

Eaton Corp plc
Form 10-Q
November 01, 2016
Table of Contents

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, 2016
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)

Eaton House, 30 Pembroke Road, Dublin 4, Ireland -
(Address of principal executive offices) (Zip Code)

+353 1637
2900
(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

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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 451.7 million Ordinary Shares outstanding as of September 30, 2016.

Table of Contents

TABLE OF CONTENTS

PART I — FINANCIAL INFORMATION

<u>ITEM 1. FINANCIAL STATEMENTS</u>	<u>2</u>
<u>ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	<u>23</u>
<u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	<u>29</u>
<u>ITEM 4. CONTROLS AND PROCEDURES</u>	<u>29</u>

PART II — OTHER INFORMATION

<u>ITEM 1. LEGAL PROCEEDINGS</u>	<u>29</u>
<u>ITEM 1A. RISK FACTORS</u>	<u>29</u>
<u>ITEM 2. UNRESTRICTED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	<u>30</u>
<u>ITEM 6. EXHIBITS</u>	<u>30</u>
<u>SIGNATURES</u>	<u>31</u>
<u>EXHIBIT INDEX</u>	<u>32</u>

EX-12

EX-31.1

EX-31.2

EX-32.1

EX-32.2

EX-101 INSTANCE DOCUMENT

EX-101 SCHEMA DOCUMENT

EX-101 CALCULATION LINKBASE DOCUMENT

EX-101 DEFINITION LINKBASE DOCUMENT

EX-101 LABELS LINKBASE DOCUMENT

EX-101 PRESENTATION LINKBASE DOCUMENT

Table of Contents

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	
	2016	2015	2016	2015
Net sales	\$4,987	\$5,203	\$14,880	\$15,798
Cost of products sold	3,371	3,597	10,081	10,865
Selling and administrative expense	853	907	2,642	2,723
Research and development expense	146	156	444	472
Interest expense - net	59	59	173	175
Other income - net	(15	) (3	) (28	) (27
Income before income taxes	573	487	1,568	1,590
Income tax expense	51	42	151	143
Net income	522	445	1,417	1,447
Less net loss for noncontrolling interests	1	1	1	—
Net income attributable to Eaton ordinary shareholders	\$523	\$446	\$1,418	\$1,447
Net income per share attributable to Eaton ordinary shareholders				
Diluted	\$1.15	\$0.96	\$3.09	\$3.09
Basic	1.15	0.96	3.10	3.10
Weighted-average number of ordinary shares outstanding				
Diluted	455.6	466.4	457.9	468.5
Basic	453.9	465.1	456.5	466.8
Cash dividends declared per ordinary share	\$0.57	\$0.55	\$1.71	\$1.65

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

Table of ContentsEATON CORPORATION plc
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In millions)	Three months ended		Nine months ended	
	September 30 2016	September 30 2015	September 30 2016	September 30 2015
Net income	\$522	\$445	\$1,417	\$1,447
Less net loss for noncontrolling interests	1	1	1	—
Net income attributable to Eaton ordinary shareholders	523	446	1,418	1,447
Other comprehensive (loss) income, net of tax				
Currency translation and related hedging instruments	(22)	(372)	(57)	(883)
Pensions and other postretirement benefits	45	60	132	164
Cash flow hedges	1	—	(33)	3
Other comprehensive (loss) income attributable to Eaton ordinary shareholders	24	(312)	42	(716)
Total comprehensive income attributable to Eaton ordinary shareholders	\$547	\$134	\$1,460	\$731

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

Table of ContentsEATON CORPORATION plc
CONDENSED CONSOLIDATED BALANCE SHEETS

(In millions)	September 30, 2016	December 31, 2015
Assets		
Current assets		
Cash	\$ 494	\$ 268
Short-term investments	213	177
Accounts receivable - net	3,659	3,479
Inventory	2,328	2,323
Prepaid expenses and other current assets	393	369
Total current assets	7,087	6,616
Property, plant and equipment - net	3,506	3,565
Other noncurrent assets		
Goodwill	13,434	13,479
Other intangible assets	5,689	6,014
Deferred income taxes	412	362
Other assets	1,109	960
Total assets	\$ 31,237	\$ 30,996
Liabilities and shareholders' equity		
Current liabilities		
Short-term debt	\$ 1	\$ 426
Current portion of long-term debt	550	242
Accounts payable	1,790	1,758
Accrued compensation	388	366
Other current liabilities	1,866	1,833
Total current liabilities	4,595	4,625
Noncurrent liabilities		
Long-term debt	7,881	7,746
Pension liabilities	1,532	1,586
Other postretirement benefits liabilities	429	440
Deferred income taxes	366	390
Other noncurrent liabilities	988	978
Total noncurrent liabilities	11,196	11,140
Shareholders' equity		
Eaton shareholders' equity	15,404	15,186
Noncontrolling interests	42	45
Total equity	15,446	15,231
Total liabilities and equity	\$ 31,237	\$ 30,996

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

Table of ContentsEATON CORPORATION plc
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)	Nine months ended	
	September 30 2016	2015
Operating activities		
Net income	\$1,417	\$1,447
Adjustments to reconcile to net cash provided by operating activities		
Depreciation and amortization	700	692
Deferred income taxes	(105)	(101)
Pension and other postretirement benefits expense	177	244
Contributions to pension plans	(114)	(290)
Contributions to other postretirement benefits plans	(26)	(24)
Changes in working capital	(224)	(184)
Other - net	89	(155)
Net cash provided by operating activities	1,914	1,629
Investing activities		
Capital expenditures for property, plant and equipment	(346)	(368)
Cash received from (paid for) acquisitions of businesses, net of cash acquired	1	(38)
Sales (purchases) of short-term investments - net	(29)	76
Proceeds from sale of businesses	—	1
Other - net	3	(44)
Net cash used in investing activities	(371)	(373)
Financing activities		
Proceeds from borrowings	633	1
Payments on borrowings	(666)	(405)
Cash dividends paid	(780)	(771)
Exercise of employee stock options	60	48
Repurchase of shares	(567)	(454)
Other - net	(5)	(8)
Net cash used in financing activities	(1,325)	(1,589)
Effect of currency on cash	8	(30)
Total increase (decrease) in cash	226	(363)
Cash at the beginning of the period	268	781
Cash at the end of the period	\$494	\$418

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

Table of Contents

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 United States generally accepted accounting principles (US GAAP) 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 2015 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 Securities and Exchange Commission.

During the first quarter of 2016, the Company adopted Accounting Standards Update 2015-03, Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs (ASU 2015-03). ASU 2015-03 requires that debt issuance costs be presented in the balance sheet as a direct deduction from the related debt liability rather than an asset. The Company has applied this standard retrospectively. The adoption of ASU 2015-03 resulted in the reclassification of \$36 and \$35 within the Company's Condensed Consolidated Balance Sheets as of September 30, 2016 and December 31, 2015, respectively, from Other noncurrent assets to a reduction in Long-term debt.

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

Recently Issued Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2016-02, Leases (Topic 842), (ASU 2016-02). This accounting standard requires that a lessee recognize a lease asset and a lease liability on its balance sheet for all leases, including operating leases, with a term greater than 12 months. ASU 2016-02 will require additional disclosures in the notes to the consolidated financial statements and is effective for annual and interim reporting periods beginning after December 15, 2018. Eaton is evaluating the impact of ASU 2016-02 and an estimate of the impact to the consolidated financial statements cannot be made at this time.

In May 2014, the FASB issued Accounting Standards Update 2014-09, Revenue from Contracts with Customers (ASU 2014-09). This accounting standard supersedes all existing US GAAP revenue recognition guidance. Under ASU 2014-09, a company will recognize revenue when it transfers the control of promised goods or services to customers in an amount that reflects the consideration which the company expects to collect in exchange for those goods or services. ASU 2014-09 will require additional disclosures in the notes to the consolidated financial statements and is effective for annual and interim reporting periods beginning after December 15, 2016. In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers: Deferral of the Effective Date (ASU 2015-14). This accounting standard defers the effective date of ASU 2014-09 for one year and permits early adoption as of the original effective date. Eaton is evaluating the impact of ASU 2014-09 and an estimate of the impact to the consolidated financial statements cannot be made at this time.

Note 2. ACQUISITIONS OF BUSINESSES

Acquisition of Ephesus Lighting, Inc.

On October 28, 2015, Eaton acquired Ephesus Lighting, Inc. (Ephesus). Ephesus is a leader in LED lighting for stadiums and other high lumen outdoor and industrial applications. Its sales for the 12 months ended September 30, 2015 were \$23. Ephesus is reported within the Electrical Products business segment.

Acquisition of UK Safety Technology Manufacturer Oxalis Group Ltd.

On January 12, 2015, Eaton acquired Oxalis Group Ltd. (Oxalis). Oxalis is a manufacturer of closed-circuit television camera stations, public address and general alarm systems and other electrical products for the hazardous area, marine and industrial communications markets. Its sales for the 12 months ended December 31, 2014 were \$9. Oxalis is

reported within the Electrical Systems and Services business segment.

6

Table of Contents

Note 3. ACQUISITION INTEGRATION CHARGES

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

	Three months ended September 30 2016		Nine months ended September 30 2015	
Electrical Products	\$1	\$5	\$2	\$17
Electrical Systems and Services	—	3	1	10
Hydraulics	—	—	—	2
Total business segments	1	8	3	29
Corporate	—	2	—	4
Total acquisition integration charges before income taxes	1	10	3	33
Income taxes	—	3	1	11
Total after income taxes	\$1	\$7	\$2	\$22
Per ordinary share - diluted	\$—	\$0.01	\$—	\$0.05

Business segment acquisition integration charges in 2016 related to the integration of Ephesus Lighting, Inc. (Ephesus) and

Oxalis Group Ltd. (Oxalis), which were acquired in 2015. The charges associated with Ephesus were included in Cost of

products sold and Selling and administrative expense, while the charges associated with Oxalis were included in Cost of

products sold. Business segment acquisition integration charges in 2015 related primarily to the integration of Cooper Industries plc (Cooper), which was acquired in 2012. 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. See Note 14 for additional information about business segments.

Corporate acquisition integration charges in 2015 also related 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.

Note 4. RESTRUCTURING CHARGES

During 2015, Eaton announced its intention to undertake actions to reduce its cost structure in all business segments and at corporate. Restructuring charges for the three and nine months ended September 30, 2016, were \$23 and \$121, respectively, and were \$113 and \$127 for the three and nine months ended September 30, 2015, respectively. The charges associated with restructuring activities are anticipated to be \$145 in 2016 and \$180 in 2017.

A summary of restructuring charges by type follows:

	Three months ended September 30 2016		Nine months ended September 30 2015	
Workforce reductions	\$18	\$99	\$95	\$111
Plant closings and other	5	14	26	16
Total	\$23	\$113	\$121	\$127

Table of Contents

A summary of restructuring charges by segment follows:

	Three months ended September 30 2016		Nine months ended September 30 2015	
Electrical Products	\$1	\$11	\$27	\$12
Electrical Systems & Services	7	26	20	26
Hydraulics	10	25	44	34
Aerospace	(1)	5	3	5
Vehicle	5	29	22	33
Corporate	1	17	5	17
Total	\$23	\$113	\$121	\$127

A summary of liabilities related to workforce reductions, plant closings and other associated costs follows:

	Workforce reductions	Plant closings and other	Total
Balance at December 31, 2014	\$ —	\$ —	\$—
Liability recognized	112	17	129
Payments	(59)	(3)	(62)
Other adjustments	1	(14)	(13)
Balance at December 31, 2015	54	—	54
Liability recognized	95	26	121
Payments	(89)	(11)	(100)
Other adjustments	(1)	(14)	(15)
Balance at September 30, 2016	\$ 59	\$ 1	\$60

These charges were included in Cost of products sold, Selling and administrative expenses or Other income-net, as appropriate. In Business Segment Information, the charges reduced Operating profit of the related business segment. See Note 14 for additional information about business segments.

Note 5. GOODWILL

A summary of goodwill follows:

	Electrical Products	Electrical Systems and Services	Hydraulics	Aerospace	Vehicle	Total
December 31, 2015	\$ 6,642	\$ 4,279	\$ 1,259	\$ 956	\$ 343	\$13,479
Translation	(24)	(12)	2	(13)	2	(45)
September 30, 2016	\$ 6,618	\$ 4,267	\$ 1,261	\$ 943	\$ 345	\$13,434

Table of Contents

Note 6. DEBT

On September 20, 2016, a subsidiary of Eaton issued Euro denominated notes (Euro Notes) with a face value of €550 (\$615 based on the September 20, 2016 spot rate), in accordance with Regulation S promulgated under the Securities Act of 1933, as amended. The Euro Notes mature in 2024 with interest payable annually at a rate of 0.75%. The issuer received proceeds totaling €544 (\$609 based on the September 20, 2016 spot rate) from the issuance, net of financing costs and discounts. The senior Euro Notes are fully and unconditionally guaranteed on an unsubordinated, unsecured basis by Eaton and certain of its direct and indirect subsidiaries. The Euro Notes contain an optional redemption provision by which the Company may make an offer to purchase all or any part of the Euro Notes prior to June 20, 2024 at a purchase price of the greater of (a) 100% of the principal amount of the respective Euro Notes being redeemed, or (b) the sum of the present values of the respective remaining scheduled payments of principal and interest, discounted to the redemption date on an annual basis at the benchmark Bund Rate plus 20 basis points. In each case, the redemption price will include any accrued and unpaid interest on the Euro Notes being redeemed. At any time on or after June 20, 2024, the Company may redeem the Euro Notes, in whole or in part, at a redemption price equal to 100% of the principal amount to be redeemed plus accrued and unpaid interest. The Euro Notes also contain a change of control provision which requires the Company to make an offer to purchase all or any part of the Euro Notes at a purchase price of 101% of the principal amount plus accrued and unpaid interest. The capitalized deferred financing fees and discounts are amortized in Interest expense - net over the respective terms of the Euro Notes. The Euro Notes are subject to customary non-financial covenants.

On October 14, 2016, Eaton refinanced a \$750, five-year revolving credit facility with a \$750, five-year revolving credit facility that will expire October 14, 2021. Eaton also maintains a \$500, four-year revolving credit facility that will expire on October 3, 2018 and a \$750, five-year credit facility that will expire October 3, 2019. This refinancing maintains long-term revolving credit facilities at a total of \$2,000. The revolving credit facilities are used to support commercial paper borrowings and are fully and unconditionally guaranteed by Eaton and certain of its direct and indirect subsidiaries on an unsubordinated, unsecured basis. There were no borrowings outstanding under these revolving credit facilities at September 30, 2016 or October 14, 2016.

Note 7. RETIREMENT BENEFITS PLANS

The components of retirement benefits expense follow:

	United States pension benefit expense		Non-United States pension benefit expense		Other postretirement benefits expense	
	2016	2015	2016	2015	2016	2015
Service cost	\$28	\$31	\$16	\$18	\$ 1	\$ 2
Interest cost	31	39	16	18	4	6
Expected return on plan assets	(63)	(65)	(23)	(25)	(2)	(2)
Amortization	23	29	8	10	(2)	—
	19	34	17	21	1	6
Settlements	24	25	—	—	—	—
Total expense	\$43	\$59	\$17	\$21	\$ 1	\$ 6
	United States pension benefit expense		Non-United States pension benefit expense		Other postretirement benefits expense	
	2016	2015	2016	2015	2016	2015

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Service cost	\$83	\$92	\$49	\$55	\$ 3	\$ 5
Interest cost	94	117	48	54	13	18
Expected return on plan assets	(188)	(196)	(71)	(75)	(5)	(4)
Amortization	69	89	25	30	(6)	1
	58	102	51	64	5	20
Settlements and curtailments	63	58	—	—	—	—
Total expense	\$121	\$160	\$51	\$64	\$ 5	\$ 20

9

Table of Contents

Note 8. 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, antitrust matters and employment-related matters. Eaton is also subject to asbestos claims from historic products which may have contained asbestos. Insurance may cover some of the costs associated with these claims. 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. The judgment was based on an alleged violation of an agency agreement between Raysul and Saturnia. At March 31, 2016, the Company had a total accrual of 100 Brazilian Reais related to this matter (\$31 based on June 2016 exchange rates). In June 2016, Eaton signed a settlement agreement and resolved the matter, which did not have a material impact on the consolidated financial statements.

Note 9. INCOME TAXES

The effective income tax rate for the third quarter and first nine months of 2016 was expense of 9%, and 10%, respectively, compared to an expense of 9% for the third quarter and first nine months of 2015. The increase in the effective tax rate in the first nine months of 2016 was primarily due to more income earned in higher tax jurisdictions.

Note 10. EQUITY

On October 22, 2013, Eaton's Board of Directors adopted a share repurchase program (2013 Program) that authorizes the repurchase of 40 million ordinary shares. During the first quarter of 2016, 1.5 million ordinary shares were repurchased under the 2013 Program in the open market at a total cost of \$82. During the three and nine months ended September 30, 2015, 4.8 million and 7.2 million ordinary shares were repurchased under the 2013 Program in the open market at a total cost of \$284 and \$454, respectively. On February 24, 2016, the Board of Directors approved a new share repurchase program for share repurchases up to \$2,500 of ordinary shares (2016 Program). Under the 2016 Program, the ordinary shares are expected to be repurchased over time, depending on market conditions, the market price of ordinary shares, capital levels, and other considerations. During the three and nine months ended September 30, 2016, 3.7 million and 7.7 million ordinary shares, respectively, were purchased on the open market under the 2016 Program for a total cost of \$243 and \$485, respectively.

The changes in Shareholders' equity follow:

	Eaton shareholders' equity	Noncontrolling interests	Total equity
Balance at December 31, 2015	\$ 15,186	\$ 45	\$ 15,231
Net income (loss)	1,418	(1)	1,417
Other comprehensive income	42	—	42
Cash dividends paid	(780)	(2)	(782)
Issuance of shares under equity-based compensation plans - net	105	—	105
Repurchase of shares	(567)	—	(567)
Balance at September 30, 2016	\$ 15,404	\$ 42	\$ 15,446

The changes in Accumulated other comprehensive loss follow:

	Currency translation and related hedging instruments	Pensions and other postretirement benefits	Cash flow hedges	Total
Balance at December 31, 2015	\$ (2,492)	\$ (1,374)	\$ 3	\$(3,863)
Other comprehensive (loss) income	(57)	33	(35)	(59)

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before reclassifications				
Amounts reclassified from Accumulated other comprehensive loss (income)	—	99	2	101
Net current-period Other comprehensive income (loss)	(57	) 132	(33	) 42
Balance at September 30, 2016	\$ (2,549	) \$ (1,242	) \$ (30	) \$(3,821)

10

Table of Contents

The reclassifications out of Accumulated other comprehensive loss follow:

	Nine months ended September 30, 2016	Consolidated statements of income classification
Amortization of defined benefit pensions and other postretirement benefits items		
Actuarial loss and prior service cost	\$ (151) ¹	
Tax benefit	52	
Total, net of tax	(99)	
Gains and (losses) on cash flow hedges		
Currency exchange contracts	(3)	Cost of products sold
Tax benefit	1	
Total, net of tax	(2)	
Total reclassifications for the period	\$ (101)	

¹ These components of Accumulated other comprehensive loss are included in the computation of net periodic benefit cost. See Note 7 for additional information about pension and other postretirement benefits items.

Net Income Per Share Attributable to Eaton Ordinary Shareholders

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

	Three months ended September 30		Nine months ended September 30	
(Shares in millions)	2016	2015	2016	2015
Net income attributable to Eaton ordinary shareholders	\$523	\$446	\$1,418	\$1,447
Weighted-average number of ordinary shares outstanding - diluted	455.6	466.4	457.9	468.5
Less dilutive effect of equity-based compensation	1.7	1.3	1.4	1.7
Weighted-average number of ordinary shares outstanding - basic	453.9	465.1	456.5	466.8
Net income per share attributable to Eaton ordinary shareholders				
Diluted	\$1.15	\$0.96	\$3.09	\$3.09
Basic	1.15	0.96	3.10	3.10

For the third quarter and first nine months of 2016, 1.5 million and 1.8 million stock options, respectively, were excluded from the calculation of diluted net income per share attributable to Eaton ordinary shareholders 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 first nine months of 2015, 1.8 million and 1.3 million stock options, respectively, were excluded from the calculation of diluted net income per share attributable to Eaton ordinary shareholders because the exercise price of the options exceeded the average market price of the ordinary shares during the periods and their effect, accordingly, would have been antidilutive.

Note 11. 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.

Table of Contents

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

	Total	Level 1	Level 2	Level 3
September 30, 2016				
Cash	\$494	\$494	\$ —	\$ —
Short-term investments	213	213	—	—
Net derivative contracts	148	—	148	—
Long-term debt converted to floating interest rates by interest rate swaps - net	(172)	—	(172)	—
December 31, 2015				
Cash	\$268	\$268	\$ —	\$ —
Short-term investments	177	177	—	—
Net derivative contracts	86	—	86	—
Long-term debt converted to floating interest rates by interest rate swaps - net	(94)	—	(94)	—

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 measured using unobservable inputs.

Other Fair Value Measurements

Long-term debt and the current portion of long-term debt had a carrying value of \$8,431 and fair value of \$9,050 at September 30, 2016 compared to \$7,988 and \$8,231, respectively, at December 31, 2015. The fair value of Eaton's debt instruments were estimated using prevailing market interest rates on debt with similar creditworthiness, terms and maturities, and are considered a Level 2 fair value measurement.

Note 12. 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 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 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.

Table of Contents

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. Gains and losses associated with commodity hedge contracts are classified in Cost of products sold.

Eaton uses certain of its debt denominated in foreign currency to hedge portions of its net investments in foreign operations against foreign currency exposure (net investment hedges). Foreign currency denominated debt designated as non-derivative net investment hedging instruments on an after-tax basis was \$99 at September 30, 2016 and \$83 at December 31, 2015, and designated on a pre-tax basis was \$607 at September 30, 2016.

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 noncurrent assets	Other current liabilities	Other noncurrent liabilities	Type of hedge	Term
September 30, 2016							
Derivatives designated as hedges							
Fixed-to-floating interest rate swaps	\$ 3,765	\$ —	\$ 172	\$ —	\$ —	Fair value	1 month to 19 years
Forward starting floating-to-fixed interest rate swaps	450	—	—	—	18	Cash flow	12 years
Currency exchange contracts	826	5	1	19	14	Cash flow	1 to 36 months
Total		\$ 5	\$ 173	\$ 19	\$ 32		
Derivatives not designated as hedges							
Currency exchange contracts	\$ 3,991	\$ 34	\$ —	\$ 15	\$ —		1 to 24 months
Commodity contracts	41	2	—	—	—		1 to 12 months
Total		\$ 36	\$ —	\$ 15	\$ —		
December 31, 2015							
Derivatives designated as hedges							
Fixed-to-floating interest rate swaps	\$ 3,715	\$ —	\$ 96	\$ —	\$ 2	Fair value	2 to 19 years
Forward starting floating-to-fixed interest rate swaps	50	—	—	—	—	Cash flow	12 years
Currency exchange contracts	724	18	1	8	6	Cash flow	1 to 36 months
Commodity contracts	1	—	—	—	—	Cash flow	1 to 12 months
Total		\$ 18	\$ 97	\$ 8	\$ 8		
Derivatives not designated as hedges							
Currency exchange contracts	\$ 4,198	\$ 27	—	\$ 40	—		

1 to 12
months

Total	\$ 27	\$ 40
-------	-------	-------

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.

13

Table of Contents

The impact of derivative instruments to the Consolidated Statement of Income and Comprehensive Income follow:

	Gain (loss) recognized in other comprehensive (loss) income		Location of gain (loss) reclassified from Accumulated other comprehensive loss	Gain (loss) reclassified from Accumulated other comprehensive loss	
	Three months ended September 30			Three months ended September 30	
	2016	2015		2016	2015
Derivatives designated as cash flow hedges					
Forward starting floating-to-fixed interest rate swaps	\$ 1	\$ —	Interest expense - net	\$ —	\$ —
Currency exchange contracts	(3)	6	Cost of products sold	(4)	5
Total	\$ (2)	\$ 6		\$ (4)	\$ 5

	Gain (loss) recognized in other comprehensive (loss) income		Location of gain (loss) reclassified from Accumulated other comprehensive loss	Gain (loss) reclassified from Accumulated other comprehensive loss	
	Nine months ended September 30			Nine months ended September 30	
	2016	2015		2016	2015
Derivatives designated as cash flow hedges					
Forward starting floating-to-fixed interest rate swaps	\$ (18)	\$ —	Interest expense - net	\$ —	\$ —
Currency exchange contracts	(35)	16	Cost of products sold	(3)	11
Total	\$ (53)	\$ 16		\$ (3)	\$ 11

Amounts recognized in net income follow:

	Three months ended September 30		Nine months ended September 30		
	2016	2015	2016	2015	
Derivatives designated as fair value hedges					
Fixed-to-floating interest rate swaps		\$(28)	\$65	\$78	\$62
Related long-term debt converted to floating interest	28	(65)	(78)	(62)	

rates by interest rate swaps

\$— \$— \$— \$—

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

Note 13. INVENTORY

The components of inventory follow:

	September 30, 2016	December 31, 2015
Raw materials	\$ 910	\$ 885
Work-in-process	431	412
Finished goods	1,083	1,131
Inventory at FIFO	2,424	2,428
Excess of FIFO over LIFO cost	(96)	(105)
Total inventory	\$ 2,328	\$ 2,323

Table of Contents

Note 14. 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 Products, Electrical Systems and Services, Hydraulics, Aerospace and Vehicle. Operating profit includes the operating profit from intersegment sales. For additional information regarding Eaton's business segments, see Note 15 to the Consolidated Financial Statements contained in the 2015 Form 10-K.

	Three months ended		Nine months ended	
	September 30		September 30	
	2016	2015	2016	2015
Net sales				
Electrical Products	\$1,767	\$1,771	\$5,231	\$5,246
Electrical Systems and Services	1,436	1,487	4,207	4,437
Hydraulics	562	599	1,702	1,907
Aerospace	436	449	1,328	1,367
Vehicle	786	897	2,412	2,841
Total net sales	\$4,987	\$5,203	\$14,880	\$15,798
Segment operating profit				
Electrical Products	\$331	\$322	\$924	\$858
Electrical Systems and Services	197	164	534	573
Hydraulics	61	44	161	184
Aerospace	88	79	251	233
Vehicle	122	136	377	490
Total segment operating profit	799	745	2,247	2,338
Corporate				
Amortization of intangible assets	(99	) (102	) (297	) (306
Interest expense - net	(59	) (59	) (173	) (175
Pension and other postretirement benefits expense	(18	) (38	) (45	) (99
Other corporate expense - net	(50	) (59	) (164	) (168
Income before income taxes	573	487	1,568	1,590
Income tax expense	51	42	151	143
Net income	522	445	1,417	1,447
Less net loss for noncontrolling interests	1	1	1	—
Net income attributable to Eaton ordinary shareholders	\$523	\$446	\$1,418	\$1,447

Note 15. CONDENSED CONSOLIDATING FINANCIAL STATEMENTS

On November 14, 2013, Eaton Corporation registered senior notes under the Securities Act of 1933 (the Senior Notes). Eaton and certain other of Eaton's 100% owned direct and indirect 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 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 only be automatically and unconditionally released and discharged in connection with the release or termination of such 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.

During 2015 and 2016, the Company undertook certain steps to restructure ownership of various subsidiaries. The transactions were entirely among wholly-owned subsidiaries under the common control of Eaton. This restructuring has been reflected as of the beginning of the earliest period presented below.

CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net sales	\$ —	\$ 1,660	\$ 1,583	\$ 3,040	\$ (1,296)	\$ 4,987
Cost of products sold	—	1,329	1,162	2,173	(1,293)	3,371
Selling and administrative expense	2	330	197	324	—	853
Research and development expense	—	59	43	44	—	146
Interest expense (income) - net	—	59	4	(3)	(1)	59
Other expense (income) - net	(1)	18	—	(32)	—	(15)
Equity in loss (earnings) of subsidiaries, net of tax	(628)	(173)	(895)	(219)	1,915	—
Intercompany expense (income) - net	104	(47)	336	(393)	—	—
Income (loss) before income taxes	523	85	736	1,146	(1,917)	573
Income tax expense (benefit)	—	(11)	10	53	(1)	51
Net income (loss)	523	96	726	1,093	(1,916)	522
Less net loss (income) for noncontrolling interests	—	—	—	—	1	1
Net income (loss) attributable to Eaton ordinary shareholders	\$ 523	\$ 96	\$ 726	\$ 1,093	\$ (1,915)	\$ 523
Other comprehensive income (loss)	\$ 24	\$ 24	\$ 29	\$ 2	\$ (55)	\$ 24
Total comprehensive income (loss) attributable to Eaton ordinary shareholders	\$ 547	\$ 120	\$ 755	\$ 1,095	\$ (1,970)	\$ 547

CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2015

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net sales	\$ —	\$ 1,755	\$ 1,664	\$ 3,105	\$ (1,321)	\$ 5,203
Cost of products sold	—	1,380	1,269	2,265	(1,317)	3,597
Selling and administrative expense	2	375	191	339	—	907
Research and development expense	—	65	51	40	—	156
Interest expense (income) - net	—	54	5	(3)	3	59
Other expense (income) - net	—	11	3	(17)	—	(3)
Equity in loss (earnings) of subsidiaries, net of tax	(534)	(264)	(888)	(64)	1,750	—
Intercompany expense (income) - net	86	(54)	258	(290)	—	—
Income (loss) before income taxes	446	188	775	835	(1,757)	487
Income tax expense (benefit)	—	17	(15)	38	2	42
Net income (loss)	446	171	790	797	(1,759)	445
Less net loss (income) for noncontrolling interests	—	—	—	1	—	1
Net income (loss) attributable to Eaton ordinary shareholders	\$ 446	\$ 171	\$ 790	\$ 798	\$ (1,759)	\$ 446
Other comprehensive income (loss)	\$ (312)	\$ (24)	\$ (305)	\$ (411)	\$ 740	\$ (312)
Total comprehensive income (loss) attributable to Eaton ordinary shareholders	\$ 134	\$ 147	\$ 485	\$ 387	\$ (1,019)	\$ 134

CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2016

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net sales	\$ —	\$ 4,842	\$ 4,793	\$ 8,983	\$ (3,738)	\$ 14,880
Cost of products sold	—	3,788	3,554	6,478	(3,739)	10,081
Selling and administrative expense	6	1,048	583	1,005	—	2,642
Research and development expense	—	176	138	130	—	444
Interest expense (income) - net	—	169	13	(13)	4	173
Other expense (income) - net	(1)	34	(3)	(58)	—	(28)
Equity in loss (earnings) of subsidiaries, net of tax	(1,726)	(495)	(2,384)	(434)	5,039	—
Intercompany expense (income) - net	303	(135)	913	(1,081)	—	—
Income (loss) before income taxes	1,418	257	1,979	2,956	(5,042)	1,568
Income tax expense (benefit)	—	9	24	119	(1)	151
Net income (loss)	1,418	248	1,955	2,837	(5,041)	1,417
Less net loss (income) for noncontrolling interests	—	—	—	(2)	3	1
Net income (loss) attributable to Eaton ordinary shareholders	\$ 1,418	\$ 248	\$ 1,955	\$ 2,835	\$ (5,038)	\$ 1,418

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Other comprehensive income (loss)	\$ 42	\$ 68	\$ 54	\$ (21) \$ (101) \$42
Total comprehensive income (loss) attributable to Eaton ordinary shareholders	\$ 1,460	\$ 316	\$ 2,009	\$ 2,814	\$ (5,139) \$1,460

17

CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2015

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net sales	\$ —	\$ 5,263	\$ 5,065	\$ 9,469	\$ (3,999)	\$ 15,798
Cost of products sold	—	4,123	3,837	6,864	(3,959)	10,865
Selling and administrative expense	6	1,120	539	1,058	—	2,723
Research and development expense	—	202	145	125	—	472
Interest expense (income) - net	—	166	16	(10)	3	175
Other expense (income) - net	—	17	(5)	(39)	—	(27)
Equity in loss (earnings) of subsidiaries, net of tax	(1,698)	(529)	(2,403)	(315)	4,945	—
Intercompany expense (income) - net	245	(362)	1,010	(893)	—	—
Income (loss) before income taxes	1,447	526	1,926	2,679	(4,988)	1,590
Income tax expense (benefit)	—	36	(32)	154	(15)	143
Net income (loss)	1,447	490	1,958	2,525	(4,973)	1,447
Less net loss (income) for noncontrolling interests	—	—	—	(1)	1	—
Net income (loss) attributable to Eaton ordinary shareholders	\$ 1,447	\$ 490	\$ 1,958	\$ 2,524	\$ (4,972)	\$ 1,447
Other comprehensive income (loss)	\$ (716)	\$ 39	\$ (691)	\$ (875)	\$ 1,527	\$ (716)
Total comprehensive income (loss) attributable to Eaton ordinary shareholders	\$ 731	\$ 529	\$ 1,267	\$ 1,649	\$ (3,445)	\$ 731

CONDENSED CONSOLIDATING BALANCE SHEETS
SEPTEMBER 30, 2016

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Assets						
Current assets						
Cash	\$ 1	\$ 70	\$ 4	\$ 419	\$ —	\$494
Short-term investments	—	—	—	213	—	213
Accounts receivable - net	—	510	1,072	2,077	—	3,659
Intercompany accounts receivable	2	637	4,149	3,484	(8,272)	—
Inventory	—	365	647	1,395	(79)	2,328
Prepaid expenses and other current assets	—	107	40	219	27	393
Total current assets	3	1,689	5,912	7,807	(8,324)	7,087
Property, plant and equipment - net	—	863	712	1,931	—	3,506
Other noncurrent assets						
Goodwill	—	1,355	6,264	5,815	—	13,434
Other intangible assets	—	172	3,481	2,036	—	5,689
Deferred income taxes	—	987	—	231	(806)	412
Investment in subsidiaries	32,690	13,491	72,562	12,194	(130,937)	—
Intercompany loans receivable	—	7,614	2,182	56,101	(65,897)	—
Other assets	—	603	129	377	—	1,109
Total assets	\$ 32,693	\$ 26,774	\$ 91,242	\$ 86,492	\$(205,964)	\$31,237
Liabilities and shareholders' equity						
Current liabilities						
Short-term debt	\$ —	\$ —	\$ —	\$ 1	\$ —	\$1
Current portion of long-term debt	—	251	299	—	—	550
Accounts payable	—	415	259	1,116	—	1,790
Intercompany accounts payable	194	3,966	2,982	1,130	(8,272)	—
Accrued compensation	—	85	51	252	—	388
Other current liabilities	1	630	297	939	(1)	1,866
Total current liabilities	195	5,347	3,888	3,438	(8,273)	4,595
Noncurrent liabilities						
Long-term debt	—	6,889	971	16	5	7,881
Pension liabilities	—	605	168	759	—	1,532
Other postretirement benefits liabilities	—	237	114	78	—	429
Deferred income taxes	—	—	771	401	(806)	366
Intercompany loans payable	17,094	2,377	44,900	1,526	(65,897)	—
Other noncurrent liabilities	—	344	214	430	—	988
Total noncurrent liabilities	17,094	10,452	47,138	3,210	(66,698)	11,196

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Shareholders' equity						
Eaton shareholders' equity	15,404	10,975	40,216	79,807	(130,998) 15,404
Noncontrolling interests	—	—	—	37	5	) 42
Total equity	15,404	10,975	40,216	79,844	(130,993	) 15,446
Total liabilities and equity	\$ 32,693	\$ 26,774	\$ 91,242	\$ 86,492	\$ (205,964	) \$31,237

19

CONDENSED CONSOLIDATING BALANCE SHEETS
DECEMBER 31, 2015

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Assets						
Current assets						
Cash	\$ —	\$ 26	\$ 7	\$ 235	\$ —	\$268
Short-term investments	—	—	2	175	—	177
Accounts receivable - net	—	512	1,030	1,937	—	3,479
Intercompany accounts receivable	1	842	3,888	2,928	(7,659)	—
Inventory	—	357	651	1,395	(80)	2,323
Prepaid expenses and other current assets	—	77	40	229	23	369
Total current assets	1	1,814	5,618	6,899	(7,716)	6,616
Property, plant and equipment - net	—	930	750	1,885	—	3,565
Other noncurrent assets						
Goodwill	—	1,355	6,264	5,860	—	13,479
Other intangible assets	—	182	3,624	2,208	—	6,014
Deferred income taxes	—	1,016	—	218	(872)	362
Investment in subsidiaries	29,627	12,883	60,139	10,046	(112,695)	—
Intercompany loans receivable	—	8,641	1,573	44,835	(55,049)	—
Other assets	—	492	122	346	—	960
Total assets	\$ 29,628	\$ 27,313	\$ 78,090	\$ 72,297	\$ (176,332)	\$30,996
Liabilities and shareholders' equity						
Current liabilities						
Short-term debt	\$ —	\$ 408	\$ —	\$ 18	\$ —	\$426
Current portion of long-term debt	—	1	240	1	—	242
Accounts payable	—	392	260	1,106	—	1,758
Intercompany accounts payable	219	4,009	2,248	1,183	(7,659)	—
Accrued compensation	—	77	53	236	—	366
Other current liabilities	1	644	318	875	(5)	1,833
Total current liabilities	220	5,531	3,119	3,419	(7,664)	4,625
Noncurrent liabilities						
Long-term debt	—	7,053	675	17	1	7,746
Pension liabilities	—	639	165	782	—	1,586
Other postretirement benefits liabilities	—	245	118	77	—	440
Deferred income taxes	—	—	815	447	(872)	390
Intercompany loans payable	14,222	2,962	36,432	1,433	(55,049)	—
Other noncurrent liabilities	—	346	200	432	—	978
Total noncurrent liabilities	14,222	11,245	38,405	3,188	(55,920)	11,140

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Shareholders' equity						
Eaton shareholders' equity	15,186	10,537	36,566	65,653	(112,756) 15,186
Noncontrolling interests	—	—	—	37	8	45
Total equity	15,186	10,537	36,566	65,690	(112,748	) 15,231
Total liabilities and equity	\$ 29,628	\$ 27,313	\$ 78,090	\$ 72,297	\$ (176,332	) \$30,996

20

CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2016

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net cash provided by (used in) operating activities	\$ (158)	\$ (29)	\$ (283)	\$ 2,384	\$ —	\$ 1,914
Investing activities						
Capital expenditures for property, plant and equipment	—	(62)	(75)	(209)	—	(346)
Cash received from (paid for) acquisitions of businesses, net of cash acquired	—	—	1	—	—	1
Sales (purchases) of short-term investments - net	—	—	2	(31)	—	(29)
Investments in affiliates	(1,250)	—	(120)	(1,370)	2,740	—
Return of investments in affiliates	—	—	47	—	(47)	—
Loans to affiliates	—	(287)	(655)	(6,457)	7,399	—
Repayments of loans from affiliates	—	1,288	—	4,501	(5,789)	—
Other - net	—	—	30	(27)	—	3
Net cash provided by (used in) investing activities	(1,250)	939	(770)	(3,593)	4,303	(371)
Financing activities						
Proceeds from borrowings	—	22	611	—	—	633
Payments on borrowings	—	(408)	(240)	(18)	—	(666)
Proceeds from borrowings from affiliates	3,333	2,815	1,051	200	(7,399)	—
Payments on borrowings from affiliates	(637)	(3,453)	(1,658)	(41)	5,789	—
Capital contributions from affiliates	—	—	1,370	1,370	(2,740)	—
Return of capital to affiliates	—	—	—	(47)	47	—
Other intercompany financing activities	—	158	(81)	(77)	—	—
Cash dividends paid	(780)	—	—	—	—	(780)
Exercise of employee stock options	60	—	—	—	—	60
Repurchase of shares	(567)	—	—	—	—	(567)
Excess tax benefit from equity-based compensation	—	—	—	—	—	—
Other - net	—	—	(3)	(2)	—	(5)
Net cash provided by (used in) financing activities	1,409	(866)	1,050	1,385	(4,303)	(1,325)
Effect of currency on cash	—	—	—	8	—	8
Total increase (decrease) in cash	1	44	(3)	184	—	226
Cash at the beginning of the period	—	26	7	235	—	268
Cash at the end of the period	\$ 1	\$ 70	\$ 4	\$ 419	\$ —	\$ 494

CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2015

	Eaton Corporation plc	Eaton Corporation	Guarantors	Other subsidiaries	Consolidating adjustments	Total
Net cash provided by (used in) operating activities	\$ (85)	\$ (93)	\$ (23)	\$ 1,830	\$ —	\$ 1,629
Investing activities						
Capital expenditures for property, plant and equipment	—	(68)	(100)	(200)	—	(368)
Cash received from (paid for) acquisitions of businesses, net of cash acquired	—	—	—	(38)	—	(38)
Sales (purchases) of short-term investments - net	—	—	—	76	—	76
Investments in affiliates	(1,482)	—	(1,176)	(1,482)	4,140	—
Loans to affiliates	—	(307)	(39)	(7,638)	7,984	—
Repayments of loans from affiliates	—	306	58	5,514	(5,878)	—
Proceeds from sale of businesses	—	—	—	1	—	1
Other - net	—	(41)	33	(36)	—	(44)
Net cash provided by (used in) investing activities	(1,482)	(110)	(1,224)	(3,803)	6,246	(373)
Financing activities						
Proceeds from borrowings	—	—	—	1	—	1
Payments on borrowings	—	(102)	(301)	(2)	—	(405)
Proceeds from borrowings from affiliates	2,783	4,577	581	43	(7,984)	—
Payments on borrowings from affiliates	(40)	(4,617)	(1,160)	(61)	5,878	—
Capital contributions from affiliates	—	1,176	1,482	1,482	(4,140)	—
Other intercompany financing activities	—	(859)	644	215	—	—
Cash dividends paid	(771)	—	—	—	—	(771)
Exercise of employee stock options	48	—	—	—	—	48
Repurchase of shares	(454)	—	—	—	—	(454)
Other - net	—	—	—	(8)	—	(8)
Net cash provided by (used in) financing activities	1,566	175	1,246	1,670	(6,246)	(1,589)
Effect of currency on cash	—	—	—	(30)	—	(30)
Total increase (decrease) in cash	(1)	(28)	(1)	(333)	—	(363)
Cash at the beginning of the period	1	173	13	594	—	781
Cash at the end of the period	\$ —	\$ 145	\$ 12	\$ 261	\$ —	\$ 418

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 with 2015 net sales of \$20.9 billion. The Company provides energy-efficient solutions that help its customers effectively manage electrical, hydraulic, and mechanical power more efficiently, safely, and sustainably. Eaton has approximately 95,000 employees in over 60 countries and sells products to customers in more than 175 countries.

Summary of Results of Operations

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

	Three months ended September 30 2016		Nine months ended September 30 2015	
Net sales	\$4,987	\$5,203	\$14,880	\$15,798
Net income attributable to Eaton ordinary shareholders	523	446	1,418	1,447
Net income per share attributable to Eaton ordinary shareholders - diluted	\$1.15	\$0.96	\$3.09	\$3.09

During 2015, Eaton announced a multi-year restructuring initiative to reduce its cost structure and gain efficiencies in all business segments and at corporate in order to respond to declining market conditions. Restructuring charges in the third quarter and first nine months of 2016 were \$23 and \$121, respectively, and were \$113 and \$127 in 2015, respectively. These charges were primarily comprised of severance costs. Restructuring charges are anticipated to be \$145 in 2016 and \$180 in 2017. The projected annualized savings from these restructuring actions are expected to be \$508, when fully realized in 2018.

RESULTS OF OPERATIONS

Non-GAAP Financial Measures

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, each of which differs from the most directly comparable measure calculated in accordance with generally accepted accounting principles (GAAP). A reconciliation of operating earnings and operating earnings per ordinary share to the most directly comparable GAAP measure is included in the table below. Operating profit before acquisition integration charges is reconciled in the discussion of the operating results of each business segment, and excludes acquisition integration expense related to the integration of Ephesus Lighting, Inc. and Oxalis Group Ltd. in 2016 and primarily Cooper Industries plc in 2015. Management believes that these financial measures are useful to investors because they exclude certain transactions, 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.

Table of Contents

Consolidated Financial Results

	Three months ended September 30		Increase (decrease)	Nine months ended September 30		Decrease
	2016	2015		2016	2015	
Net sales	\$4,987	\$5,203	(4)%	\$14,880	\$15,798	(6)%
Gross profit	1,616	1,606	1 %	4,799	4,933	(3)%
Percent of net sales	32.4 %	30.9 %		32.3 %	31.2 %	
Income before income taxes	573	487	18 %	1,568	1,590	(1)%