

GENERAL DYNAMICS CORP

Form 11-K

June 27, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 11-K

- X **ANNUAL REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 (No Fee Required)**

For the fiscal year ended December 31, 2002

OR

- O **TRANSITION REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 (No Fee Required)**

For the transition period from _____ to _____

Commission file number 1-3671

- A. Full title of the plan and the address of the plan, if different from that of the issuer named below:

**GENERAL DYNAMICS CORPORATION
HOURLY EMPLOYEES
SAVINGS AND STOCK INVESTMENT PLAN**

- B. Name of issuer of the securities help pursuant to the plan and the address of its principal executive office:

3190 Fairview Park Drive
Falls Church, Virginia 22042-4253

**GENERAL DYNAMICS CORPORATION
HOURLY EMPLOYEES SAVINGS AND STOCK INVESTMENT PLAN**

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	Exhibit 23.2 Consent of KPMG LLP	
	Exhibit 99.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	

Independent Auditors Report

To the General Dynamics Corporation
Hourly Employees Savings and Stock
Investment Plan and Participants:

We have audited the accompanying statements of net assets available for benefits of the General Dynamics Corporation Hourly Employees Savings and Stock Investment Plan (the Plan) as of December 31, 2002 and 2001 and the related statement of changes in net assets available for benefits for the year ended December 31, 2002. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets available for benefits of the Plan as of December 31, 2002 and 2001 and the changes in net assets available for benefits for the year ended December 31, 2002 in conformity with accounting principles generally accepted in the United States of America.

/s/ KPMG LLP

McLean, VA
June 20, 2003

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HOURLY EMPLOYEES SAVINGS AND STOCK INVESTMENT PLAN

Statements of Net Assets Available for Benefits

December 31, 2002 and 2001

	2002	2001
Assets:		
Investments in Master Trust at fair value (note 4)	\$ 361,375,691	392,171,660
Investments in Master Trust at contract value (notes 4 and 8)	247,725,723	230,991,600
Participant loans	16,175,429	12,050,814
Contributions receivable employer	291,604	
Contributions receivable employee	611,545	
	626,179,992	635,214,074
Liabilities:		
Accrued administrative expenses	72,539	70,168
	\$ 626,107,453	635,143,906

See accompanying notes to financial statements.

GENERAL DYNAMICS CORPORATION
HOURLY EMPLOYEES SAVINGS AND STOCK INVESTMENT PLAN

Statement of Changes in Net Assets Available for Benefits

Year ended December 31, 2002

Additions to net assets attributable to:		
Participation in income of master trust investment loss (note 4)		\$ (11,535,179)
Transfers in from other plans		9,556,373
Contributions:		
Participant		25,946,006
Employer		14,098,830
		40,044,836
Total additions		38,066,030
Deductions from net assets attributable to:		
Benefits paid to participants		45,914,740
Administrative expenses		1,187,743
		47,102,483
Total deductions		47,102,483
Net decrease		(9,036,453)
Net assets available for benefits:		
Beginning of year		635,143,906
End of year		\$626,107,453

See accompanying notes to financial statements.

**GENERAL DYNAMICS CORPORATION
HOURLY EMPLOYEES SAVINGS AND STOCK INVESTMENT PLAN**

Notes to Financial Statements

December 31, 2002 and 2001

(1) Plan Description

The following description of the General Dynamics Corporation Hourly Employees Savings and Stock Investment Plan (the Plan) provides only general information. Participants should refer to the Plan document for a more complete description of the Plan's provisions.

(a) General

The Plan is a defined contribution plan covering eligible hourly employees of General Dynamics Corporation (the Company). The Plan document was restated effective January 1, 2001 to comply with recent legislative changes. Substantially all hourly employees of the Company are eligible to participate immediately upon hire except those not included as eligible by a collective bargaining agreement. The Company is the Plan sponsor and the Plan administrator. During 2002, the Gulfstream Aerospace Technologies Hourly 401(k) Plan (Gulfstream Plan) was merged into the Plan. Total assets transferred to the Plan were \$9,556,373.

(b) Contributions

Other than noted below, participants may contribute 1 to 10% of base earnings up to \$12.01 per hour and 1 to 6% of base earnings in excess of \$12.01 per hour up to \$25.00 per hour and another 1 to 4% of base earnings on an unmatched basis. In addition, participants at Advanced Information Systems (AIS), Advanced Technical Products (ATP), C4, Land Systems, and Network Systems (NS) may contribute 1 to 15% of their base earnings on a pre-tax basis. Participants at Bath Iron Works (BIW) may contribute 1 to 16% of their base earnings on a pre-tax basis.

Most company matching contributions to the Plan are invested in Company common stock. However, at certain locations, the Company match follows the participant's election. Generally, participants that are eligible for the Company matching contribution and invest 100% in the General Dynamics Stock Fund receive a 100% Company matching contribution in the General Dynamics Stock Fund. Participants that are eligible for the Company matching contribution but invest less than 100% in the General Dynamics Stock Fund receive a 50% Company matching contribution in the General Dynamics Stock Fund. The matching contributions vary for participants at AIS, ATP, BIW, CA, NS, and Gulfstream.

(c) Participant Accounts

Each participant shall direct his or her contributions to be invested in 1% increments in various funds. Changes to investment elections can be made according to rules set by the Plan administrator. Each participant's account is credited with allocations of (a) his or her pre-tax contributions, (b) the Company's contributions and (c) the earnings on all contributions. The benefit to which a participant is entitled is based on the vested balance of his or her account.

(d) Vesting

Participants are eligible to participate in the Plan upon hire, and their contributions are always 100% vested. Vesting in the Company's contribution portion of their accounts is based on years of continuous service. Although the time required for vesting varies among participants at different subsidiaries of the Company, a participant will be 100% vested after having no more than three years of continuous service. Generally, for participants from many of the Company's subsidiaries, contributions invested in the General Dynamics Stock Fund must be maintained in that fund for five years before becoming eligible for transfer to any other fund. Therefore, a portion of the balance in the General Dynamics Stock Fund represents nonparticipant-directed investments due to the match. With the exception of the General Dynamics Stock Fund, all other investment funds are completely participant-directed.

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Notes to Financial Statements

December 31, 2002 and 2001

(e) Participant Loans

The Plan permits active participants and employed inactive participants to borrow up to 50% of the vested amount in their accounts (as limited by the Plan and the Internal Revenue Service) and to repay the loan by regular payroll deductions over a period of up to five years. Loans are issued at the prime rate of interest. The Plan also offers primary residence loans (up to twenty years).

(f) Payment of Benefits

On termination of service due to death, disability, or retirement, a participant may elect to (a) receive a lump-sum amount equal to the value of the participant's vested interest in his or her account, (b) roll over the value of the participant's vested interest in his or her account into another qualified plan or (c) receive annual installments over a specified period. Participants may also receive hardship withdrawals in a lump-sum payment. Active participants are eligible to receive in-service, hardship, or age 59 1/2 withdrawals.

(g) Forfeited Accounts

Total forfeited nonvested accounts during 2002 totaled \$48,682. These amounts were used to reduce future employer contributions.

(2) Summary of Accounting Policies

(a) Basis of Accounting

The accompanying financial statements are prepared under the accrual basis of accounting.

(b) Investment Valuation and Income Recognition

The Plan's investments are stated at fair value using the quoted market price of the underlying assets except for its fully benefit-responsive investment contracts with insurance companies, which are valued at contract value (see note 8). Loans are carried at cost, which approximates fair value. Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on an accrual basis. Dividends are recorded on the ex-dividend date.

(c) Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and changes therein, and disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

(d) Payment of Benefits

Benefits are recorded when paid.

(3) Tax Status

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The Internal Revenue Service (IRS) issued a favorable determination letter on March 18, 1999, indicating that the Plan is a qualified profit-sharing plan under Section 401(a) of the Internal Revenue Code (IRC). The trust formed thereunder is exempt from federal income tax under Section 501(a). Although the Plan has been amended subsequent to the date of the latest determination from the IRS, the Plan administrator

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Notes to Financial Statements

December 31, 2002 and 2001

The interests for each of the Plans participating in the Master Trust net assets available for benefits at December 31, 2002 and 2001 were as follows:

	<u>2002</u>	<u>2001</u>
General Dynamics Corporation Savings and Stock Investment Plan	\$ 3,247,401,553	3,132,935,404
General Dynamics Corporation Hourly Employees Savings and Stock Investment Plan	626,107,453	635,143,906
Total	\$ 3,873,509,006	3,768,079,310

Investment income (loss) for the Master Trust for the year ended December 31, 2002 is as follows:

Net investment loss in depreciation of investments in registered investment companies	\$(212,843,819)
Interest	98,373,883
Net investment gain in appreciation of investments in corporate bonds	18,775,563
Dividends	17,538,873
Net investment gain in appreciation of General Dynamics Corporation common stock	4,757,704
Net investment gain in appreciation of guaranteed investment contracts	317,448
	<u>\$ (73,080,348)</u>

The interests of each of the Plans participating in the investment income in the Master Trust for the year ended December 31, 2002 were as follows:

General Dynamics Corporation Savings and Stock Investment Plan	\$(61,545,169)
General Dynamics Corporation Hourly Employees Savings and Stock Investment Plan	(11,535,179)
Total	\$ (73,080,348)

The investments of the Master Trust that represent five percent or more of the Plan's net assets each year, were as follows:

	<u>2002</u>	<u>2001</u>
Fixed Income Fund	\$ 1,508,115,565	1,372,218,765
General Dynamics Corporation common stock	1,229,038,124	1,217,794,358
S&P 500 Stock Index Fund	561,132,443	743,555,410
Bond Fund	216,357,123	169,242,175

(5) Plan Termination

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Although it has not expressed any intent to do so, the Company has the right under the Plan to discontinue its contributions at any time and to terminate the Plan subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA). In the event the Plan is terminated, each participant will automatically become vested in the unvested Company contributions. Each participant will receive

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Notes to Financial Statements

December 31, 2002 and 2001

payments based on the specific dollar amounts and shares of the Company's common stock in his or her account.

(6) Plan Administration

The Master Trust primarily pays administrative expenses, although employees of the Company perform certain administrative functions that are not reimbursed by the Master Trust. Although the Company reimbursed no costs in 2002, the Plan document provides that the Company may reimburse these costs. Total administrative expenses of the Master Trust for the year ended December 31, 2002 were \$7,155,081.

Administrative expenses are allocated to the Plan using the percentage of the Plan's interest in the net assets of the Master Trust.

(7) Reconciliation of Financial Statements to Form 5500

The following is a reconciliation of net assets available for benefits as reported in the financial statements at December 31, 2002 and 2001 to Form 5500:

	<u>2002</u>	<u>2001</u>
Net assets available for benefits as reported in the financial statements	\$ 626,107,453	635,143,906
Amount allocated to withdrawing participants	(727,516)	(504,261)
Net assets available for benefits as reported in the Form 5500	<u>625,379,937</u>	<u>634,639,645</u>

The following is a reconciliation of benefits paid to participants as reported in the financial statements for the year ended December 31, 2002, to Form 5500:

Benefits paid to participants as reported in the financial statements	\$45,914,740
Add: Amounts allocated to withdrawing participants at December 31, 2002	727,516
Less: Amounts allocated to withdrawing participants at December 31, 2001	(504,261)
Benefits paid to participants as reported in the Form 5500	<u>\$46,137,995</u>

Amounts allocated to withdrawing participants are recorded on the Form 5500 for benefit claims that have been processed and approved for payment prior to December 31, 2002, but not yet paid as of that date.

(8) Investment Contracts with Insurance Companies

Most investments held by the Master Trust are recorded at quoted market value as stated on public exchanges as of December 31, 2002 and 2001. The Company values the guaranteed investment contracts (GICs) in the Fixed Income Fund and Long Beach Prudential Fund in accordance with AICPA Statement of Position No. 94-4, *Reporting of Investment Contracts Held by Health and Welfare Benefit Plans and Defined Contribution Pension Plans*. As of December 31, 2002 and 2001, the GICs included in the Master Trust are reported at contract value because they have been determined to be fully benefit responsive (i.e., participants may direct the withdrawal or transfer of all or a portion of their investment at contract value). There are no reserves against contract value for credit risk of the contract issuers or otherwise. The contract value of the GICs at December 31, 2002, was \$1,508,932,776 as compared to the fair value of

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Notes to Financial Statements

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\$1,626,354,393. The average yield and crediting interest rates ranged from 6.0% to 12.3% for 2002 and from 6.3% to 9.2% for 2001.

(9) Derivative Financial Instruments

To reduce interest rate risk, the Master Trust has entered into U.S. Treasury and Agency Bond futures contracts. These futures contracts serve to match the price sensitivity and duration of the Master Trust assets with the duration of various obligations of the Master Trust. A futures contract is a contract to purchase U.S. Treasury or Agency Bonds, Notes or Bills at a fixed price on a set date in the future, generally during the next three to six months. The Master Trust pays or receives cash daily for changes in market price of these instruments, with gains or losses reflected in investment income. The total fair value of derivatives at December 31, 2002 and 2001 was \$22,985,359 and \$9,292,812, respectively, and is included in Corporate Bonds.

(10) Non-participant-directed investments

Information about the net assets and the significant components of the changes in net assets relating to the nonparticipant-directed investments as of December 31, 2002 and 2001 and for the year ended December 31, 2002 is as follows:

	<u>2002</u>	<u>2001</u>
General Dynamics Corporation common stock	\$ 188,263,648	174,853,999
Change in net assets:		
Participation in income of the Master Trust	\$ 4,920,586	
Participants' contributions	15,288,706	
Employer's contributions	12,125,338	
Distributions to withdrawn participants	(12,191,315)	
Interfund transfers	(6,733,666)	
Net increase	<u>\$ 13,409,649</u>	

(11) Related Party Transactions

The Plan may, at the discretion of the Plan's participants or via the Company match, invest through the Master Trust an unlimited amount of its assets in common stock of the Company. The Master Trust held 15,179,221 and 14,996,339 shares of common stock of the Company as of December 31, 2002 and 2001, respectively. Dividends in the Master Trust on the Company's common stock were \$17,538,873 for the year ended December 31, 2002.

(12) Subsequent Event

Effective February 1, 2003, the NASSCO 401(k) Savings Plan merged into the Plan and all assets were transferred to the Plan's trustee.

SIGNATURE

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

GENERAL DYNAMICS CORPORATION

As Plan Administrator of the General Dynamics
Corporation Savings and Stock Investment Plan

By /s/ JOHN W. SCHWARTZ

John W. Schwartz
Vice President and Controller

Dated: June 27, 2003