

UNITED TECHNOLOGIES CORP /DE/  
Form 10-Q  
July 20, 2007  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON D.C. 20549**

\_\_\_\_\_  
**FORM 10-Q**  
\_\_\_\_\_

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the quarterly period ended June 30, 2007

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-812

**UNITED TECHNOLOGIES CORPORATION**

**DELAWARE**

**06-0570975**

**One Financial Plaza, Hartford, Connecticut 06103**

**(860) 728-7000**

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

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At June 30, 2007 there were 991,783,733 shares of common stock outstanding.

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**UNITED TECHNOLOGIES CORPORATION**  
**AND SUBSIDIARIES**  
**CONTENTS OF QUARTERLY REPORT ON FORM 10-Q**  
**Quarter Ended June 30, 2007**

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

**Table of Contents****Part I Financial Information****Item 1. Financial Statements****CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS****(Unaudited)**

| In Millions (except per share amounts)                   | Quarter Ended<br>June 30, |                 |
|--|---------------------------|-----------------|
|  | 2007                      | 2006            |
| <b>Revenues:</b>   |                           |                 |
| Product sales  | \$ 10,196                 | \$ 8,948        |
| Service sales  | 3,570                     | 3,098           |
| Other income, net  | 138                       | 218             |
|  | 13,904                    | 12,264          |
| <b>Costs and expenses:</b>                               |                           |                 |
| Cost of products sold                                    | 7,683                     | 6,628           |
| Cost of services sold                                    | 2,446                     | 2,147           |
| Research and development                                 | 416                       | 370             |
| Selling, general and administrative                      | 1,494                     | 1,378           |
| <b>Operating Profit</b>                                  | <b>1,865</b>              | <b>1,741</b>    |
| Interest   | 163                       | 155             |
| <b>Income before income taxes and minority interests</b> | <b>1,702</b>              | <b>1,586</b>    |
| Income tax expense                                       | (479)                     | (415)           |
| Minority interests                                       | (75)                      | (68)            |
| <b>Net income</b>  | <b>\$ 1,148</b>           | <b>\$ 1,103</b> |
| <b>Earnings per share of Common Stock:</b>               |                           |                 |
| Basic  | \$ 1.19                   | \$ 1.12         |
| Diluted  | \$ 1.16                   | \$ 1.09         |
| <b>Dividends per share of Common Stock</b>               | <b>\$ .27</b>             | <b>\$ .27</b>   |
| <b>Average number of shares outstanding:</b>             |                           |                 |
| Basic  | 966                       | 983             |
| Diluted  | 990                       | 1,009           |

See accompanying Notes to Condensed Consolidated Financial Statements

**Table of Contents****CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS****(Unaudited)**

| <b>In Millions (except per share amounts)</b>            | <b>Six Months Ended<br/>June 30,</b> |                 |
|--|--------------------------------------|-----------------|
|  | <b>2007</b>                          | <b>2006</b>     |
| <b>Revenues:</b>   |                                      |                 |
| Product sales  | \$ 18,731                            | \$ 16,431       |
| Service sales  | 6,971                                | 6,061           |
| Other income, net  | 480                                  | 387             |
|  | 26,182                               | 22,879          |
| <b>Costs and expenses:</b>                               |                                      |                 |
| Cost of products sold                                    | 14,318                               | 12,301          |
| Cost of services sold                                    | 4,807                                | 4,124           |
| Research and development                                 | 798                                  | 739             |
| Selling, general and administrative                      | 2,890                                | 2,692           |
| <b>Operating Profit</b>                                  | <b>3,369</b>                         | <b>3,023</b>    |
| Interest   | 313                                  | 297             |
| <b>Income before income taxes and minority interests</b> | <b>3,056</b>                         | <b>2,726</b>    |
| Income tax expense                                       | (921)                                | (734)           |
| Minority interests                                       | (168)                                | (121)           |
| <b>Net income</b>  | <b>\$ 1,967</b>                      | <b>\$ 1,871</b> |
| <b>Earnings per share of Common Stock:</b>               |                                      |                 |
| Basic  | \$ 2.03                              | \$ 1.90         |
| Diluted  | \$ 1.98                              | \$ 1.85         |
| <b>Dividends per share of Common Stock</b>               | <b>\$ .53</b>                        | <b>\$ .49</b>   |
| <b>Average number of shares outstanding:</b>             |                                      |                 |
| Basic  | 967                                  | 984             |
| Diluted  | 991                                  | 1,009           |

See accompanying Notes to Condensed Consolidated Financial Statements

**Table of Contents****CONDENSED CONSOLIDATED BALANCE SHEET****(Unaudited)**

| In Millions   | June 30,<br>2007 | December 31,<br>2006 |
|---|------------------|----------------------|
| <b>Assets</b>   |                  |                      |
| Cash and cash equivalents                             | \$ 3,292         | \$ 2,546             |
| Accounts receivable, net                              | 8,428            | 7,679                |
| Inventories and contracts in progress, net            | 7,974            | 6,657                |
| Future income tax benefits                            | 1,330            | 1,261                |
| Other current assets                                  | 688              | 701                  |
| <b>Total Current Assets</b>                           | <b>21,712</b>    | <b>18,844</b>        |
| Customer financing assets                             | 971              | 1,073                |
| Future income tax benefits                            | 1,648            | 1,690                |
| Fixed assets  | 14,166           | 13,738               |
| Less: Accumulated depreciation                        | (8,291)          | (8,013)              |
| <b>Net Fixed Assets</b>                               | <b>5,875</b>     | <b>5,725</b>         |
| Goodwill  | 14,610           | 14,146               |
| Intangible assets                                     | 3,284            | 3,216                |
| Other assets  | 2,457            | 2,447                |
| <b>Total Assets</b>                                   | <b>\$ 50,557</b> | <b>\$ 47,141</b>     |
| <b>Liabilities and Shareowners' Equity</b>            |                  |                      |
| Short-term borrowings                                 | \$ 1,513         | \$ 857               |
| Accounts payable                                      | 5,100            | 4,263                |
| Accrued liabilities                                   | 10,323           | 10,051               |
| Long-term debt currently due                          | 35               | 37                   |
| <b>Total Current Liabilities</b>                      | <b>16,971</b>    | <b>15,208</b>        |
| Long-term debt  | 7,045            | 7,037                |
| Future pension and postretirement benefit obligations | 2,220            | 2,926                |
| Other long-term liabilities                           | 4,241            | 3,837                |
| <b>Total Liabilities</b>                              | <b>30,477</b>    | <b>29,008</b>        |
| Minority interests in subsidiary companies            | 885              | 836                  |
| Shareowners' Equity:                                  |                  |                      |
| Common Stock  | 10,205           | 9,622                |
| Treasury Stock  | (10,343)         | (9,413)              |
| Retained earnings                                     | 20,123           | 18,754               |
| Unearned ESOP shares                                  | (219)            | (227)                |
| Accumulated other non-shareowners' changes in equity  | (571)            | (1,439)              |
| <b>Total Shareowners' Equity</b>                      | <b>19,195</b>    | <b>17,297</b>        |
| <b>Total Liabilities and Shareowners' Equity</b>      | <b>\$ 50,557</b> | <b>\$ 47,141</b>     |

See accompanying Notes to Condensed Consolidated Financial Statements

**Table of Contents****CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS****(Unaudited)**

| <b>In Millions</b>  | <b>Six Months Ended</b> |                 |
|---|-------------------------|-----------------|
|   | <b>June 30,</b>         |                 |
|   | <b>2007</b>             | <b>2006</b>     |
| <b>Operating Activities:</b>  |                         |                 |
| Net income  | \$ 1,967                | \$ 1,871        |
| Adjustments to reconcile net income to net cash flows provided by operating activities: |                         |                 |
| Depreciation and amortization   | 555                     | 520             |
| Deferred income tax provision   | (160)                   | (1)             |
| Minority interests in subsidiaries earnings   | 168                     | 121             |
| Stock compensation cost   | 97                      | 91              |
| Change in:  |                         |                 |
| Accounts receivable   | (606)                   | (423)           |
| Inventories and contracts in progress   | (1,199)                 | (1,100)         |
| Accounts payable and accrued liabilities  | 1,408                   | 845             |
| Other current assets  | 2                       | (63)            |
| Voluntary contributions to global pension plans*  |                         |                 |
| Other, net  | (330)                   | (74)            |
| <b>Net cash flows provided by operating activities</b>                                  | <b>1,902</b>            | <b>1,787</b>    |
| <b>Investing Activities:</b>  |                         |                 |
| Capital expenditures  | (459)                   | (419)           |
| Investments in businesses   | (370)                   | (372)           |
| Dispositions of businesses  | 162                     | 215             |
| Increase in customer financing assets, net  | (23)                    | (99)            |
| Other, net  | 153                     | 15              |
| <b>Net cash flows used in investing activities</b>                                      | <b>(537)</b>            | <b>(660)</b>    |
| <b>Financing Activities:</b>  |                         |                 |
| Issuance (repayment) of long-term debt, net   | (40)                    | 1,087           |
| Increase (decrease) in short-term borrowings, net                                       | 634                     | (640)           |
| Common Stock issued under employee stock plans  | 264                     | 215             |
| Dividends paid on Common Stock  | (490)                   | (456)           |
| Repurchase of Common Stock  | (1,000)                 | (750)           |
| Other, net  | (59)                    | 23              |
| <b>Net cash flows used in financing activities</b>                                      | <b>(691)</b>            | <b>(521)</b>    |
| <b>Effect of foreign exchange rate changes on Cash and cash equivalents</b>             | <b>72</b>               | <b>30</b>       |
| <b>Net increase in Cash and cash equivalents</b>  | <b>746</b>              | <b>636</b>      |
| <b>Cash and cash equivalents, beginning of year</b>                                     | <b>2,546</b>            | <b>2,247</b>    |
| <b>Cash and cash equivalents, end of period</b>   | <b>\$ 3,292</b>         | <b>\$ 2,883</b> |

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



See accompanying Notes to Condensed Consolidated Financial Statements

**Table of Contents****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)**

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

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

**Business Acquisitions.** During the first six months of 2007, our investment in businesses was approximately \$418 million, including debt assumed of approximately \$48 million, and consisted of a number of small acquisitions in both the commercial and aerospace businesses. The assets and liabilities of acquired businesses are recorded at fair value at the date of acquisition under the purchase method. The final purchase price allocation of all acquired businesses is subject to the completion of the valuation of certain assets and liabilities, as well as plans for consolidation of facilities, the relocation or reduction of employees and other restructuring activities.

On July 2, 2007, we closed on the previously announced acquisition of Initial Electronic Security Group (IESG), a division of Rentokil Initial, plc, with the exception of the French operations, which are pending regulatory review. The purchase price of the acquired portion was approximately \$1.1 billion. The acquisition of IESG is expected to enhance UTC Fire & Security's scale and capability in the electronic security business in key markets where we have a significant presence. IESG sells integrated security systems, intrusion detection, closed circuit television, access control and security software. It is headquartered in the United Kingdom, with operations in the United Kingdom, the Netherlands, France and the United States, and had sales of approximately \$580 million in 2006. We also intend to divest UTC Fire & Security's manned guarding businesses in Australia, New Zealand and the United Kingdom. The combined revenues of these guarding businesses are approximately \$600 million annually. The acquisition of IESG, coupled with the divestiture of these low-technology manned guarding businesses, is intended to assist in the transition of UTC Fire & Security's portfolio towards higher margin and growth opportunities.

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

| In Millions          | Balance as of<br>January 1, 2007 | Goodwill resulting<br>from business<br>combinations | Foreign currency<br>translation and other | Balance as of<br>June 30, 2007 |
|----------------------|----------------------------------|---|---|--------------------------------|
| Otis                 | \$ 1,305                         | \$ 14   | \$ 4                                      | \$ 1,323                       |
| Carrier              | 2,604                            | 179   | 20  | 2,803                          |
| UTC Fire & Security  | 4,430                            | 103   | 58  | 4,591                          |
| Pratt & Whitney      | 1,002                            | 12  |   | 1,014                          |
| Hamilton Sundstrand  | 4,525                            | 46  | 12  | 4,583                          |
| Sikorsky             | 192                              | 17  | 1   | 210                            |
| Total Segments       | 14,058                           | 371   | 95  | 14,524                         |
| Eliminations & Other | 88                               |   | (2)                                       | 86                             |
| Total                | \$ 14,146                        | \$ 371  | \$ 93                                     | \$ 14,610                      |

The majority of the \$464 million increase in goodwill pertains to the finalization of purchase accounting completed in the preceding twelve months.

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

| In Millions                               | June 30, 2007 |                          | December 31, 2006 |                          |
|---|---------------|--------------------------|-------------------|--------------------------|
|   | Gross Amount  | Accumulated Amortization | Gross Amount      | Accumulated Amortization |
| <b>Amortizable:</b>                       |               |                          |                   |                          |
| Service portfolios                        | \$ 1,356      | \$ (560)                 | \$ 1,304          | \$ (507)                 |
| Patents and trademarks                    | 369           | (87)                     | 362               | (79)                     |
| Other, principally customer relationships | 1,997         | (528)                    | 1,845             | (421)                    |
|   | 3,722         | (1,175)                  | 3,511             | (1,007)                  |
| <b>Unamortizable:</b>                     |               |                          |                   |                          |
| Trademarks and other                      | 737           |                          | 712               |                          |
| Totals                                    | \$ 4,459      | \$ (1,175)               | \$ 4,223          | \$ (1,007)               |

Amortization of intangible assets for the quarter and six months ended June 30, 2007 was \$79 million and \$151 million, respectively, compared with \$65 million and \$132 million for the same periods of 2006. Amortization of these intangible assets for 2007 through 2011 is expected to approximate \$240 million per year.

**Note 2: Earnings Per Share**

| (In millions except per share amounts) | Quarter Ended<br>June 30, |          | Six Months Ended<br>June 30, |          |
|--|---------------------------|----------|------------------------------|----------|
|  | 2007                      | 2006     | 2007                         | 2006     |
| Net income                             | \$ 1,148                  | \$ 1,103 | \$ 1,967                     | \$ 1,871 |
| Average shares:                        |                           |          |                              |          |
| Basic                                  | 966                       | 983      | 967                          | 984      |
| Stock awards                           | 24                        | 26       | 24                           | 25       |
| Diluted                                | 990                       | 1,009    | 991                          | 1,009    |
| Earnings per share of Common Stock:    |                           |          |                              |          |
| Basic                                  | \$ 1.19                   | \$ 1.12  | \$ 2.03                      | \$ 1.90  |
| Diluted                                | \$ 1.16                   | \$ 1.09  | \$ 1.98                      | \$ 1.85  |

**Note 3: Inventories and Contracts in Progress**

Inventories consist of the following:

| In Millions           | June 30, | December 31, |
|-----------------------|----------|--------------|
|                       | 2007     | 2006         |
| Raw materials         | \$ 1,172 | \$ 1,082     |
| Work-in-process       | 2,716    | 2,409        |
| Finished goods        | 3,892    | 2,956        |
| Contracts in progress | 4,243    | 3,603        |

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|  |          |          |
|--|----------|----------|
|  | 12,023   | 10,050   |
| Less:  |          |          |
| Progress payments, secured by lien, on U.S. Government contracts | (309)    | (259)    |
| Billings on contracts in progress                                | (3,740)  | (3,134)  |
|  | \$ 7,974 | \$ 6,657 |

**Note 4: Borrowings and Lines of Credit**

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

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acquisitions. As of June 30, 2007, approximately \$650 million had been borrowed against this revolving credit agreement to fund general corporate purchases and in anticipation of the IESG acquisition funding requirements. This credit agreement expires in November 2011.

As of June 30, 2007, we could issue additional debt and equity securities of up to \$900 million under a shelf registration statement on file with the Securities and Exchange Commission.

**Note 5: Income Taxes**

We adopted the provisions of Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes, on January 1, 2007. As a result of this adoption, we recognized a charge of approximately \$19 million to the January 1, 2007 retained earnings balance. As of the adoption date, we had gross tax-affected unrecognized tax benefits of \$815 million of which \$604 million, if recognized, would affect the effective tax rate. Also as of the adoption date, we had accrued interest expense related to the unrecognized tax benefits of \$142 million. We recognize interest accrued related to unrecognized tax benefits in interest expense. Penalties, if incurred, would be recognized as a component of income tax expense. In the normal course of business, we provide for uncertain tax positions and adjust our unrecognized tax benefits, including related interest, accordingly. In the second quarter of 2007, those adjustments were not significant.

We conduct business globally and, as a result, UTC or one or more of our subsidiaries files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. In the normal course of business, we are subject to examination by taxing authorities throughout the world, including such major jurisdictions as Australia, Canada, China, France, Germany, Hong Kong, Italy, Japan, Korea, Singapore, Spain, the U.K. and the United States. With few exceptions, we are no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations for years before 1995.

We are currently under audit by the Internal Revenue Service (IRS) for tax years 2000 through 2005. We have received and are reviewing the initial IRS audit report for the 2000 to 2003 tax years. We expect that several proposed adjustments will be disputed at the Appeals Division of the IRS. Although the timing and outcome of tax settlements are uncertain, it is reasonably possible that at various points over the next twelve months a reduction in unrecognized tax benefits may occur in the range of \$100 to \$125 million, a substantial portion of which would not impact the effective tax rate. The potential reduction relates primarily to adjustments for foreign income inclusions and related foreign tax credits, export income exclusions, and research and experimentation credits.

**Note 6: Employee Benefit Plans**

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

| In Millions                 | Quarter Ended |               | Six Months Ended |               |
|-----------------------------|---------------|---------------|------------------|---------------|
|                             | June 30, 2007 | June 30, 2006 | June 30, 2007    | June 30, 2006 |
| Defined Benefit Plans:      |               |               |                  |               |
| Voluntary                   | \$            | \$            | \$               | \$            |
| Mandatory                   | 13            | 22            | 28               | 39            |
| Total Defined Benefit Plans | \$ 13         | \$ 22         | \$ 28            | \$ 39         |
| Defined Contribution Plans  | \$ 49         | \$ 48         | \$ 106           | \$ 102        |

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

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



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approximately \$620 million. There was no effect on our results of operations. The remaining provisions of SFAS 158 were effective for fiscal years ending after December 15, 2006 and, as such, were adopted during 2006.

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

| In Millions                         | Pension Benefits |        | Other Postretirement Benefits |      |
|-------------------------------------|------------------|--------|-------------------------------|------|
|                                     | Quarter Ended    |        | Quarter Ended                 |      |
|                                     | 2007             | 2006   | 2007                          | 2006 |
| Service cost                        | \$ 110           | \$ 110 | \$ 1                          | \$ 2 |
| Interest cost                       | 294              | 281    | 14                            | 14   |
| Expected return on plan assets      | (387)            | (352)  |                               | (1)  |
| Amortization                        | 9                | 10     | (2)                           | (6)  |
| Recognized actuarial net loss       | 64               | 81     |                               |      |
|                                     | 90               | 130    | 13                            | 9    |
| Net settlement and curtailment loss |                  | 4      |                               |      |
| Total net periodic benefit cost     | \$ 90            | \$ 134 | \$ 13                         | \$ 9 |

| In Millions                         | Pension                   |        | Other Postretirement      |       |
|-------------------------------------|---------------------------|--------|---------------------------|-------|
|                                     | Benefits Six Months Ended |        | Benefits Six Months Ended |       |
|                                     | 2007                      | 2006   | 2007                      | 2006  |
| Service cost                        | \$ 218                    | \$ 218 | \$ 2                      | \$ 4  |
| Interest cost                       | 587                       | 560    | 28                        | 28    |
| Expected return on plan assets      | (768)                     | (704)  | (1)                       | (2)   |
| Amortization                        | 18                        | 18     | (4)                       | (12)  |
| Recognized actuarial net loss       | 126                       | 162    |                           |       |
|                                     | 181                       | 254    | 25                        | 18    |
| Net settlement and curtailment loss |                           | 6      |                           |       |
| Total net periodic benefit cost     | \$ 181                    | \$ 260 | \$ 25                     | \$ 18 |

**Note 7: Restructuring and Related Costs**

During the first six months of 2007, we recorded net pre-tax restructuring and related charges/(credits) in our business segments totaling \$60 million for new and ongoing restructuring actions as follows:

| In Millions         |      |
|---------------------|------|
| Otis                | \$ 5 |
| Carrier             | 13   |
| UTC Fire & Security | 6    |
| Pratt & Whitney     | 27   |

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|                     |       |
|---------------------|-------|
| Hamilton Sundstrand | 12    |
| Sikorsky            | (3)   |
| Totals              | \$ 60 |

The net charges included \$41 million in cost of sales, \$20 million in selling, general and administrative expenses and (\$1) million in other income and, as described below, relate to actions initiated during 2007 and 2006 and trailing costs related to certain 2005 actions.

**2007 Actions.** During the first six months of 2007, we initiated restructuring actions relating to ongoing cost reduction efforts, including workforce reductions and the consolidation of manufacturing facilities. We recorded net pre-tax



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restructuring and related charges totaling \$34 million, including \$10 million in cost of sales and \$24 million in selling, general and administrative expenses.

As of June 30, 2007, net workforce reductions of approximately 300 employees of an expected 700 employees have been completed, with 450,000 net square feet of facilities expected to be exited. The majority of the remaining workforce and all facility related cost reduction actions are targeted for completion during 2007.

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

| In Millions                              | Severance | Asset<br>Write-Downs | Termination                            |       |
|--|-----------|----------------------|--|-------|
|  |           |                      | Facility<br>Exit<br>and Lease<br>Costs | Total |
| Restructuring accruals at March 31, 2007 | \$ 13     | \$                   | \$ 7                                   | \$ 20 |
| Net pre-tax restructuring charges        | 9         |                      | 2                                      | 11    |
| Utilization                              | (4)       |                      | (1)                                    | (5)   |
| Balance at June 30, 2007                 | \$ 18     | \$                   | \$ 8                                   | \$ 26 |

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

| In Millions                                 | Severance | Asset<br>Write-Downs | Termination                            |       |
|---|-----------|----------------------|--|-------|
|   |           |                      | Facility<br>Exit<br>and Lease<br>Costs | Total |
| Expected costs                              | \$ 28     | \$ 1                 | \$ 30                                  | \$ 59 |
| Costs incurred quarter ended March 31, 2007 | (14)      | (1)                  | (8)                                    | (23)  |
| Costs incurred quarter ended June 30, 2007  | (9)       |                      | (2)                                    | (11)  |
| Remaining costs at June 30, 2007            | \$ 5      | \$                   | \$ 20                                  | \$ 25 |

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

| In Millions         | Expected<br>Costs | Costs Incurred                     |                                   | Remaining                    |
|---------------------|-------------------|------------------------------------|-----------------------------------|------------------------------|
|                     |                   | Quarter Ended<br>March 31,<br>2007 | Quarter Ended<br>June 30,<br>2007 | Costs at<br>June 30,<br>2007 |
| Otis                | \$ 12             | \$ (1)                             | \$ (7)                            | \$ 4                         |
| Carrier             | 16                | (13)                               | (1)                               | 2                            |
| UTC Fire & Security | 2                 | (1)                                | (1)                               |                              |
| Pratt & Whitney     | 27                | (8)                                | (1)                               | 18                           |
| Hamilton Sundstrand | 1                 |                                    | (1)                               |                              |

|          |    |    |    |      |    |      |    |    |
|----------|----|----|----|------|----|------|----|----|
| Sikorsky |    |    |    |      | 1  | 1    |    |    |
| Total    | \$ | 59 | \$ | (23) | \$ | (11) | \$ | 25 |

**2006 Actions.** During the first six months of 2007, we recorded net pre-tax restructuring and related charges/(credits) in the business segments totaling \$11 million for restructuring actions initiated in 2006, including \$10 million in cost of sales and \$1 million in selling, general and administrative expenses. The 2006 actions relate to ongoing cost reduction efforts including workforce reductions and the consolidation of manufacturing facilities.

As of June 30, 2007, net workforce reductions of approximately 2,600 employees of an expected 3,800 employees have been completed, and 100,000 net square feet of facilities of an expected 600,000 net square feet have been exited. The majority of the remaining workforce and facility related cost reduction actions are targeted for completion during 2007.

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The following table summarizes the accrual balances and utilization by cost type for the 2006 restructuring actions:

| In Millions                              | Severance | Asset<br>Write-Downs | Facility<br>Exit<br>and Lease | Total |
|--|-----------|----------------------|-------------------------------|-------|
|  |           |                      | Termination<br>Costs          |       |
| Restructuring accruals at March 31, 2007 | \$ 27     | \$                   | \$ 8                          | \$ 35 |
| Net pre-tax restructuring charges        |           | 1                    | 8                             | 9     |
| Utilization                              | (11)      | (1)                  | (7)                           | (19)  |
| Balance at June 30, 2007                 | \$ 16     | \$                   | \$ 9                          | \$ 25 |

The following table summarizes expected, incurred and remaining costs for the 2006 restructuring actions by type:

| In Millions   | Severance | Asset<br>Write-Downs | Facility<br>Exit<br>and Lease | Total  |
|---|-----------|----------------------|-------------------------------|--------|
|   |           |                      | Termination<br>Costs          |        |
| Expected costs  | \$ 180    | \$ 13                | \$ 71                         | \$ 264 |
| Costs incurred through December 31, 2006                | (179)     | (12)                 | (29)                          | (220)  |
| Reversals (costs incurred) quarter ended March 31, 2007 | 2         |                      | (4)                           | (2)    |
| Costs incurred quarter ended June 30, 2007              |           | (1)                  | (8)                           | (9)    |
| Remaining costs at June 30, 2007                        | \$ 3      | \$                   | \$ 30                         | \$ 33  |

The following table summarizes expected, incurred and remaining costs for the 2006 restructuring actions by segment:

| In Millions         | Expected<br>Costs | Costs Incurred<br>through<br>December 31, | Costs Incurred<br>Quarter Ended<br>March 31, | Costs Incurred<br>Quarter Ended<br>June 30, | Remaining<br>Costs at<br>June 30, |
|---------------------|-------------------|---|--|---|-----------------------------------|
|                     |                   | 2006                                      | 2007   | 2007  | 2007                              |
| Otis                | \$ 46             | \$ (47)                                   | \$ 1   | \$  | \$                                |
| Carrier             | 64                | (61)                                      | (1)  |   | 2                                 |
| UTC Fire & Security | 51                | (40)                                      | (1)  | (3)   | 7                                 |
| Pratt & Whitney     | 79                | (46)                                      | (3)  | (6)   | 24                                |
| Hamilton Sundstrand | 6                 | (5)                                       | (1)  |   |                                   |
| Sikorsky            | 18                | (21)                                      | 3  |   |                                   |
| Total               | \$ 264            | \$ (220)                                  | \$ (2)                                       | \$ (9)                                      | \$ 33                             |

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**2005 and Prior Actions.** During the first six months of 2007, we recorded net pre-tax restructuring and related charges/(credits) in our business segments totaling \$15 million for restructuring actions initiated in 2005 and prior years, including \$21 million in cost of sales, (\$5) million in selling, general and administrative expenses, and (\$1) million in other income. These actions relate to ongoing cost reduction efforts, including workforce reductions and the consolidation of manufacturing sales and service facilities, including the closure of a portion of Hamilton Sundstrand's Rockford manufacturing facility.

As of June 30, 2007, net workforce reductions of approximately 2,700 employees of an expected 2,900 employees have been completed, and 700,000 net square feet of facilities of an expected 1.2 million net square feet have been exited. The remaining facility related cost reductions will be completed through 2008 as a result of aerospace supply chain issues.

The following table summarizes the accrual balances and utilization by cost type for the 2005 and prior restructuring actions:

| In Millions                              | Severance | Asset<br>Write-Downs | Facility<br>Exit<br>and Lease | Total |
|--|-----------|----------------------|-------------------------------|-------|
|  |           |                      | Termination<br>Costs          |       |
| Restructuring accruals at March 31, 2007 | \$ 5      | \$                   | \$ 15                         | \$ 20 |
| Net pre-tax restructuring charges        |           |                      | 5                             | 5     |
| Utilization                              | (1)       |                      | (6)                           | (7)   |
| Balance at June 30, 2007                 | \$ 4      | \$                   | \$ 14                         | \$ 18 |

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The following table summarizes expected, incurred and remaining costs for the 2005 and prior restructuring actions by type:

| In Millions   | Severance | Asset<br>Write-Downs | Facility<br>Exit<br>and Lease<br>Costs | Termination<br>Costs | Total  |
|---|-----------|----------------------|--|----------------------|--------|
|   |           |                      |  |                      |        |
| Expected costs  | \$ 132    | \$ 45                | \$ 88                                  |                      | \$ 265 |
| Costs incurred through December 31, 2006                | (139)     | (38)                 | (64)                                   |                      | (241)  |
| Reversals (costs incurred) quarter ended March 31, 2007 | 7         | (7)                  | (10)                                   |                      | (10)   |
| Costs incurred quarter ended June 30, 2007              |           |                      | (5)                                    |                      | (5)    |
| Remaining costs at June 30, 2007                        | \$        | \$                   | \$ 9                                   |                      | \$ 9   |

The following table summarizes expected, incurred and remaining costs for the 2005 and prior restructuring actions by segment:

| In Millions          | Expected<br>Costs | Costs Incurred<br>through<br>December 31,<br>2006 | Costs<br>Incurred<br>Quarter Ended<br>March 31,<br>2007 | Costs<br>Incurred<br>Quarter Ended<br>June 30,<br>2007 | Remaining<br>Costs at<br>June 30,<br>2007 |
|----------------------|-------------------|---|---|--|---|
|                      |                   |   |   |  |   |
| Otis                 | \$ 49             | \$ (51)   | \$ 2  | \$   | \$  |
| Carrier              | 67                | (69)  | 2   |  |   |
| UTC Fire & Security  | 25                | (25)  |   |  |   |
| Pratt & Whitney      | 44                | (31)  | (9)   |  | 4   |
| Hamilton Sundstrand  | 71                | (56)  | (5)   | (5)  | 5   |
| Sikorsky             | 3                 | (3)   |   |  |   |
| Eliminations & Other | 6                 | (6)   |   |  |   |
| Total                | \$ 265            | \$ (241)  | \$ (10)   | \$ (5)   | \$ 9                                      |

**Note 8: Derivative Instruments and Hedging Activities**

We use derivative instruments, including swaps, forward contracts and options to manage certain foreign currency, commodity and interest rate exposures. We view derivative instruments as risk management tools and do not use them for trading or speculative purposes. Derivatives used for hedging purposes must be designated and effective as a hedge of the identified risk exposure at the inception of the contract. Accordingly, changes in the fair value of the derivative contract must be highly correlated with changes in the fair value of the underlying hedged item at inception of the hedge and over the life of the hedge contract.

At June 30, 2007 and December 31, 2006, the fair value of derivatives recorded as assets was \$157 million and \$93 million, respectively, and the fair value of derivatives recorded as liabilities was \$89 million and \$98 million, respectively. Of the amount recorded in shareowners' equity, a \$78 million pre-tax gain is expected to be reclassified into sales or cost of products sold to reflect the fixed prices obtained from hedging within the next 12 months. Gains and losses recognized in earnings related to the ineffectiveness of cash flow hedges during the quarter ended June 30, 2007 were not significant. All open derivative contracts accounted for as cash flow hedges mature by December 2010.

**Table of Contents****Note 9: Shareowners Equity**

A summary of the changes in shareowners equity for the quarters and six months ended June 30, 2007 and 2006 is provided below:

| In Millions   | Quarter Ended<br>June 30, |           | Six Months Ended<br>June 30, |           |
|---|---------------------------|-----------|------------------------------|-----------|
|   | 2007                      | 2006      | 2007                         | 2006      |
| Shareowners Equity, beginning of period   | \$ 18,106                 | \$ 17,357 | \$ 17,297                    | \$ 16,991 |
| Effects of changing pension plan measurement dates pursuant to SFAS No. 158, net of taxes |                           |           | 425                          |           |
| Adoption of FASB Interpretation No. 48  |                           |           | (19)                         |           |
|   | \$ 18,106                 | \$ 17,357 | \$ 17,703                    | \$ 16,991 |
| Common Stock issued under employee plans  | 240                       | 227       | 489                          | 416       |
| Common Stock repurchased  | (485)                     | (375)     | (1,000)                      | (750)     |
| Common Stock contributed to pension plans   |                           | 150       | 150                          | 150       |
| Dividends paid on Common Stock  | (245)                     | (249)     | (490)                        | (456)     |
| Dividends paid on ESOP Common Stock   | (11)                      | (10)      | (22)                         | (21)      |
| Non-shareowners Changes in Equity:  |                           |           |                              |           |
| Net income  | 1,148                     | 1,103     | 1,967                        | 1,871     |
| Foreign currency translation, net   | 312                       | 257       | 334                          | 274       |
| Increases (decreases) in unrealized gains from available-for-sale investments, net        | 2                         | (18)      | (84)                         | (24)      |
| Cash flow hedging (income) loss, net  | 108                       | 6         | 81                           | (3)       |
| Change in pension and post-retirement benefit plans, net                                  | 20                        |           | 67                           |           |
| Shareowners Equity, end of period   | \$ 19,195                 | \$ 18,448 | \$ 19,195                    | \$ 18,448 |

**Note 10: Guarantees**

We extend a variety of financial, market value and product performance guarantees to third parties. There have been no material changes to guarantees outstanding since December 31, 2006.

The changes in the carrying amount of service and product warranties and product performance guarantees for the six months ended June 30, 2007 and 2006 are as follows:

| In Millions                                  | 2007     | 2006     |
|--|----------|----------|
| Balance as of January 1                      | \$ 1,321 | \$ 1,183 |
| Warranties and performance guarantees issued | 172      | 263      |
| Settlements made                             | (255)    | (194)    |
| Other  | 6        | 9        |
| Balance as of June 30                        | \$ 1,244 | \$ 1,261 |

**Note 11: Contingent Liabilities**

Summarized below are the matters previously described in Notes 1 and 14 of the Notes to the Consolidated Financial Statements in our Annual Report, incorporated by reference in our Form 10-K for calendar year 2006.

**Environmental.** Our operations are subject to environmental regulation by federal, state and local authorities in the United States and regulatory authorities with jurisdiction over our foreign operations.

Environmental investigatory, remediation, operating and maintenance costs are accrued when it is probable that a liability has been incurred and the amount can be reasonably estimated. The most likely of these costs to be incurred is accrued based on an evaluation of currently available facts with respect to each individual site, including existing technology, current laws and regulations and prior remediation experience. Where no amount within a range of estimates is more likely, the minimum is accrued. For sites with multiple responsible parties, we consider our likely proportionate share of the anticipated remediation costs and the ability of the other parties to fulfill their obligations in establishing a provision for those costs. Liabilities with fixed or reliably determinable future cash payments are discounted. Accrued environmental liabilities are not reduced by potential insurance reimbursements. We periodically reassess these accrued amounts. We believe that the likelihood of incurring losses materially in excess of amounts accrued is remote.

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**Government.** We are now, and believe that in light of the current U.S. government contracting environment we will continue to be, the subject of one or more U.S. government investigations. If we or one of our business units were charged with wrongdoing as a result of any of these investigations or other government investigations (including violations of certain environmental or export laws) the U.S. government could suspend us from bidding on or receiving awards of new U.S. government contracts pending the completion of legal proceedings. If convicted or found liable, the U.S. government could fine us and debar us from new U.S. government contracting for a period generally not to exceed three years. The U.S. government could void any contracts found to be tainted by fraud.

Our contracts with the U.S. government are also subject to audits. Like many defense contractors, we have received audit reports, which recommend that certain contract prices should be reduced to comply with various government regulations. Some of these audit reports involve substantial amounts. We have made voluntary refunds in those cases we believe appropriate and continue to litigate certain cases. In addition, we accrue for liabilities associated with those matters that are probable and can be reasonably estimated.

As previously disclosed, the U.S. Department of Justice (DoJ) sued us in 1999 under the civil False Claims Act and other theories related to the Fighter Engine Competition between Pratt & Whitney's F100 engine and GE's F110 engine. The DoJ alleges that the government overpaid for engines because Pratt & Whitney inflated certain costs and withheld data. The U.S. government claims damages of \$624 million. We deny any liability, believe this estimate of damages is substantially overstated, and are vigorously defending the matter. Trial of this matter was completed in December 2004 and a decision is pending.

Should the U.S. government ultimately prevail with respect to the foregoing government contracting matter, the outcome could result in a material effect on our results of operations in the period in which a liability would be recognized or cash flows for the period in which damages would be paid. However, we believe that the resolution of this matter will not have a material adverse effect on our results of operations, competitive position, cash flows or financial condition.

As previously reported, the European Commission's Competition Directorate (EU Commission) conducted inspections in early 2004 at offices of our Otis subsidiary in Berlin, Brussels, Luxembourg and Paris relating to an investigation of possible unlawful collusive arrangements involving the European elevator and escalator industry. On February 21, 2007, the EU Commission ruled that Otis subsidiaries in Belgium, Luxembourg and the Netherlands, and a portion of the business of Otis German subsidiary, violated EU competition rules and assessed a 225 million Euro (approximately \$300 million) civil fine against Otis, its relevant local entities, and UTC. We paid \$88 million of the fine in March 2007. The remaining \$212 million was deposited into a trust that disbursed the funds to the EU Commission in May 2007. The charge for the fine, net of previously established reserves of approximately \$80 million, was recorded in cost of sales in the first quarter of 2007 and is included in Eliminations and Other for segment reporting. In May 2007, we filed an appeal of the decision before the European Court of First Instance. Resolution of this matter is not expected within the next twelve months.

**Other.** We extend performance and operating cost guarantees beyond our normal warranty and service policies for extended periods on some of our products. We have accrued our estimate of liability that may result under these guarantees and for service costs which are probable and can be reasonably estimated.

We also have other commitments and contingent liabilities related to legal proceedings, self insurance programs and matters arising out of the normal course of business.

We have accrued for environmental investigatory, remediation, operating and maintenance costs, performance guarantees and other litigation and claims based on our estimate of the probable outcome of these matters. While it is possible that the outcome of these matters may differ from the recorded liability, we believe that resolution of these matters will not have a material impact on our financial condition, results of operations or cash flows.

### **Note 12: Segment Financial Data**

Our operations are classified into six principal segments: Otis, Carrier, UTC Fire & Security, Pratt & Whitney, Hamilton Sundstrand and Sikorsky. The segments are generally based on the management structure of the businesses and the groupings of similar operating companies, where each management organization has general operating autonomy over diversified products and services.



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Results for the quarters and six months ended June 30, 2007 and 2006 are as follows:

| Quarter Ended June 30,<br>(In Millions) | Revenues  |           | Operating Profits |          | Operating Profit Margin |       |
|---|-----------|-----------|-------------------|----------|-------------------------|-------|
|   | 2007      | 2006      | 2007              | 2006     | 2007                    | 2006  |
|   | Otis      | \$ 2,858  | \$ 2,529          | \$ 532   | \$ 472                  | 18.6% |
| Carrier                                 | 4,055     | 3,751     | 489               | 410      | 12.1%                   | 10.9% |
| UTC Fire & Security                     | 1,349     | 1,167     | 101               | 65       | 7.5%                    | 5.6%  |
| Pratt & Whitney                         | 3,108     | 2,727     | 522               | 535      | 16.8%                   | 19.6% |
| Hamilton Sundstrand                     | 1,404     | 1,281     | 246               | 212      | 17.5%                   | 16.5% |
| Sikorsky                                | 1,198     | 767       | 87                | 42       | 7.3%                    | 5.5%  |
| Total segment                           | 13,972    | 12,222    | 1,977             | 1,736    | 14.1%                   | 14.2% |
| Eliminations & Other                    | (68)      | 42        | (20)              | 84       |                         |       |
| General corporate expenses              |           |           | (92)              | (79)     |                         |       |
| Consolidated                            | \$ 13,904 | \$ 12,264 | \$ 1,865          | \$ 1,741 | 13.4%                   | 14.2% |

| Six Months Ended June 30,<br>(In Millions) | Revenues  |           | Operating Profits |          | Operating Profit Margin |       |
|--|-----------|-----------|-------------------|----------|-------------------------|-------|
|  | 2007      | 2006      | 2007              | 2006     | 2007                    | 2006  |
|  | Otis      | \$ 5,586  | \$ 4,877          | \$ 1,106 | \$ 911                  | 19.8% |
| Carrier                                    | 7,185     | 6,655     | 702               | 614      | 9.8%                    | 9.2%  |
| UTC Fire & Security                        | 2,595     | 2,279     | 187               | 130      | 7.2%                    | 5.7%  |
| Pratt & Whitney                            | 5,875     | 5,295     | 1,012             | 965      | 17.2%                   | 18.2% |
| Hamilton Sundstrand                        | 2,717     | 2,445     | 464               | 393      | 17.1%                   | 16.1% |
| Sikorsky                                   | 2,204     | 1,279     | 160               | 45       | 7.3%                    | 3.5%  |
| Total segment                              | 26,162    | 22,830    | 3,631             | 3,058    | 13.9%                   | 13.4% |
| Eliminations & Other                       | 20        | 49        | (83)              | 129      |                         |       |
| General corporate expenses                 |           |           | (179)             | (164)    |                         |       |
| Consolidated                               | \$ 26,182 | \$ 22,879 | \$ 3,369          | \$ 3,023 | 12.9%                   | 13.2% |

See Note 7 to the Condensed Consolidated Financial Statements for a discussion of restructuring charges included in segment operating results.

In view of the risks and costs associated with developing new engines, Pratt & Whitney has entered into certain collaboration arrangements in which costs, revenues and risks are shared. Revenues from Pratt & Whitney's engine programs under collaboration agreements are recorded as earned and collaborator share of revenue is recorded as a reduction of revenue at that time. The collaborator share of revenue for the quarters ended June 30, 2007 and 2006 was approximately \$227 million and \$207 million, respectively. For the six months ended June 30, 2007 and 2006, the approximate collaborator share of revenue was \$441 million and \$391 million, respectively.

**Note 13: Accounting Pronouncements**

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities—Including an Amendment of FASB Statement No. 115," which is effective for fiscal years beginning after November 15, 2007. This statement permits an entity to choose to measure many financial instruments and certain other items at fair value on specified election dates. Subsequent unrealized gains and losses on items for which the fair value option has been elected will be reported in earnings. We are currently evaluating the potential impact of this statement.



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With respect to the unaudited condensed consolidated financial information of UTC for the quarter and six months ended June 30, 2007 and 2006, PricewaterhouseCoopers LLP ( PricewaterhouseCoopers ) reported that it has applied limited procedures in accordance with professional standards for a review of such information. However, its report dated July 20, 2007, appearing below, states that the firm did not audit and does not express an opinion on that unaudited condensed consolidated financial information. PricewaterhouseCoopers has not carried out any significant or additional audit tests beyond those that would have been necessary if their report had not been included. Accordingly, the degree of reliance on its report on such information should be restricted in light of the limited nature of the review procedures applied. PricewaterhouseCoopers is not subject to the liability provisions of Section 11 of the Securities Act of 1933 (the Act ) for its report on the unaudited condensed consolidated financial information because that report is not a report or a part of a registration statement prepared or certified by PricewaterhouseCoopers within the meaning of Sections 7 and 11 of the Act.

### **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareowners of United Technologies Corporation:

We have reviewed the accompanying condensed consolidated balance sheet of United Technologies Corporation (the Corporation ) and its subsidiaries as of June 30, 2007, and the related condensed consolidated statements of operations for each of the three-month and six-month periods ended June 30, 2007 and 2006 and the condensed consolidated statements of cash flows for the six-month periods ended June 30, 2007 and 2006. This interim financial information is the responsibility of the Corporation s management.

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

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

As discussed in Note 5 of the condensed consolidated interim financial statements, the Corporation has recognized uncertain tax positions in accordance with the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109*, as of January 1, 2007. As discussed in Note 6 of the condensed consolidated interim financial statements, the Corporation has changed the measurement date of its pension and postretirement plans to be consistent with the Corporation s fiscal year end in accordance with the provisions of FASB Statement No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106 and 132(R)*, as of January 1, 2007.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2006, and the related consolidated statements of operations, of cash flows and of changes in shareowners equity for the year then ended, management s assessment of the effectiveness of the Corporation s internal control over financial reporting as of December 31, 2006 and the effectiveness of the Corporation s internal control over financial reporting as of December 31, 2006; and in our report dated February 8, 2007, we expressed unqualified opinions thereon. The consolidated financial statements and management s assessment of the effectiveness of internal control over financial reporting referred to above are not presented herein. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2006, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP

Hartford, Connecticut

July 20, 2007

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
**BUSINESS OVERVIEW**

We operate in six principal segments: Otis, Carrier, UTC Fire & Security, Pratt & Whitney, Hamilton Sundstrand and Sikorsky. Otis, Carrier and UTC Fire & Security are collectively referred to as the commercial businesses, while Pratt & Whitney, Hamilton Sundstrand and Sikorsky are collectively referred to as the aerospace businesses. The current status of significant factors impacting our business environment in 2007 is discussed below. For additional discussion, refer to the Business Overview section in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report, which is incorporated by reference in our Form 10-K for calendar year 2006.

**General**

As worldwide businesses, our operations are affected by global and regional industrial, economic and political factors. However, our geographic and industry diversity, as well as the diversity of our product sales and services, has helped limit the impact of any one industry or the economy of any single country on our consolidated results.

Global economic conditions remained solid in the first half of 2007, with continued strength in the commercial aerospace markets and positive growth in most commercial markets, with the exception of the U.S. residential new construction market. As noted over the past three quarters, sharp declines in new construction starts, coupled with increases in housing inventories, have continued to adversely impact Carrier's North American residential heating, ventilating and air conditioning (HVAC) business. However, the overall positive economic conditions in other markets and regions across UTC, higher opening order backlogs, and a strong presence in emerging markets generated strong organic revenue growth of 10% in both the first and second quarters of 2007. This organic growth follows the 9% realized in 2006 and the 7% realized in 2005. The increase in organic growth to 10% in the first half of 2007, as compared with the 8% in the first half of 2006, is largely attributable to the absence of the labor strike that adversely affected Sikorsky's operating results in the first half of 2006. As previously disclosed, Sikorsky's union workforce in its Connecticut and Florida facilities were on strike for six weeks during the first quarter of 2006. This resulted in a substantial reduction to aircraft deliveries, spares and overhaul and repair volumes along with a corresponding adverse impact on operating results due to the lower volumes and higher than average manufacturing costs. The first half 2007 revenues reflect the resumption of full production at Sikorsky as well as a significant increase in volume associated with the strong demand for both commercial and military helicopters and services. The favorable impact of foreign currency translation (3%) contributed the majority of the remainder of the 13% total growth in year-over-year revenues in the second quarter.

Strong commercial aerospace aftermarket volume, operational efficiencies, including savings from previously initiated restructuring actions, continued cost containment efforts and favorable impact of foreign currency translation offset higher research and development spending and the adverse impact of higher commodity and energy costs to generate a 7% increase in operating profit in the second quarter of 2007 as compared with the same period in 2006. The benefit received from foreign currency translation, lower restructuring charges and acquisitions was offset by the absence of a gain in connection with a reserve reversal associated with the settlement of a Department of Defense claim against Pratt & Whitney and tax settlement impact that benefited the second quarter of 2006. Increases in energy and certain commodity prices experienced over the last two years continued to adversely impact earnings in the first half of 2007. After a partial recovery through pricing, the net impact to earnings for the six months ended June 30, 2007 was approximately \$178 million. The net impact for the full year 2007 is expected to be approximately \$300 million.

Operating profit for the six months ended June 30, 2007 includes charges for a fine, net of existing reserves, of \$216 million. As previously disclosed, the European Commission's Competition Directorate assessed a civil fine of approximately \$300 million (EU Fine) against Otis, its relevant local entities and UTC, as a result of certain Otis subsidiaries in Europe violating European Union competition rules. Gains from the sale of certain assets and the favorable impact of a contract termination at Pratt & Whitney helped to offset the adverse impact of this fine and restructuring charges, resulting in a net charge to earnings per share of \$.07 in the first quarter of 2007. Incremental restructuring charges had an additional \$.02 adverse impact to earnings per share in the second quarter of 2007.

Weakness of the U.S. dollar against certain currencies such as the Euro generated a positive foreign currency translation impact of \$.03 per share in the second quarter of 2007. Foreign currency translation did not have a significant impact on earnings per share in the second quarter of 2006. For the six months ended June 30, 2007, foreign currency translation had a positive impact of \$.05 per share as compared with a \$.02 per share adverse impact for the same period in 2006.

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### **Commercial Businesses**

Our commercial businesses generally serve customers in the worldwide commercial and residential property industries, although Carrier also serves customers in the commercial and transport refrigeration industries. Revenues in the commercial businesses are influenced by residential and commercial construction activity, domestic and world gross domestic product growth levels, overall global economic conditions and, for Carrier, seasonal weather conditions. To ensure an adequate supply of Carrier products in the distribution channel, Carrier customarily offers its customers incentives to purchase products.

Revenues for Carrier increased in both the quarter and six months ended June 30, 2007 due to strength in commercial construction, international HVAC market which has benefited from favorable weather conditions in Europe, and refrigeration due to a strong first half container market. These conditions more than offset lower residential sales in the U.S. following the continued downturn in the North American residential housing industry. The impact to Carrier of a soft new construction market is exacerbated by Carrier's strong position in this market.

In the second quarter of 2007, Carrier signed a Letter of Intent to acquire an existing HVAC distributor serving customers in Northern California and parts of Nevada. In addition, Carrier launched a company-owned sales and distribution network for its HVAC and Refrigeration products in Southern California following the termination of a contract with a previous distributor in the region. We expect some start-up expenses associated with this initiative, particularly in the third quarter of 2007.

Within the Otis segment, organic revenue growth of 8% in the first half of 2007 was aided by a strong opening new equipment backlog and revenues increased in all geographic regions, led by Asia Pacific and North America. New equipment orders remained strong in the second quarter, up 26% globally with particular strength in North America and Asia Pacific. Prices remain under significant pressure in Asia.

UTC Fire & Security's organic revenue growth in the quarter was 2%, reflecting double digit growth at Lenel and in Asia, while Australia continues to be weak.

### **Aerospace Businesses**

The aerospace businesses serve both commercial and government aerospace customers. In addition, elements of Pratt & Whitney and Hamilton Sundstrand also serve customers in the industrial markets. Revenue passenger miles (RPMs), U.S. government military and space spending, and the general economic health of airline carriers are all barometers for our aerospace businesses. The strong production levels at airframe manufacturers, as well as the continued high usage of aircraft, as evidenced by the growth in RPMs, are supporting our commercial aerospace growth year-to-date. Commercial aftermarket revenue growth of 14% was augmented by strong original equipment manufacture and helicopter growth. Excluding helicopter revenues, military volume was essentially flat. However, positive global economic conditions and government military spending are helping to drive helicopter demand and, as a result, Sikorsky's military and commercial backlog remains very strong at almost \$9 billion. As noted previously, the strike at Sikorsky's Connecticut and Florida facilities in the first quarter of 2006 resulted in significantly lower volumes for comparative purposes. Although helicopter deliveries improved significantly following the resumption of full production, Sikorsky continues to work towards reducing the incremental manufacturing costs that were incurred to accommodate the steep ramp up required to meet production requirements for more complex helicopters and strong backlog. Concurrently, Sikorsky has been reconfiguring manufacturing processes including the sourcing of certain activities and the transfer of work to other manufacturing facilities to increase capacity. These efforts will continue through 2008.

Overall economic conditions are also affecting the cost and availability of raw materials, such as titanium and nickel, as industry demand outpaces current capacity. The availability and pricing of these materials are expected to continue to affect aerospace performance and could have a further adverse impact on future performance depending on market conditions.

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### **Acquisition Activity**

Our growth strategy contemplates acquisitions. The rate and extent to which appropriate acquisition opportunities are available and to which acquired businesses are effectively integrated, and anticipated synergies or cost savings are achieved, can affect our operations and results. During the first six months of 2007, we invested approximately \$418 million in acquisitions across our businesses, including debt assumed (approximately \$48 million), and recorded the excess of the purchase price over the estimated fair value of the assets acquired as an increase in goodwill. As a result of acquisition activity and the finalization of purchase accounting, goodwill has increased approximately \$464 million in the first six months of 2007.

On July 2, 2007, we closed on the previously announced acquisition of Initial Electronic Security Group (IESG), a division of Rentokil Initial, plc, with the exception of the French operations, which are pending regulatory review. The purchase price of the acquired portion was approximately \$1.1 billion. The acquisition of IESG is expected to enhance UTC Fire & Security's scale and capability in the electronic security business in key markets where we have a significant presence. IESG sells integrated security systems, intrusion detection, closed circuit television, access control and security software. It is headquartered in the United Kingdom, with operations in the Netherlands, France and the United States, and had sales of approximately \$580 million in 2006. As part of the integration of IESG into UTC Fire & Security, restructuring actions will be conducted to achieve operational synergies where possible, including the closure of certain facilities. Approximately \$30 million of savings is anticipated from approximately \$55 million of related restructuring charges, of which a portion will be treated under purchase accounting.

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

We continue to expect to invest approximately \$2 billion in acquisitions for 2007, including those announced during the first half of 2007, although this will depend upon the timing and availability of acquisition opportunities.

### **Other**

Government legislation, policies and regulations can have an impact on our worldwide operations. Government regulation of refrigerants and energy efficiency standards, elevator safety codes and fire protection regulations are important to our commercial businesses. Government and market-driven safety and performance regulations, restrictions on aircraft engine noise and emissions and government procurement practices can impact our aerospace and defense businesses.

Commercial airline financial performance, global economic conditions, changes in raw material, energy and commodity prices, interest rates and foreign currency exchange rates create uncertainties that could impact our earnings outlook for the remainder of 2007.

## **CRITICAL ACCOUNTING ESTIMATES**

Preparation of our financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. We believe the most complex and sensitive judgments, because of their significance to the Consolidated Financial Statements, result primarily from the need to make estimates about the effects of matters that are inherently uncertain. Management's Discussion and Analysis and Note 1 to the Consolidated Financial Statements in our Annual Report, incorporated by reference in our Form 10-K for the calendar year 2006, describe the significant accounting estimates and policies used in preparation of the Consolidated Financial Statements. Actual results in these areas could differ from management's estimates. As discussed below and in Notes 5 and 6 to the Condensed Consolidated Financial Statements, we have adopted the provisions of Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes, and the measurement date provisions of Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106 and 132(R), on January 1, 2007. Other than these changes, there have been no significant changes in our critical accounting estimates during the first six months of 2007.

In the ordinary course of business there is inherent uncertainty in quantifying our income tax positions. We assess our income tax positions and record tax benefits for all years subject to examination based upon management's evaluation of the



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facts, circumstances, and information available at the reporting date. For those tax positions where it is more likely than not that a tax benefit will be sustained, we have recorded the largest amount of tax benefit with a greater than 50 percent likelihood of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. For those income tax positions where it is not more likely than not that a tax benefit will be sustained, no tax benefit has been recognized in the financial statements. Where applicable, associated interest has also been recognized.

**RESULTS OF CONTINUING OPERATIONS****Revenues**

| In Millions           | Quarter Ended<br>June 30, |                  |              | Six Months Ended<br>June 30, |                  |              |
|-----------------------|---------------------------|------------------|--------------|------------------------------|------------------|--------------|
|                       | 2007                      | 2006             | % change     | 2007                         | 2006             | % change     |
| Sales                 | \$ 13,766                 | \$ 12,046        | 14.3%        | \$ 25,702                    | \$ 22,492        | 14.3%        |
| Other income, net     | 138                       | 218              | (36.7)%      | 480                          | 387              | 24.0%        |
| <b>Total Revenues</b> | <b>\$ 13,904</b>          | <b>\$ 12,264</b> | <b>13.4%</b> | <b>\$ 26,182</b>             | <b>\$ 22,879</b> | <b>14.4%</b> |

Revenue growth in the second quarter of 2007 includes organic growth of 10%, the favorable impact from foreign currency translation of 3%, resulting from the weakness of the U.S. dollar relative to currencies such as the Euro, and revenue contributed by acquired companies of 1%. A decrease in other income slightly offset these increases. As discussed above in the Business Overview section, the organic revenue growth results principally from strength in the commercial aerospace aftermarket, strong helicopter deliveries and generally favorable economic conditions in most global markets. As also previously noted, the comparative revenue growth was impacted by the reduced volumes at Sikorsky in the second quarter of 2006 as they recovered from the first quarter strike and the weak North American residential revenues at Carrier in the second quarter of 2007 due to the decline in the residential housing market. The comparative decline in residential revenues was exacerbated by the strong North American demand that existed in the second quarter of 2006.

The six month revenue increase of 14.4% consists of organic growth of 10%, the favorable impact of foreign currency translation of 3%, and revenue from acquisitions of 1%. As with the second quarter growth, the six month revenue growth is due largely to the strength in the commercial aerospace aftermarket, overall helicopter demand and generally favorable global economic conditions.

The higher level of other income in the second quarter of 2006, as compared with 2007, is due largely to pretax interest income of approximately \$60 million associated with the final 1994 -1999 settlement with the Appeals Division of the IRS. Other income in the first six months of 2007 includes approximately \$150 million in gains resulting from the sale of marketable securities and an approximately \$80 million gain recognized on the sale of land by Otis. In addition to the interest income noted above, other income for the first six months of 2006 also included a \$25 million gain realized on Pratt & Whitney Canada's sale of an interest in a newly formed partnership designed to expand market share in the commercial turboshaft engine market, and an approximately \$25 million gain generated from the sale of marketable securities.

**Gross Margin**

| In Millions         | Quarter Ended<br>June 30, |          | Six Months Ended<br>June 30, |          |
|---------------------|---------------------------|----------|------------------------------|----------|
|                     | 2007                      | 2006     | 2007                         | 2006     |
| Gross margin        | \$ 3,637                  | \$ 3,271 | \$ 6,577                     | \$ 6,067 |
| Percentage of sales | 26.4%                     | 27.2%    | 25.6%                        | 27.0%    |

Gross margin increases for the second quarter and for the first six months of 2007 resulted from higher volumes, savings from previously initiated restructuring actions, and net operational efficiencies. However, gross margin as a percentage of sales declined by 80 basis points in the second quarter of 2007 as compared with the second quarter of 2006. The impact of higher commodity costs, the absence of an \$80 million benefit received in the second quarter of 2006 on a reserve reversal associated with the settlement of a Department of Defense claim against Pratt & Whitney, the shift in mix at Otis towards new equipment, and lower margins at Sikorsky from the manufacturing ramp and re-configuration efforts all contributed to the decline as a percentage of sales. For the first six months of 2007, gross margin was adversely



impacted by the previously noted EU fine, the impact of higher commodity costs, Otis' shift in mix towards new equipment and the

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Sikorsky manufacturing cost issues. After a partial recovery through pricing, the net impact to earnings of higher commodity and energy costs was approximately \$70 million in the second quarter of 2007, and approximately \$178 million for the six months ended June 30, 2007. Offsetting the reserve reversal noted above in the first six months of 2006 was the effect of the first quarter strike at Sikorsky and the subsequent ramp up to full production in the second quarter, as well as supplier issues and manufacturing inefficiencies associated with the ramp up of 13 SEER production at Carrier, and increased commodity and energy costs.

**Research and Development**

| In Millions     | Quarter Ended June 30, |             |               |             | Six Months Ended June 30, |             |                 |             |
|-----------------|------------------------|-------------|---------------|-------------|---------------------------|-------------|-----------------|-------------|
|                 | 2007                   |             | 2006          |             | 2007                      |             | 2006            |             |
|                 | Amount                 | % of Sales  | Amount        | % of Sales  | Amount                    | % of Sales  | Amount          | % of Sales  |
| Company-funded  | \$ 416                 | 3.0%        | \$ 370        | 3.1%        | \$ 798                    | 3.1%        | \$ 739          | 3.3%        |
| Customer-funded | 454                    | 3.3%        | 405           | 3.4%        | 885                       | 3.4%        | 803             | 3.6%        |
| <b>Total</b>    | <b>\$ 870</b>          | <b>6.3%</b> | <b>\$ 775</b> | <b>6.4%</b> | <b>\$ 1,683</b>           | <b>6.5%</b> | <b>\$ 1,542</b> | <b>6.9%</b> |

The increase in company-funded research and development in the second quarter and first six months of 2007, compared to the same periods in 2006, was driven largely by spending on the Boeing 787 program at Hamilton Sundstrand. Company-funded research and development spending for the full year 2007 is expected to increase over \$100 million from 2006 levels due to continued investment in new technology programs. The increase in customer-funded research and development in the second quarter of 2007 largely relates to increased effort at Sikorsky on the CH-53K program, offset partially by reduced efforts at Pratt & Whitney and Hamilton Sundstrand on the Joint Strike Fighter development program as it nears completion.

**Selling, General and Administrative**

| In Millions         | Quarter Ended |          | Six Months Ended |          |
|---------------------|---------------|----------|------------------|----------|
|                     | June 30,      |          | June 30,         |          |
|                     | 2007          | 2006     | 2007             | 2006     |
| Total expenses      | \$ 1,494      | \$ 1,378 | \$ 2,890         | \$ 2,692 |
| Percentage of sales | 10.9%         | 11.4%    | 11.2%            | 12.0%    |

The increase in selling, general and administrative expenses for the quarter and six months ended June 30, 2007, compared to the same periods of 2006, is due primarily to general increases across the businesses in support of higher volume and to the adverse impact of foreign currency translation. However, the continued strong control of spending coupled with the significant growth in revenues has led to an 80 basis point reduction in first half expenses as a percentage of sales.

**Interest Expense**

| In Millions           | Quarter Ended |        | Six Months Ended |        |
|-----------------------|---------------|--------|------------------|--------|
|                       | June 30,      |        | June 30,         |        |
|                       | 2007          | 2006   | 2007             | 2006   |
| Interest expense      | \$ 163        | \$ 155 | \$ 313           | \$ 297 |
| Average interest rate | 6.2%          | 6.3%   | 6.2%             | 6.3%   |

Interest expense for the quarter and six months ended June 30, 2007 has increased primarily as a result of the April 2005 issuance of long-term debt in connection with the acquisitions of Kidde, Rocketdyne and Lenel, the issuance of additional long-term debt in May 2006, and interest accrued on unrecognized tax benefits in open tax years.

**Table of Contents****Income Taxes**

|                    | Quarter Ended |       | Six Months Ended |       |
|--------------------|---------------|-------|------------------|-------|
|                    | June 30,      |       | June 30,         |       |
|                    | 2007          | 2006  | 2007             | 2006  |
| Effective tax rate | 28.1%         | 26.2% | 30.1%            | 26.9% |

The effective tax rate for the first six months of 2007 was adversely impacted by the EU fine and the sale of land and marketable securities. The effective tax rate for the first six months of 2006 benefited from the 1994 - 1999 dispute settlement with IRS Appeals, but was adversely impacted by the tax effect of the previously noted settlement of the Pratt & Whitney collaboration matter. The effective tax rate for the remainder of the year is expected to approximate 28% absent any additional discrete activity.

**Net Income**

| In Millions (except per share amounts) | Quarter Ended |          | Six Months Ended |          |
|--|---------------|----------|------------------|----------|
|  | June 30,      |          | June 30,         |          |
|  | 2007          | 2006     | 2007             | 2006     |
| Net income                             | \$ 1,148      | \$ 1,103 | \$ 1,967         | \$ 1,871 |
| Diluted earnings per share             | \$ 1.16       | \$ 1.09  | \$ 1.98          | \$ 1.85  |

Foreign currency translation had a positive impact on earnings per share in the second quarter of 2007 of \$.03 per share; foreign currency translation did not have a significant impact on earnings per share in the second quarter of 2006. For the six months ended June 30, 2007, the EU Fine, net of previously established reserves against the fine, and incremental restructuring charges were partially offset by gains on the sale of land and marketable securities, and the favorable impact of a contract termination at Pratt & Whitney, resulting in a \$.07 adverse impact on diluted earnings per share in the first quarter and an additional \$.02 adverse impact in the second quarter of 2007. Net income was further reduced by an increase in minority interest which included \$27 million for the minority partner's share of the gain from the previously noted sale of land. For the six months ended June 30, 2006, the benefit from the reserve reversal on the Pratt & Whitney collaboration matter and the benefit recorded on the completion of the IRS examination of tax years 1994 through 1999 was partially offset by incremental restructuring charges resulting in a \$.07 favorable impact on diluted earnings per share.

**Restructuring and Related Costs**

During the first six months of 2007, we recorded net pre-tax restructuring and related charges/(credits) in the business segments totaling \$60 million for new and ongoing restructuring actions as follows:

| In Millions         |       |
|---------------------|-------|
| Otis                | \$ 5  |
| Carrier             | 13    |
| UTC Fire & Security | 6     |
| Pratt & Whitney     | 27    |
| Hamilton Sundstrand | 12    |
| Sikorsky            | (3)   |
| Total               | \$ 60 |

The charges included \$41 million in cost of sales, \$20 million in selling, general and administrative expenses and (\$1) million in other income. As described below, these charges principally relate to actions initiated during 2007 and 2006, and trailing costs related to certain 2005 actions.

**2007 Actions.** During the first six months of 2007, we initiated restructuring actions relating to ongoing cost reduction efforts, including workforce reductions and the consolidation of manufacturing facilities. We recorded net pre-tax



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restructuring and related charges in the business segments totaling \$34 million as follows: Otis \$8 million, Carrier \$14 million, UTC Fire & Security \$2 million, Pratt & Whitney \$9 million and Hamilton Sundstrand \$1 million. The charges included \$10 million in cost of sales and \$24 million in selling, general and administrative expenses. Those costs included \$23 million for severance and related employee termination costs, \$1 million for asset write-downs, and \$10 million for facility exit and lease termination costs.

We expect the 2007 actions to result in net workforce reductions of approximately 700 hourly and salaried employees, the exiting of approximately 450,000 net square feet of facilities and the disposal of assets associated with the exited facilities. As of June 30, 2007, we have completed net workforce reductions of approximately 300 employees. We are targeting the majority of the remaining workforce and all facility related cost reduction actions for completion during 2007. Approximately 85% of the total pre-tax charge will require cash payments, which we will primarily fund with cash generated from operations. During the first six months of 2007, we had cash outflows of approximately \$8 million related to the 2007 programs. We expect to incur additional restructuring and related charges of \$25 million to complete these actions. We expect recurring pre-tax savings to increase over the two-year period subsequent to initiating the actions to approximately \$30 million annually.

**2006 Actions.** During the first six months of 2007, we recorded net pre-tax restructuring and related charges/(credits) of \$11 million for actions initiated in 2006. The 2006 actions relate to ongoing cost reduction efforts, including workforce reductions and the consolidation of manufacturing facilities. We recorded the charges/(credits) for the first six months of 2007 in our segments as follows:

| <b>In Millions</b>  |              |
|---------------------|--------------|
| Otis                | \$ (1)       |
| Carrier             | 1            |
| UTC Fire & Security | 4            |
| Pratt & Whitney     | 9            |
| Hamilton Sundstrand | 1            |
| Sikorsky            | (3)          |
| <b>Total</b>        | <b>\$ 11</b> |

The net charges included \$10 million in cost of sales and \$1 million in selling, general and administrative expenses. Those costs included \$12 million for facility exit and lease termination costs, \$1 million for asset write-downs, and there were reversals of \$2 million for severance and related employee termination costs.

We expect the 2006 actions to result in net workforce reductions of approximately 3,800 hourly and salaried employees, the exiting of approximately 600,000 net square feet of facilities and the disposal of assets associated with the exited facilities. As of June 30, 2007, we have completed net workforce reductions of approximately 2,600 employees and exited 100,000 net square feet of facilities. We target the majority of the remaining workforce and facility actions for completion during 2007. Approximately 90% of the total pre-tax charges will require cash payments, which we will primarily fund with cash generated from operations. During the first six months of 2007, we had cash outflows of approximately \$50 million related to the 2006 programs. We expect to incur additional restructuring and related charges of \$33 million to complete these actions. We expect recurring pre-tax savings to increase over the two-year period subsequent to initiating the actions to approximately \$140 million annually.

**2005 and Prior Actions.** During 2005, the more significant actions related to the consolidation of manufacturing sales and service facilities, including the closure of a portion of Hamilton Sundstrand's Rockford manufacturing facility. These actions, when complete, will provide for workforce reductions of approximately 2,900 hourly and salaried employees, the exiting of approximately 1.2 million net square feet of facilities and the disposal of assets associated with the exited facilities. As of June 30, 2007, we have completed net workforce reductions of approximately 2,700 employees and exited 700,000 net square feet of facilities. Savings are expected to increase over the two-year period subsequent to initiating the actions, resulting in recurring pre-tax savings of approximately \$115 million. We expect cash outflows on these programs to be approximately \$160 million, of which approximately \$145 million has been funded to date.

**Additional 2007 Actions**

We expect to incur approximately \$33 million of additional restructuring costs in the remainder of 2007 related to previously announced restructuring actions. We expect to initiate additional restructuring actions during the remainder of



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2007 due to our continuing cost reduction efforts, including certain actions to be taken to integrate IESG into the UTC Fire & Security segment. No specific plans for other significant new actions have been finalized at this time.

**Segment Review**

Segments are generally based on the management structure of the businesses and the grouping of similar operating companies, where each management organization has general operating autonomy over diversified products and services. Adjustments to reconcile segment reporting to the consolidated results for the quarters ended June 30, 2007 and 2006 are included in Eliminations and other, which also includes certain small subsidiaries.

Results for the quarters ended June 30, 2007 and 2006 are as follows:

| In Millions                | Revenues  |           | Operating Profits |          | Operating Profit Margin |       |
|----------------------------|-----------|-----------|-------------------|----------|-------------------------|-------|
|                            | 2007      | 2006      | 2007              | 2006     | 2007                    | 2006  |
| Otis                       | \$ 2,858  | \$ 2,529  | \$ 532            | \$ 472   | 18.6%                   | 18.7% |
| Carrier                    | 4,055     | 3,751     | 489               | 410      | 12.1%                   | 10.9% |
| UTC Fire & Security        | 1,349     | 1,167     | 101               | 65       | 7.5%                    | 5.6%  |
| Pratt & Whitney            | 3,108     | 2,727     | 522               | 535      | 16.8%                   | 19.6% |
| Hamilton Sundstrand        | 1,404     | 1,281     | 246               | 212      | 17.5%                   | 16.5% |
| Sikorsky                   | 1,198     | 767       | 87                | 42       | 7.3%                    | 5.5%  |
| Total segment              | 13,972    | 12,222    | 1,977             | 1,736    | 14.1%                   | 14.2% |
| Eliminations and other     | (68)      | 42        | (20)              | 84       |                         |       |
| General corporate expenses |           |           | (92)              | (79)     |                         |       |
| Consolidated               | \$ 13,904 | \$ 12,264 | \$ 1,865          | \$ 1,741 | 13.4%                   | 14.2% |

Second quarter 2007 and 2006 restructuring and related charges included in consolidated operating profit totaled \$25 million and \$82 million, respectively, as follows:

| In Millions         | Quarter Ended |       |
|---------------------|---------------|-------|
|                     | 2007          | 2006  |
| Otis                | \$ 7          | \$ 6  |
| Carrier             | 1             | 25    |
| UTC Fire & Security | 4             | 12    |
| Pratt & Whitney     | 7             | 11    |
| Hamilton Sundstrand | 6             | 9     |
| Sikorsky            |               | 19    |
| Totals              | \$ 25         | \$ 82 |

Results for the six months ended June 30, 2007 and 2006 were as follows:

| In Millions | Revenues |          | Operating Profits |        | Operating Profit Margin |       |
|-------------|----------|----------|-------------------|--------|-------------------------|-------|
|             | 2007     | 2006     | 2007              | 2006   | 2007                    | 2006  |
| Otis        | \$ 5,586 | \$ 4,877 | \$ 1,106          | \$ 911 | 19.8%                   | 18.7% |
| Carrier     | 7,185    | 6,655    | 702               | 614    | 9.8%                    | 9.2%  |

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|                            |           |           |          |          |        |       |
|----------------------------|-----------|-----------|----------|----------|--------|-------|
| UTC Fire & Security        | 2,595     | 2,279     | 187      | 130      | 7.2%   | 5.7%  |
| Pratt & Whitney            | 5,875     | 5,295     | 1,012    | 965      | 17.2%  | 18.2% |
| Hamilton Sundstrand        | 2,717     | 2,445     | 464      | 393      | 17.1%  | 16.1% |
| Sikorsky                   | 2,204     | 1,279     | 160      | 45       | 7.3%   | 3.5%  |
| Total segment              | 26,162    | 22,830    | 3,631    | 3,058    | 13.9%  | 13.4% |
| Eliminations and other     | 20        | 49        | (83)     | 129      |        |       |
| General corporate expenses |           |           | (179)    | (164)    |        |       |
| Consolidated               | \$ 26,182 | \$ 22,879 | \$ 3,369 | \$ 3,023 | 12.9 % | 13.2% |



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For the first six months of 2007 and 2006, restructuring and related charges included in consolidated operating profit totaled \$60 million and \$113 million, respectively, as follows:

| In Millions         | Six Months Ended |        |
|---------------------|------------------|--------|
|                     | June 30,         |        |
|                     | 2007             | 2006   |
| Otis                | \$ 5             | \$ 8   |
| Carrier             | 13               | 32     |
| UTC Fire & Security | 6                | 14     |
| Pratt & Whitney     | 27               | 23     |
| Hamilton Sundstrand | 12               | 17     |
| Sikorsky            | (3)              | 19     |
| Totals              | \$ 60            | \$ 113 |

**Otis** In the second quarter of 2007, revenues increased \$329 million (13%) compared with the same period of 2006, reflecting organic growth (8%) and the favorable impact of foreign currency translation (4%). For the first six months of 2007, revenues increased \$709 million (15%) compared with the same period of 2006 reflecting organic growth (8%), the favorable impact of foreign currency translation (5%) and a gain on the sale of land (2%). Organic growth included increases in all geographic regions, led by new equipment sales as a result of the strong backlog entering the year.

In the second quarter of 2007, operating profits increased \$60 million (13%) compared with the same period of 2006 as a result of higher revenues and cost containment actions partially offset by escalating commodity and labor costs (net 7%), as well as the favorable impact of foreign currency translation (6%). In the first six months of 2007, operating profits increased \$195 million (21%) compared with the same period in 2006 as a result of higher revenues and cost containment actions partially offset by escalating commodity and labor costs (net 6%), the favorable impact of foreign currency translation (6%), and a gain realized on the sale of land (9%). Operating margins remained essentially flat despite the continued shift in sales mix towards new equipment, which has a lower contribution margin than service.

**Carrier** Revenues increased \$304 million (8%) in the second quarter of 2007 compared with the same period of 2006. Revenue growth was led by Building Systems and Services (3%), the favorable impact of foreign currency translation (3%), Residential and Light Commercial International HVAC (2%) and the Refrigeration business (2%), partially offset by our Residential and Light Commercial Systems business in North America (2%) due to a continued weakness in the U.S. housing market. For the first six months of 2007, revenues increased \$530 million (8%) compared with the same period of 2006. Similar to the second quarter of 2007, revenue growth was led by Building Systems and Services (3%), Refrigeration (3%), the favorable impact of foreign currency translation (3%) and Residential and Light Commercial International HVAC (2%), partially offset by our Residential and Light Commercial Systems business in North America (2%) as a result of continued weakness in the U.S. housing market. The comparative decline was exacerbated by the strong North American demand that existed in the first half of 2006.

Operating profits increased \$79 million (19%) in the second quarter of 2007 compared with the same period of 2006. Earnings growth in Building Systems and Services, Residential and Light Commercial International HVAC, and Refrigeration, net of the decline in North America Residential and Light Commercial Systems business volume, were augmented by the absence of manufacturing inefficiencies associated with the ramp up of 13 SEER production (combined 10%) and generated the majority of the operating profit growth. Lower restructuring charges (6%) and the favorable impact of foreign currency translation (3%) comprised the remaining increase during the quarter. Price realization entirely offset commodity cost increases in the quarter. For the first six months of 2007, operating profits increased \$88 million (14%) compared with the same period in 2006. Similar to the second quarter of 2007, earnings growth in Building Systems and Services, Residential and Light Commercial International HVAC, and Refrigeration, net of the decline in Residential and Light Commercial Systems business North America volume, were augmented by the absence of manufacturing inefficiencies associated with the ramp up of 13 SEER production (combined 13%) and generated the majority of the operating profit growth. Lower restructuring charges (3%) and the favorable impact of foreign currency translation (3%) were largely offset by the adverse impact of higher commodity costs (5%).

**UTC Fire & Security** Revenues increased \$182 million (16%) in the second quarter of 2007 compared with the same period of 2006. The increase reflects acquisitions (8%), the favorable impact of foreign currency translation (6%) and organic growth (2%) reflecting double digit growth in Asia and at Lenel, while Australia continued to be weak. For the six months ended June 30, 2007, revenues increased \$316 million (14%) compared with the same period of 2006 due to acquisitions (6%), the favorable impact of foreign currency translation (6%) and organic growth (2%).



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Operating profits increased \$36 million (55%) in the second quarter of 2007 compared with the same period of 2006. Volume and net cost reductions, including those from previous restructuring actions (21%), acquisitions (14%), lower restructuring charges (12%) and the favorable impact of foreign currency translation (9%) generated the improvement to operating profits. For the first six months of 2007, operating profits increased \$57 million (44%) compared with the same period of 2006. Operating profits from the increased volume and net cost reductions from previous restructuring actions (combined 21%), net acquisitions, principally Red Hawk and Hall & Kay, (9%), lower restructuring costs (6%) and the favorable impact of foreign currency translation (8%) generated the increase in operating profits.

**Pratt & Whitney** Revenues increased \$381 million (14%) in the second quarter of 2007 compared with the same period of 2006. The increase is primarily attributable to higher commercial aftermarket services (6%), higher engine shipments at Pratt & Whitney Canada (4%), and higher volumes at Pratt & Whitney Power Systems (3%). For the six months ended June 30, 2007, revenues increased \$580 million (11%) compared with the same period in 2006. Similar to the second quarter of 2007, the six month revenue growth is primarily attributable to higher commercial aftermarket services (6%), higher engine shipments at Pratt & Whitney Canada (3%), and higher volumes at Pratt & Whitney Power Systems (2%).

Operating profits decreased \$13 million (2%) in the second quarter of 2007 compared with the same period of 2006 primarily due to the positive impact of a 2006 settlement of a government litigation matter (15%). Operating profits otherwise increased primarily as a result of the profit contribution from higher volumes, principally in the commercial markets and aftermarket services (16%) and Pratt & Whitney Canada (6%), partially offset by the impact of higher year over year commodity and manufacturing costs (11%). For the first six months of 2007, operating profits increased \$47 million (5%) compared with the same period in 2006. The increase is primarily attributable to the profit contributions from higher volumes in commercial markets and aftermarket services (17%) and the favorable impact received from a contract termination (4%), partially offset by the absence of the impact of a 2006 settlement of a government litigation matter (9%) and the impact of higher year over year commodity costs (9%). Higher volumes at Pratt & Whitney Canada comprised the majority of the remaining increase.

**Hamilton Sundstrand** Revenues increased \$123 million (10%) in the second quarter of 2007 compared with the same period in 2006, principally due to organic volume growth across the aerospace (5%) and industrial (2%) businesses, and the favorable impact of foreign currency translation (2%). For the six months ended June 30, 2007, revenues increased \$272 million (11%) compared with the same period in 2006, principally due to organic volume growth in both the aerospace (6%) and industrial (3%) businesses and the favorable impact of foreign currency translation (2%). Within aerospace, commercial aftermarket volumes contributed the majority of both the quarter and six month increases.

Hamilton Sundstrand's operating profits increased \$34 million (16%) in the second quarter of 2007 compared with the same period of 2006, principally due to improvements in both the commercial aftermarket (15%) and industrial (2%) businesses. Operating profits from the commercial OEM revenue growth were largely offset by increased company funded research and development costs principally related to the Boeing 787 program. For the six months ended June 30, 2007, operating profit increased \$71 million (18%) compared with the same period in 2006, principally due to volume growth in both the commercial aftermarket (14%) and industrial (2%) businesses, and the favorable impact of foreign currency translation (2%). Similar to the second quarter, operating profits from commercial OEM revenue growth were largely offset by increased company funded research and development costs principally related to the Boeing 787 program.

**Sikorsky** Revenues increased \$431 million (56%) in the second quarter of 2007 compared with the same period of 2006. The revenue increase was driven by higher business volume in the second quarter of 2007 as compared with the second quarter of 2006 which was adversely impacted by the six week strike of Sikorsky's union workforce which ended early in the second quarter of 2006. Increases in military aircraft deliveries and program support (30%), commercial aircraft revenues (14%), and aftermarket operations (13%) comprised the majority of the year over year revenue increase. For the first six months of 2007, revenues increased \$925 million (72%) compared with the same period of 2006. As with the second quarter, the six month revenue increase was driven by higher business volume in the first half of 2007 as compared with the first half of 2006 which was adversely impacted by the strike of Sikorsky's union workforce. Increases in military aircraft deliveries and program support (33%), aftermarket operations (20%) and commercial aircraft revenues (19%), comprised the majority of the year over year revenue increase.

Operating profits increased \$45 million (107%) in the second quarter of 2007 compared with the same period of 2006. The absence of the strike related impact in the second quarter of 2006, and the increased volume from strong commercial and military demand, generated the significant improvement to operating profit in the second quarter of 2007. For the six months ended June 30, 2007, operating profits increased \$115 million (256%) compared with the same period of 2006. Similar to the second quarter, the absence of the strike related impact in the first half of 2006, and the

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increased volume from strong commercial and military demand, generated the majority of the increase in operating profit in the first half of 2007. Lower year over year restructuring charges contributed an additional 49%.

**Eliminations and other** The decrease in Eliminations and other in the second quarter of 2007 reflects the absence of approximately \$60 million in interest income that was included in the second quarter of 2006 from the re-evaluation of liabilities and contingencies in light of the IRS completion of its examination and the U.S. Congress Joint Committee on Taxation's approval of the settlement and close-out of the 1994 through 1999 tax years. For the six months ended June 30, 2007, Eliminations and other included the EU Fine of \$216 million (net of previously established reserves) offset partially by gains of approximately \$150 million from the sale of marketable securities. In addition to the interest income noted above, Eliminations and other in the first six months of 2006 included a \$25 million gain from the sale of marketable securities.

**LIQUIDITY AND FINANCIAL CONDITION**

|  | June 30, | December 31, | June 30, |
|--|----------|--------------|----------|
| In Millions  | 2007     | 2006         | 2006     |
| Cash and cash equivalents  | \$ 3,292 | \$ 2,546     | \$ 2,883 |
| Total debt   | 8,593    | 7,931        | 8,759    |
| Net debt (total debt less cash and cash equivalents)                 | 5,301    | 5,385        | 5,876    |
| Shareowners' equity  | 19,195   | 17,297       | 18,448   |
| Total capitalization (debt plus equity)                              | 27,788   | 25,228       | 27,207   |
| Net capitalization (debt plus equity less cash and cash equivalents) | 24,496   | 22,682       | 24,324   |
| Debt to total capitalization   | 31%      | 31%          | 32%      |
| Net debt to net capitalization                                       | 22%      | 24%          | 24%      |

**Cash Flow from Operating Activities**

| In Millions                                     | Six Months Ended June 30, |          |
|---|---------------------------|----------|
|   | 2007                      | 2006     |
| Net cash flows provided by operating activities | \$ 1,902                  | \$ 1,787 |

Operating cash flow in the first half of 2007 was adversely impacted by the payment of the EU Fine (approximately \$300 million), the payment of Canadian taxes in connection with ongoing tax planning activities (approximately \$200 million), and an increase in working capital of \$395 million. Receivables and inventory growth was driven by the normal seasonality of Carrier's operating activities and increased service billings at Otis. Aerospace inventory increased in support of the strong organic growth and the continued tight aerospace supply chain. Working capital benefited from increased accounts payable to fund the inventory increases and by customer advanced payments received. We expect inventory levels to remain high due to the strong organic growth levels and will continue to work to offset with a focus on advances and receivables collections. Relative to the prior year, operating cash flow benefited from lower use of cash for working capital of \$346 million because of the effects of the Sikorsky strike in the prior year and the advance payments received during 2007.

**Cash Flow from Investing Activities**

| In Millions                                 | Six Months Ended June 30, |          |
|---|---------------------------|----------|
|   | 2007                      | 2006     |
| Net cash flows used in investing activities | \$ (537)                  | \$ (660) |

The reduction in cash flows used in investing activities is largely the result of lower levels of customer financing activity (\$76 million) and an increase in the cash received from the sale of marketable securities (\$116 million), partially offset by an increase in capital expenditures (\$40 million). For the year, capital expenditures are expected to increase by approximately \$100 million from 2006 levels to approximate depreciation and amortization expense in 2007. While we expect that 2007 customer financing activity will be a net use of funds, actual funding is subject to usage under existing customer financing commitments during the remainder of the year. We may also arrange for third-party investors to assume a portion of our commitments. We had financing and rental commitments of approximately \$1,787 million and \$1,126 million related to commercial aircraft at June 30, 2007 and December 31, 2006, respectively. Acquisition activity in the first half of 2007 consisted of a number of small purchases in both the aerospace and commercial businesses.



**Table of Contents****Cash Flow from Financing Activities**

| In Millions                                 | Six Months Ended June 30, |          |
|---|---------------------------|----------|
|   | 2007                      | 2006     |
| Net cash flows used in financing activities | \$ (691)                  | \$ (521) |

A net increase in borrowings (\$147 million) was more than offset by higher levels of share repurchases (\$250 million) resulting in the additional usage of cash in financing activities in the first half of 2007 as compared to the same period in 2006. In the first six months of 2007, short-term borrowings increased \$634 million primarily in anticipation of the IESG acquisition funding requirements as noted below. At June 30, 2007, we had credit commitments from banks totaling \$2.5 billion. We have a credit commitment of \$1.5 billion under a revolving credit agreement that serves as a back-up facility for the issuance of commercial paper. As of June 30, 2007, there were no borrowings against this revolving credit agreement, which expires in October 2011. We also have a \$1.0 billion multi-currency revolving credit agreement that is to be used for general corporate funding purposes, including acquisitions. As of June 30, 2007, \$650 million had been borrowed against this revolving credit agreement. This credit agreement expires in November 2011.

At June 30, 2007, total cash and cash equivalents were \$3,292 million, or an increase of \$746 million over the \$2,546 million at December 31, 2006. A portion of this increase was a result of our cash positioning in anticipation of the July 2, 2007 acquisition of IESG and was drawn from the previously discussed multi-currency revolving credit facility.

At June 30, 2007, up to \$900 million of additional debt and equity securities could be issued under a shelf registration statement on file with the Securities and Exchange Commission.

We repurchased \$1 billion of common stock under an existing 60 million share repurchase program. Share repurchases in the first six months of 2007 represent approximately 15.0 million shares. At June 30, 2007, approximately 43.3 million shares remain available for repurchase under the program. We expect total share repurchases in 2007 to be approximately \$1.5 billion and expect the total number of outstanding shares to decrease during the year. However, total repurchases may vary depending upon the level of other investing activities. The share repurchase program continues to be a significant use of our cash flows and, at a minimum, is expected to offset the dilutive effect of the issuance of stock and options under stock-based employee benefit programs. We paid dividends of \$0.265 per share in the first quarter of 2007 totaling \$245 million, and \$0.265 per share in the second quarter for a total of \$245 million. On June 13, 2007, the Board of Directors declared a dividend of \$0.32 per share payable September 10, 2007.

The funded status of our pension plans is dependent upon many factors, including returns on invested assets and the level of market interest rates. We can contribute cash or company stock to our plans at our discretion. During the first six months of 2007, we made a voluntary \$150 million contribution of UTC common stock to our U.S. pension plans. We expect total voluntary contributions to our global pension plans in 2007 to be up to \$250 million, including the \$150 million common stock contribution.

We assess our liquidity in terms of our ability to generate cash to fund our operating, investing and financing activities. Our principal source of liquidity is operating cash flows, which, after netting out capital expenditures, we target to equal or exceed net income for the full year. In addition to operating cash flows, other significant factors that affect our overall management of liquidity include: capital expenditures, customer financing requirements, investments in businesses, dividends, common stock repurchases, pension funding, adequacy of available bank lines of credit, and the ability to attract long-term capital at satisfactory terms.

A large portion of our cash is denominated in foreign currencies. We manage our worldwide cash requirements considering available funds among the many subsidiaries through which we conduct our business and the cost effectiveness with which those funds can be accessed. The repatriation of cash balances from certain of our subsidiaries could have adverse tax consequences; however, those balances are generally available without legal restrictions to fund ordinary business operations. We have and will continue to transfer cash from those subsidiaries to us and to other international subsidiaries when it is cost effective to do so.

The timing and levels of certain cash flow activities, such as acquisitions, have resulted in the issuance of both long-term and short-term debt. Commercial paper borrowings and revolving credit facilities provide short-term liquidity to supplement operating cash flows and are used for general corporate purposes as well as the potential funding of certain acquisitions. As of June 30, 2007, we did not have any commercial paper outstanding, but had \$650 million outstanding under our multi-currency revolving line of credit.



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Our ability to obtain debt financing at comparable risk-based interest rates is partly a function of our existing debt to capitalization levels as well as our current credit standing. Our credit ratings are reviewed regularly by major debt rating agencies such as Standard and Poor's and Moody's Investor Service. In 2006, Standard and Poor's affirmed our long-term and short-term debt ratings as A and A-1, respectively. Similarly, Moody's Investor Service also affirmed its corporate rating on our long-term and short-term debt as A2 and P-1, respectively.

We believe our future operating cash flows will be sufficient to meet our future operating cash needs. Further, our ability to obtain debt or equity financing, as well as the availability under committed credit lines, provides additional potential sources of liquidity should they be required.

### **Off-Balance Sheet Arrangements and Contractual Obligations**

In our Annual Report, incorporated by reference in our Form 10-K for the calendar year 2006, we disclosed our off-balance sheet arrangements and contractual obligations. At June 30, 2007, there have been no material changes to off-balance sheet arrangements outside the ordinary course of business. There has been a material decrease in Future Pension and Postretirement Obligations since December 31, 2006, due to early-adoption of the measurement date provisions of SFAS 158. For additional discussion of the SFAS 158 adoption, see Note 6 to the Condensed Consolidated Financial Statements in this Form 10-Q.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

There has been no significant change in our exposure to market risk during the first six months of 2007. For discussion of our exposure to market risk, refer to Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk, contained in our Annual Report, incorporated by reference in our Form 10-K for the calendar year 2006.

### **Item 4. Controls and Procedures**

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the Exchange Act) we carried out an evaluation under the supervision and with the participation of our management, including the Chief Executive Officer, the President and Chief Operating Officer, the Vice President, Accounting and Finance; Controller and the Vice President, Finance, of the effectiveness of the design and operation of our disclosure controls and procedures as of June 30, 2007. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon our evaluation, our Chief Executive Officer, our President and Chief Operating Officer, our Vice President, Accounting and Finance; Controller and our Vice President, Finance have concluded that, as of June 30, 2007, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the applicable rules and forms, and that it is accumulated and communicated to our management, including our Chief Executive Officer, our President and Chief Operating Officer, our Vice President, Accounting and Finance; Controller and our Vice President, Finance, as appropriate, to allow timely decisions regarding required disclosure.

There has been no change in our internal control over financial reporting during the quarter ended June 30, 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

### **CAUTIONARY NOTE CONCERNING FACTORS THAT MAY AFFECT FUTURE RESULTS**

This report on Form 10-Q contains statements which, to the extent they are not statements of historical or present fact, constitute forward-looking statements under the securities laws. From time to time, oral or written forward-looking statements may also be included in other materials released to the public. These forward-looking statements are intended to provide management's current expectations or plans for our future operating and financial performance, based on assumptions currently believed to be valid. Forward-looking statements can be identified by the use of words such as believe, expect, plans, strategy, prospects, estimate, project, target, anticipate and other words or phrases having meaning in connection with a discussion of future operating or financial performance. These include, among others, statements relating to:

Future earnings and other measures of financial performance



Future cash flow and uses of cash

The effect of economic downturns or growth in particular regions

The effect of changes in the level of activity in particular industries or markets

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The availability and cost of materials, components, services and supplies

The scope, nature or impact of acquisition activity and integration into our businesses

The development, production and support of advanced technologies and new products and services

New business opportunities

Restructuring costs and savings

The effective negotiation of collective bargaining agreements

The outcome of contingencies

Future repurchases of common stock

Future levels of indebtedness and capital spending

Pension plan assumptions and future contributions

All forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from those expressed or implied in the forward-looking statements. This Quarterly Report on Form 10-Q includes important information as to factors that may cause actual results to vary materially from those stated in the forward-looking statements in the Notes to Condensed Consolidated Financial Statements under the heading **Contingent Liabilities**, in the section titled **Management's Discussion and Analysis of Financial Condition and Results of Operations** under the headings **Business Overview**, **Critical Accounting Estimates**, **Results of Continuing Operations**, **Liquidity and Financial Condition** and in the section titled **Risk Factors**. Our Annual Report on Form 10-K for the calendar year 2006 also includes important information as to these risk factors in the **Business** section under the headings **Description of Business by Segment**, **Other Matters Relating to our Business as a Whole**, **Risk Factors** and in the **Legal Proceedings** section. Additional important information as to these factors is included in our 2006 Annual Report to Shareowners in the section titled **Management's Discussion and Analysis of Financial Condition and Results of Operations** under the headings **Business Overview**, **Critical Accounting Estimates**, **Environmental Matters** and **Restructuring and Other Costs**. For additional information identifying factors that may cause actual results to vary materially from those stated in the forward-looking statements, see our reports on Forms 10-Q and 8-K filed with the Securities and Exchange Commission from time to time.

## **Part II Other Information**

### **Item 1. Legal Proceedings**

As previously reported, the European Commission's Competition Directorate (EU Commission) conducted inspections in early 2004 at offices of our Otis subsidiary in Berlin, Brussels, Luxembourg and Paris relating to an investigation of possible unlawful collusive arrangements involving the European elevator and escalator industry. On February 21, 2007, the EU Commission ruled that Otis subsidiaries in Belgium, Luxembourg and the Netherlands, and a portion of the business of Otis German subsidiary, violated EU competition rules and assessed a 225 million Euro (approximately \$300 million) civil fine against Otis, its relevant local entities, and UTC. We paid \$88 million of the fine in March 2007. The remaining \$212 million was deposited into a trust that disbursed the funds to the EU Commission in May 2007. In May 2007, we filed an appeal of the decision before the European Court of First Instance. Resolution of the matter is not expected within the next twelve months.

Except as noted above, there have been no material developments in legal proceedings. For a description of previously reported legal proceedings refer to Part II, Item 1, Legal Proceedings, of our Quarterly Report on Form 10-Q for the quarter ended March 31, 2007 and Part I, Item 3, Legal Proceedings, of our Annual Report on Form 10-K for the year ended December 31, 2006.

**Item 1A. Risk Factors**

Our business, financial condition, operating results and cash flows can be impacted by a number of factors, including, but not limited to those set forth below, any one of which could cause our actual results to vary materially from recent results or from our anticipated future results. For a discussion identifying additional risk factors and important factors that could cause actual results to differ materially from those anticipated, see the discussion in *Other Matters Relating to Our Business as a Whole* and *Cautionary Note Concerning Factors That May Affect Future Results* in our Form 10-K for 2006 and in *Management's Discussion and Analysis of Financial Condition and Results of Operations* and *Notes to Consolidated Financial Statements* in our 2006 Annual Report and in this Form 10-Q.

**Table of Contents*****Our Financial Performance Is Dependent on the Conditions of the Aerospace and Construction Industries***

The results of our commercial and military aerospace businesses, which generated 37 percent of our revenues in 2006, are directly tied to the economic conditions in the commercial aviation and defense industries. The aviation industry is cyclical, and capital spending by airlines and aircraft manufacturers may be influenced by a wide variety of factors, including current and predicted traffic levels, load factors, aircraft fuel pricing, labor issues, competition, the retirement of older aircraft, regulatory changes, terrorism and related safety concerns, general economic conditions, worldwide airline profits and backlog levels. Also, since a substantial portion of the backlog for commercial aerospace customers is scheduled for delivery beyond 2007, changes in economic conditions may cause customers to request that firm orders be rescheduled or canceled. In addition, our aerospace businesses face intense competition from domestic and foreign manufacturers of new equipment and spare parts. The defense industry is also affected by a changing global political environment, continued pressure on U.S. and global defense spending and U.S. foreign policy and the level of activity in military flight operations. Spare parts sales and aftermarket service trends are affected by similar factors, including usage, pricing, regulatory changes, the retirement of older aircraft and technological improvements to new engines that increase reliability. Furthermore, because of the lengthy research and development cycle involved in bringing products in these business segments to market, we cannot predict the economic conditions that will exist when any new product is complete. A reduction in capital spending in the aviation or defense industries could have a significant effect on the demand for our products, which could have an adverse effect on our financial performance or results of operations.

The results of our commercial and industrial businesses, which generated 63 percent of our revenues in 2006, are influenced by a number of external factors including fluctuations in residential and commercial construction activity, interest rates, labor costs, foreign currency exchange rates, customer attrition, raw material and energy costs and other global and political factors. In addition to these factors, Carrier's financial performance can also be influenced by production and utilization of transport equipment and, in its residential business, weather conditions.

***Our Business May Be Affected by Government Contracting Risks***

U.S. government contracts are subject to termination by the government, either for the convenience of the government or for default as a result of our failure to perform under the applicable contract. If terminated by the government as a result of our default, we could be liable for additional costs the government incurs in acquiring undelivered goods or services from another source and any other damages it suffers. We are now, and believe that in light of the current U.S. government contracting environment we will continue to be, the subject of one or more U.S. government investigations. If we or one of our business units were charged with wrongdoing as a result of any U.S. government investigations (including violation of certain environmental or export laws), the U.S. government could suspend us from bidding on or receiving awards of new U.S. government contracts pending the completion of legal proceedings. If convicted or found liable, the U.S. government could subject us to fines, penalties, repayments and treble and other damages. The U.S. government could void any contracts found to be tainted by fraud. The U.S. government also reserves the right to debar a contractor from receiving new government contracts for fraudulent, criminal or other seriously improper conduct. Debarment generally does not exceed three years. Independently, failure to comply with U.S. laws and regulations related to the export of goods and technology outside the U.S. could result in civil or criminal penalties and suspension or termination of our export privileges.

***Our International Operations Subject Us to Economic Risk As Our Results of Operations May Be Adversely Affected by Foreign Currency Fluctuations and Changes in Local Government Regulation***

We conduct our business on a global basis, with 60 percent of our total 2006 segment revenues derived from operations outside of the United States and from U.S. export sales. Fluctuations in exchange rates may affect product demand in export markets and affect reported profits of our non-U.S. operations (primarily the commercial businesses) where transactions are generally denominated in local currencies. In addition, currency fluctuations may affect the prices we pay suppliers for materials used in our products. Our financial statements are denominated in U.S. dollars. Accordingly, fluctuations in exchange rates may also give rise to translation gains or losses when financial statements of non-U.S. operating units are translated into U.S. dollars. Given that the majority of our revenues are non-U.S. based, a strengthening of the U.S. dollar against other major foreign currencies could adversely affect our results of operations.

The majority of sales in the aerospace businesses are transacted in U.S. dollars, consistent with established industry practice, while the majority of costs at locations outside the United States are incurred in the applicable local currency (principally the Euro and the Canadian dollar). For differences between the U.S. dollar sales and local currency costs, there is a foreign currency exposure that could impact the results of operations depending on market changes in the exchange rate of the U.S. dollar against these foreign currencies. To manage this exposure, we employ long-term hedging strategies associated with U.S. dollar revenues.

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Our international sales and operations are subject to risks associated with changes in local government laws, regulations and policies, including those related to tariffs and trade barriers, investments, taxation, exchange controls, employment regulations, and repatriation of earnings. Our international sales and operations are also sensitive to changes in foreign national priorities, including government budgets, as well as to political and economic instability. International transactions may involve increased financial and legal risks due to differing legal systems and customs in foreign countries. For example, as a condition of sale or award of a contract, some international customers require us to agree to offset arrangements, which may include in-country purchases, manufacturing and financial support arrangements. The contract may provide for penalties in the event we fail to perform in accordance with the offset requirements. In addition, as part of our globalization strategy, we have invested in certain countries, including Argentina, Brazil, China, India, Russia and South Africa, that carry high levels of currency, political and economic risk. While these factors or the impact of these factors are difficult to predict, any one or more of them could adversely affect our business, financial condition or operating results.

***We Use a Variety of Raw Materials, Supplier Provided Parts, Components, Sub-Systems and Third Party Contract Manufacturing Services in Our Businesses, and Significant Shortages, Supplier Capacity Constraints, Supplier Production Disruptions or Price Increases Could Increase Our Operating Costs and Adversely Impact the Competitive Positions of Our Products***

Our reliance on suppliers, third party contract manufacturing and commodity markets to secure raw materials, parts, components and sub-systems used in our products exposes us to volatility in the prices and availability of these materials. In some instances, we depend upon a single source of supply, manufacturing or assembly or participate in commodity markets that may be subject to allocations by suppliers. A disruption in deliveries from our suppliers or third party contract manufacturers, supplier capacity constraints, supplier and third party contract manufacturer production disruptions, price increases, or decreased availability of raw materials or commodities, could have an adverse effect on our ability to meet our commitments to customers or increase our operating costs. We believe that our supply management and production practices are based on an appropriate balancing of the foreseeable risks and the costs of alternative practices. Nonetheless, price increases, supplier capacity constraints, supplier production disruptions or the unavailability of some raw materials may have an adverse effect on our results of operations or financial condition.

***We Engage in Acquisitions, and May Encounter Difficulties Integrating Acquired Businesses with Our Current Operations; Therefore, We May Not Realize the Anticipated Benefits of the Acquisitions***

We seek to grow through strategic acquisitions. In the past several years, we have made various acquisitions and entered into joint venture arrangements intended to complement and expand our businesses, and may continue to do so in the future. The success of these transactions will depend on our ability to integrate assets and personnel acquired in these transactions, apply our internal controls processes to these acquired businesses, and cooperate with our strategic partners. We may encounter difficulties in integrating acquisitions with our operations, and in managing strategic investments. Furthermore, we may not realize the degree, or timing, of benefits we anticipate when we first enter into a transaction. Any of the foregoing could adversely affect our business and results of operations.

***We Design, Manufacture and Service Products that Incorporate Advanced Technologies; The Introduction of New Products and Technologies Involves Risks and We May Not Realize the Degree or Timing of Benefits Initially Anticipated***

We seek to achieve growth through the design, development, production, sale and support of innovative products that incorporate advanced technologies. We regularly invest substantial amounts in research and development efforts that pursue advancements in a wide range of technologies, products and services. Our ability to realize the anticipated benefits of these advancements depends on a variety of factors, including meeting development, production, certification and regulatory approval schedules; execution of internal and external performance plans; availability of internal and supplier produced parts and materials; performance of suppliers and subcontractors; achieving cost and production efficiencies and validation of innovative technologies. These factors involve significant risks and uncertainties. We may encounter difficulties in developing and producing these new products and services, and may not realize the degree or timing of benefits initially anticipated. In particular, we cannot predict with certainty whether, when and in what quantities Pratt & Whitney or its affiliates will produce aircraft engines currently in development or pending required certifications. Any of the foregoing could adversely affect our business and results of operations.

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***We Are Subject to Litigation and Legal Compliance Risks That Could Adversely Affect Our Operating Results***

We are subject to a variety of litigation and legal compliance risks. These risks include, among other things, litigation concerning product liability matters, personal injuries, intellectual property rights, government contracts, taxes, environmental matters, compliance with competition laws and sales and trading practices. While we believe we have adopted appropriate risk management and compliance programs to address and reduce these risks, the global and diverse nature of our operations means that these risks will continue to exist and additional legal proceedings and contingencies will arise from time to time. Our results may be affected by the outcome of legal proceedings and other contingencies that cannot be predicted with certainty. As required by generally accepted accounting principles, we estimate material loss contingencies and establish reserves based on our assessment of contingencies where liability is deemed probable and reasonably estimable in light of the facts and circumstances known to us at a particular point in time. Subsequent developments in legal proceedings may affect our assessment and estimates of the loss contingency recorded as a liability or as a reserve against assets in our financial statements and could result in an adverse effect on our results of operations in the period in which a liability would be recognized or cash flows for the period in which damages would be paid. For a description of current legal proceedings, see Part II, Item 1 Legal Proceedings in this Form 10-Q and the Form 10-K.

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**  
**Issuer Purchases of Equity Securities**

The following table provides information about our purchases during the quarter ended June 30, 2007 of equity securities that are registered by us pursuant to Section 12 of the Exchange Act.

|             |          | <b>Total</b>     |                   |   | <b>Maximum Number of</b>      |
|-------------|----------|------------------|-------------------|---|-------------------------------|
|             |          | <b>Number of</b> | <b>Average</b>    | <b>Total Number of Shares Purchased</b> | <b>Shares that may yet be</b> |
|             |          | <b>Shares</b>    | <b>Price Paid</b> | <b>as Part of a Publicly</b>            | <b>Purchased Under</b>        |
|             |          | <b>Purchased</b> | <b>per</b>        | <b>Announced Program</b>                | <b>the Program</b>            |
|             |          | <b>(000 s)</b>   | <b>Share</b>      | <b>(000 s)</b>                          | <b>(000 s)</b>                |
| <b>2007</b> |          |                  |                   |   |                               |
| April 1     | April 30 | 2,780            | \$ 66.17          | 2,776                                   | 47,674                        |
| May 1       | May 31   | 2,049            | \$ 68.45          | 2,049                                   | 45,625                        |
| June 1      | June 30  | 2,285            | \$ 70.66          | 2,282                                   | 43,343                        |
| Total       |          | 7,114            | \$ 68.27          | 7,107                                   |                               |

On December 13, 2006, we announced that our Board of Directors authorized the repurchase of up to 60 million shares of our common stock. Shares may be purchased on the open market, in privately negotiated transactions, and under plans complying with Rules 10b5-1 and 10b-18 under the Exchange Act. These repurchases are included within the scope of our overall repurchase program discussed above. We may also reacquire shares outside of the program in connection with the surrender of shares to cover taxes on vesting of restricted stock. Approximately 7,000 shares were reacquired in transactions outside the program during the quarter.

**Item 6. Exhibits**

- (12) Statement re: computation of ratio of earnings to fixed charges.\*
- (15) Letter re: unaudited interim financial information.\*
- (31) Rule 13a-14(a)/15d-14(a) Certifications.\*
- (32) Section 1350 Certifications.\*

\* Submitted electronically herewith.

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**SIGNATURES**

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

UNITED TECHNOLOGIES CORPORATION

Dated: July 20, 2007

by: /s/ James E. Geisler  
James E. Geisler  
Vice President, Finance

Dated: July 20, 2007

by: /s/ Gregory J. Hayes  
Gregory J. Hayes  
Vice President, Accounting and Finance;  
Controller

Dated: July 20, 2007

by: /s/ Charles D. Gill  
Charles D. Gill  
Senior Vice President and General Counsel

**EXHIBIT INDEX**

- (12) Statement re: computation of ratio of earnings to fixed charges.\*
- (15) Letter re: unaudited interim financial information.\*
- (31) Rule 13a-14(a)/15d-14(a) Certifications.\*
- (32) Section 1350 Certifications.\*

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\* Submitted electronically herewith.