

Eaton Corp plc
Form 10-Q
November 07, 2013
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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 September 30, 2013
Commission file number 000-54863

EATON CORPORATION plc

(Exact name of registrant as specified in its charter)

Ireland

98-1059235

(State or other jurisdiction of incorporation or
organization)

(IRS Employer Identification Number)

Fitzwilliam Hall, Fitzwilliam Place, Dublin 2, Ireland
(Address of principal executive offices)

-
(Zip Code)

+1 (440) 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 (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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 Exchange Act). Yes No

There were 474.5 million Ordinary Shares outstanding as of September 30, 2013.

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PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

EATON CORPORATION plc
CONSOLIDATED STATEMENTS OF INCOME

(In millions except for per share data)	Three months ended		Nine months ended	
	September 30		September 30	
	2013	2012	2013	2012
Net sales	\$5,607	\$3,950	\$16,519	\$11,978
Cost of products sold	3,883	2,747	11,488	8,316
Selling and administrative expense	967	687	2,885	2,079
Research and development expense	166	102	479	313
Interest expense - net	63	42	209	100
Other expense (income) - net	7	(4	) 3	7
Income before income taxes	521	376	1,455	1,163
Income tax expense	7	29	64	123
Net income	514	347	1,391	1,040
Less net income for noncontrolling interests	(4	) (2	) (9	) (2
Net income attributable to Eaton ordinary shareholders	\$510	\$345	\$1,382	\$1,038
Net income per ordinary share				
Diluted	\$1.07	\$1.02	\$2.90	\$3.05
Basic	1.08	1.02	2.92	3.08
Weighted-average number of ordinary shares outstanding				
Diluted	477.2	339.8	476.2	339.7
Basic	474.0	337.6	473.1	336.7
Cash dividends declared per ordinary share	\$0.42	\$0.76	\$1.26	\$1.52

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

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In millions)	Three months ended		Nine months ended	
	September 30		September 30	
	2013	2012	2013	2012
Net income	\$514	\$347	\$1,391	\$1,040
Less net income for noncontrolling interests	(4	) (2	) (9	) (2
Net income attributable to Eaton ordinary shareholders	510	345	1,382	1,038
Other comprehensive income, net of tax				
Currency translation and related hedging instruments	286	146	(104	) 47
Pensions and other postretirement benefits	31	22	120	93
Cash flow hedges	5	4	—	16
Other comprehensive income attributable to Eaton ordinary shareholders	322	172	16	156
Total comprehensive income attributable to Eaton ordinary shareholders	\$832	\$517	\$1,398	\$1,194

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

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CONDENSED CONSOLIDATED BALANCE SHEETS

(In millions)	September 30, 2013	December 31, 2012
Assets		
Current assets		
Cash	\$642	\$577
Short-term investments	698	527
Accounts receivable - net	3,950	3,510
Inventory	2,403	2,339
Deferred income taxes	404	393
Prepaid expenses and other current assets	669	429
Total current assets	8,766	7,775
Property, plant and equipment - net	3,757	3,823
Other noncurrent assets		
Goodwill	14,276	14,211
Other intangible assets	7,231	7,468
Deferred income taxes	328	369
Other assets	954	1,704
Total assets	\$35,312	\$35,350
Liabilities and shareholders' equity		
Current liabilities		
Short-term debt	\$88	\$757
Current portion of long-term debt	576	314
Accounts payable	1,976	1,879
Accrued compensation	430	463
Other current liabilities	1,984	2,008
Total current liabilities	5,054	5,421
Noncurrent liabilities		
Long-term debt	9,029	9,762
Pension liabilities	1,801	2,004
Other postretirement benefits liabilities	733	740
Deferred income taxes	1,513	1,456
Other noncurrent liabilities	1,065	812
Total noncurrent liabilities	14,141	14,774
Shareholders' equity		
Eaton shareholders' equity	16,071	15,113
Noncontrolling interests	46	42
Total equity	16,117	15,155
Total liabilities and equity	\$35,312	\$35,350

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)	Nine months ended	
	September 30	
	2013	2012
Operating activities		
Net income	\$1,391	\$1,040
Adjustments to reconcile to net cash provided by operating activities		
Depreciation and amortization	740	419
Pension expense	239	205
Contributions to pension plans	(303)	(383)
Contributions to other postretirement benefits plans	(45)	(34)
Changes in working capital	(813)	(318)
Other - net	204	48
Net cash provided by operating activities	1,413	977
Investing activities		
Cash paid for acquisitions of businesses	(11)	(554)
Capital expenditures for property, plant and equipment	(372)	(357)
(Purchases) sales of short-term investments - net	(185)	89
Proceeds from sales of businesses	761	3
Other - net	(50)	(38)
Net cash provided by (used in) investing activities	143	(857)
Financing activities		
Proceeds from borrowings	6	600
Payments on borrowings	(1,012)	(321)
Payments of financing costs	—	(63)
Cash dividends paid	(597)	(384)
Exercise of employee stock options	98	54
Excess tax benefit from equity-based compensation	24	18
Other - net	(4)	—
Net cash used in financing activities	(1,485)	(96)
Effect of currency on cash	(6)	16
Total increase in cash	65	40
Cash at the beginning of the period	577	385
Cash at the end of the period	\$642	\$425

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

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EATON CORPORATION plc

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 plc (Eaton or the 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 2012 Form 10-K, as updated by Exhibit 99.1 of Eaton's current report on Form 8-K filed on September 6, 2013. 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 Securities Exchange Commission.

During the first quarter of 2013, Eaton re-segmented certain reportable operating segments due to a reorganization of the Company's businesses. The new reportable business segments include Electrical Products and Electrical Systems and Services (which include legacy Eaton and former Cooper Industries plc (Cooper) electrical businesses), and Vehicle (which includes truck and automotive drivetrain and powertrain systems businesses). For those reportable segments that were re-segmented, previously reported segment information has been updated for all periods presented. See Note 13 for additional information related to these segments.

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

Note 2. ACQUISITIONS AND SALE OF BUSINESSES

In 2012, Eaton acquired businesses in separate transactions. The Consolidated Statements of Income include the results of these businesses from the dates of the transactions. These transactions and the related annual sales prior to acquisition are summarized below:

Acquired businesses	Date of transaction	Business segment	Annual sales
Cooper Industries plc A diversified global manufacturer of electrical products and systems, with brands including Bussmann electrical and electronic fuses; Crouse-Hinds and CEAG explosion-proof electrical equipment; Halo and Metalux lighting fixtures; and Kyle and McGraw-Edison power systems products.	November 30, 2012	Electrical Products; Electrical Systems and Services	\$5,409 for 2011
Rolec Comercial e Industrial S.A. A Chilean manufacturer of integrated power assemblies and low- and medium-voltage switchgear, and a provider of engineering services serving mining and other heavy industrial applications in Chile and Peru.	September 28, 2012	Electrical Systems and Services	\$85 for the 12 months ended September 30, 2012
Jeil Hydraulics Co., Ltd. A Korean manufacturer of track drive motors, swing drive motors, main control valves and remote control valves for the construction equipment market.	July 6, 2012	Hydraulics	\$189 for 2011
Polimer Kaucuk Sanayi ve Pazarlama A.S.	June 1, 2012	Hydraulics	\$335 for 2011

A Turkish manufacturer of hydraulic and industrial hose for construction, mining, agriculture, oil and gas, manufacturing, food and beverage, and chemicals markets. This business sells its products under the SEL brand name.

Gycom Electrical Low-Voltage Power Distribution, Control and Automation

A Swedish electrical low-voltage power distribution, control and automation components business.

June 1,
2012

Electrical
Systems and
Services

\$24
for 2011

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Cooper Industries plc

On November 30, 2012, Eaton Corporation acquired Cooper for a purchase price of \$13,192. The acquisition of Cooper has been accounted for using the acquisition method of accounting which requires, among other things, the assets acquired and liabilities assumed be recognized at their respective fair values as of the acquisition date. For accounting purposes, Eaton has been treated as the acquirer in the transaction.

The estimated purchase price allocation below represents Cooper's opening balance sheet on November 30, 2012, as updated for adjustments made during 2013 primarily related to intangible assets, goodwill, certain property values and the related deferred tax impact. Eaton's consolidated balance sheet at December 31, 2012 and the related notes to the consolidated financial statements have been adjusted to reflect these adjustments. The Company did not revise the Consolidated Statement of Income for the year ended December 31, 2012, as any adjustment was considered immaterial. For additional information, refer to Eaton's Form 10-K for the year ended December 31, 2012, as updated by Exhibit 99.1 of Eaton's current report on Form 8-K filed on September 6, 2013.

	November 30, 2012 (as adjusted)
Working capital accounts ⁽¹⁾	\$2,304
Prepaid expenses and other current assets	204
Property, plant and equipment	885
Investment in Apex Tool Group, LLC	807
Intangible assets	5,250
Other assets	35
Debt	(1,221)
Accounts payable	(519)
Other current liabilities	(673)
Other noncurrent liabilities	(2,185)
Total identifiable net assets	4,887
Goodwill	8,305
Total consideration	\$13,192

⁽¹⁾ Working capital accounts include Cash, Short-term investments, Accounts receivable and Inventory.

The purchase price allocation for Cooper continues to be evaluated. As the Company finalizes the fair value of assets acquired and liabilities assumed, additional purchase price adjustments will be recorded. Fair value estimates are based on a complex series of judgments about future events and uncertainties and rely heavily on estimates and assumptions. The finalization of the purchase accounting assessment will result in changes in the valuation of assets acquired and liabilities assumed and may have a material impact on the Company's results of operations and financial position.

Goodwill has been allocated to the Electrical Products and Electrical Systems and Services segments. The goodwill recognized is calculated as the excess of the consideration transferred over the net assets recognized and represents the expected revenue and cost synergies of the combined company and assembled workforce. Goodwill recognized as a result of the acquisition is not deductible for tax purposes. See Note 4 for additional information about goodwill. Contingent liabilities assumed as part of the transaction total \$226 and are included in Other current liabilities and Other noncurrent liabilities. These contingent liabilities are related to environmental, legal (including product liability claims) and tax matters. Contingent liabilities are recorded at fair value in purchase accounting, aside from those pertaining to uncertainty in income taxes which are an exception to the fair value basis of accounting. Legal matters, and certain environmental matters that are legal in nature, are recorded at the respective probable and estimable amount. The estimated fair values noted above continue to be evaluated and are subject to change upon completion of the final valuation. Changes in the respective fair value of these assumed contingent liabilities may be material.

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Sale of Apex Tool Group, LLC

In July 2010, Cooper formed a joint venture, named Apex Tool Group, LLC (Apex), with Danaher Corporation (Danaher). Apex was formed by combining Cooper's tools business with certain tools businesses from Danaher's Tools and Components segment. Cooper and Danaher each owned a 50% interest in the joint venture, had equal representation on its board of directors and had a 50% voting interest in the joint venture.

On October 10, 2012, Cooper and Danaher announced they had entered into a definitive agreement to sell Apex to Bain Capital for approximately \$1.6 billion subject to post-closing adjustments. On February 1, 2013, the sale of Apex was completed.

Note 3. ACQUISITION INTEGRATION AND RESTRUCTURING CHARGES

Eaton incurs integration charges and transaction costs related to acquired businesses. A summary of these charges follows:

	Three months ended		Nine months ended	
	September 30		September 30	
	2013	2012	2013	2012
Acquisition integration charges				
Electrical Products	\$9	\$1	\$24	\$1
Electrical Systems and Services	10	1	26	8
Hydraulics	8	5	28	9
Total business segments	27	7	78	18
Corporate	9	1	21	2
Total acquisition integration charges	\$36	\$8	\$99	\$20
Transaction costs				
Corporate	\$2	\$19	\$9	\$26
Total transaction costs	\$2	\$19	\$9	\$26
Total acquisition integration charges and transaction costs before income taxes	\$38	\$27	\$108	\$46
Total after income taxes	\$26	\$18	\$73	\$30
Per ordinary share - diluted	\$0.05	\$0.05	\$0.15	\$0.09

Business segment integration charges in 2013 were related primarily to the integrations of Cooper and Polimer Kaucuk Sanayi ve Pazarlama. Business segment integration charges in 2012 were related primarily to the integrations of Internormen Technology Group, Jeil Hydraulics, Polimer Kaucuk Sanayi ve Pazarlama and E. Begerow GmbH & Co. KG. These charges were included in Cost of products sold or Selling and administrative expense, as appropriate. In Business Segment Information the charges reduced Operating profit of the related business segment.

Corporate integration charges in 2013 and 2012 were related primarily to the integration of Cooper. These charges were included in Selling and administrative expense. In Business Segment Information the charges were included in Other corporate expense - net.

Acquisition-related transaction costs, such as investment banking, legal, other professional fees, and costs associated with change in control agreements, are not included as a component of consideration transferred in an acquisition but are expensed as incurred. Acquisition-related transaction costs in 2013 and 2012 were related to the acquisition of Cooper. These charges were included in Selling and administrative expense, Interest expense - net and Other corporate expense - net, as appropriate. In Business Segment Information the charges were included in Interest expense - net and Other corporate expense - net.

See Note 2 for additional information about business acquisitions.

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Restructuring Charges

During the fourth quarter of 2012, Eaton undertook restructuring activities to improve the efficiency of certain businesses. These actions resulted in a charge in the fourth quarter of 2012 of \$50, comprised of severance costs totaling \$34 and other non-cash expenses totaling \$16.

During 2013, Eaton undertook restructuring activities related to the acquisition and integration of Cooper in an effort to gain efficiencies in selling, marketing, traditional back-office functions and manufacturing and distribution. These actions resulted in charges totaling \$26, comprised primarily of severance costs, and are included in the table above in acquisition integration charges. These restructuring initiatives are expected to continue through the second half of 2013.

Restructuring charges were included in Cost of products sold or Selling and administrative expense, as appropriate. In Business Segment Information, the charges reduced Operating profit of the related business segment. See Note 13 for additional information about business segments. As of September 30, 2013, the liabilities related to restructuring actions totaled \$29.

Note 4. GOODWILL

A summary of goodwill follows:

	September 30, 2013	December 31, 2012
Electrical Products	\$5,937	\$5,874
Electrical Systems and Services	5,550	5,531
Hydraulics	1,388	1,404
Aerospace	1,045	1,045
Vehicle	356	357
Total goodwill	\$14,276	\$14,211

Assessing Goodwill for Impairment

Goodwill is tested for impairment annually as of July 1 at the reporting unit level, which is equivalent to Eaton's operating segments. Impairment testing for 2013 was performed using a quantitative analysis under which the fair value for each reporting unit was estimated using a discounted cash flow model, which considered forecasted cash flows discounted at an estimated weighted-average cost of capital. The forecasted cash flows were based on the Company's long-term operating plan and a terminal value was used to estimate the operating segment's cash flows beyond the period covered by the operating plan. The weighted-average cost of capital is an estimate of the overall after-tax rate of return required by equity and debt market holders of a business enterprise. These analyses require the exercise of significant judgments, including judgments about appropriate discount rates, perpetual growth rates and the timing of expected future cash flows of the respective operating segment. Sensitivity analyses were performed around these assumptions in order to assess the reasonableness of the assumptions and the resulting estimated fair values.

For 2013, based on a quantitative analysis, the fair values of Eaton's reporting units continue to substantially exceed the respective carrying amounts.

Note 5. DEBT

On November 30, 2012, the closing date of the acquisition of Cooper, Eaton borrowed \$1,669 on a \$6.75 billion, 364-day bridge facility (the Facility) which was obtained on May 21, 2012. The Facility was obtained to finance a portion of the cash paid to acquire Cooper and was available in a single draw on the closing date of the acquisition. On February 1, 2013, Eaton repaid the outstanding balance on the Facility.

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Note 6. RETIREMENT BENEFITS PLANS

The components of retirement benefits expense follow:

	Three months ended September 30					
	United States		Non-United States		Other postretirement	
	pension benefit expense		pension benefit expense		benefits expense	
	2013	2012	2013	2012	2013	2012
Service cost	\$32	\$28	\$16	\$13	\$5	\$5
Interest cost	37	33	20	18	10	10
Expected return on plan assets	(56)	(46)	(21)	(18)	(2)	(2)
Amortization	33	30	7	3	3	3
	46	45	22	16	16	16
Settlement loss	23	8	—	—	—	—
Total expense	\$69	\$53	\$22	\$16	\$16	\$16
	Nine months ended September 30					
	United States		Non-United States		Other postretirement	
	pension benefit expense		pension benefit expense		benefits expense	
	2013	2012	2013	2012	2013	2012
Service cost	\$96	\$86	\$46	\$37	\$15	\$13
Interest cost	111	100	59	56	27	29
Expected return on plan assets	(169)	(136)	(63)	(56)	(5)	(5)
Amortization	99	88	21	11	10	10
	137	138	63	48	47	47
Settlement loss	39	17	—	2	—	—
Total expense	\$176	\$155	\$63	\$50	\$47	\$47

Note 7. LEGAL CONTINGENCIES

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. 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 September 30, 2013, the Company has a total accrual of 74 Brazilian Reais related to this matter (\$33 based on current exchange rates), comprised of 60 Brazilian Reais recognized in the fourth quarter of 2010 (\$27 based on current exchange rates) with an additional 14 Brazilian Reais recognized through September 30, 2013 (\$6 based on current exchange rates). In 2010, Eaton filed motions for clarification with the Brazilian court of appeals which were denied on April 6, 2011. Eaton Holding and Eaton Ltda. filed appeals on various issues to the Superior Court of Justice in Brasilia. In April 2013, the Superior Court of Justice ruled in favor of Raysul. Additional motions for clarification have been filed with the Superior Court of Justice in Brasilia and an additional appeal is being considered. 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.

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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. That motion was denied on June 9, 2011. On August 19, 2011, the Court entered final judgment of liability but awarded zero damages to plaintiffs. The Court also entered an injunction prohibiting Eaton from offering rebates or other incentives based on purchasing targets but stayed the injunction pending appeal. Eaton appealed the liability finding and the injunction to the Third Circuit Court of Appeals. Meritor cross-appealed the finding of zero damages. On September 28, 2012, the Court of Appeals affirmed the District Court's denial of Eaton's motion for judgment as a matter of law, and let stand the jury verdict in favor of Meritor. The Third Circuit also ruled that the plaintiffs' damages report was properly excluded, but reversed the judgment of zero damages and ordered that the District Court must allow plaintiffs a limited opportunity to amend the damages report, which may be re-considered for reliability and admissibility. Injunctive relief also was vacated. An estimate of any potential loss related to this action cannot be made at this time.

Frisby Corporation, now known as Triumph Actuation Systems, LLC, and other claimants (collectively, the Frisby Parties) asserted claims alleging, among other things, unfair competition, defamation, malicious prosecution, deprivation of civil rights, and antitrust in the Hinds County Circuit Court of Mississippi in 2004 and in the Federal District Court of North Carolina in 2011. Eaton had asserted claims against the Frisby Parties regarding improper use of trade secrets and these claims were dismissed by the Hinds County Circuit Court. The dismissal of Eaton's claims by the Hinds County Circuit Court is on appeal to the Mississippi Supreme Court which, on September 25, 2013, issued an order that stayed all proceedings in the Hinds County Circuit Court pending further order of the Mississippi Supreme Court. During the third quarter of 2013, the Frisby Parties submitted various expert damage designations related to their claims in the Hinds County Circuit Court. An estimate of potential loss, if any, cannot be made at this time.

Note 8. INCOME TAXES

The effective income tax rate for the third quarter of 2013 was 1.4% compared to 7.7% for the third quarter of 2012 and 4.4% for the first nine months of 2013 compared to 10.6% for the first nine months of 2012. The lower effective tax rate in the third quarter of 2013 was primarily attributable to tax effects associated with the acquisition of Cooper. The lower effective tax rate in the first nine months of 2013 was attributable to the item noted above, the recording of the entire 2012 U.S. research and experimentation credit in the first quarter of 2013, the reinstatement in 2013 of the U.S. research and experimentation credit and enhanced utilization of foreign tax credits in the U.S.

At the end of the fourth quarter of 2011, the IRS issued a Statutory Notice of Deficiency (Notice) for Eaton's 2005 and 2006 tax years. The Notice proposes assessments of \$75 in additional taxes plus \$52 in penalties related primarily to transfer pricing adjustments for products manufactured in the Company's facilities in Puerto Rico and the Dominican Republic and sold to affiliated companies located in the U.S., net of agreed credits and deductions. The Company has set its transfer prices for products sold between these affiliates at the same prices that the Company sells such products to third parties. The Notice was issued despite the IRS having previously recognized the validity of the Company's transfer pricing methodology by entering into two successive Advance Pricing Agreements (APAs) that approved and, in fact, required the application of the Company's transfer pricing methodology for the ten year period of 2001 through 2010. For the years 2001 through 2004, the IRS had previously accepted the transfer pricing methodology related to these APAs after a comprehensive review conducted in two separate audit cycles. On December 16, 2011, immediately prior to the Notice being issued, the IRS sent a letter stating that it was canceling the APAs.

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The Company firmly believes that the proposed assessments are without merit. The Company also believes that it was in full compliance with the terms of the two APAs, and that the IRS's unilateral attempt to retroactively cancel these two APAs is also without merit, and represents a breach of the two agreements. On February 29, 2012, the Company filed a Petition with the U.S Tax Court in which it asserted that the transfer pricing established in the two APA contracts meets the arms-length standard set by the U.S. income tax laws, and accordingly, that the two APA contracts should be enforced in accordance with their terms. On June 11, 2012, the Company filed a motion for partial summary judgment with the U.S. Tax Court, asking the U.S. Tax Court to find that the APAs are binding contracts and that the IRS has the burden of proof to substantiate cancellation of the APAs. On June 26, 2013, the U.S. Tax Court ruled that the IRS has the discretion to unilaterally cancel an APA and that the taxpayer bears the burden of proving that the IRS abused that discretion. While the Company disagrees with the Tax Court's ruling, the Company remains confident that it will be able to demonstrate that it was in full compliance with the APAs and that the IRS abused its discretion in canceling the APAs after their terms expired. In addition, the Company continues to believe the transfer pricing methodology contained in the APAs is correct and that the ultimate resolution of this matter will not have a material impact on the consolidated financial statements.

During the third quarter of 2013, adjustments were made to Deferred income taxes and Other current liabilities on the Consolidated Balance Sheet at December 31, 2012 to net certain deferred tax assets against deferred tax liabilities within current and long-term classifications in the amount of \$49 and \$885, respectively. These adjustments are related to the acquisition of Cooper and combining both Eaton and Cooper U.S. operations into one tax paying component. The Company concluded that the impact of these adjustments were not material to its 2012 consolidated financial statements.

Note 9. EQUITY

The changes in Shareholders' equity follow:

	Eaton shareholders' equity	Noncontrolling interests	Total equity
Balance at December 31, 2012	\$15,113	\$42	\$15,155
Net income	1,382	9	1,391
Other comprehensive loss	16	—	16
Cash dividends paid	(597	) (5	) (602
Issuance of shares under equity-based compensation plans - net	157	—	157
Balance at September 30, 2013	\$16,071	\$46	\$16,117

The changes in Accumulated other comprehensive (loss) income follow:

	Currency translation and related hedging instruments	Pensions and other postretirement benefits	Cash flow hedges	Total
Balance at December 31, 2012	\$(367	) \$(1,599	) \$2	\$(1,964
Other comprehensive (loss) income before reclassifications	(104	) 12	(1	) (93
Amounts reclassified from Accumulated other comprehensive (loss) income	—	108	1	109
Net current-period other comprehensive (loss) income	(104) 120	—	16
Balance at September 30, 2013	\$(471) \$(1,479) \$2	\$(1,948

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The reclassifications out of Accumulated other comprehensive loss follow:

	Nine months ended September 30, 2013	Consolidated Statements of Income classification
Amortization of defined benefit pension items		
Actuarial loss	\$(169)	)¹
	(169))
Tax benefit	61	
Total, net of tax	(108))
Gains and losses on cash flow hedges		
Floating-to-fixed interest rate swaps	(1)	) Interest expense - net
Currency exchange contracts	1	) Cost of products sold
Commodity contracts	(1)	) Cost of products sold
	(1))
Tax expense	—	
Total, net of tax	(1))
Total reclassifications for the period	\$(109))

¹ These components of Accumulated other comprehensive loss are included in the computation of net periodic pension cost. See Note 6 for additional information about defined benefit pension items.

Net Income per Ordinary Share

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

(Shares in millions)	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
Net income attributable to Eaton ordinary shareholders	\$510	\$345	\$1,382	\$1,038
Weighted-average number of ordinary shares outstanding - diluted	477.2	339.8	476.2	339.7
Less dilutive effect of equity-based compensation	3.2	2.2	3.1	3.0
Weighted-average number of ordinary shares outstanding - basic	474.0	337.6	473.1	336.7
Net income per ordinary share				
Diluted	\$1.07	\$1.02	\$2.90	\$3.05
Basic	1.08	1.02	2.92	3.08

For the third quarter and the first nine months of 2013, 0.2 million stock options were excluded from the calculation of diluted net income per ordinary share because the exercise price of the options exceeded the average market price of the ordinary shares during the period and their effect, accordingly, would have been antidilutive. For the third quarter and the first nine months of 2012, 4.2 million and 2.5 million stock options, respectively, were excluded from the calculation of diluted net income per ordinary share because the exercise price of the options exceeded the average market price of the ordinary shares during the period and their effect, accordingly, would have been antidilutive.

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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)
September 30, 2013				
Cash	\$642	\$642	\$—	\$—
Short-term investments	698	698	—	—
Net derivative contracts	(7	) —	(7) —
Long-term debt converted to floating interest rates by interest rate swaps - net	4	—	4	—
December 31, 2012				
Cash	\$577	\$577	\$—	\$—
Short-term investments	527	527	—	—
Net derivative contracts	83	—	83	—
Long-term debt converted to floating interest rates by interest rate swaps - net	87	—	87	—

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 \$9,605 and fair value of \$9,787 at September 30, 2013 compared to \$10,076 and \$10,793, respectively, at December 31, 2012. The fair value of Eaton's debt instruments was estimated using prevailing market interest rates on debt with similar creditworthiness, terms and maturities and is considered a Level 2 fair value measurement.

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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, currency exchange rates and commodity prices. The Company uses various derivative and non-derivative financial instruments, primarily interest rate swaps, currency forward exchange contracts, 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 designated hedges and the hedged item, as well as its risk-management objective and strategy for undertaking the hedge transaction. This process includes linking 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 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 currency and certain commodity contracts that arise in the normal course of business. Gains and losses associated with commodity hedge contracts are classified in Cost of products sold.

Eaton uses certain of its debt denominated in various currencies to hedge portions of its net investments in foreign operations against currency exposure (net investment hedges). Debt denominated in various currencies and designated as non-derivative net investment hedging instruments was \$102 and \$116 at September 30, 2013 and December 31, 2012, respectively.

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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	Other long-term liabilities	Type of hedge	Term
September 30, 2013							
Derivatives designated as hedges							
Fixed-to-floating interest rate swaps	\$ 3,090	\$ 1	\$ 45	\$—	\$ 42	Fair value	6 months to 21 years
Floating-to-fixed interest rate swaps	300	—	—	1	—	Cash flow	9 months
Currency exchange contracts	451	7	—	2	—	Cash flow	12 to 36 months
Commodity contracts	2	—	—	—	—	Cash flow	12 months
Total		\$ 8	\$ 45	\$ 3	\$ 42		
Derivatives not designated as hedges							
Currency exchange contracts	\$ 4,729	\$ 25		\$ 40			12 months
Commodity contracts	10	—		—			12 months
Total		\$ 25		\$ 40			
December 31, 2012							
Derivatives designated as hedges							
Fixed-to-floating interest rate swaps	\$ 1,290	\$ 2	\$ 85	\$—	\$—	Fair value	6 months to 21 years
Floating-to-fixed interest rate swaps	300	—	—	—	2	Cash flow	1 year
Currency exchange contracts	451	9	—	4	—	Cash flow	12 to 36 months
Commodity contracts	17	—	—	—	—	Cash flow	12 months
Total		\$ 11	\$ 85	\$ 4	\$ 2		
Derivatives not designated as hedges							
Currency exchange contracts	\$ 4,997	\$ 23		\$ 31			12 months
Commodity contracts	19	1		—			12 months
Total		\$ 24		\$ 31			

The currency exchange contracts shown in the table above as derivatives not designated as hedges are primarily contracts entered into to manage 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 currency exchange contracts.

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

	Three months ended September 30			
	2013	Gain (loss) reclassified from Accumulated other comprehensive income (loss)	2012	Gain (loss) reclassified from Accumulated other comprehensive income (loss)
Derivatives designated as cash flow hedges				
Floating-to-fixed interest rate swaps	\$—	\$—	\$(1) \$—
Currency exchange contracts	9	—	4	2
Commodity contracts	—	—	2	(3
Total	\$9	\$—	\$5	\$(1

	Nine months ended September 30			
	2013	Gain (loss) reclassified from Accumulated other comprehensive income (loss)	2012	Gain (loss) reclassified from Accumulated other comprehensive income (loss)
Derivatives designated as cash flow hedges				
Floating-to-fixed interest rate swaps	\$—	\$(1	) \$(3	) \$(1
Foreign currency exchange contracts	1	1	10	1
Commodity contracts	(1	) (1	) 2	(7
Total	\$—	\$(1	) \$9	\$(7

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

Amounts recognized in net income follow:

	Three months ended		Nine months ended	
	September 30	2012	September 30	2012
	2013	2012	2013	2012
Derivatives designated as fair value hedges				
Fixed-to-floating interest rate swaps	\$5	\$11	\$(83	) \$25
Related long-term debt converted to floating interest rates by interest rate swaps	(5	) (11	) 83	(25
	\$—	\$—	\$—	\$—

Gains and losses described above were recognized in Interest expense - net.

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Note 12. INVENTORY

The components of inventory follow:

	September 30, 2013	December 31, 2012
Raw materials	\$1,008	\$919
Work-in-process	400	424
Finished goods	1,118	1,129
Inventory at FIFO	2,526	2,472
Excess of FIFO over LIFO cost	(123	) (133
Total inventory	\$2,403	\$2,339

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.

During the first quarter of 2013, Eaton re-segmented certain reportable operating segments due to a reorganization of the Company's businesses. The new reportable business segments are Electrical Products and Electrical Systems and Services (which include legacy Eaton and former Cooper electrical businesses), and Vehicle (which includes truck and automotive drivetrain and powertrain systems businesses). Previously reported segment financial information has been updated for all periods reported.

Electrical Products consists of electrical components, industrial controls, residential products, single phase power quality, emergency lighting, fire detection, wiring devices, structural support systems, circuit protection, and lighting products.

Electrical Systems and Services consists of power distribution and assemblies, three phase power quality, hazardous duty electrical equipment, intrinsically safe explosion-proof instrumentation, utility power distribution, power reliability equipment, and services.

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	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
Net sales				
Electrical Products	\$1,817	\$919	\$5,235	\$2,708
Electrical Systems and Services	1,639	910	4,784	2,675
Hydraulics	739	763	2,267	2,267
Aerospace	448	419	1,328	1,285
Vehicle	964	939	2,905	3,043
Total net sales	\$5,607	\$3,950	\$16,519	\$11,978
Segment operating profit				
Electrical Products	\$301	\$172	\$814	\$462
Electrical Systems and Services	231	111	668	278
Hydraulics	89	93	271	325
Aerospace	64	49	193	168
Vehicle	161	144	465	472
Total segment operating profit	846	569	2,411	1,705
Corporate				
Amortization of intangible assets	(110	) (45	) (325	) (129
Interest expense - net	(63	) (42	) (209	) (100
Pension and other postretirement benefits expense	(55	) (41	) (136	) (121
Inventory step-up adjustment	—	(1	) (34	) (4
Other corporate expense - net	(97	) (64	) (252	) (188
Income before income taxes	521	376	1,455	1,163
Income tax expense	7	29	64	123
Net income	514	347	1,391	1,040
Less net income for noncontrolling interests	(4	) (2	) (9	) (2
Net income attributable to Eaton ordinary shareholders	\$510	\$345	\$1,382	\$1,038
Business segment operating profit was reduced by acquisition integration charges as follows:				
	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
Electrical Products	\$9	\$1	\$24	\$1
Electrical Systems and Services	10	1	26	8
Hydraulics	8	5	28	9
Total	\$27	\$7	\$78	\$18

Corporate acquisition integration charges totaled \$9 and \$21 for the third quarter and the first nine months of 2013, respectively, and \$1 and \$2 for the third quarter and the first nine months of 2012, respectively. Corporate acquisition integration charges related primarily to the acquisition of Cooper and are included above in Other corporate expense - net.

Acquisition-related transaction costs, such as investment banking, legal, other professional fees, and costs associated with change in control agreements, are included above in Interest expense - net and Other corporate expense - net and are related to the acquisition of Cooper. These charges totaled \$2 and \$9 for the third quarter and the first nine months of 2013, respectively, and \$19 and \$26 for the third quarter and the first nine months of 2012, respectively. See Note 3 for additional information about acquisition integration charges and transaction costs.

For additional information regarding Eaton's business segments, see Note 14 to the Consolidated Financial Statements contained in the 2012 Form 10-K, as updated by Exhibit 99.1 of Eaton's current report on Form 8-K filed on

September 6, 2013.

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Note 14. CONDENSED CONSOLIDATING FINANCIAL STATEMENTS

On November 20, 2012, Eaton Corporation issued senior notes (the "Senior Notes") totaling \$4,900 to finance part of the cash portion of the acquisition of Cooper. Eaton and certain other of Eaton's principal 100% owned operating subsidiaries (the "Guarantors") fully and unconditionally guaranteed (subject, in the case of the Guarantors, other than Eaton, to customary release provisions as described below), on a joint and several basis, the Senior Notes. The following condensed consolidating financial statements are included so that separate financial statements of Eaton, Eaton Corporation and each of the Guarantors are not required to be filed with the Securities and Exchange Commission. The consolidating adjustments primarily relate to eliminations of investments in subsidiaries and intercompany balances and transactions. The condensed consolidating financial statements present investments in subsidiaries using the equity method of accounting.

The guarantee of a Guarantor that is not a parent of the issuer will be automatically and unconditionally released and discharged in the event of any sale of the Guarantor or of all or substantially all of its assets; or following, or in connection with, the release or termination of the Guarantor as a guarantor under all other U.S. debt securities or U.S. syndicated credit facilities, subject to limitations set forth in the indenture. The guarantee of a Guarantor that is a direct or indirect parent of the issuer will be automatically and unconditionally released and discharged following, or in connection with, the release or termination of the Guarantor as a guarantor under all other debt securities or syndicated credit facilities (in both cases, U.S. or otherwise), subject to limitations set forth in the indenture.

Eaton was incorporated under the laws of Ireland on May 10, 2012, and became the successor registrant to Eaton Corporation on November 30, 2012 in connection with the acquisition of Cooper. Therefore, for presentation purposes of entities under common control, Eaton is presented as the parent company in the 2013 condensed consolidating financial statements. For periods prior to November 30, 2012, Eaton Corporation is presented as the parent company.

CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2013

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net sales	\$—	\$1,695	\$1,636	\$3,424	\$(1,148)	\$5,607
Cost of products sold	—	1,319	1,214	2,500	(1,150)	3,883
Selling and administrative expense	2	370	194	401	—	967
Research and development expense	—	71	46	49	—	166
Interest expense (income) - net	—	63	7	(7)	—	63
Other expense (income) - net	—	2	(9)	14	—	7
Equity in (earnings) loss of subsidiaries, net of tax	(563)	(292)	(676)	(224)	1,755	—
Intercompany expense (income) - net	63	(90)	222	(195)	—	—
Income before income taxes	498	252	638	886	(1,753)	521
Income tax expense (benefit)	(12)	(21)	45	(5)	—	7
Net income	510	273	593	891	(1,753)	514
Less net income for noncontrolling interests	—	—	—	(1)	(3)	(4)
Net income attributable to Eaton ordinary shareholders	\$510	\$273	\$593	\$890	\$(1,756)	\$510
Other comprehensive loss	\$322	\$109	\$347	\$505	\$(961)	\$322

Total comprehensive income attributable to Eaton ordinary shareholders	\$832	\$382	\$940	\$1,395	\$(2,717) \$832
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**CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2012**

	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net sales	\$1,653	\$622	\$2,511	\$(836)	) \$3,950
Cost of products sold	1,197	489	1,897	(836)	) 2,747
Selling and administrative expense	319	77	291	—	687
Research and development expense	55	26	21	—	102
Interest expense (income) - net	47	1	(6)	) —	42
Other expense (income) - net	1	—	(5)	) —	(4)
Equity in (earnings) loss of subsidiaries, net of tax	(276)	) (13)	) —	289	—
Intercompany (income) expense - net	(52)	) (5)	) 57	—	—
Income before income taxes	362	47	256	(289)	) 376
Income tax expense (benefit)	17	9	3	—	29
Net income	345	38	253	(289)	) 347
Less net income for noncontrolling interests	—	—	(2)	) —	(2)
Net income attributable to Eaton ordinary shareholders	\$345	\$38	\$251	\$(289)	) \$345
Other comprehensive loss	\$172	\$12	\$146	\$(158)	) \$172
Total comprehensive income attributable to Eaton ordinary shareholders	\$517	\$50	\$397	\$(447)	) \$517

**CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2013**

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net sales	\$—	\$5,026	\$4,835	\$10,117	\$(3,459)	) \$16,519
Cost of products sold	—	3,911	3,588	7,450	(3,461)	) 11,488
Selling and administrative expense	6	1,081	565	1,233	—	2,885
Research and development expense	—	199	138	142	—	479
Interest expense (income) - net	—	206	21	(18)	) —	209
Other expense (income) - net	—	16	13	(26)	) —	3
Equity in (earnings) loss of subsidiaries, net of tax	(1,576)	) (916)	) (848)	) (629)	) 3,969	—
Intercompany expense (income) - net	188	(304)	) (462)	) 578	—	—
Income before income taxes	1,382	833	1,820	1,387	(3,967)	) 1,455
Income tax expense (benefit)	—	(66)	) 28	102	—	64
Net income	1,382	899	1,792	1,285	(3,967)) 1,391
Less net income for noncontrolling interests	—	—	—	(6)) (3)) (9)

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Net income attributable to Eaton ordinary shareholders	\$1,382	\$899	\$1,792	\$1,279	\$(3,970)) \$1,382
Other comprehensive income (loss)	\$16	\$45	\$41	\$(66)	) \$(20)	) \$16
Total comprehensive income attributable to Eaton ordinary shareholders	\$1,398	\$944	\$1,833	\$1,213	\$(3,990)) \$1,398

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CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2012

	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net sales	\$5,097	\$1,965	\$7,606	\$(2,690)	) \$11,978
Cost of products sold	3,890	1,499	5,616	(2,689)	) 8,316
Selling and administrative expense	960	243	876	—	) 2,079
Research and development expense	166	74	73	—	) 313
Interest expense (income) - net	116	5	(21)	) —	) 100
Other expense - net	1	5	1	—	) 7
Equity in (earnings) loss of subsidiaries, net of tax	(948)	) (44)	) —	992) —
Intercompany (income) expense - net	(176)	) (14)	) 190	—) —
Income before income taxes	1,088	197	871	(993)	) 1,163
Income tax expense	50	53	20	—	) 123
Net income	1,038	144	851	(993)	) 1,040
Less net income for noncontrolling interests	—	—	(2)	) —	) (2)
Net income attributable to Eaton ordinary shareholders	\$1,038	\$144	\$849	\$(993)	) \$1,038
Other comprehensive income	\$156	\$17	\$64	\$(81)	) \$156
Total comprehensive income attributable to Eaton ordinary shareholders	\$1,194	\$161	\$913	\$(1,074)) \$1,194

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SEPTEMBER 30, 2013

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Assets						
Current assets						
Cash	\$2	\$37	\$17	\$586	\$—	\$642
Short-term investments	—	140	20	538	—	698
Accounts receivable - net	—	27	1,116	2,807	—	3,950
Intercompany accounts receivable	21	1,042	2,871	3,950	(7,884)	—
Inventory	—	345	612	1,483	(37)	2,403
Prepaid expenses and other current assets	—	694	190	228	(39)	1,073
Total current assets	23	2,285	4,826	9,592	(7,960)	8,766
Property, plant and equipment - net	—	949	769	2,039	—	3,757
Other noncurrent assets						
Goodwill	—	1,382	9,433	3,461	—	14,276
Other intangible assets	—	216	4,033	2,982	—	7,231
Deferred income taxes	—	846	—	236	(754)	328
Investment in subsidiaries	23,952	8,563	31,089	8,705	(72,309)	—
Intercompany loans receivable	—	7,690	2,069	18,319	(28,078)	—
Other assets	—	471	95	388	—	954
Total assets	\$23,975	\$22,402	\$52,314	\$45,722	\$(109,101)	\$35,312
Liabilities and shareholders' equity						
Current liabilities						
Short-term debt	\$—	\$75	\$—	\$13	\$—	\$88
Current portion of long-term debt	—	552	8	16	—	576
Accounts payable	—	422	396	1,158	—	1,976
Intercompany accounts payable	1	3,716	3,418	749	(7,884)	—
Accrued compensation	—	101	52	277	—	430
Other current liabilities	1	611	350	1,074	(52)	1,984
Total current liabilities	2	5,477	4,224	3,287	(7,936)	5,054
Noncurrent liabilities						
Long-term debt	—	7,739	1,274	16	—	9,029
Pension liabilities	—	788	221	792	—	1,801
Other postretirement benefits liabilities	—	448	185	100	—	733
Deferred income taxes	—	—	1,434	833	(754)	1,513

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Intercompany loans payable	7,902	1,986	17,362	828	(28,078) —
Other noncurrent liabilities	—	597	103	365	—	1,065
Total noncurrent liabilities	7,902	11,558	20,579	2,934	(28,832	) 14,141
Shareholders' equity						
Eaton shareholders' equity	16,071	5,367	27,511	39,468	(72,346	) 16,071
Noncontrolling interests	—	—	—	33	13	46
Total equity	16,071	5,367	27,511	39,501	(72,333) 16,117
Total liabilities and equity	\$23,975	\$22,402	\$52,314	\$45,722	\$(109,101) \$35,312

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CONDENSED CONSOLIDATING BALANCE SHEETS

DECEMBER 31, 2012

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Assets						
Current assets						
Cash	\$7	\$54	\$14	\$502	\$—	\$577
Short-term investments	—	25	38	464	—	527
Accounts receivable - net	—	624	413	2,473	—	3,510
Intercompany accounts receivable	38	365	4,693	5,643	(10,739)	—
Inventory	—	341	563	1,474	(39)	2,339
Prepaid expenses and other current assets	—	391	149	273	9	822
Total current assets	45	1,800	5,870	10,829	(10,769)	7,775
Property, plant and equipment - net	—	934	793	2,096	—	3,823
Other noncurrent assets						
Goodwill	—	1,382	9,381	3,448	—	14,211
Other intangible assets	—	231	4,104	3,133	—	7,468
Deferred income taxes	—	941	12	262	(846)	369
Investment in subsidiaries	20,662	7,678	14,428	6,365	(49,133)	—
Intercompany loans receivable	—	7,650	13,262	14,125	(35,037)	—
Other assets	—	460	90	1,154	—	1,704
Total assets	\$20,707	\$21,076	\$47,940	\$41,412	\$(95,785)	\$35,350
Liabilities and shareholders' equity						
Current liabilities						
Short-term debt	\$—	\$753	\$—	\$4	\$—	\$757
Current portion of long-term debt	—	303	8	3	—	314
Accounts payable	—	424	343	1,112	—	1,879
Intercompany accounts payable	2	2,794	4,855	3,088	(10,739)	—
Accrued compensation	—	129	76	258	—	463
Other current liabilities	—	523	375	1,114	(4)	2,008
Total current liabilities	2	4,926	5,657	5,579	(10,743)	5,421
Noncurrent liabilities						
Long-term debt	—	8,397	1,331	34	—	9,762
Pension liabilities	—	895	255	854	—	2,004
Other postretirement benefits liabilities	—	454	189	97	—	740
Deferred income taxes	—	—	1,464	838	(846)	1,456

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Intercompany loans payable	5,592	1,401	14,857	13,187	(35,037) —
Other noncurrent liabilities	—	440	86	286	—	812
Total noncurrent liabilities	5,592	11,587	18,182	15,296	(35,883	) 14,774
Shareholders' equity						
Eaton shareholders' equity	15,113	4,563	24,101	20,505	(49,169	) 15,113
Noncontrolling interests	—	—	—	32	10	42
Total equity	15,113	4,563	24,101	20,537	(49,159	) 15,155
Total liabilities and equity	\$20,707	\$21,076	\$47,940	\$41,412	\$(95,785	) \$35,350

Table of ContentsCONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2013

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net cash provided by (used in) operating activities	\$88	\$542	\$313	\$523	\$(53)	) \$1,413
Investing activities						
Cash paid for acquisitions of businesses, net of cash acquired	—	—	—	(11)	) —	(11)
Capital expenditures for property, plant and equipment	—	(112)	) (66)	(194)	) —	(372)
(Purchases) sales of short-term investments - net	—	(115)	) 18	(88)	) —	(185)
Loans to affiliates	—	(219)	) (23)	(4,267)	) 4,509	—
Repayments of loans from affiliates	—	28	102	4,030	(4,160)) —
Proceeds from sale of business	—	—	—	761	—	761
Other - net	—	(25)	) 4	(29)	) —	(50)
Net cash (used in) provided by investing activities	—	(443)	) 35	202	349	143
Financing activities						
Proceeds from borrowings	—	—	—	6	—	6
Payments on borrowings	—	(975)	) (35)	(2)	) —	(1,012)
Proceeds from borrowings from affiliates	—	1,975	2,436	98	(4,509)) —
Payments on borrowings from affiliates	—	(2,391)	) (1,639)	(130)	) 4,160	—
Other intercompany financing activities	504	1,153	(1,107)	) (550)) —	—
Cash dividends paid	(597)	) —	—	—	—	(597)
Cash dividends paid to affiliates	—	—	—	(53)	) 53	—
Exercise of employee stock options	—	98	—	—	—	98
Excess tax benefit from equity-based compensation	—	24	—	—	—	24
Other - net	—	—	—	(4)) —	(4)
Net cash used in financing activities	(93)) (116)) (345)	(635)) (296)) (1,485)

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Effect of currency on cash	—	—	—	(6) —	(6)
Total (decrease) increase in cash	(5) (17) 3	84	—	65	
Cash at the beginning of the period	7	54	14	502	—	577	
Cash at the end of the period	\$2	\$37	\$17	\$586	\$—	\$642	

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Table of ContentsCONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2012

	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net cash provided by operating activities	\$25	\$29	\$923	\$—	\$977
Investing activities					
Cash paid for acquisitions of businesses, net of cash acquired	1	—	(555	) —	(554)
Capital expenditures for property, plant and equipment	(198	) (33	) (126	) —	(357)
Sales (purchases) of short-term investments - net	100	—	(11	) —	89
Loans to affiliates	(183	) —	(6,528	) 6,711	—
Repayments of loans from affiliates	143	—	6,320	(6,463) —
Proceeds from sale of business	2	—	1	—	3
Other - net	(31	) (7	) —	—	(38)
Net cash (used in) provided by investing activities	(166	) (40	) (899	) 248	(857)
Financing activities					
Proceeds from borrowings	600	—	—	—	600
Payments on borrowings	(306	) (12	) (3	) —	(321)
Payments of financing costs	(63	) —	—	—	(63)
Proceeds from borrowings from affiliates	6,528	—	183	(6,711) —
Payments on borrowings from affiliates	(6,320	) —	(143	) 6,463	—
Other intercompany financing activities	(15	) 22	(7) —	—
Cash dividends paid	(384	) —	—	—	(384)
Exercise of employee stock options	54	—	—	—	54
Excess tax benefit from equity-based compensation	18	—	—	—	18
Other - net	(2	) —	2	—	—
Net cash provided by (used in) financing activities	110	10	32	(248	) (96)
Effect of currency on cash	—	—	16	—	16
Total (decrease) increase in cash	(31	) (1	) 72	—	40
Cash at the beginning of the period	120	3	262	—	385
Cash at the end of the period	\$89	\$2	\$334	\$—	\$425

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).

COMPANY OVERVIEW

Eaton Corporation plc (Eaton or the Company) is a power management company providing energy-efficient solutions that help its customers effectively manage electrical, hydraulic and mechanical power. With 2012 net sales of \$16.3 billion, the Company is a global technology leader in electrical products, systems and services for power quality, distribution and control, power transmission, lighting and wiring products; 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 102,000 employees in over 60 countries, and sells products to customers in more than 175 countries.

In 2012, Eaton acquired certain businesses that affect comparability on a year over year basis, the most substantial of which was Cooper Industries plc (Cooper). Cooper was acquired November 30, 2012 for a purchase price of \$13,192. See Note 2 in the 2012 Form 10-K, as updated by Exhibit 99.1 of Eaton's current report on Form 8-K filed on September 6, 2013 for additional information on the acquisition of Cooper. The Consolidated Statements of Income include the results of these businesses from the dates of the transactions or formation. For a complete list of business acquisitions impacting the comparative periods, see Note 2 to the Condensed Consolidated Financial Statements. The acquisition of Cooper has significantly transformed Eaton's mix of businesses. As a result, during the first quarter of 2013, Eaton re-segmented certain reportable operating segments due to a reorganization of the Company's businesses. The new reportable business segments are Electrical Products and Electrical Systems and Services (which include legacy Eaton and former Cooper electrical businesses), and Vehicle (which includes truck and automotive drivetrain and powertrain systems businesses). For those reportable segments that were re-segmented, previously reported segment financial information has been updated for all prior periods. See Note 13 to the Condensed Consolidated Financial Statements contained in the Form 10-Q for the quarterly period ending March 31, 2013. The re-segmentation did not impact previously reported consolidated results of operations. For additional information regarding Eaton's business segments, see Note 14 to the Consolidated Financial Statements contained in the 2012 Form 10-K, as updated by Exhibit 99.1 of Eaton's current report on Form 8-K filed on September 6, 2013.

Summary of Results of Operations

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

	Three months ended		Nine months ended	
	September 30		September 30	
	2013	2012	2013	2012
Net sales	\$5,607	\$3,950	\$16,519	\$11,978
Net income attributable to Eaton ordinary shareholders	510	345	1,382	1,038
Net income per ordinary share-diluted	\$1.07	\$1.02	\$2.90	\$3.05

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 ordinary share, and operating profit before acquisition integration charges for each business segment, as well as corporate expense, 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. For additional information on acquisition integration charges, see Note 3 to the Condensed Consolidated Financial Statements.

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Consolidated Financial Results

	Three months ended		Increase (decrease)		Nine months ended		Increase (decrease)	
	September 30				September 30			
	2013	2012			2013	2012		
Net sales	\$5,607	\$3,950	42	%	\$16,519	\$11,978	38	%
Gross profit	1,724	1,203	43	%	5,031	3,662	37	%
Percent of net sales	30.7	% 30.5	%		30.5	% 30.6	%	
Income before income taxes	521	376	39	%	1,455	1,163	25	%
Net income	\$514	\$347	48	%	\$1,391	\$1,040	34	%
Less net income for noncontrolling interests	(4	) (2	)		(9	) (2)	
Net income attributable to Eaton ordinary shareholders	510	345	48	%	1,382	1,038	33	%
Excluding acquisition integration charges and transaction costs (after-tax)	26	18			73	30		
Operating earnings	\$536	\$363	48	%	\$1,455	\$1,068	36	%
Net income per ordinary share-diluted	\$1.07	\$1.02	5	%	\$2.90	\$3.05	(5)%
Excluding per share impact of acquisition integration charges and transaction costs (after-tax)	0.05							