

CUMMINS INC
Form 10-Q
October 30, 2009

**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 27, 2009

Commission File Number 1-4949

CUMMINS INC.

(Exact name of registrant as specified in its charter)

Indiana
(State of Incorporation)

35-0257090
(IRS Employer Identification No.)

500 Jackson Street

Box 3005

Columbus, Indiana 47202-3005

(Address of principal executive offices)

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Telephone (812) 377-5000

(Registrant's telephone number, including area code)

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 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 definition 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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of September 27, 2009, there were 201,792,780 shares of common stock outstanding with a par value of \$2.50 per share.

Website Access to Company's Reports

Cummins maintains an internet website at www.cummins.com. Investors can obtain copies of our filings from this website free of charge as soon as reasonably practicable after they are electronically filed with, or furnished to the Securities and Exchange Commission.

CUMMINS INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

ITEM 1. Condensed Financial Statements

CUMMINS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

In millions (except per share amounts)	Three months ended		Nine months ended	
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
NET SALES (a)	\$ 2,530	\$ 3,693	\$ 7,400	\$ 11,054
Cost of sales	2,027	2,873	6,004	8,648
GROSS MARGIN	503	820	1,396	2,406
OPERATING EXPENSES AND INCOME				
Selling, general and administrative expenses	304	388	891	1,109
Research, development and engineering expenses	90	113	254	320
Equity, royalty and interest income from investees (Note 4)	57	66	147	202
Restructuring and other charges (Note 5)	22		95	
Other operating income (expense), net	3	(2)	(6)	(9)
OPERATING INCOME	147	383	297	1,170
Interest income	2	4	5	14
Interest expense	9	10	26	33
Other income (expense), net	6	(7)	(10)	(20)
INCOME BEFORE INCOME TAXES	146	370	266	1,131
Income tax expense	36	123	72	372
NET INCOME	110	247	194	759
Less: net income attributable to noncontrolling interests	15	18	36	47
NET INCOME ATTRIBUTABLE TO CUMMINS INC.	\$ 95	\$ 229	\$ 158	\$ 712
EARNINGS PER COMMON SHARE ATTRIBUTABLE TO CUMMINS INC.				
Basic	\$ 0.48	\$ 1.18	\$ 0.80	\$ 3.65
Diluted	\$ 0.48	\$ 1.17	\$ 0.80	\$ 3.62
WEIGHTED AVERAGE SHARES OUTSTANDING				
Basic	197.4	194.9	197.1	195.1
Dilutive effect of stock compensation awards	0.4	1.6	0.3	1.4
Diluted	197.8	196.5	197.4	196.5
	\$ 0.175	\$ 0.175	\$ 0.525	\$ 0.425

**CASH DIVIDENDS DECLARED PER
COMMON SHARE**

(a) Includes sales to nonconsolidated equity investees of \$428 million and \$1,279 million and \$554 million and \$1,636 million for the three and nine months ended September 27, 2009 and September 28, 2008, respectively.

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

CUMMINS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

In millions (except par value)	September 27, 2009	December 31, 2008
ASSETS		
Current assets		
Cash and cash equivalents	\$ 686	\$ 426
Marketable securities	148	77
Accounts and notes receivable, net		
Trade and other	1,534	1,551
Nonconsolidated equity investees	197	231
Inventories (Note 7)	1,461	1,783
Deferred income taxes	363	347
Prepaid expenses and other current assets	254	298
Total current assets	4,643	4,713
Long-term assets		
Property, plant and equipment	4,736	4,539
Accumulated depreciation	(2,877)	(2,698)
Property, plant and equipment, net	1,859	1,841
Investments and advances related to equity method investees	538	588
Goodwill	363	362
Other intangible assets, net	229	223
Deferred income taxes	400	491
Other assets	323	301
Total assets	\$ 8,355	\$ 8,519
LIABILITIES		
Current liabilities		
Current portion of long-term debt and loans payable	\$ 60	\$ 69
Accounts payable (principally trade)	875	1,009
Current portion of accrued product warranty (Note 8)	422	434
Accrued compensation, benefits and retirement costs	335	364
Other accrued expenses	619	763
Total current liabilities	2,311	2,639
Long-term liabilities		
Long-term debt	621	629
Pensions	425	574
Postretirement benefits other than pensions	455	452
Other liabilities and deferred revenue	740	745
Total liabilities	4,552	5,039
Commitments and contingencies (Note 9)		
EQUITY		
Cummins Inc. shareholders' equity		
Common stock, \$2.50 par value, 500 shares authorized, 222.1 and 221.7 shares issued	1,842	1,793
Retained earnings	3,340	3,288
Treasury stock, at cost, 20.3 and 20.4 shares	(713)	(715)
Common stock held by employee benefits trust, at cost, 3.5 and 5.1 shares	(43)	(61)
Unearned compensation	(1)	(5)
Accumulated other comprehensive loss		
Defined benefit postretirement plans	(741)	(798)
Other	(121)	(268)
Total accumulated other comprehensive loss	(862)	(1,066)
Total Cummins Inc. shareholders' equity	3,563	3,234

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Noncontrolling interests	240	246
Total equity	3,803	3,480
Total liabilities and equity	\$ 8,355	\$ 8,519

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

CUMMINS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

In millions	Nine months ended	
	September 27, 2009	September 28, 2008
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 194	\$ 759
Adjustments to reconcile net income to net cash provided by operating activities:		
Restructuring charges, net of cash payments (Note 5)	21	
Depreciation and amortization	238	233
Deferred income taxes	(11)	38
Equity in income of investees, net of dividends	56	(80)
Pension expense, net of pension contributions (Note 6)	(49)	(40)
Other post-retirement benefits expense, net of cash payments (Note 6)	(18)	(11)
Stock-based compensation expense	16	27
Excess tax deficiencies (benefits) on stock-based awards	2	(12)
Translation and hedging activities	33	15
Changes in current assets and liabilities, net of acquisitions and dispositions:		
Accounts and notes receivable	89	(310)
Inventories	360	(334)
Other current assets	32	(35)
Accounts payable	(155)	198
Accrued expenses	(185)	206
Changes in long-term liabilities	103	78
Other, net	4	(7)
Net cash provided by operating activities	730	725
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(204)	(330)
Investments in internal use software	(24)	(53)
Proceeds from disposals of property, plant and equipment	8	20
Investments in and advances to equity investees	(5)	(51)
Acquisition of businesses, net of cash acquired	(2)	(142)
Proceeds from the sale of an equity investment		64
Investments in marketable securities acquisitions	(234)	(264)
Investments in marketable securities liquidations	171	281
Purchases of other investments	(54)	(54)
Cash flows from derivatives not designated as hedges	(21)	(24)
Other, net	1	1
Net cash used in investing activities	(364)	(552)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from borrowings	11	91
Payments on borrowings and capital lease obligations	(60)	(111)
Net borrowings under short-term credit agreements	(4)	5
Distributions to noncontrolling interests	(16)	(14)
Dividend payments on common stock	(106)	(86)
Proceeds from sale of common stock held by employee benefit trust	54	52
Repurchases of common stock		(123)
Excess tax (deficiencies) benefits on stock-based awards	(2)	12
Other, net	3	3
Net cash used in financing activities	(120)	(171)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	14	(7)

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Net increase (decrease) in cash and cash equivalents	260	(5)
Cash and cash equivalents at beginning of year	426	577
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 686	\$ 572

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

CUMMINS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(Unaudited)

In millions	Common Stock	Additional paid-in Capital	Accumulated Other Retained Earnings	Comprehensive Loss	Treasury Stock	Common Stock Held in Trust	Unearned Compensation	Total Cummins Inc. Shareholder Equity	Noncontrolling Interests	Total Equity
BALANCE AT DECEMBER 31, 2007	\$ 551	\$ 1,168	\$ 2,660	\$ (286)	\$ (593)	\$ (79)	\$ (11)	\$ 3,410	\$ 292	\$ 3,702
Comprehensive income:										
Net income			712					712	47	759
Other comprehensive income (loss) (Note 13)				(96)				(96)	(26)	(122)
Total comprehensive income								616	21	637
Effect of changing pension plan measurement date			(5)	(2)				(7)		(7)
Issuance of shares	3							3	8	11
Employee benefits trust activity		41				11		52		52
Acquisition of shares					(123)			(123)		(123)
Purchase of equity from noncontrolling interests									(54)	(54)
Cash dividends on common stock			(86)					(86)		(86)
Distribution to noncontrolling interests									(14)	(14)
Stock option exercises		(1)			5			4		4
Other shareholder transactions		22					5	27	(4)	23
BALANCE AT SEPTEMBER 28, 2008	\$ 554	\$ 1,230	\$ 3,281	\$ (384)	\$ (711)	\$ (68)	\$ (6)	\$ 3,896	\$ 249	\$ 4,145
BALANCE AT DECEMBER 31, 2008	\$ 554	\$ 1,239	\$ 3,288	\$ (1,066)	\$ (715)	\$ (61)	\$ (5)	\$ 3,234	\$ 246	\$ 3,480
Comprehensive income:										
Net income			158					158	36	194
Other comprehensive income (loss) (Note 13)				204				204	9	213
Total comprehensive income								362	45	407
Issuance of shares	1	6						7		7
Cash dividends on common stock			(106)					(106)		(106)
Employee benefits trust activity		40				18		58		58
Distribution to noncontrolling interests									(16)	(16)
Stock option exercises		(1)			2			1		1
Conversion to capital lease (Note 12)									(35)	(35)
		3					4	7		7

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Other shareholder
transactions

BALANCE AT

SEPTEMBER 27, 2009	\$	555	\$	1,287	\$	3,340	\$	(862)	(1)	\$	(713)	\$	(43)	\$	(1)	\$	3,563	\$	240	\$	3,803
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(1) Comprised of defined benefit postretirement plans of \$(741) million, foreign currency translation adjustments of \$(121) million, unrealized gain on marketable securities of \$2 million and unrealized loss on derivatives of \$(2) million.

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

CUMMINS INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. NATURE OF OPERATIONS

Cummins Inc. (Cummins, the Company, the registrant, we, our, or us) is a leading global power provider that designs, manufactures, distributes and services diesel and natural gas engines, electric power generation systems and engine-related component products, including filtration and emissions solutions, turbochargers, fuel systems, controls and air handling systems. We were founded in 1919 as one of the first manufacturers of diesel engines and are headquartered in Columbus, Indiana. We sell our products to Original Equipment Manufacturers (OEMs), distributors and other customers worldwide. We serve our customers through a network of more than 500 company-owned and independent distributor locations and approximately 5,200 dealer locations in more than 190 countries and territories.

NOTE 2. BASIS OF PRESENTATION

The unaudited *Condensed Consolidated Financial Statements* reflect all adjustments which, in the opinion of management, are necessary for a fair statement of the results of operations, financial position and cash flows. All such adjustments are of a normal recurring nature. The *Condensed Consolidated Financial Statements* have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted as permitted by such rules and regulations. Certain reclassifications have been made to prior period amounts to conform to the presentation of the current period condensed financial statements.

Our reporting period ends on the Sunday closest to the last day of the quarterly calendar period. The third quarters of 2009 and 2008 ended on September 27, and September 28, respectively. The interim periods for both 2009 and 2008 contain 13 weeks. Our fiscal year ends on December 31, regardless of the day of the week on which December 31 falls.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect reported amounts in the *Condensed Consolidated Financial Statements*. Significant estimates and assumptions in these *Condensed Consolidated Financial Statements* require the exercise of judgment and are used for, but not limited to, allowance for doubtful accounts, estimates of future cash flows and other assumptions associated with goodwill and long-lived asset impairment tests, useful lives for depreciation and amortization, warranty programs, determination of discount and other rate assumptions for pension and other postretirement benefit expenses, income taxes and deferred tax valuation allowances and contingencies. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be different from these estimates.

The weighted-average diluted common shares outstanding exclude the anti-dilutive effect of certain stock options since such options had an exercise price in excess of the monthly average market value of our common stock. The options excluded from diluted earnings per share for the three and nine month periods ended September 27, 2009, and September 28, 2008, were as follows:

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	Three months ended		Nine months ended	
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
Options excluded	28,717	5,950	61,585	6,885

You should read these interim condensed financial statements in conjunction with the *Consolidated Financial Statements* included in our Annual Report on Form 10-K for the year ended December 31, 2008. Our interim period financial results for the three and nine month interim periods presented are not necessarily indicative of results to be expected for any other interim period or for the entire year. The year-end *Condensed Consolidated Balance Sheet* data was derived from audited financial statements, but does not include all disclosures required by GAAP.

NOTE 3. RECENTLY ADOPTED AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Accounting Pronouncements Recently Adopted

In December 2007, the Financial Accounting Standards Board (FASB) amended its existing standards for noncontrolling interests in consolidated financial statements, which was effective for interim and annual fiscal periods beginning after December 15, 2008. The new standard established accounting and reporting standards for the noncontrolling interest in a subsidiary and for the accounting for future ownership changes with respect to those subsidiaries. The new standard defined a noncontrolling interest, previously called a minority interest, as the portion of equity in a subsidiary not attributable, directly or indirectly, to a parent. The new standard required, among other items, that a noncontrolling interest be included in the consolidated balance sheet within equity, separate from the parent's equity; consolidated net income to be reported at amounts inclusive of both the parent's and noncontrolling interest's shares and, separately, the amounts of consolidated net income attributable to the parent and noncontrolling interest all on the consolidated statements of income; and if a subsidiary is deconsolidated, any retained noncontrolling equity investment in the former subsidiary be measured at fair value and a gain or loss be recognized in net income based on such fair value. We adopted the new standard effective January 1, 2009, and applied it retrospectively. As a result, we reclassified noncontrolling interests of \$246 million from the mezzanine section to equity in the December 31, 2008, balance sheet. Certain reclassifications have been made to prior period amounts to conform to the presentation of the current period under the new standard.

In March 2008, the FASB amended its existing standards for disclosures about derivative instruments and hedging activities, which was effective for interim and annual fiscal periods beginning after November 15, 2008. The new standards require enhanced disclosures about a company's derivative and hedging activities. We adopted the new standard effective January 1, 2009, and applied it prospectively. The new disclosures required are included in Note 11.

In April 2009, the FASB amended its existing standards for accounting and disclosures related to certain financial instruments including: (a) providing additional rules for estimating fair value when the volume and level of activity for the asset or liability has significantly decreased; (b) identifying circumstances that indicate a transaction is not orderly; (c) amending the other-than-temporary impairment rules for debt securities to make it more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities in the financial statements; and (d) requiring enhanced disclosures about the fair value of financial instruments on an interim basis in addition to the annual disclosure requirements (Note 10). The new standards were required to be adopted for interim periods ending after June 15, 2009. The adoption of the new standards did not have a material impact on our *Condensed Consolidated Financial Statements*.

In June 2009, the FASB amended its existing standards for subsequent events, which was effective for interim and annual fiscal periods ending after June 15, 2009, and established general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. The new standard established the period after the balance sheet date during which we should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, the circumstances under which we should recognize events or transactions occurring after the balance sheet date and the disclosures that should be made about events or transactions that occurred after the balance sheet date. In preparing our *Condensed Consolidated Financial Statements*, we evaluated subsequent events through October 30, 2009, which is the date our quarterly report was filed with the Securities and Exchange Commission.

Accounting Pronouncements Issued But Not Yet Effective

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In June 2009, the FASB amended its standards for accounting for transfers of financial assets, which is effective for interim and annual fiscal periods beginning after November 15, 2009. The new standard removes the concept of a qualifying special-purpose entity from GAAP. The new standard modifies the financial-components approach used in previous standards and limits the circumstances in which a financial asset, or portion of a financial asset, should be derecognized. The new standard also requires enhanced disclosure regarding transfers of financial interests and a transferor's continuing involvement with transferred assets. The new standard will require us to report any future activity under our sale of receivables program as secured borrowings as of January 1, 2010.

In June 2009, the FASB amended its existing standards related to the consolidation of variable interest entities, which is effective for interim and annual fiscal periods beginning after November 15, 2009. The new standard requires entities to analyze whether their variable interests give it a controlling financial interest of a variable interest entity (VIE) and outlines what defines a primary beneficiary. The new standard amends GAAP by: (a) changing certain rules for determining whether an entity is a VIE; (b) replacing the quantitative approach previously required for determining the primary beneficiary with a more qualitative approach; and (c) requiring entities to continuously analyze whether they are the primary beneficiary of a VIE among other amendments. The new standard also requires enhanced disclosures regarding an entity's involvement in a VIE. It is possible that application of this new standard will change our assessment of whether or not we are the primary beneficiary of any VIEs with which we are involved. We are currently evaluating the impact of this standard on our *Condensed Consolidated Financial Statements*.

NOTE 4. EQUITY, ROYALTY AND INTEREST INCOME FROM INVESTEES

Equity, royalty and interest income from investees included in our *Condensed Consolidated Statements of Income* for the interim reporting periods was as follows:

In millions	Three months ended		Nine months ended	
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
Distribution Entities				
North American distributors	\$ 25	\$ 26	\$ 74	\$ 72
Komatsu Cummins Chile, Ltda.	3	2	9	5
All other distributors	1	2	2	3
Manufacturing Entities				
Dongfeng Cummins Engine Company, Ltd	11	16	18	50
Chongqing Cummins Engine Company, Ltd	8	9	28	23
Valvoline Cummins, Ltd.	3	1	5	2
Shanghai Fleetguard Filter Co. Ltd.	2	2	5	7
Tata Cummins Ltd.	2		2	7
Cummins MerCruiser Diesel Marine LLC.	(2)	(1)	(5)	5
All other manufacturers		4	(2)	12
Cummins share of net income	53	61	136	186
Royalty and interest income	4	5	11	16
Equity, royalty and interest income from investees	\$ 57	\$ 66	\$ 147	\$ 202

NOTE 5. RESTRUCTURING AND OTHER CHARGES

2009 Restructuring Actions

In 2009, we executed restructuring actions in response to a reduction in orders in most of our U.S. and foreign markets due to the continuing deterioration in the global economy. We reduced our global workforce by approximately 1,000 professional employees. In addition, we took numerous employee actions at many of our manufacturing locations, including approximately 3,150 hourly employees, significant downsizing at numerous facilities and complete closure of several facilities and branch distributor locations. Employee termination and severance costs were recorded based on approved plans developed by the businesses and corporate management which specified positions to be eliminated, benefits to be paid under existing severance plans, union contracts or statutory requirements and the expected timetable for completion of the plan.

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Estimates of restructuring were made based on information available at the time charges were recorded. Due to the inherent uncertainty involved, actual amounts paid for such activities may differ from amounts initially recorded and we may need to revise previous estimates.

In response to closures and downsizing noted above, we incurred \$2 million of restructuring expenses for lease terminations and \$5 million of restructuring expenses for asset impairments. During 2009 we recorded a total pre-tax restructuring charge of \$83 million, comprising \$85 million of charges related to 2009 actions net of the \$2 million favorable change in estimate related to 2008 actions, in Restructuring and other charges in the *Condensed*

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Consolidated Statements of Income. The estimated completion date for the workforce reductions and the exit activities is March 2010. These restructuring actions included:

In millions	September 27, 2009	
	Three months ended	Nine months ended
Workforce reductions	\$ 11	\$ 79
Exit activities		7
Changes in estimate	(1)	(3)
Total restructuring charges	10	83
Curtailment loss	12	12
Total restructuring and other charges	\$ 22	\$ 95

In addition, as a result of the restructuring actions described above, we also recorded a \$12 million curtailment loss in the third quarter of 2009 in our pension and other postretirement plans. See Note 6 for additional detail.

The following table summarizes the balance of accrued restructuring charges by expense type and the changes in the accrued amounts for the applicable periods. The restructuring related accruals were recorded in Other accrued expenses in the *Condensed Consolidated Balance Sheets*.

In millions	Severance Costs	Exit Activities	Total
2009 Restructuring charges	\$ 79	\$ 7	\$ 86
Cash payments for 2009 actions	(61)	(1)	(62)
Noncash items		(5)	(5)
Changes in estimates	(1)		(1)
Translation	1		1
Balance at September 27, 2009	\$ 18	\$ 1	\$ 19

We do not include restructuring charges in our operating segment results. The pretax impact of allocating restructuring charges to the segment results would have been as follows:

In millions	September 27, 2009	
	Three months ended	Nine months ended
Engine	\$ 11	\$ 47
Power Generation	4	11
Components	8	34
Distribution	(1)	3
Total restructuring charges	\$ 22	\$ 95

2008 Restructuring Actions

In 2008, we executed restructuring actions in response to the continued deterioration in our U.S. businesses and most key markets around the world in the second half of 2008, as well as a reduction in orders in most U.S. and foreign markets for 2009. In 2008, we announced reductions of our global workforce by approximately 650 professional employees. In addition, we took numerous employee actions at many of our

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manufacturing locations, including approximately 800 hourly employees. Total workforce reductions as of September 27, 2009, were substantially completed.

The charges recorded during the year ended December 31, 2008, included severance costs related to both voluntary and involuntary terminations. During 2008, we incurred a pretax charge related to the professional and hourly restructuring initiatives of \$37 million. The following table summarizes the balance of accrued restructuring charges and the changes in the accrued amounts for the applicable periods. The restructuring related accruals were recorded in Other accrued expenses in the *Condensed Consolidated Balance Sheets*.

In millions	Severance Costs	
Balance at December 31, 2008	\$	34
Cash payments for 2008 actions		(30)
Change in estimate		(2)
Balance at September 27, 2009	\$	2

NOTE 6. PENSION AND OTHER POSTRETIREMENT BENEFITS

We sponsor funded and unfunded domestic and foreign defined benefit pension and other postretirement plans. Cash contributions to these plans were as follows:

In millions	Three months ended		Nine months ended	
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
Defined benefit pension and postretirement plans:				
Voluntary	\$ 55	\$ 46	\$ 100	\$ 70
Mandatory	21	21	62	51
Total defined benefit plans	\$ 76	\$ 67	\$ 162	\$ 121
Defined contribution pension plans	\$ 9	\$ 6	\$ 32	\$ 24

We presently anticipate contributing \$130 million to \$135 million to our defined benefit pension plans in 2009 and paying approximately \$53 million in claims and premiums for other postretirement benefits. The \$130 million to \$135 million of contributions for the full year include voluntary contributions of \$100 million to \$105 million. These contributions and payments include payments from Company funds either to increase pension assets or to make direct payments to plan participants.

The components of net periodic pension and other postretirement benefit cost under our plans consisted of the following:

In millions	Pension				Other Postretirement Benefits	
	U.S. Plans		Non-U.S. Plans		September 27, 2009	September 28, 2008
	September 27, 2009	September 28, 2008	Three months ended			
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
Service cost	\$ 11	\$ 12	\$ 5	\$ 6	\$ 7	\$ 8
Interest cost	28	28	15	17		
Expected return on plan assets	(34)	(37)	(16)	(18)		
Amortization of prior service cost (credit)			1		(2)	(2)
Recognized net actuarial loss	8	5	5	5		
Net periodic benefit costs	13	8	10	10	5	6
Curtailed loss	6				6	
Net periodic benefit cost after curtailment losses	\$ 19	\$ 8	\$ 10	\$ 10	\$ 11	\$ 6

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In millions	Pension				Other Postretirement Benefits	
	U.S. Plans		Non-U.S. Plans		September 27, 2009	September 28, 2008
	September 27, 2009	September 28, 2008	Nine months ended			
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
Service cost	\$ 34	\$ 36	\$ 13	\$ 20	\$	\$
Interest cost	85	86	42	49	22	24
Expected return on plan assets	(104)	(113)	(44)	(56)		
Amortization of prior service (credit) cost	(1)		3	2	(6)	(7)
Recognized net actuarial loss (gain)	23	15	15	15		(1)
Other	1					
Net periodic benefit cost	38	24	29	30	16	16
Curtailement loss	6				6	
Net periodic benefit cost after curtailement losses	\$ 44	\$ 24	\$ 29	\$ 30	\$ 22	\$ 16

As disclosed in Note 5, we have executed many restructuring actions over the past four quarters. As a result, our U.S. pension and other postretirement benefit plans were remeasured and we recognized curtailement losses as prescribed under U.S. GAAP pension and other postretirement benefit standards due to the significant reduction in the expected aggregate years of future service of the employees affected by the actions. In the third quarter of 2009, we recorded net curtailement losses of \$6 million and \$6 million related to the pension and other postretirement plans, respectively. The curtailement losses include recognition of the change in the projected benefit obligation (PBO) or accumulated postretirement benefit obligation (APBO) and a portion of the previously unrecognized prior service cost reflecting the reduction in expected future service.

The remeasurement of these pension and other postretirement benefit plans generated a decrease in the 2009 annual net periodic benefit cost for pension plans of \$3 million and a zero net change in the 2009 annual net periodic benefit cost for other postretirement benefit plans. The decrease will be recognized in the fourth quarter of 2009. Further, the pension plans' PBO and plan assets increased from December 31, 2008 by \$22 million and \$181 million, respectively (net of \$138 million in benefit payments and plan assets reflecting a contribution of \$100 million). The other postretirement benefit plans' APBO increased by \$3 million, due to the remeasurement.

Additionally, in the third quarter of 2009, we recorded a credit of \$87 million for pension plans and a charge of \$11 million for other postretirement benefit plans to accumulated other comprehensive loss in accordance with the provisions of U.S. GAAP pension and other postretirement benefit standards due to the remeasurement of the curtailed plans.

NOTE 7. INVENTORIES

Inventories included the following:

In millions	September 27, 2009	December 31, 2008
Finished products	\$ 833	\$ 860
Work-in-process and raw materials	716	1,021
Inventories at FIFO cost	1,549	1,881

Excess of FIFO over LIFO		(88)		(98)
Total inventories	\$	1,461	\$	1,783

NOTE 8. PRODUCT WARRANTY LIABILITY

We charge the estimated costs of warranty programs, other than product recalls, to income at the time products are shipped to customers. We use historical claims experience to develop the estimated liability. We review product recall programs on a quarterly basis and, if necessary, record a liability when we commit to an action. We also sell extended

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warranty coverage on several engines. The following is a tabular reconciliation of the product warranty liability, including the deferred revenue related to our extended warranty coverage:

In millions	Nine months ended	
	September 27, 2009	September 28, 2008
Balance, beginning of period	\$ 962	\$ 749
Provision for warranties issued	241	319
Deferred revenue on extended warranty contracts sold	77	73
Payments	(352)	(258)
Amortization of deferred revenue on extended warranty contracts	(54)	(47)
Changes in estimates for pre-existing warranties	67	63
Foreign currency translation	12	(10)
Balance, end of period	\$ 953	\$ 889

The amount of deferred revenue related to extended coverage programs as of September 27, 2009, was \$247 million. As of September 27, 2009, we had \$11 million of receivables related to estimated supplier recoveries of which \$5 million was included in Trade and other receivables and \$6 million was included in Other assets in our *Condensed Consolidated Balance Sheets*.

During 2008 and 2009, actual cost trends for certain midrange engine products, including product launched in 2007 and for which warranty periods can extend to five years, indicated higher per claim repair cost than the product on which the initial accrual rate was developed. These products include more electronic parts than historical models, contributing to the higher cost per claim. In addition, certain products introduced in 2003 and sold prior to 2007 for which the warranty period extended five years also demonstrated higher cost per claim than that of predecessor products. We increased our liability in 2008 and 2009 as these experience trends became evident.

NOTE 9. COMMITMENTS AND CONTINGENCIES

We are subject to numerous lawsuits and claims arising out of the ordinary course of our business, including actions related to product liability; personal injury; the use and performance of our products; warranty matters; patent, trademark or other intellectual property infringement; contractual liability; the conduct of our business; tax reporting in foreign jurisdictions; distributor termination; workplace safety; and environmental matters. We also have been identified as a potentially responsible party at multiple waste disposal sites under federal and related state environmental statutes and regulations and may have joint and several liability for any investigation and remediation costs incurred with respect to such sites. Some of these lawsuits, claims and proceedings involve substantial amounts. We have denied liability with respect to many of these lawsuits, claims and proceedings and are vigorously defending such lawsuits, claims and proceedings. We carry various forms of commercial, property and casualty, product liability and other forms of insurance; however, such insurance may not be applicable or adequate to cover the costs associated with a judgment against us with respect to these lawsuits, claims and proceedings. We do not believe that these lawsuits are material individually or in the aggregate. While we believe we have also established adequate accruals for our expected future liability with respect to pending lawsuits, claims and proceedings, where the nature and extent of any such liability can be reasonably estimated based upon then presently available information, there can be no assurance that the final resolution of any existing or future lawsuits, claims or proceedings will not have a material adverse effect on our business, results of operation, financial condition or cash flows.

In June 2008, four Cummins sites in Southern Indiana, including our Technical Center, experienced extensive damage caused by flood water from an unusually high amount of rainfall. We have been in ongoing discussions with our insurance carriers regarding our claim. In May 2009, our insurance carriers filed a lawsuit seeking a declaratory judgment that a lower policy sublimit applies to the Technical Center based upon an allegation that the site is located in a flood plain. In addition, they allege that certain other damages and losses claimed by Cummins are not covered by insurance. Cummins has also filed suit seeking a declaratory judgment that all losses suffered by Cummins are covered under the

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insurance policies, as well as a claim that the insurance companies have acted in bad faith. We have finalized the documentation of Cummins \$199 million claim (\$116 million expense and \$83

million capital), which does not include an additional claim amount related to business interruption. We remain confident that we will recover a majority of the amounts due to us under the insurance policies. We have incurred approximately \$99 million in expense and \$51 million in capital of our \$199 million claim through September 27, 2009. We recorded gains on insurance recoveries related to flood damage of \$8 million and \$5 million for the three and nine months ended September 27, 2009, respectively. These gains were included in Other operating (expense) income in the *Condensed Consolidated Statements of Income*.

U.S. Distributor Commitments

We had an operating agreement with a financial institution that provided financing to certain independent Cummins and Onan distributors in the U.S., and to certain distributors in which we own an equity interest. Under this agreement, if any distributor defaulted under its financing arrangement with the financial institution, and the maturity of amounts owed under the agreement were accelerated, then we were required to purchase from the financial institution, at amounts approximating fair market value, certain property, inventory and rental generator sets manufactured by Cummins that are secured by the distributor's financing agreement.

In May 2009, the distributor agreement with the financial institution was refinanced and Cummins did not make any new commitments, thereby relieving Cummins of responsibility to purchase any assets from the financial institution in event of default by the distributors.

Our licensing agreements with independent and partially owned distributors generally have a three-year term and are restricted to specified territories. Our distributors develop and maintain a network of dealers with which we have no direct relationship. The distributors are permitted to sell other, noncompetitive products only with our consent. We license all of our distributors to use our name and logo in connection with the sale and service of our products, with no right to assign or sublicense the marks, except to authorized dealers, without our consent. Products are sold to the distributors at standard domestic or international distributor net prices, as applicable. Net prices are wholesale prices we establish to permit our distributors an adequate margin on their sales. Subject to local laws, we can refuse to renew these agreements at will and we may terminate them upon 90-day notice for inadequate sales, change in principal ownership and certain other reasons. Distributors also have the right to terminate the agreements upon 60-day notice without cause, or 30-day notice for cause. Upon termination or failure to renew, we are required to purchase the distributor's current inventory, signage and special tools, and may, at our option purchase other assets of the distributor, but are under no obligation to do so.

Residual Value Guarantees

We have various residual value guarantees on equipment leased under operating leases. The total amount of these residual value guarantees at September 27, 2009, was \$8 million.

Other Guarantees and Commitments

In addition to the guarantees discussed above, from time to time we enter into other guarantee arrangements, including guarantees of non-U.S. distributor financing and other miscellaneous guarantees of third-party obligations. As of September 27, 2009, the maximum potential loss related to these other guarantees is \$74 million (\$72 million of which relates to the Beijing Foton agreement discussed below).

We have arrangements with certain suppliers that require us to purchase minimum volumes or be subject to monetary penalties. The penalty amounts are less than our purchase commitments and essentially allow the supplier to recover their tooling costs in most instances. As of September 27, 2009, if we were to stop purchasing from each of these suppliers, the amount of the penalty would be approximately \$82 million, of which \$68 million relates to a contract with an engine parts supplier that extends to 2013. This arrangement enables us to secure critical components. We do not currently anticipate paying any penalties under these contracts.

In July 2008, Beijing Foton Cummins Engine Company, a 50 percent owned entity accounted for under the equity method, entered into a line of credit agreement with a borrowing capacity of up to \$176 million (at current exchange rates). The line will be used primarily to fund equipment purchases for a new manufacturing plant. As a part of this transaction, we guaranteed 50 percent of any outstanding borrowings up to a maximum guarantee of \$88 million (at

current exchange rates). As of September 27, 2009, outstanding borrowings under this agreement were \$144 million and our guarantee was \$72 million (at current exchange rates). We recorded a liability for the fair value of this guarantee. The amount of the liability was less than \$1 million. The offset to this liability was an increase in our investment in the joint venture.

We had a standby commitment with Irwin Financial Corporation (Irwin) to purchase up to \$25 million of its common shares in connection with a potential rights offering being planned by Irwin. Our commitment was subject to the satisfaction of several conditions. On September 18, 2009, Irwin Union Bank and Trust Company, Columbus, Indiana, was placed into receivership by the Indiana Department of Financial Institutions and Irwin Union Bank, F.S.B., Louisville, Kentucky, was placed into receivership by the Office of Thrift Supervision. In light of these actions, Cummins terminated the Standby Purchase Agreement on September 21, 2009, and no further commitments to Irwin remain.

Indemnifications

Periodically, we enter into various contractual arrangements where we agree to indemnify a third-party against certain types of losses. Common types of indemnifications include:

- product liability and license, patent or trademark indemnifications,
- asset sale agreements where we agree to indemnify the purchaser against future environmental exposures related to the asset sold and
- any contractual agreement where we agree to indemnify the counter-party for losses suffered as a result of a misrepresentation in the contract.

We regularly evaluate the probability of having to incur costs associated with these indemnifications and accrue for expected losses that are probable. Because the indemnifications are not related to specified known liabilities and due to their uncertain nature, we are unable to estimate the maximum amount of the potential loss associated with these indemnifications.

Joint Venture Commitments

As of September 27, 2009, we have committed to invest \$8 million into existing joint ventures. It is expected that \$4 million will be funded in 2009.

NOTE 10. FAIR VALUE OF FINANCIAL INSTRUMENTS

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The majority of the assets and liabilities we carry at fair value are available-for-sale (AFS) securities and derivatives. AFS securities are derived from level 1 or level 2 inputs. The predominance of market inputs are actively quoted and can be validated through external sources, including brokers, market transactions and third-party pricing services.

The fair value measurement of derivatives results primarily from level 2 inputs. Many of our derivative contracts are valued utilizing publicly available pricing data of contracts with similar terms. In other cases, the contracts are valued using current spot market data adjusted for the appropriate current forward curves provided by external financial institutions. We participate in commodity swap contracts, currency forward contracts, and interest rate swaps. When material, we adjust the values of our derivative contracts for counter-party or our credit risk.

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The following table summarizes our financial instruments recorded at fair value in our *Condensed Consolidated Balance Sheets* at September 27, 2009:

In millions	Quoted prices in active markets for identical assets (Level 1)	Fair Value Measurements Using Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Available-for-sale securities	\$ 138	\$ 10	\$	\$ 148
Derivative assets		49		49
Derivative liabilities		(13)		(13)
Total	\$ 138	\$ 46	\$	\$ 184

Fair Value of Other Financial Instruments

Based on borrowing rates currently available to us for bank loans with similar terms and average maturities, considering our risk premium, the fair value of total debt, including current maturities, at September 27, 2009, was approximately \$628 million. The carrying value at that date was \$681 million. At December 31, 2008, the fair and carrying values of total debt, including current maturities, were \$567 million and \$698 million, respectively. The carrying values of all other receivables and liabilities approximated fair values.

NOTE 11. DERIVATIVES

We are exposed to financial risk resulting from volatility in foreign exchange rates, commodity prices and interest rates. This risk is closely monitored and managed through the use of financial derivative instruments including foreign currency forward contracts, commodity swap contracts and interest rate swaps. As stated in our internal policies and procedures, financial derivatives are used expressly for hedging purposes, and under no circumstances are they used for speculative purposes. When material, we adjust the value of our derivative contracts for counter-party or our credit risk. The results and status of our hedging transactions are reported to senior management on a monthly and quarterly basis.

Foreign Currency Exchange Rate Risk

Due to our international business presence, we are exposed to foreign currency exchange risks. We transact business in foreign currencies and, as a result, our income experiences some volatility related to movements in foreign currency exchange rates. To help manage our exposure to exchange rate volatility, we use foreign exchange forward contracts on a regular basis to hedge forecasted intercompany and third-party sales and purchases denominated in non-functional currencies. Our internal policy allows for managing anticipated foreign currency cash flows for up to one year. These foreign currency forward contracts are designated and qualify as foreign currency cash flow hedges under GAAP. The effective portion of the unrealized gain or loss on the forward contract is deferred and reported as a component of Accumulated other comprehensive loss (AOCL). When the hedged forecasted transaction (sale or purchase) occurs, the unrealized gain or loss is reclassified into income in the same line item associated with the hedged transaction in the same period or periods during which the hedged transaction affects income. The ineffective portion of the hedge, unrealized gain or loss, if any, is recognized in current income during the period of change. As of September 27, 2009, we expect to reclassify an unrealized net gain of \$1 million from AOCL to income over the next year. For the nine month periods ended September 27, 2009, and September 28, 2008, there were no circumstances that would have resulted in the discontinuance of a foreign currency cash flow hedge.

To minimize the income volatility resulting from the remeasurement of net monetary assets and payables denominated in a currency other than the functional currency, we enter into foreign currency forward contracts, which are considered economic hedges. The objective is to offset the gain or loss from remeasurement with the gain or loss from the fair market valuation of the forward contract. These derivative instruments are not designated as hedges under GAAP.

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The table below summarizes our outstanding foreign currency forward contracts. The currencies in this table represent 90% of the notional amounts of contracts outstanding as of September 27, 2009.

In millions Currency	Currency Denomination September 27, 2009
United States Dollar (USD)	21
British Pound Sterling (GBP)	93
Euro (EUR)	8
Singapore Dollar (SGD)	26
Indian Rupee (INR)	550
Romanian Leu (RON)	40
Chinese Renminbi (CNY)	35

Commodity Price Risk

We are exposed to fluctuations in commodity prices due to contractual agreements with component suppliers. In order to protect ourselves against future price volatility and, consequently, fluctuations in gross margins, we periodically enter into commodity swap contracts with designated banks to fix the cost of certain raw material purchases with the objective of minimizing changes in inventory cost due to market price fluctuations. The swap contracts are derivative contracts that are designated as cash flow hedges under GAAP. The effective portion of the unrealized gain or loss is deferred and reported as a component of AOCL. When the hedged forecasted transaction (purchase) occurs, the unrealized gain or loss is reclassified into income in the same line item associated with the hedged transaction in the same period or periods during which the hedged transaction affects income. The ineffective portion of the hedge, if any, is recognized in current income in the period in which the ineffectiveness occurs. As of September 27, 2009, we expect to reclassify an unrealized net loss of \$4 million from AOCL to income over the next year. For the nine month period ended September 27, 2009, we discontinued hedge accounting on certain contracts where the forecasted transactions were no longer probable. The amount reclassified to income as a result of this action was a loss of \$4 million.

Our internal policy allows for managing these cash flow hedges for up to three years. The following table summarizes our outstanding commodity swap contracts that were entered into to hedge the cost of certain raw material purchases:

Dollars in millions Commodity	September 27, 2009	
	Notional Amount	Quantity
Copper	\$ 100	14,670 metric tons(1)
Platinum	17	19,468 troy ounces(2)
Palladium	1	3,822 troy ounces(2)

(1) A metric ton is a measurement of mass equal to 1,000 kilograms.

(2) A troy ounce is a measurement of mass equal to approximately 31 grams.

Interest Rate Risk

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We are exposed to market risk from fluctuations in interest rates. We manage our exposure to interest rate fluctuations through the use of interest rate swaps. The objective of the swaps is to more effectively balance our borrowing costs and interest rate risk.

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In November 2005, we entered into an interest rate swap to effectively convert our \$250 million debt, due in 2028, from a fixed rate of 7.125% to a floating rate based on a LIBOR spread. The terms of the swap mirror those of the debt, with interest paid semi-annually. This swap qualifies as a fair value hedge under GAAP. The gain or loss on this derivative instrument as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in current income as Interest expense. These gains and losses for the three and nine month periods ended September 27, 2009, were as follows:

In millions Income Statement Classification	September 27, 2009			
	Three months ended		Nine months ended	
	Gain/(Loss) on Swaps	Gain/(Loss) on Borrowings	Gain/(Loss) on Swaps	Gain/(Loss) on Borrowings
Interest expense	\$ 6	\$ (6)	\$ (40)	\$ 40

Cash Flow Hedging

The tables below summarize the effect on our *Condensed Consolidated Statements of Income* for derivative instruments classified as cash flow hedges for the three and nine month interim reporting periods presented below. The tables do not include amounts related to ineffectiveness as it was not material for the periods presented.

In millions Derivatives in Cash Flow Hedging Relationships	Three months ended September 27, 2009			Location of Gain/(Loss) Reclassified into Income (Effective Portion)
	Amount of Gain/(Loss) Recognized in AOCL on Derivative (Effective Portion)		Amount of Gain/(Loss) Reclassified from AOCL into Income (Effective Portion)	
Foreign currency forward contracts	\$ (1)	\$	5	Sales
Commodity swap contracts	14		(5)	Cost of sales
Total	\$ 13	\$		

In millions Derivatives in Cash Flow Hedging Relationships	Nine months ended September 27, 2009			Location of Gain/(Loss) Reclassified into Income (Effective Portion)
	Amount of Gain/(Loss) Recognized in AOCL on Derivative (Effective Portion)		Amount of Gain/(Loss) Reclassified from AOCL into Income (Effective Portion)	
Foreign currency forward contracts	\$ 8	\$	(3)	Sales
Commodity swap contracts	43		(22)	Cost of sales
Total	\$ 51	\$	(25)	

Derivatives Not Designated as Hedging Instruments

The following table summarizes the effect on our *Condensed Consolidated Statements of Income* for derivative instruments that are not classified as hedges for the three and nine month interim reporting periods ended September 27, 2009.

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In millions	Location of Gain/(Loss) Recognized in Income on Derivatives	Amount of Gain/(Loss) Recognized in Income on Derivatives	
		September 27, 2009	
Derivatives Not Designated as Hedging Instruments		Three months ended	Nine months ended
Foreign currency forward contracts	Cost of sales	\$ 2	\$ 2
Foreign currency forward contracts	Other (expense) income, net	(8)	10

Fair Value Amount and Location of Derivative Instruments

The following tables summarize the location and fair value of derivative instruments on our *Condensed Consolidated Balance Sheets*:

In millions	Asset Derivatives	
	Fair Value September 27, 2009	Balance Sheet Location
Derivatives Designated as Hedging Instruments		
Foreign currency forward contracts	\$ 2	Prepaid expenses and other current assets
Commodity swap contracts	5	Prepaid expenses and other current assets
Commodity swap contracts	3	Other assets
Interest rate contract	39	Other assets
Total Derivatives Designated as Hedging Instruments	\$ 49	
Total asset derivatives	\$ 49	

In millions	Liability Derivatives	
	Fair Value September 27, 2009	Balance Sheet Location
Derivatives Designated as Hedging Instruments		
Commodity swap contracts	\$ 10	Other accrued expenses
Commodity swap contracts	2	Other liabilities and deferred revenue
Total Derivatives Designated as Hedging Instruments	\$ 12	
Derivatives Not Designated as Hedging Instruments		
Foreign currency forward contracts	\$ 1	Other accrued expenses
Total Derivatives Not Designated as Hedging Instruments	\$ 1	
Total liability derivatives	\$ 13	

NOTE 12. LEASE AMENDMENT AND EXTENSION

During 2001, we entered into a sale-leaseback transaction with a financial institution with regard to certain heavy-duty engine manufacturing equipment. The lease was classified as an operating lease with a lease term of 11.5 years, expiring June 28, 2013. The financial institution created a grantor trust to act as the lessor in the arrangement. The financial institution owns all of the equity in the trust. The grantor trust has no assets other than the equipment and its rights to the lease agreement with us. On the initial sale, we received \$125 million from the financial institution which was financed with \$99 million of non-recourse debt and \$26 million of equity. Our obligations to the grantor trust consisted of the payments due under the lease and a \$9 million guarantee of the residual value of the equipment. In addition, we had a fixed price purchase option that was exercisable on January 14, 2009, for approximately \$35 million; however, we decided not to exercise this option.

In December 2003, the grantor trust which acts as the lessor in the sale and leaseback transaction described above was consolidated as a result of the adoption of new accounting standards for variable interest entities, due primarily to the existence of the residual value guarantee. As a result of the consolidation, the manufacturing equipment and the trust's obligations under its non-recourse debt arrangement was included in our *Condensed Consolidated Balance Sheets* as property, plant and equipment and long-term debt, respectively. The equity in the trust held by the financial institution was reported as noncontrolling interest. The non-recourse debt arrangement is more fully discussed in Note 10, DEBT to our annual *Consolidated Financial Statements* included in our 2008 Form 10-K. In addition, our *Condensed Consolidated Statements of Income* included interest expense on the lessor's debt

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obligations and depreciation expense on the manufacturing equipment rather than rent expense under the lease agreement. In April 2008, the trust made the final payment on the non-recourse debt.

In February 2009, we amended the lease agreement to extend the lease for an additional two years to June 2015, and we removed the residual value guarantee. As a result of removing the residual value guarantee, we are no longer required to consolidate the grantor trust and we deconsolidated the trust in the first quarter of 2009. With the deconsolidation, we are now required to account for the leasing arrangement with the trust which qualifies as a capital lease. The deconsolidation of the trust had minimal impact on our *Condensed Consolidated Financial Statements* as the present value of the minimum lease payments (including the extension) approximated the amount that was reported as noncontrolling interest as of the date of the amendment. The reduction in noncontrolling interests and increase in our capital lease liabilities was \$35 million.

The future lease payments required under the amended lease are as follows:

In millions Due date	Payment amount
2009	\$ 1
2010	
2011	
2012	12
2013	10
Thereafter	18

The lease agreement includes certain default provisions requiring us to make timely rent payments, maintain, service, repair and insure the equipment and maintain minimum debt ratings for our long-term senior unsecured debt obligations.

NOTE 13. COMPREHENSIVE INCOME

The tables below represent a reconciliation of our net income to comprehensive income for the three and nine month periods ended September 27, 2009, and September 28, 2008.

In millions	Three months ended September 27, 2009			Three months ended September 28, 2008		
	Attributable to Cummins Inc.	Attributable to Noncontrolling Interests	Total Consolidated	Attributable to Cummins Inc.	Attributable to Noncontrolling Interests	Total Consolidated
Net income	\$ 95	\$ 15	\$ 110	\$ 229	\$ 18	\$ 247
Other comprehensive income (loss), net of tax						
Unrealized gain on marketable securities				1	1	2
Unrealized (loss) gain on derivatives	21		21	(25)		(25)
Foreign currency translation adjustments	(5)	3	(2)	(99)	(14)	(113)

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Change in pensions and other postretirement defined benefit plans	53		53		5		5
Total other comprehensive income (loss)	69	3	72	(118)	(13)	(131)	
Total comprehensive income	\$ 164	\$ 18	\$ 182	\$ 111	\$ 5	\$ 116	

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In millions	Nine months ended September 27, 2009			Nine months ended September 28, 2008		
	Attributable to Cummins Inc.	Attributable to Noncontrolling Interests	Total Consolidated	Attributable to Cummins Inc.	Attributable to Noncontrolling Interests	Total Consolidated
Net income	\$ 158	\$ 36	\$ 194	\$ 712	\$ 47	\$ 759
Other comprehensive income (loss), net of tax						
Unrealized loss on marketable securities				(1)	(1)	(2)
Unrealized gain (loss) on derivatives	65		65	(7)		(7)
Foreign currency translation adjustments	82	9	91	(105)	(25)	(130)
Change in pensions and other postretirement defined benefit plans	57		57	17		17
Total other comprehensive income (loss)	204	9	213	(96)	(26)	(122)
Total comprehensive income	\$ 362	\$ 45	\$ 407	\$ 616	\$ 21	\$ 637

NOTE 14. OPERATING SEGMENTS

Our reportable operating segments consist of the following: Engine, Power Generation, Components and Distribution. This reporting structure is organized according to the products and markets each segment serves. We use segment EBIT (defined as earnings or loss before interest expense, income taxes and noncontrolling interests) as the primary basis for the chief operating decision-maker to evaluate the performance of each operating segment.

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A summary of operating results by segment for the three and nine month periods is shown below:

In millions	Engine	Power Generation	Components	Distribution	Non-segment items(1)	Total
Three months ended September 27, 2009						
External sales	\$ 1,270	\$ 444	\$ 395	\$ 421	\$	\$ 2,530
Intersegment sales	169	105	196	1	(471)	
Total sales	1,439	549	591	422	(471)	2,530
Depreciation and amortization(2)	49	13	18	5		85
Research, development and engineering expense	59	9	22			90
Equity, royalty and interest income from investees	16	5	4	32		57
Restructuring and other charges					22	22
Interest income	1		1			2
Segment EBIT	61	23	31	55	(15)	155
Three months ended September 28, 2008						
External sales	\$ 1,927	\$ 653	\$ 535	\$ 578	\$	\$ 3,693
Intersegment sales	352	235	266	3	(856)	
Total sales	2,279	888	801	581	(856)	3,693
Depreciation and amortization(2)	43	9	16	6		74
Research, development and engineering expense	75	11	27			113
Equity, royalty and interest income from investees	26	6	3	31		66
Interest income	2	1	1			4
Segment EBIT	160	108	61	61	(10)	380
Nine months ended September 27, 2009						
External sales	\$ 3,608	\$ 1,402	\$ 1,096	\$ 1,294	\$	\$ 7,400
Intersegment sales	629	414	527	4	(1,574)	
Total sales	4,237	1,816	1,623	1,298	(1,574)	7,400
Depreciation and amortization(2)	135	35	53	14		237
Research, development and engineering expense	168	25	61			254
Equity, royalty and interest income from investees	30	16	9	92		147
Restructuring and other charges					95	95
Interest income	2	1	1	1		5
Segment EBIT	41	133	22	168	(72)	292
Nine months ended September 28, 2008						
External sales	\$ 5,842	\$ 1,926	\$ 1,686	\$ 1,600	\$	\$ 11,054
Intersegment sales	1,032	687	790	7	(2,516)	
Total sales	6,874	2,613	2,476	1,607	(2,516)	11,054
Depreciation and amortization(2)	133	31	49	17		230
Research, development and engineering expense	215	31	74			320
Equity, royalty and interest income from investees	91	17	10	84		202
Interest income	7	3	3	1		14

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Segment EBIT	575	301	175	178	(65)	1,164
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(1) Includes intersegment sales and profit in inventory eliminations and unallocated corporate expenses. For the three and nine months ended September 27, 2009, unallocated corporate expenses include \$22 million and \$95 million of restructuring and other charges and an \$8 million and \$5 million gain related to flood damage expenses, respectively. For the three and nine months ended September 28, 2008, unallocated corporate expenses included losses of zero and \$6 million related to flood damages.

(2) Depreciation and amortization as shown on a segment basis excludes the amortization of debt discount that is included in the *Condensed Consolidated Statements of Income* as Interest expense.

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A reconciliation of our segment information to the corresponding amounts in the *Condensed Consolidated Statements of Income* is shown in the table below:

In millions	Three months ended		Nine months ended	
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
Segment EBIT	\$ 155	\$ 380	\$ 292	\$ 1,164
Less:				
Interest expense	9	10	26	33
Income before income taxes	\$ 146	\$ 370	\$ 266	\$ 1,131

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Cummins Inc. and its consolidated subsidiaries are hereinafter sometimes referred to as Cummins, the Company, the registrant, we, our, or

CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING INFORMATION

Certain parts of this quarterly report contain forward-looking statements that are based on current expectations, estimates and projections about the industries in which we operate and management's beliefs and assumptions. Forward-looking statements are generally accompanied by words, such as anticipates, expects, forecasts, intends, plans, believes, seeks, estimates or similar expressions. These statements are not guaranteed and involve certain risks, uncertainties and assumptions, which we refer to as future factors, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. Future factors that could cause our results to differ materially from the results discussed in such forward-looking statements are discussed below. We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. Future factors that could affect the outcome of forward-looking statements include the following:

- price and product competition by foreign and domestic competitors, including new entrants;
- rapid technological developments of diesel engines;
- the ability to continue to introduce competitive new products in a timely, cost-effective manner;
- the sales mix of products;
- the continued achievement of lower costs and expenses;
- domestic and foreign governmental and public policy changes, including environmental regulations;
- protection and validity of patent and other intellectual property rights;
- reliance on large customers;

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- technological, implementation and cost/financial risks in increasing use of large, multi-year contracts;
- the cyclical nature of some of our markets;
- the outcome of pending and future litigation and governmental proceedings;
- continued availability of financing, financial instruments and financial resources in the amounts, at the times and on the terms required to support our future business;
- the overall stability of global economic markets and conditions; and
- other risk factors described in Part II of this report under the caption Risk Factors Relating to Our Business.

In addition, such statements could be affected by general industry and market conditions and growth rates, general domestic and international economic conditions, including the price of crude oil (diesel fuel), interest rate and currency exchange rate fluctuations, commodity prices and other future factors.

ORGANIZATION OF INFORMATION

The following Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) was prepared to provide the reader with a view and perspective of our business through the eyes of management and should be read in conjunction with our *Consolidated Financial Statements* and related *Notes to Consolidated Financial Statements* in the Financial Statements section of our 2008 Form 10-K. Our MD&A is presented in the following sections:

- Executive Summary and Financial Highlights
- Results of Operations
- Restructuring and Other Charges
- Outlook
- Operating Segment Results
- Liquidity and Capital Resources
- Off Balance Sheet Financing
- Application of Critical Accounting Estimates
- Recently Adopted and Recently Issued Accounting Pronouncements

EXECUTIVE SUMMARY AND FINANCIAL HIGHLIGHTS

We are a leading global power provider that designs, manufactures, distributes and services diesel and natural gas engines, electric power generation systems and engine-related component products, including filtration and exhaust aftertreatment, turbochargers, fuel systems, controls and air handling systems. We sell our products to Original Equipment Manufacturers (OEMs), distributors and other customers worldwide. We have long-standing relationships with many of the leading manufacturers in the markets we serve, including PACCAR Inc., International Truck and Engine Corporation (Navistar International Corporation), Chrysler Group, LLC (Chrysler), Volvo AB, Daimler Trucks North America, Ford Motor Company, Case New Holland, Komatsu, and Volkswagen. We serve our customers through a network of more than 500 company-owned and independent distributor locations and approximately 5,200 dealer locations in more than 190 countries and territories.

Our reportable operating segments consist of the following: Engine, Power Generation, Components and Distribution. This reporting structure is organized according to the products and markets each segment serves. This type of reporting structure allows management to focus its efforts on providing enhanced service to a wide range of customers. The Engine segment produces engines and parts for sale to customers in on-highway and various industrial markets. The engines are used in trucks of all sizes, buses and recreational vehicles, as well as various industrial applications including construction, mining, agriculture, marine, oil and gas, rail and military. The Power Generation segment is an integrated provider of power systems which sells engines, generator sets and alternators. The Components segment includes sales of filtration products, exhaust aftertreatment systems, turbochargers and fuel systems. The Distribution segment includes wholly-owned and partially-owned distributorships engaged in wholesaling engines, generator sets, and service parts, as well as performing service and repair activities on our products and maintaining relationships with various OEMs throughout the world.

Our financial performance depends, in large part, on varying conditions in the markets we serve, particularly the on-highway, construction and general industrial markets. Demand in these markets tends to fluctuate in response to overall economic conditions and is particularly sensitive to changes in interest rate levels and our customers' access to credit. Our sales may also be impacted by OEM inventory levels and production schedules and stoppages. Economic downturns in markets we serve generally result in reductions in sales and could impact pricing of our products. As a worldwide business, our operations are also affected by political, economic and regulatory matters, including environmental and emissions standards, in the countries we serve. At the same time, our geographic diversity and broad product and service offerings have helped limit the impact of any one industry or customer and the economy of any single country on our consolidated results.

However, as was the case in the first half of 2009, the widespread nature of the current global economic downturn continues to create immediate challenges for most of our businesses and the markets in which they operate. Demand in most of our markets around the world appears to have reached bottom and we are seeing signs that markets are stabilizing at these levels. We are also seeing improvement in emerging markets including China, India and Brazil. In North America, we are seeing improvement in demand in the second half of the year relating to higher engine sales prior to the 2010 emissions standards change. This increase in demand is consistent with prior emissions standard implementations. We expect demand to remain weak in most of our other markets throughout the remainder of 2009. We took actions to align our businesses with reduced customer demand in the first nine months of 2009. These actions included global workforce reductions and closing certain manufacturing operations. Costs associated with these restructuring actions, in conjunction with the significantly reduced demand, negatively impacted our operating results for the three and nine months ended September 27, 2009. Should our performance for the remainder of the year differ adversely from our projections, we could be required to take additional actions as local conditions require.

While we expect global demand for our products to be weak for the remainder of the year (excluding the North American on-highway markets), certain emerging markets are expected to improve in the fourth quarter of the year. The actions that were initiated in the fourth quarter of 2008 and the first nine months of 2009 have and will continue to enable us to navigate through the downturn and position us to respond to market conditions when and where they improve. Our short term priorities remain:

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- to align costs and capacity with the real demand for our products, so that we maintain a solid profit through the downturn;

- to manage the business in such a way that generates positive cash flow; and
- to continue to invest in critical technologies and products for 2010 and beyond.

Net income attributable to Cummins was \$95 million, or \$0.48 per diluted share, on sales of \$2.5 billion for the three month interim reporting period ended September 27, 2009, versus the comparable prior year period with net income attributable to Cummins of \$229 million, or \$1.17 per diluted share, on sales of \$3.7 billion. The decrease in income was driven by a 31 percent decrease in net sales and a 39 percent decrease in gross margin primarily due to significantly lower demand and volumes across most of our businesses. Restructuring and other charges in the third quarter of 2009 were \$22 million (\$15 million after-tax, or \$0.08 per diluted share).

Net income attributable to Cummins was \$158 million, or \$0.80 per diluted share, on sales of \$7.4 billion for the nine month interim reporting period ended September 27, 2009, versus the comparable prior year period with net income attributable to Cummins of \$712 million, or \$3.62 per diluted share, on sales of \$11.1 billion. The decrease in income was driven by a 33 percent decrease in net sales and a 42 percent decrease in gross margin, as we were impacted by lower demand across most of our businesses. Focused cost reduction efforts helped mitigate the impact of lower volumes. Restructuring and other charges in the first three quarters of 2009 were \$95 million (\$63 million after-tax, or \$0.32 per diluted share). For a detailed discussion of restructuring see Note 5, RESTRUCTURING AND OTHER CHARGES in the *Notes to the Condensed Consolidated Financial Statements*.

We continued to strengthen our balance sheet in a challenging environment. Cash, cash equivalents and marketable securities increased \$331 million from year end as we reduced inventories by 18 percent in the same period. We also reduced total debt by \$17 million compared to December 31, 2008.

RESULTS OF OPERATIONS

In millions (except per share amounts)	Three months ended		Favorable/		Nine months ended		Favorable/	
	September 27, 2009	September 28, 2008	(Unfavorable)		September 27, 2009	September 28, 2008	(Unfavorable)	
	2009	2008	Amount	Percent	2009	2008	Amount	Percent
Net sales	\$ 2,530	\$ 3,693	\$ (1,163)	(31)%	\$ 7,400	\$ 11,054	\$ (3,654)	(33)%
Cost of sales	2,027	2,873	846	29%	6,004	8,648	2,644	31%
Gross margin	503	820	(317)	(39)%	1,396	2,406	(1,010)	(42)%
Operating expenses and income								
Selling, general and administrative expenses	304	388	84	22%	891	1,109	218	20%
Research, development and engineering expenses	90	113	23	20%	254	320	66	21%
Equity, royalty and interest income from investees	57	66	(9)	(14)%	147	202	(55)	(27)%
Restructuring and other charges	22		(22)	NM	95		(95)	NM
Other operating income (expense), net	3	(2)	5	NM	(6)	(9)	3	33%
Operating income	147	383	(236)	(62)%	297	1,170	(873)	(75)%
Interest income	2	4	(2)	(50)%	5	14	(9)	(64)%

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Interest expense	9	10	1	10%	26	33	7	21%
Other income (expense), net	6	(7)	13	NM	(10)	(20)	10	50%
Income before income taxes	146	370	(224)	(61)%	266	1,131	(865)	(76)%
Income tax expense	36	123	87	71%	72	372	300	81%
Net income	110	247	(137)	(55)%	194	759	(565)	(74)%
Less: net income attributable to noncontrolling interests	15	18	3	17%	36	47	11	23%
Net income attributable to Cummins Inc.	\$ 95	\$ 229	\$ (134)	(59)%	\$ 158	\$ 712	\$ (554)	(78)%
Diluted earnings per common share attributable to Cummins Inc.	\$ 0.48	\$ 1.17	\$ (0.69)	(59)%	\$ 0.80	\$ 3.62	\$ (2.82)	(78)%

Net Sales

Net sales for the three and nine month periods ended September 27, 2009, decreased in all segments versus the comparable periods in 2008, primarily due to decreased demand due to the global economic downturn.

A more detailed discussion of sales by segment is presented in the OPERATING SEGMENT RESULTS section.

Sales to international markets based on location of customers for the three and nine month periods ended September 27, 2009, were 54 percent of total net sales for both periods, compared with 61 percent and 60 percent of total net sales for the comparable periods in 2008.

A summary of net sales (dollar amount and percentage of total) by geographic territory follows:

In millions	Three months ended				Nine months ended			
	September 27, 2009		September 28, 2008		September 27, 2009		September 28, 2008	
United States	\$ 1,161	46%	\$ 1,447	39%	\$ 3,414	46%	\$ 4,471	40%
Asia/Australia	563	22%	799	22%	1,579	21%	2,339	21%
Europe/CIS(1)	323	13%	622	17%	1,071	15%	2,013	18%
Mexico/Latin America	261	10%	411	11%	645	9%	1,166	11%
Africa/Middle East	155	6%	242	6%	458	6%	633	6%
Canada	67	3%	172	5%	233	3%	432	4%
Total international	1,369	54%	2,246	61%	3,986	54%	6,583	60%
Total consolidated net sales	\$ 2,530	100%	\$ 3,693	100%	\$ 7,400	100%	\$ 11,054	100%

(1) The Commonwealth of Independent States (CIS) refers to a regional organization of former Soviet Republics.

Gross Margin

Significant drivers of the change in gross margins for the three and nine month periods ended September 27, 2009, versus the comparable periods ended September 28, 2008, were as follows:

In millions	Increase (Decrease) 2009 vs. 2008	
	Three months ended	Nine months ended
Volume/Mix	\$ (417)	\$ (1,151)
Currency	(9)	(26)
Warranty expense	(3)	(39)
Price	56	197
Production costs	38	68
Material costs	19	(59)

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Other		(1)		
Total	\$	(317)	\$	(1,010)

Gross margin decreased by \$317 million and \$1,010 million for the three and nine month periods ended September 27, 2009, versus the comparable periods in 2008, and decreased as a percentage of sales by 2.3 percentage points and 2.9 percentage points, respectively. For the three and nine months ended September 27, 2009, versus the comparable period in 2008, the decrease was led by lower volumes which were partially offset by improved pricing and decreased production costs. The decreases in volumes were due to lower sales resulting from the global economic downturn. The increased materials costs for the nine months ended were largely due to losses on hedged commodities which were partially offset by decreasing commodity costs. The provision for warranties issued as a percent of sales was 3.3 percent for both periods in 2009 compared to 2.7 percent and 2.9 percent in 2008 for the three and nine month periods, respectively.

A more detailed discussion of margin by segment is presented in the **OPERATING SEGMENT RESULTS** section.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to decreases of \$46 million and \$98 million in compensation and related expenses and decreases of \$20 million and \$71 million in discretionary spending, in order to conserve cash, respectively. Compensation and related expenses include salaries, fringe benefits and variable compensation. Variable compensation was reduced due to lower sales and income compared to the prior year period. Selling, general and administrative expenses also decreased due to cost savings from restructuring actions. Overall, selling, general and administrative expenses as a percentage of sales increased to 12.0 percent for both periods in 2009 compared to 10.5 percent and 10.0 percent in 2008 for the three and nine month periods ended, respectively.

Research, Development and Engineering Expenses

Research, development and engineering expenses for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to a decrease in the number of engineering projects to conserve cash while focusing on the development of critical technologies and new products, decreased compensation and related expenses due to implemented severance programs and increased reimbursements for engineering projects. Compensation and related expenses include salaries, fringe benefits and variable compensation. Overall, research, development and engineering expenses as a percentage of sales increased to 3.6 percent and 3.4 percent in 2009 from 3.1 percent and 2.9 percent in 2008 for the three and nine month periods ended, respectively. Research activities continue to focus on development of new products to meet future environmental standards around the world and improvements to fuel economy performance.

Equity, Royalty and Interest Income From Investees

Equity, royalty and interest income from investees for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to the following:

In millions	Increase/(Decrease)	
	September 27, 2009 vs. September 28, 2008	
	Three months ended	Nine months ended
Dongfeng Cummins Engine Company, Ltd. (DCEC)	\$ (5)	\$ (32)
Cummins MerCruiser Diesel LLC (MerCruiser)	(1)	(10)
Chongqing Cummins Engine Company, Ltd. (CCEC)	(1)	5
Tata Cummins Ltd. (TCL)	2	(5)

These decreases for both periods were primarily due to lower demand as a result of the global economic conditions. For the nine months ended September 27, 2009, the effects of the global economic downturn were partially offset by the increase in income from CCEC due to a one-time tax benefit recorded in the second quarter of 2009.

Other Operating Income (Expense), net

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In millions	Three months ended		Nine months ended	
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
Other operating income (expense):				
Flood gain (loss)	\$ 8(1)	\$	\$ 5(1)	\$ (6)
Royalty income	2	2	6	9
Amortization of intangible assets	(1)	(4)	(5)	(9)
Gain (loss) on sale of fixed assets	(2)	2	(1)	5
Royalty expense	(2)	(2)	(7)	(6)
Other income (expense), net	(2)		(4)	(2)
Total other income (expense), net	\$ 3	\$ (2)	\$ (6)	\$ (9)

(1) The flood gain represents flood insurance proceeds received during the third quarter of 2009 which offset flood related expenses recognized in 2008 and 2009.

Interest Income

Interest income for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to lower interest rates in 2009 compared to 2008.

Interest Expense

Interest expense for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to declining short-term interest rates and lower debt.

Other Income (Expense), Net

In millions	Three months ended		Nine months ended	
	September 27, 2009	September 28, 2008	September 27, 2009	September 28, 2008
Other income (expense):				
Foreign currency gains (losses), net	\$ (1)	\$ (10)	\$ (18)	\$ (23)
Dividend income	1	2	3	4
Bank charges	(3)	(4)	(10)	(9)
Other, net	9	5	15	8
Total other income (expense), net	\$ 6	\$ (7)	\$ (10)	\$ (20)

Income Tax Expense

Our effective tax rate for the year is expected to approximate 27 percent, absent any additional discrete period activity. Our tax rate is generally less than the 35 percent U.S. income tax rate primarily due to lower tax rates on foreign income and research tax credits. The tax rates for the three and nine month periods ended September 27, 2009, were 25 percent and 27 percent, respectively. Our effective tax rate for both comparable prior year periods was 33 percent. The lower effective tax rates for both periods in 2009 compared to 2008 are primarily due to research tax credits, which were not included in the 2008 effective tax rates until the U.S. research credit was retroactively reinstated in the fourth quarter of 2008.

Noncontrolling Interests

Noncontrolling interests eliminate the income or loss attributable to non-Cummins ownership interests in our consolidated entities. Noncontrolling interests in income of consolidated subsidiaries for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to lower income at Cummins India Ltd., a publicly traded company at various exchanges

in India, reflecting the decline in demand as a result of the global economic downturn.

Net income and diluted earnings per share attributable to Cummins Inc.

Net income and diluted earnings per share attributable to Cummins Inc. for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to significantly lower volumes, restructuring charges and lower equity income. These decreases were partially offset by lower income tax expense, decreased selling, general and administrative expenses, and lower research, development and engineering expenses.

RESTRUCTURING AND OTHER CHARGES

2009 Restructuring Actions

In 2009, we executed restructuring actions in response to a reduction in orders in most of our U.S. and foreign markets due to the continuing deterioration in the global economy. We reduced our global workforce by approximately 1,000 professional employees. In addition, we took numerous employee actions at many of our manufacturing locations, including approximately 3,150 hourly employees, significant downsizing at numerous facilities and complete closure of several facilities and branch distributor locations. Employee termination and

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severance costs were recorded based on approved plans developed by the businesses and corporate management which specified positions to be eliminated, benefits to be paid under existing severance plans, union contracts or statutory requirements and the expected timetable for completion of the plan. Estimates of restructuring were made based on information available at the time charges were recorded. Due to the inherent uncertainty involved, actual amounts paid for such activities may differ from amounts initially recorded and we may need to revise previous estimates.

In response to closures and downsizing noted above, we incurred \$2 million of restructuring expenses for lease terminations and \$5 million of restructuring expenses for asset impairments. During 2009 we recorded a total pre-tax restructuring charge of \$83 million, comprising \$85 million of charges related to 2009 actions net of the \$2 million favorable change in estimate related to 2008 actions, in Restructuring and other charges in the *Condensed Consolidated Statements of Income*. The estimated completion date for the workforce reductions and the exit activities is March 2010. These restructuring actions included:

In millions	September 27, 2009	
	Three months ended	Nine months ended
Workforce reductions	\$ 11	\$ 79
Exit activities		7
Changes in estimate	(1)	(3)
Total restructuring charges	10	83
Curtailed loss	12	12
Total restructuring and other charges	\$ 22	\$ 95

In addition, as a result of the restructuring actions described above, we also recorded a \$12 million curtailment loss in the third quarter of 2009 in our pension and other postretirement plans. See Note 6 for additional detail.

The following table summarizes the balance of accrued restructuring charges by expense type and the changes in the accrued amounts for the applicable periods. The restructuring related accruals were recorded in Other accrued expenses in the *Condensed Consolidated Balance Sheets*.

In millions	Severance Costs		Exit Activities		Total
2009 Restructuring charges	\$ 79	\$ 7	\$ 86		
Cash payments for 2009 actions	(61)	(1)	(62)		
Noncash items		(5)	(5)		
Changes in estimates	(1)		(1)		
Translation	1		1		
Balance at September 27, 2009	\$ 18	\$ 1	\$ 19		

We do not include restructuring charges in our operating segment results. The pretax impact of allocating restructuring charges to the segment results would have been as follows:

In millions	September 27, 2009	
	Three months ended	Nine months ended
Engine	\$ 11	\$ 47
Power Generation	4	11
Components	8	34

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Distribution		(1)		3
Total restructuring charges	\$	22	\$	95

If the restructuring actions are successfully implemented, we expect the annualized savings from the professional actions to be approximately \$50 million. Our charge related to the professional actions was approximately \$30million. Approximately 40 percent of the savings from the restructuring actions will be realized in cost of sales, 45 percent in selling, general and administrative expenses, and 15 percent in research, development and engineering expenses. We expect all of the pretax charge, except for asset impairment and curtailment amounts, to be paid in cash which will be funded with cash generated from operations.

2008 Restructuring Actions

In 2008 we executed restructuring actions in response to the continued deterioration in our U.S. businesses and most key markets around the world in the second half of 2008, as well as a reduction in orders in most U.S. and foreign markets for 2009. In 2008 we announced reductions of our global workforce by approximately 650 professional employees. In addition, we took numerous employee actions at many of our manufacturing locations, including approximately 800 hourly employees. Total workforce reductions as of September 27, 2009, were substantially completed.

The charges recorded during the year ended December 31, 2008, included severance costs related to both voluntary and involuntary terminations. During 2008, we incurred a pretax charge related to the professional and hourly restructuring initiatives of \$37 million. The following table summarizes the balance of accrued restructuring charges and the changes in the accrued amounts for the applicable periods. The restructuring related accruals were recorded in Other accrued expenses in the *Condensed Consolidated Balance Sheets*.

In millions	Severance Costs	
Balance at December 31, 2008	\$	34
Cash payments for 2008 actions		(30)
Change in estimate		(2)
Balance at September 27, 2009	\$	2

There were no material changes to the estimated savings, or periods under which we expect to recognize the savings, for the 2008 actions.

OUTLOOK*Near-Term:*

Many of the markets we serve have slowed significantly as a result of the credit crisis and the current global economic environment, thus we expect full year 2009 sales will be down significantly from 2008 levels. Demand in most of our markets around the world appears to have reached bottom and we are seeing signs that markets are stabilizing at these levels. We are also seeing improvement in emerging markets including China, India and Brazil. Consistent with prior emissions standards implementation, the North American on-highway markets are experiencing increased demand prior to the implementation of the Environmental Protection Agency's 2010 emissions standards. Based on our prior experience we also expect engine sales to on-highway OEM customers to be weaker than current levels in the first half of 2010. In most of our other markets we expect demand to remain stable with current levels through the remainder of 2009 and into early 2010.

Our operating results in the fourth quarter of 2009 will depend on how the current global economic recession impacts the markets we serve. In response to anticipated market conditions we initiated voluntary and involuntary separation actions in December of 2008 and the first nine months of 2009. We also initiated certain exit activities during the first nine months of 2009. We expect to continue to focus on cost reductions and scaling production to meet current demand. If uncertainties in the credit and capital markets continue, the overall impact on our customers as well as end user demand for our products could have a significant adverse impact on our near-term results. Although demand appears to have reached bottom, in light of current economic conditions, if demand declines further, it is reasonably possible that we may be required to take additional restructuring actions and incur additional costs as we decrease production. These costs could have a material impact on our results of

operations and financial position. At this time we cannot estimate these potential charges.

Long-Term:

While there is uncertainty in the near-term market as a result of the current economic conditions, we are confident that opportunities for long-term growth and profitability will continue in the future.

OPERATING SEGMENT RESULTS

Our operating segments consist of the following: Engine, Power Generation, Components and Distribution. This reporting structure is organized according to the products and markets each segment serves. We use segment EBIT (defined as earnings or loss before interest expense, income taxes and noncontrolling interests) as the primary basis for the chief operating decision-maker to evaluate the performance of each operating segment.

Following is a discussion of operating results for each of our business segments.

Engine Segment Results

Financial data for the Engine segment was as follows:

In millions	Three months ended		Favorable/		Nine months ended		Favorable/	
	September 27, 2009	September 28, 2008	(Unfavorable) Amount	Percent	September 27, 2009	September 28, 2008	(Unfavorable) Amount	Percent
External sales	\$ 1,270	\$ 1,927	\$ (657)	(34)%	\$ 3,608	\$ 5,842	\$ (2,234)	(38)%
Intersegment sales	169	352	(183)	(52)%	629	1,032	(403)	(39)%
Total sales	1,439	2,279	(840)	(37)%	4,237	6,874	(2,637)	(38)%
Depreciation and amortization	49	43	(6)	(14)%	135	133	(2)	(2)%
Research, development and engineering expenses	59	75	16	21%	168	215	47	22%
Equity, royalty and interest income from investees	16	26	(10)	(38)%	30	91	(61)	(67)%
Interest income	1	2	(1)	(50)%	2	7	(5)	(71)%
Segment EBIT	61	160	(99)	(62)%	41	575	(534)	(93)%
Segment EBIT as a percentage of total sales	4.2%	7.0%	(2.8) percentage points		1.0%	8.4%	(7.4) percentage points	

A summary and discussion of Engine segment net sales by market follows:

In millions	Three months ended		Favorable/		Nine months ended		Favorable/	
	September 27, 2009	September 28, 2008	(Unfavorable) Amount	Percent	September 27, 2009	September 28, 2008	(Unfavorable) Amount	Percent
Heavy-duty truck	\$ 493	\$ 630	\$ (137)	(22)%	\$ 1,282	\$ 1,838	\$ (556)	(30)%
Medium-duty truck and bus	294	406	(112)	(28)%	763	1,225	(462)	(38)%
Light-duty automotive and RV	120	170	(50)	(29)%	370	650	(280)	(43)%
Total on-highway	907	1,206	(299)	(25)%	2,415	3,713	(1,298)	(35)%
Industrial	407	788	(381)	(48)%	1,314	2,325	(1,011)	(43)%
Stationary power	125	285	(160)	(56)%	508	836	(328)	(39)%
Total sales	\$ 1,439	\$ 2,279	\$ (840)	(37)%	\$ 4,237	\$ 6,874	\$ (2,637)	(38)%

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A summary of unit shipments by engine classification (including unit shipments to Power Generation) follows:

	Three months ended		Favorable/		Nine months ended		Favorable/	
	September 27, 2009	September 28, 2008	(Unfavorable)		September 27, 2009	September 28, 2008	(Unfavorable)	
			Amount	Percent			Amount	Percent
Midrange	58,800	102,400	(43,600)	(43)%	168,600	331,400	(162,800)	(49)%
Heavy-duty	20,600	29,400	(8,800)	(30)%	53,600	85,800	(32,200)	(38)%
High-horsepower	2,600	5,300	(2,700)	(51)%	9,700	15,400	(5,700)	(37)%
Total unit shipments	82,000	137,100	(55,100)	(40)%	231,900	432,600	(200,700)	(46)%

Sales

Engine segment sales for the three month period ended September 27, 2009, experienced significant deterioration across all major markets, versus the comparable period in 2008, as a result of the global economic downturn. The following are the primary drivers by market.

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- Industrial market sales decreased due to deterioration in units sold in the construction, marine and mining markets by 64 percent, 54 percent and 69 percent, respectively.
- Stationary power market sales declined due to decreased sales to the Power Generation segment as they utilized existing inventory to meet customer demand.
- Heavy-duty truck sales declined sharply as North American (includes the U.S and Canada and excludes Mexico) unit sales declined 21 percent and international units sold were down 43 percent. The decrease in heavy-duty sales was due to global truck fleets continuing to experience financial challenges due to a lack of freight and limited access to credit.
- Medium-duty truck sales decreased significantly due to a 34 percent decline in global truck units sold as a result of the global economic downturn.

Engine segment sales for the nine month period ended September 27, 2009, experienced significant deterioration across all major markets, versus the comparable period in 2008, as a result of the global economic downturn. The following are the primary drivers by market.

- Industrial market sales decreased due to deterioration in units sold in the construction, marine and mining markets by 70 percent, 50 percent and 51 percent, respectively.
- Heavy-duty truck sales declined sharply as North American unit sales declined 24 percent and international units sold were down 74 percent. The decrease in heavy-duty sales was due to global truck fleets continuing to experience financial challenges due to a lack of freight and limited access to credit. In addition, we experienced a decline in Mexican heavy-duty sales due to an increase in heavy-duty truck sales in the first six months of 2008 resulting from the increased activity ahead of Mexico's July 1, 2008, new emissions requirements, appreciation of the U.S. dollar and an influx of used trucks into the market from the U.S. and Canada permitted under a new law.
- Medium-duty truck sales decreased significantly due to a 41 percent decline in global truck units sold as a result of the global economic downturn.
- Stationary power market sales declined due to decreased sales to the Power Generation segment as they utilized existing inventory to meet customer demand.

Total on-highway-related sales for the three and nine month periods ended September 27, 2009, were 63 percent and 57 percent of total engine segment sales, compared to 53 percent and 54 percent for the comparable periods in 2008, respectively.

Segment EBIT

Engine segment EBIT for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to lower gross margin and equity, royalty and interest income from investees which were partially offset by decreased selling, general and administrative expenses and decreased research, development and engineering expenses. Changes in Engine segment EBIT and EBIT as a percentage of sales were as follows:

In millions	Three months ended September 27, 2009 vs. September 28, 2008 Favorable/(Unfavorable) Change			Nine months ended September 27, 2009 vs. September 28, 2008 Favorable/(Unfavorable) Change		
	Amount	Percent	Percentage point change as a percent of sales	Amount	Percent	Percentage point change as a percent of sales
Gross margin	\$ (143)	(37)%	(0.1)%	\$ (588)	(50)%	(3.1)%
Equity, royalty and interest (loss) income from investees	(10)	(38)%	%	(61)	(67)%	(0.6)%
Research, development and engineering	16	21%	(0.8)%	47	22%	(0.9)%
Selling, general and administrative	33	19%	(2.0)%	76	16%	(2.5)%

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The decrease in gross margin for the three month period ended September 27, 2009, was primarily due to lower engine volumes in all markets as a result of the global economic downturn, which was partially offset by price improvements and decreased material costs. Equity, royalty and interest income from investees decreased due to significantly lower demand at DCEC, ZAO Cummins Kama and Komatsu-Cummins Engine Company (KCEC). The decrease in selling, general and administrative expense and research, development and engineering expenses was primarily due to lower discretionary spending, decreased variable compensation and implementation of severance programs.

The decrease in gross margin for the nine month period ended September 27, 2009, was primarily due to lower engine volumes in all markets as a result of the global economic downturn, which was partially offset by price improvements. Equity, royalty and interest income from investees decreased due to significantly lower demand at DCEC, KCEC and Cummins MerCruiser Diesel Marine LLC. The decrease in selling, general and administrative expenses and research, development and engineering expenses was primarily due to lower discretionary spending, decreased variable compensation and higher recovery of engineering expenses.

Power Generation Segment Results

Financial data for the Power Generation segment was as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Nine months ended		Favorable/ (Unfavorable)	
	September 27, 2009	September 28, 2008	Amount	Percent	September 27, 2009	September 28, 2008	Amount	Percent
External sales	\$ 444	\$ 653	\$ (209)	(32)%	\$ 1,402	\$ 1,926	\$ (524)	(27)%
Intersegment sales	105	235	(130)	(55)%	414	687	(273)	(40)%
Total sales	549	888	(339)	(38)%	1,816	2,613	(797)	(31)%
Depreciation and amortization	13	9	(4)	(44)%	35	31	(4)	(13)%
Research, development and engineering expenses	9	11	2	18%	25	31	6	19%
Equity, royalty and interest income from investees	5	6	(1)	(17)%	16	17	(1)	(6)%
Interest income	1	1	(1)	(100)%	1	3	(2)	(67)%
Segment EBIT	23	108	(85)	(79)%	133	301	(168)	(56)%
Segment EBIT as a percentage of total sales	4.2%	12.2%	(8.0) percentage points		7.3%	11.5%	(4.2) percentage points	

In 2009, the Power Generation segment reorganized its reporting structure to include the following businesses: Commercial Products, Alternators, Commercial Projects, Power Electronics and Consumer. Sales for our Power Generation segment by business were as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Nine months ended		Favorable/ (Unfavorable)	
	September 27, 2009	September 28, 2008	Amount	Percent	September 27, 2009	September 28, 2008	Amount	Percent
Commercial Products	\$ 316	\$ 559	\$ (243)	(43)%	\$ 1,098	\$ 1,558	\$ (460)	(30)%
Alternator	124	174	(50)	(29)%	394	508	(114)	(22)%
Commercial Projects	39	63	(24)	(38)%	127	260	(133)	(51)%
Consumer	37	57	(20)	(35)%	100	194	(94)	(48)%
Power Electronics	33	35	(2)	(6)%	97	93	4	4%

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Total sales \$ **549** \$ 888 \$ (339) (38)% \$ **1,816** \$ 2,613 \$ (797) (31)%

A summary of unit shipments used in power generation equipment by engine classification follows:

	Three months ended		Favorable/ (Unfavorable)		Nine months ended		Favorable/ (Unfavorable)	
	September 27, 2009	September 28, 2008	Amount	Percent	September 27, 2009	September 28, 2008	Amount	Percent
Midrange	6,300	8,900	(2,600)	(29)%	16,000	25,100	(9,100)	(36)%
Heavy-duty	1,200	2,300	(1,100)	(48)%	3,400	6,300	(2,900)	(46)%
High-horsepower	1,500	2,800	(1,300)	(46)%	5,700	8,600	(2,900)	(34)%
Total unit shipments	9,000	14,000	(5,000)	(36)%	25,100	40,000	(14,900)	(37)%

Sales

Power Generation segment sales for the three month period ended September 27, 2009, decreased in most businesses, versus the comparable period in 2008, as the result of the global economic downturn. The following are the primary drivers by business.

- Commercial Products business sales decreased due to lower demand across most regions, especially in the Middle East, the U.K., North America, Latin America, India, South Pacific and Russia.
- Alternator business sales decreased due to lower demand in the commercial power markets noted above.
- Commercial Projects business sales decreased due to lower demand in most regions, especially in the Middle East and the U.K.
- Consumer business sales decreased primarily due to lower demand in the portables, marine and commercial mobile markets in North America.

Power Generation segment sales for the nine month period ended September 27, 2009, decreased in most businesses, versus the comparable period in 2008, as the result of the global economic downturn. The following are the primary drivers by business.

- Commercial Products business sales decreased due to lower demand across most regions, especially in the U.K., India, Latin America, North America, and the Middle East.
- Commercial Projects business sales decreased due to lower demand in most regions, especially in North America, Western Europe and the South Pacific.
- Alternator business sales decreased due to lower demand in the commercial power markets noted above.
- Consumer business sales decreased primarily due to lower demand in the recreational vehicle and marine markets in North America.

Segment EBIT

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Power Generation segment EBIT for the three and nine month periods ended September 27, 2009, decreased versus the comparable periods in 2008, primarily due to decreased gross margin partially offset by lower selling, general and administrative expenses. Changes in Power Generation segment EBIT and EBIT as a percentage of sales were as follows:

In millions	Three month period September 27, 2009 vs. September 28, 2008 Favorable/(Unfavorable) Change			Nine month period September 27, 2009 vs. September 28, 2008 Favorable/(Unfavorable) Change		
	Amount	Percent	Percentage point change as a percent of sales	Amount	Percent	Percentage point change as a percent of sales
	Gross margin	\$ (97)	(55)%	(5.3)%	\$ (209)	(41)%
Selling, general and administrative	17	25%	(1.6)%	52	25%	(0.6)%
Research, development and engineering	2	18%	(0.4)%	6	19%	(0.2)%

The decrease in gross margin for the three month period ended September 27, 2009, was primarily due to lower volumes, unfavorable sales mix and increased material and commodity costs, which was partially offset by improved pricing and favorable foreign currency translation. The decrease in selling, general and administrative expenses was primarily due to decreased discretionary spending, lower variable compensation costs, implementation of severance programs and favorable foreign currency translation.

The decrease in gross margin for the nine month period ended September 27, 2009, was primarily due to lower volumes, unfavorable sales mix, increased material and commodity costs, which was partially offset by improved pricing and favorable foreign currency translation. The decrease in selling, general and administrative expenses was primarily due to favorable foreign currency translation, decreased discretionary spending, lower variable compensation costs and implementation of severance programs.

Components Segment Results

Financial data for the Components segment was as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Nine months ended		Favorable/ (Unfavorable)	
	September 27, 2009	September 28, 2008	Amount	Percent	September 27, 2009	September 28, 2008	Amount	Percent
External sales	\$ 395	\$ 535	\$ (140)	(26)%	\$ 1,096	\$ 1,686	\$ (590)	(35)%
Intersegment sales	196	266	(70)	(26)%	527	790	(263)	(33)%
Total sales	591	801						