GENERAL DYNAMICS CORP
Form 10-Q
October 24, 2018

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2018
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 1-3671

GENERAL DYNAMICS CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	13-1673581
State or other jurisdiction of incorporation or organization	I.R.S. employer identification no.
2941 Fairview Park Drive, Suite 100 Falls Church, Virginia	22042-4513
Address of principal executive offices	Zip code

(703) 876-3000
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 ü No ___

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes ü No ___

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.
Large accelerated filer ü Accelerated filer ___ Non-accelerated filer ___
Smaller reporting company ___ Emerging growth company ___

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ___

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ___ No ü

296,149,755 shares of the registrant’s common stock, $1 par value per share, were outstanding on September 30, 2018.

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PART I – FINANCIAL INFORMATION

ITEM 1. UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF EARNINGS (UNAUDITED)

(Dollars in millions, except per-share amounts)	Three Months Ended September 30, 2018	October 1, 2017
Revenue:		
Products	$4,842	$ 4,718
Services	4,252	2,862
	9,094	7,580
Operating costs and expenses:		
Products	(3,797)	(3,635)
Services	(3,610)	(2,379)
General and administrative (G&A)	(552)	(503)
	(7,959)	(6,517)
Operating earnings	1,135	1,063
Interest, net	(114)	(27)
Other, net	2	(9)
Earnings from continuing operations before income tax	1,023	1,027
Provision for income tax, net	(159)	(263)
Earnings from continuing operations	864	764
Discontinued operations, net of tax	(13)	—
Net earnings	$851	$ 764
Earnings per share		
Basic:		
Continuing operations	$2.92	$ 2.56
Discontinued operations	(0.04)	—
Net earnings	$2.88	$ 2.56
Diluted:		
Continuing operations	$2.89	$ 2.52
Discontinued operations	(0.04)	—
Net earnings	$2.85	$ 2.52

The accompanying Notes to Unaudited Consolidated Financial Statements are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF EARNINGS (UNAUDITED)

(Dollars in millions, except per-share amounts)	Nine Months Ended September 30, 2018	Nine Months Ended October 1, 2017
Revenue:		
Products	$14,172	$13,851
Services	11,643	8,845
	25,815	22,696
Operating costs and expenses:		
Products	(11,045)	(10,670)
Services	(9,838)	(7,381)
G&A	(1,701)	(1,469)
	(22,584)	(19,520)
Operating earnings	3,231	3,176
Interest, net	(244)	(76)
Other, net	(34)	(31)
Earnings from continuing operations before income tax	2,953	3,069
Provision for income tax, net	(504)	(793)
Earnings from continuing operations	2,449	2,276
Discontinued operations, net of tax	(13)	—
Net earnings	$2,436	$2,276
Earnings per share		
Basic:		
Continuing operations	$8.27	$7.59
Discontinued operations	(0.04)	—
Net earnings	$8.23	$7.59
Diluted:		
Continuing operations	$8.16	$7.45
Discontinued operations	(0.04)	—
Net earnings	$8.12	$7.45

The accompanying Notes to Unaudited Consolidated Financial Statements are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)

(Dollars in millions)	Three Months Ended September 30, 2018	Three Months Ended October 1, 2017	Nine Months Ended September 30, 2018	Nine Months Ended October 1, 2017
Net earnings	$851	$ 764	$2,436	$2,276
Gains on cash flow hedges	61	138	40	286
Unrealized gains on marketable securities	—	1	—	8
Foreign currency translation adjustments	85	128	(130)	409
Change in retirement plans’ funded status	84	61	247	193
Other comprehensive income, pretax	230	328	157	896
Provision for income tax, net	(33)	(57)	(60)	(160)
Other comprehensive income, net of tax	197	271	97	736
Comprehensive income	$1,048	$ 1,035	$2,533	$3,012

The accompanying Notes to Unaudited Consolidated Financial Statements are an integral part of these financial statements.

CONSOLIDATED BALANCE SHEET

(Dollars in millions)	(Unaudited) September 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and equivalents	$ 1,010	$ 2,983
Accounts receivable	3,736	3,617
Unbilled receivables	7,564	5,240
Inventories	6,247	5,303
Other current assets	1,401	1,185
Total current assets	19,958	18,328
Noncurrent assets:		
Property, plant and equipment, net	4,244	3,517
Intangible assets, net	2,667	702
Goodwill	19,486	11,914
Other assets	608	585
Total noncurrent assets	27,005	16,718
Total assets	$ 46,963	$ 35,046
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Short-term debt and current portion of long-term debt	$ 1,678	$ 2
Accounts payable	3,033	3,207
Customer advances and deposits	7,327	6,992
Other current liabilities	3,651	2,898
Total current liabilities	15,689	13,099
Noncurrent liabilities:		
Long-term debt	11,403	3,980
Other liabilities	7,116	6,532
Commitments and contingencies (see Note M)		
Total noncurrent liabilities	18,519	10,512
Shareholders' equity:		
Common stock	482	482
Surplus	2,914	2,872
Retained earnings	28,691	26,444
Treasury stock	(15,971)	(15,543)
Accumulated other comprehensive loss	(3,361)	(2,820)
Total shareholders' equity	12,755	11,435
Total liabilities and shareholders' equity	$ 46,963	$ 35,046

The accompanying Notes to Unaudited Consolidated Financial Statements are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED)

(Dollars in millions)	Nine Months Ended September 30, 2018	October 1, 2017
Cash flows from operating activities - continuing operations:		
Net earnings	$2,436	$ 2,276
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation of property, plant and equipment	352	269
Amortization of intangible assets	190	57
Equity-based compensation expense	110	93
Deferred income tax (benefit) provision	(66)	155
Discontinued operations, net of tax	13	—
(Increase) decrease in assets, net of effects of business acquisitions:		
Accounts receivable	472	26
Unbilled receivables	(1,625)	(1,361)
Inventories	(854)	57
Increase (decrease) in liabilities, net of effects of business acquisitions:		
Accounts payable	(324)	167
Customer advances and deposits	112	(296)
Income taxes payable	250	223
Other, net	15	216
Net cash provided by operating activities	1,081	1,882
Cash flows from investing activities:		
Business acquisitions, net of cash acquired	(10,039)	(364)
Capital expenditures	(447)	(273)
Other, net	169	52
Net cash used by investing activities	(10,317)	(585)
Cash flows from financing activities:		
Proceeds from fixed-rate notes	6,461	985
Proceeds from (repayments of) commercial paper, net	1,668	(2)
Proceeds from floating-rate notes	1,000	—
Dividends paid	(801)	(735)
Purchases of common stock	(533)	(1,172)
Repayment of CSRA accounts receivable purchase agreement	(450)	—
Other, net	(68)	43
Net cash provided (used) by financing activities	7,277	(881)
Net cash used by discontinued operations	(14)	(28)
Net (decrease) increase in cash and equivalents	(1,973)	388
Cash and equivalents at beginning of period	2,983	2,334
Cash and equivalents at end of period	$1,010	$ 2,722
Supplemental cash flow information:		
Income tax payments, net	$305	$ 398
Interest payments	$144	$ 66

The accompanying Notes to Unaudited Consolidated Financial Statements are an integral part of these financial statements.

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CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY (UNAUDITED)

	Common Stock		Retained	Treasury	Accumulated Other Comprehensive	Total Shareholders'
(Dollars in millions)	Par	Surplus	Earnings	Stock	Loss	Equity
December 31, 2017	$482	$2,872	$26,444	$(15,543)	$ (2,820)	$ 11,435
Cumulative-effect adjustments (see Note A)	—	—	638	—	(638)	—
Net earnings	—	—	2,436	—	—	2,436
Cash dividends declared	—	—	(827)	—	—	(827)
Equity-based awards	—	42	—	95	—	137
Shares purchased	—	—	—	(523)	—	(523)
Other comprehensive income	—	—	—	—	97	97
September 30, 2018	$482	$2,914	$28,691	$(15,971)	$ (3,361)	$ 12,755
December 31, 2016	$482	$2,819	$24,543	$(14,156)	$ (3,387)	$ 10,301
Cumulative-effect adjustment*	—	—	(3)	—	—	(3)
Net earnings	—	—	2,276	—	—	2,276
Cash dividends declared	—	—	(758)	—	—	(758)
Equity-based awards	—	22	—	127	—	149
Shares purchased	—	—	—	(1,137)	—	(1,137)
Other comprehensive income	—	—	—	—	736	736
October 1, 2017	$482	$2,841	$26,058	$(15,166)	$ (2,651)	$ 11,564

The accompanying Notes to Unaudited Consolidated Financial Statements are an integral part of these financial statements.

* Reflects the cumulative effect of Accounting Standards Update (ASU) 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory, which we adopted on January 1, 2017.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in millions, except per-share amounts or unless otherwise noted)

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
Organization. General Dynamics is a global aerospace and defense company that offers a broad portfolio of products and services in business aviation; combat vehicles, weapons systems and munitions; information technology (IT) services; C4ISR (command, control, communications, computers, intelligence, surveillance and reconnaissance) solutions; and shipbuilding and ship repair.

On April 3, 2018, we completed our acquisition of CSRA Inc. (CSRA). See Note B for further discussion of the acquisition. For segment reporting purposes, concurrent with the acquisition, our Information Systems and Technology operating segment was reorganized into the Information Technology and Mission Systems segments. Our company now has five operating segments: Aerospace, Combat Systems, Information Technology, Mission Systems and Marine Systems. We collectively refer to Combat Systems, Information Technology, Mission Systems and Marine Systems as our defense segments. Prior-period segment information has been restated for this change.

We are divesting certain non-core operations in our Information Technology segment. Accordingly, the assets and liabilities of these operations, including an estimated allocation of goodwill, were classified as held for sale on September 30, 2018. As we expect these operations to be divested within the next 12 months, the assets and liabilities held for sale are included in other current assets and liabilities on the unaudited Consolidated Balance Sheet.

Basis of Consolidation and Classification. The unaudited Consolidated Financial Statements include the accounts of General Dynamics Corporation and our wholly owned and majority-owned subsidiaries. We eliminate all inter-company balances and transactions in the unaudited Consolidated Financial Statements. Some prior-year amounts have been reclassified among financial statement accounts or disclosures to conform to the current-year presentation.

Consistent with industry practice, we classify assets and liabilities related to long-term contracts as current, even though some of these amounts may not be realized within one year.

Further discussion of our significant accounting policies is contained in the other notes to these financial statements.

Interim Financial Statements. The unaudited Consolidated Financial Statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. These rules and regulations permit some of the information and footnote disclosures included in financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) to be condensed or omitted.

Our fiscal quarters are 13 weeks in length. Because our fiscal year ends on December 31, the number of days in our first and fourth quarters varies slightly from year to year. Operating results for the three- and nine-month periods ended September 30, 2018, are not necessarily indicative of the results that may be expected for the year ending December 31, 2018.

The unaudited Consolidated Financial Statements contain all adjustments that are of a normal recurring nature necessary for a fair presentation of our results of operations and financial condition for the three- and nine-month periods ended September 30, 2018, and October 1, 2017.

These unaudited Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2017.

Discontinued Operations, Net of Tax. Concurrent with the acquisition of CSRA, we were required by a government customer to dispose of certain CSRA operations to address an organizational conflict of interest with respect to services provided to the customer. In the third quarter of 2018, we sold these operations. In accordance with GAAP, the sale did not result in a gain for financial reporting purposes. However, the sale generated a taxable gain, resulting in tax expense of $13.

Accounting Standards Updates. On January 1, 2018, we adopted the following accounting standards issued by the Financial Accounting Standards Board (FASB):

- ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. ASU 2016-01 addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. Specific to our business, ASU 2016-01 requires equity investments to be measured at fair value with changes in fair value recognized in net income. The ASU eliminates the available-for-sale classification for equity investments that recognized changes in fair value as a component of other comprehensive income. We adopted the standard on a modified retrospective basis on January 1, 2018, and recognized the cumulative effect as a $24 increase to retained earnings on the date of adoption.
- ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. ASU 2016-15 is intended to reduce diversity in practice in how certain cash receipts and cash payments are presented and classified in the Consolidated Statement of Cash Flows by providing guidance on eight specific cash flow issues. We adopted the standard retrospectively on January 1, 2018. The adoption of the ASU did not have a material effect on our cash flows for the nine-month period ended October 1, 2017.
- ASU 2017-07, Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. ASU 2017-07 requires the service cost component of net retirement benefit cost to be reported separately from the other components of net retirement benefit cost in the Consolidated Statement of Earnings. We adopted the standard retrospectively on January 1, 2018. Our restated operating earnings increased $11 and $33 for the three- and nine-month periods ended October 1, 2017, respectively, due to the reclassification of the non-service cost components of net benefit cost, and other income decreased by the same amount, with no impact to net earnings.
- ASU 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. ASU 2018-02 allows the reclassification from accumulated other comprehensive income to retained earnings of stranded tax effects resulting from the implementation of the Tax Cuts and Jobs Act (tax reform) enacted on December 22, 2017. We adopted the standard on January 1, 2018, and recognized a $614 increase to retained earnings on the date of adoption.

There are several other accounting standards that have been issued by the FASB but are not yet effective, including the following:

- ASU 2016-02, Leases (Topic 842). ASU 2016-02 requires the recognition of lease rights and obligations as assets and liabilities on the balance sheet. Previously, lessees were not required to recognize on the balance sheet assets and liabilities arising from operating leases. The ASU also requires disclosure of key information about leasing arrangements. ASU 2016-02 is effective on January 1, 2019, using a modified retrospective method of adoption as of January 1, 2017. In July 2018, the FASB issued ASU 2018-11, Leases (Topic 842): Targeted Improvements, that provides an alternative transition method of adoption, permitting the recognition of a cumulative-effect adjustment to retained earnings on the date of adoption.

We intend to adopt the standard on the effective date using the alternative transition method provided by ASU 2018-11. We are currently evaluating our population of leased assets in order to assess the impact of the ASU on our lease portfolio, and designing and implementing new processes and controls. Until this effort is completed, we cannot determine the effect of the ASU on our results of operations, financial condition or cash flows.

- ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities. ASU 2017-12 is intended to simplify hedge accounting by better aligning an entity’s financial reporting for hedging relationships with its risk management activities. The ASU also simplifies the application of the hedge accounting guidance. ASU 2017-12 is effective on January 1, 2019, with early adoption permitted. For cash flow hedges existing at the adoption date, the standard requires adoption on a modified retrospective basis with a cumulative-effect adjustment to the Consolidated Balance Sheet as of the beginning of the year of adoption. The amendments to presentation guidance and disclosure requirements are required to be adopted prospectively. We intend to adopt the standard on the effective date, and we do not expect the adoption of the ASU to have a material effect on our results of operations, financial condition or cash flows.

B. ACQUISITIONS AND DIVESTITURES, GOODWILL, AND INTANGIBLE ASSETS

CSRA Acquisition

On April 3, 2018, we acquired 100% of the outstanding shares of CSRA Inc. (CSRA) for $41.25 per share in cash. CSRA has been combined with General Dynamics Information Technology (GDIT) to create a premier provider of IT solutions to the defense, intelligence and federal civilian markets. Except where otherwise noted in the Notes to Unaudited Consolidated Financial Statements, changes in balances and activity were generally driven by the CSRA acquisition.

Purchase Price and Fair Value of Net Assets Acquired. The cash purchase price totaled $9.7 billion and consisted of the following:

CSRA shares outstanding (in millions)	165.4
Cash consideration per CSRA share	$41.25
Cash paid to purchase outstanding CSRA shares	$6,825
Cash paid to extinguish CSRA debt	2,846
Cash settlement of outstanding CSRA stock options and restricted stock units	78
Total purchase price	$9,749

The following table summarizes the preliminary allocation of the purchase price to the estimated fair values of the assets acquired and liabilities assumed on the acquisition date, with the excess recorded as goodwill:

Cash and equivalents	$45
Accounts receivable	145
Unbilled receivables	718
Other current assets	290
Property, plant and equipment, net	684
Intangible assets, net	2,069
Goodwill	7,792
Other noncurrent assets	20
Total assets	$11,763
Account payable	$(136)
Customer advances and deposits	(151)
Current capital lease obligation	(51)
Other current liabilities	(540)
Noncurrent capital lease obligation	(207)
Noncurrent deferred tax liability	(406)
Other noncurrent liabilities	(523)
Total liabilities	$(2,014)
Net assets acquired	$9,749

During the quarter ended September 30, 2018, we continued to obtain information to refine the estimated fair values. The additional information obtained during the quarter did not result in any material adjustments. However, these provisional amounts are subject to change as we complete the valuations throughout the measurement period, which will extend throughout 2018.

The $2.1 billion of estimated acquired intangible assets consists of acquired backlog and probable follow-on work and associated customer relationships (contract and program intangible assets), with a weighted-average life of 17 years. The intangible assets will be amortized using an accelerated method, which approximates the pattern of how the economic benefit is expected to be used. Under this method, approximately 50% of the aggregate value of the intangible assets will be amortized within six years. We expect to record amortization expense associated with these intangible assets over the next five years as follows:

2018 (9 months post-acquisition)	$188
2019	204
2020	195
2021	154
2022	136

Goodwill represents the purchase price paid in excess of the fair value of net tangible and intangible assets acquired, and is attributable primarily to expected synergies, economies of scale and the assembled workforce of CSRA. Approximately $490 of this goodwill is pre-acquisition goodwill deductible for income tax purposes over its remaining tax life.

CSRA’s operating results have been included with our reported results since the acquisition date. As we immediately began integrating CSRA with GDIT following the acquisition, it is becoming increasingly difficult to separate the results of legacy CSRA from those of the combined entity. Approximately $1.2 billion and $2.5 billion of revenue, $130 and $265 of operating earnings, and $140 and $285 of pretax earnings from legacy CSRA were included in our unaudited Consolidated Statement of Earnings for the three- and nine-month periods ended September 30, 2018, respectively. These amounts exclude amortization of intangible assets and acquisition financing.

In addition, we have recognized approximately $75 of one-time, acquisition-related costs, reported in operating costs and expenses and other income (expense) in the unaudited Consolidated Statement of Earnings.

Pro Forma Information. The following pro forma information presents our consolidated revenue and earnings from continuing operations as if the acquisition of CSRA and the related financing transactions had occurred on January 1, 2017:

	Three Months Ended		Nine Months Ended	
	September 30, 2018	October 1, 2017	September 30, 2018	October 1, 2017
Revenue	$9,094	$8,799	$27,156	$26,296
Earnings from continuing operations	872	776	2,470	2,213
Diluted earnings per share from continuing operations	$2.92	$2.55	$8.23	$7.24

The pro forma information was prepared by combining our reported historical results with the historical results of CSRA for the pre-acquisition periods. In addition, the reported historical amounts were adjusted for the following items, net of associated tax effects:

- The impact of acquisition financing.
- The removal of certain CSRA operations we were required by a government customer to dispose of to address an organizational conflict of interest with respect to services provided to the customer. We completed the sale of these operations in the third quarter of 2018.
- The removal of CSRA's historical pre-acquisition intangible asset amortization expense and debt-related interest expense.
- The impact of intangible asset amortization expense assuming our current estimate of fair value was applied on January 1, 2017.
- The payment of acquisition-related costs assuming they were incurred on January 1, 2017.

The pro forma information is based on the preliminary amounts allocated to the estimated fair value of net assets acquired and may be revised as the provisional amounts change. The pro forma information does not reflect the realization of expected cost savings or synergies from the acquisition, and does not reflect what our combined results of operations would have been had the acquisition occurred on January 1, 2017.

Other Acquisitions and Divestitures

In addition to the acquisition of CSRA, we acquired two businesses in the first nine months of 2018 for an aggregate of $335: Hawker Pacific, a leading provider of integrated aviation solutions across Asia Pacific and the Middle East, in our Aerospace segment, and a provider of specialized transmitters and receivers in our Mission Systems segment. In 2017, we acquired four businesses for an aggregate of $399: a fixed-base operation (FBO) in our Aerospace segment; a provider of mission-critical support services in our Information Technology segment; and a manufacturer of electronics and communications products and a manufacturer of signal distribution products in our Mission Systems segment.

The operating results of these acquisitions have been included with our reported results since the respective closing dates. The purchase prices of the acquisitions have been allocated to the estimated fair value of net tangible and intangible assets acquired, with any excess purchase price recorded as goodwill.
In the first nine months of 2018, we completed the sale of a commercial health products business in our Information Technology segment and the sale of certain CSRA operations we were required by a government customer to dispose of to address an organizational conflict of interest with respect to services provided to the customer. The proceeds from the sales are included in other investing activities in the unaudited Consolidated Statement of Cash Flows.
Goodwill
The changes in the carrying amount of goodwill by reporting unit were as follows:

	Aerospace	Combat Systems	Information Systems and Technology	Information Technology	Mission Systems	Marine Systems	Total Goodwill
December 31, 2017 (a)	$ 2,638	$ 2,677	$ 6,302	$ —	$ —	$ 297	$ 11,914
Acquisitions/ divestitures (b)	—	—	16	—	—	—	16
Other (c)	40	(14)	(1)	—	—	—	25
April 1, 2018 (a)	2,678	2,663	6,317	—	—	297	11,955
Change in reporting unit composition (d)	—	—	(6,317)	2,076	4,241	—	—
Acquisitions/ divestitures (b)	148	—	—	7,796	1	—	7,945
Other (c)	(37)	(21)	—	(347)	(9)	—	(414)
September 30, 2018 (e)	$ 2,789	$ 2,642	$ —	$ 9,525	$ 4,233	$ 297	$ 19,486

(a)Goodwill in the Information Systems and Technology reporting unit is net of $1.9 billion of accumulated impairment losses.
(b)Includes adjustments during the purchase price allocation period. Activity in the first quarter of 2018 also includes an allocation of goodwill associated with the sale of the commercial health products business discussed above.
(c)Consists primarily of adjustments for foreign currency translation. Activity in the six-month period ended September 30, 2018, also includes an allocation of goodwill in our Information Technology reporting unit associated with the operations classified as held for sale on the unaudited Consolidated Balance Sheet on September 30, 2018.
(d)Concurrent with the acquisition of CSRA, we reorganized our Information Systems and Technology operating segment into the Information Technology and Mission Systems segments. See Note A for further discussion of the segment reorganization. This reorganization similarly changed the composition of our reporting units. Accordingly, goodwill of the Information Systems and Technology reporting unit was reassigned to the Information Technology and Mission Systems reporting units using a relative fair value allocation approach as of the date of the reorganization.
(e)Goodwill in the Information Technology and Mission Systems reporting units is net of $526 and $1.3 billion of accumulated impairment losses, respectively.
Intangible Assets
Intangible assets consisted of the following:

	Gross Carrying Amount (a)	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount (a)	Accumulated Amortization	Net Carrying Amount
	September 30, 2018			December 31, 2017		
Contract and program intangible assets (b)	$ 3,792	$ (1,473)	$ 2,319	$ 1,684	$ (1,320)	$ 364
Trade names and trademarks	468	(173)	295	465	(160)	305
Technology and software	167	(115)	52	137	(105)	32
Other intangible assets	155	(154)	1	155	(154)	1

Total intangible assets	$4,582	$ (1,915)	$ 2,667	$2,441	$ (1,739)	$ 702

(a) Change in gross carrying amounts consists primarily of adjustments for acquired intangible assets and foreign currency translation.

(b) Consists of acquired backlog and probable follow-on work and associated customer relationships.

Amortization expense was $86 and $190 for the three- and nine-month periods ended September 30, 2018, and $19 and $57 for the three- and nine-month periods ended October 1, 2017.

C. REVENUE

The majority of our revenue is derived from long-term contracts and programs that can span several years. We account for revenue in accordance with ASC Topic 606, Revenue from Contracts with Customers.

Performance Obligations. A performance obligation is a promise in a contract to transfer a distinct good or service to the customer, and is the unit of account in ASC Topic 606. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. The majority of our contracts have a single performance obligation as the promise to transfer the individual goods or services is not separately identifiable from other promises in the contracts and is, therefore, not distinct. Some of our contracts have multiple performance obligations, most commonly due to the contract covering multiple phases of the product lifecycle (development, production, maintenance and support). For contracts with multiple performance obligations, we allocate the contract's transaction price to each performance obligation using our best estimate of the standalone selling price of each distinct good or service in the contract. The primary method used to estimate standalone selling price is the expected cost plus a margin approach, under which we forecast our expected costs of satisfying a performance obligation and then add an appropriate margin for that distinct good or service.

Contract modifications are routine in the performance of our contracts. Contracts are often modified to account for changes in contract specifications or requirements. In most instances, contract modifications are for goods or services that are not distinct and, therefore, are accounted for as part of the existing contract.

Our performance obligations are satisfied over time as work progresses or at a point in time. Revenue from products and services transferred to customers over time accounted for 74% and 75% of our revenue for the three- and nine-month periods ended September 30, 2018, and 70% of our revenue for the three- and nine-month periods ended October 1, 2017, respectively. Substantially all of our revenue in the defense segments is recognized over time because control is transferred continuously to our customers. Typically, revenue is recognized over time using costs incurred to date relative to total estimated costs at completion to measure progress toward satisfying our performance obligations. Incurred cost represents work performed, which corresponds with, and thereby best depicts, the transfer of control to the customer. Contract costs include labor, material, overhead and, when appropriate, G&A expenses.

Revenue from goods and services transferred to customers at a point in time accounted for 26% and 25% of our revenue for the three- and nine-month periods ended September 30, 2018, and 30% of our revenue for the three- and nine-month periods ended October 1, 2017, respectively. The majority of our revenue recognized at a point in time is for the manufacture of business-jet aircraft in our Aerospace segment. Revenue on these contracts is recognized when the customer obtains control of the asset, which is generally upon delivery and acceptance by the customer of the fully outfitted aircraft.

On September 30, 2018, we had $69.5 billion of remaining performance obligations, which we also refer to as total backlog. We expect to recognize approximately 50% of our remaining performance obligations as revenue by year-end 2019, an additional 30% by year-end 2021 and the balance thereafter. On December 31, 2017, we had $63.2 billion of remaining performance obligations, at which time we expected to recognize approximately 40% of these remaining performance obligations as revenue in 2018, an additional 40% by year-end 2020 and the balance thereafter.

Contract Estimates. Accounting for long-term contracts and programs involves the use of various techniques to estimate total contract revenue and costs. For long-term contracts, we estimate the profit on

a contract as the difference between the total estimated revenue and expected costs to complete a contract and recognize that profit over the life of the contract.
Contract estimates are based on various assumptions to project the outcome of future events that often span several years. These assumptions include labor productivity and availability; the complexity of the work to be performed; the cost and availability of materials; the performance of subcontractors; and the availability and timing of funding from the customer.
The nature of our contracts gives rise to several types of variable consideration, including claims and award and incentive fees. We include in our contract estimates additional revenue for submitted contract modifications or claims against the customer when we believe we have an enforceable right to the modification or claim, the amount can be estimated reliably and its realization is probable. In evaluating these criteria, we consider the contractual/legal basis for the claim, the cause of any additional costs incurred, the reasonableness of those costs and the objective evidence available to support the claim. We include award or incentive fees in the estimated transaction price when there is a basis to reasonably estimate the amount of the fee. These estimates are based on historical award experience, anticipated performance and our best judgment at the time. Because of our certainty in estimating these amounts, they are included in the transaction price of our contracts and the associated remaining performance obligations.
As a significant change in one or more of these estimates could affect the profitability of our contracts, we review and update our contract-related estimates regularly. We recognize adjustments in estimated profit on contracts under the cumulative catch-up method. Under this method, the impact of the adjustment on profit recorded to date on a contract is recognized in the period the adjustment is identified. Revenue and profit in future periods of contract performance are recognized using the adjusted estimate. If at any time the estimate of contract profitability indicates an anticipated loss on the contract, we recognize the total loss in the period it is identified.
The impact of adjustments in contract estimates on our operating earnings can be reflected in either operating costs and expenses or revenue. The aggregate impact of adjustments in contract estimates increased our revenue, operating earnings and diluted earnings per share as follows:

	Three Months Ended		Nine Months Ended	
	September 30, 2018	October 1, 2017	September 30, 2018	October 1, 2017
Revenue	$ 96	$ 94	$ 302	$ 256
Operating earnings	103	103	283	274
Diluted earnings per share	$ 0.27	$ 0.22	$ 0.75	$ 0.58

No adjustment on any one contract was material to the unaudited Consolidated Financial Statements for the three- and nine-month periods ended September 30, 2018, or October 1, 2017.
Revenue by Category. Our portfolio of products and services consists of over 10,000 active contracts. The following series of tables presents our revenue disaggregated by several categories.

Revenue by major products and services was as follows:

	Three Months Ended		Nine Months Ended	
	September 30, 2018	October 1, 2017	September 30, 2018	October 1, 2017
Aircraft manufacturing and completions	$1,437	$1,562	$4,165	$4,791
Aircraft services	525	422	1,507	1,302
Pre-owned aircraft	69	11	79	54
Total Aerospace	2,031	1,995	5,751	6,147
Wheeled combat and tactical vehicles	657	623	1,926	1,749
Weapons systems, armament and munitions	425	412	1,251	1,167
Tanks and tracked vehicles	334	315	1,011	840
Engineering and other services	107	150	309	445
Total Combat Systems	1,523	1,500	4,497	4,201
Information technology services	2,307	1,068	5,887	3,178
Total Information Technology	2,307	1,068	5,887	3,178
Platform systems and sensors	423	387	1,197	1,170
Intelligence, surveillance and reconnaissance systems	398	351	1,147	1,013
Communication systems	409	348	1,131	1,043
Total Mission Systems	1,230	1,086	3,475	3,226
Nuclear-powered submarines	1,369	1,248	4,103	3,794
Surface combatants	293	256	834	757
Auxiliary and commercial ships	152	129	567	427
Repair and other services	189	298	701	966
Total Marine Systems	2,003	1,931	6,205	5,944
Total revenue	$9,094	$7,580	$25,815	$22,696

Revenue by contract type was as follows:

Three Months Ended September 30, 2018	Aerospace	Combat Systems	Information Technology	Mission Systems	Marine Systems	Total Revenue
Fixed-price	$ 1,807	$ 1,309	$ 941	$ 695	$ 1,284	$ 6,036
Cost-reimbursement	—	204	955	499	718	2,376
Time-and-materials	224	10	411	36	1	682
Total revenue	$ 2,031	$ 1,523	$ 2,307	$ 1,230	$ 2,003	$ 9,094
Three Months Ended October 1, 2017						
Fixed-price	$ 1,835	$ 1,258	$ 359	$ 612	$ 1,131	$ 5,195
Cost-reimbursement	—	233	552	437	797	2,019
Time-and-materials	160	9	157	37	3	366
Total revenue	$ 1,995	$ 1,500	$ 1,068	$ 1,086	$ 1,931	$ 7,580

Nine Months Ended September 30, 2018	Aerospace	Combat Systems	Information Technology	Mission Systems	Marine Systems	Total Revenue
Fixed-price	$ 5,171	$ 3,892	$ 2,387	$ 1,973	$ 3,961	$ 17,384
Cost-reimbursement	—	580	2,462	1,390	2,241	6,673
Time-and-materials	580	25	1,038	112	3	1,758
Total revenue	$ 5,751	$ 4,497	$ 5,887	$ 3,475	$ 6,205	$ 25,815
Nine Months Ended October 1, 2017						
Fixed-price	$ 5,650	$ 3,538	$ 1,049	$ 1,744	$ 3,514	