L 3 COMMUNICATIONS HOLDINGS INC
Form 10-Q
August 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 June 26, 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 Smaller reporting company o
(Do not check if a smaller reporting company)

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 116,576,254 shares of L-3 Communications Holdings, Inc. common stock with a par value of $0.01 outstanding as of the close of business on July 31, 2009.

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

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For the quarterly period ended June 26, 2009

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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)

	June 26, 2009	December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 897	$ 867
Billed receivables, net of allowances, of $35 in 2009 and $26 in 2008	1,332	1,226
Contracts in process	2,402	2,267
Inventories	267	259
Deferred income taxes	211	211
Other current assets	124	131
Total current assets	5,233	4,961
Property, plant and equipment, net	830	821
Goodwill	8,127	8,029
Identifiable intangible assets	399	417
Deferred debt issue costs	38	44
Other assets	209	212
Total assets	$ 14,836	$ 14,484
LIABILITIES AND EQUITY		
Current liabilities:		
Current portion of long-term debt	$ 650	$
Accounts payable, trade	652	602
Accrued employment costs	654	700
Accrued expenses	518	479
Advance payments and billings in excess of costs incurred	482	530
Income taxes	56	45
Other current liabilities	347	351
Total current liabilities	3,359	2,707
Pension and postretirement benefits	833	802
Deferred income taxes	155	127

Other liabilities	432	414
Long-term debt	3,854	4,493
Total liabilities	8,633	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, 116,031,097 shares outstanding at June 26, 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)	4,286	4,136
L-3 Communications Holdings, Inc. s treasury stock at cost, 18,352,663 shares at June 26, 2009 and 13,995,450 shares at December 31, 2008	(1,620)	(1,319)
Retained earnings	3,713	3,373
Accumulated other comprehensive loss	(268)	(332)
Total L-3 shareholders equity	6,111	5,858
Noncontrolling interests	92	83
Total equity	6,203	5,941
Total liabilities and equity	$ 14,836	$ 14,484

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)

	Second Quarter Ended	
	June 26, 2009	June 27, 2008
Net sales:		
Products	$ 1,884	$ 1,765
Services	2,045	1,957
Total net sales	3,929	3,722
Cost of sales:		
Products	1,690	1,598
Services	1,822	1,749
Total cost of sales	3,512	3,347
Litigation Gain		126
Operating income	417	501
Interest and other income, net	6	7
Interest expense	69	66
Income before income taxes	354	442
Provision for income taxes	127	164
Net income	$ 227	$ 278
Less: Net income attributable to noncontrolling interests	2	3
Net income attributable to L-3	$ 225	$ 275
Less: Net income allocable to participating securities	2	2
Net income allocable to L-3 Communications Holdings, Inc. s common shareholders	$ 223	$ 273
L-3 Communications Holdings, Inc. s earnings per common share:		
Basic	$ 1.91	$ 2.24
Diluted	$ 1.90	$ 2.21
L-3 Communications Holdings, Inc. s weighted average common shares outstanding:		
Basic	116.5	122.0

Diluted	117.2	123.5

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)

	First Half Ended June 26, 2009	First Half Ended June 27, 2008
Net sales:		
Products	$ 3,646	$ 3,368
Services	3,919	3,860
Total net sales	7,565	7,228
Cost of sales:		
Products	3,256	3,027
Services	3,516	3,458
Total cost of sales	6,772	6,485
Litigation Gain		126
Operating income	793	869
Interest and other income, net	9	15
Interest expense	135	142
Income before income taxes	667	742
Provision for income taxes	239	272
Net income	$ 428	$ 470
Less: Net income attributable to noncontrolling interests	4	6
Net income attributable to L-3	$ 424	$ 464
Less: Net income allocable to participating securities	4	3
Net income allocable to L-3 Communications Holdings, Inc. s common shareholders	$ 420	$ 461
L-3 Communications Holdings, Inc. s earnings per common share:		
Basic	$ 3.58	$ 3.77
Diluted	$ 3.56	$ 3.72
L-3 Communications Holdings, Inc. s weighted average common shares outstanding:		
Basic	117.4	122.3
Diluted	118.0	123.8

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 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 first half ended June 26, 2009:								
Balance at December 31, 2008	118.6	$ 1	$ 4,135	$ (1,319)	$ 3,373	$ (332)	$ 83	$ 5,941
Comprehensive income:								
Net income					424		4	428
Pension and postretirement benefit plans:								
Amortization of net loss and prior service cost, net of income taxes of $10						15		15
Unrealized loss on hedging instruments, net of income taxes of $1						(1)		(1)
Foreign currency translation adjustment						50		50
Total comprehensive income								492
Distributions to noncontrolling interests							(3)	(3)
Cash dividends paid on common stock ($0.35 per share)					(84)			(84)
Recognition of non-controlling interest in consolidated subsidiary							8	8
Shares issued:								
Employee savings plans	1.1		80					80
Exercise of stock options	0.1		4					4
Employee stock purchase plan	0.6		34					34

Stock-based compensation expense			35					35
Treasury stock purchased	(4.4)			(301)				(301)
Other			(3)					(3)
Balance at June 26, 2009	116.0	$ 1	$ 4,285	$ (1,620)	$ 3,713	$ (268)	$ 92	$ 6,203
For the first half ended June 27, 2008:								
Balance at December 31, 2007	124.2	$ 1	$ 3,816	$ (525)	$ 2,582	$ 153	$ 87	$ 6,114
Comprehensive income:								
Net income					464		6	470
Pension and postretirement benefit plans:								
Amortization of net loss and prior service cost, net of income taxes of $2						2		2
Unrealized gain on hedging instruments, net of income taxes of $1						1		1
Foreign currency translation adjustment						4		4
Total comprehensive income								477
Distributions to noncontrolling interests							(5)	(5)
Cash dividends paid on common stock ($0.30 per share)					(74)			(74)
Shares issued:								
Employee savings plans	0.7		72					72
Exercise of stock options	0.4		32					32
Employee stock purchase plan	0.4		35					35
Stock-based compensation expense			30					30
Treasury stock purchased	(4.8)			(500)				(500)
Other	(0.1)		(2)					(2)
Balance at June 27, 2008	120.8	$ 1	$ 3,983	$ (1,025)	$ 2,972	$ 160	$ 88	$ 6,179

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)

	First Half Ended June 26, 2009	First Half Ended June 27, 2008
Operating activities:		
Net income	$ 428	$ 470
Depreciation of property, plant and equipment	77	76
Amortization of intangibles and other assets	30	27
Deferred income tax provision	29	107
Stock-based employee compensation expense	35	30
Contributions to employee savings plans in L-3 Communications Holdings, Inc. s common stock	74	72
Amortization of pension and postretirement benefit plans net loss and prior service cost	26	4
Amortization of bond discounts (included in interest expense)	11	10
Amortization of deferred debt issue costs (included in interest expense)	6	5
Impairment charge		28
Gain on sale of a product line		(12)
Other non-cash items	(3)	(5)
Subtotal	713	812
Changes in operating assets and liabilities, excluding acquired amounts:		
Billed receivables	(83)	(29)
Contracts in process	(116)	(72)
Inventories	(9)	(27)
Other current assets	11	(33)
Accounts payable, trade	70	81
Accrued employment costs	(46)	(5)
Accrued expenses	(1)	51
Advance payments and billings in excess of costs incurred	(43)	10
Income taxes	21	(24)
Excess income tax benefits related to share-based payment arrangements	(1)	(7)
Other current liabilities	(8)	(137)
Pension and postretirement benefits	31	21
All other operating activities	(11)	(13)
Subtotal	(185)	(184)
Net cash from operating activities	528	628
Investing activities:		
Business acquisitions, net of cash acquired	(82)	(218)

Proceeds from sale of product lines		12
Capital expenditures	(86)	(76)
Dispositions of property, plant and equipment	6	5
Other investing activities		2
Net cash used in investing activities	(162)	(275)
Financing activities:		
Common stock repurchased	(301)	(500)
Dividends paid on L-3 Communications Holdings, Inc. s common stock	(84)	(74)
Proceeds from exercise of stock options	3	24
Proceeds from employee stock purchase plan	34	35
Excess income tax benefits related to share-based payment arrangements	1	7
Other financing activities	1	(8)
Net cash used in financing activities	(346)	(516)
Effect of foreign currency exchange rate changes on cash and cash equivalents	10	5
Net increase (decrease) in cash and cash equivalents	30	(158)
Cash and cash equivalents, beginning of the period	867	780
Cash and cash equivalents, end of the period	$ 897	$ 622

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 international commercial customers and select other U.S. federal, state and local government agencies.

The Company has the following four reportable segments, comprised of: (1) C^3ISR, (2) Government Services, (3) Aircraft Modernization and Maintenance (AM&M), and (4) Specialized Products. Financial information relating to the Company s reportable segments is included in Note 20. C^3ISR provides products and services for the global ISR market, 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, 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 training and operational support services, enterprise information technology solutions, intelligence solutions and support, command & control systems and software services and global security & engineering solutions services. AM&M provides modernization, upgrades and sustainment, maintenance and logistics support services for military and various government aircraft and other platforms. 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, avionics & displays, simulation & training, precision engagement, security & detection, propulsion systems, telemetry & advanced technology, undersea warfare and marine services.

2. Basis of Presentation

These unaudited condensed consolidated financial statements for the quarterly period and first half period ended June 26, 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 first half ended June 26, 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 unconditionally guaranteed by L-3 Communications and certain of its wholly-owned domestic subsidiaries.

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

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.

3. New Accounting Standards Implemented

The Company adopted eight new accounting standards during the first half ended June 26, 2009. The following six standards were effective January 1, 2009:

- Financial Accounting Standards Board (FASB) Staff Position (FSP) Accounting Pronouncement Bulletin (APB) 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* (FSP APB 14-1);

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS (Continued)

FSP Emerging Issues Task Force (EITF) 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities* (FSP EITF 03-6-1);

FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements* (SFAS 160);

FASB Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities* (SFAS 161);

FASB Statement No. 141(R), *Business Combinations*, as amended by FSP Financial Accounting Standard (FAS) 141(R)-1, *Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies* (SFAS 141(R)); and

FSP FAS 157-2, *Effective Date of FASB Statement No. 157* (FSP FAS 157-2).

For the impact of the adoption of FSP APB 14-1, FSP EITF 03-6-1 and SFAS 160 on the Company s: (1) the Condensed Consolidated Balance Sheet, at December 31, 2008, (2) the Consolidated Equity Account Balances, at December 31, 2007, and (3) the Condensed Consolidated Statements of Operations for the quarter and first half ended June 27, 2008, see pages 10-12. The adoption of SFAS 161, SFAS 141(R) and FSP FAS 157-2 did not have a material impact on the Company s prior period financial statements.

FSP APB 14-1: In accordance with FSP APB 14-1, 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. FSP APB 14-1 does not apply to the Company s other outstanding debt instruments because they are not convertible debt instruments within the scope of FSP APB 14-1. The Company has retrospectively applied the provisions of this standard and adjusted the prior period financial statements accordingly.

The following table presents the impact of FSP APB 14-1 on the Statements of Operations for the quarter and first half ended June 26, 2009.

	Second Quarter Ended June 26, 2009	First Half Ended June 26, 2009
	(in millions, except per share data)	
Interest expense	$ 5	$ 10
Provision for income taxes	(2)	(4)
Net income attributable to L-3	(3)	(6)
L-3 Holdings earnings per common share:		
Basic	$ (0.03)	$ (0.05)
Diluted	$ (0.03)	$ (0.05)

FSP EITF 03-6-1: In accordance with FSP EITF 03-6-1, the Company is including the impact of restricted stock and restricted stock units that are entitled to receive non-forfeitable dividends (Participating Securities) 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 FSP EITF 03-6-1 decreased basic EPS by $0.02 and diluted EPS by $0.01 for the quarter ended June 26, 2009 and decreased basic EPS by $0.03 and diluted EPS by $0.02 for the first half ended June 26, 2009.

SFAS 160: The Company retrospectively applied the presentation requirements of SFAS 160 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.

SFAS 161: The enhanced disclosures for derivative instruments and related hedging activities required in accordance with SFAS 161 can be found in Note 15.

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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED
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SFAS 141(R): The Company adopted the provisions of SFAS 141(R) 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 first half ended June 26, 2009. In accordance with SFAS 141(R) 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 FAS 5 *Accounting for Contingencies,* as appropriate, and (4) capitalizing in-process research and development. In addition, pursuant to SFAS 141(R), 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. The Company has not resolved any uncertain tax positions related to acquisitions completed prior to January 1, 2009. The adoption of SFAS 141(R) did not have a material impact on the Company s financial position, results of operations and cash flows for the quarter and first half ended June 26, 2009.

FSP FAS 157-2: The Company adopted the provisions of SFAS No. 157, *Fair Value Measurements,* for non-financial assets and non-financial liabilities not recognized or disclosed at fair value in the financial statements on a recurring basis. FSP FAS 157-2 previously delayed the effective date of applying the provisions of SFAS 157 to all non-financial assets and non-financial liabilities not recognized or disclosed at fair value on a recurring basis until January 1, 2009. The adoption 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 June 26, 2009.

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

SFAS 165, *Subsequent Events* (SFAS 165); and

FSP FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments* (FSP FAS 107-1).

SFAS 165: The adoption of SFAS 165 requires the Company to evaluate events after the balance sheet date and disclose the date through which the evaluation is performed. The Company evaluated subsequent events through August 4, 2009, the date the Company filed this quarterly report on Form 10-Q, and did not identify any subsequent events that should be disclosed pursuant to SFAS 165.

FSP FAS 107-1: The adoption of FSP FAS 107-1 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 FSP FAS 107-1.

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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 first half ended June 27, 2008, in each case to reflect the adjustments made to adopt SFAS 160, FSP APB 14-1, and FSP EITF 03-6-1, as applicable.

	As Previously Reported	Adjustments for: SFAS 160	FSP APB 14-1	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

	As Previously Reported	Adjustments for: SFAS 160	FSP APB 14-1	As Currently Reported
		(in millions)		
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: SFAS 160	FSP EITF 03-6-1	FSP APB 14-1	As Currently Reported
	(in millions, except per share data)				
Condensed Consolidated Statement of Operations, for the quarter ended June 27, 2008:					
Net sales	$ 3,722	$	$	$	$ 3,722
Cost of sales	3,347				3,347
Litigation Gain	126				126
Operating income	501				501
Interest and other income, net	7				7
Interest expense	61			5	66
Minority interests in net income of consolidated subsidiaries	3	(3)			
Income before income taxes	444	3		(5)	442
Provision for income taxes	166			(2)	164
Net income	$ 278	$ 3	$	$ (3)	$ 278
Less: Net income attributable to noncontrolling interests		3			3
Net income attributable to L-3	$ 278	$	$	$ (3)	$ 275
Less: Net income allocable to participating securities			2		2
Net income allocable to L-3 Communications Holdings, Inc. s common shareholders	$ 278	$	$ (2)	$ (3)	$ 273
L-3 Communications Holdings, Inc. s earnings per common share:					
Basic	$ 2.28	$	$ (0.02)	$ (0.02)	$ 2.24
Diluted	$ 2.24	$	$ (0.01)	$ (0.02)	$ 2.21

L-3 Communications Holdings, Inc. s weighted average common shares outstanding:			
Basic	122.0		122.0
Diluted	124.0	(0.5)	123.5

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	As Previously Reported	Adjustments for: SFAS 160	FSP EITF 03-6-1	FSP APB 14-1	As Currently Reported
	(in millions, except per share data)				
Condensed Consolidated Statement of Operations, for the first half ended June 27, 2008:					
Net sales	$ 7,228	$	$	$	$ 7,228
Cost of sales	6,485				6,485
Litigation Gain	126				126
Operating income	869				869
Interest and other income, net	15				15
Interest expense	132			10	142
Minority interests in net income of consolidated subsidiaries	6	(6)			
Income before income taxes	746	6		(10)	742
Provision for income taxes	276			(4)	272
Net income	$ 470	$ 6	$	$ (6)	$ 470
Less: Net income attributable to noncontrolling interests		6			6
Net income attributable to L-3	$ 470	$	$	$ (6)	$ 464
Less: Net income allocable to participating securities			3		3
Net income allocable to L-3 Communications Holdings, Inc. s common shareholders	$ 470	$	$ (3)	$ (6)	$ 461
L-3 Communications Holdings, Inc. s earnings per common share:					
Basic	$ 3.84	$	$ (0.03)	$ (0.04)	$ 3.77
Diluted	$ 3.78	$	$ (0.02)	$ (0.04)	$ 3.72

L-3 Communications Holdings, Inc. s weighted average common shares outstanding:			
Basic	122.3		122.3
Diluted	124.3	(0.5)	123.8

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

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was $58 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 by the 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 first half ended June 26, 2009, the Company completed the final purchase price allocation for G.A. International (GAI), except for the finalization of the contractual purchase price, which is subject to additional consideration not to exceed $1 million that is contingent upon GAI s post-acquisition financial performance through July 25, 2011. Additional consideration, if any, will be accounted for as goodwill. The final purchase price allocation for GAI compared to the preliminary purchase price allocation did not have a material impact on the Company s results of operations or financial position. The purchase price allocation for International Resources Group Ltd. (IRG) is expected to be completed during the third quarter of 2009, and will be based on the final purchase price, final appraisals and other analyses of fair values for acquired assets and assumed liabilities. The purchase price for IRG is subject to adjustment based on actual closing date net assets, which has not yet been finalized. Additional consideration, if any, will be accounted for as goodwill. The Company does not expect the difference, if any, between the preliminary and final purchase price allocation for IRG to have a material impact on its 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 first half ended June 26, 2009 and the year ended December 31, 2008, in each case assuming that the business acquisitions completed during these periods had occurred on January 1, 2008.

	Second Quarter Ended		First Half Ended	
	June 26, 2009	June 27, 2008	June 26, 2009	June 27, 2008
	(in millions, except per share data)			
Pro forma net sales	$ 3,929	$ 3,762	$ 7,571	$ 7,341
Pro forma net income attributable to L-3	$ 225	$ 275	$ 424	$ 464
Pro forma diluted EPS	$ 1.90	$ 2.21	$ 3.56	$ 3.72

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 SFAS No. 144, *Accounting for Impairment or Disposal of Long-Lived Assets.* 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 $1 million of operating income for the quarter ended June 27, 2008, $30 million of sales and $2 million of

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operating income for the first half ended June 27, 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 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 $4 million of sales for the quarter ended June 27, 2008, and $8 million of sales for both the first half ended June 27, 2008, and the year ended December 31, 2008.

5. Contracts in Process

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

	June 26, 2009	December 31, 2008
	(in millions)	
Unbilled contract receivables, gross	$ 2,250	$ 2,079
Less: unliquidated progress payments	(557)	(462)
Unbilled contract receivables, net	1,693	1,617
Inventoried contract costs, gross	855	754
Less: unliquidated progress payments	(146)	(104)
Inventoried contract costs, net	709	650
Total contracts in process	$ 2,402	$ 2,267

Inventoried Contract Costs. In accordance with the American Institute of Certified Public Accountants Statement of Position 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* (SOP 81-1) and the AICPA Audit and Accounting Guide, *Audits of Federal Government Contractors,* 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.

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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.

	Second Quarter Ended		First Half Ended	
	June 26, 2009	June 27, 2008	June 26, 2009	June 27, 2008
	(in millions)			
Amounts included in inventoried contract costs at beginning of the period	$ 79	$ 69	$ 74	$ 68
Add: Contract costs incurred[1]	334	318	646	600
Amounts included in acquired inventoried contract costs		7		7
Less: Amounts charged to cost of sales	(334)	(315)	(641)	(596)
Amounts included in inventoried contract costs at end of the period	$ 79	$ 79	$ 79	$ 79

(1) Incurred costs include IRAD and B&P costs of $79 million for the quarter ended June 26, 2009, $78 million for the quarter ended June 27, 2008, $156 million for the first half ended June 26, 2009 and $137 million for the first half ended June 27, 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.

	Second Quarter Ended		First Half Ended	
	June 26, 2009	June 27, 2008	June 26, 2009	June 27, 2008
	(in millions)			
Selling, general and administrative expenses	$ 57	$ 73	$ 118	$ 139
Research and development expenses	20	24	37	48
Total	$ 77	$ 97	$ 155	$ 187

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 realized value.

	June 26, 2009	December 31, 2008
	(in millions)	
Raw materials, components and sub-assemblies	$ 104	$ 95
Work in process	126	121
Finished goods	37	43
Total	$ 267	$ 259

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7. Goodwill and Identifiable Intangible Assets

Goodwill. In accordance with SFAS No. 141(R), adopted on January 1, 2009, 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	Specialized Products	Consolidated Total
			(in millions)		
Balance at December 31, 2008[1]	$ 862	$ 2,313	$ 1,121	$ 3,733	$ 8,029
Business acquisition		1		58	59
Foreign currency translation adjustments[2]	9	2	13	15	39
Balance at June 26, 2009	$ 871	$ 2,316	$ 1,134	$ 3,806	$ 8,127

(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.

(2) The increase in goodwill from foreign currency translation adjustments is due to the weakening of the U.S. dollar during the first half of 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.

	June 26, 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	$	511	$	144	$	367	$	505	$	124	$	381
Technology	8		78		52		26		76		47		29
Other, primarily favorable leasehold interests	7		14		8		6		14		7		7
Total	22	$	603	$	204	$	399	$	595	$	178	$	417

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

	Second Quarter Ended		**First Half Ended**	
	June 26, 2009	**June 27, 2008**	**June 26, 2009**	**June 27, 2008**
	(in millions)			
Amortization expense	$ 13	$ 11	$ 26	$ 22

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Based on gross carrying amounts at June 26, 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	$ 38	$ 30

At June 26, 2009 and December 31, 2008, the Company had $1 million of indefinite-lived identifiable intangible assets.

8. Other Current Liabilities and Other Liabilities

The table below presents the components of other current liabilities.

	June 26, 2009	December 31, 2008
	(in millions)	
Other Current Liabilities:		
Accruals for pending and threatened litigation (see Note 16)	$ 2	$ 4
Accrued product warranty costs	92	97
Accrued interest	62	66
Estimated costs in excess of estimated contract value to complete contracts in process in a loss position	68	58
Deferred revenues	28	25
Aggregate purchase price payable for acquired businesses	5	
Other	90	101
Total other current liabilities	$ 347	$ 351

The table below presents the components of other liabilities.

	June 26, 2009	December 31, 2008
	(in millions)	

Other Liabilities:		
Non-current income taxes payable (see Note 11)	$ 189	$ 177
Deferred compensation	87	79
Accrued workers compensation	49	45
Unfavorable lease obligations	7	8
Non-current portion of net deferred gains from terminated interest rate swap agreements	7	9
Notes payable and capital lease obligations	10	10
Accrued product warranty costs	6	5
Other non-current liabilities	77	81
Total other liabilities	$ 432	$ 414

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

	First Half Ended	
	June 26, 2009	June 27, 2008
	(in millions)	
Accrued product warranty costs[1]:		
Balance at January 1	$ 102	$ 98
Acquisitions during the period		2
Accruals for product warranties issued during the period	22	18
Foreign currency translation adjustments	1	1
Changes to accruals for product warranties existing before January 1		1
Settlements made during the period	(27)	(19)
Balance at end of period	$ 98	$ 101

(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.

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.

	June 26, 2009	December 31, 2008
	(in millions)	
L-3 Communications:		
Borrowings under Revolving Credit Facility[1]	$	$
Borrowings under Term Loan Facility maturing 2010[2]	650	650
75/8% Senior Subordinated Notes due 2012	750	750
61/8% Senior Subordinated Notes due 2013	400	400
61/8% Senior Subordinated Notes due 2014	400	400
57/8% Senior Subordinated Notes due 2015	650	650
63/8% 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	(46)	(57)
Carrying amount of long-term debt	4,504	4,493
Less: Current portion of long-term debt	(650)	
Carrying amount of long-term debt, excluding current portion	$ 3,854	$ 4,493

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(1) The Company s five-year revolving credit facility, which matures on March 9, 2010, allows for total aggregate borrowings of up to $1 billion. At June 26, 2009, available borrowings under the revolving credit facility were $964 million after reductions for outstanding letters of credit of $36 million.

(2) The interest rate at June 26, 2009 and December 31, 2008 was 1.19% and 2.70%, respectively, and is based on the LIBOR rate (as defined) 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. The term loan facility matures on March 9, 2010 and is classified as a current liability.

(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 ($100.14 as of July 29, 2009) 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 June 26, 2009 conversion price of $101.13, the aggregate consideration to be delivered upon conversion would be determined based on 6.9 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 July 31, 2009 was $75.50 per share. The effective interest rate on the CODES is 6.33%. Interest expense relates to both the contractual interest coupon and amortization of the discount on the liability component. Interest expense recognized was $10 million for the second quarter periods ended June 26, 2009 and June 27, 2008 and $20 million for the first half periods ended June 26, 2009 and June 27, 2008. The following table provides additional information about the Company s CODES:

	June 26, 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	$ 35	$ 45
Net carrying amount of liability component	$ 665	$ 655

10. Comprehensive Income

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

	Second Quarter Ended		First Half Ended	
	June 26, 2009	June 27, 2008	June 26, 2009	June 27, 2008

	(in millions)			
Net income	$ 227	$ 278	$ 428	$ 470
Other comprehensive income (loss):				
Foreign currency translation adjustments	62	4	50	4
Unrealized (losses) gains on hedging instruments[1]	(1)		(1)	1
Amortization of pension and postretirement benefit plans net loss and prior service cost[2]	8	1	15	2
Total comprehensive income	296	283	492	477
Less: Comprehensive income attributable to noncontrolling interests	2	3	4	6
Comprehensive income attributable to L-3	$ 294	$ 280	$ 488	$ 471

(1) Amounts are net of income taxes of $1 million for the quarterly period ended June 26, 2009 and $1 million for the first half periods ended June 26, 2009 and June 27, 2008.

(2) Amounts are net of income taxes of $5 million and $1 million for the quarterly periods ended June 26, 2009 and June 27, 2008, respectively, and $10 million and $2 million for the first half periods ended June 26, 2009 and June 27, 2008, respectively. See Note 17.

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11. Income Taxes

The U.S. Federal income tax jurisdiction is the Company s major tax jurisdiction. The statute of limitations for the Company s U.S. Federal income tax returns for the years ended December 31, 2004 through 2007 is open as of June 26, 2009. The Company expects the statute of limitations on the 2004 and 2005 years to close in the third quarter of 2009. 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 June 26, 2009, the Company anticipates that unrecognized tax benefits will decrease by approximately $39 million over the next 12 months.

Current and non-current income taxes payable include potential interest of $21 million ($13 million after income taxes) at June 26, 2009 and $18 million ($11 million after income taxes) at December 31, 2008, and potential penalties of $8 million at June 26, 2009 and $7 million at December 31, 2008.

12. L-3 Holdings Earnings Per Common Share

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

	Second Quarter Ended		First Half Ended	
	June 26, 2009	June 27, 2008	June 26, 2009	June 27, 2008
	(in millions, except per share data)			
Basic:				
Net income allocable to L-3 Holdings common shareholders	$ 223	$ 273	$ 420	$ 461
Weighted average common shares outstanding	116.5	122.0	117.4	122.3
Basic EPS	$ 1.91	$ 2.24	$ 3.58	$ 3.77
Diluted:				
Net income allocable to L-3 Holdings common shareholders	$ 223	$ 273	$ 420	$ 461
Common and potential common shares:				
Weighted average common shares outstanding	116.5	122.0	117.4	122.3
Assumed exercise of stock options	3.5	4.3	3.5	4.4
Unvested restricted stock awards	0.1		0.1	
Employee stock purchase plan contributions	0.6	0.4	0.6	0.4

Performance unit awards	0.1			
Assumed purchase of common shares for treasury	(3.6)	(3.5)	(3.6)	(3.6)
Assumed conversion of the CODES	[1]	0.3	[1]	0.3
Common and potential common shares	117.2	123.5	118.0	123.8
Diluted EPS	$ 1.90	$ 2.21	$ 3.56	$ 3.72

(1) L-3 Holdings CODES had no impact on diluted EPS for the quarter and first half ended June 26, 2009, 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 July 29, 2009, the current conversion price was $100.14.

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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 2.8 million for the quarter and first half ended June 26, 2009, and 1.6 million for the quarter and first half ended June 27, 2008, because they were anti-dilutive.

EPS for the quarter and first half ended June 27, 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.

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. All share repurchases of L-3 Holdings common stock have been recorded as treasury shares. At June 26, 2009, the remaining dollar value of the authorized share repurchase program was $630 million.

From June 27, 2009 through August 4, 2009, L-3 repurchased 246,755 shares of L-3 Holdings common stock at an average price of $70.84 per share for an aggregate amount of $17 million.

On July 14, 2009, L-3 Holdings Board of Directors declared a quarterly cash dividend of $0.35 per share, payable on September 15, 2009 to shareholders of record at the close of business on August 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.

	June 26, 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	$ 676	$	$	$ 794	$	$
Derivative instruments		12			22	
Total Assets	$ 676	$ 12	$	$ 794	$ 22	$
Liabilities						

Derivative instruments	$		$	13	$	$	$	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 June 26, 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

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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 forward contracts were estimated based on forward exchange rates at June 26, 2009 and December 31, 2008. The carrying amounts and estimated fair values of the Company s financial instruments are presented in the table below.

	June 26, 2009		December 31, 2008	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in millions)			
Borrowings under the Term Loan Facility	$ 650	$ 639	$ 650	$ 608
Senior Subordinated Notes	3,189	2,956	3,188	2,916
CODES	665	669	655	697
Foreign currency forward contracts[(1)]	(1)	(1)	1	1

(1) Notional amounts of foreign currency forward contracts were $343 million at June 26, 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 Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133). 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 loss (accumulated OCI) and then recognized in earnings when the underlying hedged transaction affects earnings. The estimated net amount of existing losses at June 26, 2009 that are expected to be reclassified into earnings within the next 12 months is $1 million. Gains and losses on foreign currency forward contracts that do not meet the SFAS 133 hedge accounting criteria are recognized in earnings immediately.

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The table below presents the notional amounts of the Company s outstanding foreign currency forward contracts by currency as of June 26, 2009:

Currency	Notional Amount (in millions)	
U.S. dollar	$	127
British pound		103
Euro		19
Canadian dollar		85
Other		9
Total	$	343

The notional amounts are used to measure the volume of these contracts and do not represent exposure to foreign currency losses. At June 26, 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 June 26, 2009.

	Fair Values of Derivative Instruments[1]			
	Other Current Assets	Other Assets	Other Current Liabilities	Other Liabilities
	(in millions)			
Derivatives designated as hedging instruments under SFAS 133:				
Foreign currency forward contracts	$ 3	$ 8	$ 6	$ 2
Derivatives not designated as hedging instruments under SFAS 133:				
Foreign currency forward contracts	1		4	1
Embedded derivative related to the CODES				
Total derivative instruments	$ 4	$ 8	$ 10	$ 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.

Derivatives in SFAS 133 Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)	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)	
		Location	Amount	Location	Amount
			(in millions)		
For the quarter ended June 26, 2009:					
Foreign currency forward contracts	$ (5)	Cost of Sales	$ (2)	Cost of Sales	$
For the first half ended June 26, 2009:					
Foreign currency forward contracts	$ (6)	Cost of Sales	$ (3)	Cost of Sales	$

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Derivatives not Designated as Hedging Instruments	Gain or (Loss) Recognized in Income on Derivative Location	Amount (in millions)
For the quarter ended June 26, 2009:		
Foreign currency forward contracts	Cost of Sales	$
For the first half ended June 26, 2009:		
Foreign currency forward contracts	Cost of Sales	$

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 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 SFAS No. 5, *Accounting for 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 June 26, 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

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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 Air. In 1996, the FAA determined that the engineering data provided by Hayes/Pemco supporting the STCs was inadequate and issued an Airworthiness Directive that effectively grounded the ten modified aircraft. The Kalitta Air aircraft have not been in revenue service since that date. The matter was tried in January 2001 against GATX and CTAS with the jury finding fault on the part of GATX, but rendering a unanimous defense verdict in favor of CTAS. Certain co-defendants had settled prior to trial. The U.S. Court of Appeals for the Ninth Circuit subsequently reversed and remanded the trial court s summary judgment rulings in favor of CTAS regarding a negligence claim by Kalitta Air, which asserts that CTAS as an expert in aircraft modification should have known that the STCs were deficient. The retrial began on January 18, 2005, and ended on March 2, 2005 with a deadlocked jury and mistrial. At the retrial, Kalitta Air claimed damages of $235 million plus interest. By order dated July 22, 2005, the trial court granted the Company s motion for judgment as a matter of law as to negligence dismissing that claim, denied the Company s motion for judgment as a matter of law as to negligent misrepresentation, and certified the decision for interlocutory appeal to the U.S. Court of Appeals for the Ninth Circuit. On October 8, 2008, the Ninth Circuit reversed the trial court s dismissal of the negligence claim and affirmed the trial court s ruling as to the negligent misrepresentation claim. The case has been remanded to the trial court to reconsider the negligence claim and for further proceedings on the negligent misrepresentation claim. A court-ordered mediation held on March 18, 2009 was unsuccessful. A hearing on the Company s motion to dismiss the negligence claim was held on April 30, 2009, after which the trial court determined to take the matter under advisement and ordered the parties to attend another mediation not later than September 4, 2009. The case is currently scheduled to go to a third trial on November 1, 2010. CTAS insurance carrier has accepted defense of the matter and has retained counsel, subject to a reservation of rights by the insurer to dispute its obligations under the applicable insurance policies in the event of an adverse finding.

Korean Lot II Program. On April 4, 2005, Lockheed Martin Corporation (Lockheed) filed a lawsuit in the Federal District Court for the Northern District of Georgia alleging misappropriation of proprietary information and breach of a license agreement. The complaint alleges that L-3 Integrated Systems (L-3 IS) is in breach of its license agreement with Lockheed and is infringing on Lockheed s intellectual property rights as a result of its performance of a subcontract awarded to L-3 IS for the Korean Lot II program. On May 21, 2009, a jury found in favor of Lockheed and awarded $30 million on the misappropriation claim, $7.28 million on the breach of license agreement claim, plus legal fees and expenses. On July 3, 2009, Lockheed filed a motion with the court seeking approximately $17 million in legal fees and expenses, and an injunction prohibiting L-3 s further use of the intellectual property that was the basis of the jury s award. The Company believes that the verdict and the damages awarded are inconsistent with the law and evidence presented, and intends to appeal following entry of the judgment by the trial court.

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SafeView Arbitration. The Company was previously subject to an American Arbitration Association proceeding initiated by Paladin Homeland Security Fund on behalf of all former stockholders of SafeView, Inc. alleging violations of federal securities laws, fraud, negligent misrepresentation, breach of contract and unjust enrichment in connection with L-3 s acquisition of SafeView. On May 28, 2009, the arbitration panel ruled in favor of L-3 and denied any award to the claimants. Under the terms of the agreement governing the acquisition, the decision is final, conclusive and binding on the parties.

Aircrew Training and Rehearsal Support (ATARS) Investigation. Following a lawsuit filed by Lockheed on April 6, 2006 in the U.S. District Court for the Middle District of Florida against the Company and certain individuals related to the ATARS II Program (which was settled in November 2007), the Company received Grand Jury subpoenas in connection with an investigation being conducted by the United States Attorney for the Middle District of Florida, Orlando Division. The subpoenas request the production of documents related to Lockheed s allegations or produced in the civil litigation settled in November 2007. The Company is cooperating fully with the U.S. Government.

Titan Government Investigation. In October 2002, Titan received a grand jury subpoena from the Antitrust Division of the DoJ requesting the production of documents relating to information technology services performed for the U.S. Air Force at Hanscom Air Force Base in Massachusetts and Wright-Patterson Air Force Base in Ohio. Titan was informed that other companies who have performed similar services had received subpoenas as well. The Company acquired Titan in July 2005. On September 20, 2006, counsel for the Company was informed by the New York Field Office of the DoJ s Criminal Antitrust Division that it was considering indictment. Additionally, a former Titan employee received a letter from the DoJ indicating that he was a target of the investigation. If the Field Office recommends indictment then, under normal DoJ procedures, Tit