

EATON CORP  
Form 10-Q  
July 29, 2011  
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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, 2011  
Commission file number 1-1396  
EATON CORPORATION  
(Exact name of registrant as specified in its charter)

Ohio 34-0196300  
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification Number)

Eaton Center, Cleveland, Ohio 44114-2584  
(Address of principal executive offices) (Zip Code)  
(216) 523-5000  
(Registrant's telephone number, including area code)

Not applicable  
(Former name, former address and former fiscal year if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No   
There were 341.1 million Common Shares outstanding as of June 30, 2011.

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## PART 1 — FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS.

EATON CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME

(In millions except for per share data)	Three months ended		Six months ended	
	June 30	June 30	June 30	June 30
	2011	2010	2011	2010
Net sales	\$4,090	\$3,378	\$7,893	\$6,481
Cost of products sold	2,862	2,387	5,544	4,588
Selling and administrative expense	698	604	1,363	1,191
Research and development expense	107	103	212	204
Interest expense-net	31	34	63	69
Other income-net	(4	) (1	) (20	) (9
Income before income taxes	396	251	731	438
Income tax expense	58	22	107	53
Net income	338	229	624	385
Less net income for noncontrolling interests	(2	) (3	) (1	) (4
Net income attributable to Eaton common shareholders	\$336	\$226	\$623	\$381
Net income per common share				
Diluted	\$0.97	\$0.66	\$1.80	\$1.12
Basic	0.99	0.67	1.83	1.14
Weighted-average number of common shares outstanding				
Diluted	345.7	340.4	345.7	339.8
Basic	340.9	334.7	340.5	334.5
Cash dividends paid per common share	\$0.34	\$0.25	\$0.68	\$0.50

Net income per common share, weighted-average number of common shares outstanding and cash dividends paid per common share have been restated to give effect to the two-for-one stock split. See Note 1 for additional information. The accompanying notes are an integral part of these condensed consolidated financial statements.

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CONDENSED CONSOLIDATED BALANCE SHEETS

(In millions)	June 30, 2011	December 31, 2010
Assets		
Current assets		
Cash	\$282	\$333
Short-term investments	601	838
Accounts receivable-net	2,625	2,239
Inventory	1,766	1,564
Other current assets	643	532
Total current assets	5,917	5,506
Property, plant and equipment-net	2,589	2,477
Other noncurrent assets		
Goodwill	5,723	5,454
Other intangible assets	2,360	2,272
Deferred income taxes	961	1,001
Other assets	571	542
Total assets	\$18,121	\$17,252
Liabilities and shareholders' equity		
Current liabilities		
Short-term debt	\$101	\$72
Current portion of long-term debt	16	4
Accounts payable	1,534	1,408
Accrued compensation	367	465
Other current liabilities	1,385	1,284
Total current liabilities	3,403	3,233
Noncurrent liabilities		
Long-term debt	3,650	3,382
Pension liabilities	1,222	1,429
Other postretirement benefits liabilities	639	743
Deferred income taxes	499	487
Other noncurrent liabilities	521	575
Total noncurrent liabilities	6,531	6,616
Shareholders' equity		
Eaton shareholders' equity	8,152	7,362
Noncontrolling interests	35	41
Total equity	8,187	7,403
Total liabilities and equity	\$18,121	\$17,252

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



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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)	Six months ended	
	June 30	
	2011	2010
Operating activities		
Net income	\$624	\$385
Adjustments to reconcile to net cash provided by operating activities		
Depreciation and amortization	280	277
Contributions to pension plans	(309 )	(349 )
Contributions to other postretirement benefits plans	(132 )	(39 )
Changes in working capital	(472 )	(121 )
Other-net	56	154
Net cash provided by operating activities	47	307
Investing activities		
Cash paid for acquisitions of businesses	(212 )	—
Capital expenditures for property, plant and equipment	(221 )	(101 )
Sales (purchases) of short-term investments-net	251	(121 )
Other-net	7	6
Net cash used in investing activities	(175 )	(216 )
Financing activities		
Borrowings with original maturities of more than three months		
Proceeds	307	55
Payments	(17 )	(27 )
Borrowings (payments) with original maturities of less than three months-net (primarily commercial paper)	18	(48 )
Cash dividends paid	(232 )	(168 )
Exercise of employee stock options	62	36
Repurchase of shares	(68 )	—
Other-net	(5 )	2
Net cash provided by (used in) financing activities	65	(150 )
Effect of foreign exchange rate changes on cash	12	(32 )
Total decrease in cash	(51 )	(91 )
Cash at the beginning of the period	333	340
Cash at the end of the period	\$282	\$249

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

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## EATON CORPORATION

## NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Amounts are in millions unless indicated otherwise (per share data assume dilution).

## Note 1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of Eaton Corporation (Eaton or Company) have been prepared in accordance with generally accepted accounting principles for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. However, in the opinion of management, all adjustments (consisting of normal recurring accruals) have been made that are necessary for a fair presentation of the condensed consolidated financial statements for the interim periods.

This Form 10-Q should be read in conjunction with the consolidated financial statements and related notes included in Eaton's 2010 Form 10-K. The interim period results are not necessarily indicative of the results to be expected for the full year. Management has evaluated subsequent events through the date this Form 10-Q was filed with the SEC.

On January 27, 2011, Eaton's Board of Directors announced a two-for-one stock split of the Company's common shares effective in the form of a 100% stock dividend. The record date for the stock split was February 7, 2011, and the additional shares were distributed on February 28, 2011. Accordingly, all per share amounts, weighted-average shares outstanding, and equity-based compensation presented in the condensed consolidated financial statements and notes have been adjusted retroactively to reflect the stock split.

Certain prior year amounts have been reclassified to conform to the current year presentation.

## Note 2. ACQUISITIONS OF BUSINESSES

In 2011 and 2010, Eaton acquired businesses and entered into a joint venture in separate transactions. The Consolidated Statements of Income include the results of these businesses from the dates of the transactions or formation. These transactions are summarized below:

Acquired business	Date of transaction	Business segment	Annual sales
ACTOM Low Voltage A South Africa manufacturer and supplier of motor control components, engineered electrical distribution systems and uninterruptible power supply (UPS) systems.	June 30, 2011	Electrical Rest of World	\$65 for the year ended May 31, 2011
C.I. ESI de Colombia S.A. A Colombia-based distributor of industrial electrical equipment and engineering services in the Colombian market, focused on oil and gas, mining, and industrial and commercial construction.	June 2, 2011	Electrical Americas	\$8 for 2010
Internormen Technology Group A Germany-based manufacturer of hydraulic filtration and instrumentation with sales and distribution subsidiaries in China, the United States, India and Brazil.	May 12, 2011	Hydraulics	\$55 for 2010
Eaton-SAMC (Shanghai) Aircraft Conveyance System Manufacturing Co., Ltd. A 49%-owned joint venture in China focusing on the design, development, manufacturing and support of fuel and hydraulic conveyance systems for the global civil aviation market.	March 8, 2011	Aerospace	New joint venture
Tuthill Coupling Group		Hydraulics	

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A United States and France-based manufacturer of pneumatic and hydraulic quick coupling solutions and leak-free connectors used in industrial, construction, mining, defense, energy and power applications.	January 1, 2011		\$35 for the year ended November 30, 2010
Chloride Phoenixtec Electronics			
A China manufacturer of UPS systems. Eaton acquired the remaining shares to increase its ownership from 50% to 100%.	October 12, 2010	Electrical Rest of World	\$25 for the year ended September 30, 2010



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Acquired business	Date of transaction	Business segment	Annual sales
CopperLogic, Inc. A United States-based manufacturer of electrical and electromechanical systems.	October 1, 2010	Electrical Americas	\$35 for the year ended September 30, 2010
Wright Line Holding, Inc. A United States provider of customized enclosures, rack systems, and air-flow management systems to store, power, and secure mission-critical IT data center electronics.	August 25, 2010	Electrical Americas	\$101 for the year ended June 30, 2010
EMC Engineers, Inc. A United States energy engineering and energy services company that delivers energy efficiency solutions for a wide range of governmental, educational, commercial and industrial facilities.	July 15, 2010	Electrical Americas	\$24 for 2009

On June 30, 2011, Eaton reached an agreement to acquire E. Begerow GmbH & Co. KG, a Germany-based system provider of advanced liquid filtration solutions. This business develops and produces technologically innovative filter media and filtration systems for food and beverage, chemical, pharmaceutical and industrial applications and had sales of \$84 in 2010. The terms of the agreement are subject to customary closing conditions. The acquisition is expected to close during the third quarter of 2011. This business will be included in the Hydraulics segment.

## Note 3. ACQUISITION INTEGRATION AND RESTRUCTURING CHARGES

## Acquisition Integration Charges

Eaton incurs charges related to the integration of acquired businesses. A summary of these charges follows:

	Three months ended		Six months ended	
	June 30 2011	2010	June 30 2011	2010
Business segment				
Electrical Americas	\$1	\$1	\$4	\$2
Electrical Rest of World	1	7	1	14
Aerospace	—	1	—	2
Total integration charges before income taxes	\$2	\$9	\$5	\$18
After-tax integration charges	\$2	\$6	\$4	\$12
Per common share	\$—	\$0.02	\$0.01	\$0.03

Charges in 2011 were related primarily to CopperLogic, Wright Line Holding and EMC Engineers. Charges in 2010 were related primarily to Moeller and Phoenixtec. These charges were included in Cost of products sold or Selling and administrative expense, as appropriate. In Note 13. Business Segment Information, the charges reduced Operating profit of the related business segment.

## Workforce Reduction and Plant Closing Liabilities

The following table summarizes the liabilities related to acquisition integration, plant closing charges, and other workforce reduction actions:

	Workforce reductions		Plant closing and other		Total
	Employees	Dollars			
Balance at January 1, 2011	327	\$11	\$5	\$16	
Liabilities recognized	64	1	4	5	
Utilized	(151	) (3	) (7	) (10	)
Balance at June 30, 2011	240	\$9	\$2	\$11	



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## Note 4. GOODWILL

A summary of goodwill follows:

	June 30, 2011	December 31, 2010
Electrical Americas	\$2,155	\$2,061
Electrical Rest of World	1,044	985
Hydraulics	1,112	1,007
Aerospace	1,045	1,037
Truck	153	151
Automotive	214	213
Total goodwill	\$5,723	\$5,454

The increase in goodwill in 2011 was due to foreign currency translation and businesses acquired during 2011. For additional information regarding acquired businesses, see Note 2.

## Note 5. DEBT

On June 16, 2011, Eaton completed the issuance of \$300 floating rate senior unsecured Notes due June 16, 2014 (the Notes). The Notes bear interest annually at a floating rate, reset quarterly, equal to the three-month LIBOR rate for U.S. dollars plus 0.33% (33 basis points). Interest is payable quarterly in arrears beginning on September 16, 2011. The Notes contain a provision which requires the Company to make an offer to purchase all or any part of the Notes at a purchase price of 101% of the principal amount plus accrued and unpaid interest if certain change of control events occur. The Notes are subject to customary non-financial covenants.

Eaton completed the refinancing of a \$500, five-year revolving credit facility in June 2011 (the facility). This refinancing maintains long-term revolving credit facilities at a total of \$1.5 billion. The revolving credit facility is used to support commercial paper borrowings. The facility will expire June 16, 2016, replacing a \$500 facility that had been set to expire on September 1, 2011.

## Note 6. RETIREMENT BENEFITS PLANS

The components of retirement benefits expense follow:

	Three months ended June 30					
	United States		Non-United States		Other postretirement	
	pension benefit expense		pension benefit expense		benefits expense	
	2011	2010	2011	2010	2011	2010
Service cost	\$23	\$20	\$12	\$10	\$4	\$4
Interest cost	33	33	20	17	10	12
Expected return on plan assets	(41	) (39	) (18	) (16	) —	—
Amortization	19	13	3	2	3	2
	34	27	17	13	17	18
Settlement loss	4	4	3	—	—	—
Total expense	\$38	\$31	\$20	\$13	\$17	\$18

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	Six months ended June 30					
	United States		Non-United States		Other postretirement	
	pension benefit expense		pension benefit expense		benefits expense	
	2011	2010	2011	2010	2011	2010
Service cost	\$46	\$40	\$25	\$19	\$8	\$8
Interest cost	66	66	40	34	20	23
Expected return on plan assets	(82	) (78	) (36	) (31	) —	—
Amortization	38	26	6	4	6	5
	68	54	35	26	34	36
Settlement loss	7	9	3	—	—	—
Total expense	\$75	\$63	\$38	\$26	\$34	\$36

During the second quarter of 2011, Eaton contributed \$100 into a Voluntary Employee Benefit Association trust for the pre-funding of postretirement Medicare Part D prescription drug benefits for the Company's eligible United States employees and retirees. The contribution was made as part of the Company's strategy to improve the funding of its pension and postretirement obligations. As part of that strategy, in the first quarter of 2011, the Company contributed \$250 to its United States qualified pension plans.

## Note 7. LEGAL CONTINGENCIES

In December 2010, a Brazilian court held that a judgment obtained by a Brazilian company, Raysul, against another Brazilian company, Saturnia, which was sold by Eaton in 2006, could be enforced against Eaton Ltda. This judgment is based on an alleged violation of an agency agreement between Raysul and Saturnia. At June 30, 2011, the Company has a total accrual of 65 Brazilian Reais related to this matter, comprised of 60 Brazilian Reais recognized in the fourth quarter of 2010 (\$39 based on current exchange rates) with an additional 5 Brazilian Reais recognized in 2011 (\$3 based on current exchange rates) due to subsequent accruals for interest and inflation. The Company expects that any sum it may be required to pay in connection with this matter will not exceed the amount of the recorded liability. In 2010, Eaton filed motions for clarification with the Brazilian court of appeals which were denied on April 6, 2011. On July 1, 2011, Eaton Ltda. filed an appeal of this decision to the Superior Court of Justice in Brasilia. On October 5, 2006, ZF Meritor LLC and Meritor Transmission Corporation (collectively, Meritor) filed an action against Eaton in the United States District Court for Delaware. The action sought damages, which would be trebled under United States antitrust laws, as well as injunctive relief and costs. The suit alleged that Eaton engaged in anti-competitive conduct against Meritor in the sale of heavy-duty truck transmissions in North America. Following a four week trial on liability only, on October 8, 2009, the jury returned a verdict in favor of Meritor. Eaton firmly believes that it competes fairly and honestly for business in the marketplace, and that at no time did it act in an anti-competitive manner. During an earlier stage in the case, the judge concluded that damage estimates contained in a report filed by Meritor were not based on reliable data and the report was specifically excluded from the case. On November 3, 2009, Eaton filed a motion for judgment as a matter of law and to set aside the verdict. That motion was denied on March 10, 2011. On March 14, 2011, Eaton filed a motion for entry of final judgment of liability, zero damages and no injunctive relief. On June 9, 2011, that motion was denied. On July 8, 2011, Eaton filed a motion for interlocutory appeal. Accordingly, an estimate of any potential loss related to this action cannot be made at this time. Eaton is subject to a broad range of claims, administrative and legal proceedings such as lawsuits that relate to contractual allegations, tax audits, patent infringement, personal injuries (including asbestos claims), antitrust matters and employment-related matters. Although it is not possible to predict with certainty the outcome or cost of these matters, the Company believes they will not have a material adverse effect on the consolidated financial statements.

## Note 8. INCOME TAXES

The effective income tax rate for the second quarter of 2011 was 14.7% compared to 9.0% for the second quarter of 2010 and 14.6% for the first six months of 2011 compared to 12.2% for the first six months of 2010. Higher effective tax rates in both the second quarter and first six months of 2011 were primarily attributable to greater levels of income in high tax jurisdictions, particularly in the United States, due to improved economic conditions.



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## Note 9. EQUITY

Eaton has a common share repurchase plan that authorizes the repurchase of 10 million common shares. The shares are expected to be repurchased over time, depending on market conditions, the market price of the Company's common shares, the Company's capital levels and other considerations. During the first six months of 2011, 1.3 million common shares were repurchased in the open market at a total cost of \$68. No common shares were repurchased in the open market in the first six months of 2010.

The changes in Shareholders' equity follow:

	Eaton shareholders' equity	Noncontrolling interests	Total equity
Balance at December 31, 2010	\$7,362	\$41	\$7,403
Net income	623	1	624
Other comprehensive income	368	—	368
Total comprehensive income	991	1	992
Cash dividends paid	(232	) (7	) (239
Issuance of shares under equity-based compensation plans-net	99	—	99
Repurchase of shares	(68	) —	(68
Balance at June 30, 2011	\$8,152	\$35	\$8,187

## Comprehensive Income (Loss)

Comprehensive income (loss) consists primarily of net income, foreign currency translation and related hedging instruments, changes in unrecognized costs of pension and other postretirement benefits, and changes in the effective portion of open derivative contracts designated as cash flow hedges. The following table summarizes the components of Comprehensive income (loss):

	Three months ended June 30		Six months ended June 30	
	2011	2010	2011	2010
Net income	\$338	\$229	\$624	\$385
Foreign currency translation and related hedging instruments	121	(307	) 338	(483
Pensions and other postretirement benefits	19	28	35	47
Cash flow hedges	(4	) (5	) (5	) (9
Other comprehensive income (loss)	136	(284	) 368	(445
Total comprehensive income (loss)	474	(55	) 992	(60
Adjustment for comprehensive income attributable to noncontrolling interests	(1	) (3	) (1	) (4
Total Comprehensive income (loss) attributable to Eaton common shareholders	\$473	\$(58	) \$991	\$(64

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## Net Income per Common Share

A summary of the calculation of net income per common share attributable to common shareholders follows:

(Shares in millions)	Three months ended		Six months ended	
	June 30	June 30	June 30	June 30
	2011	2010	2011	2010
Net income attributable to Eaton common shareholders	\$336	\$226	\$623	\$381
Weighted-average number of common shares outstanding-diluted	345.7	340.4	345.7	339.8
Less dilutive effect of stock options and restricted stock awards	4.8	5.7	5.2	5.3
Weighted-average number of common shares outstanding-basic	340.9	334.7	340.5	334.5

## Net income per common share

Diluted	\$0.97	\$0.66	\$1.80	\$1.12
Basic	0.99	0.67	1.83	1.14

For the second quarter and first six months of 2011, 0.7 million stock options, respectively, were excluded from the calculation of diluted net income per common share because the exercise price of the options exceeded the average market price of the common shares during the period and their effect, accordingly, would have been antidilutive. For the second quarter and first six months of 2010, 7.2 million stock options, respectively, were excluded from the calculation of diluted net income per common share because the exercise price of the options exceeded the average market price of the common shares during the period and their effect, accordingly, would have been antidilutive.

## Note 10. FAIR VALUE MEASUREMENTS

Fair value is measured based on an exit price, representing the amount that would be received to sell an asset or paid to satisfy a liability in an orderly transaction between market participants. Fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, a fair value hierarchy is established, which categorizes the inputs used in measuring fair value as follows: (Level 1) observable inputs such as quoted prices in active markets; (Level 2) inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and (Level 3) unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

A summary of financial instruments recognized at fair value, and the fair value measurements used, follows:

	Total	Quoted prices in active markets for identical assets (Level 1)	Other observable inputs (Level 2)	Unobservable inputs (Level 3)
June 30, 2011				
Cash	\$282	\$282	\$—	\$—
Short-term investments	601	601	—	—
Net derivative contracts	61	—	61	—
Long-term debt converted to floating interest rates by interest rate swaps	44	—	44	—
December 31, 2010				
Cash	\$333	\$333	\$—	\$—
Short-term investments	838	838	—	—
Net derivative contracts	69	—	69	—
	42	—	42	—

Long-term debt converted to floating interest rates  
by  
interest rate swaps

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Eaton values its financial instruments using an industry standard market approach, in which prices and other relevant information is generated by market transactions involving identical or comparable assets or liabilities. No financial instruments were recognized using unobservable inputs.

Other Fair Value Measurements

Long-term debt and the current portion of long-term debt had a carrying value of \$3,666 and fair value of \$4,091 at June 30, 2011 compared to \$3,386 and \$3,787, respectively, at December 31, 2010.

Note 11. DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

In the normal course of business, Eaton is exposed to certain risks related to fluctuations in interest rates, foreign currency exchange rates and commodity prices. The Company uses various derivative and non-derivative financial instruments, primarily interest rate swaps, foreign currency forward exchange contracts, foreign currency swaps and, to a lesser extent, commodity contracts, to manage risks from these market fluctuations. The instruments used by Eaton are straightforward, non-leveraged instruments. The counterparties to these instruments are financial institutions with strong credit ratings. Eaton maintains control over the size of positions entered into with any one counterparty and regularly monitors the credit rating of these institutions. Such instruments are not purchased and sold for trading purposes.

Derivative financial instruments are accounted for at fair value and recognized as assets or liabilities in the Condensed Consolidated Balance Sheets. Accounting for the gain or loss resulting from the change in the fair value of the derivative financial instrument depends on whether it has been designated, and is effective, as part of a hedging relationship and, if so, as to the nature of the hedging activity. Eaton formally documents all relationships between derivative financial instruments accounted for as hedges and the hedged item, as well as its risk-management objective and strategy for undertaking the hedge transaction. This process includes linking all derivative financial instruments to a recognized asset or liability, specific firm commitment, forecasted transaction, or net investment in a foreign operation. These financial instruments can be designated as:

- Hedges of the change in the fair value of a recognized fixed-rate asset or liability, or the firm commitment to acquire such an asset or liability (a fair value hedge); for these hedges, the gain or loss from the derivative financial instrument, as well as the offsetting loss or gain on the hedged item attributable to the hedged risk, are recognized in income during the period of change in fair value.

Hedges of the variable cash flows of a recognized variable-rate asset or liability, or the forecasted acquisition of such an asset or liability (a cash flow hedge); for these hedges, the effective portion of the gain or loss from the derivative financial instrument is recognized in Accumulated other comprehensive income (loss) and reclassified to income in the same period when the gain or loss on the hedged item is included in income.

Hedges of the foreign currency exposure related to a net investment in a foreign operation (a net investment hedge); for these hedges, the effective portion of the gain or loss from the derivative financial instrument is recognized in Accumulated other comprehensive income (loss) and reclassified to income in the same period when the gain or loss related to the net investment in the foreign operation is included in income.

The gain or loss from a derivative financial instrument designated as a hedge that is effective is classified in the same line of the Consolidated Statements of Income as the offsetting loss or gain on the hedged item. The change in fair value of a derivative financial instrument that is not effective as a hedge is immediately recognized in income.

For derivatives that are not designated as a hedge, any gain or loss is immediately recognized in income. The majority of derivatives used in this manner relate to risks resulting from assets or liabilities denominated in a foreign currency and certain commodity contracts that arise in the normal course of business.

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## Derivative Financial Statement Impacts

The fair value of derivative financial instruments recognized in the Condensed Consolidated Balance Sheets follows:

	Notional amount	Other current assets	Other long-term assets	Other current liabilities	Type of hedge	Term
June 30, 2011						
Derivatives designated as hedges						
Fixed-to-floating interest rate swaps	\$540	\$—	\$44	\$—	Fair value	2 to 23 years
Foreign currency exchange contracts	361	5	—	6	Cash flow	12 to 36 months
Commodity contracts	47	2	—	—	Cash flow	12 months
Total		\$7	\$44	\$6		
Derivatives not designated as hedges						
Foreign currency exchange contracts	\$3,586	\$41		\$28		12 months
Commodity contracts	128	3		—		12 months
Total		\$44		\$28		
December 31, 2010						
Derivatives designated as hedges						
Fixed-to-floating interest rate swaps	\$540	\$—	\$42	\$—	Fair value	2 to 23 years
Foreign currency exchange contracts	227	4	—	5	Cash flow	12 to 36 months
Commodity contracts	39	8	—	—	Cash flow	12 months
Cross currency swaps	75	2	—	—	Net investment	12 months
Total		\$14	\$42	\$5		
Derivatives not designated as hedges						
Foreign currency exchange contracts	\$2,777	\$20		\$19		12 months
Commodity contracts	102	17		—		12 months
Total		\$37		\$19		

The foreign currency exchange contracts shown in the table above as derivatives not designated as hedges are primarily contracts entered into to manage foreign currency volatility or exposure on intercompany sales and loans. While Eaton does not elect hedge accounting treatment for these derivatives, Eaton targets managing 100% of the intercompany balance sheet exposure to minimize the effect of currency volatility related to the movement of goods and services in the normal course of its operations. This activity represents the great majority of these foreign currency exchange contracts.

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Amounts recognized in Accumulated other comprehensive income (loss) follow:

	Three months ended June 30 2011		2010	
	Gain (loss) recognized in Accumulated other comprehensive income (loss)	Gain (loss) reclassified from Accumulated other comprehensive income (loss)	Gain (loss) recognized in Accumulated other comprehensive income (loss)	Gain (loss) reclassified from Accumulated other comprehensive income (loss)
Derivatives designated as cash flow hedges				
Foreign currency exchange contracts	\$—	\$—	\$2	\$—
Commodity contracts	(1	) 3	(4	) 3
Derivatives designated as net investment hedges				
Cross currency swaps	1	—	4	—
Total	\$—	\$3	\$2	\$3

	Six months ended June 30 2011		2010	
	Gain (loss) recognized in Accumulated other comprehensive income (loss)	Gain (loss) reclassified from Accumulated other comprehensive income (loss)	Gain (loss) recognized in Accumulated other comprehensive income (loss)	Gain (loss) reclassified from Accumulated other comprehensive income (loss)
Derivatives designated as cash flow hedges				
Foreign currency exchange contracts	\$1	\$—	\$(1	) \$—
Commodity contracts	(1	) 5	(3	) 5
Derivatives designated as net investment hedges				
Cross currency swaps	1	—	4	—
Total	\$1	\$5	\$—	\$5

Gains and losses reclassified from Accumulated other comprehensive income (loss) to the Consolidated Statements of Income were recognized in Cost of products sold.

Amounts recognized in net income follow:

	Three months ended June 30		Six months ended June 30	
	2011	2010	2011	2010
Derivatives designated as fair value hedges				
Fixed-to-floating interest rate swaps	\$8	\$32	\$2	\$36
Related long-term debt converted to floating interest rates by interest rate swaps	(8	) (32	) (2	) (36
	\$—	\$—	\$—	\$—

Gains and losses described above were recognized in Interest expense.

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## Note 12. INVENTORY

The components of inventory follow:

	June 30, 2011	December 31, 2010
Raw materials	\$721	\$651
Work-in-process	255	229
Finished goods	915	800
Inventory at FIFO	1,891	1,680
Excess of FIFO over LIFO cost	(125	) (116
Total inventory	\$1,766	\$1,564

## Note 13. BUSINESS SEGMENT INFORMATION

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated on a regular basis by the chief operating decision maker, or decision making group, in deciding how to allocate resources to an individual segment and in assessing performance. Eaton's operating segments are Electrical Americas, Electrical Rest of World, Hydraulics, Aerospace, Truck and Automotive. For additional information regarding Eaton's business segments, see Note 14 to the Consolidated Financial Statements contained in the 2010 Form 10-K.

Table of ContentsEATON CORPORATION  
BUSINESS SEGMENT INFORMATION

	Three months ended		Six months ended	
	June 30		June 30	
	2011	2010	2011	2010
Net sales				
Electrical Americas	\$1,033	\$894	\$1,997	\$1,696
Electrical Rest of World	787	665	1,530	1,273
Hydraulics	728	568	1,413	1,058
Aerospace	409	370	798	746
Truck	673	492	1,249	945
Automotive	460	389	906	763
Total net sales	\$4,090	\$3,378	\$7,893	\$6,481
Segment operating profit				
Electrical Americas	\$144	\$120	\$276	\$225
Electrical Rest of World	77	60	147	102
Hydraulics	120	77	226	131
Aerospace	50	48	95	97
Truck	120	59	210	105
Automotive	55	39	105	81
Total segment operating profit	566	403	1,059	741
Corporate				
Amortization of intangible assets	(48	) (43	) (96	) (88
Interest expense-net	(31	) (34	) (63	) (69
Pension and other postretirement benefits expense	(37	) (29	) (70	) (61
Other corporate expense-net	(54	) (46	) (99	) (85
Income before income taxes	396	251	731	438
Income tax expense	58	22	107	53
Net income	338	229	624	385
Less net income for noncontrolling interests	(2	) (3	) (1	) (4
Net income attributable to Eaton common shareholders	\$336	\$226	\$623	\$381

Table of ContentsITEM MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
2. OPERATIONS.

Amounts are in millions of dollars or shares unless indicated otherwise (per share data assume dilution).

## TWO-FOR-ONE STOCK SPLIT

On January 27, 2011, Eaton's Board of Directors announced a two-for-one split of the Company's common shares effective in the form of a 100% stock dividend. The record date for the stock split was February 7, 2011, and the additional shares were distributed on February 28, 2011. Accordingly, all share and per share data have been adjusted retroactively to reflect the stock split.

## COMPANY OVERVIEW

Eaton Corporation is a diversified power management company with 2010 sales of \$13.7 billion. The Company is a global technology leader in electrical components and systems for power quality, distribution and control; hydraulics components, systems and services for industrial and mobile equipment; aerospace fuel, hydraulics and pneumatic systems for commercial and military use; and truck and automotive drivetrain and powertrain systems for performance, fuel economy and safety. Eaton has approximately 73,000 employees in over 50 countries, and sells products to customers in more than 150 countries.

Eaton acquired certain businesses that affect comparability on a year over year basis. The Consolidated Statements of Income include the results of these businesses from the dates of the transactions or formation. For a list of business acquisitions and joint ventures impacting the comparative periods, see Note 2 to the Condensed Consolidated Financial Statements.

A summary of Eaton's Net sales, Net income attributable to Eaton common shareholders, and Net income per common share-diluted follows:

	Three months ended		Six months ended	
	June 30		June 30	
	2011	2010	2011	2010
Net sales	\$4,090	\$3,378	\$7,893	\$6,481
Net income attributable to Eaton common shareholders	336	226	623	381
Net income per common share-diluted	\$0.97	\$0.66	\$1.80	\$1.12

## RESULTS OF OPERATIONS

The following discussion of Consolidated Financial Results and Business Segment Results of Operations includes certain non-GAAP financial measures. These financial measures include operating earnings, operating earnings per common share, and operating profit before acquisition integration charges for each business segment, each of which excludes amounts that differ from the most directly comparable measure calculated in accordance with generally accepted accounting principles (GAAP). A reconciliation of each of these financial measures to the most directly comparable GAAP measure is included in the table below and in the discussion of the operating results of each business segment. Management believes that these financial measures are useful to investors because they exclude transactions of an unusual nature, allowing investors to more easily compare Eaton's financial performance period to period. Management uses this information in monitoring and evaluating the on-going performance of Eaton and each business segment.

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## Consolidated Financial Results

	Three months ended			Six months ended			
	June 30			June 30			
	2011	2010	Increase	2011	2010	Increase	
Net sales	\$4,090	\$3,378	21 %	\$7,893	\$6,481	22 %	
Gross profit	1,228	991	24 %	2,349	1,893	24 %	
Percent of net sales	30.0 %	29.3 %		29.8 %	29.2 %		
Income before income taxes	396	251	58 %	731	438	67 %	
Net income	\$338	\$229	48 %	\$624	\$385	62 %	
Less net income for noncontrolling interests	(2 )	(3 )		(1 )	(4 )		
Net income attributable to Eaton common shareholders	336	226	49 %	623	381	64 %	
Excluding acquisition integration charges (after-tax)	2	6		4	12		
Operating earnings	\$338	\$232	46 %	\$627	\$393	60 %	
Net income per common share-diluted	\$0.97	\$0.66	47 %	\$1.80	\$1.12	61 %	
Excluding per share impact of acquisition integration charges (after-tax)	—	0.02		0.01	0.03		
Operating earnings per common share	\$0.97	\$0.68	43 %	\$1.81	\$1.15	57 %	

## Net Sales

Net sales in the second quarter of 2011 increased by 21% compared to the second quarter of 2010. The sales increase was due to 14% from higher core sales, an increase of 6% from the favorable impact of foreign exchange, and an increase of 1% from acquisitions of businesses. End markets increased 12% in the second quarter of 2011 compared to the same period in 2010. Net sales in the first six months of 2011 increased by 22% compared to the first six months of 2010. The sales increase was due to 16% from higher core sales, an increase of 4% from the favorable impact of foreign exchange, and an increase of 2% from acquisitions of businesses. The increase in core sales in both the second quarter and first six months of 2011 reflects the continuing global expansion of the Company's markets and global economic recovery from the depressed levels of 2009. Eaton now anticipates its end markets for all of 2011 will grow by 11%.

## Gross Profit

Gross profit increased by 24% in the second quarter of 2011 compared to the second quarter of 2010, improving to 30.0% of net sales, up 0.7 percentage points from the second quarter of 2010. Gross profit increased by 24% in the first six months of 2011 compared to the first six months of 2010, improving to 29.8% of net sales, up 0.6 percentage points from the first six months of 2010. The increase in the gross profit margin in both the second quarter and first six months of 2011 was primarily due to higher sales volumes and the benefits of substantial changes in the Company's cost structure implemented in the past two years, partially offset by higher raw materials and commodity costs.

## Income Taxes

The effective income tax rate for the second quarter of 2011 was 14.7% compared to 9.0% for the second quarter of 2010 and 14.6% for the first six months of 2011 compared to 12.2% for the first six months of 2010. Higher effective tax rates in both the second quarter and first six months of 2011 were primarily attributable to greater levels of income in high tax jurisdictions, particularly in the United States, due to improved economic conditions.

## Net Income

Net income attributable to Eaton common shareholders of \$336 in the second quarter of 2011 increased 49% compared to net income of \$226 in the second quarter of 2010, and Net income per common share of \$0.97 in the second quarter of 2011 increased 47% over Net income per common share of \$0.66 in the second quarter of 2010. Net income attributable to Eaton common shareholders of \$623 in the first six months of 2011 increased 64% compared to net income of \$381 in the first six months of 2010, and Net income per common share of \$1.80 in the first six months

of 2011 increased 61% over Net income per common share of \$1.12 in the first six months of 2010. The increase in both the second quarter and first six months of 2011 was primarily due to higher sales and the factors noted above that affected gross profit.



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## Business Segment Results of Operations

The following is a discussion of net sales, operating profit and operating profit margin by business segment which includes a discussion of operating profit and operating profit margin before acquisition integration charges. For additional information related to integration charges see Note 3 to the Condensed Consolidated Financial Statements. For additional information related to acquired businesses see Note 2 to the Condensed Consolidated Financial Statements.

## Electrical Americas

	Three months ended			Six months ended			
	June 30		Increase	June 30		Increase	
	2011	2010		2011	2010		
Net sales	\$1,033	\$894	16 %	\$1,997	\$1,696	18 %	
Operating profit	144	120	20 %	276	225	23 %	
Operating margin	13.9 %	13.4 %		13.8 %	13.3 %		
Acquisition integration charges	\$1	\$1		\$4	\$2		
Before acquisition integration charges							
Operating profit	\$145	\$121	20 %	\$280	\$227	23 %	
Operating margin	14.0 %	13.5 %		14.0 %	13.4 %		

Net sales increased 16% in the second quarter of 2011 compared to the second quarter of 2010 due to an increase of 11% in core sales, an increase of 4% from the acquisitions of businesses, and an increase of 1% from the favorable impact of foreign exchange. End markets increased 10% in the second quarter of 2011 compared to the same period in 2010. Net sales increased 18% in the first six months of 2011 compared to the first six months of 2010 due to an increase of 13% in core sales, an increase of 4% from the acquisitions of businesses, and an increase of 1% from the favorable impact of foreign exchange. The increase in net sales in both the second quarter and first six months of 2011 was due to particularly strong growth in the industrial electrical markets.

Operating profit before acquisition integration charges in the second quarter of 2011 increased 20% from the second quarter of 2010. Operating profit before acquisition integration charges in the first six months of 2011 increased 23% from the first six months of 2010. The increase in both the second quarter and first six months of 2011 was largely due to higher net sales as noted above, partially offset by higher raw materials and commodity costs.

## Electrical Rest of World

	Three months ended			Six months ended			
	June 30		Increase	June 30		Increase	
	2011	2010		2011	2010		
Net sales	\$787	\$665	18 %	\$1,530	\$1,273	20 %	
Operating profit	77	60	28 %	147	102	44 %	
Operating margin	9.8 %	9.0 %		9.6 %	8.0 %		
Acquisition integration charges	\$1	\$7		\$1	\$14		
Before acquisition integration charges							
Operating profit	\$78	\$67	16 %	\$148	\$116	28 %	
Operating margin	9.9 %	10.1 %		9.7 %	9.1 %		

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Net sales increased 18% in the second quarter of 2011 compared to the second quarter of 2010 due to an increase of 13% from the favorable impact of foreign exchange and an increase in core sales of 5%. End markets grew 6% in the second quarter of 2011 compared to the second quarter of 2010, with growth of 6% in both European and Asian markets. Net sales increased 20% in the first six months of 2011 compared to the first six months of 2010 due to an increase in core sales of 11%, an increase of 8% from the favorable impact of foreign exchange, and an increase of 1% from the acquisition of a business.

Operating profit before acquisition integration charges in the second quarter of 2011 increased 16% from the second of 2010. Operating profit before acquisition integration charges in the first six months of 2011 increased 28% from the first six months of 2010. The increase in operating profit in both the second quarter and first six months of 2011 was primarily due to higher sales volumes, partially offset by higher raw materials and commodity costs.

## Hydraulics

	Three months ended			Six months ended			
	June 30		Increase	June 30		Increase	
	2011	2010		2011	2010		
Net sales	\$728	\$568	28	% \$1,413	\$1,058	34	%
Operating profit	120	77	56	% 226	131	73	%
Operating margin	16.5	% 13.6	%	16.0	% 12.4	%	

Net sales in the second quarter of 2011 increased 28% compared to the second quarter of 2010 due to higher core sales of 20%, an increase of 5% from the favorable impact of foreign exchange, and an increase of 3% from the acquisition of businesses. Global hydraulics markets grew 18% over the second quarter of 2010, of which U.S. markets grew 21% while markets outside the U.S. grew 16%. Net sales in the first six months of 2011 increased 34% compared to the first six months of 2010 due to higher core sales of 27%, an increase of 4% from the favorable impact of foreign exchange, and an increase of 3% from the acquisition of businesses.

Operating profit in the second quarter of 2011 increased 56% from the second quarter of 2010. Operating profit in the first six months of 2011 increased 73% from the first six months of 2010. The increase in operating profit in both the second quarter and first six months of 2011 was primarily due to higher sales volumes, partially offset by higher raw materials and commodity costs.

## Aerospace

	Three months ended			Increase (decrease)	Six months ended		Increase (decrease)
	June 30		June 30				
	2011	2010	2011	2010			
Net sales	\$409	\$370	11	% \$798	\$746	7	%
Operating profit	50	48	4	% 95	97	(2)	)%
Operating margin	12.2	% 13.0	%	11.9	% 13.0	%	

## Acquisition integration charges

	\$—	\$1		\$—	\$2		
Before acquisition integration charges							
Operating profit	\$50	\$49	2	% \$95	\$99	(4)	)%
Operating margin	12.2	% 13.2	%	11.9	% 13.3	%	

Net sales in the second quarter of 2011 increased 11% compared to the second quarter of 2010 due to higher core sales of 8% and an increase of 3% from the favorable impact of foreign exchange. End markets grew 4% in the second quarter of 2011 compared to the second quarter of 2010. Net sales in the first six months of 2011 increased 7% compared to the first six months of 2010 due to higher core sales of 5% and an increase of 2% from the favorable impact of foreign exchange. Growth in both the second quarter and first six months of 2011 was primarily driven by higher customer demand in commercial OEM markets and commercial aftermarkets.



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Operating profit before acquisition integration charges in the second quarter of 2011 increased 2% from the second quarter of 2010. Operating profit before acquisition integration charges in the first six months of 2011 decreased 4% from the first six months of 2010. Operating margin before acquisition integration charges decreased 1.0 percentage points from 13.2% in the second quarter of 2010 to 12.2% in the second quarter of 2011. Operating margin before acquisition integration charges decreased 1.4 percentage points from 13.3% in the first six months of 2010 to 11.9% in the first six months of 2011. The decrease was primarily due to increased expenses stemming from changes in scope, program delays, and execution of new customer programs.

## Truck

	Three months ended			Six months ended				
	June 30		Increase	June 30		Increase		
	2011	2010		2011	2010			
Net sales	\$673	\$492	37	% \$1,249	\$945	32	%	
Operating profit	120	59	103	%	210	105	100	%
Operating margin	17.8	% 12.0	%	16.8	% 11.1	%		

Net sales increased 37% in the second quarter of 2011 compared to the second quarter of 2010 due to an increase in core sales of 30% and an increase of 7% from the favorable impact of foreign exchange. End markets grew 24% in the second quarter of 2011 compared to the second quarter of 2010, with particular strength in U.S. markets. Net sales increased 32% in the first six months of 2011 compared to the first six months of 2010 due to an increase in core sales of 26% and an increase of 6% from the favorable impact of foreign exchange. The increase in core sales reflects the continuing rebound in global end markets.

Operating profit in the second quarter of 2011 increased 103% from the second quarter of 2010. Operating profit in the first six months of 2011 increased 100% from the first six months of 2010. The increase in operating profit in both the second quarter and first six months of 2011 was primarily due to higher sales volumes in 2011 and the resulting manufacturing efficiencies.

## Automotive

	Three months ended			Six months ended				
	June 30		Increase	June 30		Increase		
	2011	2010		2011	2010			
Net sales	\$460	\$389	18	% \$906	\$763	19	%	
Operating profit	55	39	41	%	105	81	30	%
Operating margin	12.0	% 10.0	%	11.6	% 10.6	%		

Net sales increased 18% in the second quarter of 2011 compared to the second quarter of 2010 due to an increase in core sales of 11% and an increase of 7% from the favorable impact of foreign exchange. The increase in core sales reflects the continued rebound in global automotive markets, which grew 9% in the second quarter of 2011 compared to the second quarter of 2010. U.S. markets grew 15% while markets outside the U.S. grew 7%. Net sales increased 19% in the first six months of 2011 compared to the first six months of 2010 due to an increase in core sales of 14% and an increase of 5% from the favorable impact of foreign exchange. The increase in core sales in the first six months of 2011 is due to the same factors noted above.

Operating profit in the second quarter of 2011 increased 41% from the second quarter of 2010. Operating profit in the first six months of 2011 increased 30% from the first six months of 2010. The increase in operating profit in both the second quarter and first six months of 2011 was primarily due to higher sales volumes.

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## Corporate Expense

	Three months ended		Increase (decrease)		Six months ended		Increase (decrease)	
	June 30				June 30			
	2011	2010			2011	2010		
Amortization of intangible assets	\$48	\$43	12	%	\$96	\$88	9	%
Interest expense-net	31	34	(9)	)%	63	69	(9)	)%
Pension and other postretirement benefits expense	37	29	28	%	70	61	15	%
Other corporate expense-net	54	46	17	%	99	85	16	%
Total corporate expense	\$170	\$152	12	%	\$328	\$303	8	%

Total Corporate expense increased 12% in the second quarter of 2011 to \$170 from \$152 in the second quarter of 2010 due to a 28% increase in Pension and other postretirement benefits expense primarily related to changes in the discount rate and asset return assumptions, a 17% increase in Other corporate expense-net due to higher general corporate expense as Eaton continues to add resources to support its rapid growth, and a 12% increase in Amortization of intangible assets resulting from acquisitions of businesses. Total Corporate expense increased 8% in the first six months of 2011 to \$328 from \$303 in the first six months of 2010 due to the same factors noted above.

## LIQUIDITY, CAPITAL RESOURCES AND CHANGES IN FINANCIAL CONDITION

## Financial Condition and Liquidity

Eaton's objective is to finance its business through operating cash flow and an appropriate mix of equity and long-term and short-term debt. By diversifying its debt maturity structure, Eaton reduces liquidity risk. The Company maintains access to the commercial paper markets through credit facilities that support Eaton's commercial paper borrowings. There were no borrowings outstanding under these revolving credit facilities at June 30, 2011. Over the course of a year, cash, short-term investments and short-term debt may fluctuate in order to manage global liquidity. Eaton believes it has the operating flexibility, cash flow, cash and short-term investment balances, and access to capital markets in excess of the liquidity necessary to meet future operating needs of the business.

During the second quarter in 2011, Eaton completed the issuance of \$300 floating rate senior unsecured Notes due June 16, 2014. The Company also completed the refinancing of a \$500, five-year revolving credit facility which maintains long-term revolving credit facilities at a total of \$1.5 billion. For additional information on these financing transactions, see Note 5 to the Condensed Consolidated Financial Statements.

Eaton was in compliance with each of its debt covenants as of June 30, 2011 and for all periods presented.

## Undistributed Assets of Non-U.S. Subsidiaries

At June 30, 2011, approximately 75% of the Company's consolidated cash and short-term investments resided in non-U.S. locations. These funds are considered permanently reinvested to be used to expand operations either organically or through acquisitions outside the U.S. The largest growth areas that are expected to require capital are in developing foreign markets such as Africa, Brazil, China, India, the Middle East and Southeast Asia. The Company's U.S. operations generate cash flow sufficient to satisfy U.S. operating requirements. The Company does not intend to repatriate any significant amounts of cash to the U.S. in the foreseeable future.

## Sources and Uses of Cash Flow

## Operating Cash Flow

Net cash provided by operating activities was \$47 in the first six months of 2011, a decrease of \$260 compared to \$307 in the first six months of 2010. Operating cash flows in 2011 were primarily impacted by higher working capital requirements compared to 2010 as well as contributions of \$100 to other postretirement benefits plans that were not contributed in 2010. Partially offsetting these uses of cash were higher net income in 2011, which resulted from increased sales due to the global economic recovery that continued in 2011 and the positive effect of recent changes in the Company's cost structure. For additional information on postretirement benefits plans, see Note 6 to the Condensed Consolidated Financial Statements.



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### Investing Cash Flow

Net cash used in investing activities was \$175 in the first six months of 2011, a decrease of \$41 compared to \$216 in the first six months of 2010. The decrease in 2011 was due primarily to cash proceeds of \$251 from the sale of short-term investments compared to purchases of \$121 in the first six months of 2010, partially offset by an increase in capital expenditures to \$221 in 2011 from \$101 in the first six months of 2010 and \$212 related to the acquisitions of businesses. Higher capital expenditures were due to the Company's increased investments in property, plant and equipment to facilitate growth. For additional information on business acquisitions see to Note 2 to the Condensed Consolidated Financial Statements.

### Financing Cash Flow

Net cash provided by financing activities was \$65 in the first six months of 2011, an increase of \$215 compared to a use of cash of \$150 in the first six months of 2010. The increase was primarily due to proceeds received from a \$300 debt issuance completed by Eaton during the second quarter of 2011, partially offset by an increase of \$64 in cash dividends paid in 2011 to Eaton common shareholders. Higher cash dividends paid was due to an increase in the quarterly cash dividend paid per common share from \$0.50 to \$0.68 per share, which was announced during the first quarter of 2011.

### OTHER MATTERS

In December 2010, a Brazilian court held that a judgment obtained by a Brazilian company, Raysul, against another Brazilian company, Saturnia, which was sold by Eaton in 2006, could be enforced against Eaton Ltda. This judgment is based on an alleged violation of an agency agreement between Raysul and Saturnia. At June 30, 2011, the Company has a total accrual of 65 Brazilian Reais related to this matter, comprised of 60 Brazilian Reais recognized in the fourth quarter of 2010 (\$39 based on current exchange rates) and an additional 5 Brazilian Reais recognized in 2011 (\$3 based on current exchange rates) due to subsequent accruals for interest and inflation. The Company expects that any sum it may be required to pay in connection with this matter will not exceed the amount of the recorded liability. In 2010, Eaton filed motions for clarification with the Brazilian court of appeals which were denied on April 6, 2011. On July 1, 2011, Eaton Ltda. filed an appeal of this decision to the Superior Court of Justice in Brasilia.

On October 5, 2006, ZF Meritor LLC and Meritor Transmission Corporation (collectively, Meritor) filed an action against Eaton in the United States District Court for Delaware. The action sought damages, which would be trebled under United States antitrust laws, as well as injunctive relief and costs. The suit alleged that Eaton engaged in anti-competitive conduct against Meritor in the sale of heavy-duty truck transmissions in North America. Following a four week trial on liability only, on October 8, 2009, the jury returned a verdict in favor of Meritor. Eaton firmly believes that it competes fairly and honestly for business in the marketplace, and that at no time did it act in an anti-competitive manner. During an earlier stage in the case, the judge concluded that damage estimates contained in a report filed by Meritor were not based on reliable data and the report was specifically excluded from the case. On November 3, 2009, Eaton filed a motion for judgment as a matter of law and to set aside the verdict. That motion was denied on March 10, 2011. On March 14, 2011, Eaton filed a motion for entry of final judgment of liability, zero damages and no injunctive relief. On June 9, 2011, that motion was denied. On July 8, 2011, Eaton filed a motion for interlocutory appeal. Accordingly, an estimate of any potential loss related to this action cannot be made at this time.

### FORWARD-LOOKING STATEMENTS

This Form 10-Q Report contains forward-looking statements concerning the performance in 2011 of Eaton's worldwide end markets. These statements may discuss goals, intentions and expectations as to future trends, plans, events, results of operations or financial condition, or state other information relating to Eaton, based on current beliefs of management as well as assumptions made by, and information currently available to, management. Forward-looking statements generally will be accompanied by words such as "anticipate," "believe," "could," "estimate," "expect," "forecast," "guidance," "intend," "may," "possible," "potential," "predict," "project" or other similar words, phrases expressions. These statements should be used with caution and are subject to various risks and uncertainties, many of which are outside Eaton's control. The following factors could cause actual results to differ materially from those in the forward-looking statements: unanticipated changes in the markets for the company's business segments;

unanticipated downturns in business relationships with customers or their purchases from us; the availability of credit to customers and suppliers; competitive pressures on sales and pricing; increases in the cost of material and other production costs, or unexpected costs that cannot be recouped in product pricing; the introduction of competing technologies; unexpected technical or marketing difficulties; unexpected claims, charges, litigation or dispute resolutions; strikes or other labor unrest; the impact of acquisitions and divestitures; unanticipated difficulties integrating acquisitions; new laws and governmental regulations; interest rate changes; stock market and currency fluctuations; and unanticipated deterioration of economic and financial conditions in the United States and around the world. Eaton does not assume any obligation to update these forward-looking statements.



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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

There have been no material changes in exposures to market risk since December 31, 2010.

ITEM 4. CONTROLS AND PROCEDURES.

Pursuant to Rule 13a-15 under the Securities Exchange Act of 1934 (the Exchange Act), an evaluation was performed, under the supervision and with the participation of Eaton's management, including Alexander M. Cutler - Chairman, Chief Executive Officer and President; and Richard H. Fearon - Vice Chairman and Chief Financial and Planning Officer, of the effectiveness of the design and operation of Eaton's disclosure controls and procedures. Based on that evaluation, management concluded that Eaton's disclosure controls and procedures were effective as of June 30, 2011.

Disclosure controls and procedures are designed to ensure that information required to be disclosed in Eaton's reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in Eaton's reports filed under the Exchange Act is accumulated and communicated to management, including Eaton's Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

There were no changes in Eaton's internal control over financial reporting that materially affected, or is reasonably likely to materially affect, Eaton's internal control over financial reporting.

PART II — OTHER INFORMATION

ITEM 6. EXHIBITS.

Exhibits — See Exhibit Index attached.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

EATON CORPORATION  
Registrant

Date: July 29, 2011

By: /s/ Richard H. Fearon  
Richard H. Fearon  
Vice Chairman and Chief Financial  
and  
Planning Officer  
(Principal Financial Officer)

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Eaton Corporation

Second Quarter 2011 Report on Form 10-Q

Exhibit Index

3 (a)	Amended Articles of Incorporation (amended and restated as of April 27, 2011) — Incorporated by reference to the Form 10-Q Report for the three months ended March 31, 2011
3 (b)	Amended Regulations (amended and restated as of April 27, 2011) — Incorporated by reference to the Form 10-Q Report for the three months ended March 31, 2011
4	Pursuant to Regulation S-K Item 601(b)(4), Eaton agrees to furnish to the SEC, upon request, a copy of the instruments defining the rights of holders of its other long-term debt
12	Ratio of Earnings to Fixed Charges — Filed in conjunction with this Form 10-Q Report *
31.1	Certification of Chief Executive Officer (Pursuant to Rule 13a-14(a)) — Filed in conjunction with this Form 10-Q Report *
31.2	Certification of Chief Financial Officer (Pursuant to Rule 13a-14(a)) — Filed in conjunction with this Form 10-Q Report *
32.1	Certification of Chief Executive Officer (Pursuant to Rule 13a-14(b) as adopted pursuant to Section 906 of the Sarbanes-Oxley Act) — Filed in conjunction with this Form 10-Q Report *
32.2	Certification of Chief Financial Officer (Pursuant to Rule 13a-14(b) as adopted pursuant to Section 906 of the Sarbanes-Oxley Act) — Filed in conjunction with this Form 10-Q Report *
101.INS	XBRL Instance Document *
101.SCH	XBRL Taxonomy Extension Schema Document *
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document *
101.DEF	XBRL Taxonomy Extension Label Definition Document *
101.LAB	XBRL Taxonomy Extension Label Linkbase Document *
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document *

\* Submitted electronically herewith.

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Statements of Income for the three months ended June 30, 2011 and 2010, (ii) Consolidated Statements of Income for the six months ended June 30, 2011 and 2010, (iii) Condensed Consolidated Balance Sheets at June 30, 2011 and December 31, 2010, (iv) Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2011 and 2010 and (v) Notes to Condensed Consolidated Financial Statements for the six months ended June 30, 2011.

In accordance with Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be part of any registration statement or other document filed under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

