Item 8. ***Financial Statements and Supplementary Data.***

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

We, the management team of Rockwell Collins, are responsible for the preparation, integrity and objectivity of the financial statements and other financial information we have presented in this report. The financial statements were prepared in accordance with accounting principles generally accepted in the United States of America, applying our estimates and judgments.

Deloitte & Touche LLP, our independent registered public accounting firm, is retained to audit our financial statements. Their accompanying report is based on audits conducted in accordance with standards of the Public Company Accounting Oversight Board (United States), which include the consideration of our internal controls to determine the nature, timing and extent of audit tests to be applied.

Our Board of Directors exercises its responsibility for these financial statements through its Audit Committee, which consists entirely of independent, non-management Board members. The Audit Committee meets regularly with the independent registered public accounting firm and with the Company's internal auditors, both privately and with management present, to review accounting, auditing, internal control and financial reporting matters.

/s/ CLAYTON M. JONES	/s/ PATRICK E. ALLEN
Clayton M. Jones Chairman, President & Chief Executive Officer	Patrick E. Allen Senior Vice President & Chief Financial Officer

MANAGEMENT'S REPORT ON
INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934. Rockwell Collins' internal control over financial reporting is a process designed, under the supervision of the Chief Executive Officer and Chief Financial Officer, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Our internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of Rockwell Collins; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with accounting principles generally accepted in the United States of America, and that our receipts and expenditures are being made only in accordance with authorizations of Rockwell Collins' management and directors; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of Rockwell Collins' internal control over financial reporting as of October 3, 2008. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control-Integrated Framework*. Based on this assessment, management determined that Rockwell Collins, Inc. maintained effective internal control over financial reporting as of October 3, 2008.

Rockwell Collins' internal control over financial reporting as of October 3, 2008 has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report which is included herein.

/s/ Clayton M. Jones	/s/ Patrick E. Allen
Clayton M. Jones Chairman, President & Chief Executive Officer	Patrick E. Allen Senior Vice President & Chief Financial Officer

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareowners of
Rockwell Collins, Inc.

We have audited the internal control over financial reporting of Rockwell Collins, Inc. and subsidiaries (the "Company") as of October 3, 2008, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of October 3, 2008, based on the criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended October 3, 2008 of the Company and our report dated November 3, 2008, except for Note 24, as to which the date is November 25, 2008, expressed an unqualified opinion on those financial statements.

/s/ DELOITTE & TOUCHE LLP

Minneapolis, Minnesota
November 3, 2008, except for Note 24, as to which the date is November 25, 2008

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareowners of
Rockwell Collins, Inc.

We have audited the accompanying consolidated statements of financial position of Rockwell Collins, Inc. and subsidiaries (the "Company") as of October 3, 2008 and September 28, 2007, and the related consolidated statements of operations, cash flows, and shareowners' equity and comprehensive income for each of the three years in the period ended October 3, 2008. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as of October 3, 2008 and September 28, 2007, and the consolidated results of its operations and its cash flows for each of the three years in the period ended October 3, 2008, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 11 to the consolidated financial statements, as of the beginning of fiscal 2007 the Company changed its measurement date for its defined benefit plans and as of September 28, 2007 the Company changed its method of accounting for the funded status of its defined benefit plans.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of October 3, 2008, based on the criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated November 3, 2008, except for Note 24, as to which the date is November 25, 2008, expressed an unqualified opinion on the Company's internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

Minneapolis, Minnesota
November 3, 2008, except for Note 24, as to which the date is November 25, 2008

ROCKWELL COLLINS, INC.
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
(in millions, except per share amounts)

	September 30 2008	September 30 2007
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 175	$ 231
Receivables	950	883
Inventories	970	823
Current deferred income taxes	139	176
Other current assets	104	56
Total current assets	2,338	2,169
Property	680	607
Intangible Assets	198	147
Goodwill	609	544
Prepaid Pension Asset	—	88
Other Assets	319	195
TOTAL ASSETS	$ 4,144	$3,750
LIABILITIES AND SHAREOWNERS' EQUITY		
Current Liabilities:		
Short-term debt	$ 287	$ —
Accounts payable	419	395
Compensation and benefits	295	305
Advance payments from customers	308	304
Product warranty costs	226	213
Income taxes payable	2	29
Other current liabilities	203	213
Total current liabilities	1,740	1,459
Long-Term Debt	228	223
Retirement Benefits	600	359
Other Liabilities	168	136
Shareowners' Equity:		
Common stock ($0.01 par value; shares authorized: 1,000; shares issued: 183.8)	2	2
Additional paid-in capital	1,378	1,353
Retained earnings	2,058	1,533
Accumulated other comprehensive loss	(578)	(336)
Common stock in treasury, at cost (shares held: 2008, 25.2; 2007, 18.0)	(1,452)	(979)
Total shareowners' equity	1,408	1,573
TOTAL LIABILITIES AND SHAREOWNERS' EQUITY	$ 4,144	$3,750

See Notes to Consolidated Financial Statements.

ROCKWELL COLLINS, INC.
CONSOLIDATED STATEMENT OF OPERATIONS
(in millions, except per share amounts)

	Year Ended September 30		
	2008	2007	2006
Sales:			
Product sales	$4,337	$4,007	$3,482
Service sales	432	408	381
Total sales	4,769	4,415	3,863
Costs, expenses and other:			
Product cost of sales	3,041	2,819	2,491
Service cost of sales	293	273	261
Selling, general and administrative expenses	485	482	441
Interest expense	21	13	13
Other income, net	(24)	(15)	(32)
Total costs, expenses and other	3,816	3,572	3,174
Income before income taxes	953	843	689
Income tax provision	275	258	212
Net income	$ 678	$ 585	$ 477
Earnings per share:			
Basic	$ 4.22	$ 3.50	$ 2.77
Diluted	$ 4.16	$ 3.45	$ 2.73
Weighted average common shares:			
Basic	160.8	167.1	172.0
Diluted	162.9	169.7	174.5
Cash dividends per share	$ 0.80	$ 0.64	$ 0.56

See Notes to Consolidated Financial Statements.

ROCKWELL COLLINS, INC.
CONSOLIDATED STATEMENT OF CASH FLOWS
(in millions)

	Year Ended September 30		
	2008	2007	2006
Operating Activities:			
Net income	$ 678	$ 585	$ 477
Adjustments to arrive at cash provided by operating activities:			
Gain on sale of equity affiliate	—	—	(20)
Restructuring charge (adjustment)	—	(5)	14
Depreciation	106	96	85
Amortization of intangible assets	23	22	21
Stock-based compensation	19	17	18
Compensation and benefits paid in common stock	65	58	50
Tax benefit from exercise of stock options	8	34	28
Excess tax benefit from stock-based compensation	(8)	(33)	(28)
Deferred income taxes	73	43	33
Pension plan contributions	(14)	(90)	(66)
Changes in assets and liabilities, excluding effects of acquisitions and foreign currency adjustments:			
Receivables	(68)	(126)	(78)
Inventories	(176)	(128)	(43)
Accounts payable	26	55	35
Advance payments from customers	4	61	24
Compensation and benefits	(10)	41	(16)
Income taxes	(67)	(23)	(12)
Other assets and liabilities	(39)	—	73
Cash Provided by Operating Activities	620	607	595
Investing Activities:			
Property additions	(171)	(125)	(144)
Acquisition of businesses, net of cash acquired	(105)	(32)	(100)
Acquisition of intangible assets	(8)	(8)	—
Proceeds from settlement of discontinued license agreement	—	14	—
Sale of investment in equity affiliate, net	(1)	(2)	84
Proceeds from disposition of property	1	—	1
Cash Used for Investing Activities	(284)	(153)	(159)
Financing Activities:			
Purchases of treasury stock	(576)	(333)	(492)
Cash dividends	(129)	(107)	(96)
Increase in short-term borrowings	287	—	—
Decrease in long-term borrowings	—	(27)	—
Proceeds from exercise of stock options	17	61	73
Net proceeds from issuance of long-term debt	—	—	46
Excess tax benefit from stock-based compensation	8	33	28
Cash Used for Financing Activities	(393)	(373)	(441)
Effect of exchange rate changes on cash and cash equivalents	1	6	4
Net Change in Cash and Cash Equivalents	(56)	87	(1)
Cash and Cash Equivalents at Beginning of Year	231	144	145
Cash and Cash Equivalents at End of Year	$ 175	$ 231	$ 144

See Notes to Consolidated Financial Statements.

ROCKWELL COLLINS, INC.
CONSOLIDATED STATEMENT OF SHAREOWNERS' EQUITY
AND COMPREHENSIVE INCOME
(in millions)

	Year Ended September 30		
	2008	2007	2006
Common Stock			
Beginning and ending balance	$ 2	$ 2	$ 2
Additional Paid-In Capital			
Beginning balance	1,353	1,305	1,263
Tax benefit from exercise of stock options	8	33	28
Stock-based compensation	19	17	18
Other	(2)	(2)	(4)
Ending balance	1,378	1,353	1,305
Retained Earnings			
Beginning balance	1,533	1,105	771
Net income	678	585	477
Cash dividends	(129)	(107)	(96)
Shares issued under stock option and benefit plans	(19)	(45)	(47)
Defined benefit plans remeasurement adjustment	—	(5)	—
Change in accounting for tax contingencies	(5)	—	—
Ending balance	2,058	1,533	1,105
Accumulated Other Comprehensive Income (Loss)			
Beginning balance	(336)	(393)	(604)
Minimum pension liability adjustment	—	369	199
Defined benefit retirement plan recognition adjustment	—	(329)	—
Pension and other retirement benefit adjustment	(229)	—	—
Currency translation gain (loss)	(15)	19	11
Foreign currency cash flow hedge adjustment	2	(2)	1
Ending balance	(578)	(336)	(393)
Common Stock in Treasury			
Beginning balance	(979)	(813)	(493)
Share repurchases	(576)	(333)	(492)
Shares issued from treasury	103	167	172
Ending balance	(1,452)	(979)	(813)
Total Shareowners' Equity	$ 1,408	$1,573	$1,206
Comprehensive Income			
Net income	$ 678	$ 585	$ 477
Other comprehensive income (loss), net of deferred tax assets (liabilities) (2008, $132; 2007, $(216); 2006, $(117))	(242)	386	211
Comprehensive income	$ 436	$ 971	$ 688

See Notes to Consolidated Financial Statements

1. Business Description and Basis of Presentation

Rockwell Collins, Inc. (the Company or Rockwell Collins) designs, produces and supports communications and aviation electronics for commercial and military customers worldwide.

The Company operates on a 52/53 week fiscal year ending on the Friday closest to September 30. The Company's fiscal year 2008 was a 53 week year ending on October 3, 2008, while 2007 and 2006 were 52 week fiscal years. For ease of presentation, September 30 is utilized consistently throughout these financial statements and notes to represent the fiscal year end date. All date references contained herein relate to the Company's fiscal year unless otherwise stated.

2. Significant Accounting Policies

Consolidation

The consolidated financial statements include the accounts of the Company and all majority-owned subsidiaries. The Company's investments in entities it does not control but over which it has the ability to exercise significant influence are accounted for under the equity method and are included in Other Assets. All intercompany transactions are eliminated.

Revenue Recognition

The Company enters into sales arrangements that may provide for multiple deliverables to a customer. The Company identifies all goods and/or services that are to be delivered separately under a sales arrangement and allocates revenue to each deliverable based on relative fair values. Fair values are generally established based on the prices charged when sold separately by the Company. In general, revenues are separated between hardware, engineering services, maintenance services, and installation services. The allocated revenue for each deliverable is then recognized using appropriate revenue recognition methods.

Sales related to long-term contracts requiring development and delivery of products over several years are accounted for under the percentage-of-completion method of accounting under the American Institute of Certified Public Accountants' Statement of Position 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*. Sales and earnings under these contracts are recorded either as products are shipped under the units-of-delivery method (for production effort), or based on the ratio of actual costs incurred to total estimated costs expected to be incurred related to the contract under the cost-to-cost method (for development effort). Purchase options and change orders are accounted for either as an integral part of the original contract or separately depending upon the nature and value of the item. Sales and costs related to profitable purchase options are included in estimates only when the options are exercised while sales and costs related to unprofitable purchase options are included in estimates when exercise is determined to be probable. Sales related to change orders are included in estimates only if they can be reliably estimated and collectability is reasonably assured. Anticipated losses on contracts are recognized in full in the period in which losses become probable and estimable. Changes in estimates of profit or loss on contracts are included in earnings on a cumulative basis in the period the estimate is changed.

Sales related to long-term separately priced product maintenance or warranty contracts are accounted for based on the terms of the underlying agreements. Certain contracts are fixed price contracts with sales recognized ratably over the contractual life, while other contracts have a fixed hourly rate with sales recognized based on actual labor or flight hours incurred. The cost of providing these services is expensed as incurred.

The Company recognizes sales for all other products or services when all of the following criteria are met: an agreement of sale exists, product delivery and acceptance has occurred or services have been rendered, pricing is fixed or determinable, and collection is reasonably assured.

Research and Development

The Company performs research and development activities relating to the development of new products and the improvement of existing products. Company-funded research and development programs are expensed as incurred and included in Cost of Sales. Customer-funded research and development expenditures are accounted for as contract costs within Cost of Sales, and the reimbursement is accounted for as a sale.

Cash and Cash Equivalents

Cash and cash equivalents includes time deposits and certificates of deposit with original maturity dates of three months or less.

Allowance for Doubtful Accounts

Allowances are established in order to report receivables at net realizable value on the Company's Statement of Financial Position. The determination of these allowances requires management of the Company to make estimates and judgments as to the collectability of customer account balances. These allowances are estimated for customers who are considered credit risks by reviewing the Company's collection experience with those customers as well as evaluating the customers' financial condition. The Company also considers both current and projected economic and market conditions. Special attention is given to accounts with invoices that are past due. Past due is defined as any invoice for which payment has not been received by the due date specified on the billing invoice. The uncollectible portion of receivables is charged against the allowance for doubtful accounts when collection efforts have ceased. Recoveries of receivables previously charged-off are recorded when received.

Inventories

Inventories are stated at the lower of cost or market using costs which approximate the first-in, first-out method, less related progress payments received. Inventoried costs include direct costs of manufacturing, certain engineering costs and allocable overhead costs. The Company regularly compares inventory quantities on hand on a part level basis to estimated forecasts of product demand and production requirements as well as historical usage. Based on these comparisons, management establishes an excess and obsolete inventory reserve on an aggregate basis. Inventory valuation reserves were $105 million and $99 million at September 30, 2008 and 2007, respectively.

The Company defers certain pre-production engineering costs as work-in-process inventory in connection with long-term supply arrangements that contain contractual guarantees for reimbursement from customers. Such customer guarantees generally take the form of a minimum order quantity with quantified reimbursement amounts if the minimum order quantity is not taken by the customer. Such costs are typically deferred to the extent of the contractual guarantees and are generally amortized over a period of 1 to 8 years as a component of Cost of Sales as revenue is recognized on the minimum order quantity. Deferred pre-production engineering costs were $166 million and $126 million at September 30, 2008 and 2007, respectively. Pre-production engineering costs incurred pursuant to supply arrangements that do not contain customer guarantees for reimbursement are expensed as incurred.

Progress Payments

Progress payments relate to both receivables and inventories and represent cash collected from government-related contracts whereby the governments have a legal right of offset related to the receivable or legal title to the work-in-process inventory.

Property

Property is stated at acquisition cost. Depreciation of property is generally provided using accelerated and straight-line methods over the following estimated useful lives: buildings and improvements, 15-40 years; machinery and equipment, 6-12 years; information systems software and hardware, 3-10 years; and furniture and fixtures 5-12 years. Depreciation methods and lives are reviewed periodically with any changes recorded on a prospective basis.

Significant renewals and betterments are capitalized and replaced units are written off. Maintenance and repairs, as well as renewals of minor amounts, are charged to expense in the period incurred. The fair value of liabilities associated with the retirement of property is recorded when there is a legal or contractual requirement to incur such costs and the costs are reasonably estimable. Upon the initial recognition of a contractual or legal liability for an asset retirement obligation, the Company capitalizes the asset retirement cost by increasing the carrying amount of the property by the same amount as the liability. This asset retirement cost is then depreciated over the estimated useful life of the underlying property. The Company had no significant asset retirement obligations at September 30, 2008 and 2007.

Goodwill and Intangible Assets

Goodwill and intangible assets generally result from business acquisitions. Business acquisitions are accounted for under the purchase method by assigning the purchase price to tangible and intangible assets acquired and liabilities assumed, including research and development projects which have not yet reached technological feasibility and have no alternative future use (purchased research and development). Assets acquired and liabilities assumed are recorded at their fair values; the fair value of purchased research and development is immediately charged to expense; and the excess of the purchase price over the amounts assigned is recorded as goodwill. Assets acquired and liabilities assumed are allocated to the Company's reporting units based on the Company's integration plans and internal reporting structure. Purchased intangible assets with finite lives are amortized over their estimated useful lives. Goodwill and intangible assets with indefinite lives are not amortized, but reviewed at least annually for impairment.

Customer Incentives

Rockwell Collins provides sales incentives to certain commercial customers in connection with sales contracts. Incentives consisting of cash payments or customer account credits are recognized as a reduction of sales and incentives consisting of free product are recognized as cost of sales.

Incentives granted to customers prior to delivering products or performing services are recorded as a customer relationship intangible asset and amortized over the period the Company has received a contractually enforceable right related to the incentive. The net book value of incentives included in Intangible Assets were $56 million and $36 million at September 30, 2008 and 2007, respectively.

Incentives earned by customers based on purchases of Company products or services are recognized as a liability when the related sale is recorded. The liability for these incentives is included in Other Current Liabilities.

Impairment of Long-Lived Assets

Long-lived assets are reviewed for impairment when management plans to dispose of assets or when events or circumstances indicate that the carrying amount of a long-lived asset may not be recoverable. Assets held for disposal are reported at the lower of the carrying amount or fair value less cost to sell. Management determines fair value using a discounted future cash flow analysis or other accepted valuation techniques. Long-lived assets held for use are reviewed for impairment by comparing the carrying amount of an asset to the undiscounted future cash flows expected to be generated by the asset over its remaining useful life. If an asset is considered to be impaired, the impairment to be recognized is measured as the amount by which the carrying amount of the asset exceeds its fair value.

Goodwill and indefinite-lived intangible assets are tested annually for impairment with more frequent tests performed if indications of impairment exist. The Company's annual impairment testing date is in the second quarter of each fiscal year. Impairment for intangible assets with indefinite lives exists if the carrying value of the intangible asset exceeds its fair value. Goodwill is potentially impaired if the carrying value of a reporting unit exceeds its estimated fair value. Management determines fair value using a discounted future cash flow analysis or other accepted valuation techniques. The Company's annual impairment testing performed in the second quarter of 2008, 2007, and 2006 yielded no impairments.

Advance Payments from Customers

Advance payments from customers represent cash collected from customers in advance of revenue recognition.

Environmental

Liabilities for environmental matters are recorded in the period in which it is probable that an obligation has been incurred and the cost can be reasonably estimated. At environmental sites in which more than one potentially responsible party has been identified, the Company records a liability for its estimated allocable share of costs related to its involvement with the site as well as an estimated allocable share of costs related to the involvement of insolvent or unidentified parties. At environmental sites in which the Company is the only responsible party, the Company records a liability for the total estimated costs of remediation. Costs of future expenditures for environmental remediation obligations do not consider inflation and are not discounted to present values. If recovery from insurers or other third parties is determined to be probable, the Company records a receivable for the estimated recovery.

Income Taxes

Current tax liabilities and assets are based upon an estimate of taxes payable or refundable in the current year for each of the jurisdictions in which the Company transacts business. As part of the determination of its tax liability, management exercises considerable judgment in evaluating tax positions taken by the Company in determining the income tax provision under Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes* (SFAS 109) and establishes reserves for tax contingencies in accordance with FASB Interpretation No. 48, *Accounting for uncertainty in income* *taxes, an interpretation of SFAS 109* (FIN 48). Deferred tax assets and liabilities are recorded for the estimated future tax effects attributable to temporary differences between the carrying amounts of assets and liabilities used for financial reporting purposes and their respective carrying amounts for income tax purposes. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Derivative Financial Instruments

The Company uses derivative financial instruments in the form of foreign currency forward exchange contracts and interest rate swap contracts for the purpose of minimizing exposure to changes in foreign currency exchange rates on business transactions and interest rates, respectively. The Company's policy is to execute such instruments with banks the Company believes to be creditworthy and not to enter into derivative financial instruments for speculative purposes or to manage exposure for net investments in foreign subsidiaries. These derivative financial instruments do not subject the Company to undue risk as gains and losses on these instruments generally offset gains and losses on the underlying assets, liabilities, or anticipated transactions that are being hedged.

All derivative financial instruments are recorded at fair value in the Statement of Financial Position. For a derivative that has not been designated as an accounting hedge, the change in the fair value is recognized immediately through earnings. For a derivative that has been designated as an accounting hedge of an existing asset or liability (a fair value hedge), the change in the fair value of both the derivative and underlying asset or liability is recognized immediately through earnings. For a derivative designated as an accounting hedge of an anticipated transaction (a cash flow hedge), the change in the fair value is recorded on the Statement of Financial Position in Accumulated Other Comprehensive Loss to the extent the derivative is effective in mitigating the exposure related to the anticipated transaction. The change in the fair value related to the ineffective portion of the hedge, if any, is immediately recognized in earnings. The amount recorded within Accumulated Other Comprehensive Loss is reclassified in earnings in the same period during which the underlying hedged transaction affects earnings. The Company does not exclude any amounts from the measure of effectiveness for both fair value and cash flow hedges.

Use of Estimates

The financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America, which require management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates. Estimates are used in accounting for, among other items, long-term contracts, allowances for doubtful accounts, inventory obsolescence, product warranty cost liabilities, customer incentives, retirement benefits, income taxes, environmental matters, recoverability of long-lived assets and contingencies. Estimates and assumptions are reviewed periodically and the effects of changes, if any, are reflected in the Statement of Operations in the period that they are determined.

Concentration of Risks

The Company's products and services are concentrated within the aerospace and defense industries with customers consisting primarily of military and commercial aircraft manufacturers, commercial airlines, and the United States and international governments. As a result of this industry focus, the Company's current and future financial performance is largely dependent upon the overall economic conditions within these industries. In particular, the commercial aerospace market has been historically cyclical and subject to downturns during periods of weak economic conditions, which could be prompted by or exacerbated by political or other domestic or international events. The defense market may be affected by changes in budget appropriations, procurement policies, political developments both domestically and abroad, and other factors. While management believes the Company's product offerings are well positioned to meet the needs of its customer base, any material deterioration in the economic and environmental factors that impact the aerospace and defense industries could have a material adverse effect on the Company's results of operations, financial position or cash flows.

In addition to the overall business risks associated with the Company's concentration within the aerospace and defense industries, the Company is also exposed to a concentration of collection risk on credit extended to commercial airlines. At September 30, 2008, accounts receivable due from U.S. and international commercial airlines were approximately $20 million and $85 million, respectively. The Company performs ongoing credit evaluations on the financial condition of all of its commercial airline customers and maintains allowances for uncollectible accounts receivable based on expected collectability. Although management believes its allowances are adequate, the Company is not able to predict with certainty the changes in the financial stability of its customers. Any material change in the financial status of any one or group of customers could have a material adverse effect on the Company's results of operations, financial position or cash flows.

As of September 30, 2008, approximately 12 percent of the Company's employees were represented by collective bargaining agreements, which are generally set to expire between September 2010 and May 2013.

Recently Issued Accounting Standards

In May 2008, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 162, *The Hierarchy of Generally Accepted Accounting Principles* (GAAP) (SFAS 162). The purpose of the new standard is to provide a consistent framework for determining what accounting principles should be used when preparing U.S. GAAP financial statements. Previous guidance did not properly rank the accounting literature. The new standard is effective 60 days following the Securities and Exchange Commission's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles.* The adoption of SFAS 162 is not expected to have a material effect on the Company's financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133* (SFAS 161). SFAS 161 requires, among other things, enhanced disclosure about the volume and nature of derivative and hedging activities and a tabular summary showing the fair value of derivative instruments included in the statement of financial position and statement of operations. SFAS 161 also requires expanded disclosure of contingencies included in derivative instruments related to credit risk. SFAS 161 is effective for the Company in the second quarter of fiscal year 2009. The adoption of SFAS 161 is not expected to have a material effect on the Company's financial statements other than providing certain enhanced disclosures.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* (SFAS 141R). SFAS 141R significantly changes the way companies account for business combinations and will generally require more assets acquired and liabilities assumed to be measured at their acquisition-date fair value. Under SFAS 141R, legal fees and other transaction-related costs are expensed as incurred and are no longer included in goodwill as a cost of acquiring the business. SFAS 141R also requires, among other things, acquirers to estimate the acquisition-date fair value of any contingent consideration and to recognize any subsequent changes in the fair value of contingent consideration in earnings. In addition, restructuring costs the acquirer expects, but is not obligated to incur, will be recognized separately from the business acquisition. This accounting standard is applied prospectively and is effective for the Company at the beginning of fiscal year 2010. The adoption of SFAS 141R is not expected to materially effect the Company's financial position, results of operations, or cash flows on the date the standard becomes effective; however, it is expected to have a significant effect on business acquisitions the Company makes subsequent to September 30, 2009.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51* (SFAS 160). SFAS 160 requires all entities to report noncontrolling interests in subsidiaries as a separate component of equity in the consolidated financial statements. SFAS 160 establishes a single method of accounting for changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation. Companies will no longer recognize a gain or loss on partial disposals of a subsidiary where control is retained. In partial acquisitions where control is obtained, the acquiring company will recognize and measure at fair value 100 percent of the assets and liabilities, including goodwill, as if the entire target company had been acquired. SFAS 160 is effective for the Company at the beginning of fiscal year 2010. The adoption of SFAS 160 is not expected to have a material effect on the Company's financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits entities to choose to measure certain eligible financial assets and financial liabilities at fair value (the fair value option). SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. Unrealized gains and losses on items for which the fair value option is elected would be reported in earnings. SFAS 159 is effective for the Company's fiscal year 2009. The Company does not currently plan to elect the fair value option for its financial assets or financial liabilities.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements. SFAS 157 indicates that, among other things, a fair value measurement assumes that the transaction to sell an asset or transfer a liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. SFAS 157 is effective for the Company's fiscal year 2009, with the exception of certain non-financial assets and liabilities for which the effective date is the Company's fiscal year 2010. The Company does not currently anticipate the implementation of SFAS 157 will materially effect the Company's financial position, results of operations, or cash flows.

3. Acquisitions

During the years ended September 30, 2008, 2007 and 2006, the Company completed five acquisitions that are summarized as follows:

(dollars in millions)	Fiscal Year Acquired	Cash Purchase Price	Goodwill	Intangible Assets Finite Lived	Intangible Assets Weighted Average Life in Years
Athena Technologies, Inc	2008	$107	$67	$46	10
Information Technology & Applications Corporation	2007	37	26	12	7
Anzus, Inc.	2006	19	12	9	7
IP Unwired, Inc.	2006	10	7	3	8
E&S Simulation Business	2006	64	33	22	9

Athena Technologies, Inc.

On April 4, 2008, the Company acquired all of the shares of Athena Technologies, Inc. (Athena). Athena, located in Warrenton, Virginia, is a provider of navigation and control solutions, primarily to the Unmanned Aerial Vehicle market segment. The total cash purchase price, net of cash acquired, was $107 million. The Company is in the process of finalizing the pre-acquisition income tax return and its implications on the purchase price allocation. Based on the Company's preliminary allocation of the purchase price, $67 million has been allocated to goodwill and $46 million to finite-lived intangible assets with a weighted average life of approximately 10 years. The excess purchase price over net assets acquired reflects the Company's view that this acquisition will enhance the Company's navigation and control solution capabilities. None of the goodwill resulting from the acquisition is tax deductible. Goodwill is included within the assets of the Government Systems segment.

Information Technology & Applications Corporation

On August 10, 2007, the Company acquired all of the shares of Information Technology & Applications Corporation (ITAC). ITAC, located in Reston, Virginia, is a provider of intelligence, surveillance, reconnaissance and communications solutions to support the global war on terror and homeland security. The total cash purchase price, net of cash acquired, was $37 million. In the fourth quarter of fiscal year 2008, the purchase price allocation was finalized with $26 million allocated to goodwill and $12 million to finite-lived intangible assets with a weighted average life of approximately 7 years. The excess purchase price over net assets acquired reflects the Company's view that this acquisition will enhance the Company's communications intelligence capabilities. None of the goodwill resulting from the acquisition is tax deductible. Goodwill is included within the assets of the Government Systems segment.

Anzus, Inc.

On September 25, 2006, the Company acquired all of the shares of Anzus, Inc. (Anzus). Anzus, located in Poway, California, is a developer of software that enables high-speed tactical data link processing and sensor correlation for the U.S. Department of Defense as well as international governments. The total cash purchase price, net of cash acquired, was $19 million. In the fourth quarter of fiscal year 2007, the purchase price allocation was finalized with $12 million of the purchase price allocated to goodwill and $9 million to finite-lived intangible assets with a weighted average life of approximately

7 years. The excess purchase price over net assets acquired reflects the Company's view that this acquisition will enhance the Company's tactical data link integration solutions. None of the goodwill resulting from the acquisition is tax deductible. Goodwill is included within the assets of the Government Systems segment.

IP Unwired, Inc.

On September 5, 2006, the Company acquired all of the shares of IP Unwired, Inc. (IP Unwired). IP Unwired, located in Ottawa, Canada, is a provider of advanced digital communications and networking technology for U.S. and international military customers. The total cash purchase price, net of cash acquired, was $10 million. In the fourth quarter of fiscal year 2007, the purchase price allocation was finalized with $7 million of the purchase price allocated to goodwill and $3 million to finite-lived intangible assets with a weighted average life of approximately 8 years. The excess purchase price over net assets acquired reflects the Company's view that this acquisition will strengthen the Company's network-centric operational capabilities. All goodwill resulting from the acquisition is tax deductible. Goodwill is included within the assets of the Government Systems segment.

E&S Simulation Business

On May 26, 2006, the Company acquired Evans & Sutherland Computer Corporation's (E&S) military and commercial simulation assets and certain liabilities, including operations in the United States and United Kingdom (the E&S Simulation Business). The E&S Simulation Business produces hardware and software to create visual images for simulation, training, engineering, and other applications throughout the world. The total cash purchase price was approximately $64 million, which is net of a $5 million post-closing purchase price adjustment received by the Company in 2007 and a $2 million adjustment received in 2008. During the third quarter of fiscal year 2007, the purchase price and purchase price allocation were finalized with $33 million of the purchase price allocated to goodwill and $22 million to finite-lived intangible assets with a weighted average life of approximately 9 years. The excess purchase price over net assets acquired reflects the Company's view that this acquisition will further enhance the Company's simulation and training capabilities and provide more robust solutions for the Company's customers. All goodwill resulting from the acquisition is tax deductible. $22 million of goodwill was included in the Government Systems segment and $11 million of goodwill was included in the Commercial Systems segment.

The results of operations for each of these acquired businesses are included in the Statement of Operations since their respective dates of acquisition. Pro forma financial information is not presented as the effect of these acquisitions is not material to the Company's results of operations.

4. Receivables

Receivables are summarized as follows:

(in millions)	September 30 2008	2007
Billed	$726	$715
Unbilled	254	207
Less progress payments	(21)	(30)
Total	959	892
Less allowance for doubtful accounts	(9)	(9)
Receivables	$950	$883

The Company expects to collect all receivables outstanding as of September 30, 2008 within the next twelve months.

Unbilled receivables principally represent sales recorded under the percentage-of-completion method of accounting that have not been billed to customers in accordance with applicable contract terms.

5. Inventories

Inventories are summarized as follows:

(in millions)	September 30 2008	2007
Finished goods	$ 244	$187
Work in process	436	362
Raw materials, parts, and supplies	362	371
Total	1,042	920
Less progress payments	(72)	(97)
Inventories	$ 970	$823

In accordance with industry practice, inventories include amounts which are not expected to be realized within one year. These amounts primarily relate to life-time buy inventory and certain pre-production engineering costs not expected to be realized within one year of $227 million and $183 million at September 30, 2008 and 2007, respectively. Life-time buy inventory is inventory that is typically no longer being produced by the Company's vendors but for which multiple years of supply are purchased in order to meet production and service requirements over the life span of a product.

6. Property

Property is summarized as follows:

(in millions)	September 30 2008	2007
Land	$ 30	$ 31
Buildings and improvements	342	307
Machinery and equipment	807	769
Information systems software and hardware	243	224
Furniture and fixtures	60	52
Construction in progress	99	72
Total	1,581	1,455
Less accumulated depreciation	(901)	(848)
Property	$ 680	$ 607

In the current year, furniture and fixtures have been presented separately within Property. In prior years, such amounts had been presented within information systems software and hardware. Prior year amounts have been reclassified to conform to the current year presentation.

Property additions acquired by incurring accounts payable, which are reflected as a non-cash transaction in the Company's Consolidated Statement of Cash Flows, were $26 million, $29 million, and $14 million at September 30, 2008, 2007, and 2006, respectively.

7. Goodwill and Intangible Assets

Changes in the carrying amount of goodwill are summarized as follows:

(in millions)	Government Systems	Commercial Systems	Total
Balance at September 30, 2006	$323	$194	$517
ITAC acquisition	25	—	25
Foreign currency translation adjustment	6	—	6
Other adjustments to goodwill	(1)	(3)	(4)
Balance at September 30, 2007	353	191	544
Athena acquisition	67	—	67
Foreign currency translation adjustment	(3)	—	(3)
Other adjustments to goodwill	1	—	1
Balance at September 30, 2008	$418	$191	$609

Intangible assets are summarized as follows:

(in millions)	September 30, 2008 Gross	Accum Amort	Net	September 30, 2007 Gross	Accum Amort	Net
Intangible assets with finite lives:						
Developed technology and patents	$181	$ (87)	$ 94	$156	$ (72)	$ 84
License agreements	20	(4)	16	11	(3)	8
Customer relationships	105	(25)	80	67	(19)	48
Trademarks and tradenames	14	(8)	6	12	(7)	5
Intangible assets with indefinite lives:						
Trademarks and tradenames	2	—	2	2	—	2
Intangible assets	$322	$(124)	$198	$248	$(101)	$147

In December 2007, the Commercial Systems segment acquired a license agreement in connection with its purchase of the SKYLink broadband terminal product line from ARINC Incorporated (ARINC). Under the terms of the six-year agreement, the Company will sell and support broadband terminals to the business jet market under the Company's eXchange brand and ARINC will provide certain satellite connectivity services. The initial purchase price was $7 million, of which $6 million was paid during the year ended September 30, 2008, and is subject to adjustment based on future sales volume of the product line.

In prior years, the Company paid $14 million for a license fee related to a strategic agreement with The Boeing Company to provide a global broadband connectivity solution for business aircraft through the Company's Collins eXchange product. In August of 2006, The Boeing Company announced they would exit the high-speed broadband communications connectivity markets. During the year ended September 30, 2007, the Company and The Boeing Company reached a settlement that included, among other things, repayment of $14 million to the Company representing the carrying value of the license agreement.

Amortization expense for intangible assets for the years ended September 30, 2008, 2007 and 2006 was $23 million, $22 million, and $21 million, respectively. Annual amortization expense for intangible assets for 2009, 2010, 2011, 2012 and 2013 is expected to be $27 million, $35 million, $38 million, $34 million, and $16 million, respectively.

8. Other Assets

Other assets are summarized as follows:

(in millions)	September 30 2008	2007
Long-term deferred income taxes (Note 16)	$144	$ 1
Long-term receivables	71	73
Investments in equity affiliates	9	10
Exchange and rental assets, net of accumulated depreciation of $98 at September 30, 2008 and $95 at September 30, 2007	41	37
Other	54	74
Other assets	$319	$195

Investments in Equity Affiliates

Investments in equity affiliates primarily consist of four joint ventures: Vision Systems International, LLC (VSI), Data Link Solutions, LLC (DLS), Integrated Guidance Systems, LLC (IGS), and Quest Flight Training Limited (Quest). Each joint venture is 50 percent owned by the Company and accounted for under the equity method.

VSI is a joint venture with Elbit Systems, Ltd. for the joint pursuit of helmet mounted cueing systems for the worldwide military fixed wing aircraft market.

DLS is a joint venture with BAE Systems, plc for the joint pursuit of the worldwide military data link market.

IGS is a joint venture with Honeywell International Inc. for the joint pursuit of integrated precision guidance solutions for worldwide guided weapons systems.

Quest is a joint venture with Quadrant Group plc (Quadrant) that provides aircrew training services primarily for the United Kingdom Ministry of Defence. The 50 percent investment in Quest was acquired from Evans & Sutherland in May of 2006.

Rockwell Scientific Company, LLC (RSC) was a joint venture with Rockwell Automation, Inc. (Rockwell Automation) that was engaged in advanced research and development of technologies in electronics, imaging and optics, material and computational sciences and information technology. On September 15, 2006, the Company and Rockwell Automation sold RSC to Teledyne Brown Engineering, Inc. for $168 million in cash, of which the Company received approximately $84 million (50 percent), excluding expenses and certain retained liabilities. In the fourth quarter of 2006, the Company recorded a pre-tax gain of $20 million ($13 million after taxes, or 7 cents per share) related to the sale of RSC. This 2006 pre-tax gain was recorded in Other Income, Net.

Under the equity method of accounting for investments, the Company's proportionate share of the earnings or losses of its equity affiliates are included in Net Income and classified as Other Income, Net in the Statement of Operations. For segment performance reporting purposes, Rockwell Collins' share of earnings or losses of VSI, DLS, IGS, and Quest are included in the operating results of the Government Systems segment. RSC was considered a corporate-level investment prior to its sale in 2006.

In the normal course of business or pursuant to the underlying joint venture agreements, the Company may sell products or services to equity affiliates. The Company defers a portion of the profit generated from these sales equal to its ownership interest in the equity affiliates until the underlying product is ultimately sold to an unrelated third party. Sales to equity affiliates were $120 million, $128 million, and $139 million for the years ended September 30, 2008, 2007, and 2006, respectively. The deferred portion of profit generated from sales to equity affiliates was $4 million and $6 million at September 30, 2008 and 2007, respectively.

Exchange and Rental Assets

Exchange and rental assets consist of Company products that are either loaned or rented to customers on a short-term basis in connection with warranty and other service related activities or under operating leases. These assets are recorded at acquisition or production cost and depreciated using the straight-line method over their estimated lives which range from 3-11 years. Depreciation methods and lives are reviewed periodically with any changes recorded on a prospective basis.

9. Other Current Liabilities

Other current liabilities are summarized as follows:

	September 30	
(in millions)	2008	2007
Customer incentives	$119	$117
Contract reserves	13	18
Other	71	78
Other current liabilities	$203	$213

10. Debt

Short-term Debt

Under the Company's commercial paper program, the Company may sell up to $850 million face amount of unsecured short-term promissory notes in the commercial paper market. The commercial paper notes may bear interest or may be sold at a discount, and will have a maturity of not more than 364 days from the time of issuance. At September 30, 2008, short-term commercial paper borrowings outstanding were $266 million with a weighted average interest rate and maturity period of 1.99 percent and 12 days, respectively.

Revolving Credit Facilities

The Company has an $850 million unsecured revolving credit facility with various banks that matures in March 2012. The credit facility has options to extend the term for up to two one-year periods and/or increase the aggregate principal amount up to $1.2 billion. These options are subject to the approval of lenders. This credit facility exists primarily to support the Company's commercial paper program, but may be used for other corporate purposes in the event access to the commercial paper market is impaired or eliminated. The credit facility includes one financial covenant requiring the Company to maintain a consolidated debt to total capitalization ratio of not greater than 60 percent. The ratio excludes the accumulated other comprehensive loss equity impact related to defined benefit retirement plans. The ratio was 21 percent as of September 30, 2008. In addition, the credit facility contains covenants that require the Company to satisfy certain conditions in order to incur debt secured by liens, engage in sale/leaseback transactions, or merge or consolidate with another entity. Borrowings under this credit facility bear interest at the London Interbank Offered Rate (LIBOR) plus a variable margin based on the Company's unsecured long-term debt rating or, at the Company's option, rates determined by competitive bid. At September 30, 2008 and 2007, there were no outstanding borrowings under this revolving credit facility.

In addition, short-term credit facilities available to foreign subsidiaries amounted to $60 million as of September 30, 2008, of which $23 million was utilized to support commitments in the form of commercial letters of credit. At September 30, 2008 and 2007, there were no significant commitment fees or compensating balance requirements under any of the Company's credit facilities. As of September 30, 2008, there were $21 million of short-term borrowings outstanding under the Company's foreign subsidiaries' credit facilities.

Long-Term Debt

In June 2006, the Company entered into a five-year unsecured variable rate loan facility agreement for 20.4 million euros ($25 million). The interest rate is variable at the Euro Interbank Offered Rate plus 35 basis points and interest is payable quarterly. The outstanding balance of this loan facility was $24 million at September 30, 2008 and 2007. The interest rate was 5.31 percent and 5.08 percent at September 30, 2008 and 2007, respectively. The variable rate loan facility contains customary loan covenants, none of which are financial covenants. Failure to comply with customary covenants or the occurrence of customary events of default contained in the agreement would require the repayment of any outstanding borrowings under the agreement.

In June 2006, the Company entered into a five-year unsecured variable rate loan facility agreement for 11.5 million British pounds ($21 million). This loan facility was repaid in 2007.

In addition, the Company has a shelf registration statement filed with the Securities and Exchange Commission, which expires on November 30, 2008, covering up to $750 million in debt securities, common stock, preferred stock or warrants that may be offered in one or more offerings on terms to be determined at the time of sale. On November 20, 2003, the Company issued $200 million of 4.75 percent fixed rate unsecured debt under the shelf registration due December 1, 2013 (the Notes). Interest payments on the Notes are due on June 1 and December 1 of each year. The Notes contain certain covenants and events of default, including requirements that the Company satisfy certain conditions in order to incur debt secured by liens, engage in sale/leaseback transactions, or merge or consolidate with another entity. In 2004, the Company entered into interest rate swap contracts which effectively converted $100 million aggregate principal amount of the Notes to floating rate debt based on six-month LIBOR less 7.5 basis points. See Note 17 for additional information relating to the interest rate swap contracts. At September 30, 2008, $550 million of the shelf registration statement was available for future use.

Long-term debt and a reconciliation to the carrying amount is summarized as follows:

	September 30	
(in millions)	2008	2007
Principal amount of Notes due December 1, 2013	$200	$200
Principal amount of variable rate loan facility due June 2011	24	24
Fair value swap adjustment (Note 17)	4	(1)
Long-term debt	$228	$223

The Company was in compliance with all debt covenants at September 30, 2008 and 2007.

Interest paid on debt for the years ended September 30, 2008, 2007, and 2006 was $20 million, $13 million, and $11 million, respectively.

11. Retirement Benefits

The Company sponsors defined benefit pension (Pension Benefits) and other postretirement (Other Retirement Benefits) plans covering most of its U.S. employees and certain employees in foreign countries which provide monthly pension and other benefits to eligible employees upon retirement.

SFAS 158 Adoption

During the first quarter of 2007, the Company changed its measurement date from June 30 to September 30 for all of the Company's defined benefit retirement plans. In accordance with the measurement date transition provisions of SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)* (SFAS 158), the Company remeasured benefit obligations and plan assets as of the beginning of fiscal year 2007. As a result of this remeasurement, retirement benefit liabilities increased $141 million and Accumulated Other Comprehensive Loss increased $47 million, primarily due to a decline in the discount rate for Pension Benefits from 6.5 percent to 6.1 percent. The Company also recorded a charge to Retained Earnings in fiscal year 2007 of $5 million, after tax, which was the net benefit cost for the period from July 1, 2006 to September 30, 2006.

Effective September 30, 2007, the Company adopted the recognition provisions of SFAS 158 and recognized the funded status of the Company's defined benefit retirement plans on the Statement of Financial Position. At September 30, 2007, the previously unrecognized differences between actual amounts and estimates based on actuarial assumptions were included in Accumulated Other Comprehensive Loss in the Statement of Financial Position as required by SFAS 158. The Company has recognized the aggregate of all overfunded plans as a Prepaid Pension Asset and the aggregate of all underfunded plans as a Retirement Benefit Liability. The current portion of the liability is the amount by which the actuarial present value of benefits included in the benefit obligation payable in the next 12 months exceeds the fair value of plan assets and is reflected in Compensation and Benefits in the Statement of Financial Position.

Other Comprehensive Loss

The following table summarizes the amounts included in Accumulated Other Comprehensive Loss before tax related to retirement benefits as of September 30, 2008 and 2007 and changes recognized in Other Comprehensive Loss before tax for the year ended September 30, 2008:

(in millions)	Pension Benefits	Other Retirement Benefits	Total
September 30, 2007	$501	$ 70	$571
Current year prior service cost	3	9	12
Current year net actuarial (gain) / loss	404	(43)	361
Amortization of prior service cost	19	33	52
Amortization of actuarial loss	(46)	(14)	(60)
Foreign currency translation	(3)	—	(3)
September 30, 2008	$878	$ 55	$933

Components of Expense / (Income)

The components of expense / (income) for Pension Benefits and Other Retirement Benefits are summarized below:

	Pension Benefits			Other Retirement Benefits		
(in millions)	2008	2007	2006	2008	2007	2006
Service cost	$ 8	$ 8	$ 50	$ 4	$ 4	$ 4
Interest cost	163	151	140	14	15	15
Expected return on plan assets	(201)	(189)	(181)	(1)	(1)	(1)
Amortization:						
Prior service cost	(19)	(19)	(18)	(33)	(39)	(39)
Net actuarial loss	46	58	79	14	16	19
Net benefit expense (income)	$ (3)	$ 9	$ 70	$ (2)	$ (5)	$ (2)

Funded Status and Net Asset (Liability)

The following table reconciles the projected benefit obligations (PBO), plan assets, funded status, and net asset (liability) for the Company's Pension Benefits and the Other Retirement Benefits.

(in millions)	Pension Benefits 2008	Pension Benefits 2007	Other Retirement Benefits 2008	Other Retirement Benefits 2007
PBO at beginning of period	$2,554	$2,557	$ 238	$ 278
Service cost	8	8	4	4
Interest cost	163	151	14	15
Discount rate change	(284)	(164)	(17)	(10)
Actuarial losses (gains)	40	130	(28)	(5)
Plan amendments	3	—	9	(15)
Benefits paid	(150)	(140)	(24)	(29)
Other	(12)	12	4	—
PBO at end of period	2,322	2,554	200	238
Plan assets at beginning of period	2,490	2,207	15	15
Actual return on plan assets	(448)	328	(2)	2
Company contributions	14	90	19	27
Benefits paid	(150)	(140)	(24)	(29)
Other	(8)	5	4	—
Plan assets at end of period	1,898	2,490	12	15
Funded status of plans	$ (424)	$ (64)	$(188)	$(223)
Funded status consists of:				
Prepaid pension asset	$ —	$ 88	$ —	$ —
Retirement benefits liability	(415)	(143)	(180)	(213)
Compensation and benefits liability	(9)	(9)	(8)	(10)
Net liability	$ (424)	$ (64)	$(188)	$(223)

The Company's non-US defined benefit pension plans represented 5 percent of the total PBO at both September 30, 2008 and 2007. The accumulated benefit obligation for all defined benefit pension plans was $2,316 million and $2,547 million at September 30, 2008 and September 30, 2007, respectively.

The estimated amounts that will be amortized from Accumulated Other Comprehensive Loss into net defined benefit expense / (income) during the year ending September 30, 2009 are as follows:

(in millions)	Pension Benefits	Other Retirement Benefits	Total
Prior service cost	$(19)	$(22)	$(41)
Net actuarial loss	30	10	40
Total	$ 11	$(12)	$ (1)

Actuarial Assumptions

The following table presents the significant assumptions used in determining the benefit obligations.

	Pension Benefits				Other Retirement Benefits	
	US		Non-US		US	
	2008	2007	2008	2007	2008	2007
Discount rate	7.60%	6.60%	6.23%	5.50%	7.60%	6.50%
Compensation increase rate	—	—	4.10%	4.50%	—	—

Discount rates used to determine the benefit obligations are determined by using a weighted average of market-observed yields for high quality fixed income securities that correspond to the payment of benefits.

Significant assumptions used in determining the net benefit expense (income) are as follows:

	Pension Benefits				Other Retirement Benefits	
	US		Non-US		US	
	2008	2007	2008	2007	2008	2007
Discount rate	6.60%	6.10%	5.50%	5.00%	6.50%	6.00%
Expected long-term return on plan assets	8.75%	8.75%	8.75%	8.75%	8.75%	8.75%
Compensation increase rate	—	—	4.50%	4.50%	—	—
Pre-65 health care cost gross trend rate*	—	—	—	—	11.00%	11.00%
Post-65 health care cost gross trend rate*	—	—	—	—	11.00%	11.00%
Ultimate trend rate*	—	—	—	—	5.50%	5.50%
Year that trend reaches ultimate rate*	—	—	—	—	2013	2012

* Due to the effect of the fixed Company contribution, the net impact of any change in trend rate is not significant.

Expected long-term return on plan assets for each year presented is based on both historical long-term actual and expected future investment returns considering the current investment mix of plan assets. Actuarial gains and losses in excess of 10 percent of the greater of the projected benefit obligation or market-related value of assets are amortized on a straight-line basis over the average remaining service period of active participants. Prior service costs resulting from plan amendments are amortized in equal annual amounts over the average remaining service period of affected active participants or over the remaining life expectancy of affected retired participants. The Company uses a five-year, market-related value asset method of amortizing the difference between actual and expected returns on plan assets.

Pension Plan Benefits

The Company historically provided pension benefits to most of the Company's U.S. employees in the form of non-contributory, defined benefit plans that are considered qualified plans under applicable laws. The benefits provided under these plans for salaried employees are generally based on years of service and average compensation. The benefits provided under these plans for hourly employees are generally based on specified benefit amounts and years of service. In addition, the Company sponsors an unfunded non-qualified defined benefit plan for certain employees. The Company also maintains two pension plans in foreign countries, one of which is unfunded.

In June 2003, the Company's U.S. qualified and non-qualified defined benefit pension plans were amended to discontinue benefit accruals for salary increases and services rendered after September 30, 2006. These changes affect all of the Company's domestic pension plans for all salaried and hourly employees not covered by collective bargaining agreements. The Company supplemented its existing defined contribution savings plan effective October 1, 2006 to include additional Company contributions which were $37 million in 2008 and $28 million in 2007.

For the years ended September 30, 2008 and 2007, the Company made contributions to its pension plans as follows:

(in millions)	2008	2007
Discretionary contributions to U.S. qualified plan	$—	$75
Contributions to international plans	7	7
Contributions to U.S. non-qualified plan	7	8
Total	$14	$90

The Company's objective with respect to the funding of its pension plans is to provide adequate assets for the payment of future benefits. Pursuant to this objective, the Company will fund its pension plans as required by governmental regulations and may consider discretionary contributions as conditions warrant. Although the Company does not anticipate it will be required to make any contributions to its U.S. qualified pension plan by governmental regulations in 2009, the Company plans to make a discretionary contribution of $75 million in 2009 to further improve the funded status of this plan. Contributions to the Company's international plans and the U.S. non-qualified plan are expected to total $13 million in 2009.

Other Retirement Benefits

Other retirement benefits consist of retiree health care and life insurance benefits that are provided to substantially all of the Company's U.S. employees and covered dependents. Employees generally become eligible to receive these benefits if they retire after age 55 with at least 10 years of service. Most plans are contributory with retiree contributions generally based upon years of service and adjusted annually by the Company. Retiree medical plans pay a stated percentage of expenses reduced by deductibles and other coverage, principally Medicare. The amount the Company will contribute toward retiree medical coverage for most employees is fixed. Additional premium contributions will be required from participants for all costs in excess of the Company's fixed contribution amount. As a result, increasing or decreasing the health care cost trend rate by one percentage point would not have a significant impact on the Company's cost of providing these benefits. Retiree life insurance plans provide coverage at a flat dollar amount or as a multiple of salary. With the exception of certain bargaining unit plans, Other Retirement Benefits are funded as expenses are incurred. Contributions to the Company's other postretirement plans are expected to total $17 million in 2009.

Other Retirement Benefit plan amendments reduced the benefit obligation by $15 million at September 30, 2007. The plan amendments primarily related to the Company no longer providing post-age 65 prescription drug coverage effective January 1, 2008.

Plan Assets

Total plan assets for Pension Benefits and Other Retirement Benefits as of September 30, 2008 and 2007 were $1,910 million and $2,505 million, respectively. The Company has established investment objectives that seek to preserve and maximize the amount of plan assets available to pay plan benefits. These objectives are achieved through investment guidelines requiring diversification and allocation strategies designed to maximize the long-term returns on plan assets while maintaining a prudent level of investment risk. These investment strategies are implemented using actively managed and indexed assets. Target and actual asset allocations as of September 30 are as follows:

	Target Mix	2008	2007
Equities	40%-70%	64%	69%
Fixed income	25%-60%	36%	30%
Alternative investments	0%-15%	—	—
Cash	0%-5%	—	1%

Alternative investments may include real estate, hedge funds, venture capital, and private equity. There were no plan assets invested in the securities of the Company as of September 30, 2008 and 2007 or at any time during the years then ended. Target and actual asset allocations are periodically rebalanced between asset classes in order to mitigate investment risk and maintain asset classes within target allocations.

Benefit Payments

The following table reflects estimated benefit payments to be made to eligible participants for each of the next five years and the following five years in aggregate:

(in millions)	Pension Benefits	Other Retirement Benefits
2009	$150	$21
2010	154	21
2011	158	21
2012	163	22
2013	170	22
2014 - 2018	951	85

Substantially all of the Pension Benefit payments relate to the Company's qualified funded plans which are paid from the pension trust.

12. Shareowners' Equity

Common Stock

The Company is authorized to issue one billion shares of common stock, par value $0.01 per share, and 25 million shares of preferred stock, without par value, of which 2.5 million shares are designated as Series A Junior Participating Preferred Stock for issuance in connection with the exercise of preferred share purchase rights. At September 30, 2008, 13.5 million shares of common stock were reserved for issuance under various employee incentive plans and the employee stock purchase plan (ESPP).

Preferred Share Purchase Rights

Each outstanding share of common stock provides the holder with one Preferred Share Purchase Right (Right). The Rights will become exercisable only if a person or group acquires, or offers to acquire, without prior approval of the Board of Directors, 15 percent or more of the Company's common stock. However, the Board of Directors is authorized to reduce the 15 percent threshold for triggering the Rights to not less than 10 percent. Upon exercise, each Right entitles the holder to $1/100^{th}$ of a share of Series A Junior Participating Preferred Stock of the Company (Junior Preferred Stock) at a price of $125, subject to adjustment.

Upon acquisition of the Company, each Right (other than Rights held by the acquirer) will generally be exercisable for $250 worth of either common stock of the Company or common stock of the acquirer for $125. In certain circumstances, each Right may be exchanged by the Company for one share of common stock or $1/100^{th}$ of a share of Junior Preferred Stock. The Rights will expire on June 30, 2011, unless earlier exchanged or redeemed at $0.01 per Right. The Rights have the effect of substantially increasing the cost of acquiring the Company in a transaction not approved by the Board of Directors.

Treasury Stock

The Company repurchased shares of its common stock as follows:

(in millions)	2008	2007	2006
Amount of share repurchases	$576	$333	$492
Number of shares repurchased	9.0	4.6	9.3

The Company paid $19 million in 2007 related to the settlement of an accelerated share repurchase agreement executed in 2006, which is reflected in the table above. At September 30, 2008, the Company was authorized to repurchase an additional $165 million of outstanding stock under the Company's share repurchase program.

Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss consists of the following:

	September 30		
(in millions)	2008	2007	2006
Unamortized pension and other retirement benefits, net of taxes of $344 for 2008 and $211 for 2007	$(589)	$(360)	$ —
Minimum pension liability adjustment, net of taxes of $234 for 2006	—	—	(400)
Foreign currency translation adjustment	12	27	8
Foreign currency cash flow hedge adjustment	(1)	(3)	(1)
Accumulated other comprehensive loss	$(578)	$(336)	$(393)

13. Stock-Based Compensation

Stock-Based Compensation Program Description

Under the Company's 2001 Long-Term Incentives Plan and Directors Stock Plan, up to 14.3 million shares of common stock may be issued by the Company as non-qualified options, incentive stock options, performance units, performance shares, stock appreciation rights, and restricted stock. Shares available for future grant or payment under these plans were 0.4 million at September 30, 2008.

Under the Company's 2006 Long-Term Incentives Plan, up to 11.0 million shares of common stock may be issued by the Company as non-qualified options, incentive stock options, performance units, performance shares, stock appreciation rights, restricted stock, restricted stock units, dividend equivalent rights, and other awards. Each share issued pursuant to an award of restricted stock, restricted stock units, performance shares, and performance units counts as three shares against the authorized limit. Shares available for future grant or payment under this plan were 8.9 million at September 30, 2008.

Options to purchase common stock of the Company have been granted under various incentive plans to directors, officers, and other key employees. All of the Company's stock-based incentive plans require options to be granted at prices equal to or above the fair market value of the common stock on the dates the options are granted. The plans provide that the option price for certain options granted under the plans may be paid by the employee in cash, shares of common stock, or a combination thereof. Certain option awards provide for accelerated vesting if there is a change in control. Stock options generally expire ten years from the date they are granted and generally vest ratably over three years. The Company has an ongoing share repurchase plan and expects to satisfy share option exercises from treasury stock.

Until 2006, the Company utilized stock options as the primary component of stock-based compensation awards under its long-term incentive plans for officers and other key employees. In 2006, the Company began using fewer stock options as part of these awards and introduced multi-year performance shares and restricted stock. Both the performance shares and restricted stock cliff vest at the end of three years. The number of performance shares that will ultimately be issued is based on achievement of performance targets over a three-year period that considers cumulative sales growth and return on sales with an additional potential adjustment up or down depending on the Company's total return to shareowners compared to a group of peer companies. The Company's stock-based compensation awards are designed to align management's interests with those of the Company's shareowners and to reward outstanding Company performance. The Company's stock-based compensation awards serve as an important retention tool because the awards generally vest over a three-year period or cliff vest at the end of three years.

Stock-based compensation expense is recognized on a straight-line basis over the requisite service period. Total stock-based compensation expense included within the Consolidated Statement of Operations for 2008, 2007, and 2006 is as follows:

(in millions, except per share amounts)	2008	2007	2006
Stock-based compensation expense included in:			
Product cost of sales	$ 4	$ 4	$ 4
Service cost of sales	2	1	1
Selling, general and administrative expenses	13	12	13
Total	$19	$17	$18

General Option Information

The following summarizes the activity of the Company's stock options for 2008, 2007, and 2006:

(shares in thousands, remaining life in years)	Shares	Weighted Average Exercise Price	Weighted Average Remaining Life
Outstanding at September 30, 2005	10,428	$26.52	
Granted	590	45.22	
Exercised	(2,848)	25.52	
Forfeited or expired	(79)	34.49	
Outstanding at September 30, 2006	8,091	28.16	
Granted	456	58.36	
Exercised	(2,388)	26.44	
Forfeited or expired	(29)	45.01	
Outstanding at September 30, 2007	6,130	30.99	
Granted	373	72.22	
Exercised	(637)	25.96	
Forfeited or expired	(38)	46.24	
Outstanding at September 30, 2008	5,828	$34.09	4.8
Vested or expected to vest(a)	5,786	$33.88	4.3
Exercisable at September 30, 2008	4,995	$29.49	4.2

(a) Represents outstanding options reduced by expected forfeitures

	2008	2007	2006
Weighted-average fair value per share of options granted	$ 22.97	$ 16.70	$ 13.46
Intrinsic value of options exercised	$24 million	$94 million	$75 million
Tax deduction resulting from intrinsic value of options exercised	$ 8 million	$34 million	$27 million

The intrinsic value of options outstanding and options exercisable at September 30, 2008 was $73 million and $73 million, respectively.

The following summarizes the activity of the Company's stock options that have not vested for the years ended September 30, 2008, 2007, and 2006:

(shares in thousands)	Shares	Weighted Average Exercise Price
Nonvested at September 30, 2005	3,282	$32.49
Granted	590	45.22
Vested	(1,703)	34.35
Forfeited or expired	(57)	36.12
Nonvested at September 30, 2006	2,112	36.39
Granted	456	58.36
Vested	(1,295)	33.61
Forfeited or expired	(29)	45.01
Nonvested at September 30, 2007	1,244	47.13
Granted	373	72.22
Vested	(759)	43.17
Forfeited or expired	(25)	58.59
Nonvested at September 30, 2008	833	$61.62

The total fair value of options vested was $9 million, $13 million, and $17 million during the years ended September 30, 2008, 2007, and 2006, respectively. Total unrecognized compensation expense for options that have not vested as of September 30, 2008 is $6 million and will be recognized over a weighted average period of 0.8 years.

Stock Option Fair Value Information

The Company's determination of fair value of option awards on the date of grant using an option-pricing model is affected by the Company's stock price as well as assumptions regarding a number of subjective variables. These assumptions include, but are not limited to: the Company's expected stock price volatility, the projected employee stock option exercise term, the expected dividend yield, and the risk-free interest rate. Changes in these assumptions can materially affect the estimated value of the stock options.

The fair value of each option granted by the Company was estimated using a binomial lattice pricing model and the following weighted average assumptions:

	2008 Grants	2007 Grants	2006 Grants
Risk-free interest rate	3.86%	4.55%	4.40%
Expected dividend yield	0.98%	1.09%	1.08%
Expected volatility	0.30	0.28	0.30
Expected life	6 years	5 years	5 years

The expected life of employee stock options represents the weighted-average period the stock options are expected to remain outstanding. The binomial lattice model assumes that employees' exercise behavior is a function of the option's remaining expected life and the extent to which the option is in-the-money. The binomial lattice model estimates the probability of exercise as a function of these two variables based on the entire history of exercises and forfeitures on all past option grants made by the Company.

Performance Shares, Restricted Shares, and Restricted Stock Units Information

The following summarizes the Company's performance shares, restricted shares, and restricted stock units for 2008, 2007, and 2006:

(in millions, except shares and per share amounts)	Performance Shares		Restricted Shares		Restricted Stock Units	
	Shares	Weighted Average Grant Price	Shares	Weighted Average Grant Price	Shares	Weighted Average Grant Price
Outstanding at September 30, 2005	—		—		—	
Granted	79,127	$45.18	62,875	$46.37	18,523	$52.40
Restrictions released	—		—		—	
Forfeited	(1,898)		(1,400)		—	
Outstanding at September 30, 2006	77,229		61,475		18,523	
Granted	64,377	58.36	42,520	58.69	21,323	$65.32
Restrictions released	—		(886)		(1,516)	
Forfeited	(7,756)		(1,760)		—	
Outstanding at September 30, 2007	133,850		101,349		38,330	
Granted	118,072	72.26	45,900	72.12	21,830	64.57
Restrictions released	—		(2,371)		(8,110)	
Forfeited	(7,226)		(3,150)		(1,060)	
Outstanding at September 30, 2008	244,696	$61.26	141,728	$58.46	50,990	$61.49

(in millions, remaining life in years)	Performance Shares	Restricted Shares	Restricted Stock Units
Total unrecognized compensation costs at September 30, 2008	$ 12	$ 3	$ —
Weighted average life remaining at September 30, 2008	1.2	1.2	—

The maximum number of shares of common stock that can be issued in respect of performance shares granted in 2008 based on the achievement of performance targets for fiscal years 2008 through 2010 is 277,831. The maximum number of shares of common stock that can be issued in respect of performance shares granted in 2007 based on the achievement of performance targets for fiscal years 2007 through 2009 is 144,574. The number of shares of common stock that will be issued in respect of performance shares granted in 2006 based on the achievement of performance targets for fiscal years 2006 through 2008 is 109,910.

Diluted Share Equivalents

Dilutive stock options outstanding resulted in an increase in average outstanding diluted shares of 1.8 million, 2.4 million, and 2.5 million for 2008, 2007, and 2006, respectively. The average outstanding diluted shares calculation excludes options with an exercise price that exceeds the average market price of shares during the year. Stock options excluded from the average outstanding diluted shares calculation were 0.4 million and less than 0.1 million and 0.1 million in 2008, 2007, and 2006, respectively. Dilutive performance shares, restricted shares, and restricted stock units resulted in an increase in average outstanding dilutive shares of 0.3 million in 2008, 0.2 million in 2007, and less than 0.1 million in 2006.

Employee Benefits Paid in Company Stock

The Company offers an Employee Stock Purchase Plan (ESPP) which allows employees to have their base compensation withheld to purchase the Company's common stock each month at 95 percent of the fair market value on the last day of the month. The Company is authorized to issue 9.0 million shares under the ESPP, of which 4.2 million shares are available for future grant at September 30, 2008. The ESPP is considered a non-compensatory plan and accordingly no compensation expense is recorded in connection with this benefit.

The Company also sponsors defined contribution savings plans that are available to the majority of its employees. The plans allow employees to contribute a portion of their compensation on a pre-tax and/or after-tax basis in accordance with specified guidelines. The Company matches a percentage of employee contributions using common stock of the Company up to certain limits. Employees may transfer at any time all or a portion of their balance in Company common stock to any of the other investment options offered within the plans. In addition, effective October 1, 2006, the defined contribution savings plan was amended to include an additional cash contribution based on an employee's age and service. The Company's expense related to the savings plans was $90 million, $75 million, and $39 million for 2008, 2007 and 2006, respectively.

During 2008, 2007, and 2006, 1.1 million, 0.9 million, and 1.0 million shares, respectively, of Company common stock were issued to employees under the Company's employee stock purchase and defined contribution savings plans at a value of $65 million, $58 million, and $50 million for the respective periods.

14. Research and Development

Research and development expense consists of the following:

(in millions)	2008	2007	2006
Customer-funded	$501	$480	$443
Company-funded	395	347	279
Total research and development	$896	$827	$722

15. Other Income, Net

Other income, net consists of the following:

(in millions)	2008	2007	2006
Gain on sale of equity affiliate(a)	$ —	$ —	$(20)
Earnings from equity affiliates	(8)	(8)	(8)
Interest income	(8)	(4)	(5)
Royalty income	(11)	(6)	(5)
Other, net	3	3	6
Other income, net	$(24)	$(15)	$(32)

(a) See Note 8 for a discussion of the gain on sale of Rockwell Scientific Company, LLC recorded in 2006.

16. Income Taxes

The components of income tax expense are as follows:

(in millions)	2008	2007	2006
Current:			
United States federal	$200	$189	$161
Non-United States	2	12	12
United States state and local	—	14	6
Total current	202	215	179
Deferred:			
United States federal	58	41	27
Non-United States	11	(1)	3
United States state and local	4	3	3
Total deferred	73	43	33
Income tax expense	$275	$258	$212

Net current deferred income tax benefits (liabilities) consist of the tax effects of temporary differences related to the following:

	September 30	
(in millions)	2008	2007
Inventory	$ 6	$ 4
Product warranty costs	77	73
Customer incentives	27	31
Contract reserves	11	12
Compensation and benefits	(3)	34
Other, net	18	22
Current deferred income taxes, net	$136	$176

Net long-term deferred income tax benefits (liabilities) consist of the tax effects of temporary differences related to the following:

(in millions)	September 30 2008	2007
Retirement benefits	$173	$ 55
Intangibles	(27)	(8)
Property	(69)	(62)
Stock-based compensation	17	11
Other, net	40	(39)
Long-term deferred income taxes, net	$134	$(43)

Current deferred income tax assets and liabilities and Long-term deferred income tax assets and liabilities are included in the Consolidated Statement of Financial Position as follows:

(in millions)	September 30 2008	2007
Current deferred income taxes	$139	$176
Other current liabilities	(3)	—
Current deferred income taxes, net	$136	$176
Other Assets	$144	$ 1
Other Liabilities	(10)	(44)
Long-term deferred income taxes, net	$134	$(43)

Management believes it is more likely than not that the current and long-term deferred tax assets will be realized through the reduction of future taxable income. Significant factors considered by management in its determination of the probability of the realization of the deferred tax assets include: (a) the historical operating results of Rockwell Collins ($1,861 million of United States taxable income over the past three years), (b) expectations of future earnings, and (c) the extended period of time over which the retirement benefit liabilities will be paid.

The effective income tax rate differed from the United States statutory tax rate for the reasons set forth below:

	2008	2007	2006
Statutory tax rate	35.0%	35.0%	35.0%
Research and development credit	(2.6)	(4.0)	(0.8)
Extraterritorial income exclusion	—	(0.5)	(3.0)
Domestic manufacturing deduction	(1.5)	(0.7)	(0.4)
State and local income taxes	0.6	1.1	0.5
Tax settlements	(2.3)	—	—
Other	(0.3)	(0.3)	0.5)
Effective income tax rate	28.9%	30.6%	30.8%

Income tax expense was calculated based on the following components of income before income taxes:

(in millions)	2008	2007	2006
United States income	$898	$802	$642
Non-United States income	55	41	47
Total	$953	$843	$689

The Federal Research and Development Tax Credit (R&D Tax Credit) expired December 31, 2007. On the last day of fiscal 2008, the Emergency Economic Stabilization Act of 2008 was enacted, which retroactively reinstated and extended the Federal R&D Tax Credit from January 1, 2008 to December 31, 2009. The effective tax rate for fiscal year 2008 reflects a full year of benefit from the Federal R&D tax credit.

The effective tax rate for fiscal year 2007 reflects the retroactive reinstatement of the Federal R&D Tax Credit which had previously expired December 31, 2005. On December 20, 2006, the Tax Relief and Health Care Act of 2006 was enacted, which retroactively reinstated and extended the Federal R&D Tax Credit from January 1, 2006 to December 31, 2007. The retroactive benefit for the previously expired period from January 1, 2006 to September 30, 2006 lowered the Company's effective tax rate by about 1.5 percentage points for the year ended September 30, 2007.

The phase-out period for the Federal Extraterritorial Income Exclusion (ETI) tax benefit ended on December 31, 2006. The enacted federal replacement tax benefit for ETI, the Domestic Manufacturing Deduction (DMD), applied to the full fiscal 2007 year. In 2008, the available DMD tax benefit is two-thirds of the full benefit that will be available in 2011. In 2007, the available DMD tax benefit was one-third of the full benefit that will be available in 2011.

The Company's U.S. Federal income tax returns for the tax years ended September 30, 2005 and prior have been audited by the Internal Revenue Service (IRS) and are closed to further adjustments by the IRS. The IRS is currently auditing the Company's tax returns for the years ended September 30, 2006 and 2007. The Company has not received any proposed audit adjustments from the IRS. The Company is also currently under audit in various U.S. states and foreign jurisdictions. The U.S. state and foreign jurisdictions have statutes of limitations generally ranging from 3 to 5 years. The Company believes it has adequately provided for any tax adjustments that may result from the various audits.

During 2008, the Congressional Joint Committee on Taxation completed its review of the IRS examination of the Company's tax returns for the taxable years ended September 30, 2004 and 2005 as well as the amended returns for the years ended September 30, 2002 and 2003 (the tax settlements) resulting in a benefit to the effective income tax rate for the year ended September 30, 2008 of 2.3 percentage points.

No provision has been made as of September 30, 2008 for United States federal or state, or additional foreign income taxes related to approximately $185 million of undistributed earnings of foreign subsidiaries which have been or are intended to be permanently reinvested.

The Company paid income taxes, net of refunds, of $268 million, $212 million, and $164 million, in 2008, 2007, and 2006, respectively.

FASB Interpretation No. 48

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for uncertainty in income taxes* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes by establishing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 prescribes a comprehensive model for how a company should recognize, derecognize, measure, present, and disclose in its financial statements uncertain tax positions that a company has taken or expects to take on a tax return. In addition, FIN 48 provides guidance on interest and penalties, accounting in interim periods, and transition.

The Company adopted the provisions of FIN 48 at the beginning of fiscal year 2008. The $5 million cumulative effect of adopting FIN 48 was recorded as a reduction to retained earnings in the first quarter of 2008. As of the beginning of fiscal year 2008, the Company had gross unrecognized tax benefits of $84 million recorded within Other Liabilities in the Consolidated Statement of Financial Position, of which $52 million would affect the effective income tax rate if recognized. At September 30, 2008, the Company had gross unrecognized tax benefits of $73 million recorded within Other Liabilities in the Consolidated Statement of Financial Position, of which $41 million would affect the effective income tax rate if recognized. During the next 12 months, the amount of previously unrecognized tax benefits is not expected to significantly change.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

(in millions)	
Balance at October 1, 2007	$ 84
Additions for tax positions related to the current year	19
Additions for tax positions of prior years	2
Reductions for tax positions of prior years	(20)
Reductions for tax positions related to settlements with taxing authorities	(12)
Reductions for tax positions related to prior years as a result of a lapse of statute of limitations	—
Balance at September 30, 2008	$ 73

The Company recognizes interest and penalties related to unrecognized tax benefits in income tax expense. As of October 1, 2007, the total amount of interest and penalties recognized within Other Liabilities in the Consolidated Statement of Financial Position was $9 million. As of September 30, 2008, the total amount of interest and penalties recognized within Other Liabilities in the Consolidated Statement of Financial Position was $5 million.

17. Financial Instruments

Fair Value of Financial Instruments

The carrying amounts and fair values of the Company's financial instruments are as follows:

	Asset (Liability)			
	September 30, 2008		September 30, 2007	
(in millions)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	$ 175	$ 175	$ 231	$ 231
Deferred compensation plan investments	33	33	39	39
Short-term debt	(287)	(287)	—	—
Long-term debt	(228)	(216)	(223)	(216)
Interest rate swaps	4	4	(1)	(1)
Foreign currency forward exchange contracts	(2)	(2)	(5)	(5)

The fair value of cash and cash equivalents approximate their carrying value due to the short-term nature of the instruments. Fair value for deferred compensation plan investments is based on quoted market prices and is recorded at fair value within Other Assets. The fair value of short-term debt approximates its carrying value due to the short-term nature of the debt. Fair value information for long-term debt and interest rate swaps is based on current market interest rates and estimates of current market conditions for instruments with similar terms, maturities, and degree of risk. The fair value of foreign currency forward exchange contracts is estimated based on quoted market prices for contracts with similar maturities. These fair value estimates do not necessarily reflect the amounts the Company would realize in a current market exchange.

Interest Rate Swaps

The Company manages its exposure to interest rate risk by maintaining an appropriate mix of fixed and variable rate debt, which over time should moderate the costs of debt financing. When considered necessary, the Company may use financial instruments in the form of interest rate swaps to help meet this objective. On November 20, 2003, the Company entered into two interest rate swap contracts (the Swaps) which expire on December 1, 2013 and effectively convert $100 million of the 4.75 percent fixed rate long-term notes to floating rate debt based on six-month LIBOR less 7.5 basis points. The Company has designated the Swaps as fair value hedges. At September 30, 2008 and 2007, the Swaps are recorded at a fair value of $4 million and $1 million, within Other Assets and Other Liabilities, respectively, offset by a fair value adjustment to Long-Term Debt (Note 10) of $4 million and $1 million, respectively. Cash payments or receipts between the Company and the counterparties to the Swaps are recorded as an adjustment to interest expense.

Foreign Currency Forward Exchange Contracts

The Company transacts business in various foreign currencies which subjects the Company's cash flows and earnings to exposure related to changes in foreign currency exchange rates. These exposures arise primarily from purchases or sales of products and services from third parties and intercompany transactions. The Company has established a program that utilizes foreign currency forward exchange contracts (foreign currency contracts) and attempts to minimize its exposure to fluctuations in foreign currency exchange rates relating to these transactions. Foreign currency contracts provide for the exchange of currencies at specified future prices and dates and reduce exposure to currency fluctuations by generating gains and losses that are intended to offset gains and losses on the underlying transactions. Principal currencies that are hedged include the European euro, British pound, and Japanese yen. The duration of foreign currency contracts is generally two years or less. The maximum duration of a foreign currency contract at September 30, 2008 was 142 months. The Company hedges the majority of the Company's non-functional currency firm and anticipated receivables and payables that are denominated in major currencies which can be traded on open markets. The Company does not manage exposure to net investments in foreign subsidiaries.

Notional amounts of outstanding foreign currency forward exchange contracts were $218 million and $205 million at September 30, 2008 and 2007, respectively. Notional amounts are stated in U.S. dollar equivalents at spot exchange rates at the respective dates. The net fair value of these foreign currency contracts at September 30, 2008 and 2007 were net liabilities of $2 million and $5 million, respectively. Net gains of $3 million and net losses of $3 million were deferred within Accumulated Other Comprehensive Loss relating to cash flow hedges at September 30, 2008 and 2007, respectively. The Company expects to re-classify approximately $3 million of these net gains into earnings over the next 12 months. There was no significant impact to the Company's earnings related to the ineffective portion of any hedging instruments during the three years ended September 30, 2008. Gains and losses related to all foreign currency contracts are recorded in Cost of Sales.

18. Guarantees and Indemnifications

Product warranty costs

Accrued liabilities are recorded to reflect the Company's contractual obligations relating to warranty commitments to customers. Warranty coverage of various lengths and terms is provided to customers depending on standard offerings and negotiated contractual agreements. An estimate for warranty expense is recorded at the time of sale based on the length of the warranty and historical warranty return rates and repair costs.

Changes in the carrying amount of accrued product warranty costs are summarized as follows:

(in millions)	September 30 2008	September 30 2007
Balance at beginning of year	$213	$189
Warranty costs incurred	(53)	(54)
Product warranty accrual	68	71
Reclassification	—	7
Acquisitions	1	—
Pre-existing warranty adjustments	(3)	—
Balance at September 30	$226	$213

Guarantees

In connection with the acquisition of the Quest joint venture from Evans & Sutherland, the Company entered into a parent company guarantee related to various obligations of Quest. The Company has guaranteed, jointly and severally with Quadrant Group plc (Quadrant) (the other joint venture partner), the performance of Quest in relation to its contract with the United Kingdom Ministry of Defence (which expires in 2030) and the performance of certain Quest subcontractors (up to $2 million). In addition, the Company has also pledged equity shares in Quest to guarantee payment by Quest of a loan agreement executed by Quest. In the event of default on this loan agreement, the lending institution can request that the trustee holding such equity shares surrender them to the lending institution in order to satisfy all amounts then outstanding under the loan agreement. As of September 30, 2008, the outstanding loan balance was approximately $8 million. Quadrant has made an identical pledge to guarantee this obligation of Quest.

Should Quest fail to meet its obligations under these agreements, these guarantees may become a liability of the Company. As of September 30, 2008, the Quest guarantees are not reflected on the Company's Consolidated Statement of Financial Position because the Company believes that Quest will meet all of its performance and financial obligations in relation to its contract with the United Kingdom Ministry of Defence and the loan agreement.

Letters of credit

The Company has contingent commitments in the form of letters of credit. Outstanding letters of credit are issued by banks on the Company's behalf to support certain contractual obligations to its customers. If the Company fails to meet these contractual obligations, these letters of credit may become liabilities of the Company. Total outstanding letters of credit at September 30, 2008 were $114 million. These commitments are not reflected as liabilities on the Company's Consolidated Statement of Financial Position.

Indemnifications

The Company enters into indemnifications with lenders, counterparties in transactions such as administration of employee benefit plans, and other customary indemnifications with third parties in the normal course of business. The following are other than customary indemnifications based on the judgment of management.

The Company became an independent, publicly held company on June 29, 2001, when Rockwell International Corporation (Rockwell), renamed Rockwell Automation Inc., spun off its former avionics and communications business and certain other assets and liabilities of Rockwell by means of a distribution of all the Company's outstanding shares of common stock to the shareowners of Rockwell in a tax-free spin-off (the spin-off). In connection with the spin-off, the Company may be required to indemnify certain insurers against claims made by third parties in connection with the Company's legacy insurance policies.

In connection with agreements for the sale of portions of its business, the Company at times retains the liabilities of a business of varying amounts that relate to events occurring prior to its sale, such as tax, environmental, litigation and employment matters. The Company at times indemnifies the purchaser of a Rockwell Collins business in the event that a third party asserts a claim that relates to a liability retained by the Company.

The Company also provides indemnifications of varying scope and amounts to certain customers against claims of product liability or intellectual property infringement made by third parties arising from the use of Company or customer products or intellectual property. These indemnifications generally require the Company to compensate the other party for certain damages and costs incurred as a result of third party product liability or intellectual property claims arising from these transactions.

The amount the Company could be required to pay under its indemnification agreements is generally limited based on amounts specified in the underlying agreements, or in the case of some agreements, the maximum potential amount of future payments that could be required is not limited. When a potential claim is asserted under these agreements, the Company considers such factors as the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate of the amount of loss. A liability is recorded when a potential claim is both probable and estimable. The nature of these agreements prevents the Company from making a reasonable estimate of the maximum potential amount it could be required to pay should counterparties to these agreements assert a claim; however, the Company currently has no material claims pending related to such agreements.

19. Contractual Obligations and Other Commitments

The following table reflects certain of the Company's non-cancelable contractual commitments as of September 30, 2008:

(in millions)	Payments Due By Period						
	2009	2010	2011	2012	2013	Thereafter	Total
Non-cancelable operating leases	$43	$37	$27	$23	$19	$ 51	$200
Purchase contracts	34	33	33	34	37	12	183
Long-term debt	—	—	24	—	—	200	224
Interest on long-term debt	11	11	10	10	10	2	54
Total	$88	$81	$94	$67	$66	$265	$661

Non-cancelable Operating Leases

The Company leases certain office and manufacturing facilities as well as certain machinery and equipment under various lease contracts with terms that meet the accounting definition of operating leases. Some leases include renewal options, which permit extensions of the expiration dates at rates approximating fair market rental rates. Rent expense for the years ended September 30, 2008, 2007, and 2006 was $48 million, $29 million, and $27 million, respectively. The Company's commitments under these operating leases, in the form of non-cancelable future lease payments, are not reflected as a liability on the Consolidated Statement of Financial Position.

Purchase Contracts

The Company may enter into purchase contracts with suppliers under which there is a commitment to buy a minimum amount of products or pay a specified amount. These commitments are not reflected as a liability on the Company's Consolidated Statement of Financial Position. Amounts purchased under these agreements for the years ended September 30, 2008, 2007, and 2006 was $27 million, $15 million, and $3 million, respectively.

Interest on Long-term Debt

Interest payments under long-term debt obligations exclude the potential effects of the related interest rate swap contracts.

FASB Interpretation No. 48

The table excludes $73 million of liabilities for unrecognized tax benefits recorded in accordance with FIN 48. The Company is unable to reasonably estimate the ultimate amount or timing of cash settlements to the respective taxing authorities. See Note 16 for further discussion.

20. Environmental Matters

The Company is subject to federal, state and local regulations relating to the discharge of substances into the environment, the disposal of hazardous wastes, and other activities affecting the environment that have had and will continue to have an impact on the Company's manufacturing operations. These environmental protection regulations may require the investigation and remediation of environmental impairments at current and previously owned or leased properties. In addition, lawsuits, claims and proceedings have been asserted on occasion against the Company alleging violations of environmental protection regulations, or seeking remediation of alleged environmental impairments, principally at previously owned or leased properties. As of September 30, 2008, the Company is involved in the investigation or remediation of seven sites under these regulations or pursuant to lawsuits asserted by third parties. Management estimates that the total reasonably possible future costs the Company could incur for six of these sites is not significant. Management estimates that the total reasonably possible future costs the Company could incur from one of these sites to be approximately $9 million. The Company has recorded environmental reserves for this site of $3 million as of September 30, 2008, which represents management's best estimate of the probable future cost for this site.

To date, compliance with environmental regulations and resolution of environmental claims has been accomplished without material effect on the Company's liquidity and capital resources, competitive position or financial condition. Management believes that expenditures for environmental capital investment and remediation necessary to comply with present regulations governing environmental protection and other expenditures for the resolution of environmental claims will not have a material adverse effect on the Company's business or financial position, but could possibly be material to the results of operations or cash flows of any one quarter.

21. Legal Matters

The Company is subject to various lawsuits, claims and proceedings that have been or may be instituted or asserted against the Company relating to the conduct of the Company's business, including those pertaining to product liability, intellectual property, safety and health, exporting and importing, contract, employment and regulatory matters. Although the outcome of these matters cannot be predicted with certainty and some lawsuits, claims or proceedings may be disposed of unfavorably to the Company, management believes the disposition of matters that are pending or asserted will not have a material adverse effect on the Company's business or financial position, but could possibly be material to the results of operations or cash flows of any one quarter.

22. Business Segment Information

Rockwell Collins designs, produces and supports communications and aviation electronics for commercial and military customers worldwide. The Company has two operating segments consisting of the Commercial Systems and Government Systems businesses.

Commercial Systems supplies aviation electronics systems, products, and services to customers located throughout the world. The customer base is comprised of original equipment manufacturers (OEMs) of commercial air transport, business and regional aircraft, commercial airlines, fractional and other business aircraft operators.

Government Systems provides communication and electronic systems, products and services for airborne and surface applications to the U.S. Department of Defense, other government agencies, civil agencies, defense contractors and foreign ministries of defense.

Sales made to the United States Government were 38 percent, 36 percent, and 39 percent of total sales for the years ended September 30, 2008, 2007, and 2006, respectively.

The following table reflects the sales and operating results for each of the Company's operating segments:

(in millions)	2008	2007	2006
Sales:			
Commercial Systems	$2,403	$2,184	$1,820
Government Systems	2,366	2,231	2,043
Total sales	$4,769	$4,415	$3,863
Segment operating earnings:			
Commercial Systems	$ 560	$ 485	$ 370
Government Systems	486	441	402
Total segment operating earnings	1,046	926	772
Interest expense	(21)	(13)	(13)
Earnings from corporate-level equity affiliate	—	—	2
Stock-based compensation	(19)	(17)	(18)
Gain on sale of equity affiliate.	—	—	20
Restructuring (charge) / adjustment	—	5	(14)
General corporate, net	(53)	(58)	(60)
Income before income taxes	953	843	689
Income tax provision	(275)	(258)	(212)
Net Income	$ 678	$ 585	$ 477

The Company evaluates performance and allocates resources based upon, among other considerations, segment operating earnings. The Company's definition of segment operating earnings excludes income taxes, stock-based compensation, unallocated general corporate expenses, interest expense, gains and losses from the disposition of businesses, non-recurring charges resulting from purchase accounting such as purchased research and development charges, asset impairment charges, and other special items as identified by management from time to time. Intersegment sales are not material and have been eliminated. The accounting policies used in preparing the segment information are consistent with the policies described in Note 2.

The September 2006 restructuring charge was related to decisions to implement certain business realignment and facility rationalization actions related to the operating segments as follows: Government Systems, $6 million, and Commercial Systems, $8 million. The 2007 adjustment to the restructuring charge was due to lower than expected employee separation costs and relates to the operating segments as follows: Government Systems, $3 million, and Commercial Systems, $2 million.

The following tables summarize the identifiable assets and investments in equity affiliates at September 30, as well as the provision for depreciation and amortization, the amount of capital expenditures for property, and earnings (losses) from equity affiliates for each of the three years ended September 30, for each of the operating segments and Corporate:

(in millions)	2008	2007	2006
Identifiable assets:			
Commercial Systems	$1,870	$1,711	$1,528
Government Systems	1,706	1,472	1,361
Corporate	568	567	389
Total identifiable assets	$4,144	$3,750	$3,278
Investments in equity affiliates:			
Commercial Systems	$ —	$ —	$ —
Government Systems	9	10	13
Corporate	—	—	—
Total investments in equity affiliates	$ 9	$ 10	$ 13
Depreciation and amortization:			
Commercial Systems	$ 75	$ 63	$ 58
Government Systems	54	55	48
Total depreciation and amortization	$ 129	$ 118	$ 106
Capital expenditures for property:			
Commercial Systems	$ 74	$ 60	$ 69
Government Systems	97	65	75
Total capital expenditures for property	$ 171	$ 125	$ 144
Earnings (losses) from equity affiliates:			
Commercial Systems	$ —	$ —	$ —
Government Systems	8	8	6
Corporate	—	—	2
Total earnings from equity affiliates	$ 8	$ 8	$ 8

The majority of the Company's businesses share many common resources, infrastructures and assets in the normal course of business. Certain assets have been allocated between the operating segments primarily based on occupancy or usage, principally property, plant and equipment. Identifiable assets at Corporate consist principally of cash and net deferred income tax assets for all years presented and the prepaid pension asset for the year ended September 30, 2007.

The following table summarizes sales by product category for the years ended September 30:

(in millions)	2008	2007	2006
Air transport aviation electronics	$1,257	$1,175	$ 968
Business and regional aviation electronics	1,146	1,009	852
Commercial Systems sales	2,403	2,184	1,820
Airborne solutions	1,662	1,605	1,462
Surface solutions	704	626	581
Government Systems sales	2,366	2,231	2,043
Total sales	$4,769	$4,415	$3,863

The air transport and business and regional aviation electronics product categories are delineated based upon the difference in underlying customer base, size of aircraft, and markets served.

Beginning in 2008, product category sales for defense-related products in the Government Systems segment are delineated based upon the difference in underlying customer base and markets served. In prior years, defense-related product categories were delineated based upon their underlying technologies. Sales for the years ended September 30, 2007 and 2006 for the Government Systems segment product categories have been reclassified to conform to the current year presentation.

The following table reflects sales for the years ended September 30 and property at September 30 by geographic region:

	Sales			Property		
(in millions)	2008	2007	2006	2008	2007	2006
United States	$3,164	$2,987	$2,616	$630	$559	$505
Europe	927	840	674	43	42	39
Asia-Pacific	293	252	234	5	4	5
Canada	229	218	223	—	—	—
Africa / Middle East	102	79	74	—	—	—
Latin America	54	39	39	2	2	3
Total	$4,769	$4,415	$3,863	$680	$607	$552

Sales are attributed to the geographic regions based on the country of destination.

23. Quarterly Financial Information (Unaudited)

Quarterly financial information for the years ended September 30, 2008 and 2007 is summarized as follows:

(in millions, except per share amounts)	2008 Quarters First	Second	Third	Fourth	Total
Sales	$1,112	$1,186	$1,194	$1,277	$4,769
Gross profit (total sales less product and service cost of sales)	343	346	367	379	1,435
Net income	154	168	174	182	678
Earnings per share:					
Basic	$ 0.95	$ 1.04	$ 1.09	$ 1.14	$ 4.22
Diluted	$ 0.93	$ 1.03	$ 1.07	$ 1.13	$ 4.16

(in millions, except per share amounts)	2007 Quarters First	Second	Third	Fourth	Total
Sales	$ 993	$1,083	$1,113	$1,226	$4,415
Gross profit (total sales less product and service cost of sales)	303	327	333	360	1,323
Net income	143	140	146	156	585
Earnings per share:					
Basic	$ 0.85	$ 0.83	$ 0.87	$ 0.94	$ 3.50
Diluted	$ 0.84	$ 0.82	$ 0.86	$ 0.93	$ 3.45

Earnings per share amounts are computed independently each quarter. As a result, the sum of each quarter's per share amount may not equal the total per share amount for the respective year.

Net income in the fourth quarter of 2008 includes a discrete item related to the retroactive reinstatement and extension of the Federal R&D Tax Credit, which lowered the Company's effective tax rate by about 6 percentage points within the quarter.

Net income in the second and third quarters of 2008 includes discrete items related to favorable income tax adjustments resulting from the resolution of certain tax settlements, which lowered the Company's effective tax rate by 7 and 3 percentage points in the second and third quarter of 2008, respectively.

Net income in the first quarter of 2007 includes a discrete item related to the retroactive reinstatement and extension of the Federal R&D Tax Credit, which lowered the Company's effective tax rate by about 7 percentage points within the quarter.

24. Subsequent Event

On November 24, 2008, subsequent to the Company's fiscal year ended September 30, 2008, the Company acquired all of the shares of SEOS Group Limited (SEOS). SEOS, with operations in the United Kingdom and United States, is a leading global supplier of highly realistic visual display solutions for commercial and military flight simulators. SEOS will be included within the results of both Commercial Systems and Government Systems. The cash purchase price, net of cash acquired, was $28 million and was financed with cash on hand. Additional consideration of up to $8 million may be paid post-closing, contingent upon the achievement of certain milestones. Any such additional consideration will be accounted for as goodwill.