UNITED TECHNOLOGIES CORP /DE/
Form 10-Q
October 18, 2007
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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 September 30, 2007

OR

¨ **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 1-812

UNITED TECHNOLOGIES CORPORATION

DELAWARE	**06-0570975**

One Financial Plaza, Hartford, Connecticut 06103

(860) 728-7000

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

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

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

At September 30, 2007 there were 988,508,102 shares of common stock outstanding.

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UNITED TECHNOLOGIES CORPORATION

AND SUBSIDIARIES

CONTENTS OF QUARTERLY REPORT ON FORM 10-Q

Quarter Ended September 30, 2007

We, us, our and UTC, unless the context otherwise requires, means United Technologies Corporation and its subsidiaries.

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Part I Financial Information

Item 1. Financial Statements

CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS

(Unaudited)

In Millions (except per share amounts)	Quarter Ended September 30, 2007	2006
Revenues:		
Product sales	$ 9,960	$ 8,738
Service sales	3,758	3,234
Other income, net	145	191
	13,863	12,163
Costs and expenses:		
Cost of products sold	7,533	6,659
Cost of services sold	2,535	2,135
Research and development	399	384
Selling, general and administrative	1,508	1,338
Operating Profit	1,888	1,647
Interest	179	156
Income before income taxes and minority interests	1,709	1,491
Income tax expense	(434)	(423)
Minority interests	(78)	(72)
Net income	$ 1,197	$ 996
Earnings per share of Common Stock:		
Basic	$ 1.24	$ 1.02
Diluted	$ 1.21	$ .99
Dividends per share of Common Stock	$ .32	$ .27
Average number of shares outstanding:		
Basic	963	980
Diluted	989	1,006

See accompanying Notes to Condensed Consolidated Financial Statements

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CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS

(Unaudited)

In Millions (except per share amounts)	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Revenues:		
Product sales	$ 28,691	$ 25,169
Service sales	10,729	9,295
Other income, net	625	578
	40,045	35,042
Costs and expenses:		
Cost of products sold	21,851	18,960
Cost of services sold	7,342	6,259
Research and development	1,197	1,123
Selling, general and administrative	4,398	4,030
Operating Profit	5,257	4,670
Interest	492	453
Income before income taxes and minority interests	4,765	4,217
Income tax expense	(1,355)	(1,157)
Minority interests	(246)	(193)
Net income	$ 3,164	$ 2,867
Earnings per share of Common Stock:		
Basic	$ 3.28	$ 2.92
Diluted	$ 3.19	$ 2.84
Dividends per share of Common Stock	$ .85	$ .75
Average number of shares outstanding:		
Basic	966	983
Diluted	991	1,008

See accompanying Notes to Condensed Consolidated Financial Statements

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CONDENSED CONSOLIDATED BALANCE SHEET

(Unaudited)

In Millions	September 30, 2007	December 31, 2006
Assets		
Cash and cash equivalents	$ 2,810	$ 2,546
Accounts receivable, net	8,999	7,679
Inventories and contracts in progress, net	8,550	6,657
Future income tax benefits	1,303	1,261
Other current assets	899	701
Total Current Assets	22,561	18,844
Customer financing assets	962	1,073
Future income tax benefits	1,668	1,690
Fixed assets	14,609	13,738
Less: Accumulated depreciation	(8,556)	(8,013)
Net Fixed Assets	6,053	5,725
Goodwill	15,871	14,146
Intangible assets	3,709	3,216
Other assets	2,673	2,447
Total Assets	$ 53,497	$ 47,141
Liabilities and Shareowners Equity		
Short-term borrowings	$ 2,221	$ 857
Accounts payable	4,977	4,263
Accrued liabilities	11,389	10,051
Long-term debt currently due	47	37
Total Current Liabilities	18,634	15,208
Long-term debt	7,059	7,037
Future pension and postretirement benefit obligations	2,234	2,926
Other long-term liabilities	4,428	3,837
Total Liabilities	32,355	29,008
Minority interests in subsidiary companies	864	836
Shareowners Equity:		
Common Stock	10,424	9,622
Treasury Stock	(10,840)	(9,413)
Retained earnings	21,004	18,754
Unearned ESOP shares	(216)	(227)
Accumulated other non-shareowners changes in equity	(94)	(1,439)
Total Shareowners Equity	20,278	17,297

Total Liabilities and Shareowners Equity	$ 53,497	$ 47,141

See accompanying Notes to Condensed Consolidated Financial Statements

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CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

(Unaudited)

In Millions	Nine Months Ended September 30, 2007	2006
Operating Activities:		
Net income	$ 3,164	$ 2,867
Adjustments to reconcile net income to net cash flows provided by operating activities:		
Depreciation and amortization	863	772
Deferred income tax provision	(148)	16
Minority interests in subsidiaries earnings	246	193
Stock compensation cost	141	136
Change in:		
Accounts receivable	(787)	(203)
Inventories and contracts in progress	(1,616)	(1,388)
Accounts payable and accrued liabilities	1,849	989
Other current assets	(19)	(79)
Voluntary contributions to global pension plans*		(31)
Other, net	(408)	(124)
Net cash flows provided by operating activities	3,285	3,148
Investing Activities:		
Capital expenditures	(697)	(603)
Investments in businesses	(1,634)	(518)
Dispositions of businesses	190	345
(Increase) decrease in customer financing assets, net	(23)	47
Other, net	8	62
Net cash flows used in investing activities	(2,156)	(667)
Financing Activities:		
(Repayment) Issuance of long-term debt, net	(265)	835
Increase (decrease) in short-term borrowings, net	1,330	(871)
Common Stock issued under employee stock plans	372	258
Dividends paid on Common Stock	(786)	(705)
Repurchase of Common Stock	(1,500)	(1,330)
Other, net	(153)	(63)
Net cash flows used in financing activities	(1,002)	(1,876)
Effect of foreign exchange rate changes on Cash and cash equivalents	137	62
Net increase in Cash and cash equivalents	264	667
Cash and cash equivalents, beginning of year	2,546	2,247
Cash and cash equivalents, end of period	$ 2,810	$ 2,914

*

Non-cash activities include contributions of UTC common stock of $150 million to domestic defined benefit pension plans in both 2007 and 2006.

See accompanying Notes to Condensed Consolidated Financial Statements

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

The Condensed Consolidated Financial Statements at September 30, 2007 and for the quarters and nine months ended September 30, 2007 and 2006 are unaudited, but in the opinion of management include all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the results for the interim periods. The results reported in these Condensed Consolidated Financial Statements should not necessarily be taken as indicative of results that may be expected for the entire year. The financial information included herein should be read in conjunction with the financial statements and notes in our Annual Report incorporated by reference in our Form 10-K for calendar year 2006.

Note 1: Acquisitions, Dispositions, Goodwill and Other Intangible Assets

Business Acquisitions. During the first nine months of 2007, our investment in businesses was approximately $1.9 billion, including debt assumed of approximately $300 million, and consisted largely of the acquisition of Initial Electronic Security Group (IESG), a division of Rentokil Initial, plc, and Marioff Corporation, Oy (Marioff) both now part of the UTC Fire & Security segment, and a number of small acquisitions in both the commercial and aerospace businesses.

On July 2, 2007, we closed on the previously announced acquisition of IESG with the exception of the French operations, which still requires regulatory approval. The purchase price of the acquired portion was approximately $1.1 billion. The acquisition of IESG is expected to enhance UTC Fire & Security s scale and capability in the electronic security business in key markets where we have a significant presence. IESG sells integrated security systems, intrusion detection, closed circuit television, access control and security software. It is headquartered in the United Kingdom, with operations in the United Kingdom, the Netherlands, and the United States, and had sales of approximately $480 million in 2006. Marioff, acquired in August 2007 for approximately $348 million, is a global provider of water mist fire suppression systems for land and marine applications.

The assets and liabilities of acquired businesses are recorded at fair value at the date of acquisition under the purchase method. The final purchase price allocation of all acquired businesses is subject to the completion of the valuation of certain assets and liabilities, as well as plans for consolidation of facilities, the relocation or reduction of employees and other restructuring activities.

We also intend to divest UTC Fire & Security s manned guarding businesses in Australia, New Zealand and the United Kingdom. The combined revenues of these guarding businesses are approximately $600 million annually. The acquisition of IESG and Marioff, coupled with the divestiture of these low-technology manned guarding businesses, is intended to assist in the transition of UTC Fire & Security s portfolio towards higher margin and growth opportunities.

Goodwill. Changes in our goodwill balances for the first nine months of 2007 were as follows:

In Millions	Balance as of January 1, 2007	Goodwill resulting from business combinations	Foreign currency translation and other	Balance as of September 30, 2007
Otis	$ 1,305	$ 18	$ 26	$ 1,349
Carrier	2,604	180	51	2,835
UTC Fire & Security	4,430	1,198	136	5,764
Pratt & Whitney	1,002	23		1,025
Hamilton Sundstrand	4,525	30	29	4,584
Sikorsky	192	36		228
Total Segments	14,058	1,485	242	15,785
Eliminations & Other	88		(2)	86
Total	$ 14,146	$ 1,485	$ 240	$ 15,871

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Intangible Assets. Identifiable intangible assets are comprised of the following:

	September 30, 2007		December 31, 2006	
	Gross	Accumulated	Gross	Accumulated
In Millions	**Amount**	**Amortization**	**Amount**	**Amortization**
Amortizable:				
Service portfolios	$ 1,398	$ (600)	$ 1,304	$ (507)
Patents and trademarks	367	(91)	362	(79)
Other, principally customer relationships	2,480	(597)	1,845	(421)
	4,245	(1,288)	3,511	(1,007)
Unamortizable:				
Trademarks and other	752		712	
Totals	$ 4,997	$ (1,288)	$ 4,223	$ (1,007)

Amortization of intangible assets for the quarter and nine months ended September 30, 2007 was $87 million and $238 million, respectively, compared with $67 million and $199 million for the same periods of 2006. Amortization of these intangible assets for 2007 through 2011 is expected to approximate $285 million per year.

Note 2: Earnings Per Share

	Quarter Ended		Nine Months Ended	
	September 30,		September 30,	
(In millions except per share amounts)	**2007**	**2006**	**2007**	**2006**
Net income	$ 1,197	$ 996	$ 3,164	$ 2,867
Average shares:				
Basic	963	980	966	983
Stock awards	26	26	25	25
Diluted	989	1,006	991	1,008
Earnings per share of Common Stock:				
Basic	$ 1.24	$ 1.02	$ 3.28	$ 2.92
Diluted	$ 1.21	$ .99	$ 3.19	$ 2.84

Note 3: Inventories and Contracts in Progress

Inventories consist of the following:

	September 30,	December 31,
In Millions	**2007**	**2006**
Raw materials	$ 1,274	$ 1,082
Work-in-process	2,820	2,409

Finished goods	4,032	2,956
Contracts in progress	4,731	3,603
	12,857	10,050
Less:		
Progress payments, secured by lien, on U.S. Government contracts	(277)	(259)
Billings on contracts in progress	(4,030)	(3,134)
	$ 8,550	$ 6,657

Note 4: Borrowings and Lines of Credit

At September 30, 2007, we had credit commitments from banks totaling $2.5 billion. We had a credit commitment of $1.5 billion under a revolving credit agreement serving as a back-up facility for the issuance of commercial paper. As of September 30, 2007, there were no borrowings under this revolving credit agreement, which expires in October 2011. We also have a $1.0 billion multi-currency revolving credit agreement that is to be used for general corporate funding purposes, including acquisitions. As of September 30, 2007, approximately $979 million had been borrowed under this revolving credit agreement to fund general corporate purposes and the IESG acquisition. This credit agreement expires in November 2011.

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In July 2007, we replaced our existing shelf registration statement by filing with the Securities & Exchange Commission (SEC) a universal shelf registration statement for an indeterminate amount of securities for future issuance. As of September 30, 2007, no securities had been issued under this shelf registration statement.

Note 5: Income Taxes

We adopted the provisions of Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes, on January 1, 2007. As a result of this adoption, we recognized a charge of approximately $19 million to the January 1, 2007 retained earnings balance. As of the adoption date, we had gross tax-affected unrecognized tax benefits of $815 million of which $604 million, if recognized, would affect the effective tax rate. Also as of the adoption date, we had accrued interest expense related to the unrecognized tax benefits of $142 million. We recognize interest accrued related to unrecognized tax benefits in interest expense. Penalties, if incurred, would be recognized as a component of income tax expense. In the normal course of business, we provide for uncertain tax positions and adjust our unrecognized tax benefits, including related interest, accordingly.

We conduct business globally and, as a result, UTC or one or more of our subsidiaries files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. In the normal course of business, we are subject to examination by taxing authorities throughout the world, including such major jurisdictions as Australia, Canada, China, France, Germany, Hong Kong, Italy, Japan, Korea, Singapore, Spain, the U.K. and the United States. With few exceptions, we are no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations for years before 1998.

The Internal Revenue Service (IRS) review of tax years 2004 and 2005 is ongoing. IRS examination fieldwork for tax years 2000 through 2003 was completed in the second quarter of 2007. In the third quarter of 2007, UTC filed a protest with respect to certain IRS-proposed adjustments with which it does not agree. Those adjustments will be addressed with the Appeals Division of the IRS. The timing of any resolution is currently uncertain.

We recorded a $50 million reduction in tax expense in the quarter relating to a re-evaluation of our liabilities and contingencies based on global examination activity in the quarter, including completion of our review of the 2000 to 2003 IRS audit report and our protest filing and the development of claims for research & development credits, net of charges associated with tax law changes enacted in the quarter. In addition, we recognized approximately $28 million of associated pre-tax interest income in the third quarter of 2007.

Gross tax-affected unrecognized tax benefits at September 30, 2007 were $701 million of which $521 million, if recognized, would impact the effective tax rate. The net decrease in the quarter of $139 million is principally attributable to IRS tax adjustments associated with tax years 2000 through 2003 which we agreed not to appeal in the quarter. Accrued interest expense related to the unrecognized tax benefits was $169 million at September 30, 2007.

Note 6: Employee Benefit Plans

Pension and Postretirement Plans. We sponsor both funded and unfunded domestic and foreign defined pension and postretirement plans. Cash contributions to these plans during the quarters and nine months ended September 30, 2007 and 2006 were as follows:

	Quarter Ended		Nine Months Ended	
	September 30,		September 30,	
In Millions	2007	2006	2007	2006
Defined Benefit Plans:				
Voluntary	$	$ 31	$	$ 31
Mandatory	26	19	54	58
Total Defined Benefit Plans	$ 26	$ 50	$ 54	$ 89
Defined Contribution Plans	$ 47	$ 42	$ 153	$ 144

We also contributed $150 million of UTC common stock to our defined benefit pension plans in both the first quarter of 2007 and the second quarter of 2006.

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We have early-adopted the measurement date (the date at which plan assets and the benefit obligation are measured) provisions of Statement of Financial Accounting Standards No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106 and 132(R) (SFAS 158), effective January 1, 2007. Under SFAS 158, the measurement date is required to be the company s fiscal year-end. The majority of our pension and postretirement plans previously used a November 30 measurement date. All plans are now measured as of December 31, consistent with the company s fiscal year-end. The non-cash effect of the adoption of the measurement date provisions of SFAS 158 increased shareowners equity by approximately $425 million and decreased long-term liabilities by approximately $620 million. There was no effect on our results of operations. The remaining provisions of SFAS 158 were effective for fiscal years ending after December 15, 2006 and, as such, were adopted during 2006.

The following table illustrates the components of net periodic benefit cost for our pension and other postretirement benefits:

	Pension Benefits Quarter Ended September 30,		Other Postretirement Benefits Quarter Ended September 30,	
In Millions	**2007**	**2006**	**2007**	**2006**
Service cost	$ 110	$ 107	$ 2	$ 2
Interest cost	297	277	14	15
Expected return on plan assets	(387)	(349)	(1)	(1)
Amortization	11	9	(2)	(7)
Recognized actuarial net loss	63	81		
	94	125	13	9
Net settlement and curtailment (gain) loss	(1)	6		
Total net periodic benefit cost	$ 93	$ 131	$ 13	$ 9

	Pension Benefits Nine Months Ended September 30,		Other Postretirement Benefits Nine Months Ended September 30,	
In Millions	**2007**	**2006**	**2007**	**2006**
Service cost	$ 328	$ 325	$ 4	$ 6
Interest cost	884	837	42	43
Expected return on plan assets	(1,155)	(1,053)	(2)	(3)
Amortization	29	27	(6)	(19)
Recognized actuarial net loss	189	243		
	275	379	38	27
Net settlement and curtailment (gain) loss	(1)	12		
Total net periodic benefit cost	$ 274	$ 391	$ 38	$ 27

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Note 7: Restructuring and Related Costs

During the first nine months of 2007, we recorded net pre-tax restructuring and related charges/(credits) in our business segments totaling $103 million for new and ongoing restructuring actions as follows:

In Millions	
Otis	$ 11
Carrier	28
UTC Fire & Security	8
Pratt & Whitney	39
Hamilton Sundstrand	20
Sikorsky	(3)
Totals	$ 103

The net charges included $70 million in cost of sales, $34 million in selling, general and administrative expenses and ($1) million in other income and, as described below, relate to actions initiated during 2007 and 2006 and trailing costs related to certain 2005 actions.

2007 Actions. During the first nine months of 2007, we initiated restructuring actions relating to ongoing cost reduction efforts, including workforce reductions and the consolidation of manufacturing facilities. We recorded net pre-tax restructuring and related charges totaling $62 million, including $25 million in cost of sales and $37 million in selling, general and administrative expenses.

As of September 30, 2007, net workforce reductions of approximately 800 employees of an expected 1,300 employees have been completed, with 750,000 net square feet of facilities expected to be exited. The majority of the remaining workforce and all facility related cost reduction actions are targeted for completion during 2008.

The following table summarizes the accrual balances and utilization by cost type for the 2007 restructuring actions:

In Millions	Severance	Asset Write-Downs	Facility Exit and Lease Termination Costs	Total
Restructuring accruals at June 30, 2007	$ 18	$	$ 8	$ 26
Net pre-tax restructuring charges	21		7	28
Utilization	(7)		(9)	(16)
Balance at September 30, 2007	$ 32	$	$ 6	$ 38

The following table summarizes expected, incurred and remaining costs for the 2007 restructuring actions by type:

In Millions	Severance	Asset Write-Downs	Facility Exit and Lease	Total

			Termination Costs	
Expected costs	$ 53	$ 8	$ 45	$ 106
Costs incurred quarter ended March 31, 2007	(14)	(1)	(8)	(23)
Costs incurred quarter ended June 30, 2007	(9)		(2)	(11)
Costs incurred quarter ended September 30, 2007	(21)		(7)	(28)
Remaining costs at September 30, 2007	$ 9	$ 7	$ 28	$ 44

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The following table summarizes expected, incurred and remaining costs for the 2007 restructuring actions by segment:

In Millions