HARRIS CORP /DE/
Form 10-Q
February 03, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)
þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended December 30, 2016
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number: 1-3863
HARRIS CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	34-0276860
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1025 West NASA Boulevard Melbourne, Florida	32919
(Address of principal executive offices)	(Zip Code)

(321) 727-9100
(Registrant's telephone number, including area code)

No changes
(Former name, former address and former fiscal year, if changed since last report)
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. þ Yes p 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). þ Yes p No
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	þ	Accelerated filer	o
Non-accelerated filer	o (Do not check if a smaller reporting company)	Smaller reporting company	o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). p Yes þ No
The number of shares outstanding of the registrant's common stock as of January 27, 2017 was 124,461,661 shares.

HARRIS CORPORATION
FORM 10-Q
For the Quarter Ended December 30, 2016
INDEX

This Quarterly Report on Form 10-Q contains trademarks, service marks and registered marks of Harris Corporation and its subsidiaries.

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements.
HARRIS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF INCOME
(Unaudited)

	Quarter Ended		Two Quarters Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	(In millions, except per share amounts)			
Revenue from product sales and services	$1,700	$1,748	$3,378	$3,458
Cost of product sales and services	(1,138)	(1,203)	(2,258)	(2,347)
Engineering, selling and administrative expenses	(276)	(217)	(572)	(525)
Non-operating income	1	—	2	1
Interest income	1	—	1	1
Interest expense	(44)	(46)	(88)	(93)
Income from continuing operations before income taxes	244	282	463	495
Income taxes	(76)	(85)	(139)	(152)
Income from continuing operations	168	197	324	343
Discontinued operations, net of income taxes	9	(349)	13	(347)
Net income (loss)	$177	$(152)	$337	$(4)
Net income (loss) per common share				
Basic				
Continuing operations	$1.35	$1.59	$2.60	$2.77
Discontinued operations	0.07	(2.82)	0.11	(2.81)
	$1.42	$(1.23)	$2.71	$(0.04)
Diluted				
Continuing operations	$1.33	$1.58	$2.57	$2.75
Discontinued operations	0.07	(2.80)	0.11	(2.78)
	$1.40	$(1.22)	$2.68	$(0.03)
Cash dividends paid per common share	$0.53	$0.50	$1.06	$1.00
Basic weighted average common shares outstanding	123.7	123.8	123.8	123.6
Diluted weighted average common shares outstanding	125.4	124.9	125.5	124.7

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

HARRIS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(Unaudited)

	Quarter Ended		Two Quarters Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	(In millions)			
Net income (loss)	$177	$(152)	$337	$(4)
Other comprehensive loss:				
Foreign currency translation loss, net of income taxes	(26)	(15)	(29)	(47)
Net unrealized gain (loss) on hedging derivatives, net of income taxes	(1)	1	(1)	1
Net unrecognized gain (loss) on postretirement obligations, net of income taxes	1	(4)	2	(4)
Other comprehensive loss, net of income taxes	(26)	(18)	(28)	(50)
Total comprehensive income (loss)	$151	$(170)	$309	$(54)

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

HARRIS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEET
(Unaudited)

	December 30, 2016		July 1, 2016	
	(In millions, except shares)			
Assets				
Current Assets				
Cash and cash equivalents	$	361	$	487
Receivables	762		871	
Inventories	1,001		950	
Income taxes receivable	11		58	
Other current assets	133		130	
Current assets of discontinued operations	344		112	
Total current assets	2,612		2,608	
Non-current Assets				
Property, plant and equipment	908		943	
Goodwill	5,848		5,839	
Other intangible assets	1,437		1,518	
Non-current deferred income taxes	550		552	
Other non-current assets	263		254	
Non-current assets of discontinued operations	—		279	
Total non-current assets	9,006		9,385	
	$	11,618	$	11,993
Liabilities and Equity				
Current Liabilities				
Short-term debt	$	183	$	15
Accounts payable	540		591	
Compensation and benefits	130		166	
Other accrued items	340		400	
Advance payments and unearned income	260		314	
Income taxes payable	15		6	
Current portion of long-term debt	130		382	
Current liabilities of discontinued operations	67		91	
Total current liabilities	1,665		1,965	
Non-current Liabilities				
Defined benefit plans	2,144		2,296	
Long-term debt, net	4,087		4,120	
Non-current deferred income taxes	4		4	

Other long-term liabilities	560			525		
Non-current liabilities of discontinued operations	—			26		
Total non-current liabilities	6,795			6,971		
Equity						
Shareholders’ Equity:						
Preferred stock, without par value; 1,000,000 shares authorized; none issued	—			—		
Common stock, $1.00 par value; 500,000,000 shares authorized; issued and outstanding 124,277,167 shares at December 30, 2016 and 124,643,407 shares at July 1, 2016	124			125		
Other capital	2,061			2,096		
Retained earnings	1,495			1,330		
Accumulated other comprehensive loss	(523		)	(495		)
Total shareholders’ equity	3,157			3,056		
Noncontrolling interests	1			1		
Total equity	3,158			3,057		
	$	11,618		$	11,993	

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

HARRIS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
(Unaudited)

	Two Quarters Ended	
	December 30, 2016	January 1, 2016
	(In millions)	
Operating Activities		
Net income (loss)	$337	$(4)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	101	114
Amortization of intangible assets from Exelis Inc. acquisition	66	66
Share-based compensation	22	19
Qualified pension plan contributions	(103)	(97)
Pension income	(49)	(12)
Net liability reduction for certain post-employment benefit plans	—	(101)
Impairment of goodwill and other assets	—	367
Adjustment to loss on sales of businesses, net	—	21
(Increase) decrease in:		
Accounts receivable	125	220
Inventories	(50)	(91)
Increase (decrease) in:		
Accounts payable and accrued expenses	(132)	(128)
Advance payments and unearned income	(58)	(59)
Income taxes	70	31
Other	(34)	41
Net cash provided by operating activities	295	387
Investing Activities		
Net additions of property, plant and equipment	(49)	(49)
Adjustment to proceeds from sale of business	(25)	—
Net cash used in investing activities	(74)	(49)
Financing Activities		
Proceeds from borrowings	185	209
Repayments of borrowings	(300)	(395)
Proceeds from exercises of employee stock options	27	33
Repurchases of common stock	(100)	—
Cash dividends	(134)	(127)
Other financing activities	(19)	(15)
Net cash used in financing activities	(341)	(295)
Effect of exchange rate changes on cash and cash equivalents	(6)	(13)
Net increase (decrease) in cash and cash equivalents	(126)	30
Cash and cash equivalents, beginning of year	487	481
Cash and cash equivalents, end of quarter	$361	$511

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note A — Significant Accounting Policies and Recent Accounting Standards

Basis of Presentation

The accompanying Condensed Consolidated Financial Statements (Unaudited) include the accounts of Harris Corporation and its consolidated subsidiaries. As used in these Notes to Condensed Consolidated Financial Statements (Unaudited) (these "Notes"), the terms "Harris," "Company," "we," "our" and "us" refer to Harris Corporation and its consolid subsidiaries. Intracompany transactions and accounts have been eliminated in consolidation. The accompanying Condensed Consolidated Financial Statements (Unaudited) have been prepared by Harris, without an audit, in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the rules and regulations of the Securities and Exchange Commission ("SEC"). Accordingly, such interim financial statements do not include all information and footnotes necessary for a complete presentation of financial position, results of operations and cash flows in conformity with GAAP for annual financial statements. In the opinion of management, such interim financial statements reflect all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of our financial position, results of operations and cash flows for the periods presented therein. The results for the second quarter and first two quarters of fiscal 2017 are not necessarily indicative of the results that may be expected for the full fiscal year or any subsequent period. The balance sheet at July 1, 2016 has been derived from our audited financial statements, but does not include all of the information and footnotes required by GAAP for annual financial statements. We provide complete, audited financial statements in our Annual Report on Form 10-K, which includes information and footnotes required by the rules and regulations of the SEC. The information included in this Quarterly Report on Form 10-Q (this "Report") should be read in conjunction with the Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and accompanying Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended July 1, 2016 (our "Fiscal 2016 Form 10-K").

In the second quarter of fiscal 2017, we entered into a definitive agreement to sell our Harris CapRock Communications commercial business ("CapRock"). CapRock was formerly part of our Critical Networks segment and is reported as discontinued operations in this Report. As a result, our historical financial results have been restated to account for CapRock as discontinued operations for all periods presented in this Report. Except for disclosures related to our cash flows, or unless otherwise specified, disclosures in the accompanying Condensed Consolidated Financial Statements (Unaudited) and these Notes relate solely to our continuing operations.

On January 1, 2017, we completed the sale of CapRock. See Note S — Subsequent Events in these Notes for additional information.

See Note B — Discontinued Operations in these Notes for additional information regarding discontinued operations.

Amounts contained in this Report may not always add to totals due to rounding.

Use of Estimates

The preparation of financial statements in accordance with GAAP requires us to make estimates and assumptions that affect the amounts reported in the accompanying Condensed Consolidated Financial Statements (Unaudited) and these Notes and related disclosures. These estimates and assumptions are based on experience and other information available prior to issuance of the accompanying Condensed Consolidated Financial Statements (Unaudited) and these Notes. Materially different results can occur as circumstances change and additional information becomes known.

Restructuring and Integration Charges

We record restructuring charges for sales or terminations of product lines, closures or relocations of business activities, changes in management structure, and fundamental reorganizations that affect the nature and focus of operations. Such changes include termination benefits, contract termination costs and costs to consolidate facilities or relocate employees. We record these charges at their fair value when incurred. In cases where employees are required to render service until they are terminated in order to receive the termination benefits and will be retained beyond the minimum retention period, we record the expense ratably over the future service period.

In fiscal 2016, we recorded restructuring charges of $143 million for workforce reductions and integration charges as a result of our acquisition of Exelis in the fourth quarter of fiscal 2015, including consolidation of facilties and other costs. These charges are included as a component of the "Cost of product sales and services" and "Engineering, selling and administrative expenses" line items in our Consolidated Statement of Income in our Fiscal 2016 Form 10-K.

Liabilities associated with these and previous restructuring actions were $44 million at December 30, 2016 and $53 million at July 1, 2016. The majority of the remaining liabilities as of December 30, 2016 will be paid within the next twelve months.

Adoption of New Accounting Standards

In the first quarter of fiscal 2017, we adopted an accounting standard issued by the Financial Accounting Standards Board ("FASB") that changed the accounting for certain aspects of stock options and other share-based compensation. This accounting standard requires companies to recognize excess tax benefits or expenses related to the vesting or settlement of employee share-based awards (i.e., the difference between the actual tax benefit realized and the tax benefit initially recognized for financial reporting purposes) as income tax benefit or expense in our Condensed Consolidated Statement of Income (Unaudited). Prior to adoption of this accounting standard, we were required to recognize these amounts directly in our Condensed Consolidated Balance Sheet (Unaudited) as additional paid-in capital. This accounting standard also requires classification of cash flows resulting from excess tax benefits or expenses related to employee share-based awards as cash flows from operating activities in our Condensed Consolidated Statement of Cash Flows (Unaudited). Prior to adoption of this accounting standard, we classified cash flows resulting from excess tax benefits or expenses related to employee share-based awards as cash flows from financing activities in our Condensed Consolidated Statement of Cash Flows (Unaudited). We applied all significant changes required by this accounting standard on a prospective basis from the beginning of fiscal 2017.

Adopting this accounting standard did not have a material impact on our financial position, results of operations or cash flows, except as follows:

- We recognized $3 million ($.02 per diluted share) and $13 million ($.10 per diluted share) of income tax benefit in our Condensed Consolidated Statement of Income (Unaudited) for the quarter and two quarters ended December 30, 2016, respectively; and
- We classified $13 million of cash flows resulting from excess tax benefits related to employee share-based awards as net cash provided by operating activities in our Condensed Consolidated Statement of Cash Flows (Unaudited) for the two quarters ended December 30, 2016.

Accounting Standards Issued But Not Yet Effective

In May 2014, the FASB issued a comprehensive new revenue recognition standard that supersedes nearly all revenue recognition guidance under GAAP and International Financial Reporting Standards and supersedes some cost guidance for construction-type and production-type contracts. The guidance in this standard is principles-based, and consequently, entities will be required to use more judgment and make more estimates than under prior guidance, including identifying contract performance obligations, estimating variable consideration to include in the contract price and allocating the transaction price to separate performance obligations. The guidance in this standard is applicable to all contracts with customers, regardless of industry-specific or transaction-specific fact patterns. Additionally, this standard provides guidance for transactions that were not previously addressed comprehensively (e.g., service revenue, contract modifications and licenses of intellectual property) and modifies guidance for multiple-element arrangements. The core principle of this standard is that entities should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. To help financial statement users better understand the nature, amount, timing and potential uncertainty of the revenue that is recognized, this standard requires significantly more interim and annual disclosures. This standard allows for either "full retrospective" adoption (application to all periods presented) or "modified retrospective" adoption (application to only the most current period presented in the financial statements, as well as certain additional required footnote disclosures). In August 2015, the FASB issued an accounting standards update that defers the effective date of this standard by one year, while permitting entities to elect to adopt one year earlier than the original effective date. As a result, this standard is now effective for fiscal years, and interim reporting periods within those years, beginning after December 15, 2017, which for us is our fiscal 2019. We are currently evaluating the impact the new revenue recognition standard will have on our financial position, results of operations and cash flows. As the new standard supersedes nearly all revenue recognition guidance applicable to us under GAAP, it could impact revenue and cost recognition across all of our business segments as well as related business processes and information technology systems. As a result, our evaluation of the impact of the new revenue recognition standard will continue over future periods.

In February 2016, the FASB issued a new lease standard that supersedes existing lease guidance under GAAP. This standard requires lessees to record most leases on their balance sheets but recognize expenses on their income statements in a manner similar to existing lease guidance under GAAP. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements, with the option to use certain relief. Full retrospective application is prohibited. This standard is effective for fiscal years, and interim reporting periods within those years, beginning after December 15, 2018, which for us is our fiscal 2020. We are currently evaluating the impact this standard will have on our financial position, results of operations and cash flows.

Note B — Discontinued Operations

The major components of the discontinued operations in our Condensed Consolidated Statement of Income (Unaudited) include the following:

	Quarter Ended		Two Quarters Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	(In millions)			
Revenue from product sales and services	$69	$ 95	$145	$ 196
Cost of product sales and services	(53)	(77)	(109)	(154)
Engineering, selling and administrative expenses	(11)	(22)	(26)	(43)
Impairment of goodwill and other assets	—	(367)	—	(367)
Non-operating income	7	—	7	—
Income (loss) before income taxes	12	(371)	17	(368)
Loss on sale of discontinued operation	—	(21)	—	(21)
Income tax (expense) benefit	(3)	43	(4)	42
Discontinued operations, net of income taxes	$9	$ (349)	$13	$ (347)

The carrying amounts of the major classes of assets and liabilities included in discontinued operations in our Condensed Consolidated Balance Sheet (Unaudited) as of December 30, 2016 and July 1, 2016, are as follows:

	December 30, 2016 (1)	July 1, 2016
	(In millions)	
Assets		
Receivables	$ 50	$ 67
Inventories	12	14
Property, plant and equipment	69	—
Goodwill	132	—
Other intangible assets	22	—
Other current assets	59	31
Current assets of discontinued operations	$ 344	$ 112
Property, plant and equipment	$ —	$ 73
Goodwill	—	136

Other intangible assets	—	24
Other non-current assets	—	46
Non-current assets of discontinued operations	$ —	$ 279
Liabilities		
Accounts payable	$ 15	$ 11
Post-closing adjustment liability	2	27
Other current liabilities	50	53
Current liabilities of discontinued operations	$ 67	$ 91
Non-current liabilities of discontinued operations	$ —	$ 26

(1) The assets and liabilities of discontinued operations held for sale are classified as current in our Condensed Consolidated Balance Sheet (Unaudited) as of December 30, 2016 because it was probable the sale would occur and proceeds

would be
collected
within one
year.

Cumulative foreign currency translation loss, net of taxes, associated with the assets and liabilities of discontinued operations held for sale was $63 million and $67 million as of December 30, 2016 and July 1, 2016, respectively.

Depreciation and amortization, capital expenditures, and significant noncash items of discontinued operations for all periods presented in our Condensed Consolidated Statement of Income (Unaudited) include the following:

	Quarter Ended		Two Quarters Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	(In millions)			
Depreciation and amortization	$3	$ 12	$ 11	$ 25
Capital expenditures	2	4	4	8
Significant noncash items:				
Impairment of goodwill and other assets	—	367	—	367

CapRock

On November 1, 2016, we entered into a definitive agreement to sell our CapRock business to SpeedCast International Ltd. (“SpeedCast”) for $425 million in cash, subject to customary adjustments (including a post-closing working capital adjustment). CapRock, which was formerly part of our Critical Networks segment, provided wireless, terrestrial and satellite communications services to energy and maritime customers. We consider the CapRock divestiture to be a strategic shift because we are exiting the energy and maritime industry. We will provide various transition services to SpeedCast for a period of up to 12 months following the close of the transaction pursuant to a separate agreement.

On January 1, 2017, following the close of the second quarter of fiscal 2017, we completed the sale of CapRock to SpeedCast. We subsequently used $248 million of the cash proceeds from the CapRock divestiture to repay principal on our term loans ($215 million of voluntary prepayments of principal and $33 million of scheduled repayments).

Broadcast Communications

On February 4, 2013, we completed the sale of Broadcast Communications to an affiliate of The Gores Group, LLC (the “Buyer”) pursuant to a definitive Asset Sale Agreement entered into December 5, 2012 for $225 million, including $160 million in cash, subject to customary adjustments (including a post-closing working capital adjustment), a $15 million subordinated promissory note (which was collected in fiscal 2014) and an earnout of up to $50 million based on future performance. Broadcast Communications was recorded as discontinued operations in connection with the sale.

Based on a dispute between us and the Buyer over the amount of the post-closing working capital adjustment, we and the Buyer previously appointed a nationally recognized accounting firm to render a final determination of such dispute. On January 29, 2016, the accounting firm rendered its final determination as to the disputed items, in which it concluded substantially in our favor and partly in the Buyer’s favor. As a result of such determination, we recorded a loss in discontinued operations in the second quarter of fiscal 2016 of $21 million ($17 million after-tax or $0.14 per diluted share).

Note C — Stock Options and Other Share-Based Compensation

During the two quarters ended December 30, 2016, we had options or other share-based compensation outstanding under two shareholder-approved stock incentive plans (“SIPs”), the Harris Corporation 2005 Equity Incentive Plan (As Amended and Restated Effective August 27, 2010) and the Harris Corporation 2015 Equity Incentive Plan (the “2015 EIP”). Grants of share-based awards after October 23, 2015 were made under our 2015 EIP. We believe that share-based awards more closely align the interests of participants with those of shareholders. Certain share-based awards provide for accelerated vesting if there is a change in control (as defined under our SIPs). The compensation cost related to our share-based awards that was charged against income was $11 million and $22 million for the quarter and two quarters ended December 30, 2016, respectively. The compensation cost related to our share-based awards that was charged against income was $9 million and $19 million for the quarter and two quarters ended January 1, 2016, respectively.

Grants to participants under our 2015 EIP during the second quarter ended December 30, 2016 consisted of 19,750 stock options, 13,665 restricted share awards and restricted share unit awards, and 12,820 performance unit awards. Grants to participants under our 2015 EIP during the two quarters ended December 30, 2016 consisted of 1,230,480 stock options, 81,860 restricted share awards and restricted share unit awards, and 261,275 performance unit awards.

The fair value as of the grant date of each stock option award was determined using the Black-Scholes-Merton option-pricing model, which used the following assumptions: expected dividend yield of 2.36 percent; expected volatility of 21.78 percent; risk-free interest rates averaging 1.23 percent; and expected term in years of 5.03. The fair value as of the grant date of each restricted share award was based on the closing price of our common stock on the grant date. The fair value as of the grant date of each performance unit award was determined based on the fair value from a multifactor Monte Carlo valuation model that simulates our stock price and total shareholder return relative to companies in the Standard & Poor's 500, less a discount to reflect the delay in payments of cash dividend-equivalents that are made only upon vesting.

Note D — Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss are summarized below:

	December 30, 2016 (1)	July 1, 2016 (1)
	(In millions)	
Foreign currency translation, net of income taxes of $30 million and $29 million at December 30, 2016 and July 1, 2016, respectively	$(160)	$(131)
Net unrealized loss on hedging derivatives, net of income taxes of $11 million at December 30, 2016 and July 1, 2016	(19)	(18)

Unrecognized postretirement obligations, net of income taxes of $213 million at December 30, 2016 and July 1, 2016	(344)	(346)
	$(523)	$(495)

(1) Reclassifications out of accumulated other comprehensive loss to earnings were not material for the two quarters ended December 30, 2016 or January 1, 2016.

Note E — Receivables

Receivables are summarized below:

December 30, 2016	July 1, 2016