

LOCKHEED MARTIN CORP

Form 10-K/A

February 16, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K/A

(Amendment No. 1)

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

For the fiscal year ended December 31, 2017

Commission file number 1-11437

LOCKHEED MARTIN CORPORATION

(Exact name of registrant as specified in its charter)

Maryland 52-1893632

(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

6801 Rockledge Drive, Bethesda, Maryland 20817-1877 (301/897-6000)

(Address and telephone number of principal executive offices)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class Name of each exchange on which registered

Common Stock, \$1 par value New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 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

The aggregate market value of voting and non-voting common stock held by non-affiliates of the registrant computed by reference to the last sales price of such stock, as of the last business day of the registrant's most recently completed second fiscal quarter, which was June 23, 2017, was approximately \$80.3 billion.

There were 285,570,742 shares of our common stock, \$1 par value per share, outstanding as of January 26, 2018.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of Lockheed Martin Corporation's 2018 Definitive Proxy Statement are incorporated by reference into Part III of this Form 10 K.

Explanatory Note

This Amendment No. 1 on Form 10-K/A (“Amendment No. 1”) amends Lockheed Martin Corporation’s (the Corporation) Annual Report on Form 10-K for the fiscal year ended December 31, 2017, as filed with the U.S. Securities and Exchange Commission on February 6, 2018 (the “Original Filing” and the “Original Filing Date”).

This Amendment No. 1 is being filed solely to include the phrase “and the related notes (collectively referred to as the “financial statements”)” inadvertently omitted by Ernst & Young LLP from both the first paragraph of its “Report of Ernst & Young LLP, Independent Registered Public Accounting Firm, on the Audited Consolidated Financial Statements” in Part II, Item 8 and from the second paragraph of its “Report of Ernst & Young LLP, Independent Registered Public Accounting Firm, Regarding Internal Control Over Financial Reporting” in Part II, Item 9A of the Original Filing. Pursuant to Rule 12b-15 promulgated under the Securities Exchange Act of 1934, as amended, we have included the entire text of Part II, Items 8 and 9A in this Amendment No. 1.

The changes to add the phrases to the filed copies of the reports of Ernst & Young LLP do not affect Ernst & Young LLP’s unqualified opinion on the Corporation’s financial statements included in the Original Filing and Amendment No. 1 or on the effectiveness of the Corporation’s internal control over financial reporting as of December 31, 2017.

Item 15 has been included herein to reflect a new Consent of Ernst & Young LLP and new Section 302 and Section 906 certifications. No other changes were made to the Original Filing. This amendment speaks as of the Original Filing Date, and does not reflect events that may have occurred subsequent to the Original Filing Date.

PART II

ITEM 8. Financial Statements and Supplementary Data

Report of Ernst & Young LLP,
Independent Registered Public Accounting Firm,
on the Audited Consolidated Financial Statements

Board of Directors and Stockholders
Lockheed Martin Corporation

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Lockheed Martin Corporation (the "Corporation") as of December 31, 2017 and 2016, and the related consolidated statements of earnings, comprehensive income, equity, and cash flows, for each of the three years in the period ended December 31, 2017, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the consolidated financial position of the Corporation as of December 31, 2017 and 2016, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Corporation's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework), and our report dated February 6, 2018 expressed an unqualified opinion thereon.

Basis for Opinion

These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on the Corporation's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Corporation in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB. We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Corporation's auditor since 1994.

Tysons, Virginia
February 6, 2018

Lockheed Martin Corporation
Consolidated Statements of Earnings
(in millions, except per share data)

	Years Ended December 31,		
	2017	2016	2015
Net sales			
Products	\$43,875	\$40,365	\$34,868
Services	7,173	6,883	5,668
Total net sales	51,048	47,248	40,536
Cost of sales			
Products	(39,750)	(36,616)	(31,091)
Services	(6,405)	(6,040)	(4,824)
Severance charges	—	(80)	(82)
Other unallocated, net	655	550	(47)
Total cost of sales	(45,500)	(42,186)	(36,044)
Gross profit	5,548	5,062	4,492
Other income, net	373	487	220
Operating profit	5,921	5,549	4,712
Interest expense	(651)	(663)	(443)
Other non-operating (expense) income, net	(1)	—	30
Earnings from continuing operations before income taxes	5,269	4,886	4,299
Income tax expense	(3,340)	(1,133)	(1,173)
Net earnings from continuing operations	1,929	3,753	3,126
Net earnings from discontinued operations	73	1,549	479
Net earnings	\$2,002	\$5,302	\$3,605
Earnings per common share			
Basic			
Continuing operations	\$6.70	\$12.54	\$10.07
Discontinued operations	0.26	5.17	1.55
Basic earnings per common share	\$6.96	\$17.71	\$11.62
Diluted			
Continuing operations	\$6.64	\$12.38	\$9.93
Discontinued operations	0.25	5.11	1.53
Diluted earnings per common share	\$6.89	\$17.49	\$11.46

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

Lockheed Martin Corporation
 Consolidated Statements of Comprehensive Income
 (in millions)

	Years Ended December		
	31,		
	2017	2016	2015
Net earnings	\$2,002	\$5,302	\$3,605
Other comprehensive (loss) income, net of tax			
Postretirement benefit plans			
Net other comprehensive loss recognized during the period, net of tax benefit of \$375 million in 2017, \$668 million in 2016 and \$192 million in 2015	(1,380)	(1,232)	(351)
Amounts reclassified from accumulated other comprehensive loss, net of tax expense of \$437 million in 2017, \$382 million in 2016 and \$464 million in 2015	802	699	850
Reclassifications from divestiture of IS&GS business	—	(134)	—
Other, net	140	9	(73)
Other comprehensive (loss) income, net of tax	(438)	(658)	426
Comprehensive income	\$1,564	\$4,644	\$4,031

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

Lockheed Martin Corporation
Consolidated Balance Sheets
(in millions, except par value)

	December 31,	
	2017	2016
Assets		
Current assets		
Cash and cash equivalents	\$2,861	\$1,837
Receivables, net	8,603	8,202
Inventories, net	4,487	4,670
Other current assets	1,510	399
Total current assets	17,461	15,108
Property, plant and equipment, net	5,775	5,549
Goodwill	10,807	10,764
Intangible assets, net	3,797	4,093
Deferred income taxes	3,111	6,625
Other noncurrent assets	5,570	5,667
Total assets	\$46,521	\$47,806
Liabilities and equity		
Current liabilities		
Accounts payable	\$1,467	\$1,653
Customer advances and amounts in excess of costs incurred	6,752	6,776
Salaries, benefits and payroll taxes	1,785	1,764
Current maturities of long-term debt	750	—
Other current liabilities	1,883	2,349
Total current liabilities	12,637	12,542
Long-term debt, net	13,513	14,282
Accrued pension liabilities	15,703	13,855
Other postretirement benefit liabilities	719	862
Other noncurrent liabilities	4,558	4,659
Total liabilities	47,130	46,200
Stockholders' equity		
Common stock, \$1 par value per share	284	289
Additional paid-in capital	—	—
Retained earnings	11,573	13,324
Accumulated other comprehensive loss	(12,540)	(12,102)
Total stockholders' (deficit) equity	(683)	1,511
Noncontrolling interests in subsidiary	74	95
Total (deficit) equity	(609)	1,606
Total liabilities and equity	\$46,521	\$47,806

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

Lockheed Martin Corporation
Consolidated Statements of Cash Flows
(in millions)

	Years Ended December		
	31,		
	2017	2016	2015
Operating activities			
Net earnings	\$2,002	\$5,302	\$3,605
Adjustments to reconcile net earnings to net cash provided by operating activities			
Depreciation and amortization	1,195	1,215	1,026
Stock-based compensation	158	149	138
Deferred income taxes	3,432	(152)	(445)
Severance charges	—	99	102
Gain on property sale	(198)	—	—
Gain on divestiture of IS&GS business	(73)	(1,242)	—
Gain on step acquisition of AWE	—	(104)	—
Changes in assets and liabilities			
Receivables, net	(401)	(811)	(256)
Inventories, net	183	(46)	(398)
Accounts payable	(189)	(188)	(160)
Customer advances and amounts in excess of costs incurred	(24)	3	(32)
Postretirement benefit plans	1,316	1,028	1,068
Income taxes	(1,210)	146	(48)
Other, net	285	(210)	501
Net cash provided by operating activities	6,476	5,189	5,101
Investing activities			
Capital expenditures	(1,177)	(1,063)	(939)
Acquisitions of businesses and investments in affiliates	—	—	(9,003)
Other, net	30	78	208
Net cash used for investing activities	(1,147)	(985)	(9,734)
Financing activities			
Repurchases of common stock	(2,001)	(2,096)	(3,071)
Dividends paid	(2,163)	(2,048)	(1,932)
Special cash payment from divestiture of IS&GS business	—	1,800	—
Proceeds from stock option exercises	71	106	174
Repayments of long-term debt	—	(952)	—
Proceeds from the issuance of long-term debt	—	—	9,101
Proceeds from borrowings under revolving credit facilities	—	—	6,000
Repayments of borrowings under revolving credit facilities	—	—	(6,000)
Other, net	(212)	(267)	5
Net cash (used for) provided by financing activities	(4,305)	(3,457)	4,277
Net change in cash and cash equivalents	1,024	747	(356)
Cash and cash equivalents at beginning of year	1,837	1,090	1,446
Cash and cash equivalents at end of year	\$2,861	\$1,837	\$1,090

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

Lockheed Martin Corporation
Consolidated Statements of Equity
(in millions, except per share data)

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Stockholders' (Deficit) Equity	Noncontrolling Interests in Subsidiary	Total (Deficit) Equity
Balance at December 31, 2014	\$ 314	\$ —	\$ 14,956	\$ (11,870)	\$ 3,400	\$ —	\$ 3,400
Net earnings	—	—	3,605	—	3,605	—	3,605
Other comprehensive income, net of tax	—	—	—	426	426	—	426
Repurchases of common stock	(15)	(656)	(2,400)	—	(3,071)	—	(3,071)
Dividends declared (\$6.15 per share)	—	—	(1,923)	—	(1,923)	—	(1,923)
Stock-based awards, ESOP activity and other	4	656	—	—	660	—	660
Balance at December 31, 2015	303	—	14,238	(11,444)	3,097	—	3,097
Net earnings	—	—	5,302	—	5,302	—	5,302
Other comprehensive loss, net of tax	—	—	—	(658)	(658)	—	(658)
Shares exchanged and retired in connection with divestiture of IS&GS business	(9)	—	(2,488)	—	(2,497)	—	(2,497)
Repurchases of common stock	(9)	(395)	(1,692)	—	(2,096)	—	(2,096)
Dividends declared (\$6.77 per share)	—	—	(2,036)	—	(2,036)	—	(2,036)
Stock-based awards, ESOP activity and other	4	395	—	—	399	—	399
Net increase in noncontrolling interests in subsidiary	—	—	—	—	—	95	95
Balance at December 31, 2016	289	—	13,324	(12,102)	1,511	95	1,606
Net earnings	—	—	2,002	—	2,002	—	2,002
Other comprehensive loss, net of tax	—	—	—	(438)	(438)	—	(438)
Repurchases of common stock	(7)	(398)	(1,596)	—	(2,001)	—	(2,001)
Dividends declared (\$7.46 per share)	—	—	(2,157)	—	(2,157)	—	(2,157)
Stock-based awards, ESOP activity and other	2	398	—	—	400	—	400
Net decrease in noncontrolling interests in subsidiary	—	—	—	—	—	(21)	(21)
Balance at December 31, 2017	\$ 284	\$ —	\$ 11,573	\$ (12,540)	\$ (683)	\$ 74	\$ (609)

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

Lockheed Martin Corporation

Notes to Consolidated Financial Statements

Note 1 – Significant Accounting Policies

Organization – We are a global security and aerospace company principally engaged in the research, design, development, manufacture, integration and sustainment of advanced technology systems, products and services. We also provide a broad range of management, engineering, technical, scientific, logistics, system integration and cybersecurity services. We serve both U.S. and international customers with products and services that have defense, civil and commercial applications, with our principal customers being agencies of the U.S. Government.

Basis of presentation – Our consolidated financial statements include the accounts of subsidiaries we control and variable interest entities if we are the primary beneficiary. We eliminate intercompany balances and transactions in consolidation. Our receivables, inventories, customer advances and amounts in excess of costs incurred and certain amounts in other current liabilities primarily are attributable to long-term contracts or programs in progress for which the related operating cycles are longer than one year. In accordance with industry practice, we include these items in current assets and current liabilities. Unless otherwise noted, we present all per share amounts cited in these consolidated financial statements on a “per diluted share” basis. Certain prior period amounts have been reclassified to conform with current year presentation.

The discussion and presentation of the operating results of our business segments have been impacted by the following recent events.

During the fourth quarter of 2017, the business segment formally known as Space Systems was renamed Space. There was no change to the composition of the portfolio in connection with the name change. The information for this segment for all periods included in these consolidated financial statements has been labeled using the new name.

On August 16, 2016, we completed the divestiture of the Information Systems & Global Solutions (IS&GS) business, which merged with a subsidiary of Leidos Holdings, Inc. (Leidos) in a Reverse Morris Trust transaction. Accordingly, the operating results of the IS&GS business have been classified as discontinued operations on our consolidated statements of earnings for all prior periods presented. However, the cash flows of the IS&GS business have not been reclassified in our consolidated statements of cash flows as we retained the cash as part of the Transaction. See “Note 3 – Acquisitions and Divestitures” for additional information about the divestiture of the IS&GS business.

On August 24, 2016, we increased our ownership interest in the AWE Management Limited (AWE) joint venture, which operates the United Kingdom’s nuclear deterrent program, from 33% to 51%. At which time, we began consolidating AWE. Consequently, our operating results include 100% of AWE’s sales and 51% of its operating profit. Prior to increasing our ownership interest, we accounted for our investment in AWE using the equity method of accounting. Under the equity method, we recognized only 33% of AWE’s earnings or losses and no sales. Accordingly, prior to August 24, 2016, the date we obtained control, we recorded 33% of AWE’s net earnings in our operating results and subsequent to August 24, 2016, we recognized 100% of AWE’s sales and 51% of its operating profit. See “Note 3 – Acquisitions and Divestitures” for additional information about the change in ownership of AWE.

On November 6, 2015, we completed the acquisition of Sikorsky Aircraft Corporation and certain affiliated companies (collectively “Sikorsky”) for \$9.0 billion, net of cash acquired, and aligned Sikorsky under our Rotary and Mission Systems (RMS) business segment. The operating results and cash flows of Sikorsky have been included on our consolidated statements of earnings and consolidated statements of cash flows since the November 6, 2015 acquisition date. Additionally, the assets and liabilities of Sikorsky are included in our consolidated balance sheets as of December 31, 2017 and December 31, 2016. See “Note 3 – Acquisitions and Divestitures” for additional information about the acquisition of Sikorsky and related final purchase accounting.

During the fourth quarter of 2015, we realigned certain programs among our business segments. The amounts, discussion and presentation of our business segments for all periods presented in these consolidated financial statements reflect the program realignment.

Use of estimates – We prepare our consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP). In doing so, we are required to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. We base these estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying amounts of assets and liabilities that are not

readily apparent from other sources. Our actual results may differ materially from these estimates. Significant estimates inherent in the preparation of our consolidated financial statements include, but are not limited to, accounting for sales and cost recognition, postretirement benefit plans, environmental receivables and

liabilities, evaluation of goodwill and other assets for impairment, income taxes including deferred tax assets, fair value measurements and contingencies.

Sales and earnings – We record net sales and estimated profits for substantially all of our contracts using the percentage-of-completion method for fixed-price and cost-reimbursable contracts for products and services with the U.S. Government. Sales are recorded on all time-and-materials contracts as the work is performed based on agreed-upon hourly rates and allowable costs. We account for our services contracts with non-U.S. Government customers using the services method of accounting. We classify net sales as products or services on our consolidated statements of earnings based on the attributes of the underlying contracts.

Percentage-of-Completion Method – The percentage-of-completion method for product contracts depends on the nature of the products provided under the contract. For example, for contracts that require us to perform a significant level of development effort in comparison to the total value of the contract and/or to deliver minimal quantities, sales are recorded using the cost-to-cost method to measure progress toward completion. Under the cost-to-cost method of accounting, we recognize sales and an estimated profit as costs are incurred based on the proportion that the incurred costs bear to total estimated costs. For contracts that require us to provide a substantial number of similar items without a significant level of development, we record sales and an estimated profit on a percentage-of-completion basis using units-of-delivery as the basis to measure progress toward completing the contract. For contracts to provide services to the U.S. Government, sales are generally recorded using the cost-to-cost method.

Award and incentive fees, as well as penalties related to contract performance, are considered in estimating sales and profit rates on contracts accounted for under the percentage-of-completion method. Estimates of award fees are based on past experience and anticipated performance. We record incentives or penalties when there is sufficient information to assess anticipated contract performance. Incentive provisions that increase or decrease earnings based solely on a single significant event are not recognized until the event occurs.

Accounting for contracts using the percentage-of-completion method requires judgment relative to assessing risks, estimating contract sales and costs (including estimating award and incentive fees and penalties related to performance) and making assumptions for schedule and technical issues. Due to the number of years it may take to complete many of our contracts and the scope and nature of the work required to be performed on those contracts, the estimation of total sales and costs at completion is complicated and subject to many variables and, accordingly, is subject to change. When adjustments in estimated total contract sales or estimated total costs are required, any changes from prior estimates are recognized in the current period for the inception-to-date effect of such changes. When estimates of total costs to be incurred on a contract exceed estimates of total sales to be earned, a provision for the entire loss on the contract is recorded in the period in which the loss is determined.

Many of our contracts span several years and include highly complex technical requirements. At the outset of a contract, we identify and monitor risks to the achievement of the technical, schedule and cost aspects of the contract and assess the effects of those risks on our estimates of total costs to complete the contract. The estimates consider the technical requirements (e.g., a newly-developed product versus a mature product), the schedule and associated tasks (e.g., the number and type of milestone events) and costs (e.g., material, labor, subcontractor, overhead and the estimated costs to fulfill our industrial cooperation agreements, sometimes referred to as offset agreements, required under certain contracts with international customers). The initial profit booking rate of each contract considers risks surrounding the ability to achieve the technical requirements, schedule and costs in the initial estimated total costs to complete the contract. Profit booking rates may increase during the performance of the contract if we successfully retire risks surrounding the technical, schedule and cost aspects of the contract which decreases the estimated total costs to complete the contract. Conversely, our profit booking rates may decrease if the estimated total costs to complete the contract increase. All of the estimates are subject to change during the performance of the contract and may affect the profit booking rate.

In addition, comparability of our business segment sales, operating profit and operating margins may be impacted by changes in profit booking rates on our contracts accounted for using the percentage-of-completion method of accounting. Increases in the profit booking rates, typically referred to as risk retirements, usually relate to revisions in the estimated total costs that reflect improved conditions on a particular contract. Conversely, conditions on a particular contract may deteriorate, resulting in an increase in the estimated total costs to complete and a reduction in the profit booking rate. Increases or decreases in profit booking rates are recognized in the current period and reflect

the inception-to-date effect of such changes. Segment operating profit and margins may also be impacted favorably or unfavorably by other items. Favorable items may include the positive resolution of contractual matters, cost recoveries on restructuring charges, insurance recoveries and gains on sales of assets. Unfavorable items may include the adverse resolution of contractual matters; restructuring charges, except for significant severance actions (such as those mentioned below in “Note 15 – Restructuring Charges”), which are excluded from segment operating results; reserves for disputes; asset impairments; and losses on sales of certain assets. Segment operating profit and items such as risk retirements, reductions of profit booking rates or other matters are presented net of state income taxes.

Changes in Estimates – As previously disclosed, we have a program to design, integrate, and install an air missile defense C4I systems for an international customer that has experienced performance issues and for which we have periodically accrued reserves. In 2017, we revised our estimated costs to complete the program, EADGE-T, as a consequence of ongoing performance matters and recorded an additional charge of \$120 million (\$74 million or \$0.25 per share, after tax) at our RMS business segment. As of December 31, 2017, cumulative losses, including reserves, remained at approximately \$260 million on this program. We are continuing to monitor the viability of the program and the available options and could record additional charges in future periods. However, based on the reserves already accrued and our current estimate of the costs to complete the program, at this time we do not anticipate that additional charges, if any, would be material.

We have two commercial satellite programs at our Space business segment, for which we have experienced performance issues related to the development and integration of a modernized LM 2100 satellite platform. These commercial programs require the development of new satellite technology to enhance the LM 2100's power, propulsion and electronics, among other items. The enhanced satellite is expected to benefit other commercial and government satellite programs. We have periodically revised our estimated costs to complete these developmental commercial programs. We have recorded cumulative losses of approximately \$305 million as of December 31, 2017, including approximately \$135 million (\$83 million or \$0.29 per share, after tax) recorded during the year ended December 31, 2017. While these losses reflect our estimated total losses on the programs, we will continue to incur unrecovered costs each period until we complete these programs and may have to record additional loss reserves in future periods, which could be material to our operating results. While we do not currently anticipate recording additional loss reserves, the programs remain developmental and further challenges in the delivery and integration of new satellite technology, anomalies discovered during system testing requiring repair or rework, further schedule delays and potential penalties could require that we record additional reserves. We do not currently expect to be able to meet the delivery schedule under the contracts and have informed the customers. The customers could seek to exercise a termination right under the contracts, in which case we would have to refund the payments we have received and pay certain penalties. However, we think the probability that the customers will seek to exercise any termination right is remote as the delay beyond the termination date is modest and the customers have an immediate need for the satellites.

Our consolidated net adjustments not related to volume, including net profit booking rate adjustments and other matters, net of state income taxes, increased segment operating profit by approximately \$1.5 billion in both 2017 and 2016 and \$1.7 billion in 2015. These adjustments increased net earnings by approximately \$980 million (\$3.37 per share) in 2017, \$950 million (\$3.13 per share) in 2016 and \$1.1 billion (\$3.50 per share) in 2015.

Services Method – Under fixed-price service contracts, we are paid a predetermined fixed amount for a specified scope of work and generally have full responsibility for the costs associated with the contract and the resulting profit or loss. We record net sales under fixed-price service contracts with non-U.S. Government customers on a straight-line basis over the period of contract performance, unless evidence suggests that net sales are earned or the obligations are fulfilled in a different pattern. For cost-reimbursable contracts for services to non-U.S. Government customers, we record net sales as services are performed, except for award and incentive fees. Award and incentive fees are recorded when they are fixed or determinable, generally at the date the amount is communicated to us by the customer. This approach results in the recognition of such fees at contractual intervals (typically every six months) throughout the contract and is dependent on the customer's processes for notification of awards and issuance of formal notifications. Costs for all service contracts are expensed as incurred.

Research and development and similar costs – Except for certain arrangements described below, we account for independent research and development costs as part of the general and administrative costs that are allocated among all of our contracts and programs in progress under U.S. Government contractual arrangements and charged to cost of sales. Under certain arrangements in which a customer shares in product development costs, our portion of unreimbursed costs is expensed as incurred in cost of sales. Independent research and development costs charged to cost of sales totaled \$1.2 billion in 2017, \$988 million in 2016 and \$817 million in 2015. Costs we incur under customer-sponsored research and development programs pursuant to contracts are included in net sales and cost of sales.

Stock-based compensation – Compensation cost related to all share-based payments is measured at the grant date based on the estimated fair value of the award. We generally recognize the compensation cost ratably over a three-year vesting period, net of estimated forfeitures. At each reporting date, the number of shares is adjusted to the number ultimately expected to vest.

Income taxes – We calculate our provision for income taxes using the asset and liability method, under which deferred tax assets and liabilities are recognized based on the future tax consequences attributable to temporary differences that exist between the financial statement carrying amount of assets and liabilities and their respective tax bases, as well as from operating loss and tax credit carry-forwards. We measure deferred tax assets and liabilities using enacted tax rates that will apply in the years in which we expect the temporary differences to be recovered or paid.

We periodically assess our tax exposures related to periods that are open to examination. Based on the latest available information, we evaluate our tax positions to determine whether the position will more likely than not be sustained upon examination by the Internal Revenue Service (IRS) or other taxing authorities. If we cannot reach a more-likely-than-not determination, no benefit is recorded. If we determine that the tax position is more likely than not to be sustained, we record the largest amount of benefit that is more likely than not to be realized when the tax position is settled. We record interest and penalties related to income taxes as a component of income tax expense on our consolidated statements of earnings. Interest and penalties were not material.

Cash and cash equivalents – Cash equivalents include highly liquid instruments with original maturities of 90 days or less.

Receivables – Receivables include amounts billed and currently due from customers and unbilled costs and accrued profits primarily related to sales on long-term contracts that have been recognized but not yet billed to customers. Pursuant to contract provisions, agencies of the U.S. Government and certain other customers have title to, or a security interest in, assets related to such contracts as a result of advances, performance-based payments and progress payments. We reflect those advances and payments as an offset to the related receivables balance for contracts that we account for on a percentage-of-completion basis using the cost-to-cost method to measure progress towards completion.

On occasion, our customers may seek deferred payment terms to purchase our products. In connection with these transactions, we may, at our customer's request, enter into arrangements for the non-recourse sale of customer receivables to unrelated third-party financial institutions. For accounting purposes, these transactions are not discounted and are treated as a sale of receivables as we have no continuing involvement. The sale proceeds from the financial institutions are reflected in our operating cash flows on the statement of cash flows. During 2017, we sold approximately \$698 million of customer receivables. There were no gains or losses related to sales of these receivables.

Inventories – We record inventories at the lower of cost or estimated net realizable value. Costs on long-term contracts and programs in progress represent recoverable costs incurred for production or contract-specific facilities and equipment, allocable operating overhead, advances to suppliers and, in the case of contracts with the U.S. Government and substantially all other governments, research and development and general and administrative expenses. Pursuant to contract provisions, agencies of the U.S. Government and certain other customers have title to, or a security interest in, inventories related to such contracts as a result of advances, performance-based payments and progress payments. We reflect those advances and payments as an offset against the related inventory balances for contracts that we account for on a percentage-of-completion basis using units-of-delivery as the basis to measure progress toward completing the contract. We determine the costs of other product and supply inventories by the first-in first-out or average cost methods.

Property, plant and equipment – We record property, plant and equipment at cost. We provide for depreciation and amortization on plant and equipment generally using accelerated methods during the first half of the estimated useful lives of the assets and the straight-line method thereafter. The estimated useful lives of our plant and equipment generally range from 10 to 40 years for buildings and five to 15 years for machinery and equipment. No depreciation expense is recorded on construction in progress until such assets are placed into operation. Depreciation expense related to plant and equipment was \$760 million in 2017, \$747 million in 2016, and \$716 million in 2015.

We review the carrying amounts of long-lived assets for impairment if events or changes in the facts and circumstances indicate that their carrying amounts may not be recoverable. We assess impairment by comparing the estimated undiscounted future cash flows of the related asset grouping to its carrying amount. If an asset is determined to be impaired, we recognize an impairment charge in the current period for the difference between the fair value of the asset and its carrying amount.

Capitalized software – We capitalize certain costs associated with the development or purchase of internal-use software. The amounts capitalized are included in other noncurrent assets on our consolidated balance sheets and are amortized on a straight-line basis over the estimated useful life of the resulting software, which ranges from two to six years. As of December 31, 2017 and 2016, capitalized software totaled \$424 million and \$427 million, net of accumulated amortization of \$2.0 billion and \$1.9 billion. No amortization expense is recorded until the software is ready for its intended use. Amortization expense related to capitalized software was \$123 million in 2017, \$136

million in 2016 and \$161 million in 2015.

Goodwill – The assets and liabilities of acquired businesses are recorded under the acquisition method of accounting at their estimated fair values at the date of acquisition. Goodwill represents costs in excess of fair values assigned to the underlying identifiable net assets of acquired businesses.

Our goodwill balance was \$10.8 billion at both December 31, 2017 and 2016. We perform an impairment test of our goodwill at least annually in the fourth quarter or more frequently whenever events or changes in circumstances indicate the carrying value of goodwill may be impaired. Such events or changes in circumstances may include a significant deterioration in overall economic conditions, changes in the business climate of our industry, a decline in our market capitalization, operating performance indicators,

competition, reorganizations of our business, U.S. Government budget restrictions or the disposal of all or a portion of a reporting unit. Our goodwill has been allocated to and is tested for impairment at a level referred to as the reporting unit, which is our business segment level or a level below the business segment. The level at which we test goodwill for impairment requires us to determine whether the operations below the business segment constitute a self-sustaining business for which discrete financial information is available and segment management regularly reviews the operating results.

We may use either a qualitative or quantitative approach when testing a reporting unit's goodwill for impairment. For selected reporting units where we use the qualitative approach, we perform a qualitative evaluation of events and circumstances impacting the reporting unit to determine the likelihood of goodwill impairment. Based on that qualitative evaluation, if we determine it is more likely than not that the fair value of a reporting unit exceeds its carrying amount, no further evaluation is necessary. Otherwise we perform a quantitative impairment test. We perform quantitative tests for most reporting units at least once every three years. However, for certain reporting units we may perform a quantitative impairment test every year.

For the quantitative impairment test we compare the fair value of a reporting unit to its carrying value, including goodwill. If the fair value of a reporting unit exceeds its carrying value, goodwill of the reporting unit is not impaired. If the carrying value of the reporting unit, including goodwill, exceeds its fair value, a goodwill impairment loss is recognized in an amount equal to that excess. We generally estimate the fair value of each reporting unit using a combination of a discounted cash flow (DCF) analysis and market-based valuation methodologies such as comparable public company trading values and values observed in recent business acquisitions. Determining fair value requires the exercise of significant judgments, including the amount and timing of expected future cash flows, long-term growth rates, discount rates and relevant comparable public company earnings multiples and relevant transaction multiples. The cash flows employed in the DCF analysis are based on our best estimate of future sales, earnings and cash flows after considering factors such as general market conditions, U.S. Government budgets, existing firm orders, expected future orders, contracts with suppliers, labor agreements, changes in working capital, long term business plans and recent operating performance. The discount rates utilized in the DCF analysis are based on the respective reporting unit's weighted average cost of capital, which takes into account the relative weights of each component of capital structure (equity and debt) and represents the expected cost of new capital, adjusted as appropriate to consider the risk inherent in future cash flows of the respective reporting unit. The carrying value of each reporting unit includes the assets and liabilities employed in its operations, goodwill and allocations of amounts held at the business segment and corporate levels.

During the fourth quarters of 2017 and 2016, we performed our annual goodwill impairment test for each of our reporting units. The results of our annual impairment tests of goodwill indicated that no impairment existed.

During the fourth quarter of 2017, we realigned certain programs within the RMS business segment to align with changes in management structure. We performed goodwill impairment tests prior and subsequent to the realignment, and there was no indication of goodwill impairment.

During the fourth quarter of 2015, we performed our annual goodwill impairment test for each of our reporting units. During the fourth quarter of 2015, we realigned certain programs between our business segments in connection with our strategic review of our government IT and technical services businesses. As part of the realignment, goodwill was reallocated between affected reporting units on a relative fair value basis. We performed goodwill impairment tests prior and subsequent to the realignment. The results of our 2015 annual impairment tests of goodwill indicated that no impairment existed.

Intangible assets – Intangible assets from acquired businesses are recognized at their estimated fair values at the date of acquisition and consist of customer programs, trademarks, customer relationships, technology and other intangible assets. Customer programs include values assigned to major programs of acquired businesses and represent the aggregate value associated with the customer relationships, contracts, technology and trademarks underlying the associated program and are amortized on a straight-line basis over a period of expected cash flows used to measure the fair value, which ranges from nine to 20 years. Acquired intangibles deemed to have indefinite lives are not amortized, but are subject to annual impairment testing. This testing compares carrying value to fair value and, when appropriate, the carrying value of these assets is reduced to fair value. Finite-lived intangibles are amortized to expense over the applicable useful lives, ranging from three to 20 years, based on the nature of the asset and the underlying pattern of

economic benefit as reflected by future net cash inflows. We perform an impairment test of finite-lived intangibles whenever events or changes in circumstances indicate their carrying value may be impaired.

Customer advances and amounts in excess of cost incurred – We receive advances, performance-based payments and progress payments from customers that may exceed costs incurred on certain contracts, including contracts with agencies of the U.S. Government. We classify such advances, other than those reflected as a reduction of receivables or inventories as discussed above, as current liabilities.

Postretirement benefit plans – Many of our employees are covered by defined benefit pension plans and we provide certain health care and life insurance benefits to eligible retirees (collectively, postretirement benefit plans). GAAP requires that the

amounts we record related to our postretirement benefit plans be computed, based on service to date, using actuarial valuations that are based in part on certain key economic assumptions we make, including the discount rate, the expected long-term rate of return on plan assets and other actuarial assumptions including participant longevity (also known as mortality), health care cost trend rates and employee turnover, each as appropriate based on the nature of the plans.

A market-related value of our plan assets, determined using actual asset gains or losses over the prior three year period, is used to calculate the amount of deferred asset gains or losses to be amortized. These asset gains or losses, along with those resulting from adjustments to our benefit obligation, will be amortized to expense using the corridor method, where gains and losses are recognized to the extent they exceed 10% of the greater of plan assets or benefit obligations, over the average future service period of employees expected to receive benefits under the plans of approximately nine years as of December 31, 2017. This amortization period is expected to extend (approximately double) in 2020 when our non-union pension plan is frozen to use the average remaining life expectancy of the participants instead of average future service.

We recognize on a plan-by-plan basis the funded status of our postretirement benefit plans under GAAP as either an asset recorded within other noncurrent assets or a liability recorded within noncurrent liabilities on our consolidated balance sheets. The GAAP funded status is measured as the difference between the fair value of the plan's assets and the benefit obligation of the plan. The funded status under the Employee Retirement Income Security Act of 1974 (ERISA), as amended by the Pension Protection Act of 2006 (PPA), is calculated on a different basis than under GAAP.

Environmental matters – We record a liability for environmental matters when it is probable that a liability has been incurred and the amount can be reasonably estimated. The amount of liability recorded is based on our estimate of the costs to be incurred for remediation at a particular site. We do not discount the recorded liabilities, as the amount and timing of future cash payments are not fixed or cannot be reliably determined. Our environmental liabilities are recorded on our consolidated balance sheets within other liabilities, both current and noncurrent. We expect to include a substantial portion of environmental costs in our net sales and cost of sales in future periods pursuant to U.S. Government agreement or regulation. At the time a liability is recorded for future environmental costs, we record a receivable for estimated future recovery considered probable through the pricing of products and services to agencies of the U.S. Government, regardless of the contract form (e.g., cost-reimbursable, fixed-price). We continuously evaluate the recoverability of our environmental receivables by assessing, among other factors, U.S. Government regulations, our U.S. Government business base and contract mix, our history of receiving reimbursement of such costs, and recent efforts by some U.S. Government representatives to limit such reimbursement. We include the portion of those environmental costs expected to be allocated to our non-U.S. Government contracts, or that is determined to not be recoverable under U.S. Government contracts, in our cost of sales at the time the liability is established. Our environmental receivables are recorded on our consolidated balance sheets within other assets, both current and noncurrent. We project costs and recovery of costs over approximately 20 years.

Investments in marketable securities – Investments in marketable securities consist of debt and equity securities and are classified as trading securities. As of December 31, 2017 and 2016, the fair value of our trading securities totaled \$1.4 billion and \$1.2 billion and was included in other noncurrent assets on our consolidated balance sheets. Our trading securities are held in a separate trust, which includes investments to fund our deferred compensation plan liabilities. Net gains on trading securities in 2017 and 2016 were \$150 million and \$66 million. Net losses on trading securities in 2015 were \$11 million. Gains and losses on these investments are included in other unallocated, net within cost of sales on our consolidated statements of earnings in order to align the classification of changes in the market value of investments held for the plan with changes in the value of the corresponding plan liabilities.

Equity method investments – Investments where we have the ability to exercise significant influence, but do not control, are accounted for under the equity method of accounting and are included in other noncurrent assets on our consolidated balance sheets. Significant influence typically exists if we have a 20% to 50% ownership interest in the investee. Under this method of accounting, our share of the net earnings or losses of the investee is included in operating profit in other income, net on our consolidated statements of earnings since the activities of the investee are closely aligned with the operations of the business segment holding the investment. We evaluate our equity method investments for impairment whenever events or changes in circumstances indicate that the carrying amounts of such

investments may be impaired. If a decline in the value of an equity method investment is determined to be other than temporary, a loss is recorded in earnings in the current period. As of both December 31, 2017 and 2016, our equity method investments totaled \$1.4 billion, which primarily are composed of our Space business segment's investment in United Launch Alliance (ULA), see "Note 14 – Legal Proceedings, Commitments and Contingencies", and our Aeronautics and RMS business segments' investments in the Advanced Military Maintenance, Repair and Overhaul Center (AMMROC) venture. Our share of net earnings related to our equity method investees was \$207 million in 2017, \$443 million in 2016 and \$320 million in 2015, of which approximately \$205 million, \$325 million and \$245 million related to our Space business segment.

During the year ended December 31, 2017, equity earnings included a charge recorded in the first quarter of approximately \$64 million (\$40 million or \$0.14 per share, after tax), which represented our portion of a non-cash asset impairment related to certain long-lived assets held by our equity method investee, AMMROC. We are continuing to monitor this investment. It is possible that we may have to record our portion of additional charges should their business continue to experience performance issues, which could adversely affect our business, financial condition and results of operations.

Derivative financial instruments – We use derivative instruments principally to reduce our exposure to market risks from changes in foreign currency exchange rates and interest rates. We do not enter into or hold derivative instruments for speculative trading purposes. We transact business globally and are subject to risks associated with changing foreign currency exchange rates. We enter into foreign currency hedges such as forward and option contracts that change in value as foreign currency exchange rates change. These contracts hedge forecasted foreign currency transactions in order to mitigate fluctuations in our earnings and cash flows associated with changes in foreign currency exchange rates. We designate foreign currency hedges as cash flow hedges. We also are exposed to the impact of interest rate changes primarily through our borrowing activities. For fixed rate borrowings, we may use variable interest rate swaps, effectively converting fixed rate borrowings to variable rate borrowings in order to reduce the amount of interest paid. These swaps are designated as fair value hedges. For variable rate borrowings, we may use fixed interest rate swaps, effectively converting variable rate borrowings to fixed rate borrowings in order to mitigate the impact of interest rate changes on earnings. These swaps are designated as cash flow hedges. We also may enter into derivative instruments that are not designated as hedges and do not qualify for hedge accounting, which are intended to mitigate certain economic exposures.

We record derivatives at their fair value. The classification of gains and losses resulting from changes in the fair values of derivatives is dependent on our intended use of the derivative and its resulting designation. Adjustments to reflect changes in fair values of derivatives attributable to the effective portion of hedges are either reflected in earnings and largely offset by corresponding adjustments to the hedged items or reflected net of income taxes in accumulated other comprehensive loss until the hedged transaction is recognized in earnings. Changes in the fair value of the derivatives that are attributable to the ineffective portion of the hedges or of derivatives that are not considered to be highly effective hedges, if any, are immediately recognized in earnings. The aggregate notional amount of our outstanding interest rate swaps at both December 31, 2017 and 2016 was \$1.2 billion and the fair value was not significant. The aggregate notional amount of our outstanding foreign currency hedges at December 31, 2017 and 2016 was \$4.1 billion and \$4.0 billion and the fair value was not significant. Derivative instruments did not have a material impact on net earnings and comprehensive income during the years ended December 31, 2017, 2016 and 2015. Substantially all of our derivatives are designated for hedge accounting. See “Note 16 – Fair Value Measurements” for more information on the fair value measurements related to our derivative instruments.

Recent Accounting Pronouncements

Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers, as amended (Topic 606) (commonly referred to as ASC 606), which will change the way we recognize revenue and significantly expand the disclosure requirements for revenue arrangements. The new standard is effective for annual reporting periods beginning after December 15, 2017.

We adopted the requirements of the new standard on January 1, 2018 using the full retrospective transition method, whereby ASC 606 will be applied to each prior year presented and the cumulative effect of applying ASC 606 will be recognized at January 1, 2016, the beginning of the earliest year presented. As ASC 606 supersedes substantially all existing revenue guidance affecting us under current GAAP, it will impact revenue and cost recognition across all of our business segments, as well as our business processes and our information technology systems.

We commenced our evaluation of the impact of ASC 606 in late 2014, by evaluating its impact on selected contracts at each of our business segments. With this baseline understanding, we developed a project plan to evaluate thousands of contracts across our business segments, develop processes and tools to dual report financial results under both current GAAP and ASC 606 and assess the internal control structure in order to adopt ASC 606 on January 1, 2018. We have periodically briefed our Audit Committee on our progress made towards adoption.

We currently recognize the majority of our revenue using the percentage-of-completion method of accounting, whereby revenue is recognized as we progress on the contract. For contracts with a significant amount of development and/or requiring the delivery of a minimal number of units, revenue and profit are recognized using the percentage-of-completion cost-to-cost method to measure progress. For example, we use this method at our Aeronautics business segment for the F-35 program; at our Missiles and Fire Control (MFC) business segment for the THAAD program; at our RMS business segment for the Littoral Combat Ship and Aegis Combat System programs; and at our Space business segment for government satellite programs. For contracts that

require us to produce a substantial number of similar items without a significant level of development, we currently record revenue and profit using the percentage-of-completion units-of-delivery method as the basis for measuring progress on the contract. For example, we use this method in Aeronautics for the C-130J and C-5 programs; in MFC for tactical missile programs (e.g., Hellfire, JASSM), PAC-3 programs and fire control programs (e.g., LANTIRN® and SNIPER®); in RMS for Black Hawk and Seahawk helicopter programs; and in Space for commercial satellite programs. For contracts to provide services to the U.S. Government, revenue is generally recorded using the percentage-of-completion cost-to-cost method.

Under ASC 606, revenue will be recognized as the customer obtains control of the goods and services promised in the contract (i.e., performance obligations). Given the nature of our products and terms and conditions in our contracts, in particular those with the U.S. Government (including foreign military sales (FMS) contracts), the customer obtains control as we perform work under the contract. Therefore, we expect to recognize revenue over time for substantially all of our contracts using a method similar to our current percentage-of-completion cost-to-cost method. Accordingly, adoption of ASC 606 will primarily impact our contracts where revenue is currently recognized using the percentage-of-completion units-of-delivery method. As a result, we anticipate recognizing revenue for these contracts earlier in the performance period as we incur costs, as opposed to when units are delivered. We may also have more performance obligations in our contracts under ASC 606, which may impact the timing of recording sales and operating profit, including those where sales recognition is deferred pending the incurrence of costs.

During the third quarter of 2017, we completed our preliminary assessment of the cumulative effect of adopting ASC 606 on our December 31, 2015 balance sheet using the full retrospective transition method. The adoption resulted in a decrease in inventories, an increase in billed receivables, contract assets (i.e., unbilled receivables) and contract liabilities (i.e., customer advances and amounts in excess of costs incurred) to primarily reflect the impact of converting contracts currently applying the units-of-delivery method to the cost-to-cost method for recognizing revenue and profits. We expect the net impact of these reclassifications to increase both our current assets and current liabilities by approximately 2%.

In addition, we have completed our preliminary assessment of adopting ASC 606 on our 2017 and 2016 operating results, and have presented selected recast, unaudited financial data in the following table (in millions, except per share data). The impact of adopting ASC 606 on our 2017 and 2016 operating results may not be indicative of the adoption impacts in future periods or of our operating performance.

	Years Ended	
	December 31,	
	2017	2016
	(unaudited)	
Net sales	\$49,976	\$47,320
Operating profit ^(a)	\$6,759	\$5,910

Earnings per common share

Basic		
Continuing operations	\$6.63	\$12.28
Discontinued operations	0.26	5.05
Basic earnings per common share	\$6.89	\$17.33
Diluted		
Continuing operations	\$6.57	\$12.13
Discontinued operations	0.25	4.99
Diluted earnings per common share	\$6.82	\$17.12

Operating profit includes an increase of \$846 million in 2017 and \$471 million in 2016 for the expected impact of ^(a) adopting ASU No. 2017-07, Compensation-Retirement Benefits (Topic 715) on January 1, 2018 as discussed below.

Total net cash provided by operating activities and net cash used by investing and financing activities on our consolidated statements of cash flows were not impacted by the adoption of ASC 606.

Compensation-Retirement Benefits

In March 2017, the FASB issued ASU No. 2017-07, Compensation-Retirement Benefits (Topic 715), which changes the income statement presentation of certain components of net periodic benefit cost related to defined benefit pension and other postretirement benefit plans. Currently, we record all components of net periodic benefit costs in operating profit as part of cost of sales. Under ASU No. 2017-07, we will be required to record only the service cost component of net periodic benefit cost in operating profit and the non-service cost components of net periodic benefit cost (i.e., interest cost, expected return on plan assets, amortization

of prior service cost or credits, and net actuarial gains or losses) as part of non-operating income. We adopted the requirements of ASU No. 2017-07 on January 1, 2018 using the retrospective transition method. We expect the adoption of ASU No. 2017-07 to result in an increase to consolidated operating profit of \$471 million and \$846 million for 2016 and 2017, respectively, and a corresponding decrease in non-operating income for each year. We do not expect any impact to our business segment operating profit, our consolidated net earnings, or cash flows as a result of adopting ASU No. 2017-07.

Intangibles-Goodwill and Other

In January 2017, the FASB issued ASU No. 2017-04, Intangibles-Goodwill and Other (Topic 350), which eliminates the requirement to compare the implied fair value of reporting unit goodwill with the carrying amount of that goodwill (commonly referred to as Step 2) from the goodwill impairment test. The new standard does not change how a goodwill impairment is identified. We will continue to perform our quantitative and qualitative goodwill impairment test by comparing the fair value of each reporting unit to its carrying amount, but if we are required to recognize a goodwill impairment charge, under the new standard the amount of the charge will be calculated by subtracting the reporting unit's fair value from its carrying amount. Under the prior standard, if we were required to recognize a goodwill impairment charge, Step 2 required us to calculate the implied value of goodwill by assigning the fair value of a reporting unit to all of its assets and liabilities as if that reporting unit had been acquired in a business combination and the amount of the charge was calculated by subtracting the reporting unit's implied fair value of goodwill from its actual goodwill balance. The new standard is effective for interim and annual reporting periods beginning after December 15, 2019, with early adoption permitted, and should be applied prospectively from the date of adoption. We elected to adopt the new standard for future goodwill impairment tests at the beginning of the third quarter of 2017, because it significantly simplifies the evaluation of goodwill for impairment. The impact of the new standard will depend on the outcomes of future goodwill impairment tests.

Derivatives and Hedging

In August 2017, the FASB issued ASU No. 2017-12, Derivatives and Hedging (Topic 815), which eliminates the requirement to separately measure and report hedge ineffectiveness. The guidance is effective for fiscal years beginning after December 15, 2018, with early adoption permitted. We do not expect a significant impact to our consolidated assets and liabilities, net earnings, or cash flows as a result of adopting this new standard. We plan to adopt the new standard January 1, 2019.

Leases

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842), which requires the recognition of lease assets and lease liabilities on the balance sheet and disclosure of key information about leasing arrangements for both lessees and lessors. The new standard is effective January 1, 2019 for public companies, with early adoption permitted. The new standard currently requires the application of a modified retrospective approach to the beginning of the earliest period presented in the financial statements. We are continuing to evaluate the expected impact to our consolidated financial statements and related disclosures. We plan to adopt the new standard effective January 1, 2019.

Note 2 – Earnings Per Share

The weighted average number of shares outstanding used to compute earnings per common share were as follows (in millions):

	2017	2016	2015
Weighted average common shares outstanding for basic computations	287.8	299.3	310.3
Weighted average dilutive effect of equity awards	2.8	3.8	4.4
Weighted average common shares outstanding for diluted computations	290.6	303.1	314.7

We compute basic and diluted earnings per common share by dividing net earnings by the respective weighted average number of common shares outstanding for the periods presented. Our calculation of diluted earnings per common share also includes the dilutive effects for the assumed vesting of outstanding restricted stock units (RSUs), performance stock units (PSUs) and exercise of outstanding stock options based on the treasury stock method. There were no significant anti-dilutive equity awards for the years ended December 31, 2017, 2016 and 2015.

Note 3 – Acquisitions and Divestitures

Acquisition of Sikorsky Aircraft Corporation

On November 6, 2015, we completed the acquisition of Sikorsky from United Technologies Corporation (UTC) and certain of UTC's subsidiaries. The purchase price of the acquisition was \$9.0 billion, net of cash acquired. As a result of the acquisition,

17

Sikorsky became a wholly-owned subsidiary of ours. Sikorsky is a global company primarily engaged in the research, design, development, manufacture and support of military and commercial helicopters. Sikorsky's products include military helicopters such as the Black Hawk, Seahawk, CH-53K, H-92; and commercial helicopters such as the S-76 and S-92. The acquisition enables us to extend our core business into the military and commercial rotary wing markets, allowing us to strengthen our position in the aerospace and defense industry. Further, this acquisition will expand our presence in commercial and international markets. Sikorsky has been aligned under our RMS business segment.

To fund the \$9.0 billion acquisition price, we utilized \$6.0 billion of proceeds borrowed under a temporary 364-day revolving credit facility (the 364-day Facility), \$2.0 billion of cash on hand and \$1.0 billion from the issuance of commercial paper. In the fourth quarter of 2015, we repaid all outstanding borrowings under the 364-day Facility with the proceeds from the issuance of \$7.0 billion of fixed interest-rate long-term notes in a public offering (the November 2015 Notes). In the fourth quarter of 2015, we also repaid the \$1.0 billion in commercial paper borrowings.

Allocation of Purchase Price to Assets Acquired and Liabilities Assumed

We accounted for the acquisition of Sikorsky as a business combination, which requires us to record the assets acquired and liabilities assumed at fair value. The amount by which the purchase price exceeds the fair value of the net assets acquired is recorded as goodwill.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the acquisition date, including the refinements described in the previous paragraph (in millions):

Cash and cash equivalents	\$75
Receivables, net	1,924
Inventories, net	1,632
Other current assets	46
Property, plant and equipment	649
Goodwill	2,842
Intangible assets:	
Customer programs	3,184
Trademarks	887
Other noncurrent assets	572
Deferred income taxes, noncurrent	256
Total identifiable assets and goodwill	12,067
Accounts payable	(565)
Customer advances and amounts in excess of costs incurred	(1,197)
Salaries, benefits, and payroll taxes	(105)
Other current liabilities	(430)
Customer contractual obligations ^(a)	(507)
Other noncurrent liabilities	(185)
Total liabilities assumed	(2,989)
Total consideration	\$9,078

^(a) Recorded in other noncurrent liabilities on our consolidated balance sheets.

Intangible assets related to customer programs were recognized for each major helicopter and aftermarket program and represent the aggregate value associated with the customer relationships, contracts, technology and tradenames underlying the associated program. These intangible assets will be amortized on a straight-line basis over a weighted-average useful life of approximately 15 years. The useful life is based on a period of expected cash flows used to measure the fair value of each of the intangible assets.

Customer contractual obligations represent liabilities on certain development programs where the expected costs exceed the expected sales under contract. We measured these liabilities based on the price to transfer the obligation to a market participant at the measurement date, assuming that the liability will remain outstanding in the marketplace. Based on the estimated net cash outflows of the developmental programs plus a reasonable contracting profit margin required to transfer the contracts to market participants, we recorded assumed liabilities of \$507 million. These liabilities will be liquidated in accordance with the underlying

economic pattern of the contractual obligations, as reflected by the estimated future net cash outflows incurred on the associated contracts. As of December 31, 2017, we recognized approximately \$225 million in sales related to customer contractual obligations. As of December 31, 2017, the estimated liquidation of the customer contractual obligation is approximated as follows: \$100 million in 2018, \$55 million in 2019, \$55 million in 2020, \$55 million in 2021, \$5 million in 2022 and \$12 million thereafter.

The fair values of the assets acquired and liabilities assumed were determined using income, market and cost valuation methodologies. The fair value measurements were estimated using significant inputs that are not observable in the market and thus represent a Level 3 measurement as defined in Accounting Standards Codification (ASC) 820, Fair Value Measurement. The income approach was primarily used to value the customer programs and trademarks intangible assets. The income approach indicates value for an asset or liability based on the present value of cash flow projected to be generated over the remaining economic life of the asset or liability being measured. Both the amount and the duration of the cash flows are considered from a market participant perspective. Our estimates of market participant net cash flows considered historical and projected pricing, remaining developmental effort, operational performance including company-specific synergies, aftermarket retention, product life cycles, material and labor pricing, and other relevant customer, contractual and market factors. Where appropriate, the net cash flows are adjusted to reflect the uncertainties associated with the underlying assumptions, as well as the risk profile of the net cash flows utilized in the valuation. The adjusted future cash flows are then discounted to present value using an appropriate discount rate. Projected cash flow is discounted at a required rate of return that reflects the relative risk of achieving the cash flows and the time value of money. The market approach is a valuation technique that uses prices and other relevant information generated by market transactions involving identical or comparable assets, liabilities, or a group of assets and liabilities. Valuation techniques consistent with the market approach often use market multiples derived from a set of comparables. The cost approach, which estimates value by determining the current cost of replacing an asset with another of equivalent economic utility, was used, as appropriate, for property, plant and equipment. The cost to replace a given asset reflects the estimated reproduction or replacement cost, less an allowance for loss in value due to depreciation.

The purchase price allocation resulted in the recognition of \$2.8 billion of goodwill, all of which is expected to be amortizable for tax purposes. Substantially all of the goodwill was assigned to our RMS business. The goodwill recognized is attributable to expected revenue synergies generated by the integration of our products and technologies with those of Sikorsky, costs synergies resulting from the consolidation or elimination of certain functions, and intangible assets that do not qualify for separate recognition, such as the assembled workforce of Sikorsky.

Determining the fair value of assets acquired and liabilities assumed requires the exercise of significant judgments, including the amount and timing of expected future cash flows, long-term growth rates and discount rates. The cash flows employed in the DCF analyses are based on our best estimate of future sales, earnings and cash flows after considering factors such as general market conditions, customer budgets, existing firm orders, expected future orders, contracts with suppliers, labor agreements, changes in working capital, long term business plans and recent operating performance. Use of different estimates and judgments could yield different results.

Impact to 2015 Financial Results

Sikorsky's 2015 financial results have been included in our consolidated financial results only for the period from the November 6, 2015 acquisition date through December 31, 2015. As a result, our consolidated financial results for the year ended December 31, 2015 do not reflect a full year of Sikorsky's results. From the November 6, 2015 acquisition date through December 31, 2015, Sikorsky generated net sales of approximately \$400 million and operating loss of approximately \$45 million, inclusive of intangible amortization and adjustments required to account for the acquisition.

We incurred approximately \$38 million of non-recoverable transaction costs associated with the Sikorsky acquisition in 2015 that were expensed as incurred. These costs are included in other income, net on our consolidated statements of earnings. We also incurred approximately \$48 million in costs associated with issuing the \$7.0 billion November 2015 Notes used to repay all outstanding borrowings under the 364-day Facility used to finance the acquisition. The financing costs were recorded as a reduction of debt and will be amortized to interest expense over the term of the related debt.

Supplemental Pro Forma Financial Information (unaudited)

The following table presents summarized unaudited pro forma financial information as if Sikorsky had been included in our financial results for the entire year in 2015 (in millions):

Net sales	\$45,366
Net earnings	3,534
Basic earnings per common share	11.39
Diluted earnings per common share	11.23

The unaudited supplemental pro forma financial data above has been calculated after applying our accounting policies and adjusting the historical results of Sikorsky with pro forma adjustments, net of tax, that assume the acquisition occurred on January 1, 2015. Significant pro forma adjustments include the recognition of additional amortization expense related to acquired intangible assets and additional interest expense related to the short-term debt used to finance the acquisition. These adjustments assume the application of fair value adjustments to intangibles and the debt issuance occurred on January 1, 2015 and are approximated as follows: amortization expense of \$125 million and interest expense of \$40 million. In addition, significant nonrecurring adjustments include the elimination of a \$72 million pension curtailment loss, net of tax, recognized in 2015 and the elimination of a \$58 million income tax charge related to historic earnings of foreign subsidiaries recognized by Sikorsky in 2015.

The unaudited supplemental pro forma financial information also reflects an increase in interest expense, net of tax, of approximately \$110 million in 2015. The increase in interest expense is the result of assuming the November 2015 Notes were issued on January 1, 2015. Proceeds of the November 2015 Notes were used to repay all outstanding borrowings under the 364-day Facility used to finance a portion of the purchase price of Sikorsky, as contemplated at the date of acquisition.

The unaudited supplemental pro forma financial information does not reflect the realization of any expected ongoing cost or revenue synergies relating to the integration of the two companies. Further, the pro forma data should not be considered indicative of the results that would have occurred if the acquisition, related financing and associated notes issuance and repayment of the 364-day Facility had been consummated on January 1, 2015, nor are they indicative of future results.

Consolidation of AWE Management Limited

On August 24, 2016, we increased our ownership interest in the AWE joint venture, which operates the United Kingdom's nuclear deterrent program, from 33% to 51%. At which time, we began consolidating AWE. Consequently, our operating results include 100% of AWE's sales and 51% of its operating profit. Prior to increasing our ownership interest, we accounted for our investment in AWE using the equity method of accounting. Under the equity method, we recognized only 33% of AWE's earnings or losses and no sales. Accordingly, prior to August 24, 2016, the date we obtained control, we recorded 33% of AWE's net earnings in our operating results and subsequent to August 24, 2016, we recognized 100% of AWE's sales and 51% of its operating profit.

We accounted for this transaction as a "step acquisition" (as defined by U.S. GAAP), which requires us to consolidate and record the assets and liabilities of AWE at fair value. Accordingly, we recorded intangible assets of \$243 million related to customer relationships, \$32 million of net liabilities, and noncontrolling interests of \$107 million. The intangible assets are being amortized over a period of eight years in accordance with the underlying pattern of economic benefit reflected by the future net cash flows. In 2016, we recognized a non-cash net gain of \$104 million associated with obtaining a controlling interest in AWE, which consisted of a \$127 million pretax gain recognized in the operating results of our Space business segment and \$23 million of tax-related items at our corporate office. The gain represents the fair value of our 51% interest in AWE, less the carrying value of our previously held investment in AWE and deferred taxes. The gain was recorded in other income, net on our consolidated statements of earnings. The fair value of AWE (including the intangible assets), our controlling interest, and the noncontrolling interests were determined using the income approach.

Divestiture of the Information Systems & Global Solutions Business

On August 16, 2016, we divested our former IS&GS business, which merged with Leidos, in a Reverse Morris Trust transaction (the "Transaction"). The Transaction was completed in a multi-step process pursuant to which we initially contributed the IS&GS business to Abacus Innovations Corporation (Abacus), a wholly owned subsidiary of Lockheed Martin created to facilitate the Transaction, and the common stock of Abacus was distributed to

participating Lockheed Martin stockholders through an exchange offer. Under the terms of the exchange offer, Lockheed Martin stockholders had the option to exchange shares of Lockheed Martin common stock for shares of Abacus common stock. At the conclusion of the exchange offer, all shares of Abacus common stock were exchanged for 9,369,694 shares of Lockheed Martin common stock held by Lockheed Martin stockholders that elected to participate in the exchange. The shares of Lockheed Martin common stock that were exchanged and accepted were retired, reducing the number of shares of our common stock outstanding by approximately 3%. Following the exchange offer, Abacus merged with

a subsidiary of Leidos, with Abacus continuing as the surviving corporation and a wholly-owned subsidiary of Leidos. As part of the merger, each share of Abacus common stock was automatically converted into one share of Leidos common stock. We did not receive any shares of Leidos common stock as part of the Transaction and do not hold any shares of Leidos or Abacus common stock following the Transaction. Based on an opinion of outside tax counsel, subject to customary qualifications and based on factual representations, the exchange offer and merger will qualify as tax-free transactions to Lockheed Martin and its stockholders, except to the extent that cash was paid to Lockheed Martin stockholders in lieu of fractional shares.

In connection with the Transaction, Abacus borrowed an aggregate principal amount of approximately \$1.84 billion under term loan facilities with third party financial institutions, the proceeds of which were used to make a one-time special cash payment of \$1.80 billion to Lockheed Martin and to pay associated borrowing fees and expenses. The entire special cash payment was used to repay debt, pay dividends and repurchase stock during the third and fourth quarters of 2016. The obligations under the Abacus term loan facilities were guaranteed by Leidos as part of the Transaction.

As a result of the Transaction, we recognized a net gain of approximately \$1.3 billion, including \$1.2 billion recognized in 2016. The net gain represents the \$2.5 billion fair value of the shares of Lockheed Martin common stock exchanged and retired as part of the exchange offer, plus the \$1.8 billion one-time special cash payment, less the net book value of the IS&GS business of about \$3.0 billion at August 16, 2016 and other adjustments of about \$100 million. During the fourth quarter of 2017, we recognized an additional gain of \$73 million, which reflects certain post-closing adjustments, including certain tax adjustments and the final determination of net working capital. We classified the operating results of our former IS&GS business as discontinued operations in our consolidated financial statements in accordance with U.S. GAAP, as the divestiture of this business represented a strategic shift that had a major effect on our operations and financial results. However, the cash flows generated by the IS&GS business have not been reclassified in our consolidated statements of cash flows as we retained this cash as part of the Transaction.

The operating results of the IS&GS business that have been reflected within net earnings from discontinued operations for the years ended December 31, 2016 and 2015 are as follows (in millions):

	2016	^(a) 2015
Net sales	\$3,410	\$5,596
Cost of sales	(2,953)	(4,868)
Severance charges	(19)	(20)
Gross profit	438	708
Other income, net	16	16
Operating profit	454	724
Earnings from discontinued operations before income taxes	454	724
Income tax expense	(147)	(245)
Net gain on divestiture of discontinued operations	1,242	—
Net earnings from discontinued operations	\$1,549	\$479

(a) Operating results for the year ended December 31, 2016 reflect operating results prior to the August 16, 2016 divestiture date.

The operating results of the IS&GS business reported as discontinued operations are different than the results previously reported for the IS&GS business segment. Results reported within net earnings from discontinued operations only include costs that were directly attributable to the IS&GS business and exclude certain corporate overhead costs that were previously allocated to the IS&GS business. As a result, we reclassified \$82 million in 2016 and \$165 million in 2015 of corporate overhead costs from the IS&GS business to other unallocated, net on our consolidated statements of earnings.

Additionally, we retained all assets and obligations related to the pension benefits earned by former IS&GS business salaried employees through the date of divestiture. Therefore, the non-service portion of net pension costs (e.g., interest cost, actuarial gains and losses and expected return on plan assets) for these plans have been reclassified from the operating results of the IS&GS business segment and reported as a reduction to the FAS/CAS pension adjustment. These net pension costs were \$54 million and \$71 million for the years ended December 31, 2016 and 2015. The

service portion of net pension costs related to IS&GS business's salaried employees that transferred to Leidos were included in the operating results of the IS&GS business classified as discontinued operations because such costs are no longer incurred by us.

Significant severance charges related to the IS&GS business were historically recorded at the Lockheed Martin corporate office. These charges have been reclassified into the operating results of the IS&GS business, classified as discontinued operations,

and excluded from the operating results of our continuing operations. The amount of severance charges reclassified were \$19 million in 2016 and \$20 million in 2015.

In connection with the Transaction, Lockheed Martin retained certain liabilities, including liabilities associated with the New York Metropolitan Transportation Authority and its Capital Construction Company (collectively, the MTA) litigation discussed in “Note 14 - Legal Proceedings, Commitments and Contingencies,” and has indemnified Abacus and Leidos in connection with other liabilities associated with the IS&GS business, including certain liabilities associated with ongoing investigations by the Department of Energy and the Department of Justice (DOJ) relating to the IS&GS business’s involvement in the Mission Support Alliance, LLC (MSA) joint venture that manages and operates the Hanford Nuclear site for the Department of Energy. The DOJ has issued a number of Civil Investigative Demands to MSA, Lockheed Martin and the subsidiary of Lockheed Martin that performed information technology services for MSA, as well as current and former employees of each of these entities, and is continuing its False Claims Act investigation into matters involving MSA and the IS&GS business. The DOJ also is conducting a parallel criminal investigation. The investigations relate primarily to certain information technology services performed by a subsidiary of Lockheed Martin under a fixed price/fixed unit rate subcontract to MSA. In the event that the DOJ were to pursue a claim in connection with the ongoing MSA investigation, through the indemnification provisions agreed to as part of the Transaction, Lockheed Martin and Leidos have allocated liabilities between themselves.

Financial information related to cash flows generated by the IS&GS business, such as depreciation and amortization, capital expenditures, and other non-cash items, included in our consolidated statements of cash flows for the years ended December 31, 2016 and 2015 were not significant.

Other Divestitures

During 2016, we completed the sale of our Lockheed Martin Commercial Flight Training (LMCFT) business, which was classified as held for sale in the fourth quarter of 2015. Other, net in 2015 includes a non-cash asset impairment charge of approximately \$90 million. This charge was partially offset by a net deferred tax benefit of about \$80 million, which is recorded in income tax expense. The net impact reduced net earnings by about \$10 million. LMCFT’s financial results are not material and there was no significant impact on our consolidated financial results as a result of completing the sale of our LMCFT business. Accordingly, LMCFT’s financial results are not classified in discontinued operations.

Note 4 – Goodwill and Acquired Intangibles

Changes in the carrying amount of goodwill by segment were as follows (in millions):

	Aeronautics	MFC	RMS	Space	Total
Balance at December 31, 2015	\$ 171	\$2,198	\$6,738	\$1,588	\$10,695
Purchase accounting adjustments	—	—	78	—	78
Other	—	62	(68)	(3)	(9)
Balance at December 31, 2016	171	2,260	6,748	1,585	10,764
Other	—	5	36	2	43
Balance at December 31, 2017	\$ 171	\$2,265	\$6,784	\$1,587	\$10,807

The gross carrying amounts and accumulated amortization of our acquired intangible assets consisted of the following (in millions):

	2017			2016		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Finite-Lived:						
Customer programs	\$3,184	\$ (503)	\$ 2,681	\$3,184	\$ (273)	\$ 2,911
Customer relationships	352	(140)	212	359	(92)	267
Other	71	(54)	17	111	(83)	28
Total finite-lived intangibles	3,607	(697)	2,910	3,654	(448)	3,206
Indefinite-Lived:						
Trademarks	887	—	887	887	—	887
Total acquired intangibles	\$4,494	\$ (697)	\$ 3,797	\$4,541	\$ (448)	\$ 4,093

Acquired finite-lived intangible assets are amortized to expense primarily on a straight-line basis over the following estimated useful lives: customer programs, from nine to 20 years; customer relationships, from four to 10 years; and other intangibles, from three to 10 years.

Amortization expense for acquired finite-lived intangible assets was \$312 million, \$284 million and \$68 million in 2017, 2016 and 2015. Estimated future amortization expense is as follows: \$296 million in 2018; \$285 million in 2019; \$263 million in 2020; \$256 million in 2021; \$253 million in 2022 and \$1.6 billion thereafter.

Note 5 – Information on Business Segments

We operate in four business segments: Aeronautics, MFC, RMS and Space. We organize our business segments based on the nature of the products and services offered. Following is a brief description of the activities of our business segments:

Aeronautics – Engaged in the research, design, development, manufacture, integration, sustainment, support and upgrade of advanced military aircraft, including combat and air mobility aircraft, unmanned air vehicles and related technologies.

Missiles and Fire Control – Provides air and missile defense systems; tactical missiles and air-to-ground precision strike weapon systems; logistics; fire control systems; mission operations support, readiness, engineering support and integration services; manned and unmanned ground vehicles; and energy management solutions.

Rotary and Mission Systems – Provides design, manufacture, service and support for a variety of military and civil helicopters; ship and submarine mission and combat systems; mission systems and sensors for rotary and fixed-wing aircraft; sea and land-based missile defense systems; radar systems; the Littoral Combat Ship; simulation and training services; and unmanned systems and technologies. In addition, RMS supports the needs of customers in cybersecurity and delivers communications and command and control capability through complex mission solutions for defense applications. The 2015 results of the acquired Sikorsky business have been included in our consolidated results of operations from the November 6, 2015 acquisition date through December 31, 2015. Accordingly, the consolidated results of operations for the year ended December 31, 2015 do not reflect a full year of Sikorsky operations.

Space – Engaged in the research and development, design, engineering and production of satellites, strategic and defensive missile systems and space transportation systems. Space provides network-enabled situational awareness and integrates complex space and ground-based global systems to help our customers gather, analyze and securely distribute critical intelligence data. Space is also responsible for various classified systems and services in support of vital national security systems. Prior to August 24, 2016, the date we obtained control of AWE we accounted for the venture using the equity method of accounting with 33% of AWE's earnings or losses recognized by Space. Subsequent to August 24, 2016, we obtained control of AWE and 100% of AWE's sales and 51% of AWE's earnings have been included in our consolidated results of operations. Accordingly, the consolidated results of operations for the year ended December 31, 2016 do not reflect a full year of AWE operations. Operating profit for our Space business segment also includes our share of earnings for our investment in ULA, which provides expendable launch services to the U.S. Government.

The financial information in the following tables includes the results of businesses we have acquired from their respective dates of acquisition and excludes businesses included in discontinued operations (see "Note 3 – Acquisitions and Divestitures") for all years presented. Net sales of our business segments exclude intersegment sales as these activities are eliminated in consolidation.

Operating profit of our business segments includes our share of earnings or losses from equity method investees as the operating activities of the equity method investees are closely aligned with the operations of our business segments. ULA, results of which are included in our Space business segment, is our primary equity method investee. Operating profit of our business segments excludes the FAS/CAS pension adjustment described below; expense for stock-based compensation; the effects of items not considered part of management's evaluation of segment operating performance, such as charges related to significant severance actions (see "Note 15 – Restructuring Charges") and goodwill impairments; gains or losses from significant divestitures; the effects of certain legal settlements; corporate costs not allocated to our business segments; and other miscellaneous corporate activities. These items are included in the reconciling item "Unallocated items" between operating profit from our business segments and our consolidated operating profit. See "Note 1 – Significant Accounting Policies" (under the caption "Use of Estimates") for a discussion related to certain factors that may impact the comparability of net sales and operating profit of our business segments.

Our business segments' results of operations include pension expense only as calculated under U.S. Government Cost Accounting Standards (CAS), which we refer to as CAS pension cost. We recover CAS pension cost through the pricing of our products and services on U.S. Government contracts and, therefore, the CAS pension cost is recognized in each of our business segments' net sales and cost of sales. Since our consolidated financial statements must present pension expense calculated in

23

accordance with the financial accounting standards (FAS) requirements under GAAP, which we refer to as FAS pension expense, the FAS/CAS pension adjustment increases or decreases the CAS pension cost recorded in our business segments' results of operations to equal the FAS pension expense.

Selected Financial Data by Business Segment

Summary operating results for each of our business segments were as follows (in millions):

	2017	2016	2015
Net sales			
Aeronautics	\$20,148	\$17,769	\$15,570
Missiles and Fire Control	7,212	6,608	6,770
Rotary and Mission Systems	14,215	13,462	9,091
Space	9,473	9,409	9,105
Total net sales	\$51,048	\$47,248	\$40,536
Operating profit			
Aeronautics	\$2,164	\$1,887	\$1,681
Missiles and Fire Control	1,053	1,018	1,282
Rotary and Mission Systems	905	906	844
Space ^(a)	993	1,289	1,171
Total business segment operating profit	5,115	5,100	4,978
Unallocated items			
FAS/CAS pension adjustment			
FAS pension expense ^{(b)(c)}	(1,372)	(1,019)	(1,127)
Less: CAS pension cost ^{(b)(c)}	2,248	1,921	1,527
FAS/CAS pension adjustment	876	902	400
Severance charges ^{(b)(d)}	—	(80)	(82)
Stock-based compensation	(158)	(149)	(133)
Other, net ^{(e)(f)}	88	(224)	(451)
Total unallocated, net	806	449	(266)
Total consolidated operating profit	\$5,921	\$5,549	\$4,712

On August 24, 2016, our ownership interest in the AWE joint venture increased from 33% to 51% and we were required to change our accounting for this investment from the equity method to consolidation. As a result of the ^(a) increased ownership interest, we recognized a non-cash gain of \$127 million at our Space business segment, which increased net earnings from continuing operations by \$104 million (\$0.34 per share) in 2016. See “Note 3 – Acquisitions and Divestitures” for more information.

FAS pension expense, CAS pension costs and severance charges reflect the reclassification for discontinued ^(b) operations presentation of benefits related to former IS&GS salaried employees (see “Note 11 – Postretirement Benefit Plans”).

The higher FAS expense in 2017 is primarily due to a lower discount rate and lower expected long-term rate of ^(c) return on plan assets in 2017 versus 2016. The higher CAS pension cost primarily reflects the impact of phasing in CAS Harmonization (see “Note 11 – Postretirement Benefit Plans”).

See “Note 15 – Restructuring Charges” for information on charges related to certain severance actions at our business ^(d) segments. Severance charges for initiatives that are not significant are included in business segment operating profit.

Other, net in 2017 includes a previously deferred non-cash gain of \$198 million related to properties sold in 2015 ^(e) as a result of completing our remaining obligations (see “Note 8 – Property, Plant and Equipment, net”) and a \$64 million charge, which represents our portion of a non-cash asset impairment charge recorded by our equity method investee, AMMROC (see “Note 1 – Significant Accounting Policies”).

^(f) Other, net in 2015 includes a non-cash asset impairment charge of approximately \$90 million related to our decision in 2015 to divest our LMCFT business (see “Note 3 – Acquisitions and Divestitures”). This charge was partially offset by a net deferred tax benefit of about \$80 million, which is recorded in income tax expense. The net impact reduced net earnings by about \$10 million. Additionally other, net in 2015 includes approximately \$38

million of non-recoverable transaction costs associated with the acquisition of Sikorsky.

Selected Financial Data by Business Segment (continued)

	2017	2016	2015
Intersegment sales			
Aeronautics	\$122	\$137	\$102
Missiles and Fire Control	366	305	315
Rotary and Mission Systems	2,009	1,816	1,533
Space	111	110	146
Total intersegment sales	\$2,608	\$2,368	\$2,096
Depreciation and amortization			
Aeronautics	\$311	\$299	\$317
Missiles and Fire Control	99	105	99
Rotary and Mission Systems	468	476	211
Space	245	212	220
Total business segment depreciation and amortization	1,123	1,092	847
Corporate activities	72	75	98
Total depreciation and amortization ^(a)	\$1,195	\$1,167	\$945
Capital expenditures			
Aeronautics	\$371	\$358	\$387
Missiles and Fire Control	156	167	120
Rotary and Mission Systems	308	271	169
Space	179	183	172
Total business segment capital expenditures	1,014	979	848
Corporate activities	163	75	60
Total capital expenditures ^(b)	\$1,177	\$1,054	\$908

Total depreciation and amortization in the table above excludes \$48 million and \$81 million for the years ended December 31, 2016 and 2015 related to the former IS&GS business segment. These amounts are included in depreciation and amortization in our consolidated statements of cash flows as we did not reclassify our cash flows to exclude the IS&GS business segment. See “Note 3 – Acquisitions and Divestitures” for more information.

Total capital expenditures in the table above excludes \$9 million and \$31 million for the years ended December 31, 2016 and 2015 related to the former IS&GS business segment. These amounts are included in capital expenditures in our consolidated statements of cash flows as we did not reclassify our cash flows to exclude the IS&GS business segment. See “Note 3 – Acquisitions and Divestitures” for more information.

Selected Financial Data by Business Segment (continued)

Net Sales by Customer Category

Net sales by customer category were as follows (in millions):

	2017	2016	2015
U.S. Government			
Aeronautics	\$12,753	\$11,714	\$11,195
Missiles and Fire Control	4,640	4,026	4,150
Rotary and Mission Systems	9,834	9,187	6,961
Space	8,097	8,543	8,845
Total U.S. Government net sales	\$35,324	\$33,470	\$31,151
International ^(a)			
Aeronautics	\$7,307	\$5,973	\$4,328
Missiles and Fire Control	2,423	2,444	2,449
Rotary and Mission Systems	4,006	3,798	2,016
Space	1,305	488	218
Total international net sales	\$15,041	\$12,703	\$9,011
U.S. Commercial and Other			
Aeronautics	\$88	\$82	\$47
Missiles and Fire Control	149	138	171
Rotary and Mission Systems	375	477	114
Space	71	378	42
Total U.S. commercial and other net sales	\$683	\$1,075	\$374
Total net sales	\$51,048	\$47,248	\$40,536

(a) International sales include foreign military sales contracted through the U.S. Government, direct commercial sales with international governments and commercial and other sales to international customers.

Our Aeronautics business segment includes our largest program, the F-35 Lightning II Joint Strike Fighter, an international multi-role, multi-variant, stealth fighter aircraft. Net sales for the F-35 program represented approximately 25% of our total consolidated net sales during 2017, and 23% during both 2016 and 2015.

Total assets and customer advances and amounts in excess of costs incurred for each of our business segments were as follows (in millions):

	2017	2016
Assets ^(a)		
Aeronautics	\$7,903	\$7,896
Missiles and Fire Control	4,395	4,000
Rotary and Mission Systems	18,235	18,367
Space	5,236	5,250
Total business segment assets	35,769	35,513
Corporate assets ^(b)	10,752	12,293
Total assets	\$46,521	\$47,806
Customer advances and amounts in excess of costs incurred		
Aeronautics	\$2,752	\$2,133
Missiles and Fire Control	1,268	1,517
Rotary and Mission Systems	2,288	2,590
Space	444	536
Total customer advances and amounts in excess of costs incurred	\$6,752	\$6,776

(a) We have no long-lived assets with material carrying values located in foreign countries.

(b) Corporate assets primarily include cash and cash equivalents, deferred income taxes, environmental receivables and investments held in a separate trust.

Note 6 – Receivables, net

Receivables, net consisted of the following (in millions):

	2017	2016
U.S. Government		
Amounts billed	\$1,433	\$792
Unbilled costs and accrued profits	6,337	6,877
Less: customer advances and progress payments	(1,042)	(1,346)
Total U.S. Government receivables, net	6,728	6,323
Other governments and commercial		
Amounts billed	687	546
Unbilled costs and accrued profits	1,651	1,847
Less: customer advances	(463)	(514)
Total other governments and commercial receivables, net	1,875	1,879
Total receivables, net	\$8,603	\$8,202

We expect to bill our customers for the majority of the December 31, 2017 unbilled costs and accrued profits during 2018.

Note 7 – Inventories, net

Inventories, net consisted of the following (in millions):

	2017	2016
Work-in-process, primarily related to long-term contracts and programs in progress	\$6,510	\$7,864
Spare parts, used aircraft and general stock materials	811	833
Other inventories	1,134	719
Total inventories	8,455	9,416
Less: customer advances and progress payments	(3,968)	(4,746)
Total inventories, net	\$4,487	\$4,670

Work-in-process inventories at December 31, 2017 and 2016 included general and administrative costs of \$509 million and \$529 million. General and administrative costs incurred and recorded in inventories totaled \$3.5 billion in 2017, \$3.3 billion in 2016 and \$2.7 billion in 2015. General and administrative costs charged to cost of sales from inventories totaled \$3.5 billion in 2017, \$3.3 billion in 2016 and \$2.8 billion in 2015.

Note 8 – Property, Plant and Equipment, net

Property, plant and equipment, net consisted of the following (in millions):

	2017	2016
Land	\$131	\$127
Buildings	6,401	6,385
Machinery and equipment	7,624	7,389
Construction in progress	1,205	976
Total property, plant and equipment	15,361	14,877
Less: accumulated depreciation and amortization	(9,586)	(9,328)
Total property, plant and equipment, net	\$5,775	\$5,549

Land Sales

During the fourth quarter of 2017, we recognized a previously deferred non-cash gain in other income, net in our consolidated statement of earnings of \$198 million (\$122 million or \$0.42 per share, after tax) related to properties sold in 2015 as a result of completing our remaining obligations.

Note 9 – Income Taxes

On December 22, 2017, the President signed the Tax Cuts and Jobs Act (the “Tax Act”). The Tax Act, among other things, lowered the U.S. corporate income tax rate from 35% to 21% effective January 1, 2018. Consequently, we wrote down our net deferred tax assets as of December 31, 2017 by \$1.9 billion to reflect the estimated impact of the Tax Act. We recorded a corresponding net one-time charge of \$1.9 billion (\$6.69 per share), substantially all of which was non-cash, primarily related to enactment of the Tax Act, the re-measurement of certain net deferred tax assets using the lower U.S. corporate income tax rate, a deemed repatriation tax, and a reduction in the U.S. manufacturing benefit as a result of our decision to accelerate contributions to our pension fund in 2018 in order to receive a tax deduction in 2017.

While we have substantially completed our provisional analysis of the income tax effects of the Tax Act and recorded a reasonable estimate of such effects, the net one-time charge related to the Tax Act may differ, possibly materially, due to, among other things, further refinement of our calculations, changes in interpretations and assumptions that we have made, additional guidance that may be issued by the U.S. Government, and actions and related accounting policy decisions we may take as a result of the Tax Act. We will complete our analysis over a one-year measurement period ending December 22, 2018, and any adjustments during this measurement period will be included in net earnings from continuing operations as an adjustment to income tax expense in the reporting period when such adjustments are determined.

Our provision for federal and foreign income tax expense for continuing operations consisted of the following (in millions):

	2017	2016	2015
Federal income tax expense (benefit):			
Current			
Operations	\$(189)	\$1,327	\$1,573
One-time charge due to tax legislation ^(a)	43	—	—
Deferred			
Operations	1,613	(231)	(473)
One-time charge due to tax legislation ^(a)	1,819	—	—
Total federal income tax expense	3,286	1,096	1,100
Foreign income tax expense (benefit):			
Current	53	56	39
Deferred	1	(19)	34
Total foreign income tax expense	54	37	73
Total income tax expense	\$3,340	\$1,133	\$1,173

^(a) Represents one-time charge due primarily to the re-measurement of certain net deferred tax assets using the lower U.S. corporate income tax rate and a deemed repatriation tax.

State income taxes are included in our operations as general and administrative costs and, under U.S. Government regulations, are allowable costs in establishing prices for the products and services we sell to the U.S. Government. Therefore, a substantial portion of state income taxes is included in our net sales and cost of sales. As a result, the impact of certain transactions on our operating profit and of other matters presented in these consolidated financial statements is disclosed net of state income taxes. Our total net state income tax expense was \$103 million for 2017, \$112 million for 2016, and \$106 million for 2015.

Our reconciliation of the 35% U.S. federal statutory income tax rate to actual income tax expense for continuing operations is as follows (dollars in millions):

	2017		2016		2015	
	Amount	Rate	Amount	Rate	Amount	Rate
Income tax expense at the U.S. federal statutory tax rate	\$1,844	35.0 %	\$1,710	35.0 %	\$1,505	35.0 %
Deferred tax write down and transition tax ^(a)	1,862	35.3	—	—	—	—
Excess tax benefits for share-based payment awards	(106)	(2.0)	(152)	(3.1)	—	—
U.S. manufacturing deduction benefit ^(b)	(7)	(0.1)	(117)	(2.4)	(123)	(2.9)
Research and development tax credit	(115)	(2.2)	(107)	(2.2)	(70)	(1.6)
Tax deductible dividends	(94)	(1.8)	(92)	(1.9)	(87)	(2.0)
Other, net	(44)	(0.8)	(109)	(2.2)	(52)	(1.2)
Income tax expense	\$3,340	63.4 %	\$1,133	23.2 %	\$1,173	27.3 %

(a) Includes one-time charge due primarily to the re-measurement of certain net deferred tax assets using the lower U.S. corporate income tax rate and a deemed repatriation tax.

(b) Includes a reduction in our 2017 manufacturing benefit as a result of our decision to accelerate contributions to our pension fund in 2018.

In 2016, we adopted the accounting standard update for employee share-based payment awards on a prospective basis. Accordingly, we recognized additional income tax benefits of \$106 million and \$152 million during the years ended December 31, 2017 and 2016. The 2016 income tax rate also benefited from the nontaxable gain recorded in connection with the consolidation of AWE.

Tax benefits from the U.S. manufacturing deduction were insignificant in 2017, \$117 million in 2016, and \$123 million in 2015. We recognized tax benefits of \$115 million in 2017, \$107 million in 2016, and \$70 million in 2015 from U.S. research and development (R&D) tax credits, including benefits attributable to prior periods. We receive a tax deduction for dividends paid on shares of our common stock held by certain of our defined contribution plans with an employee stock ownership plan feature. The amount of the tax deduction has increased as we increased our dividend over the last three years, partially offset by a decline in the number of shares in these plans. As a result of a decision in 2015 to divest our LMCFT business (see “Note 3 – Acquisitions and Divestitures”), we recorded an asset impairment charge of approximately \$90 million. This charge was partially offset by a net deferred tax benefit of about \$80 million. The net impact of the resulting tax benefit reduced the effective income tax rate by 1.2 percentage points in 2015.

We participate in the IRS Compliance Assurance Process program. Examinations of the years 2015, 2016, and 2017 remain under IRS review.

The primary components of our federal and foreign deferred income tax assets and liabilities at December 31 were as follows (in millions):

	2017 ^(a)	2016
Deferred tax assets related to:		
Accrued compensation and benefits	\$595	\$1,012
Pensions ^(b)	2,495	5,197
Other postretirement benefit obligations	153	302
Contract accounting methods	487	878
Foreign company operating losses and credits	27	30
Other	154	327
Valuation allowance ^(c)	(20)	(15)
Deferred tax assets, net	3,891	7,731
Deferred tax liabilities related to:		
Goodwill and purchased intangibles	266	378
Property, plant and equipment	239	346
Exchanged debt securities and other	303	418
Deferred tax liabilities	808	1,142
Net deferred tax assets	\$3,083	\$6,589

(a) Components of our federal and foreign deferred income tax assets and liabilities at December 31, 2017 after taking into account the estimated impacts of the Tax Act and related items.

The decrease in 2017 was primarily due to the enactment of the Tax Act and our decision to accelerate

(b) contributions of cash to our defined benefit pension plans, partially offset by the reduction in the discount rate used to measure our postretirement benefit plans (see “Note 11 – Postretirement Benefit Plans”).

(c) A valuation allowance was provided against certain foreign company deferred tax assets arising from carryforwards of unused tax benefits.

As of December 31, 2017 and 2016, our liabilities associated with unrecognized tax benefits are not material.

We and our subsidiaries file income tax returns in the U.S. federal jurisdiction and various foreign jurisdictions. With few exceptions, the statute of limitations is no longer open for U.S. federal or non-U.S. income tax examinations for the years before 2014, other than with respect to refunds.

U.S. income taxes have been provided on deemed repatriated earnings of \$435 million related to our non-U.S. companies as of December 31, 2017, as a result of the enactment of the Tax Act. The additional net transition tax of \$43 million on the deemed repatriated earnings was recorded for 2017. Before the Tax Act, U.S. income taxes and foreign withholding taxes have not been provided on earnings of \$386 million and \$310 million that have not been distributed by our non-U.S. companies as of December 31, 2016 and 2015. Our intention before enactment of the Tax Act was to permanently reinvest these earnings, thereby indefinitely postponing their remittance to the U.S. If these earnings had been remitted, we estimate that the additional income taxes after foreign tax credits would have been approximately \$64 million in 2016 and \$49 million in 2015. In addition, we have reevaluated our intention concerning repatriation of foreign earnings. While our investment in foreign subsidiaries continues to be permanent in duration, in light of our decision to accelerate contributions to our defined benefit pension plans, earnings from certain foreign subsidiaries may be repatriated.

Our federal and foreign income tax payments, net of refunds received, were \$1.1 billion in 2017, \$1.3 billion in 2016, and \$1.8 billion in 2015.

Note 10 – Debt

Our long-term debt consisted of the following (in millions):

	December 31,	
	2017	2016
Notes		
1.85% due 2018	\$750	\$750
4.25% due 2019	900	900
2.50% due 2020	1,250	1,250
3.35% due 2021	900	900
3.10% due 2023	500	500
2.90% due 2025	750	750
3.55% due 2026	2,000	2,000
3.60% due 2035	500	500
4.50% and 6.15% due 2036	1,054	1,152
4.85% due 2041	239	600
4.07% due 2042	1,336	1,336
3.80% due 2045	1,000	1,000
4.70% due 2046	1,326	2,000
4.09% due 2052	1,578	—
Other notes with rates from 5.50% to 8.50%, due 2023 to 2040	1,415	1,656
Total debt	15,498	15,294
Less: unamortized discounts and issuance costs	(1,235)	(1,012)
Total debt, net	14,263	14,282
Less: current portion	(750)	—
Long-term debt, net	\$13,513	\$14,282

Revolving Credit Facilities

On October 9, 2015, we entered into a \$2.5 billion revolving credit facility (the 5-year Facility) with various banks. The 5 year Facility was amended in October 2017 to extend its expiration date by one year from October 9, 2021 to October 9, 2022. The 5 year Facility is available for general corporate purposes. The undrawn portion of the 5-year Facility is also available to serve as a backup facility for the issuance of commercial paper. We may request and the banks may grant, at their discretion, an increase in the borrowing capacity under the 5-year Facility of up to an additional \$500 million. There were no borrowings outstanding under the 5-year Facility as of December 31, 2017 and 2016.

Borrowings under the 5-year Facility are unsecured and bear interest at rates based, at our option, on a Eurodollar Rate or a Base Rate, as defined in the 5-year Facility's agreement. Each bank's obligation to make loans under the 5-year Facility is subject to, among other things, our compliance with various representations, warranties, and covenants, including covenants limiting our ability and certain of our subsidiaries' ability to encumber assets and a covenant not to exceed a maximum leverage ratio, as defined in the 5 year Facility agreement. As of December 31, 2017 and 2016, we were in compliance with all covenants contained in the 5-year Facility agreement, as well as in our debt agreements.

Long-Term Debt

In September 2017, we issued notes totaling approximately \$1.6 billion with a fixed interest rate of 4.09% maturing in September 2052 (the New Notes) in exchange for outstanding notes totaling approximately \$1.4 billion with fixed interest rates ranging from 4.70% to 8.50% maturing 2029 to 2046 (the Old Notes). In connection with the exchange of principal, we paid a premium of \$237 million, substantially all of which was in the form of New Notes. This premium will be amortized as additional interest expense over the term of the New Notes using the effective interest method. We may, at our option, redeem some or all of the New Notes at any time by paying the principal amount of notes being redeemed plus a make-whole premium and accrued and unpaid interest. Interest on the New Notes is payable on March 15 and September 15 of each year, beginning on March 15, 2018. The New Notes are unsecured senior obligations and rank equally in right of payment with all of our existing and future unsecured and

unsubordinated indebtedness.

31

We made interest payments of approximately \$610 million, \$600 million and \$375 million during the years ended December 31, 2017, 2016 and 2015, respectively.

In September 2016, we repaid \$500 million of long-term notes with a fixed interest rate of 2.13% according to their scheduled maturities. In May 2016, we repaid \$452 million of long-term notes with a fixed interest rate of 7.65% according to their scheduled maturities. We also had related variable interest rate swaps with a notional amount of \$450 million mature, which did not have a significant impact on net earnings or comprehensive income.

Commercial Paper

We have agreements in place with financial institutions to provide for the issuance of commercial paper backed by our \$2.5 billion 5-year Facility. During 2017 and 2016, we borrowed and fully repaid amounts under our commercial paper programs. There were no commercial paper borrowings outstanding as of December 31, 2017 and 2016.

However, we may as conditions warrant issue commercial paper backed by our credit facility to manage the timing of cash flows and to fund a portion of our defined benefit pension contributions of approximately \$5.0 billion in 2018.

Note 11 – Postretirement Benefit Plans

Defined Benefit Pension Plans and Retiree Medical and Life Insurance Plans

Many of our employees are covered by qualified defined benefit pension plans and we provide certain health care and life insurance benefits to eligible retirees (collectively, postretirement benefit plans). We also sponsor nonqualified defined benefit pension plans to provide for benefits in excess of qualified plan limits. Non-union employees hired after December 2005 do not participate in our qualified defined benefit pension plans, but are eligible to participate in a qualified defined contribution plan in addition to our other retirement savings plans. They also have the ability to participate in our retiree medical plans, but we do not subsidize the cost of their participation in those plans as we do with employees hired before January 1, 2006. Over the last few years, we have negotiated similar changes with various labor organizations such that new union represented employees do not participate in our defined benefit pension plans. In June 2014, we amended certain of our qualified and nonqualified defined benefit pension plans for non-union employees; comprising the majority of our benefit obligations; to freeze future retirement benefits. The calculation of retirement benefits under the affected defined benefit pension plans is determined by a formula that takes into account the participants' years of credited service and average compensation. The freeze will take effect in two stages. On January 1, 2016, the pay-based component of the formula used to determine retirement benefits was frozen so that future pay increases, annual incentive bonuses or other amounts earned for or related to periods after December 31, 2015 are not used to calculate retirement benefits. On January 1, 2020, the service-based component of the formula used to determine retirement benefits will also be frozen so that participants will no longer earn further credited service for any period after December 31, 2019. When the freeze is complete, the majority of our salaried employees will have transitioned to an enhanced defined contribution retirement savings plan. As part of the November 6, 2015 acquisition of Sikorsky, we established a new defined benefit pension plan for Sikorsky's union workforce that provides benefits for their prospective service with us. The Sikorsky salaried employees participate in a defined contribution plan. We did not assume any legacy pension liability from UTC.

We have made contributions to trusts established to pay future benefits to eligible retirees and dependents, including Voluntary Employees' Beneficiary Association trusts and 401(h) accounts, the assets of which will be used to pay expenses of certain retiree medical plans. We use December 31 as the measurement date. Benefit obligations as of the end of each year reflect assumptions in effect as of those dates. Net periodic benefit cost is based on assumptions in effect at the end of the respective preceding year.

The rules related to accounting for postretirement benefit plans under GAAP require us to recognize on a plan-by-plan basis the funded status of our postretirement benefit plans as either an asset or a liability on our consolidated balance sheets. The funded status is measured as the difference between the fair value of the plan's assets and the benefit obligation of the plan.

The net periodic benefit cost recognized each year included the following (in millions):

	Qualified Defined Benefit Pension Plans ^(a)			Retiree Medical and Life Insurance Plans		
	2017	2016	2015	2017	2016	2015
Service cost	\$820	\$827	\$836	\$20	\$24	\$21
Interest cost	1,809	1,861	1,791	102	119	110
Expected return on plan assets	(2,408)	(2,666)	(2,734)	(128)	(138)	(147)
Recognized net actuarial losses	1,506	1,359	1,599	19	34	43
Amortization of net prior service (credit) cost ^(b)	(355)	(362)	(365)	15	22	4
Total net periodic benefit cost	\$1,372	\$1,019	\$1,127	\$28	\$61	\$31

Total net periodic benefit cost associated with our qualified defined benefit plans represents pension expense calculated in accordance with GAAP (FAS pension expense). We are required to calculate pension expense in accordance with both GAAP and CAS rules, each of which results in a different calculated amount of pension expense. The CAS pension cost is recovered through the pricing of our products and services on U.S. Government contracts and, therefore, is recognized in net sales and cost of sales for products and services. We include the ^(a) difference between FAS pension expense and CAS pension cost, referred to as the FAS/CAS pension adjustment, as a component of other unallocated, net on our consolidated statements of earnings. The FAS/CAS pension adjustment, which was \$876 million in 2017, \$902 million in 2016, and \$400 million in 2015, effectively adjusts the amount of CAS pension cost in the business segment operating profit so that pension expense recorded on our consolidated statements of earnings is equal to FAS pension expense. FAS pension expense and CAS pension costs reflect the reclassification for discontinued operations presentation of benefits related to former IS&GS salaried employees.

^(b) Net of the reclassification for discontinued operations presentation of pension benefits related to former IS&GS salaried employees (\$14 million in 2016 and \$24 million in 2015).

The following table provides a reconciliation of benefit obligations, plan assets and unfunded status related to our qualified defined benefit pension plans and our retiree medical and life insurance plans (in millions):

	Qualified Defined Benefit Pension Plans		Retiree Medical and Life Insurance Plans	
	2017	2016	2017	2016
Change in benefit obligation				
Beginning balance	\$45,064	\$43,702	\$2,649	\$2,883
Service cost	820	827	20	24
Interest cost	1,809	1,861	102	119
Benefits paid	(2,310)	(2,172)	(232)	(222)
Actuarial losses (gains)	3,377	1,402	23	(135)
Changes in longevity assumptions ^(a)	(352)	(687)	(24)	(53)
Plan amendments and acquisitions ^(b)	278	110	—	(32)
Service cost related to discontinued operations	—	21	—	—
Medicare Part D subsidy	—	—	—	4
Participants' contributions	—	—	64	61
Ending balance	\$48,686	\$45,064	\$2,602	\$2,649
Change in plan assets				
Beginning balance at fair value	\$31,417	\$32,096	\$1,787	\$1,813
Actual return on plan assets	3,942	1,470	224	95
Benefits paid	(2,310)	(2,172)	(232)	(222)
Company contributions	46	23	40	36
Medicare Part D subsidy	—	—	—	4

Participants' contributions	—	—	64	61
Ending balance at fair value	\$33,095	\$31,417	\$ 1,883	\$ 1,787
Unfunded status of the plans	\$(15,591)	\$(13,647)	\$(719)	\$(862)

(a) As published by the Society of Actuaries.

(b) Includes special termination benefits of \$27 million for qualified pension, and \$9 million for retiree medical, recognized in 2016 related to former IS&GS salaried employees.

The following table provides amounts recognized on our consolidated balance sheets related to our qualified defined benefit pension plans and our retiree medical and life insurance plans (in millions):

	Qualified Defined Benefit Pension Plans		Retiree Medical and Life Insurance Plans	
	2017	2016	2017	2016
Prepaid pension asset	\$112	\$208	\$ —	\$ —
Accrued postretirement benefit liabilities	(15,703)	(13,855)	(719)	(862)
Accumulated other comprehensive loss (pre-tax) related to:				
Net actuarial losses	20,169	20,184	331	447
Prior service (credit) cost ^(a)	(2,263)	(2,896)	81	96
Total ^(b)	\$17,906	\$17,288	\$ 412	\$ 543

During 2016 pre-tax amounts of \$210 million for qualified pension prior service credits and \$9 million for retiree ^(a) medical prior service costs were recognized from the divestiture of our IS&GS business (combined \$134 million, net of tax).

Accumulated other comprehensive loss related to postretirement benefit plans, after tax, of \$12.6 billion and \$12.0 billion at December 31, 2017 and 2016 (see “Note 12 – Stockholders’ Equity”) includes \$17.9 billion (\$11.8 ^(b) billion, net of tax) and \$17.3 billion (\$11.2 billion, net of tax) for qualified defined benefit pension plans, \$412 million (\$252 million, net of tax) and \$543 million (\$351 million, net of tax) for retiree medical and life insurance plans and \$705 million (\$479 million, net of tax) and \$677 million (\$448 million, net of tax) for other plans.

The accumulated benefit obligation (ABO) for all qualified defined benefit pension plans was \$48.5 billion and \$44.9 billion at December 31, 2017 and 2016, of which \$48.5 billion and \$44.8 billion related to plans where the ABO was in excess of plan assets. The ABO represents benefits accrued without assuming future compensation increases to plan participants. Certain key information related to our qualified defined benefit pension plans as of December 31, 2017 and 2016 is as follows (in millions):

	2017	2016
Plans where ABO was in excess of plan assets		
Projected benefit obligation	\$48,628	\$44,946
Less: fair value of plan assets	32,925	31,091
Unfunded status of plans ^(a)	(15,703)	(13,855)
Plans where ABO was less than plan assets		
Projected benefit obligation	58	118
Less: fair value of plan assets	170	326
Funded status of plans ^(b)	\$112	\$208

^(a) Represents accrued pension liabilities, which are included on our consolidated balance sheets.

^(b) Represents prepaid pension assets, which are included on our consolidated balance sheets in other noncurrent assets.

We also sponsor nonqualified defined benefit plans to provide benefits in excess of qualified plan limits. The aggregate liabilities for these plans at December 31, 2017 and 2016 were \$1.3 billion and \$1.2 billion, which also represent the plans’ unfunded status. We have set aside certain assets totaling \$530 million and \$460 million as of December 31, 2017 and 2016 in a separate trust which we expect to be used to pay obligations under our nonqualified defined benefit plans. In accordance with GAAP, those assets may not be used to offset the amount of the benefit obligation similar to the postretirement benefit plans in the table above. The unrecognized net actuarial losses at December 31, 2017 and 2016 were \$646 million and \$642 million. The unrecognized prior service credit at December 31, 2017 and 2016 were \$61 million and \$74 million. The expense associated with these plans totaled \$126 million in 2017, \$125 million in 2016 and \$117 million in 2015. We also sponsor a small number of other postemployment plans and foreign benefit plans. The aggregate liability for the other postemployment plans was \$60 million and \$63 million as of December 31, 2017 and 2016. The expense for the other postemployment plans, as well as the liability and expense associated with the foreign benefit plans, was not material to our results of operations, financial position or cash flows. The actuarial assumptions used to determine the benefit obligations and expense

associated with our nonqualified defined benefit plans and postemployment plans are similar to those assumptions used to determine the benefit obligations and expense related to our qualified defined benefit pension plans and retiree medical and life insurance plans as described below.

The following table provides the amounts recognized in other comprehensive income (loss) related to postretirement benefit plans, net of tax, for the years ended December 31, 2017, 2016 and 2015 (in millions):

	Incurred but Not Yet Recognized in Net Periodic Benefit Cost			Recognition of Previously Deferred Amounts		
	2017	2016	2015	2017	2016	2015
	Gains (losses)			(Gains) losses		
Actuarial gains and losses						
Qualified defined benefit pension plans	\$(1,172)	\$(1,236)	\$(291)	\$974	\$879	\$1,034
Retiree medical and life insurance plans	77	94	46	12	22	28
Other plans	(66)	(62)	21	44	37	47
	(1,161)	(1,204)	(224)	1,030	938	1,109
	Credit (cost)			(Credit) cost ^(a)		
Net prior service credit and cost						
Qualified defined benefit pension plans	(219)	(54)	(18)	(229)	(235)	(235)
Retiree medical and life insurance plans	—	27	(102)	10	14	2
Other plans	—	(1)	(7)	(9)	(9)	(10)
	(219)	(28)	(127)	(228)	(230)	(243)
	\$(1,380)	\$(1,232)	\$(351)	\$802	\$708	\$866

Reflects the reclassification for discontinued operations presentation of benefits related to former IS&GS salaried ^(a) employees (\$9 million in 2016 and \$16 million in 2015). In addition, we recognized \$134 million in 2016 of prior service credits from the divestiture of our IS&GS business, which were reclassified as discontinued operations.

We expect that approximately \$1.5 billion, or about \$1.2 billion net of tax, of actuarial losses and net prior service credit related to postretirement benefit plans included in accumulated other comprehensive loss at the end of 2017 to be recognized in net periodic benefit cost during 2018. Of this amount, \$1.4 billion, or \$1.1 billion net of tax, relates to our qualified defined benefit plans and is included in our expected 2018 pension expense of \$1.4 billion.

Actuarial Assumptions

The actuarial assumptions used to determine the benefit obligations at December 31 of each year and to determine the net periodic benefit cost for each subsequent year, were as follows:

	Qualified Defined Benefit Pension Plans			Retiree Medical and Life Insurance Plans		
	2017	2016	2015	2017	2016	2015
Weighted average discount rate	3.625 %	4.125 %	4.375 %	3.625 %	4.000 %	4.250 %
Expected long-term rate of return on assets	7.50 %	7.50 %	8.00 %	7.50 %	7.50 %	8.00 %
Rate of increase in future compensation levels (for applicable bargained pension plans)	4.50 %	4.50 %	4.50 %			
Health care trend rate assumed for next year				8.50 %	8.75 %	9.00 %
Ultimate health care trend rate				5.00 %	5.00 %	5.00 %
Year that the ultimate health care trend rate is reached				2032	2032	2032

The decrease in the discount rate from December 31, 2016 to December 31, 2017 resulted in an increase in the projected benefit obligations of our qualified defined benefit pension plans of approximately \$2.9 billion at December 31, 2017. The decrease in the discount rate from December 31, 2015 to December 31, 2016 resulted in an increase in the projected benefit obligations of our qualified defined benefit pension plans of approximately \$1.4 billion at December 31, 2016.

The long-term rate of return assumption represents the expected long-term rate of earnings on the funds invested, or to be invested, to provide for the benefits included in the benefit obligations. That assumption is based on several factors including historical market index returns, the anticipated long-term allocation of plan assets, the historical return data for the trust funds, plan expenses and the potential to outperform market index returns.

Plan Assets

Investment policies and strategies – Lockheed Martin Investment Management Company (LMIMCo), our wholly-owned subsidiary, has the fiduciary responsibility for making investment decisions related to the assets of our postretirement benefit plans. LMIMCo’s investment objectives for the assets of these plans are (1) to minimize the net present value of expected funding contributions; (2) to ensure there is a high probability that each plan meets or exceeds our actuarial long-term rate of return assumptions; and (3) to diversify assets to minimize the risk of large losses. The nature and duration of benefit obligations, along with assumptions concerning asset class returns and return correlations, are considered when determining an appropriate asset allocation to achieve the investment objectives. Investment policies and strategies governing the assets of the plans are designed to achieve investment objectives within prudent risk parameters. Risk management practices include the use of external investment managers; the maintenance of a portfolio diversified by asset class, investment approach and security holdings; and the maintenance of sufficient liquidity to meet benefit obligations as they come due.

LMIMCo’s investment policies require that asset allocations of postretirement benefit plans be maintained within the following approximate ranges:

Asset Class	Asset Allocation Ranges
Cash and cash equivalents	0-20%
Equity	15-65%
Fixed income	10-60%
Alternative investments:	
Private equity funds	0-15%
Real estate funds	0-10%
Hedge funds	0-20%
Commodities	0-15%

Fair value measurements – The rules related to accounting for postretirement benefit plans under GAAP require certain fair value disclosures related to postretirement benefit plan assets, even though those assets are not separately presented on our consolidated balance sheets. The following table presents the fair value of the assets (in millions) of our qualified defined benefit pension plans and retiree medical and life insurance plans by asset category and their level within the fair value hierarchy, which has three levels based on the reliability of the inputs used to determine fair value. Level 1 refers to fair values determined based on quoted prices in active markets for identical assets, Level 2 refers to fair values estimated using significant other observable inputs and Level 3 includes fair values estimated using significant unobservable inputs. Certain other investments are measured at their Net Asset Value (NAV) per share and do not have readily determined values and are thus not subject to leveling in the fair value hierarchy. The NAV is the total value of the fund divided by the number of the fund's shares outstanding. We recognize transfers between levels of the fair value hierarchy as of the date of the change in circumstances that causes the transfer. We did not have any transfers of assets between Level 1 and Level 2 of the fair value hierarchy during 2017.

	December 31, 2017				December 31, 2016			
	Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
Investments measured at fair value								
Cash and cash equivalents ^(a)	\$1,419	\$1,419	\$—	\$ —	\$2,301	\$2,301	\$—	\$ —
Equity ^(a) :								
U.S. equity securities	4,922	4,905	14	3	4,166	4,139	23	4
International equity securities	5,370	5,355	13	2	3,971	3,927	40	4
Commingled equity funds	4,453	1,493	2,960	—	2,332	788	1,544	—
Fixed income ^(a) :								
Corporate debt securities	4,910	—	4,905	5	4,333	—	4,316	17
U.S. Government securities	3,775	—	3,775	—	6,811	—	6,811	—
U.S. Government-sponsored enterprise securities	817	—	817	—	919	—	919	—
Other fixed income investments	2,412	—	2,401	11	2,215	—	2,214	1
Alternative investments:								
Hedge funds	7	—	7	—	33	—	33	—
Commodities ^(a)	2	1	1	—	523	525	(2)	—
Total	\$28,087	\$13,173	\$14,893	\$ 21	\$27,604	\$11,680	\$15,898	\$ 26
Investments measured at NAV ^(b)								
Commingled equity funds	99				60			
Other fixed income investments	68				—			
Private equity funds	4,334				3,614			
Real estate funds	1,611				1,411			
Hedge funds	711				462			
Total investments measured at NAV	6,823				5,547			
Receivables, net	68				53			
Total	\$34,978				\$33,204			

Cash and cash equivalents, equity securities, fixed income securities and commodities included derivative assets and liabilities whose fair values were not material as of December 31, 2017 and 2016. LMIMCo's investment ^(a) policies restrict the use of derivatives to either establish long exposures for purposes of expediency or capital efficiency or to hedge risks to the extent of a plan's current exposure to such risks. Most derivative transactions are settled on a daily basis.

Certain investments that are valued using the net asset value per share (or its equivalent) as a practical expedient ^(b) have not been classified in the fair value hierarchy and are included in the table to permit reconciliation of the fair value hierarchy to the aggregate postretirement benefit plan assets.

As of December 31, 2017 and 2016, the assets associated with our foreign defined benefit pension plans were not material and have not been included in the table above. The changes during 2017 and 2016 in the fair value of plan assets categorized as Level 3 were insignificant.

Valuation techniques – Cash equivalents are mostly comprised of short-term money-market instruments and are valued at cost, which approximates fair value.

U.S. equity securities and international equity securities categorized as Level 1 are traded on active national and international exchanges and are valued at their closing prices on the last trading day of the year. For U.S. equity securities and international equity securities not traded on an active exchange, or if the closing price is not available, the trustee obtains indicative quotes from a pricing vendor, broker or investment manager. These securities are categorized as Level 2 if the custodian obtains corroborated quotes from a pricing vendor or categorized as Level 3 if the custodian obtains uncorroborated quotes from a broker or investment manager.

Commingled equity funds categorized as Level 1 are traded on active national and international exchanges and are valued at their closing prices on the last trading day of the year. For commingled equity funds not traded on an active exchange, or if the closing price is not available, the trustee obtains indicative quotes from a pricing vendor, broker or investment manager. These securities are categorized as Level 2 if the custodian obtains corroborated quotes from a pricing vendor.

Fixed income investments categorized as Level 2 are valued by the trustee using pricing models that use verifiable observable market data (e.g., interest rates and yield curves observable at commonly quoted intervals and credit spreads), bids provided by brokers or dealers or quoted prices of securities with similar characteristics. Fixed income investments are categorized at Level 3 when valuations using observable inputs are unavailable. The trustee obtains pricing based on indicative quotes or bid evaluations from vendors, brokers or the investment manager.

Commodities are traded on an active commodity exchange and are valued at their closing prices on the last trading day of the year.

Certain commingled equity funds, consisting of equity mutual funds, are valued using the NAV. The NAV valuations are based on the underlying investments and typically redeemable within 90 days.

Private equity funds consist of partnership and co-investment funds. The NAV is based on valuation models of the underlying securities, which includes unobservable inputs that cannot be corroborated using verifiable observable market data. These funds typically have redemption periods between eight and 12 years.

Real estate funds consist of partnerships, most of which are closed-end funds, for which the NAV is based on valuation models and periodic appraisals. These funds typically have redemption periods between eight and 10 years. Hedge funds consist of direct hedge funds for which the NAV is generally based on the valuation of the underlying investments. Redemptions in hedge funds are based on the specific terms of each fund, and generally range from a minimum of one month to several months.

Contributions and Expected Benefit Payments

The funding of our qualified defined benefit pension plans is determined in accordance with ERISA, as amended by the PPA, and in a manner consistent with CAS and Internal Revenue Code rules. There were no material contributions to our qualified defined benefit pension plans during 2017. We will make contributions of \$5.0 billion to our qualified defined benefit pension plans in 2018, including required and discretionary contributions. As a result of these contributions, we do not expect any material qualified defined benefit cash funding will be required until 2021. We plan to fund these contributions using a mix of cash on hand and commercial paper. While we do not anticipate a need to do so, our capital structure and resources would allow us to issue new debt if circumstances change.

The following table presents estimated future benefit payments, which reflect expected future employee service, as of December 31, 2017 (in millions):

	2018	2019	2020	2021	2022	2023 – 2027
Qualified defined benefit pension plans	\$2,450	\$2,480	\$2,560	\$2,630	\$2,700	\$ 14,200
Retiree medical and life insurance plans	180	180	180	180	180	820

Defined Contribution Plans

We maintain a number of defined contribution plans, most with 401(k) features, that cover substantially all of our employees. Under the provisions of our 401(k) plans, we match most employees' eligible contributions at rates specified in the plan documents. Our contributions were \$613 million in 2017, \$617 million in 2016 and \$393 million in 2015, the majority of which were funded using our common stock. Our defined contribution plans held approximately 35.5 million and 36.9 million shares of our common stock as of December 31, 2017 and 2016.

Note 12 – Stockholders' Equity

At December 31, 2017 and 2016, our authorized capital was composed of 1.5 billion shares of common stock and 50 million shares of series preferred stock. Of the 285 million shares of common stock issued and outstanding as of December 31, 2017, 284 million shares were considered outstanding for consolidated balance sheet presentation purposes; the remaining shares were held in a separate trust. Of the 290 million shares of common stock issued and outstanding as of December 31, 2016, 289 million shares were considered outstanding for consolidated balance sheet presentation purposes; the remaining shares were held in a separate trust. No shares of preferred stock were issued and outstanding at December 31, 2017 or 2016.

Repurchases of Common Stock

During 2017, we repurchased 7.1 million shares of our common stock for \$2.0 billion. During 2016 and 2015, we paid \$2.1 billion and \$3.1 billion to repurchase 8.9 million and 15.2 million shares of our common stock.

On September 28, 2017, our Board of Directors approved a \$2.0 billion increase to our share repurchase program. Inclusive of this increase, the total remaining authorization for future common share repurchases under our program was \$3.5 billion as of December 31, 2017. As we repurchase our common shares, we reduce common stock for the \$1 of par value of the shares repurchased, with the excess purchase price over par value recorded as a reduction of additional paid-in capital. If additional paid-in capital is reduced to zero, we record the remainder of the excess purchase price over par value as a reduction of retained earnings. Due to the volume of repurchases made under our share repurchase program, additional paid-in capital was reduced to zero, with the remainder of the excess purchase price over par value of \$1.6 billion and \$1.7 billion recorded as a reduction of retained earnings in 2017 and 2016.

Dividends

We paid dividends totaling \$2.2 billion (\$7.46 per share) in 2017, \$2.0 billion (\$6.77 per share) in 2016 and \$1.9 billion (\$6.15 per share) in 2015. We paid quarterly dividends of \$1.82 per share during each of the first three quarters of 2017 and \$2.00 per share during the fourth quarter of 2017; \$1.65 per share during each of the first three quarters of 2016 and \$1.82 per share during the fourth quarter of 2016; and \$1.50 per share during each of the first three quarters of 2015 and \$1.65 per share during the fourth quarter of 2015.

Accumulated Other Comprehensive Loss

Changes in the balance of AOCL, net of income taxes, consisted of the following (in millions):

	Postretirement Benefit Plans (a)	Other, net	AOCL
Balance at December 31, 2014	\$ (11,813)	\$ (57)	\$ (11,870)
Other comprehensive loss before reclassifications	(351)	(73)	(424)
Amounts reclassified from AOCL			
Recognition of net actuarial losses	1,109	—	1,109
Amortization of net prior service credits	(259)	—	(259)
Total reclassified from AOCL	850	—	850
Total other comprehensive income (loss)	499	(73)	426
Balance at December 31, 2015	(11,314)	(130)	(11,444)
Other comprehensive loss before reclassifications	(1,232)	—	(1,232)
Amounts reclassified from AOCL			
Recognition of net actuarial losses	938	—	938
Amortization of net prior service credits	(239)	—	(239)
Recognition of net prior service credits from divestiture of IS&GS segment (b)	(134)	—	(134)
Other	—	9	9
Total reclassified from AOCL	565	9	574
Total other comprehensive (loss) income	(667)	9	(658)
Balance at December 31, 2016	(11,981)	(121)	(12,102)
Other comprehensive (loss) income before reclassifications	(1,380)	120	(1,260)
Amounts reclassified from AOCL			
Recognition of net actuarial losses	1,030	—	1,030
Amortization of net prior service credits	(228)	—	(228)
Other	—	20	20
Total reclassified from AOCL	802	20	822
Total other comprehensive (loss) income	(578)	140	(438)
Balance at December 31, 2017	\$ (12,559)	\$ 19	\$ (12,540)

AOCL related to postretirement benefit plans is shown net of tax benefits of \$6.5 billion at both December 31, 2017 and 2016 and \$6.2 billion at December 31, 2015. These tax benefits include amounts recognized on our

(a) income tax returns as current deductions and deferred income taxes, which will be recognized on our tax returns in future years. See “Note 9 – Income Taxes” and “Note 11 – Postretirement Benefit Plans” for more information on our income taxes and postretirement benefit plans.

(b) Associated with the 2016 divestiture of the IS&GS business and included in net gain on divestiture of discontinued operations.

Note 13 – Stock-Based Compensation

During 2017, 2016 and 2015, we recorded non-cash stock-based compensation expense totaling \$158 million, \$149 million and \$133 million, which is included as a component of other unallocated, net on our consolidated statements of earnings. The net impact to earnings for the respective years was \$103 million, \$97 million and \$86 million.

As of December 31, 2017, we had \$91 million of unrecognized compensation cost related to nonvested awards, which is expected to be recognized over a weighted average period of 1.7 years. We received cash from the exercise of stock options totaling \$71 million, \$106 million and \$174 million during 2017, 2016 and 2015. In addition, our income tax liabilities for 2017, 2016 and 2015 were reduced by \$203 million, \$219 million and \$213 million due to recognized tax benefits on stock-based compensation arrangements.

Stock-Based Compensation Plans

Under plans approved by our stockholders, we are authorized to grant key employees stock-based incentive awards, including options to purchase common stock, stock appreciation rights, RSUs, PSUs or other stock units. The exercise price of options to purchase common stock may not be less than the fair market value of our stock on the date of grant. No award of stock options may become fully vested prior to the third anniversary of the grant and no portion of a stock option grant may become vested in less than one year. The minimum vesting period for restricted stock or stock units payable in stock is three years. Award agreements may provide for shorter or pro-rated vesting periods or vesting following termination of employment in the case of death, disability, divestiture, retirement, change of control or layoff. The maximum term of a stock option or any other award is 10 years.

At December 31, 2017, inclusive of the shares reserved for outstanding stock options, RSUs and PSUs, we had approximately 10 million shares reserved for issuance under the plans. At December 31, 2017, approximately six million of the shares reserved for issuance remained available for grant under our stock-based compensation plans. We issue new shares upon the exercise of stock options or when restrictions on RSUs and PSUs have been satisfied.

RSUs

The following table summarizes activity related to nonvested RSUs:

	Number of RSUs (In thousands)	Weighted Average Grant-Date Fair Value Per Share
Nonvested at December 31, 2014	2,326	\$ 97.80
Granted	595	192.47
Vested	(1,642)	103.30
Forfeited	(43)	132.28
Nonvested at December 31, 2015	1,236	\$ 134.87
Granted	679	206.69
Vested	(1,009)	137.62
Forfeited	(118)	203.65
Nonvested at December 31, 2016	788	\$ 183.00
Granted	519	254.58
Vested	(624)	201.65
Forfeited	(32)	223.23
Nonvested at December 31, 2017	651	\$ 220.21

In 2017, we granted certain employees approximately 0.5 million RSUs with a weighted average grant-date fair value of \$254.58 per RSU. The grant-date fair value of these RSUs is equal to the closing market price of our common stock on the grant date less a discount to reflect the delay in payment of dividend-equivalent cash payments that are made only upon vesting, which is generally three years from the grant date. We recognize the grant-date fair value of RSUs, less estimated forfeitures, as compensation expense ratably over the requisite service period, which is shorter than the vesting period if the employee is retirement eligible on the date of grant or will become retirement eligible before the end of the vesting period.

Stock Options

We generally recognize compensation cost for stock options ratably over the three-year vesting period. At December 31, 2017 and 2016, there were 2.2 million (weighted average exercise price of \$82.71) and 3.0 million (weighted average exercise price of \$85.82) stock options outstanding. All of the stock options outstanding are vested as of December 31, 2017 and have a weighted average remaining contractual life of approximately 2.5 years and an aggregate intrinsic value of \$533 million. There were 0.8 million (weighted average exercise price of \$95.06) stock options exercised during 2017. We have not granted stock options to employees since 2012.

The following table pertains to stock options granted through 2012, in addition to stock options that vested and were exercised in 2017, 2016 and 2015 (in millions):

	2017	2016	2015
Grant-date fair value of all stock options that vested	\$ —	\$ —	\$ 8
Intrinsic value of all stock options exercised	139	172	265

In 2012, we estimated the fair value for stock options at the date of grant using the Black-Scholes option pricing model, which required us to make certain assumptions. We used the following weighted average assumptions in the model: risk-free interest rate of 0.78%, dividend yield of 5.40%, a five year historical volatility factor of 0.28 and an expected option life of five years.

PSUs

In 2017, we granted certain employees PSUs with an aggregate target award of approximately 0.1 million shares of our common stock. The PSUs vest three years from the grant date based on continuous service, with the number of shares earned (0% to 200% of the target award) depending upon the extent to which we achieve certain financial and market performance targets measured over the period from January 1, 2017 through December 31, 2019. About half of the PSUs were valued at \$254.53 per PSU in a manner similar to RSUs mentioned above as the financial targets are based on our operating results. We recognize the grant-date fair value of these PSUs, less estimated forfeitures, as compensation expense ratably over the vesting period based on the number of awards expected to vest at each reporting date. The remaining PSUs were valued at \$266.44 per PSU using a Monte Carlo model as the performance target is related to our total shareholder return relative to our peer group. We recognize the grant-date fair value of these awards, less estimated forfeitures, as compensation expense ratably over the vesting period.

Note 14 – Legal Proceedings, Commitments and Contingencies

We are a party to or have property subject to litigation and other proceedings that arise in the ordinary course of our business, including matters arising under provisions relating to the protection of the environment and are subject to contingencies related to certain businesses we previously owned. These types of matters could result in fines, penalties, compensatory or treble damages or non-monetary sanctions or relief. We believe the probability is remote that the outcome of each of these matters, including the legal proceedings described below, will have a material adverse effect on the corporation as a whole, notwithstanding that the unfavorable resolution of any matter may have a material effect on our net earnings in any particular interim reporting period. Among the factors that we consider in this assessment are the nature of existing legal proceedings and claims, the asserted or possible damages or loss contingency (if estimable), the progress of the case, existing law and precedent, the opinions or views of legal counsel and other advisers, our experience in similar cases and the experience of other companies, the facts available to us at the time of assessment and how we intend to respond to the proceeding or claim. Our assessment of these factors may change over time as individual proceedings or claims progress.

Although we cannot predict the outcome of legal or other proceedings with certainty, where there is at least a reasonable possibility that a loss may have been incurred, GAAP requires us to disclose an estimate of the reasonably possible loss or range of loss or make a statement that such an estimate cannot be made. We follow a thorough process in which we seek to estimate the reasonably possible loss or range of loss, and only if we are unable to make such an estimate do we conclude and disclose that an estimate cannot be made. Accordingly, unless otherwise indicated below in our discussion of legal proceedings, a reasonably possible loss or range of loss associated with any individual legal proceeding cannot be estimated.

Legal Proceedings

As a result of our acquisition of Sikorsky, we assumed the defense of and any potential liability for two civil False Claims Act lawsuits pending in the U.S. District Court for the Eastern District of Wisconsin. In October 2014, the

U.S. Government filed a complaint in intervention in the first suit, which was brought by qui tam relator Mary Patzer, a former Derco Aerospace (Derco) employee. In May 2017, the U.S. Government filed a complaint in intervention in the second suit, which was brought by qui tam

relator Peter Cimma, a former Sikorsky Support Services, Inc. (SSSI) employee. In November 2017, the Court consolidated the cases into a single action for discovery and trial.

The U.S. Government alleges that Sikorsky and two of its wholly-owned subsidiaries, Derco and SSSI, violated the civil False Claims Act, the Anti-Kickback Act, and the Truth in Negotiations Act in connection with a contract the U.S. Navy awarded to SSSI in June 2006 to support the Navy's T-34 and T-44 fixed-wing turboprop training aircraft. SSSI subcontracted with Derco, primarily to procure and manage spare parts for the training aircraft. The U.S. Government alleges that SSSI overbilled the Navy on the contract as the result of Derco's use of prohibited cost-plus-percentage-of-cost pricing to add profit and overhead costs as a percentage of the price of the spare parts that Derco procured and then sold to SSSI. The U.S. Government alleges that Derco's claims to SSSI, SSSI's claims to the Navy, and SSSI's yearly Certificates of Final Indirect Costs from 2006 through 2012 were false. In addition to violations of the False Claims Act, the U.S. Government alleges violations of the Anti-Kickback Act based on a monthly "chargeback," through which SSSI billed Derco for the cost of certain SSSI personnel, allegedly in exchange for SSSI's permitting a pricing arrangement that was "highly favorable" to Derco. The U.S. Government also claims that SSSI submitted inaccurate cost or pricing data in violation of the Truth in Negotiations Act for a sole-sourced, follow-on "bridge" contract. The U.S. Government's complaints assert common law claims for breach of contract and unjust enrichment. On January 12, 2018, the Corporation filed a partial motion to dismiss intended to narrow the Government's claims. The Corporation also moved to dismiss Cimma as a party under the False Claims Act's first-to-file rule, which permits only the first relator to recover in a pending case.

The U.S. Government currently seeks damages in these lawsuits of approximately \$52 million, subject to trebling, plus statutory penalties. We believe that we have legal and factual defenses to the U.S. Government's claims. Although we continue to evaluate our liability and exposure, we do not currently believe that it is probable that we will incur a material loss. If, contrary to our expectations, the U.S. Government prevails in this matter and proves damages at or near \$52 million and is successful in having such damages trebled, the outcome could have an adverse effect on our results of operations in the period in which a liability is recognized and on our cash flows for the period in which any damages are paid.

On April 24, 2009, we filed a declaratory judgment action against the MTA asking the U.S. District Court for the Southern District of New York to find that the MTA is in material breach of our agreement based on the MTA's failure to provide access to sites where work must be performed and the customer-furnished equipment necessary to complete the contract. The MTA filed an answer and counterclaim alleging that we breached the contract and subsequently terminated the contract for alleged default. The primary damages sought by the MTA are the cost to complete the contract and potential re-procurement costs. While we are unable to estimate the cost of another contractor to complete the contract and the costs of re-procurement, we note that our contract with the MTA had a total value of \$323 million, of which \$241 million was paid to us, and that the MTA is seeking damages of approximately \$190 million. We dispute the MTA's allegations and are defending against them. Additionally, following an investigation, our sureties on a performance bond related to this matter, who were represented by independent counsel, concluded that the MTA's termination of the contract was improper. Finally, our declaratory judgment action was later amended to include claims for monetary damages against the MTA of approximately \$95 million. This matter was taken under submission by the District Court in December 2014, after a five-week bench trial and the filing of post-trial pleadings by the parties. We continue to await a decision from the District Court. Although this matter relates to our former IS&GS business, we retained the litigation when we divested IS&GS.

Environmental Matters

We are involved in proceedings and potential proceedings relating to soil, sediment, surface water and groundwater contamination, disposal of hazardous waste and other environmental matters at several of our current or former facilities and at third-party sites where we have been designated as a potentially responsible party (PRP). A substantial portion of environmental costs will be included in our net sales and cost of sales in future periods pursuant to U.S. Government regulations. At the time a liability is recorded for future environmental costs, we record a receivable for estimated future recovery considered probable through the pricing of products and services to agencies of the U.S. Government, regardless of the contract form (e.g., cost-reimbursable, fixed-price). We continually evaluate the recoverability of our environmental receivables by assessing, among other factors, U.S. Government regulations, our U.S. Government business base and contract mix, our history of receiving reimbursement of such costs, and efforts by

some U.S. Government representatives to limit such reimbursement. We include the portion of those environmental costs expected to be allocated to our non-U.S. Government contracts, or that is determined not to be recoverable under U.S. Government contracts, in our cost of sales at the time the liability is established.

At December 31, 2017 and 2016, the aggregate amount of liabilities recorded relative to environmental matters was \$920 million and \$1.0 billion, most of which are recorded in other noncurrent liabilities on our consolidated balance sheets. We have recorded receivables totaling \$799 million and \$870 million at December 31, 2017 and 2016, most of which are recorded in other noncurrent assets on our consolidated balance sheets, for the estimated future recovery of these costs, as we consider the recovery probable based on the factors previously mentioned. We project costs and recovery of costs over approximately 20 years.

Environmental remediation activities usually span many years, which makes estimating liabilities a matter of judgment because of uncertainties with respect to assessing the extent of the contamination as well as such factors as changing remediation technologies and changing regulatory environmental standards. There are a number of former and present operating facilities that we are monitoring or investigating for potential future remediation. We perform quarterly reviews of the status of our environmental remediation sites and the related liabilities and receivables. Additionally, in our quarterly reviews, we consider these and other factors in estimating the timing and amount of any future costs that may be required for remediation activities and record a liability when it is probable that a loss has occurred and the loss can be reasonably estimated. The amount of liability recorded is based on our estimate of the costs to be incurred for remediation at a particular site. We do not discount the recorded liabilities, as the amount and timing of future cash payments are not fixed or cannot be reliably determined. We reasonably cannot determine the extent of our financial exposure in all cases as, although a loss may be probable or reasonably possible, in some cases it is not possible at this time to estimate the loss or reasonably possible loss or range of loss.

We also pursue claims for recovery of costs incurred or contribution to site cleanup costs against other PRPs, including the U.S. Government, and are conducting remediation activities under various consent decrees, orders, and agreements relating to soil, groundwater, sediment or surface water contamination at certain sites of former or current operations. Under agreements related to certain sites in California and New York, the U.S. Government reimburses us an amount equal to a percentage, specific to each site, of expenditures for certain remediation activities in the U.S. Government's capacity as a PRP under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA).

In addition to the proceedings and potential proceedings discussed above, California previously established a maximum level of the contaminant hexavalent chromium in drinking water of 10 parts per billion (ppb). Recently, this standard was successfully challenged by the California Manufacturers and Technology Association (CMTA) for failure to conduct the required economic feasibility analysis. In response to the court's ruling, the State Water Resources Control Board (State Board), a branch of the California Environmental Protection Agency, withdrew the hexavalent chromium standard from the published regulations, leaving only the 50 ppb standard for total chromium. The State Board has indicated it will work to re-establish a hexavalent chromium standard. If the standard for hexavalent chromium is re-established at 10 ppb or above, it will not have a material impact on our existing remediation costs in California. Further, the U.S. Environmental Protection Agency (U.S. EPA) is considering whether to regulate hexavalent chromium.

California is also reevaluating its existing drinking water standard of 6 ppb for perchlorate, and the U.S. EPA is taking steps to regulate perchlorate in drinking water. If substantially lower standards are adopted, in either California or at the federal level for perchlorate or for hexavalent chromium, we expect a material increase in our estimates for environmental liabilities and the related assets for the portion of the increased costs that are probable of future recovery in the pricing of our products and services for the U.S. Government. The amount that would be allocable to our non-U.S. Government contracts or that is determined not to be recoverable under U.S. Government contracts would be expensed, which may have a material effect on our earnings in any particular interim reporting period.

Operating Leases

We rent certain equipment and facilities under operating leases. Certain major plant facilities and equipment are furnished by the U.S. Government under short-term or cancelable arrangements. Our total rental expense under operating leases was \$169 million, \$202 million and \$195 million for 2017, 2016 and 2015. Future minimum lease commitments at December 31, 2017 for long-term non-cancelable operating leases were \$623 million (\$162 million in 2018, \$154 million in 2019, \$116 million in 2020, \$82 million in 2021, \$54 million in 2022 and \$55 million in later years).

Letters of Credit, Surety Bonds and Third-Party Guarantees

We have entered into standby letters of credit and surety bonds issued on our behalf by financial institutions and other directly issued guarantees to third parties primarily relating to advances received from customers and the guarantee of future performance on certain contracts. Letters of credit and surety bonds generally are available for draw down in the event we do not perform. In some cases, we may guarantee the contractual performance of third parties such as venture partners. We had total outstanding letters of credit, surety bonds and third-party guarantees aggregating \$3.3 billion at December 31, 2017 and \$3.7 billion at December 31, 2016. Third-party guarantees do not include guarantees

of subsidiaries and other consolidated entities.

At December 31, 2017 and 2016, third-party guarantees totaled \$750 million and \$709 million, of which approximately 62% and 56% related to guarantees of contractual performance of ventures to which we currently are or previously were a party. This amount represents our estimate of the maximum amount we would expect to incur upon the contractual non-performance of the venture, venture partners or divested businesses. Generally, we also have cross-indemnities in place that may enable us to recover amounts that may be paid on behalf of a venture partner.

In determining our exposures, we evaluate the reputation, performance on contractual obligations, technical capabilities and credit quality of our current and former venture partners and the transferee under novation agreements all of which include a guarantee as required by the FAR. There were no material amounts recorded in our financial statements related to third-party guarantees or novation agreements.

United Launch Alliance

In connection with our 50% ownership interest of ULA, we and The Boeing Company (Boeing) are required to provide ULA an additional capital contribution if ULA is unable to make required payments under its inventory supply agreement with Boeing. As of December 31, 2017, ULA's total remaining obligation to Boeing under the inventory supply agreement was \$120 million. The parties have agreed to defer the remaining payment obligation, as it is more than offset by other commitments to ULA. Accordingly, we do not expect to be required to make a capital contribution to ULA under this agreement.

In addition, both we and Boeing have cross-indemnified each other for guarantees by us and Boeing of the performance and financial obligations of ULA under certain launch service contracts. We believe ULA will be able to fully perform its obligations, as it has done through December 31, 2017, and that it will not be necessary to make payments under the cross-indemnities or guarantees.

Our share of ULA's net earnings are reported as equity in net earnings (losses) of equity investees in other income, net on our consolidated statements of earnings. Our investment in ULA totaled \$794 million and \$788 million at December 31, 2017 and 2016.

Note 15 – Restructuring Charges

2016 Actions

During 2016, we recorded severance charges totaling approximately \$80 million related to our Aeronautics business segment. The charges consisted of severance costs associated with the planned elimination of certain positions through either voluntary or involuntary actions. Upon separation, terminated employees receive lump-sum severance payments primarily based on years of service, the majority of which are expected to be paid over the next several quarters. As of the end of the first quarter of 2017, we had substantially paid the severance costs associated with these actions.

2015 Actions

During 2015, we recorded severance charges totaling \$82 million, of which \$67 million related to our RMS business segment and \$15 million related to businesses that were reported in our former IS&GS business prior to our fourth quarter 2015 program realignment. The charges consisted of severance costs associated with the planned elimination of certain positions through either voluntary or involuntary actions. Upon separation, terminated employees receive lump-sum severance payments primarily based on years of service. As of December 31, 2016, we substantially paid the severance costs associated with these actions.

In connection with the Sikorsky acquisition, we assumed obligations related to certain restructuring actions committed to by Sikorsky in June 2015. Net of amounts we anticipate to recover through the pricing of our products and services to our customers, we incurred and paid \$40 million of costs in 2016 related to these actions.

We have recovered a substantial amount of the restructuring charges through the pricing of our products and services to the U.S. Government and other customers in future periods, with the impact included in the respective business segment's results of operations.

Note 16 – Fair Value Measurements

Assets and liabilities measured and recorded at fair value on a recurring basis consisted of the following (in millions):

	December 31, 2017		December 31, 2016			
	Total	Level 1 Level 2	Total	Level 1 Level 2		
Assets						
Equity securities	\$39	\$ 39	\$ —	—	\$ 79	\$ —
Mutual funds	917	917	—	—	856	856
U.S. Government securities	116	—	116	—	113	113
Other securities	170	—	170	—	151	151
Derivatives	23	—	23	—	27	27
Liabilities						
Derivatives	106	—	106	—	85	85
Assets measured at NAV						
Other commingled funds	19	—	—	—	—	—

Substantially all assets measured at fair value, other than derivatives, represent investments classified as trading securities held in a separate trust to fund certain of our non-qualified deferred compensation plans and are recorded in other noncurrent assets on our consolidated balance sheets. The fair values of equity securities and mutual funds are determined by reference to the quoted market price per unit in active markets multiplied by the number of units held without consideration of transaction costs. The fair values of U.S. Government and other securities are determined using pricing models that use observable inputs (e.g., interest rates and yield curves observable at commonly quoted intervals), bids provided by brokers or dealers or quoted prices of securities with similar characteristics. The fair values of derivative instruments, which consist of foreign currency exchange forward and interest rate swap contracts, primarily are determined based on the present value of future cash flows using model-derived valuations that use observable inputs such as interest rates, credit spreads and foreign currency exchange rates. Certain other investments are measured at fair value using their NAV per share and do not have readily determined values and are thus not subject to leveling in the fair value hierarchy. We did not have any transfers of assets or liabilities between levels of the fair value hierarchy during 2017.

In addition to the financial instruments listed in the table above, we hold other financial instruments, including cash and cash equivalents, receivables, accounts payable and debt. The carrying amounts for cash and cash equivalents, receivables and accounts payable approximated their fair values. The estimated fair value of our outstanding debt was \$16.8 billion and \$16.2 billion at December 31, 2017 and 2016. The outstanding principal amount was \$15.5 billion and \$15.3 billion at December 31, 2017 and 2016, excluding \$1.2 billion and \$1.0 billion of unamortized discounts and issuance costs. The estimated fair values of our outstanding debt were determined based on quoted prices for similar instruments in active markets (Level 2).

In connection with the Sikorsky acquisition, we recorded the assets acquired and liabilities assumed at fair value. See “Note 3 – Acquisitions and Divestitures” for further information about the fair values assigned.

Note 17 – Summary of Quarterly Information (Unaudited)

A summary of quarterly information is as follows (in millions, except per share data):

	2017 Quarters			
	First ^(b)	Second	Third	Fourth ^{(c)(d)}
Net sales	\$ 11,057	\$ 12,685	\$ 12,169	\$ 15,137
Operating profit	1,149	1,485	1,428	1,859
Net earnings (loss) from continuing operations	763	942	939	(715)
Net earnings from discontinued operations	—	—	—	73
Net earnings (loss)	763	942	939	(642)
Earnings (loss) per common share from continuing operations ^(a) :				
Basic	2.63	3.27	3.27	(2.50)
Diluted	2.61	3.23	3.24	(2.50)
Earnings per common share from discontinued operations:				
Basic	—	—	—	0.25
Diluted	—	—	—	0.25
Basic earnings (loss) per common share ^(a)	2.63	3.27	3.27	(2.25)
Diluted earnings (loss) per common share ^(a)	2.61	3.23	3.24	(2.25)
	2016 Quarters			
	First	Second	Third ^{(d)(e)}	Fourth ^(e)
Net sales	\$ 10,368	\$ 11,577	\$ 11,551	\$ 13,752
Operating profit	1,158	1,375	1,588	1,428
Net earnings from continuing operations	806	899	1,089	959
Net earnings from discontinued operations	92	122	1,306	29
Net earnings	898	1,021	2,395	988
Earnings per common share from continuing operations ^(a) :				
Basic	2.65	2.97	3.64	3.29
Diluted	2.61	2.93	3.61	3.25
Earnings per common share from discontinued operations ^(a) :				
Basic	0.30	0.40	4.38	0.10
Diluted	0.30	0.39	4.32	0.10
Basic earnings per common share ^(a)	2.95	3.37	8.02	3.39
Diluted earnings per common share ^(a)	2.91	3.32	7.93	3.35

The sum of the quarterly earnings per share amounts do not equal the earnings per share amounts included on our consolidated statements of earnings. The difference in 2017 is primarily due the net loss in the fourth quarter

^(a) causing any potentially dilutive securities to have an anti-dilutive effect, which resulted in the weighted average shares outstanding for basic and dilutive earnings per share being equivalent. In addition, the differences in 2017 and 2016 also relate to the timing of our share repurchases during each respective year.

The first quarter of 2017 includes a \$120 million (\$74 million or \$0.25 per share, after tax) charge on our ^(b) EADGE-T program and a \$64 million (\$40 million or \$0.14 per share, after tax) charge, which represents our portion of a non-cash asset impairment charge recorded by our equity method investee, AMMROC (see “Note 1 – Significant Accounting Policies”).

In the fourth quarter of 2017, we recorded a net one-time tax charge of \$1.9 billion (\$6.80 per share), substantially ^(c) all of which was non-cash, primarily related to the estimated impact of the Tax Act (see “Note 9 – Income Taxes”). In addition, the fourth quarter of 2017 includes a previously deferred non-cash gain of \$198 million (\$122 million or \$0.43 per share, after tax) related to properties sold in 2015 as a result of completing our remaining obligations.

The fourth quarter of 2017 and the third quarter of 2016 include a net gain of \$73 million and \$1.2 billion, ^(d) respectively, reported in net earnings from discontinued operations, related to the 2016 divestiture of our former IS&GS business.

^(e)

The third quarter of 2016 includes the results of AWE from August 26, 2016, the date we obtained controlling interest, including \$103 million in net sales and \$104 million in net earnings. Net earnings during the third quarter of 2016 are primarily the result of a non-cash gain recognized on the step acquisition of AWE (see “Note 3 – Acquisitions and Divestitures”). The fourth quarter of 2016 includes the results of AWE for the entire quarter, including \$307 million in net sales and \$3 million in net earnings.

ITEM 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We performed an evaluation of the effectiveness of our disclosure controls and procedures as of December 31, 2017. The evaluation was performed with the participation of senior management of each business segment and key corporate functions, under the supervision of the Chief Executive Officer (CEO) and Chief Financial Officer (CFO). Based on this evaluation, the CEO and CFO concluded that our disclosure controls and procedures were effective. Management, including our CEO (principal executive officer) and CFO (principal financial officer), believes the consolidated financial statements included in this Annual Report on Form 10-K fairly represent in all material respects our financial condition, results of operations and cash flows at and for the periods presented in accordance with U.S. GAAP.

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control system is designed to provide reasonable assurance to our management and Board of Directors regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes.

Our management conducted an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2017. This assessment was based on the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework (2013 framework). Based on this assessment, management determined that our internal control over financial reporting was effective as of December 31, 2017.

Our independent registered public accounting firm has issued a report on the effectiveness of our internal control over financial reporting which is below.

Remediation of Material Weakness

During the year ended December 31, 2016, management completed its initial assessment of the effectiveness of our internal control over financial reporting for our Sikorsky business, which was acquired on November 6, 2015. During 2016, we performed our first comprehensive assessment of the design and operating effectiveness of internal controls at Sikorsky and determined that Sikorsky's internal control over financial reporting was ineffective as of December 31, 2016. Specifically, Sikorsky did not adequately identify, design and implement appropriate process-level controls for its accounting processes, including Sikorsky's contract accounting and sales recognition processes, inventory accounting process and payroll process, and appropriate information technology controls for its information technology systems.

During 2017, management improved controls at Sikorsky in order to remediate the material weakness in Lockheed Martin's internal control over financial reporting. To accomplish this we implemented several actions at Sikorsky, including increasing the number of individuals responsible for implementing and monitoring controls; training individuals responsible for designing, executing, testing and monitoring controls; expanding the scope of the internal controls program to include additional information technology systems; adding new process-level and information technology controls; modifying existing controls; and enhancing documentation that evidences that controls are performed. During the third quarter of 2017, we substantially completed our evaluation of the design of process-level and information technology controls. We successfully completed testing of the improved controls during the fourth quarter of 2017, and we have concluded that the material weakness has been remediated as of December 31, 2017. There were no material errors in our financial results or balances and there was no restatement of prior period financial statements and no change in previously released financial results as a result of the material weakness in internal controls over financial reporting.

Changes in Internal Control Over Financial Reporting

Other than the remediation efforts identified above to address the material weakness, there were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the quarter ended December 31, 2017 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Report of Ernst & Young LLP,
Independent Registered Public Accounting Firm,
Regarding Internal Control Over Financial Reporting

Board of Directors and Stockholders
Lockheed Martin Corporation

Opinion on Internal Control over Financial Reporting

We have audited Lockheed Martin Corporation's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). In our opinion, Lockheed Martin Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), consolidated balance sheets of Lockheed Martin Corporation as of December 31, 2017 and 2016, and the related consolidated statements of earnings, comprehensive income, equity, and cash flows for each of the three years in the period ended December 31, 2017, and the related notes (collectively referred to as the "financial statements") of the Corporation and our report dated February 6, 2018 expressed an unqualified opinion thereon.

Basis for Opinion

The Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Corporation's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Corporation in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control over Financial Reporting

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

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

/s/ Ernst & Young LLP
Tysons, Virginia

February 6, 2018

49

PART IV

ITEM 15. Exhibits and Financial Statement Schedules

List of financial statements filed as part of this Form 10-K

The following financial statements of Lockheed Martin Corporation and consolidated subsidiaries are included in Item 8 of this Annual Report on Form 10-K (Form 10-K) at the page numbers referenced below:

	Page
<u>Consolidated Statements of Earnings – Years ended December 31, 2017, 2016 and 2015</u>	4
<u>Consolidated Statements of Comprehensive Income – Years ended December 31, 2017, 2016 and 2015</u>	5
<u>Consolidated Balance Sheets – At December 31, 2017 and 2016</u>	6
<u>Consolidated Statements of Cash Flows – Years ended December 31, 2017, 2016 and 2015</u>	7
<u>Consolidated Statements of Equity – Years ended December 31, 2017, 2016 and 2015</u>	8
<u>Notes to Consolidated Financial Statements</u>	9

The report of Lockheed Martin Corporation’s independent registered public accounting firm with respect to the above-referenced financial statements and their report on internal control over financial reporting are included in Item 8 and Item 9A of this Form 10-K at the page numbers referenced below. Their consent appears as Exhibit 23 of this Form 10-K.

	Page
<u>Report of Independent Registered Public Accounting Firm</u>	3
<u>Report of Independent Registered Public Accounting Firm, Regarding Internal Control Over Financial Reporting</u>	49

List of financial statement schedules filed as part of this Form 10-K

All schedules have been omitted because they are not applicable, not required or the information has been otherwise supplied in the consolidated financial statements or notes to consolidated financial statements.

Exhibits

2.1 Stock Purchase Agreement dated as of July 19, 2015 by and among United Technologies Corporation, the other Sellers identified therein and Lockheed Martin Corporation (incorporated by reference to Exhibit 2.1 to Lockheed Martin Corporation’s Current Report on Form 8-K filed with the SEC on July 20, 2015). The schedules and exhibits to the Stock Purchase Agreement have been omitted pursuant to Item 601(b)(2) of Regulation S-K. Lockheed Martin agrees to furnish supplementally a copy of such schedules and exhibits, or any section thereof, to the SEC upon request.

2.2 Amendment No. 1 to Stock Purchase Agreement dated as of November 5, 2015 by and among United Technologies Corporation and certain affiliated entities identified therein and Lockheed Martin Corporation (incorporated by reference to Exhibit 2.1 to Lockheed Martin Corporation’s Current Report on Form 8-K filed with the SEC on November 6, 2015). The exhibits to Amendment No. 1 to Stock Purchase Agreement have been omitted pursuant to Item 601(b)(2) of Regulation S-K. Lockheed Martin agrees to furnish supplementally a copy of such exhibits, or any section thereof, to the SEC upon request.

2.3 Agreement and Plan of Merger, dated as of January 26, 2016, among Lockheed Martin Corporation, Leidos Holdings, Inc., Abacus Innovations Corporation and Lion Merger Co. (incorporated by reference to Exhibit 2.1 to Lockheed Martin Corporation’s Current Report on Form 8-K filed with the SEC on January 27, 2016). The schedules and attachments to the Merger Agreement have been omitted pursuant to Item 601(b)(2) of Regulation S-K, and such schedules and attachments will be furnished to the SEC upon request.

2.4 Amendment dated as of June 27, 2016 to Agreement and Plan of Merger, dated as of January 26, 2016, among Lockheed Martin Corporation, Leidos Holdings, Inc., Abacus Innovations Corporation and Lion Merger Co. (incorporated by reference to Exhibit 2.1 to Lockheed Martin Corporation’s Quarterly Report on Form 10-Q for the quarter ended June 26, 2016).

2.5 Separation Agreement, dated as of January 26, 2016, between Lockheed Martin Corporation and Abacus Innovations Corporation (incorporated by reference to Exhibit 2.2 to Lockheed Martin Corporation’s Current

Report on Form 8-K filed with the SEC on January 27, 2016). The schedules and attachments to the Separation Agreement have been omitted pursuant to Item 601(b)(2) of Regulation S-K, and such schedules and attachments will be furnished to the SEC upon request.

- 2.6 Amendment dated as of June 27, 2016 to Separation Agreement, dated as of January 26, 2016, between Lockheed Martin Corporation and Abacus Innovations Corporation (incorporated by reference to Exhibit 2.2 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended June 26, 2016). The schedules to the amendment have been omitted pursuant to Item 601(b)(2) of Regulation S-K, and such schedules and attachments will be furnished to the SEC upon request.
- 3.1 Charter of Lockheed Martin Corporation, as amended by Articles of Amendment dated April 23, 2009 (incorporated by reference to Exhibit 3.1 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2010 (File No. 001-11437)).
- 3.2 Bylaws of Lockheed Martin Corporation, as amended and restated effective December 8, 2017 (incorporated by reference to Exhibit 3.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on December 11, 2017).
- 4.1 Indenture, dated May 15, 1996, among Lockheed Martin Corporation, Lockheed Martin Tactical Systems, Inc. and First Trust of Illinois, National Association as Trustee.
**
- 4.2 Indenture, dated as of August 30, 2006, between Lockheed Martin Corporation and The Bank of New York (incorporated by reference to Exhibit 99.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on August 31, 2006 (File No. 001-11437)).
- 4.3 Indenture, dated as of March 11, 2008, between Lockheed Martin Corporation and The Bank of New York (incorporated by reference to Exhibit 4.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on March 12, 2008 (File No. 001-11437)).
- 4.4 Indenture, dated as of May 25, 2010, between Lockheed Martin Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 99.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on May 25, 2010 (File No. 001-11437)).
- 4.5 Indenture, dated as of September 6, 2011, between Lockheed Martin Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on September 8, 2011 (File No. 001-11437)).
- 4.6 Indenture, dated as of December 14, 2012, between Lockheed Martin Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 99.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on December 17, 2012 (File No. 001-11437)).
- 4.7 Indenture dated as of September 7, 2017, between Lockheed Martin Corporation and U.S. Bank National Association, as trustee (incorporated by reference to Exhibit 99.1 of Lockheed Martin's Current Report on Form 8-K filed with the SEC on September 7, 2017).

See also Exhibits 3.1 and 3.2.

No instruments defining the rights of holders of long-term debt that is not registered are filed because the total amount of securities authorized under any such instrument does not exceed 10% of the total assets of Lockheed Martin Corporation on a consolidated basis. Lockheed Martin Corporation agrees to furnish a copy of such instruments to the SEC upon request.

- 10.1 Five-Year Credit Agreement dated as of October 9, 2015, among Lockheed Martin Corporation, the lenders listed therein, and Bank of America, N.A., as administrative agent (incorporated by reference to Exhibit 10.2 to

Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on October 13, 2015).

10.2 Extension Agreement dated as of October 7, 2016 by and among Lockheed Martin Corporation, the lenders listed therein, and Bank of America, N.A., as administrative agent (incorporated by reference to Exhibit 10.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on October 7, 2016).

10.3 Extension Agreement dated as of October 9, 2017 by and among Lockheed Martin Corporation, the lenders listed therein, and Bank of America, N.A., as administrative agent (incorporated by reference to Exhibit 10.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on October 10, 2017).

10.4 Lockheed Martin Corporation Directors Deferred Compensation Plan, as amended (incorporated by reference to Exhibit 10.2 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2008 (File No. 001-11437)).

10.5 Lockheed Martin Corporation Directors Equity Plan, as amended (incorporated by reference to Exhibit 10.1 to Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on November 2, 2006 (File No. 001-11437)).

10.6 Lockheed Martin Corporation 2009 Directors Equity Plan (incorporated by reference to Appendix E to Lockheed Martin Corporation's Definitive Proxy Statement on schedule 14A filed with the SEC on March 14, 2008 (File No. 001-11437)).

- 10.7 Amendment to Lockheed Martin Corporation 2009 Directors Equity Plan, effective January 1, 2018 (incorporated by reference to Exhibit 10.2 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended September 24, 2017).
- 10.8 Lockheed Martin Corporation Supplemental Savings Plan, as amended and restated effective January 1, 2015 (incorporated by reference to Exhibit 10.4 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended March 29, 2015).
- 10.9 Lockheed Martin Corporation Deferred Management Incentive Compensation Plan, as amended and restated effective May 16, 2016 (incorporated by reference to Exhibit 10.1 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended June 26, 2016).
- 10.10 Lockheed Martin Corporation Amended and Restated 2006 Management Incentive Compensation Plan (Performance Based), amended and restated effective January 1, 2017 (incorporated by reference to Exhibit 10.1 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended March 26, 2017).
- 10.11 Amendment No. 1 dated December 19, 2017 to Lockheed Martin Corporation Amended and Restated 2006 Management Incentive Compensation Plan (Performance Based), amended and restated effective January 1, 2017.
**
- 10.12 Lockheed Martin Corporation Amended and Restated 2003 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.17 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2008 (File No. 001-11437)).
- 10.13 Forms of Stock Option Award Agreements under the Lockheed Martin Corporation 2003 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.32 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2008 (File No. 001-11437)).
- 10.14 Forms of Stock Option Award Agreements under the Lockheed Martin Corporation 2003 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.33 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2009 (File No. 001-11437)).
- 10.15 Form of Stock Option Award Agreement under the Lockheed Martin Corporation 2003 Incentive Performance Award Plan (incorporated by reference to Exhibit 99.3 of Lockheed Martin Corporation's Current Report on Form 8-K filed with the SEC on February 3, 2011 (File No. 001-11437)).
- 10.16 Form of Indemnification Agreement (incorporated by reference to Exhibit 10.34 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2009 (File No. 001-11437)).
- 10.17 Lockheed Martin Corporation 2011 Incentive Performance Award Plan, as amended June 23, 2016 effective as of January 1, 2017 (incorporated by reference to Exhibit 10.2 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended June 26, 2016).
- 10.18 Forms of Stock Option Award Agreements under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.39 of Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2011 (File No. 001-11437)).
- 10.19 Lockheed Martin Corporation Nonqualified Capital Accumulation Plan, as amended and restated generally effective as of December 18, 2015 (incorporated by reference to Exhibit 10.22 of Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2015).

- 10.20 Non-Employee Director Compensation Summary (incorporated by reference to Exhibit 10.1 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended September 24, 2017).
- 10.21 Form of Restricted Stock Unit Award Agreement, Form of Long-Term Incentive Performance Award Agreement (2015-2017 performance period), and Form of Performance Stock Unit Award Agreement (2015-2017 performance period) under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.30 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2014 (File No. 001-11437)).
- 10.22 Form of Restricted Stock Unit Award Agreement under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.2 to Lockheed Martin Corporation's Current Report on Form 8-K filed on February 2, 2016).
- 10.23 Form of Performance Stock Unit Award Agreement (2016-2018 performance period) under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.3 to Lockheed Martin Corporation's Current Report on Form 8-K filed on February 2, 2016).
- 10.24 Form of Long-Term Incentive Performance Award Agreement (2016-2018 performance period) under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.4 to Lockheed Martin Corporation's Current Report on Form 8-K filed on February 2, 2016).

- 10.25 Form of Restricted Stock Unit Award Agreement under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.2 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended March 26, 2017).
- 10.26 Form of Performance Stock Unit Award Agreement (2017 to 2019 Performance Period) under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.3 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended March 26, 2017).
- 10.27 Form of Long-Term Incentive Performance Award Agreement (2017 to 2019 Performance Period) under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan (incorporated by reference to Exhibit 10.4 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended March 26, 2017).
- 10.28 ** Lockheed Martin Corporation Consolidated Supplemental Retirement Benefit Plan, as amended and restated effective December 31, 2017.
- 10.29 Lockheed Martin Corporation Executive Severance Plan, as amended and restated effective December 1, 2016 (incorporated by reference to Exhibit 10.26 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2016).
- 10.30 Amendment to Terms of Outstanding Restricted Stock Unit Awards and Performance Stock Unit Awards under the Lockheed Martin Corporation 2011 Incentive Performance Award Plan Relating to Tax Withholding (incorporated by reference to Exhibit 10.27 to Lockheed Martin Corporation's Annual Report on Form 10-K for the year ended December 31, 2016).
- 10.31 Amendments to Terms of Outstanding Long-Term Incentive Performance Award Agreements (2015-2017 Performance Period and 2016-2018 Performance Period) under the Lockheed Martin Corporation 2011 Performance Award Plan Relating to Tax Withholding (incorporated by reference to Exhibit 10.1 to Lockheed Martin Corporation's Quarterly Report on Form 10-Q for the quarter ended June 25, 2017).
- 12 ** Computation of ratio of earnings to fixed charges.
- 21 ** Subsidiaries of Lockheed Martin Corporation.
- 23 * Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm.
- 24 ** Powers of Attorney.
- 31.1 * Certification of Marillyn A. Hewson pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 * Certification of Bruce L. Tanner pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32 * Certification of Marillyn A. Hewson and Bruce L. Tanner Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS
* XBRL Instance Document
- XBRL Taxonomy Extension Schema Document

101.SCH

*

101.CAL

*

XBRL Taxonomy Extension Calculation Linkbase Document

101.DEF

*

XBRL Taxonomy Extension Definition Linkbase Document

101.LAB

*

XBRL Taxonomy Extension Label Linkbase Document

101.PRE

*

XBRL Taxonomy Extension Presentation Linkbase Document

Exhibits 10.4 through 10.31 constitute management contracts or compensatory plans or arrangements.

*Filed herewith

**Included in the Form 10-K for the year ended December 31, 2017 filed on February 6, 2018

SIGNATURE

Pursuant to the requirements of Section 13 or 15(d) 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.

Lockheed Martin Corporation
(Registrant)

Date: February 16, 2018 By: /s/ Brian P. Colan
Brian P. Colan
Vice President, Controller, and Chief Accounting Officer