GOODRICH CORP
Form 10-Q
October 27, 2008

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

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

For the quarterly period ended September 30, 2008

OR

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

For the transition period from __________ to __________

Commission file number 1-892

GOODRICH CORPORATION

(Exact name of registrant as specified in its charter)

New York	**34-0252680**
(State of Incorporation)	*(I.R.S. Employer Identification No.)*
Four Coliseum Centre **2730 West Tyvola Road** **Charlotte, North Carolina**	**28217**
(Address of Principal Executive Offices)	*(Zip Code)*

Registrant s telephone number, including area code: (704) 423-7000

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

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

Large accelerated filer þ	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 registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

At September 30, 2008, there were 123,098,500 shares of common stock outstanding (excluding 14,000,000 shares held by a wholly owned subsidiary). There is only one class of common stock.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have reviewed the condensed consolidated balance sheet of Goodrich Corporation as of September 30, 2008, and the related condensed consolidated statement of income for the three- and nine- month periods ended September 30, 2008 and 2007, and the condensed consolidated statement of cash flows for the nine-month period ended September 30, 2008 and 2007. These financial statements are the responsibility of the Company s management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Goodrich Corporation as of December 31, 2007, and the related consolidated statements of income, shareholders equity, and cash flows for the year then ended, not presented herein; and in our report dated February 18, 2008, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2007, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Ernst & Young LLP

Charlotte, North Carolina
October 24, 2008

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CONDENSED CONSOLIDATED STATEMENT OF INCOME (UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in millions, except per share amounts)			
Sales	$ 1,772.3	$ 1,601.7	$ 5,366.6	$ 4,724.4
Operating costs and expenses:				
Cost of sales	1,214.9	1,102.9	3,715.2	3,293.4
Selling and administrative costs	260.6	262.6	791.6	777.0
	1,475.5	1,365.5	4,506.8	4,070.4
Operating Income	296.8	236.2	859.8	654.0
Interest expense	(26.7)	(31.5)	(85.2)	(93.8)
Interest income	1.4	2.2	5.1	5.5
Other income (expense) net	(9.6)	(12.5)	(32.2)	(45.6)
Income from continuing operations before income taxes	261.9	194.4	747.5	520.1
Income tax expense	(94.1)	(54.2)	(242.5)	(156.9)
Income From Continuing Operations	167.8	140.2	505.0	363.2
Income (loss) from discontinued operations net of income taxes	0.2	(13.4)	7.5	(11.8)
Net Income	$ 168.0	$ 126.8	$ 512.5	$ 351.4
Basic Earnings Per Share				
Continuing operations	$ 1.35	$ 1.12	$ 4.04	$ 2.90
Discontinued operations		(0.11)	0.06	(0.09)
Net Income	$ 1.35	$ 1.01	$ 4.10	$ 2.81
Diluted Earnings Per Share				
Continuing operations	$ 1.33	$ 1.10	$ 3.97	$ 2.84
Discontinued operations		(0.11)	0.06	(0.09)
Net Income	$ 1.33	$ 0.99	$ 4.03	$ 2.75
Dividends Declared Per Common Share	$ 0.225	$ 0.20	$ 0.675	$ 0.60

See Notes Condensed Consolidated Financial Statements (Unaudited)

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CONDENSED CONSOLIDATED BALANCE SHEET (UNAUDITED)

	September 30, 2008	December 31, 2007
	(Dollars in millions, except share amounts)	
Current Assets		
Cash and cash equivalents	$ 246.9	$ 406.0
Accounts and notes receivable, less allowances for doubtful receivables ($22.4 at September 30, 2008 and $14.3 at December 31, 2007)	1,138.4	1,006.2
Inventories net	1,985.0	1,775.6
Deferred income taxes	177.0	178.2
Prepaid expenses and other assets	59.7	108.4
Income taxes receivable	5.5	74.4
Total Current Assets	3,612.5	3,548.8
Property, plant and equipment net	1,424.9	1,387.4
Prepaid pension	28.4	16.1
Goodwill	1,410.2	1,363.2
Identifiable intangible assets net	447.8	452.1
Deferred income taxes	23.0	11.1
Other assets	674.8	755.3
Total Assets	$ 7,621.6	$ 7,534.0
Current Liabilities		
Short-term debt	$ 112.5	$ 21.9
Accounts payable	677.3	586.7
Accrued expenses	892.0	930.8
Income taxes payable	103.7	10.6
Deferred income taxes	31.0	29.7
Current maturities of long-term debt and capital lease obligations	122.1	162.9
Total Current Liabilities	1,938.6	1,742.6
Long-term debt and capital lease obligations	1,405.4	1,562.9
Pension obligations	381.6	417.8
Postretirement benefits other than pensions	337.1	358.9
Long-term income taxes payable	121.6	146.0
Deferred income taxes	133.6	170.2
Other non-current liabilities	576.0	556.2
Shareholders Equity		
Common stock $5 par value		
Authorized 200,000,000 shares; issued 143,507,229 shares at September 30, 2008 and 142,372,162 shares at December 31, 2007 (excluding 14,000,000 shares held by a wholly owned subsidiary)	717.5	711.9
Additional paid-in capital	1,513.3	1,453.1

Income retained in the business	1,481.7	1,054.8
Accumulated other comprehensive income (loss)	(191.7)	14.4
Common stock held in treasury, at cost (20,408,729 shares at September 30, 2008 and 17,761,696 shares at December 31, 2007)	(793.1)	(654.8)
Total Shareholders Equity	2,727.7	2,579.4
Total Liabilities And Shareholders Equity	$ 7,621.6	$ 7,534.0

See Notes Condensed Consolidated Financial Statements (Unaudited)

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CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED)

	Nine Months Ended September 30,	
	2008	2007
	(Dollars in millions)	
Operating Activities		
Net income	$ 512.5	$ 351.4
Adjustments to reconcile net income to net cash provided by operating activities:		
(Income) loss from discontinued operations	(7.5)	11.8
Restructuring and consolidation:		
Expenses	1.3	1.5
Payments	(1.7)	(2.9)
Pension and postretirement benefits:		
Expenses	76.9	95.6
Contributions and benefit payments	(124.2)	(137.4)
Depreciation and amortization	192.0	188.6
Excess tax benefits related to share-based payment arrangements	(8.4)	(11.7)
Share-based compensation expense	25.5	55.3
Deferred income taxes	(9.0)	(11.9)
Change in assets and liabilities, net of effects of acquisitions and divestitures:		
Receivables	(149.1)	(93.5)
Inventories, net of pre-production and excess-over-average	(144.4)	(120.0)
Pre-production and excess-over-average inventories	(83.3)	(86.7)
Other current assets	(2.8)	7.8
Accounts payable	107.9	11.8
Accrued expenses	(55.5)	76.8
Income taxes payable/receivable	151.2	68.3
Other non-current assets and liabilities	(20.6)	1.3
Net Cash Provided By Operating Activities	460.8	406.1
Investing Activities		
Purchases of property, plant and equipment	(189.6)	(160.6)
Proceeds from sale of property, plant and equipment	2.8	0.8
Payments made for acquisitions, net of cash acquired	(131.8)	
Net Cash Used In Investing Activities	(318.6)	(159.8)
Financing Activities		
Increase (decrease) in short-term debt, net	90.6	(0.3)
Repayment of long-term debt and capital lease obligations	(198.1)	(1.1)
Proceeds from issuance of common stock	24.2	78.9
Purchases of treasury stock	(138.3)	(152.5)
Dividends paid	(85.7)	(75.9)
Excess tax benefits related to share-based payment arrangements	8.4	11.7
Distributions to minority interest holders	(6.8)	(3.2)
Net Cash Used In Financing Activities	(305.7)	(142.4)

Discontinued Operations		
Net cash provided by (used in) operating activities	(2.6)	6.6
Net cash provided by (used in) investing activities	15.7	(1.4)
Net cash provided by (used in) financing activities		
Net cash provided by (used in) discontinued operations	13.1	5.2
Effect of exchange rate changes on cash and cash equivalents	(8.7)	3.9
Net increase (decrease) in cash and cash equivalents	(159.1)	113.0
Cash and cash equivalents at beginning of period	406.0	201.3
Cash and cash equivalents at end of period	$ 246.9	$ 314.3

See Notes Condensed Consolidated Financial Statements (Unaudited)

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1. Basis of Interim Financial Statement Preparation and Use of Estimates

The accompanying Unaudited Condensed Consolidated Financial Statements of Goodrich Corporation and its subsidiaries have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and notes required by accounting principles generally accepted in the United States for complete financial statements. Unless indicated otherwise or the context requires, the terms we, our, us, Goodrich or Company refe Goodrich Corporation and its subsidiaries. The Company believes that all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Certain amounts in prior year financial statements have been reclassified to conform to the current year presentation. Operating results for the three months and nine months ended September 30, 2008 are not necessarily indicative of the results that may be achieved for the twelve months ending December 31, 2008. For further information, refer to the consolidated financial statements and notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007.

As discussed in Note 5, Discontinued Operations , Goodrich Aviation Technical Services, Inc. (ATS) has been accounted for as a discontinued operation. Unless otherwise noted, disclosures pertain to the Company s continuing operations.

The preparation of financial statements requires management to make estimates and assumptions that affect amounts recognized. Estimates and assumptions are reviewed and updated regularly as new information becomes available. During the three and nine months ended September 30, 2008 and 2007, the Company changed its estimates of revenues and costs on certain long-term contracts primarily in its aerostructures and aircraft wheels and brakes businesses. The changes in estimates increased income from continuing operations before income taxes during the three months ended September 30, 2008 and 2007 by $38.7 million and $19.2 million, respectively ($23.7 million and $11.7 million after tax, respectively). The changes in estimates increased income from continuing operations before income taxes during the nine months ended September 30, 2008 and 2007 by $87.4 million and $54.4 million, respectively ($53.6 million and $33.2 million after tax, respectively).

Note 2. New Accounting Standards

Accounting Standards Adopted on January 1, 2008

Fair Value Measurements

The Company adopted Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles and expands disclosures about fair value measurements. The adoption of SFAS 157 did not have a material impact on the Company s financial condition and results of operations. For additional information on the fair value of certain financial assets and liabilities, see Note 7, Fair Value Measurements .

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Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards

The Company adopted Emerging Issues Task Force No. 06-11, Accounting for the Income Tax Benefits of Dividends on Share-Based Payment Awards (EITF 06-11). The adoption of EITF 06-11 did not have a material impact on the Company s financial condition and results of operations.

Accounting for Postretirement Benefits Associated with Split-Dollar Life Insurance

The Company adopted Emerging Issues Task Force No. 06-4, Accounting for Deferred Compensation and Postretirement Benefits Associated with Endorsement Split-Dollar Life Insurance Arrangements (EITF 06-4) and Emerging Issues Task Force No. 06-10, Accounting for Collateral Assignment Split-Dollar Insurance Arrangements (EITF 06-10). The adoption of EITF 06-4 and EITF 06-10 did not have a material impact on the Company s financial condition and results of operations.

Accounting Standards Not Yet Adopted

Two-class Method of Computing Earnings Per Share

In June 2008, the Financial Accounting Standards Board (FASB) issued Staff Position No. EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities (FSP 03-6-1). In FSP 03-6-1, unvested share-based payment awards that contain rights to receive nonforfeitable dividends or dividend equivalents (whether paid or unpaid) are participating securities, and thus, should be included in the two-class method of computing earnings per share (EPS). This FSP is effective for fiscal years beginning after December 15, 2008 and interim periods within those years and requires that all prior period EPS be adjusted retroactively. Upon adoption, the Company does not expect this standard to have a material impact on its disclosures of EPS.

Disclosures about Derivative Instruments and Hedging Activities

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 161, Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133 (SFAS 161). SFAS 161 requires entities to provide greater transparency through additional disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement of Financial Accounting Standards No. 133 Accounting for Derivative Instruments and Hedging Activities (SFAS 133) and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity s financial position, results of operations, and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. Upon adoption, the Company will include additional disclosures of its derivative instruments to comply with this standard.

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Business Combinations and Noncontrolling Interests

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141(R), Business Combinations (SFAS 141(R)) and Statement of Financial Accounting Standards No. 160 Accounting and Reporting of Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51 (SFAS 160). SFAS 141(R) and SFAS 160 significantly change the accounting for and reporting of business combination transactions and noncontrolling (minority) interests. SFAS 141(R) and SFAS 160 are effective for the fiscal years beginning after December 15, 2008. Upon adoption, the Company will change the presentation of its noncontrolling interests in its Consolidated Financial Statements to comply with the requirements of SFAS 160. SFAS 141(R) is required to be adopted concurrently with SFAS 160 and is effective for business combination transactions for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008.

Note 3. Business Segment Information

The Company s three business segments are as follows:

The Actuation and Landing Systems segment provides systems, components and related services pertaining to aircraft taxi, take-off, flight control, landing and stopping, and engine components, including fuel delivery systems and rotating assemblies.

The Nacelles and Interior Systems segment produces products and provides maintenance, repair and overhaul services associated with aircraft engines, including thrust reversers, cowlings, nozzles and their components, and aircraft interior products, including slides, seats, cargo and lighting systems.

The Electronic Systems segment produces a wide array of systems and components that provide flight performance measurements, flight management, fuel controls, electrical systems, and control and safety data, and reconnaissance and surveillance systems.

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The Company measures each reporting segment s profit based upon operating income. Accordingly, the Company does not allocate net interest expense, other income (expense) net and income taxes to its reporting segments. The company-wide Enterprise Resource Planning (ERP) implementation costs that are not directly associated with a specific business were not allocated to the segments. The accounting policies of the reportable segments are the same as those for the Company s condensed consolidated financial statements.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Sales:				
Actuation and Landing Systems	$ 664.2	$ 607.8	$ 2,035.9	$ 1,764.1
Nacelles and Interior Systems	596.5	545.2	1,882.1	1,625.8
Electronic Systems	511.6	448.7	1,448.6	1,334.5
	$ 1,772.3	$ 1,601.7	$ 5,366.6	$ 4,724.4
Intersegment sales:				
Actuation and Landing Systems	$ 8.5	$ 8.0	$ 26.4	$ 21.2
Nacelles and Interior Systems	1.9	5.1	11.3	14.2
Electronic Systems	6.6	5.9	19.3	23.0
	$ 17.0	$ 19.0	$ 57.0	$ 58.4
Operating income:				
Actuation and Landing Systems	$ 80.0	$ 73.6	$ 238.6	$ 182.0
Nacelles and Interior Systems	162.4	143.6	501.9	404.7
Electronic Systems	79.3	58.7	199.8	175.7
	321.7	275.9	940.3	762.4
Corporate general and administrative expenses	(21.1)	(34.5)	(67.8)	(95.9)
ERP implementation costs	(3.8)	(5.2)	(12.7)	(12.5)
Total operating income	$ 296.8	$ 236.2	$ 859.8	$ 654.0

Note 4. Other Income (Expense) net

Other Income (Expense) net consisted of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Retiree health care expenses related to previously owned businesses	$ (3.8)	$ (4.6)	$ (14.6)	$ (13.8)
Expenses related to previously owned businesses	(2.1)	(4.8)	(5.9)	(16.1)
Minority interest and equity in affiliated companies	(3.5)	(4.7)	(12.3)	(17.6)
Other net	(0.2)	1.6	0.6	1.9
Other income (expense) net	$ (9.6)	$ (12.5)	$ (32.2)	$ (45.6)

Expenses related to previously owned businesses primarily relates to environmental litigation costs, net of settlements, and remediation costs.

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Note 5. Discontinued Operations

On September 21, 2007, the Company reached a definitive agreement to sell ATS, which was previously reported in the Actuation and Landing Systems segment. The sale closed during the fourth quarter of 2007. In accordance with the provisions of Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets the Company compared the book value of the net assets of ATS to their fair value and recorded an estimated loss on the sale of $13.9 million after tax during the three and nine months ended September 30, 2007. All periods have been reclassified to reflect ATS as a discontinued operation. The costs and revenues, assets and liabilities, and cash flows of ATS have been reported as a discontinued operation in the Company s condensed consolidated financial statements.

On March 3, 2008, the Company sold a previously discontinued operation.

Discontinued operations were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Sales ATS	$	$ 34.4	$	$ 122.6
Operations ATS net of tax for the three and nine months ended September 30, 2007 of $0.2 and $1.3, respectively	$	$ 0.6	$	$ 2.5
Estimated loss on sale of ATS net of income tax benefit of $37.5		(13.9)		(13.9)
Previously discontinued operations net of tax expense for the three and nine months ended September 30, 2008 of $0 and $0.6, respectively; net of tax benefit for the three and nine months ended September 30, 2007 of $0.1 and $0.3, respectively	0.2	(0.1)	7.5	(0.4)
Income (loss) from discontinued operations	$ 0.2	$ (13.4)	$ 7.5	$ (11.8)

Note 6. Earnings Per Share

The computation of basic and diluted earnings per share for income from continuing operations is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(In millions, except per share amounts)			
Numerator				
Numerator for basic and diluted earnings per share income from continuing operations	$ 167.8	$ 140.2	$ 505.0	$ 363.2
Denominator				
Denominator for basic earnings per share weighted-average shares	124.4	125.0	124.9	125.2
Effect of dilutive securities:				
Stock options, employee stock purchase plan, restricted shares and restricted share units	1.8	2.6	2.1	2.5
Other deferred compensation shares	0.1	0.1	0.1	0.1

	1.9	2.7	2.2	2.6
Denominator for diluted earnings per share adjusted weighted-average shares and assumed conversion	126.3	127.7	127.1	127.8
Per share income from continuing operations				
Basic	$ 1.35	$ 1.12	$ 4.04	$ 2.90
Diluted	$ 1.33	$ 1.10	$ 3.97	$ 2.84

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At September 30, 2008 and 2007, the Company had 4.6 million and 4.8 million of outstanding stock options, respectively. Stock options are included in the diluted earnings per share calculation using the treasury stock method, unless the effect of including the stock options would be anti-dilutive. For the nine months ended September 30, 2008 and 2007, 896,000 and 1.2 million, respectively, anti-dilutive stock options were excluded from the diluted earnings per share calculation.

During the nine months ended September 30, 2008 and 2007, the Company issued 1.1 million and 2.7 million, respectively, of shares of common stock pursuant to stock option exercises and other share-based compensation plans.

During the nine months ended September 30, 2008 and 2007, the Company repurchased 2.5 million shares and 2.7 million shares, respectively, under its share repurchase program that was initially approved by the Board of Directors on October 24, 2006 and increased by the Board of Directors on February 19, 2008, for $600 million in total. As of September 30, 2008, the Company has purchased 6.4 million shares to date for approximately $354 million under the Company s share repurchase program.

Note 7. Fair Value Measurements

As described in Note 2, New Accounting Standards , the Company has adopted SFAS 157 which defines fair value as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. SFAS 157 also describes three levels of inputs that may be used to measure fair value:

Level 1 quoted prices in active markets for identical assets and liabilities.

Level 2 observable inputs other than quoted prices in active markets for identical assets and liabilities.

Level 3 unobservable inputs in which there is little or no market data available, which require the reporting entity to develop its own assumptions.

The Company s financial assets and (liabilities) measured at fair value on a recurring basis were as follows:

	Balance September 30, 2008	Level 1	Level 2	Level 3
		(Dollars in millions)		
Cash Equivalents	$37.5	$37.5	$	$
Derivative Financial Instruments (1)				
Cash Flow Hedges	(7.4)		(7.4)	
Fair Value Hedges	3.6		3.6	
Other Forward Contracts	2.1		2.1	
Rabbi Trust Assets (2)	40.5	40.5		

(1) See Note 16, Derivatives and Hedging Activities .

(2) Rabbi trust assets include mutual funds and cash equivalents for payment of certain non-qualified

benefits for
retired,
terminated and
active
employees.

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Note 8. Inventories
Inventories consist of the following:

	September 30, 2008	December 31, 2007
	(Dollars in millions)	
FIFO or average cost (which approximates current costs):		
Finished products	$ 250.6	$ 252.9
In-process	1,272.0	1,067.0
Raw materials and supplies	553.1	533.3
	2,075.7	1,853.2
Less:		
Reserve to reduce certain inventories to LIFO basis	(52.4)	(49.5)
Progress payments and advances	(38.3)	(28.1)
Total	$ 1,985.0	$ 1,775.6

In-process inventory included $603.3 million and $515.4 million at September 30, 2008 and December 31, 2007, respectively, for the following: (1) pre-production and excess-over-average inventory accounted for under long-term contract accounting; and (2) engineering costs guaranteed of recovery under long-term contractual arrangements. The September 30, 2008 balance of $603.3 million included $374.5 million related to Boeing 787 contracts.
The Company uses the last-in, first-out (LIFO) method of valuing inventory for certain of the Company s legacy aerospace manufacturing businesses, primarily the aircraft wheels and brakes business unit in the Actuation and Landing Systems segment. An actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time.
Note 9. Goodwill
The changes in the carrying amount of goodwill by segment were as follows:

	Balance December 31, 2007	Business Combinations (3)	Foreign Currency Translation	Balance September 30, 2008
		(Dollars in millions)		
Actuation and Landing Systems	$ 331.5	$	$ (16.7)	$ 314.8
Nacelles and Interior Systems	433.1	3.6(1)	(0.7)	436.0
Electronic Systems	598.6	61.0(2)	(0.2)	659.4
	$ 1,363.2	$ 64.6	$ (17.6)	$ 1,410.2

(1) On January 18, 2008, the Company acquired Skyline Industries, Inc. (Skyline) for

$9.5 million in cash. Based upon an independent valuation, identifiable intangibles were $4.1 million and will be amortized over a weighted-average useful life of 20 years.

(2) On April 17, 2008, the Company acquired TEAC Aerospace Holdings, Inc. (TEAC) for $84 million in cash, net of cash acquired. Based upon an independent valuation, identifiable intangibles were $30.9 million and will be amortized over a weighted-average useful life of 11 years.

On July 28, 2008, the Company acquired certain assets of Recon/Optical, Inc. (ROI) for $38.4 million in cash. Based upon an independent valuation, identifiable intangibles were $7.9 million and will be amortized over a weighted-average useful life of 12 years.

(3) Goodwill amounts are preliminary and may be adjusted when certain pre-acquisition contingencies are resolved.

Note 10. Financing Arrangements

The Company has a $500 million committed global syndicated revolving credit facility, which expires in May 2012. Interest rates under this facility vary depending upon:

- The amount borrowed;
- The Company s public debt rating by Standard & Poor s, Moody s and Fitch; and
- At the Company s option, rates tied to the agent bank s prime rate or, for U.S. Dollar and Great Britain Pounds Sterling borrowings, the London Interbank Offered Rate and for Euro Dollar borrowings, the Euro Interbank Offered Rate.

At September 30, 2008, there were $70 million in borrowings and $36.3 million in letters of credit outstanding under the facility. At December 31, 2007, there were $34.9 million in borrowings and $22.3 million in letters of credit outstanding under the facility. The level of unused borrowing capacity varies from time to time depending, in part, upon the Company s compliance with financial and other covenants set forth in the related agreement, including the consolidated net worth requirement and maximum leverage ratio. The Company is currently in compliance with all such covenants. Under the most restrictive of these covenants, $1,499.9 million of income retained in the business and additional paid-in capital was free from such limitations at September 30, 2008. At September 30, 2008, the Company had borrowing capacity under this facility of $393.7 million, after reductions for borrowings and letters of credit outstanding under the facility.

At September 30, 2008, the Company had letters of credit and bank guarantees of $77.1 million, inclusive of $36.3 million in letters of credit outstanding under the Company s syndicated revolving credit facility, as discussed above.

At September 30, 2008, the Company also maintained $75 million of uncommitted domestic money market facilities and $174.9 million of uncommitted and committed foreign working capital facilities with various banks to meet short-term borrowing requirements. At September 30, 2008 and December 31, 2007, there were $42.5 million and $25.9 million, respectively, in borrowings outstanding under these facilities. These credit facilities are provided by a small number of commercial banks that also provide the Company with committed credit through the syndicated revolving credit facility described above and with various cash management, trust and other services.

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Long-term Debt Repayments

The Company used cash from operations to repay $162 million for the following notes, which matured on April 15, 2008:

- $119 million principal amount of the 7.5% notes; and
- $43 million principal amount of the 6.45% notes.

On June 23, 2008, the Company also used cash from operations to repay $34.9 million under its revolving credit facility.

Lease Commitments

The Company leases certain of its office and manufacturing facilities as well as machinery and equipment, including corporate aircraft, under various committed lease arrangements provided by financial institutions.

Certain of these arrangements allow the Company, rather than the lessor, to claim a deduction for tax depreciation on the assets and allow the Company to lease corporate aircraft and equipment having a maximum unamortized value of $150 million at September 30, 2008. These leases are priced at a spread over LIBOR and are extended periodically through the end of the lease terms, unless notice is provided. At September 30, 2008, future payments under these leases were $9.5 million. At September 30, 2008, the Company had guarantees of residual values on lease obligations of $24.8 million. The Company is obligated to either purchase or remarket the leased assets at the end of the lease term. During the three months ended September 30, 2008, the Company entered into a similar arrangement to lease corporate aircraft having a maximum unamortized value of $55 million.

Future minimum lease payments under standard operating leases were $173.5 million at September 30, 2008.

Note 11. Pensions and Postretirement Benefits Other Than Pensions
Pensions
The following table sets forth the components of net periodic benefit cost. The net periodic benefit cost for divested or discontinued operations retained by the Company are included in the amounts below.

	U.S. Plans Three Months Ended September 30,		U.K. Plans Three Months Ended September 30,		Other Plans Three Months Ended September 30,	
	2008	2007	2008	2007	2008	2007
			(Dollars in millions)			
Service cost	$ 10.7	$ 11.4	$ 7.1	$ 7.4	$ 1.4	$ 1.3
Interest cost	41.9	39.5	10.7	10.0	1.6	1.4
Expected return on plan assets	(50.0)	(47.7)	(16.2)	(15.2)	(1.7)	(1.6)
Amortization of prior service cost	1.4	1.8	(0.3)	(0.3)		
Amortization of actuarial loss	12.3	14.3			0.2	0.3
Net periodic benefit cost	16.3	19.3	1.3	1.9	1.5	1.4
Settlements and curtailments loss	0.1	6.0				
Net benefit cost	$ 16.4	$ 25.3	$ 1.3	$ 1.9	$ 1.5	$ 1.4

	U.S. Plans Nine Months Ended September 30,		U.K. Plans Nine Months Ended September 30,		Other Plans Nine Months Ended September 30,	
	2008	2007	2008	2007	2008	2007
			(Dollars in millions)			
Service cost	$ 32.1	$ 34.9	$ 22.1	$ 21.9	$ 4.3	$ 3.6
Interest cost	125.7	120.0	32.8	29.5	4.8	4.0
Expected return on plan assets	(150.1)	(146.3)	(50.1)	(45.0)	(5.2)	(4.5)
Amortization of prior service cost	4.2	5.6	(0.8)	(0.8)	0.1	
Amortization of actuarial loss	36.7	47.0			0.7	0.8
Net periodic benefit cost	48.6	61.2	4.0	5.6	4.7	3.9
Settlements and curtailments loss	0.1	6.0				
Net benefit cost	$ 48.7	$ 67.2	$ 4.0	$ 5.6	$ 4.7	$ 3.9

The following table provides the weighted-average assumptions used to determine the net periodic benefit cost.

	U.S. Plans		U.K. Plans		Other Plans	
	2008	2007	2008	2007	2008	2007
Discount rate	6.30%		5.50%	5.00%	5.28%	4.88%
1/1/07 9/20/07		5.89%				

9/21/07 9/30/07		6.28%				
Expected long-term rate of return on assets	9.00%	9.00%	8.50%	8.50%	8.24%	8.28%
Rate of compensation increase	4.10%	3.86%	3.75%	3.50%	3.38%	3.36%

On September 21, 2007, a definitive agreement to divest ATS was reached and assumptions for the U.S. qualified pension plans were reevaluated to remeasure the plan obligations and assets. In connection with the remeasurement, there was a curtailment loss of $6 million reported in discontinued operations in the three and nine months ended September 30, 2007.

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Anticipated Contributions to Defined Benefit Plans and Trusts

As of September 30, 2008, the Company had contributed $101.6 million to its worldwide qualified and non-qualified pension plans. For 2008, the Company expects to contribute up to a total of $120 million to these plans.

Postretirement Benefits Other Than Pensions

The following table sets forth the components of net periodic postretirement benefit cost. Other postretirement benefits (OPEB) related to divested and discontinued operations retained by the Company are included in the amounts below.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Service cost	$ 0.3	$ 0.4	$ 1.2	$ 1.4
Interest cost	5.5	5.6	16.5	17.1
Amortization of prior service cost			(0.1)	(0.1)
Amortization of actuarial (gain) loss	0.5	1.4	1.9	2.2
Net periodic benefit cost	$ 6.3	$ 7.4	$ 19.5	$ 20.6

The following table provides the assumptions used to determine the net periodic postretirement benefit cost.

	Three and Nine Months Ended September 30,	
	2008	2007
Discount rate	6.12%	5.79%
Healthcare trend rate	8.3% in 2008 to 5% in 2015	9% in 2007 to 5% in 2013

Note 12. Comprehensive Income (Loss)

Total comprehensive income (loss) consisted of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Net income	$ 168.0	$ 126.8	$ 512.5	$ 351.4
Other comprehensive income (loss):				
Unrealized foreign currency translation gains (losses) during period	(147.7)	51.4	(117.4)	109.6
Pension/OPEB liability adjustments during the period, net of tax for the three and nine months ended September 30, 2008 of $(5.7) and ($11.8), respectively; net of tax for the three and nine months ended September 30, 2007 of ($66.3) and ($70.4), respectively	8.1	100.9	15.0	127.4
Gain (loss) on cash flow hedges, net of tax for the three and nine months ended September 30, 2008 of $49.4 and $55.7, respectively; net of tax for the three and nine months ended September 30, 2007 of ($16.3) and ($28.2), respectively	(91.7)	29.1	(103.7)	53.4

Total comprehensive income (loss)	$ (63.3)	$ 308.2	$ 306.4	$ 641.8

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Accumulated other comprehensive income (loss) consisted of the following:

	September 30, 2008	December 31, 2007
	(Dollars in millions)	
Cumulative unrealized foreign currency translation gains	$ 232.2	$ 349.6
Pension/OPEB liability adjustments, net of deferred taxes of $273.8 and $285.6, respectively	(417.8)	(432.8)
Accumulated gains (losses) on cash flow hedges, net of deferred taxes of $2.3 and $(53.4), respectively	(6.1)	97.6
Total accumulated other comprehensive income (loss)	$ (191.7)	$ 14.4

No income taxes are provided on unrealized foreign currency translation gains as foreign earnings are considered permanently invested.

Note 13. Income Taxes

The Company s effective tax rate for the three months ended September 30, 2008 was 35.9%. Significant items that impacted the Company s effective tax rate as compared to the U.S. federal statutory rate of 35% included foreign and domestic tax credits which reduced the effective tax rate by approximately 2 percentage points, earnings in foreign jurisdictions taxed at rates different from the statutory U.S. federal rate which reduced the effective tax rate by approximately 3 percentage points, deemed repatriation of non-U.S. earnings which increased the effective tax rate by approximately 2 percentage points, adjustments to reserves for tax contingencies, including interest thereon (net of related tax benefit), which increased the effective tax rate by approximately 2 percentage points and state income taxes (net of related tax benefit) which increased the effective tax rate by approximately 3 percentage points. During the three months ended September 30, 2007, the Company reported an effective tax rate of 27.9%, including a benefit from a tax settlement related to the IRS examination of the Company s 2000-2004 income tax returns which reduced the effective tax rate by approximately 8 percentage points, foreign and domestic tax credits which reduced the effective tax rate by approximately 4 percentage points, earnings in foreign jurisdictions taxed at rates different from the statutory U.S. federal rate which reduced the effective tax rate by approximately 3 percentage points, deemed repatriation of non-U.S. earnings which increased the effective tax rate by approximately 2 percentage points, adjustments to reserves for tax contingencies, including interest thereon (net of related tax benefit), which increased the effective tax rate by approximately 2 percentage points and state income taxes (net of related tax benefit) which increased the effective tax rate by approximately 3 percentage points.

For the nine months ended September 30, 2008, the Company reported an effective tax rate of 32.4%, including a benefit of approximately 3 percentage points for amended state returns primarily for additional research and development credits and changes in apportionment, and a benefit of approximately 3 percentage points related to amended returns following the settlement of a foreign tax audit. For the nine months ended September 30, 2007, the Company reported an effective tax rate of 30.2%, including a benefit of approximately 2 percentage points for the elimination of certain valuation allowances against net operating losses of a foreign subsidiary and a benefit of approximately 3 percentage points primarily related to the reversal of tax reserves associated with tax settlements.

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The Company s effective tax rates during the three and nine months ended September 30, 2008 were not reduced for the benefit of the U.S. Research and Development Credit (R&D Credit), which became law on October 3, 2008. The Company estimates that the effective tax rate for 2008 would have been approximately 1 percentage point lower had the Company been able to consider the tax benefits associated with the R&D Credit. The benefit is retroactive to the beginning of 2008, and the full year benefit will be reflected in the Company s fourth quarter 2008 results.

The Company had a $241.9 million liability recorded for unrecognized tax benefits at December 31, 2007, which included interest and penalties of $135.6 million. The Company reported interest and penalties related to unrecognized tax benefits in income tax expense. The total amount of unrecognized benefits that, if recognized, would have affected the effective tax rate was $176.2 million. At September 30, 2008, the Company had a $248.2 million liability recorded for unrecognized tax benefits, which included interest and penalties of $146.8 million. The total amount of unrecognized benefits that, if recognized, would have affected the effective tax rate was $191.6 million.

Note 14. Contingencies

General

There are various pending or threatened claims, lawsuits and administrative proceedings against the Company or its subsidiaries, arising from the ordinary course of business which seek remedies or damages. Although no assurance can be given with respect to the ultimate outcome of these matters, the Company believes that any liability that may finally be determined with respect to commercial and non-asbestos product liability claims should not have a material effect on its consolidated financial position, results of operations or cash flows. Legal costs are expensed as incurred.

Environmental

The Company is subject to environmental laws and regulations which may require that the Company investigate and remediate the effects of the release or disposal of materials at sites associated with past and present operations. At certain sites, the Company has been identified as a potentially responsible party under the federal Superfund laws and comparable state laws. The Company is currently involved in the investigation and remediation of a number of sites under applicable laws.

Estimates of the Company s environmental liabilities are based on current facts, laws, regulations and technology. These estimates take into consideration the Company s prior experience and professional judgment of the Company s environmental specialists. Estimates of the Company s environmental liabilities are further subject to uncertainties regarding the nature and extent of site contamination, the range of remediation alternatives available, evolving remediation standards, imprecise engineering evaluations and cost estimates, the extent of corrective actions that may be required and the number and financial condition of other potentially responsible parties, as well as the extent of their responsibility for the remediation.

Accordingly, as investigation and remediation proceed, it is likely that adjustments in the Company s accruals will be necessary to reflect new information. The amounts of any such adjustments could have a material adverse effect on the Company s results of operations or cash flows in a given period. Based on currently available information, however, the Company does not believe that future environmental costs in excess of those accrued with respect to sites for which the Company has been identified as a potentially responsible party are likely to have a material adverse effect on the Company s financial condition.

Environmental liabilities are recorded when the liability is probable and the costs are reasonably estimable, which generally is not later than at completion of a feasibility study or when the Company has recommended a remedy or has committed to an appropriate plan of action. The liabilities are reviewed periodically and, as investigation and remediation proceed, adjustments are made as necessary. Liabilities for losses from environmental remediation obligations do not consider the effects of inflation and anticipated expenditures are not discounted to their present value. The liabilities are not reduced by possible recoveries from insurance carriers or other third parties, but do reflect anticipated allocations among potentially responsible parties at federal Superfund sites or similar state-managed sites, third party indemnity obligations, and an assessment of the likelihood that such parties will fulfill their obligations at such sites.

The Company s Condensed Consolidated Balance Sheet included an accrued liability for environmental remediation obligations of $67.1 million and $69.6 million at September 30, 2008 and December 31, 2007, respectively. At September 30, 2008 and December 31, 2007, $22 million and $18.6 million, respectively, of the accrued liability for environmental remediation were included in current liabilities as accrued expenses. At September 30, 2008 and December 31, 2007, $28 million and $29.4 million, respectively, was associated with ongoing operations and $39.1 million and $40.2 million, respectively, was associated with previously owned businesses.

The Company expects that it will expend present accruals over many years, and will generally complete remediation in less than 30 years at sites for which it has been identified as a potentially responsible party. This period includes operation and monitoring costs that are generally incurred over 15 to 25 years.

Recently, certain states in the U.S. and countries globally are promulgating or proposing new or more demanding regulations or legislation impacting the use of various chemical substances by all companies. The Company is currently evaluating the potential impact, if any, of complying with such regulations and legislation.

Asbestos

The Company and some of its subsidiaries have been named as defendants in various actions by plaintiffs alleging damages as a result of exposure to asbestos fibers in products or at its facilities. A number of these cases involve maritime claims, which have been and are expected to continue to be administratively dismissed by the court. The Company believes that pending and reasonably anticipated future actions are not likely to have a material adverse effect on the Company s financial condition, results of operations or cash flows. There can be no assurance, however, that future legislative or other developments will not have a material adverse effect on the Company s financial position, results of operations or cash flows in a given period.

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Insurance Coverage

The Company maintains a comprehensive portfolio of insurance policies, including aviation products liability insurance which covers most of its products. The aviation products liability insurance provides first dollar coverage for defense and indemnity of third party claims.

A portion of the Company s primary and excess layers of pre-1986 insurance coverage for third party claims was provided by certain insurance carriers who are either insolvent, undergoing solvent schemes of arrangement or in run-off. The Company has entered into settlement agreements with a number of these insurers pursuant to which the Company agreed to give up its rights with respect to certain insurance policies in exchange for negotiated payments. These settlements represent negotiated payments for the Company s loss of insurance coverage, as it no longer has this insurance available for claims that may have qualified for coverage. A portion of these settlements was recorded as income for reimbursement of past claim payments under the settled insurance policies and a portion was recorded as a deferred settlement credit for future claim payments.

At September 30, 2008 and December 31, 2007, the deferred settlement credit was $51.2 million and $53.6 million, respectively, for which $6.4 million and $7.6 million, respectively, was reported in accrued expenses and $44.8 million and $46 million, respectively, was reported in other non-current liabilities. The proceeds from such insurance settlements were reported as a component of net cash provided by operating activities in the period payments were received.

Liabilities of Divested Businesses

Asbestos

In May 2002, the Company completed the tax-free spin-off of its Engineered Industrial Products (EIP) segment, which at the time of the spin-off included EnPro Industries, Inc. (EnPro) and Coltec Industries Inc (Coltec). At that time, two subsidiaries of Coltec were defendants in a significant number of personal injury claims relating to alleged asbestos-containing products sold by those subsidiaries prior to the Company s ownership. It is possible that asbestos-related claims might be asserted against the Company on the theory that it has some responsibility for the asbestos-related liabilities of EnPro, Coltec or its subsidiaries. A limited number of asbestos-related claims have been asserted against the Company as successor to Coltec or one of its subsidiaries. The Company believes that it has substantial legal defenses against these and other such claims. In addition, the agreement between EnPro and the Company that was used to effectuate the spin-off provides the Company with an indemnification from EnPro covering, among other things, these liabilities. The Company believes that such claims would not have a material adverse effect on its financial condition, but could have a material adverse effect on its results of operations and cash flows in a particular period.

Other

In connection with the divestiture of the Company s tire, vinyl and other businesses, the Company has received contractual rights of indemnification from third parties for environmental and other claims arising out of the divested businesses. Failure of these third parties to honor their indemnification obligations could have a material adverse effect on the Company s financial condition, results of operations or cash flows.

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Aerostructures Long-term Contracts

The Company s aerostructures business in the Nacelles and Interior Systems segment has several long-term contracts in the pre-production phase including the Boeing 787 and Airbus A350 XWB, and in the early production phase including the Airbus A380. These contracts are accounted for 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).

The pre-production phase includes design of the product to meet customer specifications as well as design of the processes to manufacture the product. Also involved in this phase is securing the supply of material and subcomponents produced by third party suppliers that are generally accomplished through long-term supply agreements.

Contracts in the early production phase include excess-over-average inventories, which represent the excess of current manufactured cost over the estimated average manufactured cost during the life of the contract.

Cost estimates over the lives of contracts are affected by estimates of future cost reductions including learning curve efficiencies. Because these contracts cover manufacturing periods of up to 20 years or more, there is risk associated with the estimates of future costs made during the pre-production and early production phases. These estimates may be different from actual costs due to the following:

- Ability to recover costs incurred for change orders and claims;
- Costs, including material and labor costs and related escalation;
- Labor improvements due to the learning curve experience;
- Anticipated cost productivity improvements related to new manufacturing methods and processes;
- Supplier pricing, including escalation where applicable, supplier claims (see Dispute with Supplier below), and the supplier s ability to perform;
- The cost impact of product design changes that frequently occur during the flight test and certification phases of a program; and
- Effect of foreign currency exchange fluctuations.

Additionally, total contract revenue is based on estimates of future units to be delivered to the customer and sales price escalation, where applicable. There is a risk that there could be differences between the actual units delivered and the estimated total units to be delivered under the contract and differences in actual sales price escalation compared to estimates. Changes in estimates could have a material impact on the Company s results of operations and cash flows.

Provisions for estimated losses on uncompleted contracts are recorded in the period such losses are determined to the extent total estimated costs exceed total estimated contract revenues.

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Dispute with Supplier

On July 21, 2008, Alenia Aermacchi, S.p.A. (AAeM) filed a Demand for Arbitration with the American Arbitration Association against Rohr, Inc. (Rohr), a wholly-owned subsidiary of the Company, in connection with a contract for the supply of fan cowls used in the nacelles that Rohr provides to Boeing on the 787 program. According to its Statement of Claims filed on August 15, 2008, AAeM seeks declaratory relief, rescission of the supply contract and monetary damages based upon allegations of commercial impracticability, lack of compensation for costs associated with design changes and Rohr s mismanagement of the program. On September 22, 2008, Rohr filed its answer, seeking to uphold the contract and denying liability, and instituted a counterclaim against AAeM, seeking damages for breach of contract and breach of covenant of good faith and fair dealing. AAeM has until October 31, 2008 to file its answer to Rohr s counterclaims.

The Company believes that it has substantial legal and factual defenses to AAeM s claims, and intends to defend its interests and pursue its counterclaim vigorously. Given the nature and status of this proceeding, the Company cannot yet determine the amount or a reasonable range of potential loss, if any. However, there can be no assurance that this matter could not have a material adverse effect on the Company s results of operations and/or cash flows in a given period.

Tax

The Company is continuously undergoing examination by the IRS as well as various state and foreign jurisdictions. The IRS and other taxing authorities routinely challenge certain deductions and credits reported by the Company on its income tax returns. The Company establishes reserves for tax contingencies in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes (SFAS 109) and FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). See Note 13 Income Taxes , for additional detail.

Tax Years 2000 to 2004

During 2007, the IRS and the Company reached agreement on substantially all of the issues raised with respect to the examination of taxable years 2000 to 2004. The Company submitted a protest to the Appeals Division of the IRS with respect to the remaining unresolved issues. The Company believes the amount of the estimated tax liability if the IRS were to prevail is fully reserved. The Company cannot predict the timing or ultimate outcome of a final resolution of the remaining unresolved issues.

Tax Years Prior to 2000

The previous examination cycle included the consolidated income tax groups for the audit periods identified below:

Coltec Industries Inc. and Subsidiaries	December, 1997 July, 1999 (through date of acquisition)
Goodrich Corporation and Subsidiaries	1998 1999 (including Rohr and Coltec)

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The IRS and the Company previously reached final settlement on all but one of the issues raised in this examination cycle. The Company received statutory notices of deficiency dated June 14, 2007 related to the remaining unresolved issue which involves the proper timing of certain deductions. The Company filed a petition with the U.S. Tax Court in September 2007 to contest the notices of deficiency. The Company believes the amount of the estimated tax liability if the IRS were to prevail is fully reserved. The Company cannot predict the timing or ultimate outcome of this matter.

Rohr has been under examination by the State of California for the tax years ended July 31, 1985, 1986 and 1987. The State of California has disallowed certain expenses incurred by one of Rohr s subsidiaries in connection with the lease of certain tangible property. California s Franchise Tax Board held that the deductions associated with the leased equipment were non-business deductions. The additional tax associated with the Franchise Tax Board s position is $4.5 million. The amount of accrued interest associated with the additional tax is approximately $27 million at September 30, 2008. In addition, the State of California enacted an amnesty provision that imposes nondeductible penalty interest equal to 50% of the unpaid interest amounts relating to taxable years ended before 2003. The penalty interest is approximately $13.5 million at September 30, 2008. The tax and interest amounts continue to be contested by Rohr. The Company believes that it is adequately reserved for this contingency. No payment has been made for the $27 million of interest or $13.5 million of penalty interest. The Franchise Tax Board took the position that under California law, Rohr was required to pay the full amount of interest prior to filing any suit for refund. In April 2008, the Supreme Court of California denied the Franchise Tax Board s final appeal on this procedural matter and Rohr can proceed with its refund suit.

Note 15. Guarantees

The Company extends financial and product performance guarantees to third parties. At September 30, 2008, the following environmental remediation and other indemnifications and financial guarantees were outstanding, in millions:

	Maximum Potential Payment	Carrying Amount of Liability
Environmental remediation and other indemnifications (Note 14)	No limit	$19.5
Guarantees of residual value on leases (Note 10)	$24.8	$

Service and Product Warranties

The Company provides service and warranty policies on certain of its products. The Company accrues liabilities under service and warranty policies based upon specific claims and a review of historical warranty and service claim experience in accordance with Statement of Financial Accounting Standards No. 5, Accounting for Contingencies . Adjustments are made to accruals as claim data and historical experience change. In addition, the Company incurs discretionary costs to service its products in connection with product performance issues.

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The changes in the carrying amount of service and product warranties for the nine months ended September 30, 2008, in millions, are as follows:

Balance at December 31, 2007	$ 164.3
Net provisions for warranties issued during the period	38.7
Net provisions for warranties existing at the beginning of the year	1.1
Payments	(41.3)
Foreign currency translation	(6.3)
Balance at September 30, 2008	$ 156.5

The current and long-term portions of service and product warranties were as follows:

	September 30, 2008	December 31, 2007
	(Dollars in millions)	
Accrued expenses	$ 68.9	$ 66.3
Other non-current liabilities	87.6	98.0
Total	$ 156.5	$ 164.3

Note 16. Derivatives and Hedging Activities

The Company utilizes certain financial instruments to manage risk, including foreign currency and interest rate exposures that exist as part of its ongoing business operations. A detailed description of the Company s use of derivative instruments is included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007.

Cash Flow Hedges

At September 30, 2008, the notional value of the forward contracts accounted for as cash flow hedges was $1,648.4 million and the amount of accumulated other comprehensive income that would be reclassified into earnings as an increase in sales to offset the effect of the hedged item in the next 12 months was a gain of $7 million. These forward contracts mature on a monthly basis with maturity dates that range from October 2008 to December 2012. At September 30, 2008, the total fair value of the Company s forward contracts was a liability of $7.4 million (before deferred taxes of $2.3 million), combined with $0.9 million of gains from forward contracts terminated prior to the original maturity dates, was recorded in accumulated other comprehensive income.

Fair Value Hedges

The notional amount of the outstanding interest rate swaps accounted for as fair value hedges at September 30, 2008 was $100 million with maturity dates ranging from December 2012 to July 2016. The fair value of the interest rate swaps was a net asset of $3.6 million at September 30, 2008.

Other Forward Contracts