

RAYTHEON CO/  
Form 10-Q  
July 29, 2010  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

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

For the quarterly period ended June 27, 2010

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

For the transition period from            to

Commission File Number 1-13699

**RAYTHEON COMPANY**

(Exact name of registrant as specified in its charter)

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**Delaware** **95-1778500**  
(State or other jurisdiction of **(I.R.S. Employer**  
**incorporation or organization)** **Identification No.)**  
**870 Winter Street, Waltham, Massachusetts 02451**  
**(Address of principal executive offices) (Zip Code)**  
**(781) 522-3000**  
**(Registrant's telephone number, including area code)**

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

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

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Number of shares of common stock outstanding as of July 14, 2010 was 374,112,000

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**Cautionary Note Regarding Forward-Looking Statements**

This Form 10-Q contains forward-looking statements including information regarding our 2010 financial outlook, future plans, objectives, business prospects, the impact of certain liabilities, the impact of certain legal and regulatory changes and changes in accounting treatment, the impact of the UK Border Agency program termination, including potential liabilities for losses, previous payments and other claims that may be asserted and the collection of billed and unbilled receivables, the outcome of certain litigation and audits and investigations, sufficiency of capital, our expected funding credit and required contributions, anticipated tax payments and capital expenditures, potential changes to our unrecognized tax benefits, our ability to realize a deferred tax asset and anticipated financial performance. You can identify these statements by the fact that they include words such as will, believe, anticipate, expect, estimate, intend, plan, outlook or variations of these words or expressions. These forward-looking statements are not statements of historical facts and represent only our current expectations regarding such matters. These statements inherently involve a wide range of known and unknown uncertainties. Our actual actions and results could differ materially from what is expressed or implied by these statements. Factors that could cause such a difference include, but are not limited to, those set forth under Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2009 and other important factors disclosed previously and from time to time in our other filings with the Securities and Exchange Commission (SEC). Given these factors, as well as other variables that may affect our operating results, you should not rely on forward-looking statements, assume that past financial performance will be a reliable indicator of future performance nor use historical trends to anticipate results or trends in future periods. We expressly disclaim any obligation or intention to provide updates to the forward-looking statements and the estimates and assumptions associated with them.

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## PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS  
RAYTHEON COMPANY

## CONSOLIDATED BALANCE SHEETS

| (In millions, except per share amounts)   | (Unaudited)<br>June 27, 2010 | Dec. 31, 2009    |
|---|------------------------------|------------------|
| <b>ASSETS</b>   |                              |                  |
| Current assets  |                              |                  |
| Cash and cash equivalents   | \$ 2,385                     | \$ 2,642         |
| Accounts receivable, net  | 131                          | 120              |
| Contracts in process  | 4,461                        | 4,373            |
| Inventories   | 330                          | 344              |
| Deferred taxes  | 301                          | 273              |
| Prepaid expenses and other current assets   | 112                          | 116              |
| <b>Total current assets</b>   | <b>7,720</b>                 | <b>7,868</b>     |
| Property, plant and equipment, net  | 1,953                        | 2,001            |
| Deferred taxes  | 326                          | 436              |
| Prepaid retiree benefits  | 130                          | 111              |
| Goodwill  | 11,921                       | 11,922           |
| Other assets, net   | 1,231                        | 1,269            |
| <b>Total assets</b>   | <b>\$ 23,281</b>             | <b>\$ 23,607</b> |
| <b>LIABILITIES AND EQUITY</b>   |                              |                  |
| Current liabilities   |                              |                  |
| Advance payments and billings in excess of costs incurred   | \$ 2,159                     | \$ 2,224         |
| Accounts payable  | 1,330                        | 1,397            |
| Accrued employee compensation   | 972                          | 868              |
| Other accrued expenses  | 1,214                        | 1,034            |
| <b>Total current liabilities</b>  | <b>5,675</b>                 | <b>5,523</b>     |
| Accrued retiree benefits and other long-term liabilities  | 5,261                        | 5,793            |
| Deferred taxes  | 23                           | 23               |
| Long-term debt  | 2,327                        | 2,329            |
| Commitments and contingencies (Note 9)  |                              |                  |
| Equity  |                              |                  |
| Raytheon Company stockholders' equity   |                              |                  |
| Common stock, par value, \$0.01 per share, 1,450 shares authorized, 374 and 378 shares outstanding at June 27, 2010 and December 31, 2009, respectively after deducting 121 and 107 treasury shares at June 27, 2010 and December 31, 2009, respectively. | 4                            | 4                |
| Additional paid-in capital  | 11,332                       | 10,991           |
| Accumulated other comprehensive loss  | (4,712)                      | (4,824)          |
| Treasury stock, at cost   | (6,222)                      | (5,446)          |
| Retained earnings   | 9,473                        | 9,102            |
| <b>Total Raytheon Company stockholders' equity</b>  | <b>9,875</b>                 | <b>9,827</b>     |
| Noncontrolling interests in subsidiaries  | 120                          | 112              |

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|                              |  |           |           |
|------------------------------|--|-----------|-----------|
| Total equity                 |  | 9,995     | 9,939     |
| Total liabilities and equity |  | \$ 23,281 | \$ 23,607 |

The accompanying notes are an integral part of the unaudited consolidated financial statements.

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## RAYTHEON COMPANY

## CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

| (In millions, except per share amounts)   | Three Months Ended |               | Six Months Ended |               |
|---|--------------------|---------------|------------------|---------------|
|   | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Net sales   |                    |               |                  |               |
| Products  | \$ 5,079           | \$ 5,365      | \$ 10,282        | \$ 10,543     |
| Services  | 894                | 760           | 1,744            | 1,466         |
| Total net sales   | 5,973              | 6,125         | 12,026           | 12,009        |
| Operating expenses  |                    |               |                  |               |
| Cost of sales - products  | 4,245              | 4,184         | 8,307            | 8,277         |
| Cost of sales - services  | 793                | 655           | 1,515            | 1,259         |
| Administrative and selling expenses   | 414                | 370           | 822              | 734           |
| Research and development expenses   | 176                | 151           | 328              | 262           |
| Total operating expenses  | 5,628              | 5,360         | 10,972           | 10,532        |
| Operating income  | 345                | 765           | 1,054            | 1,477         |
| Interest expense  | 33                 | 31            | 65               | 63            |
| Interest income   | (4)                | (3)           | (7)              | (7)           |
| Other (income) expense  | 6                  | (13)          | 5                | (8)           |
| Non-operating (income) expense  | 35                 | 15            | 63               | 48            |
| Income from continuing operations before taxes  | 310                | 750           | 991              | 1,429         |
| Federal and foreign income taxes  | 91                 | 246           | 311              | 468           |
| Income from continuing operations   | 219                | 504           | 680              | 961           |
| Income (loss) from discontinued operations, net of tax                                  | (4)                | (3)           | (12)             |               |
| Net income  | 215                | 501           | 668              | 961           |
| Less: Net income (loss) attributable to noncontrolling interests in subsidiaries        | 7                  | 12            | 15               | 20            |
| Net income attributable to Raytheon Company   | \$ 208             | \$ 489        | \$ 653           | \$ 941        |
| Basic earnings (loss) per share attributable to Raytheon Company common stockholders:   |                    |               |                  |               |
| Income from continuing operations   | \$ 0.56            | \$ 1.25       | \$ 1.76          | \$ 2.38       |
| Income (loss) from discontinued operations, net of tax                                  | (0.01)             | (0.01)        | (0.03)           |               |
| Net income  | 0.55               | 1.24          | 1.73             | 2.38          |
| Diluted earnings (loss) per share attributable to Raytheon Company common stockholders: |                    |               |                  |               |
| Income from continuing operations   | \$ 0.56            | \$ 1.24       | \$ 1.73          | \$ 2.35       |
| Income (loss) from discontinued operations, net of tax                                  | (0.01)             | (0.01)        | (0.03)           |               |
| Net income  | 0.55               | 1.23          | 1.70             | 2.35          |
| Amounts attributable to Raytheon Company common stockholders:                           |                    |               |                  |               |
| Income from continuing operations   | \$ 212             | \$ 492        | \$ 665           | \$ 941        |
| Income (loss) from discontinued operations, net of tax                                  | (4)                | (3)           | (12)             |               |

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|            |        |        |        |        |
|------------|--------|--------|--------|--------|
| Net income | \$ 208 | \$ 489 | \$ 653 | \$ 941 |
|------------|--------|--------|--------|--------|

The accompanying notes are an integral part of the unaudited consolidated financial statements.



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RAYTHEON COMPANY

## CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

| (In millions)  | Six Months Ended |               |
|--|------------------|---------------|
|  | June 27, 2010    | June 28, 2009 |
| <b>Cash flows from operating activities</b>  |                  |               |
| Net income   | \$ 668           | \$ 961        |
| (Income) loss from discontinued operations, net of tax   | 12               |               |
| Income from continuing operations  | 680              | 961           |
| Adjustments to reconcile to net cash provided by (used in) operating activities from continuing operations, net of the effect of acquisitions and divestitures |                  |               |
| Depreciation and amortization  | 206              | 194           |
| Stock-based compensation   | 61               | 59            |
| Deferred income taxes  | (109)            | 140           |
| Collection of financing receivables  | 22               | 15            |
| Tax benefit from stock-based awards  | (15)             | (6)           |
| Changes in assets and liabilities  |                  |               |
| Accounts receivable, net   | 13               | (10)          |
| Contracts in process and advance payments and billings in excess of costs incurred   | (175)            | (635)         |
| Inventories  | 16               | 34            |
| Prepaid expenses and other current assets  | 4                | (16)          |
| Accounts payable   | (71)             | (7)           |
| Income taxes receivable / payable  | 148              | 454           |
| Accrued employee compensation  | 100              | 3             |
| Other accrued expenses   | 87               | 6             |
| Pension and other, net   | (310)            | (269)         |
| Net cash provided by (used in) operating activities from continuing operations   | 657              | 923           |
| Net cash provided by (used in) operating activities from discontinued operations   | 2                | (9)           |
| Net cash provided by (used in) operating activities  | 659              | 914           |
| <b>Cash flows from investing activities</b>  |                  |               |
| Additions to property, plant and equipment   | (109)            | (81)          |
| Proceeds from sales of property, plant and equipment   | 2                | 1             |
| Additions to capitalized internal use software   | (31)             | (34)          |
| Payments for purchases of acquired companies, net of cash received   | (12)             |               |
| Change in other assets   | (1)              | (10)          |
| Net cash provided by (used in) investing activities  | (151)            | (124)         |
| <b>Cash flows from financing activities</b>  |                  |               |
| Dividends paid   | (260)            | (234)         |
| Repurchases of common stock  | (775)            | (600)         |
| Proceeds from warrants exercised   | 250              |               |
| Activity under common stock plans  | 12               | (16)          |
| Tax benefit from stock-based awards  | 15               | 6             |
| Other  | (7)              | (6)           |
| Net cash provided by (used in) financing activities  | (765)            | (850)         |
| Net increase (decrease) in cash and cash equivalents   | (257)            | (60)          |

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|  |          |          |
|--|----------|----------|
| Cash and cash equivalents at beginning of the year | 2,642    | 2,259    |
| Cash and cash equivalents at end of period         | \$ 2,385 | \$ 2,199 |

The accompanying notes are an integral part of the unaudited consolidated financial statements.

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RAYTHEON COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**1. Basis of Presentation**

We prepared the accompanying unaudited consolidated financial statements of Raytheon Company and all wholly-owned and majority-owned domestic and foreign subsidiaries on the same basis as our annual audited financial statements, except for the adoption of the required new accounting standards in the first six months of 2010 related to the accounting and disclosure requirements for transfers of financial assets and consolidation of variable interest entities (VIEs).

In the opinion of management, our financial statements reflect all adjustments, which are of a normal recurring nature, necessary for presentation of financial statements for interim periods in accordance with U.S. Generally Accepted Accounting Principles (GAAP) and with the instructions to Form 10-Q in Article 10 of Securities and Exchange Commission (SEC) Regulation S-X. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of our financial statements, and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from those estimates. In addition, we reclassified certain prior year amounts to conform with our current year presentation. As used in this report, the terms we, us, our, Raytheon and the Company mean Raytheon Company and its subsidiaries, unless the context indicates otherwise.

We condensed or omitted certain information and footnote disclosures normally included in our annual audited financial statements, which we prepared in accordance with GAAP. Our quarterly financial statements should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2009.

We have evaluated subsequent events through the time of filing this Quarterly Report on Form 10-Q with the SEC.

**2. Inventories**

Inventories consisted of the following at:

| (In millions)                 | June 27, 2010 | Dec. 31, 2009 |
|-------------------------------|---------------|---------------|
| Materials and purchased parts | \$ 55         | \$ 60         |
| Work in process               | 249           | 257           |
| Finished goods                | 26            | 27            |
| Total                         | \$ 330        | \$ 344        |

We capitalize costs incurred in advance of contract award or funding in inventories if we determine contract award or funding is probable, excluding any start-up costs. We included capitalized precontract and other deferred costs of \$57 million and \$88 million in inventories as work in process at June 27, 2010 and December 31, 2009, respectively.

**3. Product Warranty**

We provide product warranties in conjunction with certain product sales for which we recognize revenue upon delivery.

Activity related to our product warranty accruals was as follows:

| (In millions)                  | Three Months Ended |               | Six Months Ended |               |
|--------------------------------|--------------------|---------------|------------------|---------------|
|                                | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Balance at beginning of period | \$ 37              | \$ 39         | \$ 39            | \$ 39         |

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|                            |       |       |       |       |
|----------------------------|-------|-------|-------|-------|
| Provisions for warranties  | 5     | 2     | 6     | 6     |
| Warranty services provided | (2)   | (3)   | (5)   | (7)   |
| Balance at end of period   | \$ 40 | \$ 38 | \$ 40 | \$ 38 |

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We account for warranty provision costs incurred under our long-term contracts using the cost-to-cost measure of progress as contracts costs, as the estimation of these costs is integral in determining the price of the related long-term contracts. The table above excludes these costs.

**4. Accounting Standards**

As described in Note 1: Basis of Presentation, in January 2010, we adopted the required new accounting standards that amend the accounting and disclosure requirements for transfers of financial assets and consolidation of VIEs. These accounting standards eliminate the concept of a qualifying special-purpose entity (QSPE) and the related exception for applying the consolidation guidance. As a result, we consolidated our QSPE, General Aviation Receivables Corporation (GARC), which did not have a material impact on our unaudited consolidated financial statements and resulted in:

The removal of our \$67 million investment in GARC, previously reported in other assets, net, and

The addition of long and short-term notes receivable, net, of \$68 million; current notes payable of \$2 million; and an increase in retained earnings of less than \$1 million, net of tax.

The notes payable were paid off as of March 28, 2010.

Further, the new accounting standard related to consolidation of VIEs requires an enterprise to perform a qualitative analysis when determining whether or not it must consolidate a VIE. It also requires an enterprise to continuously reassess whether it must consolidate a VIE. Additionally, it requires enhanced disclosures about an enterprise's involvement with VIEs and any significant change in risk exposure due to that involvement, as well as how its involvement with VIEs impacts the enterprise's financial statements. Finally, an enterprise is required to disclose significant judgments and assumptions used to determine whether or not to consolidate a VIE. With the exception of GARC discussed above, the adoption of this accounting standard did not change any of our previous consolidation conclusions and thus did not have an effect on our financial position, results of operations or liquidity.

Other new pronouncements issued but not effective until after June 27, 2010 are not expected to have a material impact on our financial position, results of operations or liquidity.

**5. Acquisitions**

In pursuing our business strategies, we acquire and make investments in certain businesses that meet strategic and financial criteria.

In January 2010, we acquired substantially all of the assets of an Australian company, Compucat Research Pty. Ltd., at Intelligence and Information Systems for \$12 million in cash, which enhances our information security and cybersecurity capabilities. In connection with this acquisition we recorded \$4 million of goodwill and \$2 million of intangible assets.

A rollforward of our goodwill by segment was as follows:

| (In millions)                              | Integrated<br>Defense<br>Systems | Intelligence<br>and<br>Information<br>Systems | Missile<br>Systems | Network<br>Centric<br>Systems | Space<br>and<br>Airborne<br>Systems | Technical<br>Services | Total     |
|--|----------------------------------|---|--------------------|-------------------------------|-------------------------------------|-----------------------|-----------|
| Balance at December 31, 2009               | \$ 767                           | \$ 1,575                                      | \$ 3,432           | \$ 2,616                      | \$ 2,663                            | \$ 869                | \$ 11,922 |
| Adjustment for acquisitions                |                                  | 4   |                    |                               |                                     |                       | 4         |
| Effect of foreign exchange rates and other | (5)                              | 1   |                    |                               |                                     | (1)                   | (5)       |
| Balance at June 27, 2010                   | \$ 762                           | \$ 1,580                                      | \$ 3,432           | \$ 2,616                      | \$ 2,663                            | \$ 868                | \$ 11,921 |

**6. Discontinued Operations**

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In pursuing our business strategies we have divested of certain non-core businesses, investments and assets when appropriate. All residual activity relating to our previously disposed businesses appears in discontinued operations.

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We retained certain assets and liabilities of our previously disposed businesses. At June 27, 2010 and December 31, 2009, we had \$56 million and \$71 million, respectively, of assets primarily related to our retained interest in general aviation finance receivables previously sold by Raytheon Aircraft Company (Raytheon Aircraft). At June 27, 2010 and December 31, 2009, we had \$57 million of liabilities primarily related to certain environmental and product liabilities, aircraft lease obligations, non-income tax obligations and various contract obligations. We also have certain income tax obligations relating to these disposed businesses, which we include in our income tax disclosures. The Internal Revenue Service (IRS) concluded a federal excise tax audit and assessed us additional excise tax related to the treatment of certain Flight Options LLC customer fees and charges, which we have appealed. We continue to believe that an unfavorable outcome is not probable and expect that any potential liability will not have a material adverse effect on our financial position, results of operations or liquidity. We also retained certain U.K. pension assets and obligations for a limited number of U.K. pension plan participants as part of the Raytheon Aircraft sale, which we include in our pension disclosures.

**7. Fair Value Measurements**

The estimated fair value of certain financial instruments, including cash and cash equivalents, approximates the carrying value due to their short maturities. The estimated fair value of notes receivable approximates the carrying value based principally on their underlying interest rates and terms, maturities, collateral and credit status of the receivables. The carrying value of long-term debt of \$2,327 million and \$2,329 million at June 27, 2010 and December 31, 2009, respectively, was recorded at amortized cost. The estimated fair value of long-term debt of approximately \$2,706 million and \$2,581 million at June 27, 2010 and December 31, 2009, respectively, was based on quoted market prices.

We did not have any significant nonfinancial assets or nonfinancial liabilities that would be recognized or disclosed at fair value on a recurring basis as of June 27, 2010 and December 31, 2009.

The accounting standard for fair value measurements provides a framework for measuring fair value and requires expanded disclosures regarding fair value measurements. Fair value is defined as the price that would be received for an asset or the exit price that would be paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants on the measurement date. This accounting standard established a fair value hierarchy, which requires an entity to maximize the use of observable inputs, where available. The following summarizes the three levels of inputs required, as well as the assets and liabilities that we value using those levels of inputs.

- Level 1:** Quoted prices in active markets for identical assets or liabilities. Our Level 1 assets are investments in marketable securities held in rabbi trusts that we use to pay benefits under certain of our non-qualified deferred compensation plans, which we include in other assets, net. Our Level 1 liabilities include our obligations to pay certain non-qualified deferred compensation plan benefits, which we include in accrued retiree benefits and other long-term liabilities. Under these non-qualified deferred compensation plans, participants designate investment options (primarily mutual funds) to serve as the basis for measurement of the notional value of their accounts. We also include foreign currency forward contracts that we trade in an active exchange market in our Level 1 assets and liabilities.
- Level 2:** Observable inputs, other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or that we corroborate with observable market data for substantially the full term of the related assets or liabilities. We did not have any Level 2 assets or liabilities at June 27, 2010 and December 31, 2009.

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**Level 3:** Unobservable inputs supported by little or no market activity that are significant to the fair value of the assets or liabilities. At December 31, 2009, our Level 3 asset related to our retained interest in general aviation finance receivables (Retained Interest) that we sold in previous years, for which the underlying aircraft serve as collateral. As discussed in Note 4: Accounting Standards, we now present short-term and long-term receivables on our consolidated balance sheet at amortized cost. As a result, our Retained Interest was transferred out of our fair value tables in the three months ended March 28, 2010. We previously estimated the fair value of this asset based on the present value of the future expected cash flows using certain unobservable inputs, including the collection periods for the underlying receivables and a credit-adjusted discount rate of 5.3% at December 31, 2009. These unobservable inputs reflected our estimates about the assumptions market participants would use in pricing this asset. We did not have any Level 3 assets or liabilities at June 27, 2010.

We did not have any transfers of assets and liabilities between Level 1 and Level 2 of the fair value measurement hierarchy during the six months ended June 27, 2010.

The following tables set forth the financial assets and liabilities that we measured at fair value on a recurring basis by level within the fair value hierarchy. We classify assets and liabilities measured at fair value in their entirety based on the lowest level of input that is significant to their fair value measurement.

Assets and liabilities measured at fair value on a recurring basis consisted of the following at:

| (In millions)                      | Level 1 | Level 2 | Level 3 | Balances at<br>June 27, 2010 |
|------------------------------------|---------|---------|---------|------------------------------|
| <b>Assets</b>                      |         |         |         |                              |
| Marketable securities              | \$ 306  | \$      | \$      | \$ 306                       |
| Foreign currency forward contracts | 78      |         |         | 78                           |
| <b>Liabilities</b>                 |         |         |         |                              |
| Deferred compensation              | 197     |         |         | 197                          |
| Foreign currency forward contracts | 76      |         |         | 76                           |

| (In millions)                      | Level 1 | Level 2 | Level 3 | Balances at<br>Dec. 31,<br>2009 |
|------------------------------------|---------|---------|---------|---------------------------------|
| <b>Assets</b>                      |         |         |         |                                 |
| Marketable securities              | \$ 296  | \$      | \$      | \$ 296                          |
| Foreign currency forward contracts | 69      |         |         | 69                              |
| Retained Interest                  |         |         | 67      | 67                              |
| <b>Liabilities</b>                 |         |         |         |                                 |
| Deferred compensation              | 192     |         |         | 192                             |
| Foreign currency forward contracts | 33      |         |         | 33                              |

Activity related to our Retained Interest, which is reflected in discontinued operations, was as follows:

| (In millions)  | Six Months Ended |               |
|--|------------------|---------------|
|  | June 27, 2010    | June 28, 2009 |
| Balance at beginning of period                                     | \$ 67            | \$ 66         |
| Total gains (realized/unrealized)                                  |                  |               |
| Included in income (loss) from discontinued operations, net of tax |                  | 1             |
| Included in other comprehensive income (loss)                      |                  | (1)           |
| Transfers out  | (67)             |               |
| Balance at end of period   | \$               | \$ 66         |

**8. Derivative Financial Instruments**

Our primary market exposures are to interest rates and foreign exchange rates and we use certain derivative financial instruments to help manage these exposures. We execute these instruments with financial institutions we judge to be credit-worthy, and the majority of our foreign currency



forward contracts are denominated in currencies of major industrial countries. We do not hold or issue derivative financial instruments for trading or speculative purposes.

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**Cash flow hedges** - We enter into foreign currency forward contracts with commercial banks to fix the foreign currency exchange rates on specific commitments and payments to vendors, and customer receipts. Our foreign currency forward contracts are transaction driven and directly relate to a particular asset, liability or transaction for which commitments are in place. For foreign currency forward contracts designated and qualified for cash flow hedge accounting, we record the effective portion of the gain or loss on the derivative in accumulated other comprehensive loss (AOCL), net of tax, and reclassify it into earnings in the same period or periods during which the hedged revenue or cost of sales transaction affects earnings. We expect approximately \$1 million of after-tax net unrealized losses, included in AOCL at June 27, 2010, to be reclassified into earnings at then-current values over the next twelve months as the underlying hedged transactions occur. Realized gains and losses resulting from these cash flow hedges offset the foreign exchange gains and losses on the underlying transactions being hedged. Gains and losses on derivatives not designated for hedge accounting or representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized currently in cost of sales.

The fair value amounts of asset derivatives included in other assets, net and liability derivatives included in other accrued expenses in our consolidated balance sheets related to foreign currency forward contracts were as follows:

| (In millions)                                     | Asset Derivatives |               | Liability Derivatives |               |
|---|-------------------|---------------|-----------------------|---------------|
|   | June 27, 2010     | Dec. 31, 2009 | June 27, 2010         | Dec. 31, 2009 |
| Derivatives designated as hedging instruments     | \$ 52             | \$ 56         | \$ 49                 | \$ 23         |
| Derivatives not designated as hedging instruments | 26                | 13            | 27                    | 10            |
| <b>Total</b>                                      | <b>\$ 78</b>      | <b>\$ 69</b>  | <b>\$ 76</b>          | <b>\$ 33</b>  |

We recognized the following pretax gains (losses) related to foreign currency forward contracts designated as cash flow hedges:

| (In millions)  | Three Months Ended |               | Six Months Ended |               |
|--|--------------------|---------------|------------------|---------------|
|  | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| <b>Effective Portion</b>   |                    |               |                  |               |
| Gain (loss) recognized in AOCL   | \$ (16)            | \$ 44         | \$ (6)           | \$ 36         |
| Gain (loss) reclassified from AOCL to net sales                              | 1                  | (3)           | 1                | (7)           |
| Gain (loss) reclassified from AOCL to cost of sales                          | 5                  | (1)           | 23               | (18)          |
| <b>Amount excluded from effectiveness assessment and ineffective portion</b> |                    |               |                  |               |
| Gain (loss) recognized in cost of sales                                      | \$                 | \$            | \$               | \$            |

We recognized the following pretax losses related to foreign currency forward contracts not designated as cash flow hedges:

| (In millions)                           | Three Months Ended |               | Six Months Ended |               |
|---|--------------------|---------------|------------------|---------------|
|   | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Gain (loss) recognized in cost of sales | \$ (13)            | \$ (8)        | \$ (5)           | \$ (8)        |

**Fair value hedges** - We periodically enter into interest rate swap agreements with commercial and investment banks to manage interest rates associated with our financing arrangements. We terminated our interest rate swaps in the three months ended March 29, 2009 and collected cash of \$37 million related to the early termination. There were no interest rate swaps outstanding at June 27, 2010 and December 31, 2009.

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The notional amounts of outstanding foreign currency forward contracts consisted of the following at:

| (In millions)    | June 27, 2010   |               | Dec. 31, 2009 |               |
|------------------|-----------------|---------------|---------------|---------------|
|                  | Buy             | Sell          | Buy           | Sell          |
| British Pounds   | \$ 398          | \$ 330        | \$ 407        | \$ 498        |
| Canadian Dollars | 222             | 48            | 212           | 46            |
| Euros            | 188             | 24            | 190           | 35            |
| All other        | 195             | 78            | 176           | 53            |
| <b>Total</b>     | <b>\$ 1,003</b> | <b>\$ 480</b> | <b>\$ 985</b> | <b>\$ 632</b> |

Buy amounts represent the U.S. Dollar equivalent of commitments to purchase foreign currencies and sell amounts represent the U.S. Dollar equivalent of commitments to sell foreign currencies. Foreign currency forward contracts that do not involve U.S. Dollars have been converted to U.S. Dollars for disclosure purposes.

Our foreign currency forward contracts contain off-set, or netting provisions, to mitigate credit risk in the event of counterparty default, including payment default and cross default. As a result of these netting provisions we had no exposure at June 27, 2010. At June 28, 2009, these netting provisions effectively reduced our exposure to approximately \$26 million, which are spread across numerous highly rated counterparties.

**9. Commitments and Contingencies**

*Environmental Matters* - We are involved in various stages of investigation and cleanup related to remediation of various environmental sites. Our estimate of the liability of total environmental remediation costs includes the use of a discount rate and considers that a portion of these costs is eligible for future recovery through the pricing of our products and services to the U.S. Government. We consider such recovery probable based on government contracting regulations and our long history of receiving reimbursement for such costs and accordingly have recorded the estimated future recovery of these costs from the U.S. Government within contracts in process. Our estimates of total remediation costs, weighted average risk-free rate, total remediation costs - discounted and recoverable portion were as follows:

| (In millions, except percentages)      | June 27, 2010 | Dec. 31, 2009 |
|--|---------------|---------------|
| Total remediation costs - undiscounted | \$ 212        | \$ 208        |
| Weighted average risk-free rate        | 5.7%          | 5.7%          |
| Total remediation costs - discounted   | \$ 148        | \$ 139        |
| Recoverable portion                    | 107           | 97            |

We also lease certain government-owned properties and are generally not liable for remediation of preexisting environmental contamination at these sites; as a result, we generally do not reflect the provision for these costs in our financial statements. Due to the complexity of environmental laws and regulations, the varying costs and effectiveness of alternative cleanup methods and technologies, the uncertainty of insurance coverage and the unresolved extent of our responsibility, it is difficult to determine the ultimate outcome of these matters; however, we do not expect any additional liability to have a material adverse effect on our financial position, results of operations or liquidity.

*Financing Arrangements and Other* - We issue guarantees and banks and surety companies issue, on our behalf, letters of credit and surety bonds to meet various bid, performance, warranty, retention and advance payment obligations of us or our affiliates. These instruments expire on various dates through 2020. Additional guarantees of project performance for which there is no stated value also remain outstanding. The stated values outstanding at June 27, 2010 and December 31, 2009 were as follows:

| (In millions) | June 27, 2010 | Dec. 31, 2009 |
|---------------|---------------|---------------|
| Guarantees    | \$ 235        | \$ 227        |

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|                   |     |     |
|-------------------|-----|-----|
| Letters of Credit | 914 | 898 |
| Surety Bonds      | 199 | 203 |

Included in guarantees and letters of credit described above were \$88 million and \$235 million, respectively, at June 27, 2010, and \$80 million and \$206 million, respectively, at December 31, 2009, related to our joint venture in Thales-Raytheon Systems Co. Ltd. (TRS). We provide these guarantees and letters of credit to TRS and other affiliates to assist these entities in obtaining financing on more favorable terms, making bids on contracts and performing their contractual obligations. While we expect these entities to satisfy their loans, project performance and other contractual obligations, their failure to do so may result in a future obligation to us. At June 27, 2010 and December 31, 2009, we had an estimated liability of \$8 million and \$6 million, respectively, related to these guarantees and letters of credit. We periodically evaluate the risk of TRS and other affiliates failing to satisfy their loans, project

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performance and meet other contractual obligations described above. At June 27, 2010, we believe the risk that TRS and other affiliates will not be able to perform or meet their obligations is minimal for the foreseeable future based on their current financial condition. All obligations were current at June 27, 2010.

Our residual turbo-prop commuter aircraft portfolio has exposure to outstanding financing arrangements with the aircraft serving as collateral. We have sold and leased commuter aircraft globally to thinly capitalized companies, whose financial condition could be significantly affected by a number of factors, including fuel and other costs, industry consolidation, declining commercial aviation market conditions and the U.S. Government budget for the Essential Air Service program. Based on recent economic trends, including tightening credit markets and volatile fuel costs, these companies may increasingly experience difficulties meeting their financial commitments. At June 27, 2010 and December 31, 2009, our exposure on commuter aircraft assets held as inventory, collateral on notes or as leased assets, was approximately \$84 million relating to 88 aircraft and approximately \$109 million relating to 106 aircraft, respectively. The carrying value of our commuter aircraft portfolio assumes an orderly disposition of these assets, consistent with our historical experience and strategy. The tightening of credit markets and economic conditions have reduced the number of potential buyers who are able to obtain financing and have negatively impacted the ability of existing customers to refinance their aircraft through a third party. If the long-term market prospects for these aircraft were to significantly erode or cease, our valuation of these assets would likely be less than the carrying value. We periodically evaluate potential alternative strategies for the disposal of these assets. If we were to dispose of these assets in an other than orderly manner or sell the portfolio in its entirety, the value realized would likely be less than the carrying value.

In 1997, we provided a first loss guarantee of \$133 million on \$1.3 billion of U.S. Export-Import Bank loans (maturing in 2015) to the Brazilian Government related to Network Centric Systems System for the Vigilance of the Amazon (SIVAM) program. Loan repayments by the Brazilian Government were current at June 27, 2010.

Government contractors are subject to many levels of audit and investigation. Agencies that oversee contract performance include: the Defense Contract Audit Agency, the Inspector General of the Department of Defense and other departments and agencies, the Government Accountability Office, the Department of Justice and Congressional Committees. The Department of Justice has, from time to time, convened grand juries to investigate possible irregularities by us. We also provide products and services to customers outside of the U.S. and those sales are subject to local government laws, regulations and procurement policies and practices. Our compliance with such local government regulations or any applicable U.S. Government regulations (e.g., the Foreign Corrupt Practices Act and the International Traffic in Arms Regulations) may also be investigated or audited. We do not expect these audits and investigations to have a material adverse effect on our financial position, results of operations or liquidity, either individually or in the aggregate.

We are currently conducting a self-initiated internal review of certain of our international operations, focusing on compliance with the Foreign Corrupt Practices Act. In the course of the review, we have identified several possible areas of concern relating to payments made in connection with certain international operations related to a jurisdiction where we do business. We have voluntarily contacted the SEC and the Department of Justice to advise both agencies that an internal review is underway. Because the internal review is ongoing, we cannot predict the ultimate consequences of the review. Based on the information available to date, we do not believe that the results of this review will have a material adverse effect on our financial position, results of operations or liquidity.

In May 2006, international arbitration hearings commenced against us as the successor to the Hughes Electronics defense business, in connection with certain claims brought in 2004 relating to an alleged 1995 Workshare Agreement. The asserted claims involve breach of contract, intellectual property infringement and other related matters. The arbitration panel stayed further proceedings, including the issuance of the liability decision on the non-IP claims presented during the May 2006 hearing, while the parties engaged in settlement efforts. The parties were unable to conclude an enforceable settlement, and in August 2009, the panel released its liability decision, rejecting some of MBDA's non-IP claims, while finding Raytheon liable for some other non-IP claims. We did not record any significant additional financial liability as a result of our estimate of the impact of the decision. The proceedings will now resume to determine liability for the asserted IP claims and to assess overall damages, if any. We believe that we have meritorious defenses to the remaining asserted IP claims and intend to continue to contest them vigorously; however, an adverse resolution of this matter could have a material effect on our results of operations.

On July 22, 2010, Raytheon Systems Limited ( RSL ) was notified by the UK Border Agency that it had been terminated for default on a program. The termination notice included allegations that RSL had failed to perform on certain key milestones and other matters in addition to claims to recover certain losses incurred and previous payments made to RSL. We believe that RSL performed well and delivered substantial capabilities to the UK Border Agency under the program, which has been operating successfully and providing actionable information since live operations began in May 2009. As a result, we intend to pursue vigorously the collection of receivables for the program and damages in connection with the termination and defend ourselves against the UK Border Agency's claims for losses and previous payments.

Under the accounting requirements for subsequent events, we determined that the accounting impact of the termination notice was required to be reflected in our results for the period ended June 27, 2010. As a result, we are required to adjust our estimated amount of revenue and costs

under the program in the period ended June 27, 2010. The adjustment was based on our determination that certain assets were no longer expected to be recovered and for estimated costs for certain exit cost obligations under the contract and the estimated settlement of expected future subcontractor claims. The impact of the adjustment reduced Intelligence and Information Systems (IIS) total net sales and operating income by \$316 million and \$395 million in the three and six months ended June 27, 2010, respectively. At June 27, 2010, after the adjustment, we had approximately \$80 million in letters of credit and approximately \$30 million of billed and unbilled receivables remaining under the program for technology and services delivered, which we believe, are probable of recovery in litigation or arbitration. No amounts have been drawn down on the letters of credit. We currently do not believe it is probable that we are liable for losses, previous payments or other claims asserted by the UK Border Agency. It is reasonably possible that the ultimate amount of any resolution of the termination could be less or greater than our estimate due to the inherent uncertainties in litigation or arbitration. If we are unsuccessful in recovering amounts drawn on the letters of credit, fail to collect the billed and unbilled receivable balance or if we are required to make payments against claims or other losses asserted by the UK Border Agency or pay subcontractor claims in excess of our estimates, it could have a material adverse effect on our results of operations.

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In addition, various other claims and legal proceedings generally incidental to the normal course of business are pending or threatened against us. We do not expect any additional liability from these proceedings to have a material adverse effect on our financial position, results of operations or liquidity.

**10. Stockholders Equity**

On May 27, 2010, our stockholders approved the Raytheon 2010 Stock Plan (the Plan). Under the Plan, we may grant restricted stock awards, stock units, stock grants, stock options and stock appreciation rights.

Our repurchases of our common stock under our share repurchase programs were as follows:

| (In millions)               | Six Months Ended |               |
|-----------------------------|------------------|---------------|
|                             | June 27, 2010    | June 28, 2009 |
| Amount of stock repurchased | \$ 775           | \$ 600        |
| Shares of stock repurchased | 14.2             | 13.4          |

In October 2008, our Board of Directors authorized the repurchase of up to \$2.0 billion of our outstanding common stock. In March 2010, our Board of Directors authorized the repurchase of up to an additional \$2.0 billion of our outstanding common stock. At June 27, 2010 we had approximately \$2.1 billion available under these repurchase programs.

In March 2010, our Board of Directors authorized a 21% increase to our annual dividend payout rate from \$1.24 to \$1.50 per share. Our Board of Directors also declared two dividends totaling \$0.75 per share during the six months ended June 27, 2010, compared to two dividends totaling \$0.62 per share during the six months ended June 28, 2009. Dividends are subject to quarterly approval by our Board of Directors.

The changes in shares of our common stock outstanding for the six months ended June 27, 2010 were as follows:

| (In millions)                | Shares |
|------------------------------|--------|
| Balance at December 31, 2009 | 377.9  |
| Warrants exercised           | 6.7    |
| Stock plan activity          | 3.6    |
| Treasury stock repurchases   | (14.2) |
| Balance at June 27, 2010     | 374.0  |

**Earnings Per Share (EPS)**

We compute basic EPS attributable to Raytheon Company common stockholders by dividing income from continuing operations attributable to Raytheon Company common stockholders, income (loss) from discontinued operations attributable to Raytheon Company common stockholders and net income attributable to Raytheon Company, by our weighted-average common shares outstanding, including participating securities outstanding, as discussed below, during the period. Diluted EPS reflects the potential dilution beyond shares for basic EPS that could occur if securities or other contracts to issue common stock were exercised, converted into common stock or resulted in the issuance of common stock that would have shared in our earnings. We compute basic and diluted EPS using actual income from continuing operations attributable to Raytheon Company common stockholders, income (loss) from discontinued operations attributable to Raytheon Company common stockholders, net income attributable to Raytheon Company, and our actual weighted-average shares and participating securities outstanding rather than the numbers presented within our consolidated financial statements, which are rounded to the nearest million. As a result, it may not be possible to recalculate EPS as presented in our unaudited consolidated financial statements. Furthermore, it may not be possible to recalculate EPS attributable to Raytheon Company common stockholders by adjusting EPS from continuing operations by EPS from discontinued operations.

We include all unvested stock awards that contain non-forfeitable rights to dividends or dividend equivalents, whether paid or unpaid, in the number of shares outstanding in our basic and diluted EPS calculations. As a result, we have included all of our outstanding unvested restricted stock and Long-Term Performance Plan (LTPP) awards that meet the retirement eligible criteria in our calculation





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of basic and diluted EPS. We disclose EPS for common stock and unvested share-based payment awards, and separately disclose distributed and undistributed earnings. Distributed earnings represent common stock dividends and dividends earned on unvested share-based payment awards of retirement eligible employees. Undistributed earnings represent earnings that were available for distribution but were not distributed. Common stock and unvested share-based payment awards earn dividends equally, as shown in the table below.

EPS from continuing operations attributable to Raytheon Company common stockholders and unvested share-based payment awards was as follows:

|  | Three Months Ended |               | Six Months Ended |               |
|--|--------------------|---------------|------------------|---------------|
|  | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| <b>Basic EPS attributable to Raytheon Company common stockholders:</b>   |                    |               |                  |               |
| Distributed earnings   | \$ 0.37            | \$ 0.31       | \$ 0.75          | \$ 0.61       |
| Undistributed earnings   | 0.19               | 0.94          | 1.01             | 1.77          |
| Total  | \$ 0.56            | \$ 1.25       | \$ 1.76          | \$ 2.38       |
| <b>Diluted EPS attributable to Raytheon Company common stockholders:</b> |                    |               |                  |               |
| Distributed earnings   | \$ 0.37            | \$ 0.30       | \$ 0.73          | \$ 0.61       |
| Undistributed earnings   | 0.19               | 0.94          | 1.00             | 1.74          |
| Total  | \$ 0.56            | \$ 1.24       | \$ 1.73          | \$ 2.35       |

Basic and diluted EPS from discontinued operations attributable to Raytheon Company common stockholders and unvested share-based payment awards were losses of \$0.01 for the three months ended June 27, 2010 and June 28, 2009, and were losses of \$0.03 and less than \$0.01 for the six months ended June 27, 2010 and June 28, 2009, respectively. Earnings from discontinued operations were deemed undistributed for all periods presented.

The amount of income from continuing operations attributable to participating securities was \$4 million for the three months ended June 27, 2010 and \$8 million for the three months ended June 28, 2009 and \$11 million and \$13 million for the six months ended June 27, 2010 and June 28, 2009, respectively. The amount of income (loss) from discontinued operations attributable to participating securities was less than \$1 million for the three and six months ended June 27, 2010 and June 28, 2009. The amount of net income attributable to participating securities was \$3 million and \$7 million for the three months ended June 27, 2010 and June 28, 2009, respectively and \$10 million and \$13 million for the six months ended June 27, 2010 and June 28, 2009, respectively.

The weighted-average shares outstanding for basic and diluted EPS were as follows:

| (In millions)  | Three Months Ended |               | Six Months Ended |               |
|--|--------------------|---------------|------------------|---------------|
|  | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Shares for basic EPS (including 6.2 and 6.0 participating securities for the three months ended June 27, 2010 and June 28, 2009, respectively, and 6.0 and 5.7 for the six months ended June 27, 2010 and June 28, 2009, respectively) | 378.5              | 392.5         | 378.1            | 395.7         |
| Dilutive effect of stock options and LTTP  | 2.7                | 2.9           | 2.9              | 3.0           |
| Dilutive effect of warrants  | 1.9                | 1.9           | 2.7              | 1.9           |
| Shares for diluted EPS   | 383.1              | 397.3         | 383.7            | 400.6         |

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The following stock options with exercise prices that were less than the average market price were included in our calculations of EPS and stock options with exercise prices greater than the average market price were excluded from our calculations of EPS, as the effect of including them would be anti-dilutive:

| (In millions)                                   | Three Months Ended |               | Six Months Ended |               |
|---|--------------------|---------------|------------------|---------------|
|   | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Stock options included in calculations of EPS   | 6.9                | 6.1           | 6.9              | 10.8          |
| Stock options excluded from calculations of EPS |                    | 3.6           |                  | 2.6           |

Warrants to purchase 5.3 million and 12.0 million shares of our common stock that expire in June 2011, with an exercise price of \$37.50 per share, were outstanding and included in our calculations of diluted EPS at June 27, 2010 and June 28, 2009, respectively.

**Stock-based compensation plans**

Restricted stock activity for the six months ended June 27, 2010 was as follows:

| (In millions)                    | Shares |
|----------------------------------|--------|
| Outstanding at December 31, 2009 | 5.6    |
| Granted                          | 1.8    |
| Vested                           | (1.6)  |
| Outstanding at June 27, 2010     | 5.8    |

During the six months ended June 27, 2010 and June 28, 2009, we issued 0.8 million and 0.9 million shares, respectively, of our common stock in connection with the vesting of our 2007-2009 and 2006-2008 LTPP awards through treasury shares. During the same periods, we also granted our 2010-2012 and 2009-2011 LTPP awards with an aggregate target award of 0.4 million and 0.5 million units, respectively.

The performance goals for the 2010-2012 LTPP award are independent of each other and based on three metrics, as defined in the award agreements: return on invested capital, weighted at 50%; total shareholder return relative to a peer group, weighted at 25%; and cumulative free cash flow, weighted at 25%. The ultimate award, which is determined at the end of the three-year cycle, can range from zero to 200% of the target award and includes dividend equivalents, which are not included in the aggregate target award numbers.

**Other comprehensive income (loss)**

Other comprehensive income (loss) generally includes amortization of unfunded pension benefit obligation, foreign exchange translation adjustments and gains and losses on effective cash flow hedges. The computation of other comprehensive income (loss) was as follows:

| (In millions)                                       | Three Months Ended |               | Six Months Ended |               |
|---|--------------------|---------------|------------------|---------------|
|   | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Net income  | \$ 215             | \$ 501        | \$ 668           | \$ 961        |
| Other comprehensive income (loss), net of tax:      |                    |               |                  |               |
| Amortization of unfunded pension benefit obligation | 91                 | 61            | 181              | 122           |
| Foreign exchange translation adjustments            | (21)               | 78            | (48)             | 59            |
| Cash flow hedges                                    | (14)               | 32            | (19)             | 40            |
| Other, net  |                    | (1)           | (2)              | (1)           |
| Total other comprehensive income (loss), net of tax | 56                 | 170           | 112              | 220           |
| Comprehensive income (loss)                         | 271                | 671           | 780              | 1,181         |
|   | 7                  | 12            | 15               | 20            |

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Less: Comprehensive income (loss) attributable to noncontrolling interests  
in subsidiaries

|  |        |        |        |          |
|--|--------|--------|--------|----------|
| Comprehensive income (loss) attributable to Raytheon Company | \$ 264 | \$ 659 | \$ 765 | \$ 1,161 |
|--|--------|--------|--------|----------|

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We have pension plans covering the majority of our employees, including certain employees in foreign countries. We also provide certain health care and life insurance benefits to retired employees through other postretirement benefit plans.

The components of net periodic pension expense were as follows:

| (In millions)                      | Three Months Ended |               | Six Months Ended |               |
|------------------------------------|--------------------|---------------|------------------|---------------|
|                                    | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Service cost                       | \$ 109             | \$ 101        | \$ 218           | \$ 201        |
| Interest cost                      | 263                | 256           | 525              | 513           |
| Expected return on plan assets     | (304)              | (308)         | (609)            | (615)         |
| Amortization of prior service cost | 3                  | 4             | 6                | 7             |
| Recognized net actuarial loss      | 144                | 100           | 289              | 200           |
| Net periodic pension expense       | \$ 215             | \$ 153        | \$ 429           | \$ 306        |

Our net periodic pension expense included expense from foreign benefit plans of \$5 million in the three months ended June 27, 2010 and June 28, 2009, and \$10 million and \$9 million in the six months ended June 27, 2010 and June 28, 2009, respectively.

The components of net periodic cost (income) related to our other postretirement benefit plans were as follows:

| (In millions)                      | Three Months Ended |               | Six Months Ended |               |
|------------------------------------|--------------------|---------------|------------------|---------------|
|                                    | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Service cost                       | \$ 2               | \$ 3          | \$ 5             | \$ 5          |
| Interest cost                      | 12                 | 14            | 24               | 27            |
| Expected return on plan assets     | (8)                | (8)           | (15)             | (15)          |
| Amortization of transition asset   | 1                  | 1             | 2                | 2             |
| Amortization of prior service cost | (12)               | (13)          | (23)             | (26)          |
| Recognized net actuarial loss      | 2                  | 1             | 3                | 3             |
| Net periodic cost (income)         | \$ (3)             | \$ (2)        | \$ (4)           | \$ (4)        |

Long-term pension and other postretirement benefit plan liabilities were \$4,271 million and \$423 million, respectively, at June 27, 2010, and \$4,668 million and \$421 million, respectively, at December 31, 2009.

We make both required and discretionary contributions to our pension plans. Required contributions are primarily determined under the Employee Retirement Income Security Act of 1974 (ERISA) and are affected by the actual return on plan assets and plan funded status. We made required contributions of \$584 million and \$569 million during the six months ended June 27, 2010 and June 28, 2009, respectively, to our pension and other postretirement benefit plans. For the full-year 2010, we expect to make required contributions of approximately \$1.1 billion to our pension plans and \$30 million to our other postretirement benefit plans. We did not make any discretionary contributions to our pension plans during the six months ended June 27, 2010 and June 28, 2009, however we periodically evaluate whether to make discretionary contributions. As discretionary contributions are made, a funding credit is accumulated, which we can use to offset future calculated required contributions. The funding credit for our pension plans was \$2.6 billion at December 31, 2009. Because our expected 2010 contributions are based on the minimum required, we do not anticipate a significant increase or decrease in our funding credit at December 31, 2010.

**12. Income Taxes**

We are subject to income taxes in the U.S. and numerous foreign jurisdictions. IRS examinations of our tax returns have been completed through 2005. Reports by the IRS Appeals Division resolving benefits claimed under the Foreign Sales Corporation (FSC) and Extraterritorial Income (ETI) exclusion regimes, revenue recognition items, the deductibility of certain expenses, tax credits and certain other tax matters related to the

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1998-2005 tax years are being reviewed by the Joint Committee on Taxation. The IRS has commenced its examination of the 2006-2008 tax years. Additionally, we are under audit by multiple state and foreign tax authorities. State tax liabilities are routinely adjusted to account for any changes in federal taxable income.

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We believe that our income tax reserves are adequate; however, amounts asserted by taxing authorities could be greater than amounts accrued and reflected in our consolidated balance sheets. Accordingly, we could record additional amounts for federal, foreign and state tax-related liabilities in the future as we revise estimates or as we settle or otherwise resolve the underlying matters.

The balance of our unrecognized tax benefits at June 27, 2010 and June 28, 2009, exclusive of interest, was \$376 million and \$415 million, respectively, of which \$366 million and \$315 million, respectively, would affect our earnings if recognized. We accrue interest and penalties related to unrecognized tax benefits in tax expense. During the three months ended June 27, 2010, we filed an accounting method change with the IRS which reduced our unrecognized tax benefits and related accrued interest. Primarily as a result of the accounting method change, in the six months ended June 27, 2010, we recorded \$9 million of income related to gross interest and penalties, which, net of the federal tax liability was \$6 million. In the six months ended June 28, 2009, we recorded \$11 million of gross interest and penalties which, net of the federal tax benefit was \$7 million. At June 27, 2010 and December 31, 2009, we had \$113 million and \$123 million, respectively, of interest and penalties accrued related to unrecognized tax benefits, which, net of the federal tax benefit, was approximately \$74 million and \$80 million, respectively. In the ordinary course of business, we may take new tax positions that could increase or decrease our unrecognized tax benefits in future periods.

A rollforward of our unrecognized tax benefits was as follows:

| (In millions)                                    | Six Months Ended |               |
|--|------------------|---------------|
|  | June 27, 2010    | June 28, 2009 |
| Unrecognized tax benefits at beginning of period | \$ 469           | \$ 415        |
| Additions based on current year tax positions    | 1                |               |
| Additions based on prior year tax positions      | 1                |               |
| Reductions based on prior year tax positions     | (95)             |               |
| Unrecognized tax benefits at end of period       | \$ 376           | \$ 415        |

Based on the outcome of the Joint Committee on Taxation review of the 1998-2005 tax years and the expiration of the statute of limitations, it is reasonably possible that within the next 12 months our unrecognized tax benefits, exclusive of interest, will decrease by approximately \$195 million to \$225 million, of which approximately \$185 million to \$203 million could decrease our tax expense.

We generally account for our state income tax expense as a deferred contract cost, as we can generally recover this expense through the pricing of our products and services to the U.S. Government. We include this deferred contract cost in contracts in process until allocated to our contracts, which generally occurs upon payment or when otherwise agreed as allocable with the U.S. Government. Net state income tax expense allocated to our contracts was \$4 million and \$12 million in the three months ended June 27, 2010 and June 28, 2009, respectively and \$35 million and \$30 million in the six months ended June 27, 2010 and June 28, 2009, respectively. We include state income tax expense allocated to our contracts in administrative and selling expenses.

We recorded a non-current deferred tax asset of \$121 million as a result of the UK Border Agency program, on which RSL was notified of its termination, as previously discussed. We believe that we will have sufficient taxable income to realize this deferred tax asset. In general, any net operating losses generated in the United Kingdom may be carried forward indefinitely.

**13. Business Segment Reporting**

Our reportable segments, organized based on capabilities and technologies, are: Integrated Defense Systems, Intelligence and Information Systems, Missile Systems, Network Centric Systems, Space and Airborne Systems and Technical Services. Segment net sales and operating income generally include intersegment sales and profit recorded at cost plus a specified fee, which may differ from what the selling entity would be able to obtain on sales to external customers. Corporate and eliminations includes corporate expenses and intersegment sales and profit eliminations. Corporate expenses represent unallocated costs and certain other corporate costs not considered part of management's evaluation of reportable segment operating performance, including the net costs associated with our residual turbo-prop commuter aircraft portfolio.

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| Total Net Sales (In millions)        | Three Months Ended |               | Six Months Ended |               |
|--------------------------------------|--------------------|---------------|------------------|---------------|
|                                      | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Integrated Defense Systems           | \$ 1,352           | \$ 1,335      | \$ 2,688         | \$ 2,597      |
| Intelligence and Information Systems | 472                | 812           | 1,202            | 1,596         |
| Missile Systems                      | 1,415              | 1,384         | 2,776            | 2,752         |
| Network Centric Systems              | 1,205              | 1,197         | 2,381            | 2,351         |
| Space and Airborne Systems           | 1,197              | 1,136         | 2,292            | 2,182         |
| Technical Services                   | 834                | 780           | 1,635            | 1,476         |
| Corporate and Eliminations           | (502)              | (519)         | (948)            | (945)         |
| Total                                | \$ 5,973           | \$ 6,125      | \$ 12,026        | \$ 12,009     |

| Intersegment Sales (In millions)     | Three Months Ended |               | Six Months Ended |               |
|--------------------------------------|--------------------|---------------|------------------|---------------|
|                                      | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Integrated Defense Systems           | \$ 28              | \$ 39         | \$ 52            | \$ 73         |
| Intelligence and Information Systems | 4                  | 5             | 9                | 9             |
| Missile Systems                      | 29                 | 5             | 46               | 8             |
| Network Centric Systems              | 124                | 145           | 231              | 235           |
| Space and Airborne Systems           | 141                | 170           | 274              | 312           |
| Technical Services                   | 186                | 168           | 348              | 324           |
| Total                                | \$ 512             | \$ 532        | \$ 960           | \$ 961        |

| Operating Income (In millions)       | Three Months Ended |               | Six Months Ended |               |
|--------------------------------------|--------------------|---------------|------------------|---------------|
|                                      | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Integrated Defense Systems           | \$ 221             | \$ 205        | \$ 431           | \$ 393        |
| Intelligence and Information Systems | (329)              | 66            | (279)            | 127           |
| Missile Systems                      | 164                | 147           | 322              | 305           |
| Network Centric Systems              | 166                | 170           | 331              | 333           |
| Space and Airborne Systems           | 171                | 175           | 330              | 314           |
| Technical Services                   | 73                 | 53            | 140              | 97            |
| FAS/CAS Pension Adjustment           | (55)               | 11            | (108)            | 22            |
| Corporate and Eliminations           | (66)               | (62)          | (113)            | (114)         |
| Total                                | \$ 345             | \$ 765        | \$ 1,054         | \$ 1,477      |

The components of operating income related to Corporate and Eliminations were as follows:

| (In millions)                    | Three Months Ended |               | Six Months Ended |               |
|----------------------------------|--------------------|---------------|------------------|---------------|
|                                  | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Intersegment profit eliminations | \$ (48)            | \$ (45)       | \$ (87)          | \$ (78)       |
| Corporate                        | (18)               | (17)          | (26)             | (36)          |
| Total                            | \$ (66)            | \$ (62)       | \$ (113)         | \$ (114)      |

The FAS/CAS Pension Adjustment, which we report as a separate line item in our segment results above, represents the difference between our pension expense or income under financial accounting standards (FAS) in accordance with GAAP and our pension expense under U.S. Government Cost Accounting Standards (CAS). GAAP outlines the methodology used to determine pension expense or income for financial reporting purposes, which is not necessarily indicative of the funding requirements for pension plans that we determine by other factors. CAS

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prescribes the allocation to and recovery of pension costs on U.S. Government contracts. The results of each segment only include pension expense as determined under CAS that we generally recover through the pricing of our products and services to the U.S. Government.



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| <b>Intersegment Operating Income (In millions)</b> | <b>Three Months Ended</b> |                      | <b>Six Months Ended</b> |                      |
|--|---------------------------|----------------------|-------------------------|----------------------|
|  | <b>June 27, 2010</b>      | <b>June 28, 2009</b> | <b>June 27, 2010</b>    | <b>June 28, 2009</b> |
| Integrated Defense Systems                         | \$ 2                      | \$ 2                 | \$ 4                    | \$ 4                 |
| Intelligence and Information Systems               | 1                         | 1                    | 1                       | 1                    |
| Missile Systems                                    | 3                         | 1                    | 6                       | 1                    |
| Network Centric Systems                            | 10                        | 13                   | 18                      | 20                   |
| Space and Airborne Systems                         | 14                        | 14                   | 25                      | 25                   |
| Technical Services                                 | 18                        | 14                   | 33                      | 27                   |
| <b>Total</b>                                       | <b>\$ 48</b>              | <b>\$ 45</b>         | <b>\$ 87</b>            | <b>\$ 78</b>         |

| <b>Identifiable Assets (In millions)</b> | <b>June 27, 2010</b> | <b>Dec. 31, 2009</b> |
|--|----------------------|----------------------|
| Integrated Defense Systems               | \$ 1,910             | \$ 1,943             |
| Intelligence and Information Systems     | 2,164                | 2,391                |
| Missile Systems                          | 4,995                | 4,858                |
| Network Centric Systems                  | 4,234                | 4,199                |
| Space and Airborne Systems               | 4,303                | 4,236                |
| Technical Services                       | 1,316                | 1,340                |
| Corporate                                | 4,359                | 4,640                |
| <b>Total</b>                             | <b>\$ 23,281</b>     | <b>\$ 23,607</b>     |

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With respect to the unaudited consolidated financial information of Raytheon Company for the three and six months ended June 27, 2010 and June 28, 2009, PricewaterhouseCoopers LLP (PricewaterhouseCoopers) reported that it has applied limited procedures in accordance with professional standards for a review of such information. Its report dated July 29, 2010, appearing below, states that the firm did not audit and does not express an opinion on that unaudited consolidated financial information. Accordingly, the degree of reliance on its report on such information should be restricted in light of the limited nature of the review procedures applied. PricewaterhouseCoopers is not subject to the liability provisions of Section 11 of the Securities Act of 1933 (the Act) for its report on the unaudited consolidated financial information because that report is not a report or a part of a registration statement prepared or certified by PricewaterhouseCoopers within the meaning of Sections 7 and 11 of the Act.

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of Raytheon Company:

We have reviewed the accompanying consolidated balance sheet of Raytheon Company and its subsidiaries as of June 27, 2010, and the related consolidated statements of operations for the three and six month periods ended June 27, 2010 and June 28, 2009 and the consolidated statements of cash flows for the six month periods ended June 27, 2010 and June 28, 2009. This interim financial information is the responsibility of the Company's management.

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

Based on our review, we are not aware of any material modifications that should be made to the accompanying consolidated interim financial information for it to be in conformity with accounting principles generally accepted in the United States of America.

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2009, and the related consolidated statements of operations, equity, and of cash flows for the year then ended (not presented herein), and in our report dated February 24, 2010, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet information as of December 31, 2009, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP  
PricewaterhouseCoopers LLP  
Boston, Massachusetts  
July 29, 2010

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## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

**Overview**

We develop technologically advanced, integrated products, services and solutions in four core defense markets: Sensing; Effects; Command, Control, Communications and Intelligence (C3I); Mission Support, as well as the Cybersecurity and Homeland Security markets. We serve both domestic and international customers, principally as a prime contractor on a broad portfolio of defense and related programs for government customers.

We operate in six segments: Integrated Defense Systems (IDS), Intelligence and Information Systems (IIS), Missile Systems (MS), Network Centric Systems (NCS), Space and Airborne Systems (SAS) and Technical Services (TS). For a more detailed description of our segments, see Business Segments within Item 1 of our Annual Report on Form 10-K for the year ended December 31, 2009.

The following discussion should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2009 and our unaudited consolidated financial statements included in this Quarterly Report on Form 10-Q.

**Consolidated Results of Operations**

As discussed in our Cautionary Note Regarding Forward-Looking Statements on page 3 of this Form 10-Q, our interim period results of operations and period-to-period comparisons of such results, particularly at a segment level, may not be indicative of our future operating results. Additionally, we use a fiscal calendar, which may cause the number of workdays in the current and comparable prior interim period to differ and could affect period-to-period comparisons. There were 64 workdays in the second quarters of 2010 and 2009 and 124 workdays in the first six months of 2010 compared to 125 workdays in the first six months of 2009. The following discussions of comparative results among periods should be viewed in this context.

As discussed in Note 1: Basis of Presentation within Item 1 of this Form 10-Q, we prepared the accompanying unaudited consolidated financial statements of Raytheon Company on the same basis as our annual audited consolidated financial statements, except for the adoption of required new accounting standards in the first six months of 2010 related to the accounting and disclosure requirements for transfers of financial assets and consolidation of variable interest entities (VIEs).

Selected consolidated results were as follows:

| (In millions, except percentages and per share data)   | Three Months Ended |               | % of Total Net Sales<br>Three Months Ended |               |
|--|--------------------|---------------|--|---------------|
|  | June 27, 2010      | June 28, 2009 | June 27, 2010                              | June 28, 2009 |
| Net sales  |                    |               |  |               |
| Products   | \$ 5,079           | \$ 5,365      | 85.0%                                      | 87.6%         |
| Services   | 894                | 760           | 15.0%                                      | 12.4%         |
| Total net sales  | 5,973              | 6,125         | 100.0%                                     | 100.0%        |
| Operating expenses                                     |                    |               |  |               |
| Cost of sales-products                                 | 4,245              | 4,184         | 71.1%                                      | 68.3%         |
| Cost of sales-services                                 | 793                | 655           | 13.3%                                      | 10.7%         |
| Administrative and selling expenses                    | 414                | 370           | 6.9%                                       | 6.0%          |
| Research and development expenses                      | 176                | 151           | 2.9%                                       | 2.5%          |
| Total operating expenses                               | 5,628              | 5,360         | 94.2%                                      | 87.5%         |
| Operating income                                       | 345                | 765           | 5.8%                                       | 12.5%         |
| Non-operating (income) expense                         |                    |               |  |               |
| Interest expense                                       | 33                 | 31            | 0.6%                                       | 0.5%          |
| Interest income  | (4)                | (3)           | -0.1%                                      | %             |
| Other (income) expense                                 | 6                  | (13)          | 0.1%                                       | -0.2%         |
| Total Non-operating (income) expense                   | 35                 | 15            | 0.6%                                       | 0.2%          |
| Federal and foreign income taxes                       | 91                 | 246           | 1.5%                                       | 4.0%          |
| Income from continuing operations                      | 219                | 504           | 3.7%                                       | 8.2%          |
| Income (loss) from discontinued operations, net of tax | (4)                | (3)           | -0.1%                                      | %             |
| Net income   | 215                | 501           | 3.6%                                       | 8.2%          |

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|  |         |         |      |      |
|--|---------|---------|------|------|
| Less: Net income (loss) attributable to noncontrolling interests in subsidiaries                           | 7       | 12      | 0.1% | 0.2% |
| Net income attributable to Raytheon Company  | \$ 208  | \$ 489  | 3.5% | 8.0% |
| Diluted earnings per share from continuing operations attributable to Raytheon Company common stockholders | \$ 0.56 | \$ 1.24 |      |      |
| Diluted earnings per share attributable to Raytheon Company common stockholders                            | 0.55    | 1.23    |      |      |

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| (In millions, except percentages and per share data)   | Six Months Ended |               | % of Total Net Sales<br>Six Months Ended |               |
|--|------------------|---------------|--|---------------|
|  | June 27, 2010    | June 28, 2009 | June 27, 2010                            | June 28, 2009 |
| Net sales  |                  |               |  |               |
| Products   | \$ 10,282        | \$ 10,543     | 85.5%                                    | 87.8%         |
| Services   | 1,744            | 1,466         | 14.5%                                    | 12.2%         |
| Total net sales  | 12,026           | 12,009        | 100.0%                                   | 100.0%        |
| Operating expenses   |                  |               |  |               |
| Cost of sales-products   | 8,307            | 8,277         | 69.1%                                    | 68.9%         |
| Cost of sales-services   | 1,515            | 1,259         | 12.6%                                    | 10.5%         |
| Administrative and selling expenses  | 822              | 734           | 6.8%                                     | 6.1%          |
| Research and development expenses  | 328              | 262           | 2.7%                                     | 2.2%          |
| Total operating expenses   | 10,972           | 10,532        | 91.2%                                    | 87.7%         |
| Operating income   | 1,054            | 1,477         | 8.8%                                     | 12.3%         |
| Non-operating (income) expense   |                  |               |  |               |
| Interest expense   | 65               | 63            | 0.5%                                     | 0.5%          |
| Interest income  | (7)              | (7)           | -0.1%                                    | -0.1%         |
| Other (income) expense   | 5                | (8)           | %  | -0.1%         |
| Total Non-operating (income) expense   | 63               | 48            | 0.5%                                     | 0.4%          |
| Federal and foreign income taxes   | 311              | 468           | 2.6%                                     | 3.9%          |
| Income from continuing operations  | 680              | 961           | 5.7%                                     | 8.0%          |
| Income (loss) from discontinued operations, net of tax   | (12)             |               | -0.1%                                    | %             |
| Net income   | 668              | 961           | 5.6%                                     | 8.0%          |
| Less: Net income (loss) attributable to noncontrolling interests in subsidiaries                           | 15               | 20            | 0.1%                                     | 0.2%          |
| Net income attributable to Raytheon Company  | \$ 653           | \$ 941        | 5.4%                                     | 7.8%          |
| Diluted earnings per share from continuing operations attributable to Raytheon Company common stockholders | \$ 1.73          | \$ 2.35       |  |               |
| Diluted earnings per share attributable to Raytheon Company common stockholders                            | 1.70             | 2.35          |  |               |
| <b>Total Net Sales</b>   |                  |               |  |               |

The decrease in total net sales of \$152 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to lower external net sales of \$339 million at IIS, partially offset by higher external net sales of \$90 million at SAS, \$36 million at TS, \$29 million at NCS and \$28 million at IDS. The decrease in external net sales at IIS was primarily due to a \$316 million adjustment, in accordance with percentage-of-completion accounting, from a change in our estimated revenue and costs on a build and design phase, of a UK Border Agency program, on which Raytheon Systems Limited ( RSL ) was notified of its termination, as discussed in Commitments and Contingencies on page 42. The increase in external net sales at SAS was primarily due to higher volume, as planned, as work increased on certain classified business awarded in the first half of 2009. The increase in external net sales at TS was primarily due to higher net sales from growth on training programs, principally domestic and foreign training programs supporting the U.S. Army's Warfighter Field Operations Customer Support (FOCUS) activities. The increase in external net sales at NCS was primarily due to higher net sales related to Raytheon BBN Technologies (BBN), which we acquired in the fourth quarter of 2009, partially offset by lower net sales on certain U.S. Army programs. The increase in external net sales at IDS was primarily due to higher net

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sales on Patriot programs, principally from higher net sales on an international Patriot program awarded in the fourth quarter of 2008. The decrease in product net sales of \$286 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to lower external product net sales of \$355 million at IIS principally due to the UK Border Agency program, on which RSL was notified of its termination, as previously discussed, partially offset by higher external product net sales of \$64 million at SAS. The increase in service net sales of \$134 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to higher external service net sales of \$60 million at TS, \$34 million at NCS and \$27 million at SAS.

Sales to the U.S. Department of Defense (DoD) were 90% and 86% of total net sales in the second quarters of 2010 and 2009, respectively. Sales to the U.S. Government were 94% and 90% of total net sales in the second quarters of 2010 and 2009, respectively. Included in both DoD and U.S. Government sales were foreign military sales through the U.S. Government of \$786 million and \$624 million in the second quarters of 2010 and 2009, respectively. Total international sales, including foreign military sales, were \$1,200 million or 20.1% of total net sales in the second quarter of 2010 compared to \$1,239 million or 20.2% of total net sales in the second quarter of 2009.

The increase in total net sales of \$17 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to higher external sales of \$148 million at SAS, \$135 million at TS and \$112 million at IDS and \$34 million at NCS, partially offset by lower external net sales of \$394 million at IIS. The increase in external net sales at SAS was primarily due to higher volume, as planned, as work increased on certain classified business awarded in the first half of 2009. The increase in external net sales at TS was primarily due to higher net sales from growth on training programs, principally domestic and foreign training programs supporting the U.S. Army's Warfighter FOCUS activities. The increase in external net sales at IDS was primarily due to higher net sales on Patriot programs, principally from higher net sales on an international Patriot program awarded in the fourth quarter of 2008. The decrease in external net sales at IIS was primarily due to the change in our estimated revenue and costs on the UK Border Agency program, on which RSL was notified of its termination, as previously discussed. The decrease in product net sales of \$261 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to lower external product net sales of \$419 million at IIS principally due to the UK Border Agency program, on which RSL was notified of its termination, as previously discussed, offset by higher external product net sales of \$114 million at IDS and \$105 million at SAS. The increase in service net sales of \$278 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to higher external service net sales of \$150 million at TS, \$63 million at NCS and \$25 million at IDS.

Sales to the U.S. Department of Defense (DoD) were 88% and 85% of total net sales in the first six months of 2010 and 2009, respectively. Sales to the U.S. Government were 92% and 89% of total net sales in the first six months of 2010 and 2009, respectively. Included in both DoD and U.S. Government sales were foreign military sales through the U.S. Government of \$1,580 million and \$1,194 million in the first six months of 2010 and 2009, respectively. Total international sales, including foreign military sales, were \$2,586 million or 21.5% of total net sales in the first six months of 2010 compared to \$2,393 million or 19.9% of total net sales in the first six months of 2009.

**Cost of Sales**

The increase in cost of sales of \$199 million in the second quarter of 2010 compared to the second quarter of 2009 was due to \$133 million of increased costs, including \$79 million on the UK Border Agency program, on which RSL was notified of its termination, as discussed under IIS in Segment Results below and higher expense of \$66 million related to the FAS/CAS Pension Adjustment discussed below. The primary drivers of the remaining increase in cost of sales are discussed above in Total Net Sales and in Segment Results below.

The increase in cost of sales of \$286 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$156 million of increased costs, including \$79 million on the UK Border Agency program, on which RSL was notified of its termination, as discussed under IIS in Segment Results below and higher expense of \$130 million related to the FAS/CAS Pension Adjustment discussed below. The primary drivers of the remaining increase in cost of sales are discussed above in Total Net Sales and in Segment Results below.

The FAS/CAS Pension Adjustment, which was \$55 million of expense in the second quarter of 2010 compared to \$11 million of income in the second quarter of 2009, and \$108 million of expense in the first six months of 2010 compared to \$22 million of income in the first six months of 2009 is reported as a separate line item in our segment results. The FAS/CAS Pension Adjustment represents the difference between our pension expense or income under financial accounting standards (FAS) in accordance with U.S. Generally Accepted Accounting Principles (GAAP) and our pension expense under U.S. Government Cost Accounting Standards (CAS). The results of each segment only include pension expense under CAS that we generally recover through the pricing of our products and services to the U.S. Government. For more information on the FAS/CAS Pension Adjustment, see our discussion below in Segment Results.

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### **Administrative and Selling Expenses**

The increase in administrative and selling expenses of \$44 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to \$28 million of higher expenses related to: outside professional services; BBN which we acquired in the fourth quarter of 2009; selling expenses; and various information technology systems initiatives.

The increase in administrative and selling expenses of \$88 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$56 million of higher expenses related to: selling expenses; BBN which we acquired in the fourth quarter of 2009; outside professional services; various information technology systems initiatives; and state income taxes. The provision for state income taxes can generally be recovered through the pricing of products and services to the U.S. Government and was \$35 million and \$30 million in the six months ended June 27, 2010 and June 28, 2009, respectively. We expect administrative and selling expenses as a percentage of total net sales for the full-year 2010 to be relatively consistent with 2009.

### **Research and Development Expenses**

The increases in research and development expenses of \$25 million in the second quarter of 2010 compared to the second quarter of 2009 and \$66 million in the first six months of 2010 compared to the first six months of 2009 were primarily due to the timing of our expenditures related to numerous Company-sponsored research and development projects. We expect research and development expenses as a percentage of total net sales for the full-year 2010 to be relatively consistent with 2009.

### **Total Operating Expenses**

The increase in total operating expenses of \$268 million in the second quarter of 2010 compared to the second quarter of 2009 was due to \$133 million of increased cost of sales including \$79 million of higher operating expenses on the UK Border Agency program, on which RSL was notified of its termination, as discussed under IIS in Segment Results below, higher expense of \$66 million related to the FAS/CAS Pension Adjustment, \$44 million of higher administrative and selling expenses and \$25 million of higher research and development expenses, all as discussed above.

The increase in total operating expenses of \$440 million in the first six months of 2010 compared to the first six months of 2009 was due to \$156 million of increased cost of sales including \$79 million of higher operating expenses on the UK Border Agency program, on which RSL was notified of its termination, as discussed under IIS in Segment Results below, higher expense of \$130 million related to the FAS/CAS Pension Adjustment, \$88 million of higher administrative and selling expenses and \$66 million of higher research and development expenses, all as discussed above.

In accordance with GAAP, pension and other postretirement benefit assets and liabilities are valued annually at the end of the year for purposes of determining funded status and future year pension expense. Our long-term return on assets and discount rate assumptions are key variables in making such determinations and are discussed in more detail under Critical Accounting Estimates within Item 7 of our Form 10-K for the year ended December 31, 2009. The pro-rated return on assets through June 27, 2010 was below our annual return assumption of 8.75% at December 31, 2009. If the actual rate of return on plan assets were to be below our assumed rate of return through December 31, 2010, it would negatively impact our funded status at year-end and increase pension expense in future years. Additionally, the corporate bond yield environment as of June 27, 2010 was below our discount rate assumption of 6.25% at December 31, 2009. If the actual bond yield environment were to be below our assumed rate at December 31, 2010, it would result in a lower discount rate than our discount rate assumption at December 31, 2009 and negatively impact our funded status at year-end. The ultimate impact on our future pension expense and funded status will be based upon market conditions in effect when we perform our annual valuation for the December 31, 2010 financial statements.

### **Operating Income**

The decrease in operating income of \$420 million in the second quarter of 2010 compared with the second quarter of 2009 was primarily due to the \$395 million adjustment from a change in our estimated revenue and costs on the UK Border Agency program, on which RSL was notified of its termination, as previously discussed and higher expense of \$66 million related to the FAS/CAS Pension Adjustment. These decreases were partially offset by increased volume, which had an impact of approximately \$30 million, the primary drivers of which are discussed in Segment Results below.

The decrease in operating income of \$423 million in the first six months of 2010 compared with the first six months of 2009 was primarily due to the \$395 million adjustment from a change in our estimated revenue and costs on the UK Border Agency program, on which RSL was notified of its termination, as previously discussed and higher expense of \$130 million related to the FAS/CAS Pension Adjustment. These

decreases were partially offset by increased volume, which had an impact of approximately \$50 million, the primary drivers of which are discussed in Segment Results below.

**Non-Operating Expense, Net**

The increase in non-operating expense, net of \$20 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to a \$17 million year over year change in the fair value of investments held in rabbi trusts associated with certain of our non-qualified deferred compensation plans due to net losses of \$2 million in the second quarter of 2010 compared to net gains of \$15 million in the second quarter of 2009.



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The increase in non-operating expense, net of \$15 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to a \$9 million year over year change in the fair value of investments held in rabbi trusts associated with certain of our non-qualified deferred compensation plans due to net gains of \$2 million in the first six months of 2010 compared to net gains of \$11 million in the first six months of 2009.

**Federal and Foreign Income Taxes**

Our effective tax rate reflects the 35% U.S. statutory rate adjusted for various permanent differences between book and tax reporting. Our effective tax rates in the second quarter of 2010 and 2009 were 29.4% and 32.8%, respectively. The 3.4% decrease was primarily due to increased manufacturing tax benefits and a reduction in interest liability on an uncertain tax benefit of approximately 4.7% and 4.3%, respectively, and was offset by decreases of approximately 4.5% due to the change in the mix of jurisdictional income, as a result of the UK Border Agency program, on which RSL was notified of its termination, as previously discussed and the expiration of the research and development tax credit of approximately 1.0%. Our effective tax rates in the first six months of 2010 and 2009 were 31.4% and 32.8%, respectively. The 1.4% decrease was primarily due to increased manufacturing tax benefits and a reduction in interest liability on an uncertain tax benefit of approximately 2.0% and 1.4%, respectively, and was partially offset by the expiration of the research and development tax credit of approximately 1.0%.

**Diluted Earnings per Share from Continuing Operations Attributable to Raytheon Company Common Stockholders**

The decreases in diluted earnings per share from continuing operations attributable to Raytheon Company common stockholders of \$0.68 in the second quarter of 2010 compared to the second quarter of 2009 and \$0.62 in the first six months of 2010 compared to the first six months of 2009 was primarily due to the \$0.71 and \$0.72 per share impacts in the second quarter and first six months of 2010, respectively, of the adjustment from a change in our estimated revenue and costs on the UK Border Agency program, on which RSL was notified of its termination, as previously discussed and the FAS/CAS Pension Adjustment, partially offset by operational improvements and a decrease in average shares outstanding. The decrease in average shares outstanding in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to the repurchase of 26.6 million shares during the last 12 months.

**Diluted Earnings per Share Attributable to Raytheon Company Common Stockholders**

The decreases in diluted earnings per share attributable to Raytheon Company common stockholders of \$0.68 in the second quarter of 2010 compared to the second quarter of 2009 and \$0.65 in the first six months of 2010 compared to the first six months of 2009 were primarily due to the \$0.71 and \$0.72 per share impacts in the second quarter and first six months of 2010, respectively, of the adjustment from a change in our estimated revenue and costs on the UK Border Agency program, on which RSL was notified of its termination, as previously discussed and the FAS/CAS Pension Adjustment, partially offset by operational improvements and a decrease in average shares outstanding.

**Adjusted EPS**

Adjusted EPS is defined as diluted EPS from continuing operations attributable to Raytheon Company common stockholders excluding the earnings per share impact of the FAS/CAS Pension Adjustment and the UK Border Agency program, on which RSL was notified of its termination, as previously discussed. Adjusted Income from continuing operations attributable to Raytheon Company common stockholders is defined as income from continuing operations attributable to Raytheon Company common stockholders excluding the after-tax impact of the FAS/CAS Pension Adjustment at the federal statutory tax rate of 35% and the after-tax impact of the UK Border Agency program, on which RSL was notified of its termination, as previously discussed, at a 30.5% tax rate which is based upon the calculated impact on the rate in the quarter. We are providing this measure because management uses it for the purpose of evaluating and forecasting the Company's financial performance and we believe it allows investors to benefit from being able to assess our operating performance in the context of how our principal customer, the U.S. Government, allows us to recover pension costs and to better compare our operating performance to others in the industry on that same basis and excluding significant unusual items. Adjusted EPS is not a measure of financial performance under GAAP and should be considered supplemental to and not a substitute for financial performance in accordance with GAAP. Adjusted EPS may not be defined and calculated by other companies in the same manner. Adjusted EPS was as follows:

|   | Three Months Ended |               | Six Months Ended |               |
|---|--------------------|---------------|------------------|---------------|
|   | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Diluted EPS from continuing operations attributable to Raytheon Company common stockholders | \$ 0.56            | \$ 1.24       | \$ 1.73          | \$ 2.35       |

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|  |         |         |         |         |
|--|---------|---------|---------|---------|
| Less: Earnings per share impact of the FAS/CAS Pension Adjustment  | (0.09)  | 0.02    | (0.18)  | 0.04    |
| Less: Earnings per share impact of the UK Border Agency program on which RSL was notified of its termination | (0.71)  |         | (0.72)  |         |
| Adjusted EPS   | \$ 1.36 | \$ 1.22 | \$ 2.63 | \$ 2.31 |

**Table of Contents****Segment Results**

We report our results in the following segments: Integrated Defense Systems (IDS), Intelligence and Information Systems (IIS), Missile Systems (MS), Network Centric Systems (NCS), Space and Airborne Systems (SAS) and Technical Services (TS). The following provides some context for viewing our segment performance through the eyes of management.

Given the nature of our business, bookings, net sales and operating income (including operating margin percentage), which we disclose and discuss at the segment level, are most relevant to an understanding of management's view of our performance and often these measures have significant interrelated effects as discussed below. In addition, we disclose and discuss backlog, which represents future sales that we expect to recognize over the contract period, which is generally the next several years.

*Bookings:* We disclose the amount of bookings for each segment and notable contract awards. Bookings generally represent the dollar value of new contracts awarded to us during the reporting period and include firm orders for which funding has not been appropriated. We believe bookings are an important measure of future performance and are an indicator of potential future changes in net sales, since we cannot record revenues under a new contract without first having a booking in the current or preceding period (i.e., a contract award).

*Total Net Sales and Total Operating Expenses:* We generally express changes in net sales in terms of volume. Volume generally refers to increases or decreases in revenues related to varying amounts of total operating expenses, which are comprised of cost of sales, administrative and selling expenses and research and development expenses, incurred on individual contracts (i.e., from performance against contractual commitments on our bookings related to engineering, production or service activity). Therefore, we discuss volume changes attributable principally to individual programs unless there is a discrete event (e.g., a major contract termination, natural disaster or major labor strike, etc.), or some other unusual item that has a material effect on changes in a segment's volume for a reported period. Due to the nature of our contracts, the amount of costs incurred and related revenues will naturally fluctuate over the life of the contracts. As a result, in any reporting period, the changes in volume on numerous contracts are likely to be due to normal fluctuations in our production activity or service levels.

*Operating Income (and the related operating margin percentage):* We generally express changes in segment operating income in terms of volume, changes in program performance or changes in contract mix. Changes in volume discussed in net sales typically drive corresponding changes in our operating income based on the profit rate for a particular contract. Changes in program performance typically relate to profit recognition associated with revisions to total estimated costs at completion that reflect improved or deteriorated operating performance or award fee rates. Changes in contract mix refer to changes in operating margin due to a change in the relative volume of contracts with higher or lower fee rates such that the overall average margin rate for the segment changes. Because each segment has thousands of contracts, in any reporting period, changes in operating income and margin are likely to be due to normal changes in volume, program performance and mix on many contracts with no single change or series of related changes materially driving a segment's change in operating income or operating margin percentage.

*Backlog:* We disclose period ending backlog for each segment. Backlog represents the dollar value of contracts awarded for which work has not been performed. Backlog generally increases with bookings and generally converts into sales as we incur costs under the related contractual commitments. We therefore discuss changes in backlog, including any significant cancellations, for each of our segments, as we believe such discussion provides an understanding of the awarded but not executed portion of our contracts.

Segment financial results were as follows:

| Total Net Sales (In millions)        | Three Months Ended |               | Six Months Ended |               |
|--------------------------------------|--------------------|---------------|------------------|---------------|
|                                      | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| Integrated Defense Systems           | \$ 1,352           | \$ 1,335      | \$ 2,688         | \$ 2,597      |
| Intelligence and Information Systems | 472                | 812           | 1,202            | 1,596         |
| Missile Systems                      | 1,415              | 1,384         | 2,776            | 2,752         |
| Network Centric Systems              | 1,205              | 1,197         | 2,381            | 2,351         |
| Space and Airborne Systems           | 1,197              | 1,136         | 2,292            | 2,182         |
| Technical Services                   | 834                | 780           | 1,635            | 1,476         |
| Corporate and Eliminations           | (502)              | (519)         | (948)            | (945)         |
| Total                                | \$ 5,973           | \$ 6,125      | \$ 12,026        | \$ 12,009     |



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| <b>Operating Income (In millions)</b> | <b>Three Months Ended</b> |                      | <b>Six Months Ended</b> |                      |
|---------------------------------------|---------------------------|----------------------|-------------------------|----------------------|
|                                       | <b>June 27, 2010</b>      | <b>June 28, 2009</b> | <b>June 27, 2010</b>    | <b>June 28, 2009</b> |
| Integrated Defense Systems            | \$ 221                    | \$ 205               | \$ 431                  | \$ 393               |
| Intelligence and Information Systems  | (329)                     | 66                   | (279)                   | 127                  |
| Missile Systems                       | 164                       | 147                  | 322                     | 305                  |
| Network Centric Systems               | 166                       | 170                  | 331                     | 333                  |
| Space and Airborne Systems            | 171                       | 175                  | 330                     | 314                  |
| Technical Services                    | 73                        | 53                   | 140                     | 97                   |
| FAS/CAS Pension Adjustment            | (55)                      | 11                   | (108)                   | 22                   |
| Corporate and Eliminations            | (66)                      | (62)                 | (113)                   | (114)                |
| <b>Total</b>                          | <b>\$ 345</b>             | <b>\$ 765</b>        | <b>\$ 1,054</b>         | <b>\$ 1,477</b>      |

| <b>Bookings (In millions)</b>        | <b>Three Months Ended</b> |                      | <b>Six Months Ended</b> |                      |
|--------------------------------------|---------------------------|----------------------|-------------------------|----------------------|
|                                      | <b>June 27, 2010</b>      | <b>June 28, 2009</b> | <b>June 27, 2010</b>    | <b>June 28, 2009</b> |
| Integrated Defense Systems           | \$ 831                    | 1,796                | \$ 1,566                | \$ 3,005             |
| Intelligence and Information Systems | 648                       | 589                  | 2,369                   | 1,092                |
| Missile Systems                      | 1,280                     | 2,040                | 2,998                   | 2,815                |
| Network Centric Systems              | 964                       | 783                  | 1,928                   | 2,017                |
| Space and Airborne Systems           | 1,231                     | 1,493                | 2,041                   | 2,530                |
| Technical Services                   | 947                       | 946                  | 1,525                   | 1,397                |
| <b>Total</b>                         | <b>\$ 5,901</b>           | <b>7,647</b>         | <b>\$ 12,427</b>        | <b>\$ 12,856</b>     |

Included in bookings were international bookings of \$1,059 million and \$2,214 million in the three months ended June 27, 2010 and June 28, 2009, respectively, and \$1,912 million and \$3,553 million in the six months ended June 27, 2010 and June 28, 2009, respectively, which included foreign military bookings through the U.S. Government. International bookings amounted to 18% and 29% of total bookings in the three months ended June 27, 2010 and June 28, 2009, respectively, and 15% and 28% of total bookings in the six months ended June 27, 2010 and June 28, 2009, respectively. Classified bookings amounted to 19% and 18% of total bookings in the three months ended June 27, 2010 and June 28, 2009, respectively, and 20% and 14% of total bookings in the six months ended June 27, 2010 and June 28, 2009, respectively.

We record bookings for not-to-exceed contract awards based on a reasonable estimate of expected contract definitization, which will generally not be less than 75% of the award. We subsequently adjust bookings to reflect the actual amounts definitized, or, when prior to definitization, when facts and circumstances indicate our previous estimate is no longer reasonable. The timing of awards that may cover multiple fiscal years influences bookings in each year. Bookings exclude unexercised contract options and potential orders under ordering-type contracts (i.e., indefinite delivery/indefinite quantity (IDIQ) type contracts) and are reduced for contract cancellations and terminations of bookings recognized in the current year. We reflect contract cancellations and terminations from prior year bookings, as well as the impact of changes in foreign exchange rates, directly as an adjustment to backlog in the period in which the cancellation or termination occurs and the impact is determinable.

| <b>(In millions)</b>                 | <b>Funded Backlog</b> |                      | <b>Total Backlog</b> |                      |
|--------------------------------------|-----------------------|----------------------|----------------------|----------------------|
|                                      | <b>June 27, 2010</b>  | <b>Dec. 31, 2009</b> | <b>June 27, 2010</b> | <b>Dec. 31, 2009</b> |
| Integrated Defense Systems           | \$ 5,637              | \$ 5,595             | \$ 9,463             | \$ 10,665            |
| Intelligence and Information Systems | 1,013                 | 1,588                | 4,619                | 4,360                |
| Missile Systems                      | 6,296                 | 6,454                | 7,838                | 7,657                |
| Network Centric Systems              | 4,221                 | 4,389                | 5,143                | 5,501                |
| Space and Airborne Systems           | 3,215                 | 3,402                | 5,930                | 5,921                |
| Technical Services                   | 2,079                 | 2,051                | 2,987                | 2,773                |
| <b>Total</b>                         | <b>\$ 22,461</b>      | <b>\$ 23,479</b>     | <b>\$ 35,980</b>     | <b>\$ 36,877</b>     |

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Total backlog includes both funded backlog (unfilled orders for which funding is authorized, appropriated and contractually obligated by the customer) and unfunded backlog (firm orders for which funding has not been appropriated and/or contractually obligated by the customer). Backlog excludes unexercised contract options and potential orders under ordering-type contracts (e.g., IDIQ). Both funded and unfunded backlog are affected by changes in foreign exchange rates.

As discussed in Commitments and Contingencies on page 42, on July 22, 2010, RSL was notified of its termination on the UK Border Agency program, which resulted in a net backlog adjustment of \$556 million at IIS.

**Integrated Defense Systems**

| (In millions, except percentages) | Three Months Ended |               |          | Six Months Ended |               |          |
|-----------------------------------|--------------------|---------------|----------|------------------|---------------|----------|
|                                   | June 27, 2010      | June 28, 2009 | % Change | June 27, 2010    | June 28, 2009 | % Change |
| Total Net Sales                   | \$ 1,352           | \$ 1,335      | 1.3%     | \$ 2,688         | \$ 2,597      | 3.5%     |
| Total Operating Expenses          | 1,131              | 1,130         | 0.1%     | 2,257            | 2,204         | 2.4%     |
| Operating Income                  | 221                | 205           | 7.8%     | 431              | 393           | 9.7%     |
| Operating Margin                  | 16.3%              | 15.4%         |          | 16.0%            | 15.1%         |          |
| Bookings                          | \$ 831             | \$ 1,796      | -53.7%   | \$ 1,566         | \$ 3,005      | -47.9%   |

*Total Net Sales and Total Operating Expenses.* The increase in net sales of \$17 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to \$136 million of higher net sales on Patriot programs principally due to \$115 million of higher net sales driven by scheduled design and production effort on an international Patriot program awarded in the fourth quarter of 2008. The increase in net sales was partially offset by \$57 million of lower net sales on two joint battlefield sensor programs, driven principally by lower volume due to the completion of scheduled program production efforts and a scheduled decrease in design and development effort and \$50 million of lower net sales from the scheduled completion of certain design phases on a U.S. Navy combat systems program. The slight increase in operating expenses in the second quarter of 2010 compared to the second quarter of 2009 was driven primarily by the activity in the programs described above.

The increase in net sales of \$91 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$339 million of higher net sales on Patriot programs principally due to \$284 million of higher net sales driven by scheduled design and production effort on an international Patriot program awarded in the fourth quarter of 2008. The increase in net sales was partially offset by \$118 million of lower net sales on various U.S. Navy programs due to scheduled completion of design and production efforts, including \$60 million from the scheduled completion of certain design phases on a U.S. Navy combat systems program and \$102 million of lower net sales on two joint battlefield sensor programs, driven principally by lower volume due to the completion of scheduled program production efforts and a scheduled decrease in design and development effort. The increase in operating expenses of \$53 million in the first six months of 2010 compared to the first six months of 2009 was driven primarily by the activity in the programs described above.

*Operating Income and Margin.* The increase in operating income of \$16 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to \$9 million from a change in contract mix principally due to higher net sales on international Patriot programs. The increase in operating margin in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to the change in contract mix.

The increase in operating income of \$38 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$17 million from a change in contract mix principally due to higher net sales on international Patriot programs, \$12 million from improved program performance due to successful risk reduction efforts and numerous labor and material cost efficiencies on various production programs and \$10 million from increased volume driven primarily by the programs discussed above. The increase in operating margin in the first six months of 2010 was primarily due to the change in mix and improved program performance.

*Backlog and Bookings.* Backlog was \$9,463 million at June 27, 2010 compared to \$10,665 million at December 31, 2009. The decrease in backlog of \$1,202 million or 11.3% at June 27, 2010 compared to December 31, 2009 was primarily due to lower bookings in the first six months of 2010.

The decrease in bookings of \$965 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to the new international and domestic awards in the second quarter of 2009 discussed below. In the second quarter of 2010, IDS booked \$317 million to provide advanced Patriot air and missile defense capability for an international customer. In the second quarter of



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2009, IDS booked \$877 million to provide advanced Patriot air and missile defense capability for several domestic and international customers, principally the United Arab Emirates (UAE), \$157 million to provide Finland with Surface Launched Medium Range Air-to-Air Missile (SL-AMRAAM) systems, \$150 million for the Joint Land Attack Cruise Missile Defense Elevated Netted Sensor Systems (JLENS) program for the U.S. Army, and \$142 million for two Volume Search Radar (VSR) arrays from the U.S. Navy, one for the Zumwalt-class destroyer program and one for the CVN 78 aircraft carrier.

The decrease in bookings of \$1,439 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to the new international and domestic awards in the first six months of 2009 discussed below. In addition to the bookings noted above, in the first six months of 2010, IDS booked \$162 million to provide engineering services support for a Patriot air and missile defense program for U.S. and international customers and \$131 million on the Zumwalt-class destroyer program for the U.S. Navy, which included initial funding for the third ship. In addition to the bookings noted above, in the first six months of 2009, IDS booked \$741 million in new international and domestic Patriot awards, including \$185 million for the UAE, \$139 million for Taiwan, \$159 million to provide engineering services and \$115 million for the Patriot Pure Fleet program for the U.S. Army.

**Intelligence and Information Systems**

| (In millions, except percentages) | Three Months Ended |               |          | Six Months Ended |               |          |
|-----------------------------------|--------------------|---------------|----------|------------------|---------------|----------|
|                                   | June 27, 2010      | June 28, 2009 | % Change | June 27, 2010    | June 28, 2009 | % Change |
| Total Net Sales                   | \$ 472             | \$ 812        | -41.9%   | \$ 1,202         | \$ 1,596      | -24.7%   |
| Total Operating Expenses          | 801                | 746           | 7.4%     | 1,481            | 1,469         | 0.8%     |
| Operating Income                  | (329)              | 66            | -598.5%  | (279)            | 127           | -319.7%  |
| Operating Margin                  | -69.7%             | 8.1%          |          | -23.2%           | 8.0%          |          |
| Bookings                          | \$ 648             | \$ 589        | 10.0%    | \$ 2,369         | \$ 1,092      | 116.9%   |

*Total Net Sales and Total Operating Expenses.* The decrease in net sales of \$340 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to a \$316 million adjustment, in accordance with percentage-of-completion accounting, from a change in our estimated revenue and costs on the build and design phase on the UK Border Agency program, on which RSL was notified of its termination, as discussed in Commitments and Contingencies on page 42 and \$30 million of expected lower net sales on a distributed ground systems program for the U.S. Air Force principally from lower volume as a result of the program schedule. The increase in operating expenses of \$55 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to \$79 million of higher operating expenses related to the UK Border Agency program, on which RSL was notified of its termination, as previously discussed, offset by lower operating expenses of \$24 million primarily due to the activity in the U.S. Air Force program discussed above. The \$79 million is comprised of a \$52 million impact from the recognition of an adjustment, in accordance with percentage-of-completion accounting, from a change in our estimated costs on the build and design phase of the UK Border Agency program, a \$14 million charge to accrue a loss on the service element due to the expected reduced term of the program's service element from the termination and a \$13 million charge for certain assets no longer expected to be recoverable through the operations of the program's service element.

The decrease in net sales of \$394 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to the \$316 million adjustment to our estimated revenue on the UK Border Agency program, on which RSL was notified of its termination, as previously discussed and \$41 million of expected lower net sales on a distributed ground systems program for the U.S. Air Force principally from lower volume as a result of the program schedule. The increase in operating expenses of \$12 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$79 million of higher operating expenses related to the UK Border Agency program, on which RSL was notified of its termination, as discussed above, offset by lower operating expenses of \$67 million, primarily due to the activity in the U.S. Air Force program discussed above.

*Operating Income and Margin.* The decrease in operating income of \$395 million and the decrease in operating margin in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to a \$395 million adjustment from a change in our estimated revenue and costs on the UK Border Agency program, on which RSL was notified of its termination, as previously discussed. IIS operating income was reduced by approximately \$5 million in the second quarter of 2010 and in the second quarter of 2009 by certain cybersecurity related acquisition costs and investments.

The decrease in operating income of \$406 million and the decrease in operating margin in the first six months of 2010 compared to the first six months of 2009 was primarily due to an adjustment from a change in our estimated revenue and costs on the UK Border Agency program, on which RSL was notified of its termination, as previously discussed. IIS operating income was reduced by approximately \$10 million in the first six months of 2010 and in the first six months of 2009 by certain cybersecurity related acquisition costs and investments.



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*Backlog and Bookings.* Backlog was \$4,619 million at June 27, 2010 compared to \$4,360 million at December 31, 2009. The increase in backlog of \$259 million or 5.9% was primarily due to higher bookings in the first six months of 2010, partially offset by a \$556 million net backlog adjustment for the UK Border Agency program, on which RSL was notified of its termination, as previously discussed.

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The increase in bookings of \$59 million in the second quarter of 2010 compared to the second quarter of 2009 included an \$80 million booking on the Earth Observing System Data and Information System (EOSDIS) Maintenance and Development (EMD) program for NASA. In the second quarter of 2010, IIS booked \$371 million on a number of classified contracts compared to \$342 million in the second quarter of 2009.

The increase in bookings of \$1,277 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to an \$886 million award on a contract to develop the next-generation Global Positioning System Advanced Control Segment (GPS-OCX) for the U.S. Air Force and \$340 million on a major classified program. In addition to the bookings noted above, in the first six months of 2010, IIS also booked \$624 million on a number of classified contracts compared to \$578 million in the first six months of 2009.

**Missile Systems**

| (In millions, except percentages) | Three Months Ended |               |          | Six Months Ended |               |          |
|-----------------------------------|--------------------|---------------|----------|------------------|---------------|----------|
|                                   | June 27, 2010      | June 28, 2009 | % Change | June 27, 2010    | June 28, 2009 | % Change |
| Total Net Sales                   | \$ 1,415           | \$ 1,384      | 2.2%     | \$ 2,776         | \$ 2,752      | 0.9%     |
| Total Operating Expenses          | 1,251              | 1,237         | 1.1%     | 2,454            | 2,447         | 0.3%     |
| Operating Income                  | 164                | 147           | 11.6%    | 322              | 305           | 5.6%     |
| Operating Margin                  | 11.6%              | 10.6%         |          | 11.6%            | 11.1%         |          |
| Bookings                          | \$ 1,280           | \$ 2,040      | -37.3%   | \$ 2,998         | \$ 2,815      | 6.5%     |

*Total Net Sales and Total Operating Expenses.* The increase in net sales of \$31 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to \$45 million of higher net sales on Standard Missile-3 (SM-3), principally from higher volume due to a scheduled increase in development efforts and \$36 million of higher net sales on the Tube-launched, Optically-tracked, Wireless-guided missile (TOW) program driven by scheduled higher production build rates. The increase in net sales was partially offset by \$37 million of lower net sales on the Kinetic Energy Interceptor (KEI) program, which was terminated for convenience in the second quarter of 2009. The increase in operating expenses of \$14 million in the second quarter of 2010 compared to the second quarter of 2009 was driven primarily by the activity in the programs described above.

The increase in net sales of \$24 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$59 million of higher net sales on the TOW program driven by scheduled higher production build rates and \$51 million of higher net sales on SM-3, principally from higher volume due to a scheduled increase in development efforts. The increase in net sales was partially offset by \$63 million of lower net sales on the KEI program, which was terminated for convenience in the second quarter of 2009. The increase in operating expenses of \$7 million in the first six months of 2010 was driven primarily by the activity in the programs described above.

*Operating Income and Margin.* The increase in operating income of \$17 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to improved program performance, which had an \$11 million impact on operating income. The improved program performance was driven by material and labor efficiencies across numerous programs. The increase in operating margin in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to the improved program performance discussed above.

The increase in operating income of \$17 million in the first six months 2010 compared to the first six months of 2009 was primarily due to improved program performance, which had an impact of \$13 million on operating income. The improved program performance was driven by material and labor efficiencies across numerous programs. The increase in operating margin in the first six months of 2010 compared to the first six months of 2009 was primarily due to the improved program performance discussed above.

*Backlog and Bookings.* Backlog was \$7,838 million at June 27, 2010 compared to \$7,657 million at December 31, 2009.

The decrease in bookings of \$760 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to bookings for the Advanced Medium-Range Air-to-Air Missile (AMRAAM) program in the second quarter of 2009. In the second quarter of 2010, MS booked \$234 million for SM-3 for the Missile Defense Agency (MDA), \$223 million for the Phalanx Weapons System for the U.S. Navy, the U.S. Army and international customers, \$150 million for the Miniature Air-Launched Decoys (MALD) for the U.S. Air Force, \$123 million for Evolved Sea Sparrow Missiles (ESSM) for the U.S. Navy and international customers, \$84

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million for the production of Standard Missile-2 (SM-2) for the U.S. Navy and an international customer and \$81 million for the production of AIM-9X short range air-to-air missiles for the U.S. Navy and international customers. In the second quarter of 2009, MS booked \$521 million for the production of AMRAAM for international customers and the U.S. Air Force, \$260 million for the production of Phalanx Weapon Systems for the U.S. Navy and U.S. Army, \$207 million for the production of Tomahawk Block IV missiles for the U.S. Navy and \$167 million for the production of AIM-9X short range air-to-air missiles for the U.S. Navy and international customers.

The increase in bookings of \$183 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to classified bookings in the first six months of 2010. In addition to the bookings noted above, in the first six months of 2010, MS booked \$535 million on a classified program, \$212 million for the development of SM-3 and \$111 million for development work on the Exoatmospheric Kill Vehicle (EKV) program for the MDA, \$207 million for the production of SM-2 for an international customer and the U.S. Navy, \$203 million for the production of Tomahawk missiles for the U.S. Navy, \$102 million for the production of the Joint Stand-off Weapon (JSOW) for the U.S. Navy and \$95 million for the production of TOW missiles for international customers and the U.S. Army. In addition to the bookings noted above, in the first six months of 2009, MS booked \$131 million for the continued development and production of the EKV program.

**Network Centric Systems**

| (In millions, except percentages) | Three Months Ended |               |          | Six Months Ended |               |          |
|-----------------------------------|--------------------|---------------|----------|------------------|---------------|----------|
|                                   | June 27, 2010      | June 28, 2009 | % Change | June 27, 2010    | June 28, 2009 | % Change |
| Total Net Sales                   | \$ 1,205           | \$ 1,197      | 0.7%     | \$ 2,381         | \$ 2,351      | 1.3%     |
| Total Operating Expenses          | 1,039              | 1,027         | 1.2%     | 2,050            | 2,018         | 1.6%     |
| Operating Income                  | 166                | 170           | -2.4%    | 331              | 333           | -0.6%    |
| Operating Margin                  | 13.8%              | 14.2%         |          | 13.9%            | 14.2%         |          |
| Bookings                          | \$ 964             | \$ 783        | 23.1%    | \$ 1,928         | \$ 2,017      | -4.4%    |

*Total Net Sales and Total Operating Expenses.* The increase in net sales of \$8 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to \$82 million of higher net sales related to BBN, which we acquired in the fourth quarter of 2009, and \$26 million of higher net sales on a classified international program awarded in the fourth quarter of 2009. These increases in net sales were partially offset by \$99 million of lower net sales on certain U.S. Army programs, principally from \$54 million of lower net sales on a sensor program due to a planned decline in production and \$34 million of lower net sales on a combat vehicle sensors program, principally from lower volume due to the program's restructuring. The increase in operating expenses of \$12 million in the second quarter of 2010 compared to the second quarter of 2009 was driven primarily by the activity described above.

The increase in net sales of \$30 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$122 million of higher net sales related to BBN and \$41 million of higher net sales on a classified international program awarded in the fourth quarter of 2009. These increases in net sales were partially offset by \$108 million of lower net sales on certain U.S. Army Programs, principally from \$83 million of lower net sales on a sensor program due to a planned decline in production. The increase in operating expenses of \$32 million in the first six months of 2010 compared to the first six months of 2009 was driven primarily by the activity described above.

*Operating Income and Margin.* Operating income and margin in the second quarter and first six months of 2010 remained relatively consistent with the second quarter and first six months of 2009.

*Backlog and Bookings.* Backlog was \$5,143 million at June 27, 2010 compared to \$5,501 million at December 31, 2009.

The increase in bookings of \$181 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to a booking of \$100 million for a command and control program for an international customer in the second quarter of 2010. In the second quarter of 2009, NCS booked \$82 million for the Global Positioning Satellite-Aided Geosynchronous Augmented Navigation (GAGAN) system for the India Space Research Organization (ISRO).

The decrease in bookings of \$89 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to higher total U.S. Army bookings in the first six months of 2009. In addition to the bookings noted above, in the first six months of 2010, NCS booked \$138 million for the Long Range Advanced Scout Surveillance Systems (LRAS3) program for the U.S. Army.

**Table of Contents****Space and Airborne Systems**

| (In millions, except percentages) | Three Months Ended |               |          | Six Months Ended |               |          |
|-----------------------------------|--------------------|---------------|----------|------------------|---------------|----------|
|                                   | June 27, 2010      | June 28, 2009 | % Change | June 27, 2010    | June 28, 2009 | % Change |
| Total Net Sales                   | \$ 1,197           | \$ 1,136      | 5.4%     | \$ 2,292         | \$ 2,182      | 5.0%     |
| Total Operating Expenses          | 1,026              | 961           | 6.8%     | 1,962            | 1,868         | 5.0%     |
| Operating Income                  | 171                | 175           | -2.3%    | 330              | 314           | 5.1%     |
| Operating Margin                  | 14.3%              | 15.4%         |          | 14.4%            | 14.4%         |          |
| Bookings                          | \$ 1,231           | \$ 1,493      | -17.5%   | \$ 2,041         | \$ 2,530      | -19.3%   |

*Total Net Sales and Total Operating Expenses.* The increase in net sales of \$61 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to \$90 million of higher net sales from higher volume, as planned, as work increased on certain classified business awarded in the first half of 2009. The increase in net sales was partially offset by \$30 million of lower net sales from lower volume, as scheduled, as an advanced targeting program moved toward completion. The increase in operating expenses of \$65 million in the second quarter of 2010 compared to the second quarter of 2009 was driven primarily by the activity in the programs described above.

The increase in net sales of \$110 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$157 million of higher net sales from higher volume, as planned, as work increased on certain classified business awarded in the first half of 2009. The increase in net sales was partially offset by \$52 million of lower net sales from lower volume, as scheduled, as an advanced targeting program moved toward completion. The increase in operating expenses of \$94 million in the first six months of 2010 compared to the first six months of 2009 was driven primarily by the activity in the programs described above.

*Operating Income and Margin.* The decrease in operating income of \$4 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to a \$7 million favorable settlement of an affirmative claim on a fixed-price program in the second quarter of 2009, which had an impact on operating margin of approximately 50 basis points.

The increase in operating income of \$16 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to a change in contract mix driven by higher volume on an international tactical radar program, which had a \$20 million impact on operating income, and higher volume, which had a \$12 million impact on operating income. This increase was partially offset by \$19 million from the favorable settlement of affirmative claims on three fixed-price programs included in the first six months of 2009. Operating margin in the first six months of 2010 remained consistent with the first six months of 2009.

*Backlog and Bookings.* Backlog was \$5,930 million at June 27, 2010 compared to \$5,921 million at December 31, 2009.

The decrease in bookings of \$262 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to bookings on a number of space and airborne sensor contracts in the second quarter of 2009. In the second quarter of 2010, SAS booked \$563 million on a number of classified contracts, including \$355 million on a major classified program and \$160 million on two international tactical radar programs. In the second quarter of 2009, SAS booked approximately \$1 billion on a number of space and airborne sensor contracts, including \$110 million on the Integrated Sensor is Structure (ISIS) radar program for the Defense Advanced Research Projects Agency (DARPA).

The decrease in bookings of \$489 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to bookings on a number of space and airborne sensor contracts, as discussed above, in the first six months of 2009. In addition to the bookings noted above, in the first six months of 2010, SAS booked \$90 million for the production of Advanced Countermeasures Electronic System (ACES) for an international customer. In addition to the bookings noted above, in the first six months of 2009, SAS booked \$422 million to supply APG-63 fire control radars and support equipment for the Japan Air Self-Defense Force and \$130 million for the B-2 Radar Modernization Program (RMP).

**Table of Contents****Technical Services**

| (In millions, except percentages) | Three Months Ended |               |          | Six Months Ended |               |          |
|-----------------------------------|--------------------|---------------|----------|------------------|---------------|----------|
|                                   | June 27, 2010      | June 28, 2009 | % Change | June 27, 2010    | June 28, 2009 | % Change |
| Total Net Sales                   | \$ 834             | \$ 780        | 6.9%     | \$ 1,635         | \$ 1,476      | 10.8%    |
| Total Operating Expenses          | 761                | 727           | 4.7%     | 1,495            | 1,379         | 8.4%     |
| Operating Income                  | 73                 | 53            | 37.7%    | 140              | 97            | 44.3%    |
| Operating Margin                  | 8.8%               | 6.8%          |          | 8.6%             | 6.6%          |          |
| Bookings                          | \$ 947             | \$ 946        | 0.1%     | \$ 1,525         | \$ 1,397      | 9.2%     |

*Total Net Sales and Total Operating Expenses.* The increase in net sales of \$54 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to \$67 million of higher net sales from growth on TS training programs, principally domestic and foreign training programs supporting the U.S. Army's Warfighter FOCUS activities due to an increase in customer determined activity levels. The increase in operating expenses of \$34 million in the second quarter of 2010 compared to the second quarter of 2009 was driven primarily by the activity in the programs described above.

The increase in net sales of \$159 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to \$148 million of higher net sales from growth on TS training programs, principally domestic and foreign training programs supporting the U.S. Army's Warfighter FOCUS activities due to an increase in customer determined activity levels. The increase in operating expenses of \$116 million in the first six months of 2010 compared to the first six months of 2009 was driven primarily by the activity in the programs described above.

*Operating Income and Margin.* The increase in operating income of \$20 million in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to improved program performance, which had a \$15 million impact on operating income, and increased volume, which had a \$3 million impact on operating income. The improved program performance was driven primarily by cost efficiencies associated with an increased level of program activities on various training programs, which had a \$6 million impact on operating income, and contract modifications impacting the scope of certain training programs, which had a \$6 million impact on operating income. The increase in operating margin in the second quarter of 2010 compared to the second quarter of 2009 was primarily due to the improved program performance discussed above.

The increase in operating income of \$43 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to improved program performance, which had a \$34 million impact on operating income, and increased volume, which had an \$8 million impact on operating income. The improved program performance was driven primarily by cost efficiencies associated with an increased level of program activities on various training programs, which had an \$14 million impact on operating income, the majority of which was on programs nearing completion, contract modifications that impacted the scope on certain training programs, which had a \$7 million impact on operating income, and higher award fees on a fixed-price service contract, which had a \$3 million impact on operating income. The increase in operating margin in the first six months of 2010 compared to the first six months of 2009 was primarily due to the improved program performance discussed above.

*Backlog and Bookings.* Backlog was \$2,987 million at June 27, 2010 compared to \$2,773 million at December 31, 2009.

Bookings in the second quarter of 2010 remained relatively consistent with the second quarter of 2009. In the second quarter of 2010, TS booked \$399 million on domestic training programs and \$136 million on foreign training programs in support of the Warfighter FOCUS activities and \$95 million to provide operational and logistics support to the National Science Foundation (NSF) Office of Polar Programs. In the second quarter of 2009, TS booked \$535 million on domestic training programs and \$18 million on foreign training programs in support of the Warfighter FOCUS activities, \$160 million to upgrade Phalanx Weapon Systems for the Royal Canadian Navy and \$100 million for a Defense Threat Reduction Agency (DTRA) program.

The increase in bookings of \$128 million in the first six months of 2010 compared to the first six months of 2009 was primarily due to higher bookings in the first six months of 2010, including the awards discussed below. In addition to the bookings noted above, in the first six months of 2010, TS booked \$155 million on domestic training programs and \$25 million on foreign training programs in support of the Warfighter FOCUS activities, \$88 million on the Security Equipment Integration Services (SEIS) contract for the Transportation Security Administration (TSA) and \$78 million to provide operational and logistics support to the NSF Office of Polar Programs. In addition to the bookings noted above, in the first six months of 2009, TS booked \$90 million on domestic training programs and \$88 million on foreign training programs in support of the Warfighter FOCUS activities.



**Table of Contents****FAS/CAS Pension Adjustment**

The FAS/CAS Pension Adjustment represents the difference between our pension expense or income under FAS in accordance with GAAP and our pension expense under CAS. The results of each segment only include pension expense under CAS that we generally recover through the pricing of our products and services to the U.S. Government.

The components of the FAS/CAS Pension Adjustment were as follows:

| (In millions)                     | Three Months Ended |               | Six Months Ended |               |
|-----------------------------------|--------------------|---------------|------------------|---------------|
|                                   | June 27, 2010      | June 28, 2009 | June 27, 2010    | June 28, 2009 |
| FAS expense                       | (215)              | (153)         | \$ (429)         | \$ (306)      |
| CAS expense                       | 160                | 164           | 321              | 328           |
| <b>FAS/CAS Pension Adjustment</b> | <b>(55)</b>        | <b>11</b>     | <b>\$ (108)</b>  | <b>\$ 22</b>  |

Our FAS/CAS Pension Adjustment was \$55 million and \$108 million of expense in the three and six months ended June 27, 2010, compared to \$11 million and \$22 million of income in the three and six months ended June 28, 2009. The increase in our FAS/CAS Pension Adjustment of \$66 million in the three months ended June 27, 2010 compared to the three months ended June 28, 2009 and \$130 million in the six months ended June 27, 2010 compared to the six months ended June 28, 2009 was driven primarily by approximately \$50 million and \$100 million, respectively, from the amortization differences of the net unrecognized liability between FAS and CAS, which was principally attributable to the negative 2008 asset returns.

A key driver of the difference between FAS and CAS expense (and consequently, the FAS/CAS Pension Adjustment) is the pattern of earnings and expense recognition for gains and losses that arise when our asset and liability experience differs from our assumptions under each set of requirements. Generally, such gains or losses are amortized under FAS over the average future working lifetime of the eligible employee population of approximately 11 years, and are amortized under CAS over a 15-year period. In accordance with both FAS and CAS, a market-related value of our plan assets is used to calculate the amount of deferred asset gains or losses to be amortized. The market-related value of assets is determined using actual asset gains or losses over a certain prior period (three years for FAS and five years for CAS, subject to certain limitations under CAS on the difference between the market-related value and actual market value of assets). Because of this difference in the number of years over which actual asset gains or losses are recognized and subsequently amortized, FAS expense generally tends to reflect the recent gains or losses faster than CAS. Another driver of CAS expense (but not FAS expense) is the funded status of our pension plans under CAS. As noted above, CAS expense is only recognized for plans that are not fully funded; consequently, if plans become or cease to be fully funded under CAS due to our asset or liability experience, our CAS expense will change accordingly.

On an annual basis, at December 31<sup>st</sup>, we update our estimate of future FAS and CAS pension expense based upon actual asset returns and other actuarial factors. Other variables that can impact the pension plans' funded status and FAS and CAS expense include demographic experience such as the expected rates of salary increase, retirement age, turnover and mortality. In addition, certain pension plans provide a lump sum form of benefit that varies based upon externally determined interest rates. Assumptions for these variables are set at the beginning of the year, and are based on actual and projected plan experience. On a periodic basis, generally planned annually in the third quarter, we update our actuarial estimate of the unfunded projected benefit obligation for both FAS and CAS with final census data from the end of the prior year.

**Corporate and Eliminations**

Corporate and Eliminations includes corporate expenses and intersegment sales and profit eliminations. Corporate expenses represent unallocated costs and certain other corporate costs not considered part of management's evaluation of reportable segment operating performance, including the net costs associated with our residual commuter aircraft portfolio.

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The components of net sales related to Corporate and Eliminations were as follows:

| (In millions)                   | Three Months Ended |                 | Six Months Ended |                 |
|---------------------------------|--------------------|-----------------|------------------|-----------------|
|                                 | June 27, 2010      | June 28, 2009   | June 27, 2010    | June 28, 2009   |
| Intersegment sales eliminations | \$ (512)           | \$ (532)        | \$ (960)         | \$ (961)        |
| Corporate                       | 10                 | 13              | 12               | 16              |
| <b>Total</b>                    | <b>\$ (502)</b>    | <b>\$ (519)</b> | <b>\$ (948)</b>  | <b>\$ (945)</b> |

The components of operating income related to Corporate and Eliminations were as follows:

| (In millions)                    | Three Months Ended |                | Six Months Ended |                 |
|----------------------------------|--------------------|----------------|------------------|-----------------|
|                                  | June 27, 2010      | June 28, 2009  | June 27, 2010    | June 28, 2009   |
| Intersegment profit eliminations | \$ (48)            | \$ (45)        | \$ (87)          | \$ (78)         |
| Corporate                        | (18)               | (17)           | (26)             | (36)            |
| <b>Total</b>                     | <b>\$ (66)</b>     | <b>\$ (62)</b> | <b>\$ (113)</b>  | <b>\$ (114)</b> |

**Discontinued Operations**

In pursuing our business strategies we have divested of certain non-core businesses, investments and assets when appropriate. All residual activity relating to our previously disposed businesses appears in discontinued operations.

We retained certain assets and liabilities of our previously disposed businesses. At June 27, 2010 and December 31, 2009, we had \$56 million and \$71 million, respectively, of assets primarily related to our retained interest in general aviation finance receivables previously sold by Raytheon Aircraft Company (Raytheon Aircraft). At June 27, 2010 and December 31, 2009, we had \$57 million of liabilities primarily related to certain environmental and product liabilities, aircraft lease obligations, non-income tax obligations and various contract obligations. We also have certain income tax obligations relating to these disposed businesses, which we include in our income tax disclosures. The Internal Revenue Service (IRS) concluded a federal excise tax audit and assessed us additional excise tax related to the treatment of certain Flight Options LLC customer fees and charges, which we have appealed. We continue to believe that an unfavorable outcome is not probable and expect that any potential liability will not have a material adverse effect on our financial position, results of operations or liquidity. We also retained certain U.K. pension assets and obligations for a limited number of U.K. pension plan participants as part of the Raytheon Aircraft sale, which we include in our pension disclosures.

**Financial Condition and Liquidity****Overview**

We pursue a capital deployment strategy that balances funding for growing our business, including capital expenditures, acquisitions and research and development; managing our balance sheet, including debt repayments and pension contributions; and returning cash to our stockholders, including dividend payments and share repurchases, as outlined below. Our need for, cost of and access to funds are dependent on future operating results, as well as other external conditions. We currently expect that our cash and cash equivalents, cash flow from operations and other available financing resources will be sufficient to meet our anticipated operating, capital expenditure, investment, debt service and other financing requirements during the next twelve months and for the foreseeable future.

During the first six months of 2010, certain of our significant cash flows, discussed in more detail below, were as follows:

\$ 775 million of stock repurchases;



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\$ 584 million of required contributions to our pension and other postretirement benefit plans;

\$ 373 million of federal and net foreign tax payments;

\$ 260 million in dividend payments;

\$ 250 million of proceeds from warrants exercised; and

\$ 140 million for payments of additions to property, plant and equipment and capitalized internal use software.

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In addition, the following table highlights selected measures of our liquidity and capital resources as of June 27, 2010 and December 31, 2009:

| (In millions)                            | June 27, 2010 | Dec. 31, 2009 |
|--|---------------|---------------|
| Cash and cash equivalents                | \$ 2,385      | \$ 2,642      |
| Working capital                          | 2,045         | 2,345         |
| Amount available under credit facilities | 1,497         | 1,479         |

The decrease of \$300 million in working capital in the second quarter of 2010 compared to the fourth quarter of 2009 was primarily due to the decrease in cash and cash equivalents, principally from payments for the repurchases of common stock in the first six months of 2010. This decrease was partially offset by an increase in contracts in process driven by the timing of payments, which was partially offset by a reduction in contracts in process as a result of the UK Border Agency program, on which RSL was notified of its termination, as previously discussed.

**Operating Activities**

| (In millions)  | Six Months Ended |               |
|--|------------------|---------------|
|  | June 27, 2010    | June 28, 2009 |
| Net cash provided by operating activities from continuing operations | \$ 657           | \$ 923        |
| Net cash provided by operating activities                            | 659              | 914           |

The decrease of \$255 million in net cash provided by operating activities in the first six months of 2010 compared to the first six months of 2009 was primarily due to higher net cash tax payments as described below.

*Tax Payments* - In the first six months of 2010, we made \$373 million in federal and net foreign tax payments and \$51 million in net state tax payments. In the first six months of 2009, we received federal tax refunds totaling \$337 million and made \$255 million in federal and net foreign tax payments. In the first six months of 2009, we received state tax refunds totaling \$22 million and made \$22 million in state tax payments. We expect full year federal and foreign tax payments to be approximately \$720 million in 2010 compared to \$208 million in 2009. The increase in the expected full-year federal and foreign tax payments in 2010 is primarily due to \$337 million refund received in the first six months of 2009.

In March 2010, the Patient Protection and Affordable Care Act, as modified by the Health Care and Education Reconciliation Act of 2010, was enacted which changed the tax treatment of the U.S. Government subsidies for companies that provide qualifying drug coverage to Medicare eligible retirees. Although some companies have been adversely affected by this act, we do not receive such U.S. Government subsidies and therefore this change will not have an effect on our financial position, results of operations or liquidity.

*Pension Plan Contributions* - We make both required and discretionary contributions to our pension plans. Required contributions are primarily determined by the Employee Retirement Income Security Act of 1974 (ERISA) rules and are affected by the actual return on plan assets and plan funded status. If discretionary contributions are made, a funding credit is accumulated that we can use to offset future calculated required contributions. The funding credit for our pension plans was \$2.6 billion at December 31, 2009. We made the following required contributions to our pension plans during the first six months of 2010 and 2009:

| (In millions)          | Six Months Ended |               |
|------------------------|------------------|---------------|
|                        | June 27, 2010    | June 28, 2009 |
| Required contributions | \$ 574           | \$ 552        |

For the full-year 2010, we expect to make required contributions of approximately \$1,140 million to our pension plans and \$30 million to our other postretirement benefit plans consistent with our full-year 2009 contributions. We did not make any discretionary contributions to our pension plans during the first six months of 2010 and 2009; however we periodically evaluate whether to make discretionary contributions. Other postretirement benefit plan payments were \$10 million and \$17 million in the first six months of 2010 and 2009, respectively.

Future funding requirements will likely be affected by the Pension Protection Act of 2006, which requires companies to fully fund their pension plans over a seven-year period. For certain defense contractors, the new funding rules become effective when the rules intended to harmonize the CAS rules with the Pension Protection Act of 2006 go into effect or no later than 2011. On May 10, 2010, the CAS Pension Harmonization Notice of Proposed Rulemaking (NPRM) was published in the Federal Register with a 60 day



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comment period. The NPRM is the third step of a four step statutory process to implement a final CAS standard related to the recognition of pension costs for government contractors. Based upon the feedback received during the comment period, the CAS Board will either issue the final rule or alternatively reissue the NPRM. The final rule could impact our future CAS recovery amount and our FAS/CAS Pension Adjustment.

We made interest payments of \$58 million and \$69 million in the first six months of 2010 and 2009, respectively. The decrease in interest payments in the first six months of 2010 compared to the first six months of 2009 was primarily due to the repurchase of our 4.85% Notes due 2011 in the fourth quarter of 2009.

**Investing Activities**

| (In millions)                         | Six Months Ended |               |
|---------------------------------------|------------------|---------------|
|                                       | June 27, 2010    | June 28, 2009 |
| Net cash used in investing activities | \$ 151           | \$ 124        |

The increase of \$27 million in net cash used in investing activities in the first six months of 2010 compared to the first six months of 2009 was primarily due to higher additions to property, plant and equipment.

Additions to property, plant and equipment and capitalized internal use software were as follows:

| (In millions)                                  | Six Months Ended |               |
|--|------------------|---------------|
|  | June 27, 2010    | June 28, 2009 |
| Additions to property, plant and equipment     | \$ 109           | \$ 81         |
| Additions to capitalized internal use software | 31               | 34            |

We expect our property, plant and equipment and internal use software expenditures to be approximately \$420 million and \$100 million, respectively, in 2010, consistent with the anticipated growth of our business and for specific investments including program capital assets and facility improvements.

In pursuing our business strategies, we acquire and make investments in certain businesses that meet strategic and financial criteria, and divest of certain non-core businesses, investments and assets when appropriate.

In January 2010, we acquired substantially all of the assets of an Australian company, Compucat Research Pty. Ltd., at Intelligence and Information Systems for \$12 million in cash, which enhances our information security and cybersecurity capabilities. In connection with this acquisition we recorded \$4 million of goodwill and \$2 million of intangible assets.

**Financing Activities**

| (In millions)                         | Six Months Ended |               |
|---------------------------------------|------------------|---------------|
|                                       | June 27, 2010    | June 28, 2009 |
| Net cash used in financing activities | \$ 765           | \$ 850        |

We have used cash provided by operating activities as our primary source for the payment of dividends and the repurchase of our common stock. The decrease of \$85 million in net cash used in financing activities in the first six months of 2010 compared to the first six months of 2009 was primarily due to proceeds from warrants exercised in the first six months of 2010 offset by the repurchases of common stock.

*Stock Repurchases* - Information on repurchases of our common stock under our share repurchase programs was as follows:

Six Months Ended

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| (In millions)               | June 27, 2010 | June 28, 2009 |
|-----------------------------|---------------|---------------|
| Amount of stock repurchased | \$ 775        | \$ 600        |
| Shares of stock repurchased | 14.2          | 13.4          |

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In October 2008, our Board of Directors authorized the repurchase of up to \$2.0 billion of our outstanding common stock. In March 2010, our Board of Directors authorized the repurchase of up to an additional \$2.0 billion of our outstanding common stock. At June 27, 2010, we had approximately \$2.1 billion available under these repurchase programs. Share repurchases will take place from time to time at management's discretion depending on market conditions.

On May 27, 2010, our stockholders approved the Raytheon 2010 Stock Plan (the Plan). Under the Plan, we may grant restricted stock awards, stock units, stock grants, stock options and stock appreciation rights.

*Cash Dividends* - Our Board of Directors authorized the following cash dividends:

| (In millions, except per share amounts) | Six Months Ended |               |
|---|------------------|---------------|
|   | June 27, 2010    | June 28, 2009 |
| Cash dividends per share                | \$ 0.75          | \$ 0.62       |
| Total dividends paid                    | 260              | 234           |

In March 2010, our Board of Directors authorized a 21% increase to our annual dividend payout rate from \$1.24 to \$1.50 per share. Although we do not have a formal dividend policy, we believe that, over time, a reasonable dividend payout ratio is approximately one third of our income from continuing operations excluding the FAS/CAS Pension Adjustment. Dividends are subject to quarterly approval by our Board of Directors.

**Capital Resources**

Total debt was \$2.3 billion at June 27, 2010 and December 31, 2009. Our outstanding debt bears contractual interest at fixed interest rates ranging from 4.4% to 7.2% and matures at various dates through 2028.

*Cash and Cash Equivalents* - Cash and cash equivalents were \$2.4 billion and \$2.6 billion at June 27, 2010 and December 31, 2009, respectively. We invest cash in U.S. Treasuries; commercial paper of financial institutions and corporations with a minimum long-term debt rating of AA- or Aa3 and minimum short-term debt rating of A-1 and P-1; AAA/Aaa rated U.S. Treasury money market funds; and bank certificates of deposit and time deposits with a minimum long-term debt rating of AA- or Aa3. Cash balances held at our foreign subsidiaries were approximately 15% of our total cash balance at June 27, 2010 and December 31, 2009, and are deemed to be indefinitely reinvested.

*Credit Facilities* - We have two bank revolving credit facilities in the amount of \$1.5 billion. The first credit facility is a \$1.0 billion, three-year facility maturing in November 2012, \$150 million of which is available to Raytheon United Kingdom Limited, our U.K. subsidiary. The second facility is a \$500 million 364-day facility maturing in November 2010. Borrowings under these facilities bear interest at various rate options, including LIBOR plus a margin based on our credit default swap spread, with minimum and maximum margins that are adjusted for our credit ratings. Based on our credit ratings at June 27, 2010 and December 31, 2009, borrowings under these facilities would bear interest at LIBOR plus 100 basis points, the minimum margin.

Under the \$1.0 billion facility, we can borrow, issue letters of credit and backstop commercial paper. Under the \$500 million facility, we can borrow and backstop commercial paper. These credit facilities are comprised of commitments from approximately 25 separate highly rated lenders, each committing no more than 10% of the aggregate of the facilities. As of June 27, 2010 and December 31, 2009, there were no borrowings outstanding under these credit facilities. However, we had \$3 million and \$21 million of outstanding letters of credit at June 27, 2010 and December 31, 2009, respectively, which effectively reduced our borrowing capacity under these credit facilities by the same amounts.

Under these two facilities, we must comply with certain covenants, including a ratio of total debt to total capitalization of no more than 50% and a ratio of consolidated earnings attributable to Raytheon Company before interest, taxes, depreciation and amortization (EBITDA) to consolidated net interest expense, for any period of four consecutive fiscal quarters, of no less than 3 to 1. We were in compliance with these covenants during the 12 months ended June 27, 2010 and December 31, 2009. Our ratio of total debt to total capitalization was 18.9% and 19.0% at June 27, 2010 and December 31, 2009, respectively.

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Certain of our foreign subsidiaries maintain revolving bank lines of credit to provide them with a limited amount of short-term liquidity, including the \$150 million Raytheon United Kingdom Limited sub-line discussed above. In addition, other uncommitted bank lines totaled approximately \$15 million at June 27, 2010 and December 31, 2009, respectively. There were no amounts outstanding under these lines of credit at June 27, 2010 and December 31, 2009. Compensating balance arrangements are not material.

*Credit Ratings* - Three major corporate debt rating organizations, Fitch Ratings (Fitch), Moody's Investors Service (Moody's) and Standard & Poor's (S&P), assign ratings to our short and long-term debt. The following chart reflects the current ratings assigned by each of these agencies as of June 27, 2010 to our short-term debt and long-term senior unsecured debt:

| Rating Agency | Short-Term Debt | Long-Term Senior Debt |         | Date of Last Action |
|---------------|-----------------|-----------------------|---------|---------------------|
|               |                 | Rating                | Outlook |                     |
| Fitch         | F2              | A -                   | Stable  | September 2008      |
| Moody's       | P-2             | Baa1                  | Stable  | March 2007          |
| S&P           | A-2             | A -                   | Stable  | September 2008      |

*Shelf Registrations* - The total capacity of our current shelf registration, filed with the SEC in October 2008, is \$3.0 billion, of which \$500 million was used to issue fixed-rate long-term debt in 2009 and \$450 million was used for the registration of common stock issuable under certain outstanding warrants issued in 2006.

During the downturn in global financial markets over the past few years, some companies have experienced difficulties accessing their cash equivalents, trading investment securities, drawing on revolvers, issuing debt and raising capital generally, which have had a material adverse impact on their liquidity. Given our current cash position, credit ratings, cash needs and debt structure, along with the type of short-term investments we have made, we have not experienced any material issues and we continue to expect that our current liquidity, notwithstanding recent market conditions, will be sufficient to meet all our anticipated needs during the next 12 months and for the foreseeable future.

**Commitments and Contingencies**

*Environmental Matters* - We are involved in various stages of investigation and cleanup related to remediation of various environmental sites. Our estimate of the liability of total environmental remediation costs includes the use of a discount rate and considers that a portion of these costs is eligible for future recovery through the pricing of our products and services to the U.S. Government. We consider such recovery probable based on government contracting regulations and our long history of receiving reimbursement for such costs and accordingly have recorded the estimated future recovery of these costs from the U.S. Government within contracts in process. Our estimates of total remediation costs, weighted average risk-free rate, total remediation costs - discounted and recoverable portion were as follows:

| (In millions, except percentages)      | June 27, 2010 | Dec. 31, 2009 |
|--|---------------|---------------|
| Total remediation costs - undiscounted | \$ 212        | \$ 208        |
| Weighted average risk free rate        | 5.7%          | 5.7%          |
| Total remediation costs - discounted   | \$ 148        | \$ 139        |
| Recoverable portion                    | 107           | 97            |

We also lease certain government-owned properties and are generally not liable for remediation of preexisting environmental contamination at these sites; as a result, we generally do not reflect the provision for these costs in our financial statements. Due to the complexity of environmental laws and regulations, the varying costs and effectiveness of alternative cleanup methods and technologies, the uncertainty of insurance coverage and the unresolved extent of our responsibility, it is difficult to determine the ultimate outcome of these matters; however, we do not expect any additional liability to have a material adverse effect on our financial position, results of operations or liquidity.

*Financing Arrangements and Other* - We issue guarantees and banks and surety companies issue, on our behalf, letters of credit and surety bonds to meet various bid, performance, warranty, retention and advance payment obligations of us or our affiliates. These instruments expire on various dates through 2020. Additional guarantees of project performance for which there is no stated value also remain

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outstanding. The stated values outstanding at June 27, 2010 and December 31, 2009 were as follows:

| <b>(In millions)</b> | <b>June 27, 2010</b> | <b>Dec. 31, 2009</b> |
|----------------------|----------------------|----------------------|
| Guarantees           | \$ 235               | \$ 227               |
| Letters of Credit    | 914                  | 898                  |
| Surety Bonds         | 199                  | 203                  |



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Included in guarantees and letters of credit described above were \$88 million and \$235 million, respectively, at June 27, 2010, and \$80 million and \$206 million, respectively, at December 31, 2009, related to our joint venture in Thales-Raytheon Systems Co. Ltd. (TRS). We provide these guarantees and letters of credit to TRS and other affiliates to assist these entities in obtaining financing on more favorable terms, making bids on contracts and performing their contractual obligations. While we expect these entities to satisfy their loans, project performance and other contractual obligations, their failure to do so may result in a future obligation to us. At June 27, 2010 and December 31, 2009, we had an estimated liability of \$8 million and \$6 million, respectively, related to these guarantees and letters of credit. We periodically evaluate the risk of TRS and other affiliates failing to satisfy their loans, project performance and meet other contractual obligations described above. At June 27, 2010, we believe the risk that TRS and other affiliates will not be able to perform or meet their obligations is minimal for the foreseeable future based on their current financial condition. All obligations were current at June 27, 2010.

Our residual turbo-prop commuter aircraft portfolio has exposure to outstanding financing arrangements with the aircraft serving as collateral. We have sold and leased commuter aircraft globally to thinly capitalized companies, whose financial condition could be significantly affected by a number of factors, including fuel and other costs, industry consolidation, declining commercial aviation market conditions and the U.S. Government budget for the Essential Air Service program. Based on recent economic trends, including tightening credit markets and volatile fuel costs, these companies may increasingly experience difficulties meeting their financial commitments. At June 27, 2010 and December 31, 2009, our exposure on commuter aircraft assets held as inventory, collateral on notes or as leased assets, was approximately \$84 million relating to 88 aircraft and approximately \$109 million relating to 106 aircraft, respectively. The valuation of used aircraft is also considered in assessing the realizable value of certain commuter aircraft related to assets which serve as collateral for the underlying financial arrangements. As part of the assessment of realizable value, we evaluate many factors, including sales transaction history, current market conditions, anticipated future market conditions and age and condition of the aircraft. The carrying value of our commuter aircraft portfolio assumes an orderly disposition of these assets, consistent with our historical experience and strategy. The tightening of credit markets and economic conditions have reduced the number of potential buyers who are able to obtain financing and have negatively impacted the ability of existing customers to refinance their aircraft through a third party. If the long-term market prospects for these aircraft were to significantly erode or cease, our valuation of these assets would likely be less than the carrying value. We periodically evaluate potential alternative strategies for the disposal of these assets. If we were to dispose of these assets in an other than orderly manner or sell the portfolio in its entirety, the value realized would likely be less than the carrying value.

In 1997, we provided a first loss guarantee of \$133 million on \$1.3 billion of U.S. Export-Import Bank loans (maturing in 2015) to the Brazilian Government related to Network Centric Systems System for the Vigilance of the Amazon (SIVAM) program. Loan repayments by the Brazilian Government were current at June 27, 2010.

Government contractors are subject to many levels of audit and investigation. Agencies that oversee contract performance include: the Defense Contract Audit Agency, the Inspector General of the Department of Defense and other departments and agencies, the Government Accountability Office, the Department of Justice and Congressional Committees. The Department of Justice has, from time to time, convened grand juries to investigate possible irregularities by us. We also provide products and services to customers outside of the U.S. and those sales are subject to local government laws, regulations and procurement policies and practices. Our compliance with such local government regulations or any applicable U.S. Government regulations (e.g., the Foreign Corrupt Practices Act and the International Traffic in Arms Regulations) may also be investigated or audited. We do not expect these audits and investigations to have a material adverse effect on our financial position, results of operations or liquidity, either individually or in the aggregate.

We are currently conducting a self-initiated internal review of certain of our international operations, focusing on compliance with the Foreign Corrupt Practices Act. In the course of the review, we have identified several possible areas of concern relating to payments made in connection with certain international operations related to a jurisdiction where we do business. We have voluntarily contacted the Securities and Exchange Commission (SEC) and the Department of Justice to advise both agencies that an internal review is underway. Because the internal review is ongoing, we cannot predict the ultimate consequences of the review. Based on the information available to date, we do not believe that the results of this review will have a material adverse effect on our financial position, results of operations or liquidity.

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In May 2006, international arbitration hearings commenced against us as the successor to the Hughes Electronics defense business, in connection with certain claims brought in 2004 relating to an alleged 1995 Workshare Agreement. The asserted claims involve breach of contract, intellectual property infringement and other related matters. The arbitration panel stayed further proceedings, including the issuance of the liability decision on the non-IP claims presented during the May 2006 hearing, while the parties engaged in settlement efforts. The parties were unable to conclude an enforceable settlement, and in August 2009, the panel released its liability decision, rejecting some of MBDA's non-IP claims, while finding Raytheon liable for some other non-IP claims. We did not record any significant additional financial liability as a result of our estimate of the impact of the decision. The proceedings will now resume to determine liability for the asserted IP claims and to assess overall damages, if any. We believe that we have meritorious defenses to the remaining asserted IP claims and intend to continue to contest them vigorously; however, an adverse resolution of this matter could have a material effect on our results of operations.

On July 22, 2010, Raytheon Systems Limited ( RSL ) was notified by the UK Border Agency that it had been terminated for default on a program. The termination notice included allegations that RSL had failed to perform on certain key milestones and other matters in addition to claims to recover certain losses incurred and previous payments made to RSL. We believe that RSL performed well and delivered substantial capabilities to the UK Border Agency under the program, which has been operating successfully and providing actionable information since live operations began in May 2009. As a result, we intend to pursue vigorously the collection of receivables for the program and damages in connection with the termination and defend ourselves against the UK Border Agency's claims for losses and previous payments.

Under the accounting requirements for subsequent events, we determined that the accounting impact of the termination notice was required to be reflected in our results for the period ended June 27, 2010. As a result, we are required to adjust our estimated

amount of revenue and costs under the program in the period ended June 27, 2010. The adjustment was based on our determination that certain assets were no longer expected to be recovered and for estimated costs for certain exit cost obligations under the contract and the estimated settlement of expected future subcontractor claims. The impact of the adjustment reduced Intelligence and Information Systems (IIS) total net sales and operating income by \$316 million and \$395 million in the three and six months ended June 27, 2010, respectively. At June 27, 2010, after the adjustment, we had approximately \$80 million in letters of credit and approximately \$30 million of billed and unbilled receivables remaining under the program for technology and services delivered, which we believe, are probable of recovery in litigation or arbitration. No amounts have been drawn down on the letters of credit. We currently do not believe it is probable that we are liable for losses, previous payments or other claims asserted by the UK Border Agency. It is reasonably possible that the ultimate amount of any resolution of the termination could be less or greater than our estimate due to the inherent uncertainties in litigation or arbitration. If we are unsuccessful in recovering amounts drawn on the letters of credit, fail to collect the billed and unbilled receivable balance or if we are required to make payments against claims or other losses asserted by the UK Border Agency or pay subcontractor claims in excess of our estimates, it could have a material adverse effect on our results of operations.

In addition, various other claims and legal proceedings generally incidental to the normal course of business are pending or threatened against us. We do not expect any additional liability from these proceedings to have a material adverse effect on our financial position, results of operations or liquidity.

## **Accounting Standards**

As described in Note 1: Basis of Presentation, within Item 1 of this Form 10-Q, in January 2010, we adopted the required new accounting standards that amend the accounting and disclosure requirements for transfers of financial assets and consolidation of VIEs. These accounting standards eliminate the concept of a qualifying special-purpose entity (QSPE) and the related exception for applying the consolidation guidance. As a result, we consolidated our QSPE, General Aviation Receivables Corporation (GARC), which did not have a material impact on our consolidated financial statements and resulted in:

The removal of our \$67 million investment in GARC, previously reported in other assets, net, and

The addition of long and short-term notes receivable, net, of \$68 million; current notes payable of \$2 million; and an increase in retained earnings of less than \$1 million, net of tax.

The notes payable were paid off as of March 28, 2010.

Further, the new accounting standard related to consolidation of VIEs requires an enterprise to perform a qualitative analysis when determining whether or not it must consolidate a VIE. It also requires an enterprise to continuously reassess whether it must consolidate a VIE. Additionally,

it requires enhanced disclosures about an enterprise's involvement with VIEs and any significant change in risk exposure due to that involvement, as well as how its involvement with VIEs impacts the enterprise's financial statements. Finally, an enterprise is required to disclose significant judgments and assumptions used to determine whether or not to consolidate a VIE. With the exception of GARC discussed above, the adoption of this accounting standard did not change any of our previous consolidation conclusions and thus did not have an effect on our financial position, results of operations or liquidity.

Other new pronouncements issued but not effective until after June 27, 2010 are not expected to have a material impact on our financial position, results of operations or liquidity.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our primary market exposures are to interest rates and foreign exchange rates.

We supplement our working capital with a combination of variable-rate short-term and fixed-rate long-term financing. We periodically enter into interest rate swap agreements with commercial and investment banks to manage interest rates associated with our financing arrangements. We also enter into foreign currency forward contracts with commercial banks to fix the foreign currency exchange rates on specific commitments and payments to vendors and customer receipts. The market-risk sensitive instruments we use for hedging are entered into with commercial and investment banks and are directly related to a particular asset, liability or transaction for which a firm commitment is in place.

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The following tables provide information as of June 27, 2010 and December 31, 2009 about our market risk exposure associated with changing interest and exchange rates. For long-term debt obligations, the table presents principal cash flows by maturity date and average interest rates related to outstanding obligations.

**As of June 27, 2010**

**Principal Payments and Interest Rate Detail by Contractual Maturity Dates**

(In millions, except percentages)

| Long-Term Debt        | 2010 | 2011 | 2012   | 2013   | 2014 | Thereafter | Total    | Fair Value |
|-----------------------|------|------|--------|--------|------|------------|----------|------------|
| Fixed-rate debt       | \$   | \$   | \$ 333 | \$ 345 | \$   | \$ 1,658   | \$ 2,336 | \$ 2,706   |
| Average interest rate |      |      | 5.50%  | 5.38%  |      | 6.10%      | 5.91%    |            |

**As of December 31, 2009**

**Principal Payments and Interest Rate Detail by Contractual Maturity Dates**

(In millions, except percentages)

| Long-Term Debt        | 2010 | 2011 | 2012   | 2013   | 2014 | Thereafter | Total    | Fair Value |
|-----------------------|------|------|--------|--------|------|------------|----------|------------|
| Fixed-rate debt       | \$   | \$   | \$ 333 | \$ 345 | \$   | \$ 1,658   | \$ 2,336 | \$ 2,581   |
| Average interest rate |      | %    | 5.50%  | 5.38%  |      | 6.10%      | 5.91%    |            |

The notional amounts of outstanding foreign currency forward contracts consisted of the following at:

| (In millions)    | June 27, 2010   |               | Dec. 31, 2009 |               |
|------------------|-----------------|---------------|---------------|---------------|
|                  | Buy             | Sell          | Buy           | Sell          |
| British Pounds   | \$ 398          | \$ 330        | \$ 407        | \$ 498        |
| Canadian Dollars | 222             | 48            | 212           | 46            |
| Euros            | 188             | 24            | 190           | 35            |
| All other        | 195             | 78            | 176           | 53            |
| <b>Total</b>     | <b>\$ 1,003</b> | <b>\$ 480</b> | <b>\$ 985</b> | <b>\$ 632</b> |

Unrealized gains of \$78 million and \$69 million were included in other assets, net, and unrealized losses of \$76 million and \$33 million were included in other accrued expenses at June 27, 2010 and December 31, 2009, respectively. For foreign currency forward contracts designated and qualified for hedge accounting, we record the effective portion of the gain or loss on the derivative in accumulated other comprehensive loss, net of tax and reclassify it into earnings in the same period or periods during which the hedged revenue or cost of sales transaction affects earnings. Realized gains and losses resulting from these cash flow hedges offset the foreign currency exchange gains and losses on the underlying assets or liabilities being hedged. We believe our exposure due to changes in foreign currency rates is not material due to our hedging policy.

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

Management conducted an evaluation, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of

the Securities Exchange Act of 1934) as of June 27, 2010.

*Conclusion of Evaluation*

Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures as of June 27, 2010 were effective.

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*Inherent Limitations on Effectiveness of Controls and Procedures*

In designing and evaluating our disclosure controls and procedures, management recognizes that any controls, no matter how well designed and operated, can provide only reasonable, not absolute, assurance of achieving the desired control objectives. Due to the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the Company have been detected.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the second quarter of 2010 that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We primarily engage in providing products and services under contracts with the U.S. Government and, to a lesser degree, under direct foreign sales contracts, some of which the U.S. Government funds. These contracts are subject to extensive legal and regulatory requirements and, from time to time, agencies of the U.S. Government investigate whether our operations are being conducted in accordance with these requirements. U.S. Government investigations of us, whether relating to these contracts or conducted for other reasons, could result in administrative, civil or criminal liabilities, including repayments, fines or penalties being imposed upon us, the suspension of government export licenses or the suspension or debarment from future U.S. Government contracting. U.S. Government investigations often take years to complete and many result in no adverse action against us. Government contractors are also subject to many levels of audit and investigation. Agencies that oversee contract performance include: the Defense Contract Audit Agency, the Inspector General of the Department of Defense and other departments and agencies, the Government Accountability Office, the Department of Justice (DoJ) and Congressional Committees. The DoJ, from time to time, has convened grand juries to investigate possible irregularities by us. We also provide products and services to customers outside of the U.S. and those sales are subject to local government laws, regulations and procurement policies and practices. Our compliance with such local government regulation or any applicable U.S. Government regulation (e.g., the Foreign Corrupt Practices Act and the International Traffic in Arms Regulations) may also be investigated or audited.

We are currently conducting a self-initiated internal review of certain of our international operations, focusing on compliance with the Foreign Corrupt Practices Act. In the course of the review, we have identified several possible areas of concern relating to payments made in connection with certain international operations related to a jurisdiction where we do business. We have voluntarily contacted the Securities and Exchange Commission and the DoJ to advise both agencies that an internal review is underway. Because the internal review is ongoing, we cannot predict the ultimate consequences of the review. Based on the information available to date, we do not believe that the results of this review will have a material adverse effect on our financial condition, results of operations or liquidity.

We are involved in various stages of investigation and cleanup related to remediation of various environmental sites. We accrued all appropriate costs we expect to incur in connection therewith. Due to the complexity of environmental laws and regulations, the varying costs and effectiveness of alternative cleanup methods and technologies, the uncertainty of insurance coverage and the unresolved extent of our responsibility, it is difficult to determine the ultimate outcome of these matters. However, in the opinion of management, we do not expect any additional liability to have a material effect on our financial position, results of operations or liquidity. Additional information regarding the effect of compliance with environmental protection requirements and the resolution of environmental claims against us and our operations can be found in *Environmental Regulation* within Item 1, *Item 1A. Risk Factors, Commitments and Contingencies* within Item 7 of our Form 10-K for the year ended December 31, 2009 and *Note 11: Commitments and Contingencies* within Item 8 of our Form 10-K.

In addition, various other claims and legal proceedings generally incidental to the normal course of business are pending or threatened against us. While we cannot predict the outcome of these matters, in the opinion of management, any liability arising from them will not have a material adverse effect on our financial position, results of operations or liquidity.

**Table of Contents****ITEM 1A. RISK FACTORS**

You should carefully review and consider the information regarding certain factors which could materially affect our business, financial condition or future results set forth under Item 1A. Risk Factors in our Form 10-K for the year ended December 31, 2009. There have been no material changes from the factors disclosed in our Form 10-K for the year ended December 31, 2009, although we may disclose changes to such factors or disclose additional factors from time to time in our future filings with the Securities and Exchange Commission.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS****Issuer Purchases of Equity Securities**

| <b>Period</b>               | <b>Total<br/>Number of<br/>Shares<br/>Purchased<sup>(1)</sup></b> | <b>Average<br/>Price<br/>Paid<br/>per<br/>Share</b> | <b>Total<br/>Number of<br/>Shares<br/>Purchased<br/>as Part of<br/>Publicly<br/>Announced<br/>Plan</b> | <b>Approximate<br/>Dollar Value<br/>of<br/>Shares that<br/>May Yet Be<br/>Purchased<br/>Under the<br/>Plan<sup>(2)</sup></b> |
|-----------------------------|---|---|--|--|
| <b>April</b>                |   |   |  |  |
| (March 29 - April 25, 2010) | 3,006   | \$ 57.13  |  | \$ 2.6 billion   |
| <b>May</b>                  |   |   |  |  |
| (April 26 - May 23, 2010)   | 4,579,802   | \$ 57.44  | 4,260,256  | \$ 2.3 billion   |
| <b>June</b>                 |   |   |  |  |
| (May 24 - June 27, 2010)    | 4,531,369   | \$ 52.57  | 4,381,900  | \$ 2.1 billion   |
| <b>Total</b>                | <b>9,114,177</b>  | <b>\$ 55.02</b>                                     | <b>8,642,156</b>   |  |

- (1) Includes shares purchased related to treasury activity under our stock plans. Such activity during the second quarter of 2010 includes the surrender by employees of 472,021 shares to satisfy income tax withholding obligations in connection with the vesting of restricted stock previously issued to employees.
- (2) In October 2008, our Board of Directors authorized the repurchase of up to \$2.0 billion of our outstanding common stock and, in March 2010, authorized the repurchase of up to an additional \$2.0 billion of our outstanding common stock. Repurchases may take place from time to time at management's discretion depending upon market conditions.

**ITEM 6. EXHIBITS**

The following list of exhibits includes exhibits submitted with this Form 10-Q as filed with the Securities and Exchange Commission and those incorporated by reference to other filings.

- 3.1 Certificate of Amendment of Restated Certificate of Incorporation of Raytheon Company, as amended.\*
- 3.2 Raytheon Company By-Laws, as amended as of May 27, 2010, filed as an exhibit to the Company's Current Report on Form 8-K filed June 2, 2010, is hereby incorporated by reference.

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- 10.1 Raytheon 2010 Stock Plan, filed as Appendix B to the Company's definitive proxy statement filed on April 26, 2010, is hereby incorporated by reference.
- 15 PricewaterhouseCoopers LLP Awareness Letter.\*
- 31.1 Certification of William H. Swanson pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 31.2 Certification of David C. Wajsgas pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 32.1 Certification of William H. Swanson pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*



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32.2 Certification of David C. Wajsgras pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*

\* filed electronically herewith

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**RAYTHEON COMPANY**

By: /s/ Michael J. Wood  
Michael J. Wood  
Vice President and Chief Accounting Officer

*Principal Accounting Officer*

July 29, 2010