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# TEXTRON FINANCIAL CORPORATION

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## Quarterly Financial Statements (Unaudited) For the quarter ended September 30, 2011

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**Textron Financial Corporation is a wholly-owned subsidiary of Textron Inc.**

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*Beginning with the quarter ended March 31, 2011, Textron Financial Corporation is no longer required to file periodic reports with the Securities Exchange Commission (SEC). Reports and other information previously filed with the SEC may be obtained through the SEC's Internet website at <http://www.sec.gov>, at <http://www.textronfinancial.com> or upon request of the Company.*

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**TEXTRON FINANCIAL CORPORATION**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Unaudited)

<i>(In millions)</i>	Three Months Ended		Nine Months Ended	
	September 30, 2011	September 30, 2010	September 30, 2011	September 30, 2010
Finance charges	\$ 37	\$ 59	\$ 120	\$ 215
Rental revenues on operating leases	6	7	18	20
Portfolio losses, net of gains	(13)	(13)	(53)	(46)
Other (loss) income	(2)	2	(7)	(6)
<b>Total revenues</b>	<b>28</b>	<b>55</b>	<b>78</b>	<b>183</b>
Interest expense	20	31	60	96
Depreciation of equipment on operating leases	5	4	14	13
<b>Net interest margin</b>	<b>3</b>	<b>20</b>	<b>4</b>	<b>74</b>
Operating and administrative expenses	26	45	83	130
Provision for losses	2	28	25	127
Special charges	—	94	—	100
<b>Loss before income taxes</b>	<b>(25)</b>	<b>(147)</b>	<b>(104)</b>	<b>(283)</b>
Income tax benefit	(6)	(35)	(31)	(92)
<b>Net loss</b>	<b>\$ (19)</b>	<b>\$ (112)</b>	<b>\$ (73)</b>	<b>\$ (191)</b>

See Notes to the Consolidated Financial Statements.

**TEXTRON FINANCIAL CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**  
(Unaudited)

<i>(In millions)</i>	September 30, 2011	January 1, 2011
<b>Assets</b>		
Cash and equivalents	\$ 25	\$ 33
Finance receivables held for investment, net of unearned income:		
Installment contracts	1,407	1,773
Mortgage loans	716	859
Revolving loans	232	501
Leveraged leases	217	279
Finance leases	170	262
Floorplan receivables	75	182
Total finance receivables held for investment	2,817	3,856
Allowance for losses on finance receivables held for investment	(271)	(339)
Finance receivables held for investment – net	2,546	3,517
Finance receivables held for sale	245	413
Equipment on operating leases – net	145	177
Other assets	382	430
<b>Total assets</b>	<b>\$ 3,343</b>	<b>\$ 4,570</b>
<b>Liabilities and equity</b>		
<b>Liabilities</b>		
Accrued interest and other liabilities	\$ 352	\$ 380
Amounts due to Textron Inc.	597	254
Debt	1,994	3,435
<b>Total liabilities</b>	<b>2,943</b>	<b>4,069</b>
<b>Shareholder's Equity</b>		
Capital surplus	2,022	1,870
Subsidiary preferred stock	1	1
Investment in parent company preferred stock	(25)	(25)
Accumulated other comprehensive loss	(1)	—
Retained deficit	(1,597)	(1,345)
<b>Total shareholder's equity</b>	<b>400</b>	<b>501</b>
<b>Total liabilities and shareholder's equity</b>	<b>\$ 3,343</b>	<b>\$ 4,570</b>

See Notes to the Consolidated Financial Statements.

**TEXTRON FINANCIAL CORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**NINE MONTHS ENDED SEPTEMBER 30, 2011 AND 2010**  
**(Unaudited)**

<i>(In millions)</i>	<b>2011</b>	<b>2010</b>
<b>Cash flows from operating activities:</b>		
Net loss	\$ (73)	\$ (191)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Portfolio losses, net of gains	60	76
Decrease in accrued interest and other liabilities	(41)	(12)
Increase (decrease) in income taxes payable	35	(43)
Deferred income tax provision	(28)	(23)
Provision for losses	25	127
Depreciation and amortization	21	22
Valuation allowance on finance receivables held for sale	19	5
Special charges	—	72
Other — net	—	28
Net cash provided by operating activities	18	61
<b>Cash flows from investing activities:</b>		
Finance receivables originated or purchased	(185)	(580)
Finance receivables repaid	978	1,825
Proceeds from receivable sales	276	643
Proceeds from disposition of other assets, including repossessed assets and properties and operating leases	95	110
Other investments	22	22
Net cash provided by investing activities	1,186	2,020
<b>Cash flows from financing activities:</b>		
Principal payments on line of credit	(1,040)	—
Principal payments on long-term debt	(353)	(1,488)
Principal payments on secured debt	(153)	(194)
Principal payments on nonrecourse debt	(94)	(36)
Net increase (decrease) in intercompany loan due to Textron Inc.	343	(196)
Proceeds from issuance of secured debt	113	—
Capital contributions from Textron Inc.	159	235
Dividends paid to Textron Inc.	(186)	(362)
Other — net	—	5
Net cash used by financing activities	(1,211)	(2,036)
Effect of exchange rate changes on cash	(1)	—
Net (decrease) increase in cash and equivalents	(8)	45
Cash and equivalents at beginning of year	33	144
Cash and equivalents at end of period	\$ 25	\$ 189

See Notes to the Consolidated Financial Statements.

**TEXTRON FINANCIAL CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**Note 1: Basis of Presentation**

The accompanying Consolidated Financial Statements include the accounts of Textron Financial Corporation (Textron Financial or the Company) and its subsidiaries. We have prepared these unaudited consolidated financial statements in accordance with accounting principles generally accepted in the U.S. for interim financial information. Accordingly, these interim financial statements do not include all of the information and footnotes required by accounting principles generally accepted in the U.S. for complete financial statements. The Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements included in Textron Financial Corporation's Annual Report on Form 10-K for the year ended January 1, 2011. In the opinion of management, the interim financial statements reflect all adjustments (consisting only of normal recurring adjustments) that are necessary for the fair presentation of our consolidated financial position, results of operations and cash flows for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year.

In the fourth quarter of 2008, Textron Inc. (Textron) announced a plan to exit the non-captive portion of our commercial finance business, while retaining the captive portion of the business that supports customer purchases of products which Textron manufactures. The decision was made to exit this business in order to address Textron's long-term liquidity position in light of the disruption and instability in the capital markets. During 2009, we transitioned to operating our business in two segments, the Captive Finance segment, which is our ongoing finance business that supports customer purchases of Textron-manufactured products, and the Non-captive Finance segment, which we continue to liquidate.

**Note 2: Comprehensive Loss**

Our comprehensive loss, net of taxes, is provided below:

<i>(In millions)</i>	Three Months Ended		Nine Months Ended	
	September 30, 2011	September 30, 2010	September 30, 2011	September 30, 2010
Net loss	\$ (19)	\$ (112)	\$ (73)	\$ (191)
Other comprehensive (loss) income:				
Change in unrealized losses on marketable securities	—	—	(1)	—
Foreign currency translation	—	78	—	46
Change in unrealized net losses on hedge contracts	—	(1)	—	3
Comprehensive loss	\$ (19)	\$ (35)	\$ (74)	\$ (142)

Foreign currency translation for the three and nine months ended September 30, 2010 includes a \$74 million non-cash reclassification of the cumulative currency translation adjustments related to one of the Company's wholly-owned Canadian subsidiaries to Special charges in the Consolidated Statements of Operations.

**Note 3: Finance Receivables and Allowance for Losses on Finance Receivables Held for Investment**

*Finance Receivables by Product Line / Receivable Class*

Finance receivables by product line, which includes both finance receivables held for investment and finance receivables held for sale, are presented in the following table:

<i>(In millions)</i>	September 30, 2011	January 1, 2011
<b>Captive Finance</b>		
Aviation	\$ 1,442	\$ 1,763
Golf Equipment	141	212
<b>Non-captive Finance</b>		
Golf Mortgage	703	876
Timeshare	495	894
Structured Capital	217	317
Other Liquidating	64	207
Total finance receivables	\$ 3,062	\$ 4,269

### Finance Receivables Held for Investment

Finance receivables held for investment include approximately \$582 million and \$635 million of finance receivables at September 30, 2011 and January 1, 2011, respectively, primarily in the Captive Aviation product line, that have been legally sold to special purpose entities (SPEs) which are consolidated subsidiaries of Textron Financial. The assets of the SPEs are pledged as collateral for \$490 million and \$530 million of debt at September 30, 2011 and January 1, 2011, respectively. Third-party investors have no legal recourse to Textron Financial beyond the credit enhancement provided by the assets of the SPEs.

During the third quarter, we reclassified \$98 million of Timeshare finance receivables from held for investment to held for sale based on an agreement in place at the end of the quarter. We determined a sale of these finance receivables is consistent with our goal to maximize the economic value of our portfolio and accelerate cash collections.

### Credit Quality Indicators and Nonaccrual Finance Receivables

We internally assess the quality of our finance receivables held for investment portfolio based on a number of key credit quality indicators and statistics such as delinquency, loan balance to collateral value, the liquidity position of individual borrowers and guarantors, debt service coverage in Golf Mortgage and default rates of our notes receivable collateral in Timeshare. Because many of these indicators are difficult to apply across an entire class of receivables, we evaluate individual loans on a quarterly basis and classify these loans into three basic categories based on the key credit quality indicators for the individual loan. These three categories are Performing, Watchlist and Nonaccrual.

We classify finance receivables held for investment as Nonaccrual if credit quality indicators suggest full collection of principal and interest is doubtful. In addition, we automatically classify accounts as nonaccrual which are contractually delinquent by more than three months, unless collection of principal and interest is not doubtful. Recognition of interest income is suspended for these accounts and all cash collections are used to reduce the net investment balance. We resume the accrual of interest when the loan becomes contractually current through payment according to the original terms of the loan or, if a loan has been modified, following a period of performance under the terms of the modification, provided we conclude that collection of full principal and interest is no longer doubtful. Previously suspended interest income is recognized at that time.

Accounts are classified as Watchlist when credit quality indicators have deteriorated as compared to typical underwriting criteria and we believe collection of full principal and interest is probable, but not certain. All other finance receivables held for investment that do not meet the Watchlist or Nonaccrual categories are classified as Performing. The table below summarizes our categorization of our finance receivables held for investment, based on internally assigned credit quality indicators.

<i>(Dollars in millions)</i>	September 30, 2011				January 1, 2011			
	Performing	Watchlist	Nonaccrual	Total	Performing	Watchlist	Nonaccrual	Total
<b>Captive Finance</b>								
Aviation	\$ 1,116	\$ 206	\$ 120	\$ 1,442	\$ 1,356	\$ 238	\$ 169	\$ 1,763
Golf Equipment	91	38	12	141	138	51	23	212
<b>Non-captive Finance</b>								
Golf Mortgage	225	133	228	586	163	303	219	685
Timeshare	129	24	214	367	222	77	382	681
Structured Capital	212	5	—	217	290	27	—	317
Other Liquidating	34	—	30	64	130	11	57	198
Total finance receivables held for investment	\$ 1,807	\$ 406	\$ 604	\$ 2,817	\$ 2,299	\$ 707	\$ 850	\$ 3,856
% of total finance receivables held for investment	64.2%	14.4%	21.4%		59.6%	18.3%	22.1%	

Nonaccrual finance receivables decreased \$246 million, or 29%, from the year-end balance, primarily due to reductions of \$168 million in the timeshare portfolio, \$49 million in the aviation portfolio and \$27 million in the other liquidating portfolio. The reduction in the timeshare portfolio was mostly due to the resolution of three significant accounts and cash collections on

several other accounts. The decrease in the aviation portfolio was due to the resolution of several accounts through cash collections and repossession of collateral, partially offset by new accounts identified as nonaccrual in 2011.

We measure delinquency based on the contractual payment terms of our loans and leases. In determining the delinquency aging category of an account, any/all principal and interest received is applied to the most past due principal and/or interest amounts due. If a significant portion of the contractually due payment is delinquent, the entire finance receivable balance is reported in accordance with the most past due delinquency aging category. Finance receivables held for investment by delinquency aging category is summarized in the tables below.

<i>(In millions)</i>	Less than 31 Days Past Due	31-60 Days Past Due	61-90 Days Past Due	Greater than 90 Days Past Due	Total Finance Receivables Held for Investment
<b>September 30, 2011</b>					
<b>Captive Finance</b>					
Aviation	\$ 1,290	\$ 69	\$ 31	\$ 52	\$ 1,442
Golf Equipment	122	8	5	6	141
<b>Non-captive Finance</b>					
Golf Mortgage	502	11	13	60	586
Timeshare	283	—	—	84	367
Structured Capital	217	—	—	—	217
Other Liquidating	45	—	—	19	64
Total finance receivables held for investment	\$ 2,459	\$ 88	\$ 49	\$ 221	\$ 2,817
<b>January 1, 2011</b>					
<b>Captive Finance</b>					
Aviation	\$ 1,607	\$ 67	\$ 41	\$ 48	\$ 1,763
Golf Equipment	171	13	9	19	212
<b>Non-captive Finance</b>					
Golf Mortgage	543	12	7	123	685
Timeshare	533	14	6	128	681
Structured Capital	317	—	—	—	317
Other Liquidating	166	2	1	29	198
Total finance receivables held for investment	\$ 3,337	\$ 108	\$ 64	\$ 347	\$ 3,856

At September 30, 2011 and January 1, 2011, 60+ days contractual delinquency as a percentage of finance receivables held for investment was 9.58% and 10.67%, respectively. There were no accrual status loans that were greater than 90 days past due at September 30, 2011 and January 1, 2011, respectively.

#### *Impaired Loans*

We evaluate individual finance receivables held for investment in non-homogeneous portfolios and larger accounts in homogeneous loan portfolios for impairment on a quarterly basis. Finance receivables classified as held for sale are reflected at the lower of cost or fair value and are excluded from these evaluations. A finance receivable is considered impaired when it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement based on our review of credit quality indicators discussed above. Impaired finance receivables include both nonaccrual accounts and accounts for which full collection of principal and interest remains probable, however, the account's original terms have been, or are expected to be, significantly modified. If the modification specifies an interest rate equal to or greater than a market rate for a finance receivable with comparable risk, the account is not considered impaired in years subsequent to the modification.

A summary of impaired loans with and without a related allowance for losses, excluding leveraged leases, is presented in the following tables.

<i>(In millions)</i>	Captive		Non-captive			Total
	Aviation	Golf Equipment	Golf Mortgage	Timeshare	Other Liquidating	
<b>September 30, 2011</b>						
Impaired loans with a related allowance for losses recorded:						
Recorded investment	\$ 93	\$ 2	\$ 196	\$ 206	\$ 23	\$ 520
Unpaid principal balance	94	2	205	245	30	576
Related allowance	39	—	51	76	12	178
Impaired loans with no related allowance for losses recorded:						
Recorded investment	26	—	108	73	4	211
Unpaid principal balance	27	—	114	87	44	272
<b>Total impaired loans:</b>						
Recorded investment	119	2	304	279	27	731
Unpaid principal balance	121	2	319	332	74	848
Related allowance	39	—	51	76	12	178
<b>January 1, 2011</b>						
Impaired loans with a related allowance for losses recorded:						
Recorded investment	\$ 147	\$ 4	\$ 175	\$ 355	\$ 16	\$ 697
Unpaid principal balance	144	5	178	385	15	727
Related allowance	45	2	39	102	3	191
Impaired loans with no related allowance for losses recorded:						
Recorded investment	17	—	138	69	25	249
Unpaid principal balance	21	—	146	74	84	325
<b>Total impaired loans:</b>						
Recorded investment	164	4	313	424	41	946
Unpaid principal balance	165	5	324	459	99	1,052
Related allowance	45	2	39	102	3	191

The average recorded investment in impaired loans for the first nine months of 2011 and 2010, excluding leveraged leases, is provided below:

<i>(In millions)</i>	Captive		Non-captive			Total
	Aviation	Golf Equipment	Golf Mortgage	Timeshare	Other Liquidating	
<b>For the nine months ended September 30, 2011</b>						
Impaired loans with a related allowance for losses recorded						
	\$ 126	\$ 4	\$ 193	\$ 283	\$ 19	\$ 625
Impaired loans with no related allowance for losses recorded						
	20	—	96	54	15	185
<b>Total</b>	<b>\$ 146</b>	<b>\$ 4</b>	<b>\$ 289</b>	<b>\$ 337</b>	<b>\$ 34</b>	<b>\$ 810</b>
<b>For the nine months ended September 30, 2010</b>						
Impaired loans with a related allowance for losses recorded						
	\$ 197	\$ 5	\$ 184	\$ 356	\$ 23	\$ 765
Impaired loans with no related allowance for losses recorded						
	14	1	112	70	60	257
<b>Total</b>	<b>\$ 211</b>	<b>\$ 6</b>	<b>\$ 296</b>	<b>\$ 426</b>	<b>\$ 83</b>	<b>\$ 1,022</b>

There was no significant interest income recognized on impaired loans during the first nine months of 2011 or 2010.

### *Allowance for Losses on Finance Receivables Held for Investment*

We maintain the allowance for losses on finance receivables held for investment at a level considered adequate to cover inherent losses in the finance receivable held for investment portfolio, based on management's evaluation and analysis by product line. For larger balance accounts specifically identified as impaired, including large accounts in homogeneous portfolios, a reserve is established based on comparing the expected future cash flows, discounted at the finance receivable's effective interest rate, or the fair value if the finance receivable is collateral dependent, to its carrying amount. The expected future cash flows consider collateral value, the financial performance and liquidity of our borrower, the existence and strength of guarantors, estimated recovery costs, including legal expenses and costs associated with the repossession/foreclosure and eventual disposal of collateral. When there is a range of potential outcomes, we perform multiple discounted cash flow analyses and weight the outcomes based on their relative likelihood of occurrence.

The evaluation of our portfolios is inherently subjective, as it requires estimates, including the amount and timing of future cash flows expected to be received on impaired finance receivables and the underlying collateral, which may differ from actual results. While our analysis is specific to each individual account, the most critical factors included in this analysis vary by product line. For the Aviation product line, these factors include industry valuation guides, physical condition of the aircraft, payment history, and existence and financial strength of guarantors. For the Golf Equipment product line, the most critical factors are the age and condition of collateral, while the factors of the Golf Mortgage product line include historical golf course, hotel or marina cash flow performance; estimates of golf rounds and price per round or occupancy and room rates; market discount and capitalization rates; and the existence and financial strength of guarantors. For the Timeshare product line, the critical factors are the historical performance of consumer notes receivable collateral, real estate valuations, operating expenses of the borrower, the impact of potential bankruptcy court rulings on the value of our collateral, legal and other professional expenses and borrower's access to capital.

We also establish an allowance for losses by product line to cover probable, but specifically unknown losses existing in the portfolio. For homogeneous portfolios, including the Aviation and Golf Equipment product lines, the allowance is established as a percentage of non-recourse finance receivables, which have not been identified as requiring specific reserves. The percentage is based on a combination of factors, including historical loss experience, current delinquency and default trends, collateral values and both general economic and specific industry trends. For non-homogeneous portfolios, including the Timeshare and Golf Mortgage product lines, the allowance is established as a percentage of Watchlist balances. The percentage represents a combination of assumed default likelihood and loss severity based on historical experience, industry trends and collateral values. In establishing our allowance for losses on accounts not specifically identified, the most critical factors for the Aviation product line include the collateral value of the portfolio, historical default experience and delinquency trends while the factors considered for the Golf Equipment portfolio include historical loss experience and delinquency trends. For the Golf Mortgage product line, factors include an evaluation of individual loan credit quality indicators such as delinquency, loan balance to collateral value, debt service coverage and the existence and financial strength of guarantors, historical progression from Watchlist to nonaccrual status and historical loss severity. For the Timeshare product line, we evaluate individual loan credit quality indicators such as borrowing base shortfalls for revolving notes receivable facilities, default rates of our notes receivable collateral and the borrower's access to capital, historical progression from Watchlist to nonaccrual status and estimates of loss severity based on analysis of impaired loans in the product line.

Finance receivables held for investment are written down to the fair value (less estimated costs to sell) of the related collateral at the earlier of the date the collateral is repossessed or when no payment has been received for six months, unless management deems the receivable collectible. Finance receivables held for investment are charged off when the remaining balance is deemed to be uncollectible.

A rollforward of the Allowance for losses on finance receivables held for investment and a summary of its composition, based on how the underlying finance receivables held for investment are evaluated for impairment, is presented below. Finance receivables held for investment in the tables below specifically exclude leveraged leases based on authoritative accounting standards.

<i>(In millions)</i>	Captive			Non-captive		
	Aviation	Golf Equipment	Golf Mortgage	Timeshare	Structured Capital and Other Liquidating	Total
<b>For the nine months ended September 30, 2011</b>						
<b>Allowance for losses on finance receivables held for investment</b>						
Beginning balance	\$ 104	\$ 16	\$ 79	\$ 106	\$ 34	\$ 339
Provision for losses	16	(3)	4	7	1	25
Net charge-offs	(27)	(4)	(11)	(35)	(3)	(80)
Transfers	—	—	—	—	(13)	(13)
Ending balance	\$ 93	\$ 9	\$ 72	\$ 78	\$ 19	\$ 271
Ending balance based on individual evaluation	39	—	51	76	12	178
Ending balance based on collective evaluation	54	9	21	2	7	93
<b>Finance receivables held for investment</b>						
Individually evaluated for impairment	\$ 119	\$ 2	\$ 304	\$ 279	\$ 27	\$ 731
Collectively evaluated for impairment	1,323	139	282	88	37	1,869
Ending balance	\$ 1,442	\$ 141	\$ 586	\$ 367	\$ 64	\$ 2,600
<b>For the nine months ended September 30, 2010</b>						
<b>Allowance for losses on finance receivables held for investment</b>						
Beginning balance	\$ 112	\$ 9	\$ 65	\$ 79	\$ 74	\$ 339
Provision for losses	26	12	61	37	(9)	127
Net charge-offs	(36)	(5)	(48)	(5)	(20)	(114)
Ending balance	\$ 102	\$ 16	\$ 78	\$ 111	\$ 45	\$ 352
Ending balance based on individual evaluation	\$ 47	\$ 2	\$ 38	\$ 99	\$ 7	\$ 193
Ending balance based on collective evaluation	55	14	40	12	38	159
<b>Finance receivables held for investment</b>						
Individually evaluated for impairment	\$ 176	\$ 6	\$ 289	\$ 442	\$ 70	\$ 983
Collectively evaluated for impairment	1,727	194	438	565	266	3,190
Ending balance	\$ 1,903	\$ 200	\$ 727	\$ 1,007	\$ 336	\$ 4,173

	September 30, 2011	January 1, 2011
Allowance for losses on finance receivables held for investment as a percentage of finance receivables held for investment	9.62%	8.80%
Allowance for losses on finance receivables held for investment as a percentage of nonaccrual finance receivables held for investment	44.87%	39.92%
Allowance for losses on impaired nonaccrual finance receivables as a percentage of impaired nonaccrual finance receivables	30.50%	23.82%

#### Note 4: Other Assets

Textron Financial's Other assets are summarized below:

<i>(In millions)</i>	September 30, 2011	January 1, 2011
Repossessed assets and properties	\$ 132	\$ 157
Operating assets received in satisfaction of troubled finance receivables	82	107
Other long-term investments	49	50
Derivative financial instruments	27	34
Investments in other marketable securities	22	51
Other	70	31
Total other assets	\$ 382	\$ 430

Repossessed assets and properties are assets we intend to sell in a relatively short period of time and are initially recorded at the lower of net realizable value or the previous carrying value of the related finance receivable. Subsequent declines in fair value are recorded in Portfolio losses, net of gains.

Operating assets received in satisfaction of troubled finance receivables are assets we intend to operate for a substantial period of time and/or make substantial improvements to prior to sale. At September 30, 2011 and January 1, 2011, they primarily represent the assets of operating golf courses that have been repossessed, as well as investments in real estate associated with matured leveraged leases. These assets are initially recorded at the lower of net realizable value or the previous carrying value of the related finance receivable and are measured for impairment on an ongoing basis by comparing the estimated future undiscounted cash flows to the current carrying value. If the sum of the undiscounted cash flows is estimated to be less than the carrying value, the Company records a charge to Portfolio losses, net of gains, for the shortfall between estimated fair value and the carrying amount. Revenues, net of expenses, related to these assets are recorded in Operating and administrative expenses. In the first nine months of 2011, revenues and expenses related to these assets were \$37 million and \$45 million, respectively. In the first nine months of 2010, revenues and expenses were \$35 million and \$44 million, respectively.

#### Note 5: Derivative Financial Instruments

Textron Financial utilizes derivative instruments to mitigate its exposure to fluctuations in interest rates and foreign currencies. These instruments include interest rate exchange agreements and foreign currency exchange agreements. The Company does not hold or issue derivative financial instruments for trading or speculative purposes. The Company did not experience a significant net gain or loss in earnings as a result of the ineffectiveness, or the exclusion of any component from its assessment of hedge effectiveness, of its derivative financial instruments during the first nine months of 2011 or 2010. The fair values of derivative instruments are included in either Other assets or Accrued interest and other liabilities in the Consolidated Balance Sheets.

The following table summarizes the Company's significant derivative activities relating to qualifying hedges of interest rate risk and foreign currency exposure:

	Notional Amount		Fair Value Amount			
	September 30, 2011	January 1, 2011	Assets		Liabilities	
			September 30, 2011	January 1, 2011	September 30, 2011	January 1, 2011
<i>(In millions)</i>						
<b>Fair Value Hedges</b>						
<b>Interest Rate Exchange Agreements</b>						
Fixed-rate debt	\$ 452	\$ 628	\$ 27	\$ 34	\$ —	\$ —
Fixed-rate receivables	430	451	—	—	(9)	(6)
<b>Net Investment Hedges</b>						
<b>Foreign Currency Forward Exchange Agreements</b>						
Foreign-dollar functional currency subsidiary equity	41	38	2	—	—	—
<b>Total</b>	<b>\$ 923</b>	<b>\$ 1,117</b>	<b>\$ 29</b>	<b>\$ 34</b>	<b>\$ (9)</b>	<b>\$ (6)</b>

As a result of our exit plan announced in December 2008, we no longer viewed our investment in our Canadian subsidiary as permanent. Therefore, we began hedging our net investment in this subsidiary during the fourth quarter of 2008 to prevent any reduction in the U.S. dollar equivalent cash flows we will receive upon liquidation of this subsidiary.

The effects of derivative instruments in the Consolidated Statements of Operations are as follows:

	Gain/(Loss)	Location	Amount of Gain/(Loss)			
			Three months ended		Nine months ended	
			September 30, 2011	September 30, 2010	September 30, 2011	September 30, 2010
<i>(In millions)</i>						
<b>Fair Value Hedges</b>						
Interest rate exchange agreements	Interest expense		\$ 3	\$ 8	\$ 7	\$ 27
Interest rate exchange agreements	Finance charges		(6)	—	(8)	(11)

## Note 6: Fair Value of Financial Instruments

We measure fair value at the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We prioritize the assumptions that market participants would use in pricing the asset or liability (the “inputs”) into a three-tier fair value hierarchy. This fair value hierarchy gives the highest priority (Level 1) to quoted prices in active markets for identical assets or liabilities and the lowest priority (Level 3) to unobservable inputs in which little or no market data exists, requiring companies to develop their own assumptions. Observable inputs that do not meet the criteria of Level 1, and include quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets and liabilities in markets that are not active, are categorized as Level 2. Level 3 inputs are those that reflect our estimates about the assumptions market participants would use in pricing the asset or liability, based on the best information available in the circumstances. Valuation techniques for assets and liabilities measured using Level 3 inputs may include methodologies such as the market approach, the income approach or the cost approach, and may use unobservable inputs such as projections, estimates and management’s interpretation of current market data. These unobservable inputs are only utilized to the extent that observable inputs are not available or cost-effective to obtain.

### *Assets Recorded at Fair Value on a Recurring Basis*

#### **Derivative Financial Instruments**

We measure our derivative financial instruments, net at fair value on a recurring basis using Level 2 inputs. The net balance of these derivative financial instruments was \$18 million and \$26 million at September 30, 2011 and January 1, 2011, respectively. The Company’s derivative contracts are not exchange-traded and are measured at fair value utilizing widely accepted, third-party developed valuation models. The actual terms of each individual contract are entered into the model in addition to interest rate and foreign exchange rate data which is based on readily observable market data published by third-party leading financial news and data providers. Credit risk is factored into the fair value of derivative assets and liabilities based on the differential between both the Company’s credit default swap spread for liabilities and the counterparty’s credit default swap spread for assets as compared to a standard AA-rated counterparty, however, this had no significant impact on the valuation as of September 30, 2011 and January 1, 2011.

#### **Investments in Other Marketable Securities**

As of September 30, 2011 and January 1, 2011, our Investments in other marketable securities of \$22 million and \$51 million, respectively, were classified as available for sale and measured at fair value using Level 2 inputs. The estimate of fair value was based on observable market inputs for similar securitization interests in markets that are relatively inactive compared to the market environment in which they were originally issued and bids received from prospective purchasers.

### *Assets Recorded at Fair Value on a Nonrecurring Basis*

The table below presents the balance at September 30, 2011 and September 30, 2010 of those assets that were measured at fair value on a nonrecurring basis during the nine month periods presented, respectively, and the related losses recorded in the Consolidated Statements of Operations. These assets were measured using significant unobservable inputs (Level 3).

<i>(In millions)</i>	<b>Balance at</b>		<b>Total Loss</b>			
	<b>September 30, 2011</b>	<b>September 30, 2010</b>	<b>Three months ended</b>		<b>Nine months ended</b>	
			<b>September 30, 2011</b>	<b>September 30, 2010</b>	<b>September 30, 2011</b>	<b>September 30, 2010</b>
Impaired finance receivables	\$ 347	\$ 521	\$ (23)	\$ (26)	\$ (73)	\$ (130)
Finance receivables held for sale	245	252	(8)	(2)	(22)	(17)
Repossessed assets and properties	81	98	(6)	(12)	(17)	(29)
Operating assets received in satisfaction of troubled finance receivables	34	—	(2)	—	(9)	—
Other investments	—	28	—	—	—	(9)

#### *Impaired Finance Receivables*

Impaired nonaccrual finance receivables represent assets recorded at fair value on a nonrecurring basis since the measurement of required reserves on our impaired finance receivables is significantly dependent on the fair value of the underlying collateral. Fair values of collateral are determined based on the use of appraisals, industry pricing guides, input from market participants, our recent experience selling similar assets or internally developed discounted cash flow models.

Fair value measurements on impaired finance receivables are recorded to Provision for losses in the Consolidated Statements of Operations.

#### *Finance Receivables Held for Sale*

Finance receivables held for sale are recorded at the lower of cost or fair value. As a result of our plan to exit the Non-captive Finance business through a combination of orderly liquidation of finance receivables as they mature and selected sales, \$245 million of finance receivables, which are net of a \$41 million valuation allowance, have been classified as held for sale as of September 30, 2011. The finance receivables held for sale as of September 30, 2011 include assets in the Timeshare and Golf Mortgage product lines. Timeshare finance receivables classified as held for sale were identified at the individual loan level. Golf Mortgage finance receivables were identified as a portion of a larger portfolio with common characteristics based on the intention to balance the sale of certain loans with the collection of others to maximize economic value. These finance receivables are recorded at fair value on a nonrecurring basis during periods in which the fair value is lower than the cost value. Fair value measurements on finance receivables held for sale are recorded in Other loss in the Consolidated Statements of Operations.

During the first nine months of 2011, we sold finance receivables classified as held for sale of \$193 million in the Timeshare product line, \$48 million in the Golf Mortgage product line and \$23 million in the Other Liquidating product line. During the first nine months of 2010, we sold \$375 million of finance receivables classified as held for sale in the Distribution Finance product line and recorded a \$26 million gain related to this sale. In addition, we sold \$84 million of finance receivables classified as held for sale in the Captive Golf equipment product line at book value. Total finance receivable sales in the first nine months of 2011 and 2010 were \$276 million and \$643 million, resulting in total gains of \$3 million and \$30 million, respectively.

There are no active, quoted market prices for our finance receivables. The estimate of fair value was determined based on the use of discounted cash flow models to estimate the exit price we expect to receive in the principal market for each type of loan in an orderly transaction, which includes both the sale of pools of similar assets and the sale of individual loans. The models incorporate estimates of the rate of return, financing cost, capital structure and/or discount rate expectations of prospective purchasers combined with estimated loan cash flows based on credit losses, payment rates and credit line utilization rates. Where available, the assumptions related to the expectations of prospective purchasers are compared to observable market inputs, including bids from prospective purchasers and certain bond market indices for loans of similar perceived credit quality. Although we utilize and prioritize these market observable inputs in our discounted cash flow models, these inputs are not typically derived from markets with directly comparable loan structures, industries and collateral types. Therefore, valuations of finance receivables held for sale involve significant management judgment, which can result in differences between our fair value estimates and those of other market participants.

#### *Repossessed Assets and Properties / Operating Assets Received in Satisfaction of Troubled Finance Receivables*

The fair value of repossessed assets and properties and operating assets received in satisfaction of troubled finance receivables is determined based on the use of appraisals, industry pricing guides, input from market participants, the Company's recent experience selling similar assets or internally developed discounted cash flow models. For repossessed assets and properties, which are considered assets held for sale, if the carrying amount of the asset is higher than the estimated fair value, the Company records a corresponding charge to income for the difference. For operating assets received in satisfaction of troubled finance receivables, if the sum of the undiscounted cash flows is estimated to be less than the carrying value, the Company records a charge to income for any shortfall between estimated fair value and the carrying amount. Fair value measurements on these assets are recorded in Portfolio losses, net of gains, in the Consolidated Statements of Operations.

#### *Other Investments*

Other investments, which are accounted for under the equity method of accounting, are recorded at fair value if the sum of the undiscounted cash flows from the investment is estimated to be less than the carrying value. There are no active, quoted market prices for our equity method investments. The estimates of fair value are determined utilizing internally developed discounted cash flow models, which incorporate assumptions specific to the nature of the investments' business and underlying assets. Fair value measurements on these assets are recorded in Portfolio losses, net of gains, in the Consolidated Statements of Operations.

### Assets and Liabilities Not Recorded at Fair Value

The carrying values and estimated fair values of Textron Financial's financial instruments which are not recorded at fair value are as follows:

<i>(In millions)</i>	September 30, 2011		January 1, 2011	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
<b>Assets:</b>				
Finance receivables held for investment, net of allowance for losses	\$ 2,168	\$ 1,779	\$ 2,991	\$ 2,785
<b>Liabilities:</b>				
Debt	\$ 1,994	\$ 1,876	\$ 3,435	\$ 3,300
Amounts due to Textron Inc.	597	595	254	252
Total	\$ 2,591	\$ 2,471	\$ 3,689	\$ 3,552

#### Finance Receivables Held for Investment

There are no active, quoted market prices for these finance receivables. The estimate of fair value was determined based on the use of discounted cash flow models which incorporate estimates of the rate of return, financing cost, capital structure and/or discount rate expectations of current market participants combined with estimated loan cash flows based on credit losses, payment rates and credit line utilization rates. Where available, the assumptions related to the expectations of current market participants are compared to observable market inputs, including bids from prospective purchasers of similar loans and certain bond market indices for loans of similar perceived credit quality. Although we utilize and prioritize these market observable inputs in our discounted cash flow models, these inputs are rarely derived from markets with directly comparable loan structures, industries and collateral types. Therefore, all valuations of finance receivables involve significant management judgment, which can result in differences between our fair value estimates and those of other market participants. The net carrying amounts of Textron Financial's leveraged leases, finance leases and operating leases are specifically excluded from this disclosure under generally accepted accounting principles. As a result, a significant portion of the assets that are included in the Company's asset and liability management strategy are excluded from this disclosure.

#### Debt

At September 30, 2011 and January 1, 2011, 54% and 35%, respectively, of the estimated fair value of debt was determined based on observable market transactions. The remaining estimated fair values were determined based on discounted cash flow analyses using observable market inputs from debt with similar duration, subordination and credit default expectations.

#### Note 7: Contingencies

There are pending or threatened lawsuits and other proceedings against Textron Financial and its subsidiaries. Some of these suits and proceedings seek compensatory, treble or punitive damages in substantial amounts. These suits and proceedings are being defended by, or contested on behalf of, Textron Financial and its subsidiaries. On the basis of information presently available, Textron Financial believes any such liability would not have a material effect on Textron Financial's financial position or results of operations.

#### Note 8: Financial Information about Operating Segments

As described in Note 1. Basis of Presentation, the Company maintains two segments. The Captive Finance segment finances customer purchases of Textron manufactured aviation products and golf and turf-care equipment. The Non-captive Finance segment is composed of the Golf Mortgage, Structured Capital, Timeshare and Other Liquidating product lines.

<i>(In millions)</i>	Three Months Ended		Nine Months Ended	
	September 30, 2011	September 30, 2010	September 30, 2011	September 30, 2010
<b>Revenues:</b>				
Captive Finance	\$ 28	\$ 23	\$ 83	\$ 89
Non-captive Finance	—	32	(5)	94
<b>Total revenues</b>	<b>\$ 28</b>	<b>\$ 55</b>	<b>\$ 78</b>	<b>\$ 183</b>
<b>Loss before income taxes: (1)(2)</b>				
Captive Finance	\$ 2	\$ (18)	\$ (7)	\$ (33)
Non-captive Finance	(27)	(35)	(97)	(150)
<b>Segment loss</b>	<b>(25)</b>	<b>(53)</b>	<b>(104)</b>	<b>(183)</b>
Special charges	—	94	—	100
<b>Loss before income taxes</b>	<b>\$ (25)</b>	<b>\$ (147)</b>	<b>\$ (104)</b>	<b>\$ (283)</b>

<i>(In millions)</i>	September 30, 2011	January 1, 2011
<b>Finance assets (3):</b>		
Captive Finance	\$ 1,779	\$ 2,224
Non-captive Finance	1,749	2,588
<b>Total finance assets</b>	<b>\$ 3,528</b>	<b>\$ 4,812</b>

- (1) Interest expense is allocated to each segment in proportion to its net investment in finance assets. Net investment in finance assets includes finance assets less deferred income taxes, security deposits and other specifically identified liabilities. The interest allocation matches variable-rate finance assets in the Captive Finance segment with variable-rate debt of similar duration and fixed-rate finance assets in the Captive Finance segment with fixed-rate debt of similar duration to the extent possible. The remaining balance of interest expense incurred is included in the Non-captive Finance segment's interest expense.
- (2) Direct operating expenses are included in each segment's loss. Due to the plan to exit all of our Non-captive Finance segment and the resulting variations in personnel levels and job responsibilities, indirect corporate expenses, comprised primarily of executive salaries and benefits, are included in the segment loss of the Non-captive Finance segment, although a portion of these expenses relate to the Captive Finance segment.
- (3) Finance assets primarily include: finance receivables; equipment on operating leases, net of accumulated depreciation; repossessed assets and properties; operating assets received in satisfaction of troubled finance receivables; investments in other marketable securities and other short- and long-term investments (some of which are classified in Other assets on Textron Financial's Consolidated Balance Sheets).

#### **Note 9: Subsequent Events**

At September 30, 2011, we had \$400 million of outstanding borrowings against our credit facility, and on October 20, 2011, we repaid all outstanding amounts and elected to terminate the facility.