	(104)
Inventoried contract costs, net	709	650
Total contracts in process	$ 2,398	$ 2,267

Inventoried Contract Costs. In accordance with FASB ASC Topic 605-35-25, *Revenue Recognition Construction-Type and Production-Type Contracts General*, the Company accounts for the portion of its general and administrative (G&A) costs, independent research and development (IRAD) costs and bid and proposal (B&P) costs that are allowable and reimbursable indirect contract costs under U.S. Government procurement regulations on its U.S. Government contracts (revenue arrangements) as inventoried contract costs. G&A, IRAD and B&P costs are allocated to contracts for which the U.S. Government is the end customer and are charged to costs of sales when sales on the related contracts are recognized. The Company s unallowable portion of its G&A, IRAD and B&P costs for its U.S. Government contractor businesses are expensed as incurred and are not included in inventoried contract costs.

The table below presents a summary of G&A, IRAD and B&P costs included in inventoried contract costs and the changes to them, including amounts charged to cost of sales for U.S. Government contracts for the periods presented.

	Third Quarter Ended		Year-to-Date Ended	
	September 25,	September 26,	September 25,	September 26,

	2009	2008	2009	2008
		(in millions)		
Amounts included in inventoried contract costs at beginning of the period	$ 79	$ 79	$ 74	$ 68
Add: Contract costs incurred[1]	305	335	951	935
Amounts included in acquired inventoried contract costs				7
Less: Amounts charged to cost of sales	(294)	(339)	(935)	(935)
Amounts included in inventoried contract costs at end of the period	$ 90	$ 75	$ 90	$ 75

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(1) Incurred costs include IRAD and B&P costs of $76 million for the quarter ended September 25, 2009, $74 million for the quarter ended September 26, 2008, $232 million for the year-to-date period ended September 25, 2009 and $211 million for the year-to-date period ended September 26, 2008.

The table below presents a summary of selling, general and administrative expenses and research and development expenses for the Company s commercial businesses, which are expensed as incurred and not included in inventoried contract costs.

	Third Quarter Ended		Year-to-Date Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
	(in millions)			
Selling, general and administrative expenses	$ 57	$ 70	$ 175	$ 209
Research and development expenses	17	19	54	67
Total	$ 74	$ 89	$ 229	$ 276

6. Inventories

Inventories at Lower of Cost or Market. The table below presents the components of inventories at cost (first-in, first-out or average cost), but not in excess of realizable value.

	September 25, 2009	December 31, 2008
	(in millions)	
Raw materials, components and sub-assemblies	$ 99	$ 95
Work in process	127	121
Finished goods	32	43
Total	$ 258	$ 259

7. Goodwill and Identifiable Intangible Assets

Goodwill. In accordance with U.S. GAAP for business combinations (contained in FASB ASC Topic 805, *Business Combinations*), the Company allocates the cost of business acquisitions to the assets acquired and liabilities assumed based on their fair values at the date of acquisition (commonly referred to as the purchase price allocation). The table below presents the changes in goodwill allocated to the Company s reportable segments.

	C^3ISR	Government Services	AM&M (in millions)	Specialized Products	Consolidated Total
Balance at December 31, 2008[1]	$ 862	$ 2,313	$ 1,121	$ 3,733	$ 8,029
Business acquisition		5		57	62
Foreign currency translation adjustments[2]	14	2	30	51	97
Balance at September 25, 2009	$ 876	$ 2,320	$ 1,151	$ 3,841	$ 8,188

(1) As a result of certain re-alignments in the Company s management and organization structure as discussed in Note 2, $17 million of goodwill was reclassified from the C^3ISR reportable segment to the Government Services reportable segment, and $17 million of goodwill was reclassified from the C^3ISR reportable segment to the AM&M reportable segment.

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(2) The increase in goodwill from foreign currency translation adjustments is due to the weakening of the U.S. dollar during the year-to-date period ended September 25, 2009 against the functional currencies of L-3 s foreign subsidiaries, primarily in Canada, Germany and the United Kingdom.

Identifiable Intangible Assets. Information on the Company s identifiable intangible assets that are subject to amortization is presented in the table below.

	September 25, 2009				December 31, 2008		
	Weighted Average Amortization Period (in years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
				(in millions)			
Customer contractual relationships	23	$ 515	$ 154	$ 361	$ 505	$ 124	$ 381
Technology	8	78	55	23	76	47	29
Other, primarily favorable leasehold interests	7	14	8	6	14	7	7
Total	22	$ 607	$ 217	$ 390	$ 595	$ 178	$ 417

Amortization expense recorded by the Company for its identifiable intangible assets is presented in the table below.

	Third Quarter Ended		Year-to-Date Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
		(in millions)		
Amortization expense	$ 13	$ 12	$ 39	$ 34

Based on gross carrying amounts at September 25, 2009, the Company s estimate of amortization expense for identifiable intangible assets for the years ending December 31, 2009 through 2013 are presented in the table below.

	Years Ending December 31,				
	2009	2010	2011	2012	2013
	(in millions)				
Estimated amortization expense	$ 52	$ 52	$ 47	$ 39	$ 30

At September 25, 2009 and December 31, 2008, the Company had $1 million of indefinite-lived identifiable intangible assets.

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8. Other Current Liabilities and Other Liabilities

The table below presents the components of other current liabilities.

	September 25, 2009	December 31, 2008
	(in millions)	
Other Current Liabilities:		
Accruals for pending and threatened litigation (see Note 16)	$ 3	$ 5
Accrued product warranty costs	91	97
Accrued interest	65	66
Estimated costs in excess of estimated contract value to complete contracts in process in a loss position	58	58
Deferred revenues	27	25
Aggregate purchase price payable for acquired businesses	5	
Other	87	100
Total other current liabilities	$ 336	$ 351

The table below presents the components of other liabilities.

	September 25, 2009	December 31, 2008
	(in millions)	
Other Liabilities:		
Non-current income taxes payable (see Note 11)	$ 176	$ 177
Deferred compensation	87	79
Accrued workers compensation	51	45
Unfavorable lease obligations	6	8
Non-current portion of net deferred gains from terminated interest rate swap agreements	6	9
Notes payable and capital lease obligations	10	10
Accrued product warranty costs	7	5
Other non-current liabilities	81	81
Total other liabilities	$ 424	$ 414

The table below presents the changes in the Company s accrued product warranty costs.

	Year-to-Date Ended September 25, 2009	September 26, 2008
	(in millions)	
Accrued product warranty costs[1]:		
Balance at January 1	$ 102	$ 98
Acquisitions during the period		5
Accruals for product warranties issued during the period	36	27
Foreign currency translation adjustments	2	(1)
Settlements made during the period	(42)	(30)
Balance at end of period	$ 98	$ 99

[1] Warranty obligations incurred in connection with long-term production contracts are accounted for within the contract estimates at completion (EACs) and are excluded from the above amounts. Balances include both long-term and short-term amounts.

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9. Debt

The components of debt and a reconciliation to the carrying amount of current and long-term debt are presented in the table below.

	September 25, 2009	December 31, 2008
	(in millions)	
L-3 Communications:		
Borrowings under Revolving Credit Facility[1]	$	$
Borrowings under Term Loan Facility[2]	650	650
7 5/8% Senior Subordinated Notes due 2012	750	750
6 1/8% Senior Subordinated Notes due 2013	400	400
6 1/8% Senior Subordinated Notes due 2014	400	400
5 7/8% Senior Subordinated Notes due 2015	650	650
6 3/8% Senior Subordinated Notes due 2015	1,000	1,000
Subtotal	3,850	3,850
L-3 Holdings:		
3% Convertible Contingent Debt Securities due 2035[3]	700	700
Principal amount of long-term debt	4,550	4,550
Less: Unamortized discounts	(40)	(57)
Carrying amount of long-term debt	4,510	4,493
Less: Current portion of long-term debt	(650)	
Carrying amount of long-term debt, excluding current portion	$ 3,860	$ 4,493

(1) The Company s five-year revolving credit facility, which was replaced on October 23, 2009 by a new $1 billion three-year revolving credit facility maturing on October 23, 2012, allowed for total aggregate borrowings of up to $1 billion. At September 25, 2009, available borrowings under the revolving credit facility were $965 million after reductions for outstanding letters of credit of $35 million.

(2) The interest rate at September 25, 2009 and December 31, 2008 was 1.12% and 2.70%, respectively, and was based on the LIBOR rate (as defined in the credit agreement) plus a spread. See Note 10 to the audited

consolidated financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2008 for additional information regarding the interest on borrowings under the term loan facility. Borrowings under the term loan facility were repaid on October 7, 2009 and are classified as a current liability as of September 25, 2009.

(3) Under select conditions, including if L-3 Holdings common stock price is more than 120% (currently $120.17) of the then current conversion price (currently $100.14) for a specified period, the conversion feature of the CODES will require L-3 Holdings, upon conversion, to pay the $700 million principal amount in cash, and if the settlement amount exceeds the principal amount, the excess will be settled in cash or stock or a combination thereof, at the Company s option. At the current conversion price of $100.14, the aggregate consideration to be delivered upon conversion would be determined based on 7.0 million shares of L-3 Holdings common stock. See Note 10 to the audited consolidated financial statements for the year ended December 31, 2008, included in the Company s Annual Report on Form 10-K for additional information regarding the CODES, including conditions for conversion. L-3 s stock price on October 30, 2009 was $72.29 per share. The effective interest rate on the CODES is 6.33%. Interest expense relates to both the contractual coupon interest and amortization of the discount on the liability components. Interest expense recognized was $11 million and $10 million for the third quarter periods ended September 25, 2009 and September 26, 2008, respectively, and $31 million and $30 million for the year-to-date periods ended September 25, 2009 and September 26, 2008, respectively. The following table provides additional information about the Company s CODES:

	September 25, 2009	**December 31, 2008**
	(in millions)	
Carrying amount of the equity component (conversion feature)	$ 64	$ 64
Unamortized discount of liability component being amortized through February 1, 2011	$ 29	$ 45
Net carrying amount of liability component	$ 671	$ 655

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On October 2, 2009, L-3 Communications issued $1 billion in aggregate principal amount of 5.20% Senior Notes due October 15, 2019 (2009 Notes). The 2009 Notes have an effective interest rate of 5.25% and were issued at a discount of $4 million. The discount was recorded as a reduction to the principal amount of the notes and will be amortized as an interest expense over the term of the notes. Interest on the 2009 Notes is payable semi-annually on April 15 and October 15 of each year, commencing on April 15, 2010. The net cash proceeds from this offering amounted to approximately $988 million after deducting the discounts, commissions and estimated expenses, and were used, together with cash on hand, to redeem L-3 Communications $750 million 75/8% Senior Subordinated Notes due in 2012 (2002 Notes) on November 2, 2009 and to repay L-3 Communications outstanding $650 million term loan on October 7, 2009. In connection with the redemption of the 2002 Notes, the Company will record a debt retirement charge in the fourth quarter of 2009 of approximately $9 million ($6 million after income tax, or $0.05 per diluted share). The 2009 Notes are unsecured senior obligations of L-3 Communications, rank equal in right of payment with all of L-3 Communications existing and future senior indebtedness and rank senior in right of payment to all of L-3 Communications existing and future senior subordinated indebtedness. The 2009 Notes are also guaranteed on a senior, unsecured basis by each of L-3 Communications material domestic subsidiaries that guarantee any of L-3 Communications other indebtedness. The 2009 Notes may be redeemed at any time prior to their maturity at the option of L-3 Communications, in whole or in part, at a redemption price equal to the greater of: (1) 100% of the principal amount, or (2) the present value of the remaining principal and interest payments discounted to the date of redemption, on a semi-annual basis, at the Treasury Rate (as defined in the credit agreement) plus 0.30%. For additional information on the terms of L-3 Communications 2009 Notes, including restrictive covenants, see the Company s Current Report on Form 8-K dated October 2, 2009 and the indenture governing the terms of the 2009 Notes, which is filed as an exhibit to this report.

On October 23, 2009, L-3 Communications replaced its $1 billion revolving credit facility with a new $1 billion three-year revolving credit facility maturing on October 23, 2012. Borrowings under the new revolving credit facility bear interest, at L-3 Communications option, at either (i) a base rate equal to the higher of (a) 0.50% per annum above the latest federal funds rate, (b) the Bank of America prime rate (as defined in the credit agreement), and (c) 1.00% per annum above a LIBOR rate (as defined in the credit agreement), plus a spread ranging from 1.25% to 3.00% per annum, or (ii) a LIBOR rate (as defined in the credit agreement) plus a spread ranging from 2.25% to 4.00% per annum. The spread, in both cases, depends on L-3 Communications debt rating at the time of determination. L-3 Communications pays: (1) commitment fees calculated on the daily amounts of the available unused commitments at a rate ranging from 0.375% to 0.75% per annum, (2) letter of credit fees ranging from 1.50% to 2.67% per annum for performance and commercial letters of credit and (3) letter of credit fees ranging from 2.25% to 4.00% for financial letters of credit. The fee rate, in all cases, depends on L-3 Communications debt rating at the time of determination. The debt rating is based on the ratings as determined by Standard & Poor s Rating Services, Moody s Investors Service, Inc. and Fitch Ratings of L-3 Communications non-credit enhanced senior, unsecured long-term debt. For additional information on the terms of L-3 Communications new $1 billion three-year revolving credit facility, including the financial and other restrictive covenants, see the Company s Current Report on Form 8-K dated October 23, 2009, and the credit agreement governing the terms of the new $1 billion three-year revolving credit facility, which is incorporated by reference as an exhibit to this report.

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10. Comprehensive Income

A reconciliation of net income to comprehensive income attributable to L-3 is presented in the table below.

	Third Quarter Ended		Year-to-Date Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
	(in millions)			
Net income	$ 253	$ 212	$ 681	$ 682
Other comprehensive income (loss):				
Foreign currency translation adjustments	66	(57)	116	(54)
Unrealized gains on hedging instruments[(1)]	4	3	3	4
Amortization of pension and postretirement benefit plans net loss (gain) and prior service cost[(2)]	8	(1)	23	2
Total comprehensive income	331	157	823	634
Less: Comprehensive income attributable to noncontrolling interests	3	2	7	8
Comprehensive income attributable to L-3	$ 328	$ 155	$ 816	$ 626

(1) Amounts are net of income taxes of $2 million and $1 million for the quarterly periods ended September 25, 2009 and September 26, 2008, respectively, and $1 million and $2 million for the year-to-date periods ended September 25, 2009 and September 26, 2008, respectively.

(2) Amounts are net of income taxes of $5 million for the quarterly period ended September 25, 2009, and $16 million and $1 million for the year-to-date periods ended September 25, 2009 and September 26, 2008, respectively. See Note 17.

11. Income Taxes

The U.S. Federal income tax jurisdiction is the Company s major tax jurisdiction. The statute of limitations for the 2004 and 2005 tax years of the Company and certain of its acquired subsidiaries expired during the third quarter of 2009. The statute of limitations for the Company s U.S. Federal income tax returns for the years ended December 31, 2006 through 2008 remain open. The Internal Revenue Service (IRS) began its audit of the Company s 2006 and 2007 U.S. Federal income tax returns in April 2009. In addition, the Company has numerous state and foreign income tax audits currently in process. As of September 25, 2009, the Company anticipates that unrecognized tax benefits will decrease by approximately $15 million over the next 12 months.

Current and non-current income taxes payable include potential interest of $18 million ($11 million after income taxes) at September 25, 2009 and December 31, 2008, and potential penalties of $8 million at September 25, 2009 and $7 million at December 31, 2008.

During the third quarter of 2009, the Company recorded a tax benefit of $26 million for a net reversal of amounts previously accrued, related to the 2004 and 2005 tax years, for which the statute of limitations has expired.

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12. L-3 Holdings Earnings Per Common Share

A reconciliation of basic EPS and diluted EPS is presented in the table below.

	Third Quarter Ended		Year-to-Date Ended	
	September 25, 2009	September 26, 2008	September 25, 2009	September 26, 2008
	(in millions, except per share data)			
Basic:				
Net income allocable to L-3 Holdings common shareholders	$ 248	$ 207	$ 668	$ 668
Weighted average common shares outstanding	116.4	121.0	117.1	121.8
Basic EPS	$ 2.13	$ 1.71	$ 5.70	$ 5.48
Diluted:				
Net income allocable to L-3 Holdings common shareholders	$ 248	$ 207	$ 668	$ 668
Common and potential common shares:				
Weighted average common shares outstanding	116.4	121.0	117.1	121.8
Assumed exercise of stock options	3.5	4.0	3.5	4.3
Unvested restricted stock awards	0.6		0.3	
Employee stock purchase plan contributions		0.4	0.3	0.4
Performance unit awards				
Assumed purchase of common shares for treasury	(3.5)	(3.4)	(3.6)	(3.5)
Assumed conversion of the CODES	[1]	[1]	[1]	0.2
Common and potential common shares	117.0	122.0	117.6	123.2
Diluted EPS	$ 2.12	$ 1.70	$ 5.68	$ 5.42

[1] L-3 Holdings CODES had no impact on diluted EPS for the quarter and year-to-date period ended September 25, 2009 and the quarter ended September 26, 2008, because the average market price of L-3 Holdings common stock during these periods was less than the price at which the CODES would have been convertible into L-3 Holdings

common stock. As of September 25, 2009, the conversion price was $100.14.

Excluded from the computations of diluted EPS are shares related to stock options, restricted stock, and restricted stock units underlying employee stock-based compensation of 3.5 million and 3.0 million for the quarter and year-to-date period ended September 25, 2009, respectively, and 2.4 million and 1.9 million for the quarter and year-to-date period ended September 26, 2008, respectively, because they were anti-dilutive.

EPS for the year-to-date period ended September 26, 2008 includes: (1) a gain of $0.65 per diluted share for the reversal of a current liability for pending and threatened litigation as a result of a June 27, 2008 decision by the U.S. Court of Appeals vacating an adverse 2006 jury verdict, (2) a gain of $0.06 per diluted share for the sale of the PMD product line (see Note 4), and (3) a non-cash charge of $0.14 per diluted share related to a write-down of capitalized software development costs.

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13. Equity

Repurchases of L-3 Holdings common stock under the $1 billion share repurchase program, approved by the Board of Directors in November 2008, are made from time to time at management s discretion in accordance with applicable U.S. federal securities laws in the open market or otherwise. All share repurchases of L-3 Holdings common stock have been recorded as treasury shares. At September 25, 2009, the remaining dollar value under the share repurchase program was $535 million.

From September 26, 2009 through November 4, 2009, L-3 repurchased 324,207 shares of L-3 Holdings common stock at an average price of $74.10 per share for an aggregate amount of $24 million.

On October 6, 2009, L-3 Holdings Board of Directors declared a quarterly cash dividend of $0.35 per share, payable on December 15, 2009 to shareholders of record at the close of business on November 17, 2009.

14. Fair Value Measurements

The following table presents the fair value hierarchy level for each of the Company s assets and liabilities that are measured and recorded at fair value on a recurring basis.

	September 25, 2009			December 31, 2008		
Description	**Level 1[(a)]**	**Level 2[(b)]**	**Level 3[(c)]**	**Level 1[(a)]**	**Level 2[(b)]**	**Level 3[(c)]**
	(in millions)					
Assets						
Cash equivalents	$ 958	$	$	$ 794	$	$
Derivative instruments		18			22	$
Total Assets	$ 958	$ 18	$	$ 794	$ 22	$
Liabilities						
Derivative instruments	$	$ 9	$	$	$ 21	$

(a) Level 1 is based on quoted market prices available in active markets for identical assets or liabilities as of the reporting date.

(b) Level 2 is based on pricing inputs other than quoted prices in active markets, which are either directly or indirectly observable. The fair value is determined using a valuation model based on observable market inputs, including quoted foreign currency forward exchange rates and consideration of non-performance risk.

(c) Level 3 is based on pricing inputs that are not observable and not corroborated by market data. The Company has no Level 3 assets or liabilities.

15. Financial Instruments

Fair Value of Financial Instruments. At September 25, 2009 and December 31, 2008, the Company s financial instruments consisted primarily of cash and cash equivalents, billed receivables, trade accounts payable, borrowings under the term loan facility, senior subordinated notes, CODES and foreign currency forward contracts. The carrying amounts of cash and cash equivalents, billed receivables and trade accounts payable are representative of their respective fair values because of the short-term maturities or expected settlement dates of these instruments. The fair value of borrowings under the term loan facility are based on similar debt issued. The senior subordinated notes are registered, unlisted public debt traded in the over-the-counter market and their fair values are based on quoted trading activity. The fair values of the CODES are based on quoted prices for the same or similar issues. The fair values of foreign currency

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forward contracts were estimated based on forward exchange rates at September 25, 2009 and December 31, 2008. The carrying amounts and estimated fair values of the Company s financial instruments are presented in the table below.

	September 25, 2009		December 31, 2008	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in millions)			
Borrowings under the Term Loan Facility	$ 650	$ 643	$ 650	$ 608
Senior Subordinated Notes	3,189	3,172	3,188	2,916
CODES	671	717	655	697
Foreign currency forward contracts[(1)]	9	9	1	1

(1) Notional amounts of foreign currency forward contracts were $359 million at September 25, 2009 and $414 million at December 31, 2008.

Derivative Financial Instruments. The Company s derivative financial instruments include foreign currency forward contracts, which are entered into for risk management purposes, and an embedded derivative representing the contingent interest payment provision related to the CODES.

Foreign Currency Forward Contracts. The Company s U.S. and foreign businesses enter into contracts with customers, subcontractors or vendors that are denominated in currencies other than their functional currencies. To protect the functional currency equivalent cash flows associated with certain of these contracts, the Company enters into foreign currency forward contracts. The Company s activities involving foreign currency forward contracts are designed to hedge the changes in the functional currency equivalent cash flows due to movements in foreign exchange rates compared to the functional currency. The foreign currencies hedged are primarily the Canadian dollar, Euro, British pound and U.S. dollar. The Company manages exposure to counterparty credit risk by entering into foreign currency forward contracts only with major financial institutions that are expected to fully perform under the terms of such contracts.

Foreign currency forward contracts are recorded in the Company s Consolidated Balance Sheets at fair value and are generally designated and accounted for as cash flow hedges in accordance with U.S. GAAP for derivative instruments and hedging activities (contained in FASB ASC Topic 815, *Derivatives and Hedging*). Gains and losses on designated foreign currency forward contracts that are considered highly effective in offsetting the corresponding change in the cash flows of the hedged transaction are recorded net of income taxes in accumulated other comprehensive income (loss) (accumulated OCI) and then recognized in income when the underlying hedged transaction affects income. The estimated net amount of existing gains at September 25, 2009 that are expected to be reclassified into income within the next 12 months is $5 million. Gains and losses on foreign currency forward contracts that do not meet hedge accounting criteria are recognized in income immediately.

The table below presents the notional amounts of the Company s outstanding foreign currency forward contracts by currency as of September 25, 2009:

Currency	**Notional Amount (in millions)**
U.S. dollar	$ 130
Canadian dollar	105
British pound	99
Euro	14
Other	11
Total	$ 359

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The notional amounts are used to measure the volume of these contracts and do not represent exposure to foreign currency losses. At September 25, 2009, the Company s foreign currency forward contracts had maturities through 2016.

The table below presents the fair values and the location of the Company s derivative instruments in the Unaudited Condensed Consolidated Balance Sheet as of September 25, 2009.

	Fair Values of Derivative Instruments[1]			
	Other Current Assets	Other Assets	Other Current Liabilities	Other Liabilities
	(in millions)			
Derivatives designated as hedging instruments:				
Foreign currency forward contracts	$ 6	$ 9	$ 3	$ 2
Derivatives not designated as hedging instruments:				
Foreign currency forward contracts	2	1	3	1
Embedded derivative related to the CODES				
Total derivative instruments	$ 8	$ 10	$ 6	$ 3

(1) See Note 14 for a description of the fair value hierarchy related to the Company s foreign currency forward contracts.

The tables below present the effects of the Company s derivative instruments on the Unaudited Condensed Consolidated Statement of Operations.

	Amount of Gain or (Loss) Recognized in OCI on Derivative	Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)

Derivatives Designated as Hedging Instruments	(Effective Portion)		Location	Amount ($ in millions)		Location	Amount
For the quarter ended September 25, 2009:							
Foreign currency forward contracts	$	5	Cost of Sales	$		Cost of Sales	$
For the year-to-date ended September 25, 2009:							
Foreign currency forward contracts	$		Cost of Sales	$	(3)	Cost of Sales	$

Derivatives not Designated as Hedging Instruments	Gain or (Loss) Recognized in Income on Derivative Location	Amount (in millions)	
For the quarter ended September 25, 2009:			
Foreign currency forward contracts	Cost of Sales	$	2
For the year-to-date ended September 25, 2009:			
Foreign currency forward contracts	Cost of Sales	$	2

16. Commitments and Contingencies

U.S. and Foreign Government Procurement Regulations

A substantial majority of the Company s revenues are generated from providing products and services under legally binding agreements, or contracts, with U.S. Government and foreign government customers. U.S. Government contracts are subject to extensive legal and regulatory requirements, and, from time to time, agencies of the U.S. Government investigate whether such contracts were and are being conducted in accordance with these

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requirements. The Company is currently cooperating with the U.S. Government on several investigations from which civil, criminal or administrative proceedings could result and give rise to fines, penalties, compensatory and treble damages, restitution and/or forfeitures. The Company does not currently anticipate that any of these investigations will have a material adverse effect, individually or in the aggregate, on its consolidated financial position, results of operations or cash flows. However, under U.S. Government regulations, an indictment of the Company by a federal grand jury could result in the Company being suspended for a period of time from eligibility for awards of new government contracts or in a loss of export privileges. A conviction could result in debarment from contracting with the federal government for a specified term. In addition, all of the Company s U.S. Government contracts: (1) are subject to audit and various pricing and cost controls, (2) include standard provisions for termination for the convenience of the U.S. Government or for default, and (3) are subject to cancellation if funds for contracts become unavailable. Foreign government contracts generally include comparable provisions relating to terminations for convenience and default, as well as other procurement clauses relevant to the foreign government.

Litigation Matters

The Company has been subject to and is involved in litigation, government investigations, proceedings, claims or assessments and various contingent liabilities incidental to its businesses, including those specified below. Furthermore, in connection with certain business acquisitions, the Company has assumed some or all claims against, and liabilities of, the acquired business, including both asserted and unasserted claims and liabilities. In accordance with U.S. GAAP for contingencies (contained in FASB ASC Topic 450, *Contingencies*), the Company records a liability when management believes that it is both probable that a liability has been incurred and the Company can reasonably estimate the amount of the loss. Generally, the loss is recorded at the amount the Company expects to resolve the liability. The estimated amounts of liabilities recorded for pending and threatened litigation is disclosed in Note 8. Amounts recoverable from insurance contracts or third parties are recorded as assets when deemed probable. At September 25, 2009, the Company did not record any amounts for recoveries from insurance contracts or third parties in connection with the amount of liabilities recorded for pending and threatened litigation. Legal defense costs are expensed as incurred. The Company believes it has recorded adequate provisions for its litigation matters. The Company reviews these provisions quarterly and adjusts these provisions to reflect the impact of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular matter. While it is reasonably possible that an unfavorable outcome may occur in one or more of the following matters, unless otherwise stated below, the Company believes that it is not probable that a loss has been incurred in any of these matters. An estimate of loss or range of loss is disclosed for a particular litigation matter when such amount or amounts can be reasonably estimated and no loss has been accrued. The Company believes that any damage amounts claimed in the specific matters discussed below are not meaningful indicators of potential liability. Although the Company believes that it has valid defenses with respect to legal matters and investigations pending against it, litigation is inherently unpredictable. Therefore, it is possible that the financial position, results of operations or cash flows of the Company could be materially adversely affected in any particular period by the unfavorable resolution of one or more of these contingencies.

Kalitta Air. L-3 Integrated Systems and its predecessors have been involved in litigation with Kalitta Air arising from a contract to convert Boeing 747 aircraft from passenger configuration to cargo freighters. The lawsuit was brought in the United States District Court for the Northern District of California (the trial court) on January 31, 1997. The aircraft were modified using Supplemental Type Certificates (STCs) issued in 1988 by the Federal Aviation Administration (FAA) to Hayes International, Inc. (Hayes/Pemco) as a subcontractor to GATX/Airlog Company (GATX). Between 1988 and 1990, Hayes/Pemco modified five aircraft as a subcontractor to GATX using the STCs. Between 1990 and 1994, Chrysler Technologies Airborne Systems, Inc. (CTAS), a predecessor to L-3 Integrated Systems, performed as a subcontractor to GATX and modified an additional five aircraft using the STCs. Two of the aircraft modified by CTAS were owned by American International Airways, the predecessor to Kalitta

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