CUMMINS INC
Form 10-K
February 20, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended December 31, 2012

Commission File Number 1-4949

CUMMINS INC.

Indiana	**35-0257090**
(State of Incorporation)	(IRS Employer Identification No.)

500 Jackson Street
Box 3005
Columbus, Indiana 47202-3005
(Address of principal executive offices)

Telephone (812) 377-5000
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Common Stock, $2.50 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None.**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ý No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No ý

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 ý No o

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 (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

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

The aggregate market value of the voting stock held by non-affiliates was approximately $18.5 billion at July 1, 2012. This value includes all shares of the registrant's common stock, except for treasury shares.

As of February 1, 2013, there were 189,844,829 shares outstanding of $2.50 par value common stock.

Documents Incorporated by Reference

Portions of the registrant's definitive Proxy Statement for its 2013 annual meeting of shareholders, which will be filed with the Securities and Exchange Commission on Schedule 14A within 120 days after the end of 2012, will be incorporated by reference in Part III of this Form 10-K to the extent indicated therein upon such filing.

Website Access to Company's Reports

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

CUMMINS INC. AND SUBSIDIARIES
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Cummins Inc. and its consolidated subsidiaries are hereinafter sometimes referred to as "Cummins," "we," "our," or "us."

CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING INFORMATION

Certain parts of this annual report contain forward-looking statements intended to qualify for the safe harbors from liability established by the Private Securities Litigation Reform Act of 1995. Forward-looking statements include those 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," "could," "should," or words of similar meaning. These statements are not guarantees of future performance 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. Some future factors that could cause our results to differ materially from the results discussed in such forward-looking statements are discussed below and shareholders, potential investors and other readers are urged to consider these future factors carefully in evaluating forward-looking statements. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. Some of the future factors that could affect the outcome of forward-looking statements include the following:

- a sustained slowdown or significant downturn in our markets;
- a slowdown in infrastructure development;
- unpredictability in the adoption, implementation and enforcement of emission standards around the world;
- the actions of, and income from, joint ventures and other investees that we do not directly control;
- changes in the engine outsourcing practices of significant customers;
- a downturn in the North American truck industry or financial distress of a major truck customer;
- a major customer experiencing financial distress;
- any significant problems in our new engine platforms;
- currency exchange rate changes;
- supply shortages and supplier financial risk, particularly from any of our single-sourced suppliers;
- variability in material and commodity costs;
- product recalls;
- competitor pricing activity;

increasing competition, including increased global competition among our customers in emerging markets;

political, economic and other risks from operations in numerous countries;

changes in taxation;

the price and availability of energy;

global legal and ethical compliance costs and risks;

aligning our capacity and production with our demand;

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- product liability claims;
- the development of new technologies;
- obtaining customers for our new light-duty diesel engine platform and avoiding any related write-down in our investments in such platform;
- increasingly stringent environmental laws and regulations;
- the performance of our pension plan assets;
- labor relations;
- changes in accounting standards;
- our sales mix of products;
- protection and validity of our patent and other intellectual property rights;
- technological implementation and cost/financial risks in our 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; and
- other risk factors described in Item IA under the caption "Risk Factors."

Shareholders, potential investors and other readers are urged to consider these factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on such forward-looking statements. The forward-looking statements made herein are made only as of the date of this annual report and we undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise.

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PART I

ITEM 1. Business

OVERVIEW

Cummins Inc. was founded in 1919 as a corporation in Columbus, Indiana, as one of the first diesel engine manufacturers. We are a global power leader that designs, manufactures, distributes and services diesel and natural gas engines and engine-related component products, including filtration, aftertreatment, turbochargers, fuel systems, controls systems, air handling systems and electric power generation systems. We sell our products to original equipment manufacturers (OEMs), distributors and other customers worldwide. We serve our customers through a network of approximately 600 company-owned and independent distributor locations and approximately 6,500 dealer locations in more than 190 countries and territories.

OPERATING SEGMENTS

We have four complementary operating segments: Engine, Components, Power Generation and Distribution. These segments share technology, customers, strategic partners, brand recognition and our distribution network in order to compete more efficiently and effectively in their respective markets. In each of our operating segments, we compete worldwide with a number of other manufacturers and distributors that produce and sell similar products. Our products compete primarily on the basis of performance, fuel economy, speed of delivery, quality, customer support and price. Financial information about our operating segments, including geographic information, is incorporated by reference from Note 22, "OPERATING SEGMENTS," to our *Consolidated Financial Statements.*

Engine Segment

Engine segment sales and earnings before interest and taxes (EBIT) as a percentage of consolidated results were:

	Years ended December 31,		
	2012	**2011**	**2010**
Percent of consolidated net sales(1)	**50%**	52%	49%
Percent of consolidated EBIT(1)	**54%**	53%	48%

(1) Measured before intersegment eliminations

Our Engine segment manufactures and markets a broad range of diesel and natural gas powered engines under the Cummins brand name, as well as certain customer brand names, for the heavy- and medium-duty truck, bus, recreational vehicle (RV), light-duty automotive, agricultural, construction, mining, marine, oil and gas, rail and governmental equipment markets. We offer a wide variety of engine products including:

- Engines with a displacement range of 2.8 to 91 liters and horsepower ranging from 48 to 3,500;
- New parts and service, as well as remanufactured parts and engines, through our extensive distribution network and
- The newly developed light-duty diesel engine, which will be sold through the light construction vehicle, pick-up, bus and certain medium-duty truck markets.

Our Engine segment is organized by engine displacement size and serves these end-user markets:

Heavy-Duty Truck We manufacture diesel engines that range from 310 to 620 horsepower serving global heavy-duty truck customers worldwide.

Medium-Duty Truck and Bus We manufacture medium-duty diesel engines ranging from 150 to 400 horsepower serving medium-duty and inter-city delivery truck customers worldwide, with key markets including North America, Latin America, Europe and Mexico. We also provide diesel or natural gas engines for school buses, transit buses and shuttle buses worldwide, with key markets including North America, Europe, Latin America and Asia.

Light-Duty Automotive and RV We manufacture 320 to 385 horsepower diesel engines for Chrysler's heavy-duty chassis cab and pickup trucks and 300 to 600 horsepower diesel engines for Class A motor homes (RVs), primarily in North America.

Industrial We provide mid-range, heavy-duty and high-horsepower engines that range from 31 to 3,500 horsepower for a wide variety of equipment in the construction, agricultural, mining, rail, government, oil and gas, power generation and commercial and recreational marine applications throughout the world. Across these markets we have major customers in North America, Europe/Middle East/Africa (EMEA), China, Korea, Japan, Latin America, India, Russia, Southeast Asia, South Pacific and Mexico.

The principal customers of our heavy- and medium-duty truck engines include truck manufacturers such as PACCAR Inc (PACCAR), Daimler Trucks North America, Ford Motor Company, International Truck, MAN Latin America and Volvo. We sell our industrial engines to manufacturers of construction, agricultural and marine equipment, including Komatsu, Belaz, Hyundai, Hitachi and JLG. The principal customers of our light-duty on-highway engines are Chrysler and manufacturers of RVs.

In the markets served by our Engine segment, we compete with independent engine manufacturers as well as OEMs who manufacture engines for their own products. Our primary competitors in North America are International Truck and Engine Corporation (Engine Division), Detroit Diesel Corporation, Caterpillar Inc. (CAT), Volvo Powertrain, Ford Motor Company and Hino Power. Our primary competitors in international markets vary from country to country, with local manufacturers generally predominant in each geographic market. Other engine manufacturers in international markets include Weichai Power Co. Ltd., MAN Nutzfahrzeuge AG (MAN), Fiat Power Systems, GuangxiYuchai Group, GE Jenbacher, Tognum AG, CAT, Volvo, Yanmar Co., Ltd. and Deutz AG.

Components Segment

Components segment sales and EBIT as a percentage of consolidated results were:

	Years ended December 31,		
	2012	**2011**	**2010**
Percent of consolidated net sales(1)	**19%**	18%	19%
Percent of consolidated EBIT(1)	**18%**	18%	16%

(1) Measured before intersegment eliminations

Our Components segment supplies products which complement our Engine segment, including filtration products, turbochargers, aftertreatment systems and fuel systems for commercial diesel applications. We manufacture filtration systems for on- and off-highway heavy-duty and mid-range equipment, and we are a supplier of filtration products for industrial and passenger car applications. In addition, we develop aftertreatment systems and turbochargers to help our customers meet increasingly stringent emission standards and fuel systems which to date have primarily supplied our Engine segment and our joint venture partner Scania.

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Our Components segment is organized around the following businesses:

Emission solutions Our emission solutions business is a global leader in designing, manufacturing and integrating aftertreatment technology and solutions for the commercial on-and off-highway medium-duty, heavy-duty and high-horsepower engine markets. Our emission solutions business develops and produces various emission solutions, including custom engineering systems and integrated controls, oxidation catalysts, particulate filters, oxides of nitrogen (NOx) reduction systems such as selective catalytic reduction and NOx adsorbers and engineered components such as dosers and sensors. Our emissions solutions business primarily serves markets in North America, Europe, Brazil and China and serves both OEM and engine first fit and retrofit customers.

Turbo technologies Our turbo technologies business designs, manufactures and markets turbochargers for light-duty, mid-range, heavy-duty and high-horsepower diesel markets with manufacturing facilities in five countries and sales and distribution worldwide. Our turbo technologies business provides critical air handling technologies for engines, including variable geometry turbochargers, to meet challenging performance requirements and worldwide emission standards. Our turbo technologies business primarily serves markets in North America, Europe and Asia.

Filtration Our filtration business designs and manufactures filtration, coolant and chemical products. The filtration business offers over 7,000 products including air filters, fuel filters, fuel water separators, lube filters, hydraulic filters, coolant, diesel exhaust fluid, fuel additives and other filtration systems to OEMs, dealers/distributors and end users. Our filtration business supports a wide customer base in a diverse range of markets including on-highway, off-highway, oil and gas, agriculture, marine, industrial and light-duty automotive. We produce and sell globally recognized Fleetguard® branded products in over 160 countries including countries in North America, Europe, South America, Asia, Australia and Africa. Fleetguard products are available through thousands of distribution points worldwide.

Fuel systems Our fuel systems business designs and manufactures new and replacement fuel systems primarily for heavy-duty on-highway diesel engine applications and also remanufactures fuel systems and engine control modules. Scania and Komatsu are our fuel systems business' primary external customers. Scania is also our partner in two joint ventures within our fuel systems business. The Cummins-Scania High Pressure Injection, LLC joint venture currently manufactures fuel systems used internally and by Scania while the Cummins-Scania XPI joint venture currently produces advanced technology fuel systems for medium- and heavy-duty engines used internally and by Scania.

Customers of our Components segment generally include our Engine and Distribution segments, truck manufacturers and other OEMs, many of which are also customers of our Engine segment, such as PACCAR, Daimler, Volvo, Komatsu, Ford and other manufacturers that use our components in their product platforms.

Our Components segment competes with other manufacturers of filtration, turbochargers and fuel systems. Our primary competitors in these markets include Robert Bosch GmbH, Donaldson Company, Inc., Clarcor Inc., Mann+Hummel Group, Honeywell International, Borg-Warner, Tenneco Inc., Eberspacher Holding GmbH & Co. KG and Denso Corporation.

On July 18, 2012, we acquired the doser technology business assets from Hilite Germany GmbH (Hilite) in a $176 million cash transaction. The acquisition was accounted for as a business combination with the majority of the purchase price being allocated to goodwill and technology and customer related intangible assets. The results of the acquired entity for 2012 were included in the Components

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operating segment. See Note 2, "ACQUISITIONS AND DIVESTITURES," to our *Consolidated Financial Statements* for additional detail.

In the second quarter of 2011, we sold certain assets and liabilities of our exhaust business which manufactures exhaust products and select components for emission systems for a variety of applications not core to our other product offerings. This business was historically included in our Components segment. The sales price was $123 million. We recognized a gain on the sale of $68 million ($37 million after-tax), which included a goodwill allocation of $19 million. The gain was excluded from segment results as it was not considered in our evaluation of operating results for the year ended December 31, 2011.

During the fourth quarter of 2011, we sold certain assets and liabilities of our light-duty filtration business which manufactures light-duty automotive and industrial filtration solutions. The sales price was $90 million and included a note receivable from the buyer of approximately $1 million. There are no earnouts or other contingencies associated with the sales price. We recognized a gain on the sale of $53 million ($33 million after-tax), which included a goodwill allocation of $6 million. The gain was excluded from segment results as it was not considered in our evaluation of operating results for the year ended December 31, 2011.

Power Generation Segment

Power Generation segment sales and EBIT as a percentage of consolidated results were:

	Years ended December 31,		
	2012	**2011**	**2010**
Percent of consolidated net sales(1)	**15%**	16%	18%
Percent of consolidated EBIT(1)	**12%**	14%	18%

(1) Measured before intersegment eliminations

Our Power Generation segment designs and manufactures most of the components that make up power generation systems, including engines, controls, alternators, transfer switches and switchgear. This segment is a global provider of power generation systems, components and services for a diversified customer base, including the following:

- Standby power solutions for customers who rely on uninterrupted sources of power to meet the needs of their customers.
- Distributed generation power solutions for customers with less reliable electrical power infrastructures, typically in developing countries. In addition, our power solutions provide an alternative source of generating capacity located close to its point of use, which is purchased by utilities, independent power producers and large power customers for use as prime or peaking power.
- Mobile power solutions, which provide a secondary source of power (other than drivetrain power) for mobile applications.

In the first quarter of 2012, our Power Generation segment reorganized its reporting structure to include the following businesses:

- **Power products** Our power products business manufactures generators for commercial and consumer applications ranging from two kilowatts (kW) to one megawatt (MW) under the Cummins Power Generation and Cummins Onan brands.

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Power systems Our power systems business manufactures and sells diesel fuel-based generator sets over one MW, paralleling systems and transfer switches for critical protection and distributed generation applications. We also offer integrated systems that consist of generator sets, power transfer and paralleling switchgear for applications such as data centers, health care facilities and waste water treatment plants.

Generator technologies Our generator technologies business designs, manufactures, sells and services A/C generator/alternator products internally as well as to other generator set assemblers. Our products are sold under the Stamford, AVK and Markon brands and range in output from 0.6 kilovolt-amperes (kVA) to 30,000 kVA.

Power solutions Our power solutions business provides natural gas fuel-based turnkey solutions for distributed generation and energy management applications in the range of 300-2000 kW products. The business also serves the oil and gas segment and a global rental account for diesel and gas generator sets.

This segment continuously explores emerging technologies and provides integrated power generation products using technologies other than reciprocating engines. We use our own research and development capabilities as well as those of our business partnerships to develop cost-effective and environmentally sound power solutions.

Our customer base for our power generation products is highly diversified, with customer groups varying based on their power needs. India, China, the United Kingdom (U.K.), Western Europe, Latin America and the Middle East are our largest geographic markets outside of North America.

Power Generation competes with a variety of engine manufacturers and generator set assemblers across the world. Our primary compeitiors are CAT, Tognum (MTU) and Kohler/SDMO (Kohler Group), but we also compete with GE Jenbacher, FG Wilson (CAT group), Generac, Mitsubishi (MHI) and numerous regional generator set assemblers. Our generator technologies business competes globally with Emerson Electric Co., Marathon Electric and Meccalte, among others.

Distribution Segment

Distribution segment sales and EBIT as a percentage of consolidated results were:

	Years ended December 31,		
	2012	**2011**	**2010**
Percent of consolidated net sales(1)	**16%**	14%	14%
Percent of consolidated EBIT(1)	**16%**	15%	18%

(1) Measured before intersegment eliminations

Our Distribution segment consists of 23 company-owned and 18 joint venture distributors that service and distribute the full range of our products and services to end-users at approximately 400 locations in approximately 80 distribution territories. Our company-owned distributors are located in key markets, including North America, Australia, Europe, the Middle East, India, China, Africa, Russia, Japan, Brazil, Singapore and Central America, while our joint venture distributors are located in North America, South America, Africa, China, Thailand, Singapore and Vietnam.

The Distribution segment consists of the following businesses which service and/or distribute the full range of our products and services:

Parts and filtration,

Power generation,

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- Engines and
- Service.

The Distribution segment is organized into five primary geographic regions:

- Asia Pacific,
- Europe and the Middle East (EME),
- North and Central America,
- Africa and
- South America.

Asia Pacific and EME are composed of six smaller regional distributor organizations (South Pacific, Greater Europe, the Middle East, China, India and Northeast/Southeast Asia) which allow us to better manage these vast geographic territories.

North and Central America are mostly comprised of a network of partially-owned distributors. Internationally, our network consists of independent, partially-owned and wholly-owned distributors. Through these networks, we provide parts and service to our customers. These full-service solutions include maintenance contracts, engineering services and integrated products, where we customize our products to cater to specific needs of end-users. Our distributors also serve and develop dealers, predominantly OEM dealers, in their territories by providing new products, technical support, tools, training, parts and product information.

In addition to managing our involvement with our wholly-owned and partially-owned distributors, our Distribution segment is responsible for managing the performance and capabilities of our independent distributors. Our Distribution segment serves a highly diverse customer base with approximately 45 percent of its 2012 sales being generated from new engines and power generation equipment, compared to 47 percent in 2011, with its remaining sales generated by parts and filtration and service revenue.

Financial information about our distributors accounted for under the equity method are incorporated by reference from Note 3, "INVESTMENTS IN EQUITY INVESTEES," to our *Consolidated Financial Statements*.

Our distributors compete with distributors or dealers that offer similar products. In many cases, these competing distributors or dealers are owned by, or affiliated with the companies that are listed above as competitors of our Engine, Components or Power Generation segments. These competitors vary by geographical location.

In July 2012, we acquired an additional 45 percent interest in Cummins Central Power from the former principal for consideration of approximately $20 million. The acquisition was accounted for as a business combination, with the results of the acquired entity included in the Distribution operating segment in the third quarter of 2012. Distribution segment results also included a $7 million gain, as we were required to re-measure our pre-existing 35 percent ownership interest in Cummins Central Power to fair value in accordance with accounting principles generally accepted in the United State of America (GAAP). See Note 2, "ACQUISITIONS AND DIVESTITURES," to our *Consolidated Financial Statements* for additional detail.

JOINT VENTURES, ALLIANCES AND NON-WHOLLY-OWNED SUBSIDIARIES

We have entered into a number of joint venture agreements and alliances with business partners around the world. Our joint ventures are either distribution or manufacturing entities. We also own controlling interests in non-wholly-owned manufacturing and distribution subsidiaries. Seven entities, in

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which we own more than a 50 percent equity interest, are consolidated in our Distribution segment results as well as several manufacturing joint ventures in the other operating segments.

In the event of a change of control of either party to certain of these joint ventures and other strategic alliances, certain consequences may result including automatic termination and liquidation of the venture, exercise of "put" or "call" rights of ownership by the non-acquired partner, termination or transfer of technology license rights to the non-acquired partner and increases in component transfer prices to the acquired partner. We will continue to evaluate joint venture and partnership opportunities in order to penetrate new markets, develop new products and generate manufacturing and operational efficiencies.

Financial information about our investments in joint ventures and alliances is incorporated by reference from Note 3, "INVESTMENTS IN EQUITY INVESTEES," to the *Consolidated Financial Statements.*

Our equity income from these investees was as follows:

In millions	Years ended December 31, 2012		2011		2010	
Distribution Entities						
North American distributors	**$ 147**	**42%**	$ 134	36%	$ 101	32%
Komatsu Cummins Chile, Ltda.	**26**	**8%**	22	6%	16	5%
All other distributors	**4**	**1%**	4	1%	3	1%
Manufacturing Entities						
Chongqing Cummins Engine Company, Ltd.	**61**	**18%**	68	18%	46	14%
Dongfeng Cummins Engine Company, Ltd.	**52**	**15%**	80	21%	99	31%
Cummins Westport, Inc.	**14**	**4%**	14	4%	10	3%
Shanghai Fleetguard Filter Co., Ltd.	**13**	**4%**	15	4%	12	4%
Tata Cummins, Ltd.	**11**	**3%**	14	4%	14	4%
Valvoline Cummins, Ltd.	**8**	**2%**	7	2%	8	3%
Beijing Foton Cummins Engine Co., Ltd.	**5**	**1%**	(7)	(2)%	(16)	(5)%
Komatsu manufacturing alliances	**(3)**	**(1)%**	3	1%	11	3%
All other manufacturers	**9**	**3%**	21	5%	17	5%
Cummins share of net income(1)	**$ 347**	**100%**	$ 375	100%	$ 321	100%

(1) This total represents our share of net income of our equity investees and is exclusive of royalties and interest income from our equity investees. To see how this amount reconciles to "Equity, royalty and interest income from investees" in the *Consolidated Statements of Income*, see Note 3, "INVESTMENTS IN EQUITY INVESTEES," to our *Consolidated Financial Statements.*

Distribution Entities

North American Distributors Our distribution channel in North America includes 11 unconsolidated partially-owned distributors. Our equity interests in these nonconsolidated entities range from 30 percent to 50 percent. We also have more than a 50 percent ownership interest in four partially owned distributors which we consolidate. While each distributor is a separate legal entity, the business of each is substantially the same as that of our wholly-owned distributors based in other parts of the world. All of our distributors, irrespective of their legal structure or ownership, offer the full range of our products and services to customers and end-users in their respective markets.

Komatsu Cummins Chile, Ltda. Komatsu Cummins Chile, Ltda. is a joint venture with Komatsu America Corporation. The joint venture is a distributor that offers the full range of our products and services to customers and end-users in the Chilean and Peruvian markets.

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Our distribution agreements with independent and partially-owned distributors generally have a renewable 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. Our 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 trademarks, 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 generally refuse to renew these agreements upon expiration or terminate them upon written 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.

See further discussion of our distribution network under the Distribution segment section above.

Manufacturing Entities

Our manufacturing joint ventures have generally been formed with customers and generally are intended to allow us to increase our market penetration in geographic regions, reduce capital spending, streamline our supply chain management and develop technologies. Our largest manufacturing joint ventures are based in China and are included in the list below. Our engine manufacturing joint ventures are supplied by our Components segment in the same manner as it supplies our wholly-owned Engine segment and Power Generation segment manufacturing facilities. Our Components segment joint ventures and wholly owned entities provide fuel system, filtration and turbocharger products that are used in our engines as well as some competitors' products. The results and investments in our joint ventures in which we have 50 percent or less ownership interest are included in "Equity, royalty and interest income from investees" and "Investments and advances related to equity method investees" in our *Consolidated Statements of Income* and *Consolidated Balance Sheets*, respectively.

Chongqing Cummins Engine Company, Ltd. Chongqing Cummins Engine Company, Ltd. (CCEC) is a joint venture in China with Chongqing Machinery and Electric Co. Ltd. This joint venture manufactures several models of our heavy-duty and high-horsepower diesel engines, primarily serving the industrial and stationary power markets in China.

Dongfeng Cummins Engine Company, Ltd. Dongfeng Cummins Engine Company, Ltd. (DCEC) is a joint venture in China with Dongfeng Automotive Co. Ltd., a subsidiary of Dongfeng Motor Corporation (Dongfeng), one of the largest medium-duty and heavy-duty truck manufacturers in China. DCEC produces Cummins 4- to 13-liter mechanical engines, full-electronic diesel engines, with a power range from 125 to 545 horsepower, and natural gas engines.

Cummins Westport, Inc. Cummins Westport, Inc. is a joint venture in Canada with Westport Innovations Inc. to market and sell medium-duty automotive spark-ignited natural gas engines worldwide and to participate in joint technology projects on low-emission technologies.

Shanghai Fleetguard Filter Co., Ltd. Shanghai Fleetguard Filter Co., Ltd. is a joint venture in China with Dongfeng that manufactures filtration systems.

Tata Cummins, Ltd. Tata Cummins Ltd. is a joint venture in India with Tata Motors Ltd., the largest automotive company in India and a member of the Tata group of companies. This joint venture manufactures engines in India for use in trucks manufactured by Tata Motors, as well as for various industrial and power generation applications.

Valvoline Cummins, Ltd. Valvoline Cummins, Ltd. is a joint venture in India with Ashland Inc., USA. This joint venture manufactures and distributes lubricants and oil related products in India which are used in automotive and industrial applications. Products include transmission fluids, hydraulic lubricants, automotive filters, cooling system products, greases and specialty products.

Beijing Foton Cummins Engine Co., Ltd. Beijing Foton Cummins Engine Co., Ltd. is a joint venture in China with Beijing Foton Motor Co., Ltd., a commercial vehicle manufacturer, which produces ISF 2.8 liter and ISF 3.8 liter families of Cummins high performance light-duty diesel engines in Beijing. These engines are used in light-duty commercial trucks, pickup trucks, multipurpose and sport utility vehicles in China, Brazil and Russia. Certain types of marine, small construction equipment and industrial applications are also served by these engine families.

Komatsu manufacturing alliances Komatsu manufacturing alliances consists of two manufacturing joint ventures and one design joint venture including Komatsu Cummins Engine Company (KCEC) in Japan and Cummins Komatsu Engine Company (CKEC) in the United States (U.S.) with Komatsu Ltd. These joint ventures manufacture Cummins-designed medium-duty engines in Japan and Komatsu-designed high-horsepower engines in the U.S. The industrial engine design joint venture is located in Japan.

Cummins-Scania XPI Manufacturing, LLC Cummins-Scania XPI Manufacturing, LLC is a joint venture in the United States with Scania Holding, Inc. This joint venture manufactures several models of advanced fuel systems for heavy-duty and midrange diesel engines.

Cummins Olayan Energy Ltd. Cummins Olayan Energy Ltd. is a joint venture in the Kingdom of Saudi Arabia with General Contracting Company to operate certain rental power generation equipment, which is primarily utilized within the Kingdom of Saudi Arabia.

Guangxi Cummins Industrial Power Co., Ltd. Guangxi Cummins Industrial Power Co., Ltd. is a joint venture in China with Guangxi LiuGong Machinery Co. This joint venture manufactures 6.7 liter and 9.3 liter diesel engines for use in various construction equipment.

Fleetguard Filters Private, Ltd. Fleetguard Filters Private, Ltd. is a joint venture in India with Perfect Sealing System Private Limited that manufactures and sells filtration systems primarily for commercial vehicle applications.

Cummins MerCruiser Diesel Marine, LLC Cummins MerCruiser Diesel Marine, LLC (CMD) was a joint venture in the U.S. with Mercury Marine, a division of Brunswick Corporation, to develop, manufacture and sell recreational marine diesel products, including engines, sterndrive packages, inboard packages, instrument and controls, service systems and replacement and service parts and assemblies, complete integration systems and other related products. In April 2012, we executed our plans to dissolve the joint venture and to transition to a strategic supply arrangement between the two companies to more effectively and efficiently serve customers in the global diesel marine market. All business activities were moved from CMD to the parent companies at the time of the dissolution. We will continue to use Mercury Marine drives and control systems in conjunction with its extensive offering of mid-range and heavy-duty marine engines. The dissolution of the joint venture did not have a significant impact on our financial results.

Non-Wholly-Owned Subsidiary

We have a controlling interest in Cummins India Ltd. (CIL), which is a publicly listed company on various stock exchanges in India. CIL produces mid-range, heavy-duty and high-horsepower engines, generators for the Indian and export markets and natural gas spark-ignited engines for power generation, automotive and industrial applications. CIL also has distribution and power generation

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operations. CIL's net income attributable to Cummins was $42 million, $44 million and $46 million for 2012, 2011 and 2010, respectively.

SUPPLY

The performance of the end-to-end supply chain, extending through to our suppliers, is foundational to our ability to meet customers' expectations and support long-term growth. In order to ensure we meet the needs of our customers, we are committed to having a robust strategy for how we select and manage our suppliers.

We have a strategic sourcing policy that guides decisions on what we make, when we establish supplier partnerships and what we purchase. Today we machine and assemble strategic components used in our engines and power generation units, including blocks, heads, turbochargers, connecting rods, camshafts, crankshafts, filters, alternators and fuel systems. We source externally purchased material and manufactured components from leading suppliers both domestically and internationally. Many suppliers are managed though long-term agreements that assure capacity, delivery, quality and cost requirements are met over an extended period. We have a "take or pay" contract with an emission solutions business supplier requiring us to purchase approximately $73 million annually through 2018. Approximately 60 to 70 percent of the total types of parts in our product designs are single sourced. Although we elect to source a relatively high proportion of our total raw materials and components from sole suppliers, we have an established annual sourcing strategy process that evaluates risk. This annual review process has led us to begin increasing our use of dual sourcing to both minimize risk and increase supply chain responsiveness.

Other important elements of our sourcing strategy include:

- working with suppliers to measure and improve their environmental footprint;
- selecting and managing suppliers to comply with our supplier code of conduct and
- assuring our suppliers do not use restricted or prohibited materials in our products.

PATENTS AND TRADEMARKS

We own or control a significant number of patents and trademarks relating to the products we manufacture. These patents and trademarks were granted and registered over a period of years. Although these patents and trademarks are generally considered beneficial to our operations, we do not believe any patent, group of patents, or trademark (other than our leading brand house trademarks) is significant to our business.

SEASONALITY

While individual product lines may experience modest seasonal variation in production, there is no material effect on the demand for the majority of our products on a quarterly basis with the exception that our Power Generation segment normally experiences seasonal declines in the first quarter due to general declines in construction spending during this period and our Distribution segment normally experiences seasonal declines in its first quarter business activity due to holiday periods in Asia and Australia.

LARGEST CUSTOMERS

We have thousands of customers around the world and have developed long-standing business relationships with many of them. PACCAR is our largest customer, accounting for approximately 13 percent of our consolidated net sales in 2012, compared to approximately 12 percent in 2011 and 7 percent in 2010. We have long-term supply agreements with PACCAR for our heavy-duty ISX 15 liter

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and ISX 11.9 liter engines and our ISL 9 liter mid-range engine. While a significant number of our sales to PACCAR are under long-term supply agreements, these agreements provide for particular engine requirements for specific vehicle models and not a specific volume of engines. PACCAR is our only customer accounting for more than 10 percent of our net sales in 2012. The loss of this customer or a significant decline in the production level of PACCAR vehicles that use our engines would have an adverse effect on our results of operations and financial condition. We have been an engine supplier to PACCAR for over 68 years. A summary of principal customers for each operating segment is included in our segment discussion.

In addition to our agreement with PACCAR, we have long-term heavy-duty engine supply agreements with Volvo Trucks North America and Navistar International Corporation and long-term mid-range supply agreements with Daimler Trucks North America, Ford and MAN. We also have an agreement with Chrysler to supply engines for its Ram trucks. In our off-highway markets, we have various engine and component supply agreements ranging across our midrange and high-horsepower businesses with Komatsu Ltd., as well as various joint ventures and other license agreements in our Engine, Component and Distribution segments. Collectively, our net sales to these seven customers, including PACCAR, was approximately 33 percent of our consolidated net sales in 2012, compared to approximately 31 percent in 2011 and 25 percent in 2010. Excluding PACCAR, net sales to individual customers were less than 8 percent of our consolidated net sales to any single customer in 2012, compared to less than 6 percent in 2011 and less than 4 percent in 2010. These agreements contain standard purchase and sale agreement terms covering engine and engine parts pricing, quality and delivery commitments, as well as engineering product support obligations. The basic nature of our agreements with OEM customers is that they are long-term price and operations agreements that help assure the availability of our products to each customer through the duration of the respective agreements. Agreements with most OEMs contain bilateral termination provisions giving either party the right to terminate in the event of a material breach, change of control or insolvency or bankruptcy of the other party.

BACKLOG

Our 2012 lead times for the majority of our businesses improved from their 2011 levels. While we have supply agreements with some truck and off-highway equipment OEMs, most of our business is transacted through open purchase orders. These open orders are historically subject to month-to-month releases and are subject to cancellation on reasonable notice without cancellation charges and therefore are not considered firm.

RESEARCH AND DEVELOPMENT EXPENSE

In 2012, we increased our research, development and engineering expenses as we continued to invest in future critical technologies and products. We will continue to make investments to improve our current technologies, continue to meet the future emission requirements around the world and improve fuel economy.

Our research and development program is focused on product improvements, innovations and cost reductions for our customers. Research and development expenditures include salaries, contractor fees, building costs, utilities, administrative expenses and allocation of corporate costs and are expensed, net of contract reimbursements, when incurred. Research and development expenses, net of contract reimbursements, were $721 million in 2012, $621 million in 2011 and $402 million in 2010. Contract reimbursements were $86 million in 2012, $75 million in 2011 and $68 million in 2010.

For 2011 and 2010, approximately $1 million and $38 million or less than 1 percent and 9 percent, respectively, of our research and development expenditures were directly related to compliance with 2010 Environmental Protection Agency (EPA) emission standards. For 2012, 2011 and 2010, approximately $101 million, $104 million and $36 million or 14 percent, 17 percent and 9 percent, of our research and development expenditures were directly related to compliance with 2013 EPA emission standards.

ENVIRONMENTAL SUSTAINABILITY

Our Environmental Sustainability principles attempt to positively impact the environment through the products that we make, how we use our facilities and how we impact communities where we live and work. Our newly formed Corporate Action Committee for Environmental Sustainability is developing a global plan to more fully integrate environmental stewardship across all of our businesses and functions. We continue to invest significantly to further reduce emissions from and increase the efficiency of our products. We attempt to work collaboratively with customers to improve their fuel economy, reduce their carbon footprints and conserve other resources. Over the past four years, we believe that we have reduced company-wide water usage intensity by approximately 45 percent, U.S.-wide process-derived hazardous waste generation by approximately 52 percent and company-wide landfill waste by approximately 28 percent, all normalized to total work hours. We also have articulated our positions on key public policy issues and on a wide range of environmental issues. We are actively engaged with regulatory, industry and other stakeholder groups around the world as GHG and fuel efficiency standards become more prevalent globally. For the eighth consecutive year, we were named to the Dow Jones World Sustainability Index, which recognizes the top 10 percent of the world's largest 2,500 companies in economic, environmental and social leadership. We were also named the top environmentally conscious industrial company in the U.S. in Newsweek's Green Rankings. Our Sustainability Report for 2011/2012 as well as an addendum of more detailed environmental data is available on our website at www.cummins.com, although such report and addendum are not incorporated into this Form 10-K.

ENVIRONMENTAL COMPLIANCE

Product Environmental Compliance

Our engines are subject to extensive statutory and regulatory requirements that directly or indirectly impose standards governing emission and noise. We have substantially increased our global environmental compliance presence and expertise to better prepare for, understand and ultimately meet emerging product environmental regulations around the world. Our products comply with all current emission standards that the European Union (EU), EPA, the California Air Resources Board (CARB) and other state and international regulatory agencies have established for heavy-duty on-highway diesel and gas engines and off-highway engines. Our ability to comply with these and future emission standards is an essential element in maintaining our leadership position in regulated markets. We have made, and will continue to make, significant capital and research expenditures to comply with these standards. Our failure to comply with these standards could result in adverse effects on our future financial results.

EU and EPA Engine Certifications

The current on-highway emission standards came into effect in the EU on October 1, 2008 (Euro V) and on January 1, 2010 for the EPA. To meet the more stringent heavy-duty on-highway emission standards, we used an evolution of our proven selective catalytic reduction (SCR) and exhaust gas recirculation (EGR) technology solutions and refined them for the EU and EPA certified engines to maintain power and torque with substantial fuel economy improvement and maintenance intervals comparable with our previous compliant engines. We offer a complete lineup of on-highway engines to meet the near-zero emission standards. Mid-range and heavy-duty engines for EU and EPA require NOx aftertreatment. NOx reduction is achieved by an integrated technology solution comprised of the XPI High Pressure Common Rail fuel system, SCR technology, next-generation cooled EGR, advanced electronic controls, proven air handling and the Cummins Diesel Particulate Filter (DPF). The EU, EPA, and CARB have certified that our engines meet the current emission requirements. Emission standards in international markets, including Japan, Mexico, Australia, Brazil, Russia, India and China are becoming more stringent. We believe that our experience in meeting the EU and EPA emission standards leaves us well positioned to take advantage of opportunities in these markets as the need for emission control capability grows.

We have received certification from the EPA that we have met both the EPA 2013 and 2014 GHG regulations and rules. The EPA 2013 regulations add the requirement of On-Board Diagnostics, which were introduced on the ISX15 in 2010, across the full on-highway product line in 2013 in addition to maintaining the same near-zero emission levels of NOx and Particulate Matter (PM) required in 2010. On-Board Diagnostics provide enhanced service capability with standardized diagnostic trouble codes, service tool interface, in-cab warning lamp and service information availability. The new GHG and fuel-efficiency regulations will be required for all heavy-duty diesel and natural gas engines beginning in January 2014. Our GHG certification is the first engine certificate issued by the EPA and uses the same proven base engine with the XPI fuel system, Variable Geometry Turbocharger (VGT), Cummins Aftertreatment System with DPF and SCR technology and fully integrated electronics.

Other Environmental Statutes and Regulations

Expenditures for environmental control activities and environmental remediation projects at our facilities in the U.S. have not been a substantial portion of our annual capital outlays and are not expected to be material in 2013. We believe we are in compliance in all material respects with laws and regulations applicable to our plants and operations.

In the U.S., pursuant to notices received from federal and state agencies and/or defendant parties in site environmental contribution actions, we have been identified as a potentially responsible party (PRP) under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended or similar state laws, at approximately 20 waste disposal sites. Based upon our experiences at similar sites we believe that our aggregate future remediation costs will not be significant. We have established accruals that we believe are adequate for our expected future liability with respect to these sites.

In addition, we have several other sites where we are working with governmental authorities on remediation projects. The costs for these remediation projects are not expected to be material.

EMPLOYEES

As of December 31, 2012, we employed approximately 46,000 persons worldwide. Approximately 15,750 of our employees worldwide are represented by various unions under collective bargaining agreements that expire between 2013 and 2015.

AVAILABLE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information electronically with the Securities and Exchange Commission (the "SEC"). You may read and copy any document we file with the SEC at the SEC's public reference room at 100 F Street, N.E., Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for information on the public reference room. The SEC maintains an internet site that contains annual, quarterly and current reports, proxy and information statements and other information that issuers (including Cummins) file electronically with the SEC. The SEC's internet site is www.sec.gov.

Our internet site is www.cummins.com. You can access our Investors and Media webpage through our internet site, by clicking on the heading "Investors and Media" followed by the "Investor

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Relations" link. We make available, free of charge, on or through our Investors and Media webpage, our proxy statements, annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports filed or furnished pursuant to the Securities Exchange Act of 1934 or the Securities Act of 1933, as amended, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC.

We also have a Corporate Governance webpage. You can access our Governance Documents webpage through our internet site, www.cummins.com, by clicking on the heading "Investors and Media," followed by the "Investor Relations" link and then the topic heading of "Governance Documents" within the "Corporate Governance" heading. Code of Conduct, Committee Charters and other governance documents are included at this site. Our Code of Conduct applies to all employees, regardless of their position or the country in which they work. It also applies to the employees of any entity owned or controlled by us. We will post any amendments to the Code of Conduct and any waivers that are required to be disclosed by the rules of either the SEC or the New York Stock Exchange LLC (NYSE), on our internet site. The information on our internet site is not incorporated by reference into this report.

EXECUTIVE OFFICERS OF THE REGISTRANT

Following are the names and ages of our executive officers, their positions with us as of January 31, 2013, and summaries of their backgrounds and business experience:

Name and Age	Present Cummins Inc. position and year appointed to position	Principal position during the past five years other than Cummins Inc. position currently held
N. Thomas Linebarger (50)	Chairman of the Board of Directors and Chief Executive Officer (2012)	President and Chief Operating Officer (2008-2011), Executive Vice President and President Power Generation (2005-2008)
Sharon R. Barner (55)	Vice President General Counsel (2012)	Partner Law firm of Foley & Lardner (2011-2012) Deputy Under Secretary of Commerce Intellectual Property and Deputy Director of the United States Patent and Trademark Office (2009-2011) Partner Law firm of Foley & Lardner (1996-2009)
Jean S. Blackwell (58)	Executive Vice President Corporate Responsibility (2008)	Executive Vice President Chief Financial Officer (2005-2008)
Pamela L. Carter (63)	Vice President and President Distribution Business (2007)	
Steven M. Chapman (58)	Group Vice President China and Russia (2009)	Vice President Emerging Markets and Businesses (2005-2009)
Jill E. Cook (49)	Vice President Human Resources (2003)	

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Name and Age	Present Cummins Inc. position and year appointed to position	Principal position during the past five years other than Cummins Inc. position currently held
Richard J. Freeland (55)	Vice President and President Engine Business (2010)	Vice President and President Components Group (2008-2010), Vice President and President Worldwide Distribution Business (2005-2008)
Mark R. Gerstle (57)	Vice President Community Relations (2011)	Vice President Chief Administrative Officer (2008-2011), Vice President Corporate Quality and Chief Risk Officer (2005-2008)
Richard E. Harris (60)	Vice President Chief Investment Officer (2008)	Vice President Treasurer (2003-2008)
Marsha L. Hunt (49)	Vice President Corporate Controller (2003)	
Marya M. Rose (50)	Vice President Chief Administrative Officer (2011)	Vice President General Counsel and Corporate Secretary (2001-2011)
Livingston L. Satterthwaite (52)	Vice President and President Power Generation (2008)	Vice President Generator Set Business (2003-2008)
Anant J. Talaulicar (51)	Vice President and President Components Group (2010), Vice President and Managing Director India ABO (2004)	Chairman and Managing Director Cummins India Ltd. (2003-present)
John C. Wall (61)	Vice President Chief Technical Officer (2000)	
Patrick J. Ward (49)	Vice President Chief Financial Officer (2008)	Vice President Engine Business Controller (2006-2008)
Lisa M. Yoder (49)	Vice President Global Supply Chain & Manufacturing (2011)	Vice President Corporate Supply Chain (2010-2011), Executive Director Supply Chain & Operations-Power Generation (2007-2010)

Our Chairman and Chief Executive Officer is elected annually by our Board of Directors and holds office until the meeting of the Board of Directors at which his election is next considered. Other officers are appointed by the Chairman and Chief Executive Officer, are ratified by our Board of Directors and hold office for such period as the Chairman and Chief Executive Officer or the Board of Directors may prescribe.

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ITEM 1A. Risk Factors

Set forth below and elsewhere in this Annual Report on Form 10-K are some of the principal risks and uncertainties that could cause our actual business results to differ materially from any forward-looking statements contained in this Report and could individually, or in combination, have a material adverse effect on our results of operations, financial position or cash flows. These risk factors should be considered in addition to our cautionary comments concerning forward-looking statements in this Report, including statements related to markets for our products and trends in our business that involve a number of risks and uncertainties. Our separate section above, "CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING INFORMATION," should be considered in addition to the following statements.

A sustained slowdown or significant downturn in our markets could materially and adversely affect our results of operations, financial condition or cash flows.

The global economy continued to slow throughout 2012 as we experienced declining demand in emerging markets, including Brazil and China, and a decline in India as the result of foreign currency fluctuations. The developed economies, including the U.S. economy, experienced slowing demand as the year progressed and continued to experience economic uncertainty driven by unresolved federal tax and budget issues, while Europe continued to struggle as the result of lingering high unemployment, concerns over European sovereign debt issues and the tightening of government budgets. If the global economy or some of our significant markets encounter a sustained slowdown or our emerging markets, particularly China and Brazil, don't recover to stronger growth rates; depending upon the length, duration and severity of such a slowdown, our results of operations, financial condition and cash flow would almost certainly be materially adversely affected. Specifically, our revenues would likely decrease, we may be forced to consider further restructuring actions, we may need to increase our allowance for doubtful accounts, our days sales outstanding may increase and we could experience impairments to assets of certain of our businesses.

A slowdown in infrastructure development could adversely affect our business.

Infrastructure development has been a significant driver of our business in recent years, especially in the emerging markets of China and Brazil. In 2012, infrastructure spending in emerging markets steadily declined throughout the year. General weakness in economic growth or the perception that infrastructure has been overbuilt could lead to a further decline in infrastructure spending. Any sustained downturns in infrastructure development that result from these or other circumstances could adversely affect our business.

Unpredictability in the adoption, implementation and enforcement of increasingly stringent emission standards by multiple jurisdictions around the world could adversely affect our business.

Our engines are subject to extensive statutory and regulatory requirements governing emission and noise, including standards imposed by the EPA, the European Union, state regulatory agencies (such as the CARB) and other regulatory agencies around the world. We have made, and will be required to continue to make, significant capital and research expenditures to comply with these emission standards. Developing engines to meet numerous changing government regulatory requirements, with different implementation timelines and emission requirements, makes developing engines efficiently for multiple markets complicated and could result in substantial additional costs that may be difficult to recover in certain markets. In some cases, we may be required to develop new products to comply with new regulations, particularly those relating to air emission. While we have met previous deadlines, our ability to comply with other existing and future regulatory standards will be essential for us to maintain our position in the engine markets we serve. The successful development and introduction of new and enhanced products in order to comply with new regulatory requirements are subject to other risks, such

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as delays in product development, cost over-runs and unanticipated technical and manufacturing difficulties.

In addition to these risks, the nature and timing of government implementation and enforcement of increasingly stringent emission standards around the world is unpredictable and subject to change, or delays which could result in the products we developed or modified to comply with these standards becoming unnecessary or becoming necessary later than expected and in some cases negating our competitive advantage. This in turn can delay, diminish or eliminate the expected return on capital and research expenditures that we have invested in such products and may adversely affect our perceived competitive advantage in being an early, advanced developer of compliant engines.

We derive significant income from investees that we do not directly control.

Our net income includes significant equity, royalty and interest income from investees that we do not directly control. For 2012, we recognized $384 million of equity, royalty and interest income from investees, compared to $416 million in 2011. The majority of our equity, royalty and interest income from investees is from our 11 unconsolidated North American distributors and from two of our joint ventures in China, Dongfeng Cummins Engine Company, Ltd. (DCEC) and Chongqing Cummins Engine Company, Ltd. (CCEC). Our equity ownership interests in our unconsolidated North American distributors generally range from 30 percent to 50 percent. We have 50 percent equity ownership interests in DCEC and CCEC. As a result, although a significant percentage of our net income is derived from these unconsolidated entities, we do not unilaterally control their management or their operations, which puts a substantial portion of our net income at risk from the actions or inactions of these other entities. A significant reduction in the level of contribution by these entities to our net income would likely have a material adverse effect on our results of operations.

Our truck manufacturers and original equipment manufacturers (OEMs) customers may not continue to outsource their engine supply needs.

Several of our engine customers, including PACCAR, Volvo AB, Navistar International Corporation and Chrysler, are truck manufacturers or OEMs that manufacture engines for some of their own products. Despite their own engine manufacturing abilities, these customers have historically chosen to outsource certain types of engine production to us due to the quality of our engine products, our emission capabilities, our systems integration, their customers' preferences, their desire for cost reductions, their desire for eliminating production risks and their desire to maintain company focus. However, there can be no assurance that these customers will continue to outsource, or outsource as much of, their engine production in the future. Increased levels of OEM vertical integration could result from a number of factors, such as shifts in our customers' business strategies, acquisition by a customer of another engine manufacturer, the inability of third-party suppliers to meet product specifications and the emergence of low-cost production opportunities in foreign countries. Any significant reduction in the level of engine production outsourcing from our truck manufacturer or OEM customers could have a material adverse effect on our results of operations.

A downturn in the North American truck industry or other factors negatively affecting any of our truck OEM customers could materially adversely impact our results of operations.

We make significant sales of engines and components to a few large truck OEMs in North America. If the North American truck market suffers a significant downturn, or if one of our large truck OEM customers experienced financial distress or bankruptcy, such circumstance would likely lead to significant reductions in our revenues and earnings, commercial disputes, receivable collection issues, and other negative consequences that could have a material adverse impact on our results of operations.

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The discovery of any significant problems with our new engine platforms in North America could materially adversely impact our results of operations, financial condition and cash flow.

The EPA and CARB have certified all of our 2012/2013 on-highway and off-highway engines, which utilize SCR technology to meet requisite emission levels. We introduced SCR technology into our engine platforms in 2010. The effective performance of SCR technology and the overall performance of these engine platforms impact a number of our operating segments and remain crucial to our success in North America. While these 2010 engine platforms have performed well in the field, the discovery of any significant problems in these platforms could result in recall campaigns, increased warranty costs, reputational risk and brand risk, and could materially adversely impact our results of operations, financial condition and cash flow.

We are subject to currency exchange rate and other related risks.

We conduct operations in many areas of the world involving transactions denominated in a variety of currencies. We are subject to currency exchange rate risk to the extent that our costs are denominated in currencies other than those in which we earn revenues. In addition, since our financial statements are denominated in U.S. dollars, changes in currency exchange rates between the U.S. dollar and other currencies have had, and will continue to have, an impact on our results of operations. While we customarily enter into financial transactions that attempt to address these risks and many of our supply agreements with customers include currency exchange rate adjustment provisions, there can be no assurance that currency exchange rate fluctuations will not adversely affect our results of operations. In addition, while the use of currency hedging instruments may provide us with some protection from adverse fluctuations in currency exchange rates, by utilizing these instruments we potentially forego the benefits that might result from favorable fluctuations in currency exchange rates.

We also face risks arising from the imposition of exchange controls and currency devaluations. Exchange controls may limit our ability to convert foreign currencies into U.S. dollars or to remit dividends and other payments by our foreign subsidiaries or businesses located in or conducted within a country imposing controls. Currency devaluations result in a diminished value of funds denominated in the currency of the country instituting the devaluation.

We are vulnerable to supply shortages from single-sourced suppliers.

During 2012, we single sourced approximately 60 to 70 percent of the total types of parts in our product designs. Any delay in our suppliers' deliveries may adversely affect our operations at multiple manufacturing locations, forcing us to seek alternative supply sources to avoid serious disruptions. Delays may be caused by factors affecting our suppliers, including capacity constraints, labor disputes, economic downturns, availability of credit, the impaired financial condition of a particular supplier, suppliers' allocations to other purchasers, weather emergencies, natural disasters or acts of war or terrorism. Any extended delay in receiving critical supplies could impair our ability to deliver products to our customers and our results of operations.

Our products are exposed to variability in material and commodity costs.

Our businesses establish prices with our customers in accordance with contractual time frames; however, the timing of material and commodity market price increases may prevent us from passing these additional costs on to our customers through timely pricing actions. Additionally, higher material and commodity costs around the world may offset our efforts to reduce our cost structure. While we customarily enter into financial transactions and contractual pricing adjustment provisions with our customers that attempt to address some of these risks (notably with respect to copper, platinum and palladium), there can be no assurance that commodity price fluctuations will not adversely affect our results of operations. In addition, while the use of commodity price hedging instruments may provide

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us with some protection from adverse fluctuations in commodity prices, by utilizing these instruments we potentially forego the benefits that might result from favorable fluctuations in price. As a result, higher material and commodity costs, as well as hedging these commodity costs during periods of decreasing prices, could result in declining margins.

Our products are subject to recall for performance or safety-related issues.

Our products may be subject to recall for performance or safety-related issues. Product recalls subject us to harm to our reputation, loss of current and future customers, reduced revenue and product recall costs. Product recall costs are incurred when we decide, either voluntarily or involuntarily, to recall a product through a formal campaign to solicit the return of specific products due to a known or suspected performance issue. Any significant product recalls could have a material adverse effect on our results of operations, financial condition and cash flows.

We face significant competition in the markets we serve.

The markets in which we operate are highly competitive. We compete worldwide with a number of other manufacturers and distributors that produce and sell similar products. We primarily compete in the market with diesel engines and related diesel products; however, new technologies continue to be developed for gasoline, natural gas and other technologies and we will continue to face new competition from these expanding technologies. Our products primarily compete on the basis of price, performance, fuel economy, speed of delivery, quality and customer support. We also face competitors in some emerging markets who have established local practices and long standing relationships with participants in these markets. There can be no assurance that our products will be able to compete successfully with the products of other companies and in other markets. For a more complete discussion of the competitive environment in which each of our segments operates, see "Operating Segments" in "Item 1 Business."

Increasing global competition among our customers may affect our existing customer relationships and restrict our ability to benefit from some of our customers' growth.

As our customers in emerging markets continue to grow in size and scope, they are increasingly seeking to export their products to other countries. This has meant greater demand for our advanced engine technologies to help these customers meet the more stringent emissions requirements of developed markets, as well as greater demand for access to our distribution systems for purposes of equipment servicing. As these emerging market customers enter into and begin to compete in more developed markets, they may increasingly begin to compete with our existing customers in these markets. Our further aid to emerging market customers could adversely affect our relationships with developed market customers and, as a result, we may be pressured to restrict sale or support of some of our products in the areas of increased competition. In addition, to the extent the competition does not correspond to overall growth in demand, we may see little or no benefit from this type of expansion by our emerging market customers.

We are exposed to political, economic and other risks that arise from operating a multinational business.

Approximately 53 percent of our net sales for 2012 and 59 percent in 2011 were attributable to customers outside the U.S. Accordingly, our business is subject to the political, economic and other risks that are inherent in operating in numerous countries. These risks include:

- the difficulty of enforcing agreements and collecting receivables through foreign legal systems;
- trade protection measures and import or export licensing requirements;

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- the imposition of taxes on foreign income and tax rates in certain foreign countries that exceed those in the U.S.;
- the imposition of tariffs, exchange controls or other restrictions;
- difficulty in staffing and managing widespread operations and the application of foreign labor regulations;
- required compliance with a variety of foreign laws and regulations; and
- changes in general economic and political conditions in countries where we operate, particularly in emerging markets.

As we continue to operate our business globally, our success will depend, in part, on our ability to anticipate and effectively manage these and other related risks. There can be no assurance that the consequences of these and other factors relating to our multinational operations will not have a material adverse effect upon us.

Unanticipated changes in our effective tax rate, the adoption of new tax legislation or exposure to additional income tax liabilities could adversely affect our profitability.

We are subject to income taxes in the U.S. and numerous international jurisdictions. Our income tax provision and cash tax liability in the future could be adversely affected by changes in the distribution of earnings in countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities, changes to our assertions regarding permanent re-investment of our foreign earnings, changes in tax laws and the discovery of new information in the course of our tax return preparation process. The carrying value of deferred tax assets, which are predominantly in the U.S., is dependent on our ability to generate future taxable income in the U.S. We are also subject to ongoing tax audits. These audits can involve complex issues, which may require an extended period of time to resolve and can be highly judgmental. Tax authorities may disagree with certain tax reporting positions taken by us and, as a result, assess additional taxes against us. We regularly assess the likely outcomes of these audits in order to determine the appropriateness of our tax provision. The amounts ultimately paid upon resolution of these or subsequent tax audits could be materially different from the amounts previously included in our income tax provision and, therefore, could have a material impact on our tax provision.

We are exposed to risks arising from the price and availability of energy.

The level of demand for our products and services is influenced in multiple ways by the price and availability of energy. High energy costs generally drive greater demand for better fuel economy in almost all countries in which we operate. Some of our engine products have been developed with a primary purpose of offering fuel economy improvements, and if energy costs decrease or increase less than expected, demand for these products may likewise decrease. The relative unavailability of electricity in some emerging market countries also influences demand for our electricity generating products, such as our diesel generators. If these countries add energy capacity by expanding their power grids at a rate equal to or faster than the growth in demand for energy, the demand for our generating products could also decrease or increase less than would otherwise be the case.

Our global operations are subject to laws and regulations that impose significant compliance costs and create reputational and legal risk.

Due to the international scope of our operations, we are subject to a complex system of commercial and trade regulations around the world. Recent years have seen an increase in the development and enforcement of laws regarding trade compliance and anti-corruption such as the U.S. Foreign Corrupt Practices Act and similar laws from other countries. Our numerous foreign subsidiaries, affiliates and joint venture partners are governed by laws, rules and business practices that

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differ from those of the U.S. The activities of these entities may not comply with U.S. laws or business practices or our Code of Business Conduct. Violations of these laws may result in severe criminal or civil sanctions, could disrupt our business, and result in an adverse effect on our reputation, business and results of operations or financial condition. We cannot predict the nature, scope or effect of future regulatory requirements to which our operations might be subject or the manner in which existing laws might be administered or interpreted.

We face the challenge of accurately aligning our capacity with our demand.

We can experience capacity constraints and longer lead times for certain products in times of growing demand while we can also experience idle capacity as economies slow or demand for certain products decline. Accurately forecasting our expected volumes and appropriately adjusting our capacity have been, and will continue to be, important factors in determining our results of operations. We cannot guarantee that we will be able to increase manufacturing capacity to a level that meets demand for our products, which could prevent us from meeting increased customer demand and could harm our business. However, if we overestimate our demand and overbuild our capacity, we may have significantly underutilized assets and we may experience reduced margins. If we do not accurately align our manufacturing capabilities with demand it could have a material adverse effect on our results of operations.

Our business is exposed to risks of product liability claims.

We face an inherent business risk of exposure to product liability claims in the event that our products' failure to perform to specification results or is alleged to result in property damage, bodily injury and/or death. We may experience material product liability losses in the future. While we maintain insurance coverage with respect to certain product liability claims, we may not be able to obtain such insurance on acceptable terms in the future, if at all, and any such insurance may not provide adequate coverage against product liability claims. In addition, product liability claims can be expensive to defend and can divert the attention of management and other personnel for significant periods of time, regardless of the ultimate outcome. An unsuccessful defense of a significant product liability claim could have a material adverse effect upon us. In addition, even if we are successful in defending against a claim relating to our products, claims of this nature could cause our customers to lose confidence in our products and us.

We may need to write off significant investments in our new North American light-duty diesel engine platform if customer commitments further deteriorate.

We began development of a new North American light-duty diesel engine platform in July 2006 to be used in a variety of on- and off-highway applications. Since that time, and as of December 31, 2012, we have capitalized investments of approximately $233 million. Market uncertainty due to the global recession resulted in some customers delaying or cancelling their vehicle programs, while others remain active. If customer expectations or volume projections further deteriorate from our current expected levels and we do not identify new customers, we may need to recognize an impairment charge and write the assets down to net realizable value.

Our operations are subject to increasingly stringent environmental laws and regulations.

Our plants and operations are subject to increasingly stringent environmental laws and regulations in all of the countries in which we operate, including laws and regulations governing air emission, discharges to water and the generation, handling, storage, transportation, treatment and disposal of waste materials. While we believe that we are in compliance in all material respects with these environmental laws and regulations, there can be no assurance that we will not be adversely impacted by costs, liabilities or claims with respect to existing or subsequently acquired operations, under either

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present laws and regulations or those that may be adopted or imposed in the future. We are also subject to laws requiring the cleanup of contaminated property. If a release of hazardous substances occurs at or from any of our current or former properties or at a landfill or another location where we have disposed of hazardous materials, we may be held liable for the contamination and the amount of such liability could be material.

Significant declines in future financial and stock market conditions could diminish our pension plan asset performance and adversely impact our results of operations, financial condition and cash flow.

We sponsor both funded and unfunded domestic and foreign defined benefit pension and other retirement plans. Our pension expense and the required contributions to our pension plans are directly affected by the value of plan assets, the projected and actual rates of return on plan assets and the actuarial assumptions we use to measure our defined benefit pension plan obligations, including the discount rate at which future projected and accumulated pension obligations are discounted to a present value. We could experience increased pension expense due to a combination of factors, including the decreased investment performance of pension plan assets, decreases in the discount rate and changes in our assumptions relating to the expected return on plan assets.

Significant declines in future financial and stock market conditions could cause material losses in our pension plan assets, which could result in increased pension expense in future years and adversely impact our results of operations, financial condition and cash flow. Depending upon the severity of market declines and government regulatory changes, we may be legally obligated to make pension payments in the U.S. and perhaps other countries and these contributions could be material.

We may be adversely impacted by work stoppages and other labor matters.

As of December 31, 2012, we employed approximately 46,000 persons worldwide. Approximately 15,750 of our employees worldwide are represented by various unions under collective bargaining agreements that expire between 2013 and 2015. While we have no reason to believe that we will be materially impacted by work stoppages or other labor matters, there can be no assurance that future issues with our labor unions will be resolved favorably or that we will not encounter future strikes, work stoppages, or other types of conflicts with labor unions or our employees. Any of these consequences may have an adverse effect on us or may limit our flexibility in dealing with our workforce. In addition, many of our customers and suppliers have unionized work forces. Work stoppages or slow-downs experienced by our customers or suppliers could result in slow-downs or closures that would have a material adverse effect on our results of operations, financial condition and cash flow.

Our financial statements are subject to changes in accounting standards that could adversely impact our profitability or financial position.

Our financial statements are subject to the application of accounting principles generally accepted in the United States of America (GAAP), which are periodically revised and/or expanded. Accordingly, from time to time we are required to adopt new or revised accounting standards issued by recognized authoritative bodies, including the Financial Accounting Standards Board. Recently, accounting standard setters issued new guidance which further interprets or seeks to revise accounting pronouncements related to revenue recognition and lease accounting as well as to issue new standards expanding disclosures. The impact of accounting pronouncements that have been issued but not yet implemented is disclosed in our annual and quarterly reports on Form 10-K and Form 10-Q. An assessment of proposed standards is not provided, as such proposals are subject to change through the exposure process and, therefore, their effects on our financial statements cannot be meaningfully assessed. It is possible that future accounting standards we are required to adopt could change the current accounting treatment that we apply to our consolidated financial statements and that such changes could have a material adverse effect on the reported results of operations and financial position.

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ITEM 1B. Unresolved Staff Comments

None.

ITEM 2. Properties

Manufacturing Facilities

Our principal manufacturing facilities include our plants used by the following segments in the following locations:

Segment	U.S. Facilities	Facilities Outside the U.S.
Engine	**Indiana:** Columbus, Seymour **Tennessee:** Memphis **New Mexico:** Clovis **New York:** Lakewood **North Carolina:** Whitakers	**Brazil:** Sao Paulo **India:** Pune **Mexico:** San Luis Potosi **U.K.:** Darlington, Daventry, Cumbernauld
Components	**Indiana:** Columbus **Iowa:** Lake Mills **South Carolina:** Charleston **Tennessee:** Cookeville **Wisconsin:** Mineral Point, Neillsville	**Australia:** Kilsyth **Brazil:** Sao Paulo **China:** Beijing, Shanghai, Wuxi, Wuhan **France:** Quimper **Germany:** Marktheidenfeld **India:** Pune, Daman, Dewas, Pithampur, Radurapur **Mexico:** Ciudad Juarez, San Luis Potosi **South Africa:** Pretoria, Johannesburg **South Korea:** Suwon **Turkey:** Ismir **U.K.:** Darlington, Huddersfield
Power Generation	**Indiana:** Elkhart **Minnesota:** Fridley	**Brazil:** Sao Paulo **China:** Wuxi, Wuhan **Germany:** Ingolstadt **India:** Pirangut, Ahmendnagar, Ranjangaon **Mexico:** San Luis Potosi **Romania:** Craiova **U.K.:** Margate, Manston, Stamford

In addition, engines and engine components are manufactured by joint ventures or independent licensees at manufacturing plants in the U.S., China, India, South Korea, Mexico and Sweden.

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Distribution Facilities

The principal distribution facilities used by our Distribution segment are located in the following locations:

U.S. Facilities	Facilities Outside the U.S.
Kansas: Wichita	**Australia:** Scoresby
Massachusetts: Dedham	**Belgium:** Mechelen
Missouri: Kansas City	**Canada:** Surrey, Edmonton
Nebraska: Omaha	**China:** Beijing, Shanghai
New York: Bronx	**Germany:** Gross Gerau
Pennsylvania: Bristol, Harrisburg	**India:** Pune
	Japan: Tokyo
	Korea: Chonan
	Russia: Moscow
	Singapore: Singapore SG
	South Africa: Johannesburg
	U.K.: Wellingborough
	United Arab Emirates: Dubai

Headquarters and Other Offices

Our Corporate Headquarters are located in Columbus, Indiana. Additional marketing and operational headquarters are in the following locations:

U.S. Facilities	Facilities Outside the U.S.
Indiana: Columbus, Indianapolis	**China:** Beijing, Shanghai
Tennessee: Franklin, Nashville	**India:** Pune
Washington DC	**U.K.:** Staines, Stockton

ITEM 3. Legal Proceedings

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 U.S. 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. 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 operations, financial condition or cash flows.

We conduct significant business operations in Brazil that are subject to the Brazilian federal, state and local labor, social security, tax and customs laws. While we believe we comply with such laws, they

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are complex, subject to varying interpretations and we are often engaged in litigation regarding the application of these laws to particular circumstances.

ITEM 4. Mine Safety Disclosures

Not Applicable.

PART II

ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

(a) Our common stock is listed on the NYSE under the symbol "CMI." For information about the quoted market prices of our common stock, information regarding dividend payments and the number of common stock shareholders, see "Selected Quarterly Financial Data" in this report. For other matters related to our common stock and shareholders' equity, see Note 15, "SHAREHOLDERS' EQUITY," to the *Consolidated Financial Statements*.

(b) Use of proceeds not applicable.

(c) The following information is provided pursuant to Item 703 of Regulation S-K:

Issuer Purchases of Equity Securities

Period	(a) Total Number of Shares Purchased(1)	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs(2)
October 1 - November 4, 2012	284,881	$ 87.84	284,568	131,733
November 5 - December 2, 2012	2,653	99.54		131,514
December 3 - December 31, 2012	14,372	106.00		118,254
Total	301,906	88.80	284,568	

(1) Shares purchased represent shares under the 2011 Board of Directors authorized $1 billion repurchase program and our Key Employee Stock Investment Plan established in 1969 (there is no maximum repurchase limitation in this plan).

(2) These values reflect the sum of shares held in loan status under our Key Employee Stock Investment Plan. The repurchase program authorized by the Board of Directors does not limit the number of shares that may be purchased and was excluded from this column.

In 2011 we completed our prior authorization, purchasing the remaining $111 million (1.1 million shares) authorized under this plan. In February 2011, the Board of Directors authorized the acquisition of an additional $1 billion of our common stock beginning in 2011, and we acquired $518 million, or 5.3 million shares, under the new authorization in 2011. In 2012 we acquired $256 million, or 2.6 million shares, of our common stock leaving $226 million available for purchase under this authorization at December 31, 2012. In December 2012, the Board of Directors authorized the acquisition of an additional $1 billion of our common stock upon completion of the 2011 repurchase program.

During the fourth quarter of 2012, we repurchased 17,338 shares from employees in connection with the Key Employee Stock Investment Plan which allows certain employees, other than officers, to purchase shares of common stock on an installment basis up to an established credit limit. Loans are issued for initial five-year terms at a fixed interest rate established at the date of purchase and may be refinanced after its initial five-year period for an additional five-year period. Participants must hold

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shares for a minimum of six months from date of purchase and after shares are sold must wait six months before another share purchase may be made. We hold participants' shares as security for the loans and would, in effect repurchase shares if the participant defaulted in repayment of the loan. There is no maximum amount of shares that we may purchase under this plan.

Performance Graph (Unaudited)

The following Performance Graph and related information shall not be deemed "soliciting material" or to be "filed" with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any of our future filings under the Securities Act of 1933 or Securities Exchange Act of 1934, each as amended, except to the extent that we specifically incorporate it by reference into such filing.

The following graph compares the cumulative total shareholder return on our common stock for the last five years with the cumulative total return on the S&P 500 Index and an index of peer companies selected by us. Our peer group includes BorgWarner Inc, Caterpillar, Inc., Daimler AG, Danaher Corporation, Deere & Company, Donaldson Company Inc., Eaton Corporation, Emerson Electric Co., W.W. Grainger Inc., Honeywell International, Illinois Tool Works Inc., Ingersoll-Rand Company Ltd., Navistar International Corporation, PACCAR Inc, Parker-Hannifin Corporation, Textron Inc. and Volvo AB. Each of the measures of cumulative total return assumes reinvestment of dividends. The comparisons in this table are required by the SEC and are not intended to forecast or be indicative of possible future performance of our stock.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN
AMONG CUMMINS INC., S&P 500 INDEX AND CUSTOM PEER GROUP

ASSUMES $100 INVESTED ON DEC. 31, 2007
ASSUMES DIVIDENDS REINVESTED
FISCAL YEAR ENDING DEC. 31, 2012

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ITEM 6. Selected Financial Data

The selected financial information presented below for each of the last five years ended December 31, beginning with 2012, was derived from our *Consolidated Financial Statements*. This information should be read in conjunction with our *Consolidated Financial Statements* and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

In millions, except per share amounts	2012	2011	2010	2009	2008
For the years ended December 31,					
Net sales	**$ 17,334**	$ 18,048	$ 13,226	$ 10,800	$ 14,342
U.S. percentage of sales	**47%**	41%	36%	48%	41%
Non-U.S. percentage of sales	**53%**	59%	64%	52%	59%
Gross margin	**4,508**	4,589	3,168	2,169	2,940
Research, development and engineering expenses	**728**	629	414	362	422
Equity, royalty and interest income from investees	**384**	416	351	214	253
Interest expense	**32**	44	40	35	42
Consolidated net income(1)	**1,738**	1,946	1,140	484	818
Net income attributable to Cummins Inc.(1)(2)	**1,645**	1,848	1,040	428	755
Net earnings per share attributable to Cummins Inc.					
Basic	**$ 8.69**	$ 9.58	$ 5.29	$ 2.17	$ 3.87
Diluted	**8.67**	9.55	5.28	2.16	3.84
Cash dividends declared per share	**1.80**	1.325	0.875	0.70	0.60
Cash flows from operations	**$ 1,532**	$ 2,073	$ 1,006	$ 1,137	$ 987
Capital expenditures	**690**	622	364	310	543
At December 31,					
Cash and cash equivalents	**$ 1,369**	$ 1,484	$ 1,023	$ 930	$ 426
Total assets	**12,548**	11,668	10,402	8,816	8,519
Long-term debt	**698**	658	709	637	629
Total equity(3)	**6,974**	5,831	4,996	4,020	3,480

(1) For the year ended December 31, 2012, consolidated net income included $52 million of restructuring and other charges ($35 million after-tax), a $6 million gain ($4 million after-tax) related to adjustments from our 2011 divestitures and a $20 million reserve ($12 million after-tax) related to legal matters. For the year ended December 31, 2011, consolidated net income included a $68 million gain ($37 million after-tax) related to the disposition of certain assets and liabilities of our exhaust business and a $53 million gain ($33 million after-tax) recorded for the disposition of certain assets and liabilities of our light-duty filtration business, both from the Components segment, and a $38 million gain ($24 million after-tax) related to flood damage recoveries from the insurance settlement related to a June 2008 flood in Southern Indiana. For the year ended December 31, 2010, consolidated net income included $32 million in Brazil tax recoveries ($21 million after-tax) and $2 million in flood damage expenses. In 2010 it was determined that we overpaid a Brazilian revenue based tax during the period of 2004-2008. Consolidated net income includes a pre-tax recovery related to tax credits on imported products arising from this overpayment. For the year ended December 31, 2009, consolidated net income included $99 million in restructuring and other charges ($65 million after-tax) and a gain of $12 million related to flood damage recoveries. For the year ended December 31, 2008, consolidated net income included a $37 million restructuring charge ($26 million after-tax), a $36 million decrease in cash surrender value in corporate owned life insurance and $5 million of losses related to flood damages.

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(2)
On January 1, 2009, we adopted changes issued by the Financial Accounting Standards Board to consolidation accounting and reporting. These changes, among others, require that minority interests be renamed noncontrolling interests and a company present a consolidated net income measure that includes the amount attributable to such noncontrolling interests for all periods presented.

(3)
In 2012, 2011, 2010 and 2008, we recorded non-cash charges (credits) to equity of $83 million, $96 million, $(125) million and $433 million, respectively, to reflect gains and losses associated with the effect of market conditions on our pension plans.

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ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

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 the accompanying notes to those financial statements. Our MD&A is presented in the following sections:

- Executive Summary and Financial Highlights
- 2013 Outlook
- Results of Operations
- Restructuring and Other Charges
- Operating Segment Results
- Liquidity and Capital Resources
- Contractual Obligations and Other Commercial Commitments
- Application of Critical Accounting Estimates
- Recently Adopted and Recently Issued Accounting Pronouncements

EXECUTIVE SUMMARY AND FINANCIAL HIGHLIGHTS

We are a global power leader that designs, manufactures, distributes and services diesel and natural gas engines and engine-related component products, including filtration, aftertreatment, turbochargers, fuel systems, controls systems, air handling systems and electric power generation 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, Daimler Trucks North America, Chrysler Group, LLC, Volvo AB, Komatsu, Navistar International Corporation, Aggreko plc, Ford Motor Company and MAN Nutzfahrzeuge AG. We serve our customers through a network of approximately 600 company-owned and independent distributor locations and approximately 6,500 dealer locations in more than 190 countries and territories.

Our reportable operating segments consist of the following: Engine, Components, Power Generation and Distribution. This reporting structure is organized according to the products and markets each segment serves and 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. Our engines are used in trucks of all sizes, buses and recreational vehicles, as well as in various industrial applications, including construction, mining, agriculture, marine, oil and gas, rail and military equipment. The Components segment sells filtration products, aftertreatment, turbochargers and fuel systems. The Power Generation segment is an integrated provider of power systems which sells engines, generator sets and alternators. 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. Our sales may also be impacted by OEM inventory levels and production schedules and stoppages. Economic downturns in markets we serve

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generally result in reductions in sales and pricing of our products. As a worldwide business, our operations are also affected by currency, political, economic and regulatory matters, including adoption and enforcement of environmental and emission standards, in the countries we serve. As part of our growth strategy, we invest in businesses in certain countries that carry high levels of these risks such as China, Brazil, India, Mexico, Russia and countries in the Middle East and Africa. At the same time, our geographic diversity and broad product and service offerings have helped limit the impact from a drop in demand in any one industry or customer or the economy of any single country on our consolidated results.

The global economy continued to slow throughout 2012, although the impacts were partially offset by strong demand across several end markets in the U.S. and Canada (North America) in the first half of the year; however these markets weakened in the second half of the year, particularly the heavy-duty truck market. Economies in emerging markets, including China and Brazil experienced challenges throughout the year in most markets, especially the off-highway construction market in China and the medium-duty truck market in Brazil. Demand in India remained strong for power generation equipment; however, improved volumes were more than offset by unfavorable currency impacts. International (excludes the U.S. and Canada) off-highway construction markets have continued to deteriorate with engine shipments down 53 percent, including a 72 percent decline in China. The on-highway medium-duty truck market in Brazil declined as the result of the 2011 pre-buy ahead of the new 2012 emission requirements and one of our customers replacing our B6.7 engine with a proprietary engine in 2012 contributing to international medium-duty truck shipments being down 19 percent. North American demand for heavy-duty on-highway products increased 3 percent while medium-duty truck shipments increased 15 percent in 2012 compared to 2011; although demand in both of these markets declined in the second half of 2012. North American light-duty on-highway demand also improved with an increase in shipments to Chrysler of 37 percent in 2012 compared to 2011.

Slow growth in the U.S. economy and uncertainty driven by unresolved federal tax and budget issues caused businesses to hold back on capital expenditures in 2012, thus impacting demand for truck and power generation equipment. The governments of China and India have controlled inflation through tight monetary policies in the form of rising interest rates and tightening access to credit, although both countries began easing these policies in response to reduced inflationary concerns in 2012. Brazil also began easing their monetary policies in the second half of 2012. Easing monetary policies could enhance our end markets; however, there likely will be a delay between when these policies are implemented and when our end markets respond. The European economy remains uncertain with continued volatility in the Euro countries. Although we do not have any significant direct exposure to European sovereign debt, we generated approximately 8 percent of our net sales from Euro zone countries in 2012. As a result of a number of markets unexpectedly slowing in mid-2012, continued weak economic data in a number of regions and increasing levels of uncertainty regarding the direction of the global economy, we implemented a number of cost reduction initiatives in the second half of 2012. In October 2012, we announced strategic actions necessary to respond to the current environment by cutting costs while maintaining investments in key growth programs. Actions include a number of measures to reduce costs including planned work week reductions, shutdowns at some manufacturing facilities and some targeted workforce reductions. We reduced our workforce by 1,300 people in the fourth quarter and incurred total restructuring charges of $52 million ($35 million after-tax), or $0.18 per diluted share.

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The following table contains sales and EBIT results by operating segment for the years ended December 31, 2012 and 2011. Refer to the section titled "Operating Segment Results" for a more detailed discussion of net sales and EBIT by operating segment including the reconciliation of segment EBIT to income before taxes.

Operating Segments

	2012			2011			Percent change 2012 vs. 2011	
In millions	**Sales**	**Percent of Total**	**EBIT**	**Sales**	**Percent of Total**	**EBIT**	**Sales**	**EBIT**
Engine	**$ 10,733**	**62%**	**$ 1,248**	$ 11,307	63%	$ 1,384	(5)%	(10)%
Components	**4,012**	**23%**	**426**	4,063	23%	470	(1)%	(9)%
Power Generation	**3,268**	**19%**	**285**	3,498	19%	373	(7)%	(24)%
Distribution	**3,277**	**19%**	**369**	3,044	17%	386	8%	(4)%
Intersegment eliminations	**(3,956)**	**(23)%**		(3,864)	(22)%		2%	
Non-segment			**(25)**			102		NM
Total	**$ 17,334**	**100%**	**$ 2,303**	$ 18,048	100%	$ 2,715	(4)%	(15)%

"NM" not meaningful information.

Net income attributable to Cummins Inc. for 2012 was $1,645 million, or $8.67 per diluted share, on sales of $17.3 billion, compared to 2011 net income attributable to Cummins Inc. of $1,848 million, or $9.55 per diluted share, on sales of $18.0 billion. The decrease in income and earnings per share was driven by higher operating expenses, lower gross margins and lower equity, royalty and interest income from investees, partially offset by a lower effective tax rate of 23.5 percent versus 27.1 percent in 2011. In addition, the significant gains we recorded in 2011 for the disposition of certain assets and liabilities of our exhaust business and light-duty filtration business and flood damage recoveries did not repeat in 2012. Diluted earnings per share for 2012 benefited $0.06 from lower shares primarily due to the stock repurchase program.

In July 2012, we completed the acquisition of Hilite Germany GmbH (Hilite) in a cash transaction for $176 million. We also acquired an additional 45 percent interest in Cummins Central Power for consideration of approximately $20 million.

We generated $1.5 billion of operating cash flows in 2012, compared to $2.1 billion in 2011. Refer to the section titled "Operating Activities" in the "Liquidity and Capital Resources" section for a discussion of items impacting cash flows.

In February 2011, the Board of Directors approved a share repurchase program and authorized the acquisition of up to $1 billion of our common stock. We repurchased $256 million of common stock in 2012. In December 2012, the Board of Directors authorized the acquisition of up to $1 billion of our common stock upon completion of the 2011 repurchase program.

In July 2012, the Board of Directors authorized a dividend increase of 25 percent from $0.40 to $0.50 per share on a quarterly basis effective in the third quarter. Our debt to capital ratio (capital is defined as debt plus equity) at December 31, 2012, was 10.0 percent, compared to 11.8 percent at December 31, 2011. As of the date of filing of this Annual Report on Form 10-K, we had an 'A' credit rating with a stable outlook from Standard & Poor's Rating Services, an 'A' credit rating and a stable outlook from Fitch Ratings and a 'Baa1' credit rating with a positive outlook from Moody's Investors Service, Inc. In addition to our $1.6 billion in cash and marketable securities on hand, we have sufficient access to our credit facilities, if necessary, to meet currently anticipated investment and funding needs.

On November 9, 2012, we entered into a five-year revolving credit agreement with a syndicate of lenders. The credit agreement provides us with a $1.75 billion senior unsecured revolving credit facility, the proceeds of which are to be used by us for working capital or other general corporate purposes.

Our global pension plans, including our unfunded non-qualified plans, were 98 percent funded at year-end 2012. Our U.S. qualified plan, which represents approximately 60 percent of our worldwide pension obligation, was 106 percent funded and our United Kingdom (U.K.) plan was 104 percent funded. Asset returns in 2012 for the U.S. qualified plan were 14 percent while the year-end 2012 discount rate was 3.95 percent, down 0.85 percentage points from the 2011 discount rate of 4.80 percent. We expect to contribute $170 million of cash to our global pension plans in 2013. We do not have a required minimum pension contribution obligation for our U.S. plans in 2013. We expect pension and other postretirement benefit expense in 2013 to increase by approximately $35 million pre-tax, or $0.14 per diluted share, when compared to 2012. Refer to application of critical accounting estimates within MD&A and Note 12, "PENSION AND OTHER POST RETIREMENT BENEFITS," to the *Consolidated Financial Statements*, for additional information concerning our pension and other post-retirement benefit plans.

2013 OUTLOOK

Near-Term

The global economy continued to slow throughout 2012, although the impacts were partially offset by strong demand across several end markets in North America in the first half of the year; however these markets weakened in the second half of the year, particularly the heavy-duty truck market. Economies in emerging markets, including China and Brazil experienced challenges throughout the year in most markets, especially the off-highway construction market in China and the medium-duty truck market in Brazil. Demand in India remained strong for power generation equipment; however, improved volumes were more than offset by unfavorable currency impacts.

We currently expect the following positive trends in 2013:

- The Brazilian economy is expected to experience stronger growth in 2013 which is anticipated to result in improving demand in both truck and industrial markets over 2012 levels.
- Demand in some of our markets is expected to improve in the second half of 2013 following a slower start in the first half of the year.
- The new heavy-duty supply agreement with Navistar International Corporation is expected to have a positive impact on our heavy-duty truck engine and component sales.

We currently expect the following challenges to our business that may reduce our earnings potential in 2013:

- Political decisions in the U.S. regarding federal tax and budget issues could continue to create economic uncertainty that may limit capital investments and negatively impact the overall North American economy in the first half of 2013.
- We expect most of our markets to be weak in the first quarter of 2013 but should begin to improve in the second quarter, although remaining below 2012 levels in the first half of 2013.
- Demand in certain European markets could continue to decline due to economic uncertainty.
- Growth in international markets could be negatively impacted if emission regulations are not strictly enforced.

Demand for our products in certain industrial markets in China could remain low due to high equipment inventory levels.

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Currency volatility could continue to put pressure on earnings.

North American oil and gas markets could continue to remain weak.

Domestic and international mining markets could continue to deteriorate if commodity prices weaken.

Long-Term

We believe that, over the longer term, there will be economic improvements in most of our current markets and that our opportunities for long-term profitable growth will continue in the future as the result of the following four macroeconomic trends that will benefit our businesses:

tightening emissions controls across the world;

infrastructure needs in emerging markets;

energy availability and cost issues and

globalization of industries like ours.

RESULTS OF OPERATIONS

				Favorable/(Unfavorable)			
	Years ended December 31,			2012 vs. 2011		2011 vs. 2010	
In millions (except per share amounts)	**2012**	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
NET SALES	**$ 17,334**	$ 18,048	$ 13,226	$ (714)	(4)%	$ 4,822	36%
Cost of sales	**12,826**	13,459	10,058	633	5%	(3,401)	(34)%
GROSS MARGIN	**4,508**	4,589	3,168	(81)	(2)%	1,421	45%
OPERATING EXPENSES AND INCOME							
Selling, general and administrative expenses	**1,900**	1,837	1,487	(63)	(3)%	(350)	(24)%
Research, development and engineering expenses	**728**	629	414	(99)	(16)%	(215)	(52)%
Equity, royalty and interest income from investees	**384**	416	351	(32)	(8)%	65	19%
Gain on sale of businesses	**6**	121		(115)	(95)%	121	100%
Other operating income (expense), net	**(16)**	21	(16)	(37)	NM	37	NM
OPERATING INCOME	**2,254**	2,681	1,602	(427)	16%	1,079	67%
Interest income	**25**	34	21	(9)	(26)%	13	62%
Interest expense	**32**	44	40	12	27%	(4)	(10)%
Other income (expense), net	**24**		34	24	100%	(34)	(100)%
INCOME BEFORE INCOME TAXES	**2,271**	2,671	1,617	(400)	15%	1,054	65%
Income tax expense	**533**	725	477	192	26%	(248)	(52)%
CONSOLIDATED NET INCOME	**1,738**	1,946	1,140	(208)	11%	806	71%
Less: Net income attributable to noncontrolling interests	**93**	98	100	5	5%	2	2%

NET INCOME ATTRIBUTABLE TO CUMMINS INC.	**$**	**1,645**	$	1,848	$	1,040	$	(203)	(11)%	$	808	78%
Diluted earnings per common share attributable to Cummins Inc.	**$**	**8.67**	$	9.55	$	5.28	$	(0.88)	(9)%	$	4.27	81%

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Percent of sales	2012	2011	2010	Favorable/(Unfavorable) Percentage Points 2012 vs. 2011	2011 vs. 2010
Gross margin	26.0%	25.4%	24.0%	0.6	1.4
Selling, general and administrative expenses	11.0%	10.2%	11.2%	(0.8)	1.0
Research, development and engineering expenses	4.2%	3.5%	3.1%	(0.7)	(0.4)

2012 vs. 2011

Net Sales

Net sales decreased versus 2011 and was primarily driven by the following:

Engine segment sales decreased by 5 percent due to weakness in industrial demand, especially in international construction markets, and lower volumes in the Brazilian medium-duty truck market, which were partially offset by growth in the North American on-highway markets in the first half of the year, led by the heavy-duty business.

Foreign currency fluctuations unfavorably impacted sales by 2 percent.

Power Generation segment sales decreased by 7 percent due to lower demand in the generator technologies, power solutions and power systems businesses, which were partially offset by growing demand in the power product business, especially in North America.

Components segment sales, excluding acquisitions, decreased by 2 percent due to $126 million of sales in 2011 related to assets sold in 2011 and lower demand in the turbo technologies, filtration and fuel systems businesses, which were partially offset by higher demand in the emission solutions business, primarily in North America and Brazil.

The decreases above were partially offset as Distribution segment sales, excluding acquisitions, increased by 2 percent due to higher demand for parts and filtration products especially in North and Central America, increased power generation growth in East Asia, increased demand in the South Pacific and higher service demand from South Pacific mining customers, which were partially offset by lower engine product sales due to a slowdown in the North American oil and gas markets.

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

Sales to international markets were 49 percent of total net sales in 2012, compared with 56 percent of total net sales in 2011.

Gross Margin

Gross margin decreased by $81 million and as a percentage of sales increased by 0.6 percentage points. The increase in gross margin as a percentage of sales was primarily due to lower material costs, improved price realization, lower warranty costs and favorable product mix, which were partially offset by lower volumes, unfavorable foreign currency fluctuations and restructuring charges of $29 million.

The provision for warranties issued as a percentage of sales was 2.1 percent in both 2012 and 2011. 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 increased primarily due to higher consulting of $45 million, restructuring and other charges of $20 million and an increase of $19 million in compensation and related expenses, which were partially offset by reduced discretionary spending in the

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second half of the year. Higher compensation expense was primarily due to increased headcount to support our strategic growth initiatives launched prior to a number of markets unexpectedly slowing in mid-2012. Compensation and related expenses include salaries, fringe benefits and variable compensation. Variable compensation related to 2012 performance decreased $87 million over variable compensation related to 2011 performance. In the third quarter of 2012, we implemented a number of cost reduction initiatives to align our cost structure with the slowdown in demand at several of our key markets in the second half of the year. Overall, selling, general and administrative expenses, as a percentage of sales, increased to 11.0 percent in 2012 from 10.2 percent in 2011.

Research, Development and Engineering Expenses

Research, development and engineering expenses increased primarily due to an increase of $54 million in compensation and related expenses and increased consulting of $32 million. Higher compensation expense was primarily due to increased headcount to support our strategic growth initiatives. Compensation and related expenses include salaries, fringe benefits and variable compensation. Variable compensation related to 2012 performance decreased $25 million over variable compensation related to 2011 performance. Research, development and engineering expenses in 2012 also included restructuring and other charges of $3 million. Overall, research, development and engineering expenses, as a percentage of sales, increased to 4.2 percent in 2012 from 3.5 percent in 2011. Research activities continue to focus on development of new products to meet future emission standards around the world and improvements in fuel economy performance.

Equity, Royalty and Interest Income From Investees

Equity, royalty and interest income from investees decreased primarily due to the following:

In millions	**2012 vs. 2011 Increase/(Decrease)**	
Dongfeng Cummins Engine Company, Ltd. (DCEC)	$	(28)
Chongqing Cummins Engine Company, Ltd. (CCEC)		(7)
Beijing Foton Cummins Engine Co., Ltd. (BFCEC)		12
North American distributors		13
All other		(18)
Cummins share of net income		(28)
Royalty and interest income		(4)
Equity, royalty and interest income from investees	$	(32)

The decreases above were primarily due to lower sales in China at DCEC and CCEC, which were partially offset by growth in North American distributors and higher sales at BFCEC.

Gain on Sale of Businesses

In the second quarter of 2011, we sold certain assets and liabilities of our exhaust business which manufactures exhaust products and select components for emission systems for a variety of applications not core to our other product offerings. This business was historically included in our Components segment. The sales price was $123 million. We recognized a gain on the sale of $68 million ($37 million after-tax), which included a goodwill allocation of $19 million. The gain was excluded from segment results as it was not considered in our evaluation of operating results for the year ended December 31, 2011.

Sales for this business were $62 million and $171 million in 2011 (through closing) and 2010, respectively. Income before income taxes for this business were approximately $9 million and $22 million in 2011 (through closing) and 2010, respectively.

During the fourth quarter of 2011, we sold certain assets and liabilities of our light-duty filtration business which manufactures light-duty automotive and industrial filtration solutions. The sales price was $90 million and included a note receivable from the buyer of approximately $1 million. There are no earnouts or other contingencies associated with the sales price. We recognized a gain on the sale of $53 million ($33 million after-tax), which included a goodwill allocation of $6 million. The gain was excluded from segment results as it was not considered in our evaluation of operating results for the year ended December 31, 2011.

Sales for this business were $64 million and $74 million in 2011 (through closing) and 2010, respectively. Income before income taxes for this business were approximately $13 million and $9 million in 2011 (through closing) and 2010, respectively.

In the second quarter of 2012, we recorded an additional $6 million gain ($4 million after-tax) related to final purchase price adjustments for our 2011 divestitures. The gain was excluded from segment results as it was not considered in our evaluation of operating results for the year ended December 31, 2012.

Other Operating Income (Expense), Net

Other operating income (expense), net was as follows:

	Years ended December 31,	
In millions	**2012**	**2011**
Royalty income	**$ 18**	$ 12
Flood damage gain		38
Loss on sale of fixed assets	**(2)**	(10)
Royalty expense	**(3)**	(3)
Amortization of intangible assets	**(8)**	(5)
Legal matters	**(20)**	(5)
Other, net	**(1)**	(6)
Total other operating income (expense), net	**$ (16)**	$ 21

Interest Income

Interest income decreased primarily due to lower average investment balances in 2012 compared to 2011.

Interest Expense

Interest expense decreased primarily due to lower capitalized interest in 2011 and the termination of a capital lease in September 2011.

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Other Income (Expense), Net

Other income (expense), net was as follows:

In millions	Years ended December 31, 2012	2011
Gain on sale of equity investment	**$ 13**	$
Dividend income	**7**	7
Gain on fair value adjustment for consolidated investee(1)	**7**	
Change in cash surrender value of corporate owned life insurance	**5**	12
Gain on marketable securities, net	**3**	
Foreign currency losses, net	**(14)**	(14)
Bank charges	**(15)**	(16)
Other, net	**18**	11
Total other income (expense), net	**$ 24**	$

(1) See Note 2, "ACQUISITIONS AND DIVESTITURES," to the *Consolidated Financial Statements* for more details.

Income Tax Expense

Our income tax rates are generally less than the 35 percent U.S. statutory income tax rate primarily because of lower taxes on foreign earnings and research tax credits. Our effective tax rate for 2012 was 23.5 percent compared to 27.1 percent for 2011. Our 2012 income tax provision includes a one-time $134 million tax benefit resulting from transactions entered into and tax return elections made with respect to our U.K. operations. Our 2011 income tax provision includes a tax benefit of $48 million related to prior year refund claims filed for additional research tax credits, as well as additional foreign income and related foreign tax credits, net of related tax reserves. Our effective tax rate for 2011 also includes a tax benefit of $19 million related to the release of deferred U.S. tax liabilities on certain foreign earnings, as a result of restructuring our foreign operations. Also included in 2011 is a tax benefit of $16 million resulting from the reduction of our unrecognized tax benefits primarily due to settlements with taxing authorities. The 2011 income tax provision also includes other tax items totaling to a $2 million net tax charge, primarily relating to the enactment of state law changes in Indiana and changes in the U.K. as well as adjustments to our income tax accounts based on our 2010 tax return filings.

On January 2, 2013, the American Taxpayer Relief Act of 2012 was enacted. This legislation retroactively extended the U.S. federal research credit for two years, from January 1, 2012, through December 31, 2013. We expect our 2013 effective tax rate, which will include an estimated 1 percent benefit for the 2013 research credit, to be 26 percent excluding any one-time items that may arise. Additionally, we anticipate that our first quarter 2013 results will include a one-time tax benefit of approximately $28 million representing the net benefit attributable to the 2012 research credit. Earnings of our China operations generated after December 31, 2011, are considered to be permanently reinvested and additional U.S. deferred tax is no longer being provided on these earnings generated after 2011. We have $702 million of retained earnings and related cumulative translation adjustments in our China operations generated prior to December 31, 2011 and have provided a U.S. deferred tax liability of $158 million relating to these earnings and related translation adjustments. We anticipate that these earnings will be distributed to the U.S. within the next five years.

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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 decreased primarily due to a decline of $5 million at Wuxi Cummins Turbo Technologies Co. Ltd., $3 million at Cummins Western Canada LP. and $3 million at Power Systems India. The decreases were partially offset by an increase of $6 million at Cummins Power Solutions Ltd. and $2 million at Cummins Central Power LLC.

Net Income Attributable to Cummins Inc. and Diluted Earnings Per Share Attributable to Cummins Inc.

Net income and diluted earnings per share attributable to Cummins Inc. decreased primarily due to lower volumes, particularly in the international construction and medium-duty truck markets, higher research, development and engineering expenses, higher selling, general and administrative expenses and lower equity, royalty and interest income from investees. These decreases were partially offset by improved gross margin as a percentage of sales and a lower effective tax rate of 23.5 percent versus 27.1 percent in 2011. In addition, the significant gains we recorded in 2011 for the disposition of certain asset and liabilities of our exhaust business and light-duty filtration business and flood damage recoveries from the insurance settlement regarding a June 2008 flood in Southern Indiana did not repeat in 2012. Diluted earnings per share for 2012 also benefited $0.06 from lower shares primarily due to the stock repurchase program.

2011 vs. 2010

Net Sales

Sales increased in all segments primarily due to increased demand from most markets including recovery of the North American on-highway markets. The primary drivers for the increase in sales were:

- Engine segment sales increased by 43 percent due to increased demand in all lines of business led by heavy-duty truck, industrial and medium-duty truck and bus businesses.

- Components segment sales increased by 33 percent due to increased demand in all lines of business led by emission solutions and turbo technologies businesses.

- Power Generation segment sales increased by 20 percent due to increased demand in all lines of business led by commercial products and generator technologies businesses and improved price realization.

- Distribution segment sales increased by 31 percent due to increased demand in all product lines and all geographic regions led by Asia Pacific, North and Central America, Europe and Middle East regions.

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

Sales to international markets were 56 percent of total net sales in 2011, compared with 60 percent of total net sales in 2010.

Gross Margin

Gross margin increased by $1,421 million and as a percentage of sales increased by 1.4 percentage points. The significant improvement was led by increases in volume, improved price realization, higher product content on certain products and favorable currency impacts, partially offset by higher material costs, higher commodity costs and higher base warranty costs due to increased volumes and increasing

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mix of EPA 2010 products. Gross margin in 2010 also benefited from a one-time $32 million tax recovery in Brazil. See Note 14, "COMMITMENTS AND CONTINGENCIES," in our *Consolidated Financial Statements* for more information.

The provision for warranties issued as a percentage of sales in 2011 was 2.1 percent compared to 3.0 percent in 2010. Accrual rates for engines sold this year were generally lower than the rates charged in prior years as our warranty costs for EPA 2010 products have been lower than expected. 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 increased primarily due to an increase of $174 million in compensation and related expenses including increased headcount to support our strategic growth initiatives, merit increases and increased discretionary spending. Compensation and related expenses include salaries, fringe benefits and variable compensation. Variable compensation related to 2011 performance increased $42 million over variable compensation related to 2010 performance. Overall, selling, general and administrative expenses, as a percentage of sales, decreased from 11.2 percent in 2010 to 10.2 percent in 2011.

Research, Development and Engineering Expenses

Research, development and engineering expenses increased primarily due to an increase of $79 million in compensation and related expenses, an increase in the number of engineering programs with increased costs of $79 million and increased discretionary spending. Compensation and related expenses include salaries, fringe benefits and variable compensation. Variable compensation related to 2011 performance increased $8 million over variable compensation related to 2010 performance. Overall, research, development and engineering expenses, as a percentage of sales, increased to 3.5 percent in 2011 from 3.1 percent in 2010. Research activities continue to focus on development of new products to meet future emission standards around the world and improvements in fuel economy performance.

Equity, Royalty and Interest Income From Investees

Equity, royalty and interest income from investees increased primarily due to the following:

In millions		**2011 vs. 2010 Increase/(Decrease)**
North American distributors	$	33
Chongqing Cummins Engine Company, Ltd.		22
Beijing Foton Cummins Engine Co., Ltd.		9
Dongfeng Cummins Engine Company, Ltd.		(19)
All other		9
Cummins share of net income		54
Royalty and interest income		11
Equity, royalty and interest income from investees	$	65

These overall increases were primarily due to the economic recovery in North America, particularly in the oil and gas markets, and strong demand for power generation and mining products in China with CCEC, which was partially offset by lower sales at DCEC due to weaker demand in the on-highway truck market.

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Gain on Sale of Businesses

In the second quarter of 2011, we sold certain assets and liabilities of our exhaust business which manufactures exhaust products and select components for emission systems for a variety of applications not core to our other product offerings. This business was historically included in our Components segment. The sales price was $123 million. We recognized a gain on the sale of $68 million ($37 million after-tax), which included a goodwill allocation of $19 million. The gain was excluded from segment results as it was not considered in our evaluation of operating results for the year ended December 31, 2011.

Sales for this business were $62 million, $171 million and $126 million in 2011 (through closing), 2010 and 2009, respectively. Income before income taxes for this business were approximately $9 million, $22 million and $11 million in 2011 (through closing), 2010 and 2009, respectively.

During the fourth quarter of 2011, we sold certain assets and liabilities of our light-duty filtration business which manufactures light-duty automotive and industrial filtration solutions. The sales price was $90 million and included a note receivable from the buyer of approximately $1 million. There are no earnouts or other contingencies associated with the sales price. We recognized a gain on the sale of $53 million ($33 million after-tax), which included a goodwill allocation of $6 million. The gain was excluded from segment results as it was not considered in our evaluation of operating results for the year ended December 31, 2011.

Sales for this business were $64 million, $74 million and $54 million in 2011 (through closing), 2010 and 2009, respectively. Income before income taxes for this business were approximately $13 million, $9 million and $2 million in 2011 (through closing), 2010 and 2009, respectively.

We have entered into supply and other agreements with the operations that represent ongoing involvement and as such, the results of these operations have not been presented as discontinued operations.

Other Operating Income (Expense), Net

Other operating income (expense), net was as follows:

	Years ended December 31,	
In millions	**2011**	**2010**
Flood damage gain (loss)	**$ 38**	$ (2)
Royalty income	**12**	10
Royalty expense	**(3)**	(3)
Amortization of intangible assets	**(5)**	(15)
Legal matters	**(5)**	
Loss on sale of fixed assets	**(10)**	(4)
Other, net	**(6)**	(2)
Total other operating income (expense), net	**$ 21**	$ (16)

In June 2008, four of our sites in Southern Indiana, including our Technical Center, experienced extensive flood damage. In October 2011, we received $40 million from our insurance carriers to settle all outstanding 2008 flood claims. As a result, we recognized a gain of approximately $38 million ($24 million after-tax), net of any remaining flood related expenses, in "Other operating income (expense), net" in our *Consolidated Statements of Income*.

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Interest Income

Interest income increased primarily due to higher average cash balances in addition to higher average interest rates.

Interest Expense

Interest expense increased primarily due to lower capitalized interest in 2011 and higher average debt, partially offset by lower interest rates.

Other Income (Expense), Net

Other income (expense) was as follows:

	Years ended December 31,	
In millions	**2011**	**2010**
Change in cash surrender value of corporate owned life insurance	**$ 12**	$ 12
Dividend income	**7**	7
Gain on fair value adjustment for Cummins Western Canada		12
Life insurance proceeds		7
Foreign currency losses, net	**(14)**	(1)
Bank charges	**(16)**	(15)
Other, net	**11**	12
Total other income (expense), net	**$**	$ 34

Income Tax Expense

Our income tax rates are generally less than the 35 percent U.S. statutory income tax rate primarily because of lower taxes on foreign earnings and research tax credits. Our effective tax rate for 2011 was 27.1 percent compared to 29.5 percent for 2010. Our 2011 income tax provision includes a tax benefit of $48 million related to prior year refund claims filed for additional research tax credits, as well as additional foreign income and related foreign tax credits, net of related tax reserves. Our effective tax rate for 2011 also includes a tax benefit of $19 million related to the release of deferred U.S. tax liabilities on certain foreign earnings, as a result of restructuring our foreign operations. Also included in 2011 is a tax benefit of $16 million resulting from the reduction of our unrecognized tax benefits primarily due to settlements with taxing authorities. The 2011 income tax provision also includes other tax items totaling to a $2 million net tax charge, primarily relating to the enactment of state law changes in Indiana and changes in the U.K. as well as adjustments to our income tax accounts based on our 2010 tax return filings. Our 2010 income tax provision includes a $17 million reduction in the fourth quarter related to the legislative reinstatement of the U.S. research tax credit as well as a $3 million tax benefit related to the release of deferred U.S. tax liabilities on foreign earnings now considered to be permanently reinvested outside of the U.S.

Noncontrolling Interests

Noncontrolling interests in income of consolidated subsidiaries decreased primarily due to a decline of $9 million at Wuxi Cummins Turbo Technologies Co. Ltd. and $4 million at Cummins India Ltd., a publicly traded company on various exchanges in India. These decreases were partially offset by an increase of $6 million at Cummins Western Canada LP, $4 million at Cummins Power Systems LLC and $1 million at Cummins Northeast LLC.

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Net Income Attributable to Cummins Inc. and Diluted Earnings Per Share Attributable to Cummins Inc.

Net income and diluted earnings per share attributable to Cummins Inc. increased primarily due to higher volumes in most markets and geographic regions, including the recovery of the North American on-highway truck markets, significantly improved gross margins, the gain on disposition of certain assets and liabilities of our exhaust business and our light-duty filtration business, a lower effective tax rate, increased equity income and the gain related to flood damage recoveries from the insurance settlement regarding a June 2008 flood in Southern Indiana. These favorable drivers were partially offset by higher selling, general and administrative expenses and research, development and engineering expenses in 2011 as compared to 2010. Diluted earnings per share for 2011 also benefited $0.17 from lower shares primarily due to the stock repurchase program.

RESTRUCTURING AND OTHER CHARGES

We have executed restructuring actions primarily in the form of involuntary separation programs in the fourth quarter of 2012. These actions were in response to deterioration in our U.S. businesses and most key markets around the world in the second half of 2012, as well as a reduction in orders in most U.S. and global markets for 2013. We reduced our worldwide professional workforce by approximately 650 employees, or 3 percent. We also reduced our hourly workforce by approximately 650 employees. During 2012, we incurred a pre-tax charge related to the professional and hourly workforce reductions of approximately $49 million.

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 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.

We incurred a $1 million charge for lease terminations and a $2 million charge for asset impairments and other non-cash charges. During 2012, we recorded restructuring and other charges of $52 million ($35 million after-tax). These restructuring actions included:

In millions	Year ended December 31, 2012
Workforce reductions	$ 49
Exit activities	1
Other	2
Restructuring and other charges	$ 52

If the 2012 restructuring actions are successfully implemented, we expect the annualized savings from the professional actions to be approximately $39 million. Our charge related to the professional actions was approximately $32 million. Approximately 32 percent of the savings from the restructuring actions will be realized in cost of sales, 53 percent in selling, general and administrative expenses and 15 percent in research, development and engineering expenses. We expect the accrual to be paid in cash which will be funded with cash generated from operations.

At December 31, 2012, of the approximately 1,300 employees to be affected by this plan, 1,130 had been terminated.

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Restructuring and other charges were included in each segment in our operating results as follows:

In millions	Year ended December 31, 2012
Engine	$ 20
Distribution	14
Power Generation	12
Components	6
Restructuring and other charges	$ 52

The table below summarizes the activity and balance of accrued restructuring charges, which is included in "Other accrued expenses" in our *Consolidated Balance Sheets* for the year ended December 31, 2012.

In millions	Charges	Payments	Accrued Balance at December 31, 2012
Restructuring charges(1)	$ 50	$ 25	$ 25

(1) Restructuring charges include severance pay and benefits and related charges and lease termination costs.

The table below summarizes where the restructuring and other charges are located in our *Consolidated Statements of Income* for the year ended December 31, 2012.

In millions	Year ended December 31, 2012
Cost of sales	$ 29
Selling, general and administrative expenses	20
Research, development and engineering expenses	3
Restructuring and other charges	$ 52

OPERATING SEGMENT RESULTS

Our reportable operating segments consist of the following: Engine, Components, Power Generation and Distribution. This reporting structure is organized according to the products and markets each segment serves and 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. Our engines are used in trucks of all sizes, buses and recreational vehicles, as well as in various industrial applications, including construction, mining, agriculture, marine, oil and gas, rail and military equipment. The Components segment sells filtration products, aftertreatment, turbochargers and fuel systems. The Power Generation segment is an integrated provider of power systems which sells engines, generator sets and alternators. 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.

We use segment EBIT (defined as earnings before interest expense, taxes and noncontrolling interests) as a primary basis for the chief operating decision-maker to evaluate the performance of each of our operating segments. Segment amounts exclude certain expenses not specifically identifiable to segments.

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The accounting policies of our operating segments are the same as those applied in our *Consolidated Financial Statements*. We prepared the financial results of our operating segments on a basis that is consistent with the manner in which we internally disaggregate financial information to assist in making internal operating decisions. We have allocated certain common costs and expenses, primarily corporate functions, among segments differently than we would for stand-alone financial information prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). These include certain costs and expenses of shared services, such as information technology, human resources, legal and finance. We also do not allocate debt-related items, actuarial gains or losses, prior service costs or credits, changes in cash surrender value of corporate owned life insurance, flood damage gains or losses, divestiture gains or losses or income taxes to individual segments. In 2012, non-segment items included a $20 million reserve ($12 million after-tax) related to legal matters and a $6 million gain related to adjustments from our 2011 divestitures, while 2011 included the gain on disposition of certain assets and liabilities of our exhaust business and our light-duty filtration business and 2010 included a Brazil revenue tax recovery. These gains were not allocated to the businesses as they were not considered in our evaluation of operating results for the year. Segment EBIT may not be consistent with measures used by other companies.

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:

				Favorable/(Unfavorable)			
	Years ended December 31,			2012 vs. 2011		2011 vs. 2010	
In millions	**2012**	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
External sales	**$ 9,101**	$ 9,649	$ 6,594	$ (548)	(6)%	$ 3,055	46%
Intersegment sales	**1,632**	1,658	1,294	(26)	(2)%	364	28%
Total sales	**10,733**	11,307	7,888	(574)	(5)%	3,419	43%
Depreciation and amortization	**192**	181	171	(11)	(6)%	(10)	(6)%
Research, development and engineering expenses	**433**	397	263	(36)	(9)%	(134)	(51)%
Equity, royalty and interest income from investees	**127**	166	161	(39)	(23)%	5	3%
Interest income	**11**	18	12	(7)	(39)%	6	50%
Segment EBIT	**1,248**	1,384	809	(136)	(10)%	575	71%

				Percentage Points	Percentage Points
Segment EBIT as a percentage of total sales	**11.6%**	12.2%	10.3%	(0.6)	1.9

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Engine segment sales by market were as follows:

				Favorable/(Unfavorable)			
	Years ended December 31,			2012 vs. 2011		2011 vs. 2010	
In millions	**2012**	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
Heavy-duty truck	**$ 2,964**	$ 2,791	$ 1,503	$ 173	6%	$ 1,288	86%
Medium-duty truck and bus	**2,091**	2,320	1,435	(229)	(10)%	885	62%
Light-duty automotive and RV	**1,279**	1,176	1,022	103	9%	154	15%
Total on-highway	**6,334**	6,287	3,960	47	1%	2,327	59%
Industrial	**3,233**	3,850	2,889	(617)	(16)%	961	33%
Stationary power	**1,166**	1,170	1,039	(4)		131	13%
Total sales	**$ 10,733**	$ 11,307	$ 7,888	$ (574)	(5)%	$ 3,419	43%

Unit shipments by engine classification (including unit shipments to Power Generation) were as follows:

				Favorable/(Unfavorable)			
	Years ended December 31,			2012 vs. 2011		2011 vs. 2010	
	2012	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
Mid-range	**440,500**	509,400	368,900	(68,900)	(14)%	140,500	38%
Heavy-duty	**119,100**	116,300	61,200	2,800	2%	55,100	90%
High-horsepower	**19,800**	21,600	18,500	(1,800)	(8)%	3,100	17%
Total unit shipments	**579,400**	647,300	448,600	(67,900)	(10)%	198,700	44%

2012 vs. 2011

Sales

Engine segment sales decreased versus 2011 due to lower demand in the industrial and medium-duty truck and bus businesses, partially offset by growth in the heavy-duty truck and light-duty automotive and RV businesses. The following are the primary drivers by market:

- Industrial market sales decreased primarily due to a 53 percent decline in construction engine shipments in international markets, including a 72 percent decline in China, and a 44 percent decline in engine shipments to the North American oil and gas markets due to weakened natural gas prices, which were partially offset by a 4 percent increase in engine shipments in the North American construction market.

- Medium-duty truck and bus sales decreased primarily due to lower demand in the Brazilian truck market due to pre-buy activity in the second half of 2011 ahead of the implementation of Euro V emission regulations in the first quarter of 2012 and one of our customers replacing our B6.7 engine with a proprietary engine in 2012. The B6.7 engine replacement was partially offset by the 2012 launch of our ISF and 9 liter engines in new light-duty on-highway and medium-duty truck applications, respectively, with this same customer. The decrease was further offset by improved demand in North American markets.

The decreases above were partially offset by the following:

- Heavy-duty truck engine sales increased due to growth in the North American on-highway markets in the first half of the year, primarily as a result of the replacement of aging fleets.

Light-duty automotive and RV sales increased primarily due to a 37 percent improvement in units shipped to Chrysler.

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Total on-highway-related sales for 2012 were 59 percent of total engine segment sales, compared to 56 percent in 2011.

Segment EBIT

Engine segment EBIT decreased versus 2011, primarily due to lower gross margin, lower equity, royalty and interest income from investees, higher research, development and engineering expenses and higher selling, general and administrative expenses. Engine segment EBIT for 2012 included restructuring and other charges of $20 million in the fourth quarter. Changes in Engine segment EBIT and EBIT as a percentage of sales were as follows:

	Year ended December 31, 2012 vs. 2011 Favorable/(Unfavorable) Change		
In millions	**Amount**	**Percent**	**Percentage point change as a percent of sales**
Gross margin	$ (82)	(3)%	0.3
Selling, general and administrative expenses	(8)	(1)%	(0.4)
Research, development and engineering expenses	(36)	(9)%	(0.5)
Equity, royalty and interest income from investees	(39)	(23)%	(0.3)

The decrease in gross margin versus 2011 was primarily due to lower volumes and restructuring and other charges, which was partially offset by improved price realization, lower material costs, favorable product mix and improved product coverage. The increase in selling, general and administrative expenses was primarily due to increased headcount to support our strategic growth initiatives launched prior to a number of markets unexpectedly slowing in mid-2012, partially offset by decreased variable compensation expense. The increase in research, development and engineering expenses was primarily due to new product development spending and increased headcount to support our strategic growth initiatives. The decrease in equity, royalty and interest income from investees was primarily due to weaker demand for on-highway products at DCEC.

2011 vs. 2010

Sales

Engine segment sales increased in all businesses versus 2010, as demand improved in most markets including a significant rebound in North American on-highway markets, improvements in international construction markets, increased demand in global mining markets and significant increases in oil and gas markets. The following are the primary drivers by market:

- Heavy-duty truck engine sales increased due to recovery in North American on-highway markets as OEM customers replaced their aging fleets and the depletion of transition engine inventory purchased in 2009 in advance of the EPA's 2010 emission standard changes.

- Industrial market sales increased primarily due to a 26 percent improvement in international construction engine shipments driven by the economic recovery and infrastructure improvements in certain emerging markets, increased demand in advance of off-highway emission regulations in the U.S. and Europe, a 46 percent increase in units sold in the global mining engine markets due to increased coal and commodity demands and more than double the number of oil and gas engine shipments in North America.

- Medium-duty truck and bus sales increased primarily due to the recovery in North American on-highway markets, the depletion of transition engine inventory purchased in 2009 in advance of the EPA's 2010 emissions change and higher demand in the Brazilian truck engine market driven by a growing economy.

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Total on-highway-related sales for 2011 were 56 percent of total engine segment sales, compared to 50 percent in 2010.

Segment EBIT

Engine segment EBIT increased significantly versus 2010, primarily due to higher gross margin, partially offset by increased selling, general and administrative expenses and research, development and engineering expenses. Changes in Engine segment EBIT and EBIT as a percentage of sales were as follows:

	Year ended December 31, 2011 vs. 2010 Favorable/(Unfavorable) Change		
In millions	**Amount**	**Percent**	**Percentage point change as a percent of sales**
Gross margin	$ 864	55%	1.7
Selling, general and administrative expenses	(142)	(22)%	1.2
Research, development and engineering expenses	(134)	(51)%	(0.2)
Equity, royalty and interest income from investees	5	3%	(0.5)

The increase in gross margin versus 2010 was primarily due to higher volumes, improved price realization and favorable mix, partially offset by higher commodity costs and higher base warranty costs due to increased volumes and increasing mix of EPA 2010 products. Although our warranty costs increased, our warranty cost as a percentage of sales decreased as actual accrual rates for engines sold this year were generally lower than rates charged in prior years as our warranty costs for EPA 2010 engines have been lower than expected. The increases in selling, general and administrative expenses and research, development and engineering expenses were primarily due to new product development spending and increased headcount to support our strategic growth initiatives. The increase in equity, royalty and interest income from investees was primarily due to strong demand for power generation and mining products in China with CCEC and strong export sales to Russia and Brazil in the midrange on-highway market with Beijing Foton Cummins Engine Co., Ltd., which was partially offset by lower sales at DCEC due to weaker demand in the on-highway heavy-duty and medium-duty truck market in China.

Components Segment Results

Financial data for the Components segment was as follows:

				Favorable/(Unfavorable)			
	Years ended December 31,			2012 vs. 2011		2011 vs. 2010	
In millions	**2012**	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
External sales	**$ 2,809**	$ 2,886	$ 2,171	$ (77)	(3)%	$ 715	33%
Intersegment sales	**1,203**	1,177	875	26	2%	302	35%
Total sales	**4,012**	4,063	3,046	(51)	(1)%	1,017	33%
Depreciation and amortization	**82**	73	79	(9)	(12)%	6	8%
Research, development and engineering expenses	**213**	175	114	(38)	(22)%	(61)	(54)%
Equity, royalty and interest income from investees	**29**	31	23	(2)	(6)%	8	35%
Interest income	**3**	5	2	(2)	(40)%	3	NM
Segment EBIT	**426**	470	278	(44)	(9)%	192	69%

				Percentage Points	**Percentage Points**
Segment EBIT as a percentage of total sales	**10.6%**	11.6%	9.1%	(1.0)	2.5

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Acquisition

In April 2012, we reached an agreement to acquire the doser technology and business assets from Hilite in a cash transaction. Dosers are products that enable compliance with emission standards in certain aftertreatment systems and complement our current product offerings. The transaction was approved by German regulators in June and closed on July 18, 2012. The purchase price was $176 million. There was no contingent consideration associated with this transaction. During 2012 we expensed approximately $4 million of acquisition related costs. See Note 2, "ACQUISITIONS AND DIVESTITURES," to the *Consolidated Financial Statements* for more details.

Sales for our Components segment by business were as follows:

				Favorable/(Unfavorable)			
	Years ended December 31,			2012 vs. 2011		2011 vs. 2010	
In millions	**2012**	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
Emission solutions excluding acquisition	**$ 1,369**	$ 1,262	$ 750	$ 107	8%	$ 512	68%
Acquisition	**46**			46	100%		
Total emission solutions	**1,415**	1,262	750	153	12%	512	68%
Turbo technologies	**1,106**	1,223	948	(117)	(10)%	275	29%
Filtration	**1,048**	1,113	1,011	(65)	(6)%	102	10%
Fuel systems	**443**	465	337	(22)	(5)%	128	38%
Total sales	**$ 4,012**	$ 4,063	$ 3,046	$ (51)	(1)%	$ 1,017	33%

Excluding Acquisition

Selected financial information for our Components segment excluding the impact of the acquisition was as follows:

				Favorable/(Unfavorable)			
	Years ended December 31,			2012 vs. 2011		2011 vs. 2010	
In millions	**2012**	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
Excluding acquisition							
Sales	**$ 3,966**	$ 4,063	$ 3,046	$ (97)	(2)%	$ 1,017	33%
Segment EBIT	**434**	470	278	(36)	(8)%	192	69%

				Percentage Points	Percentage Points
Segment EBIT as a percentage of total sales	**10.9%**	11.6%	9.1%	(0.7)	2.5

2012 vs. 2011

Sales

Components segment sales, excluding the acquisition, decreased versus 2011. The following are the primary drivers:

Turbo technologies business sales decreased primarily due to a decline in OEM sales in Europe and China, reduced aftermarket demand and unfavorable foreign currency fluctuations, which were partially offset by higher OEM demand in North America in the first half of the year.

Foreign currency fluctuations unfavorably impacted sales results.

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Filtration business sales decreased primarily as a result of the disposition of certain assets and liabilities of our light-duty filtration business and our exhaust business in 2011 and unfavorable foreign currency fluctuations. Disposition related sales were $71 million in 2011. The decreases were partially offset by increased aftermarket demand in the first half of the year.

Fuel systems business sales decreased primarily due to lower European demand and reduced aftermarket demand, which were partially offset by improved demand in North American on-highway markets in the first half of the year.

The decreases above were partially offset by the emission solutions business as sales increased primarily due to higher demand in the North American on-highway market in the first half of the year and new sales in the Brazilian on-highway market as the result of new emission requirements effective January 1, 2012, partially offset by lower sales due to the disposition of certain assets and liabilities of our exhaust business in the second quarter of 2011, lower price realization and unfavorable foreign currency fluctuations. Disposition related sales were $55 million in 2011.

Segment EBIT

Components segment EBIT decreased versus 2011, primarily due to higher research, development and engineering expenses. Components segment EBIT for 2012 included restructuring and other charges of $6 million in the fourth quarter. Changes in Components segment EBIT and EBIT as a percentage of sales were as follows:

	Year ended December 31, 2012 vs. 2011 Favorable/(Unfavorable) Change		
In millions	**Amount**	**Percent**	**Percentage point change as a percent of sales**
Including acquisition			
Gross margin	$ (3)		0.2
Selling, general and administrative expenses	(4)	(1)%	(0.2)
Research, development and engineering expenses	(38)	(22)%	(1.0)
Equity, royalty and interest income from investees	(2)	(6)%	(0.1)
Excluding acquisition			
Gross margin	(3)		0.4
Selling, general and administrative expenses	(1)		(0.2)
Research, development and engineering expenses	(35)	(20)%	(1.0)

Segment EBIT Excluding Acquisition

The decrease in gross margin versus 2011 was primarily due to lower price realization, unfavorable foreign currency fluctuations, the disposition of certain assets and liabilities of our exhaust business and our light-duty filtration business in 2011 and restructuring and other charges, partially offset by higher volumes, particularly in the emission solutions business, lower material costs and improved product coverage. The increase in selling, general and administrative expenses was primarily due to increased headcount to support our strategic growth initiatives launched prior to a number of markets unexpectedly slowing in mid-2012, partially offset by decreased variable compensation expense and lower discretionary spending in the second half of 2012. The increase in research, development and engineering expenses was primarily due to new product development spending and increased headcount to support our strategic growth initiatives.

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2011 vs. 2010

Sales

Components segment sales increased in all businesses versus 2010. The following are the primary regional drivers by business:

- Emission solutions business sales increased due to the increased sales volume of North American EPA 2010 aftertreatment systems and increased demand for Euro V aftertreatment systems in Europe, which were partially offset by lower sales due to the sale of the exhaust business.

- Turbo technologies business sales increased due to higher OEM demand in North America, Europe, India and Brazil and improved aftermarket demand.

- Fuel systems business sales increased primarily due to improved demand in North American on-highway markets.

- Filtration business sales increased due to improved aftermarket demand, especially in Asia Pacific and Europe, higher OEM demand due to the recovery in North American on-highway markets and favorable foreign currency impacts which were partially offset by lower sales due to the disposition of certain assets and liabilities of our exhaust and light-duty filtration businesses.

Segment EBIT

Components segment EBIT increased versus 2010, primarily due to the improved gross margin which was partially offset by increased research, development and engineering expenses and higher selling, general and administrative expenses. Changes in Components segment EBIT and EBIT as a percentage of sales were as follows:

	Year ended December 31, 2011 vs. 2010 Favorable/(Unfavorable) Change		
In millions	**Amount**	**Percent**	**Percentage point change as a percent of sales**
Gross margin	$ 295	51%	2.5
Selling, general and administrative expenses	(44)	(19)%	0.8
Research, development and engineering expenses	(61)	(54)%	(0.6)
Equity, royalty and interest income from investees	8	35%	

The increase in gross margin was primarily due to higher volumes for all businesses and increased product content on 2010 North American truck engines. The increases in research, development and engineering expenses and selling, general and administrative expenses were primarily due to new product development spending and increased headcount to support our strategic growth initiatives. The increase in equity, royalty and interest income from investees was driven by improved joint venture income from both the filtration business in China and India and the fuel systems business.

In 2011, we sold certain assets and liabilities of our exhaust business and light-duty filtration business and recognized $68 million and $53 million, respectively, in pre-tax gain on the sales. The gains have been excluded from Components results as they were not considered in our evaluation of Components operating results for the year ended 2011. See Note 2, "ACQUISITIONS AND DIVESTITURES," to the *Consolidated Financial Statements.*

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Power Generation Segment Results

Financial data for the Power Generation segment was as follows:

	Years ended December 31,			Favorable/(Unfavorable) 2012 vs. 2011		2011 vs. 2010	
In millions	**2012**	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
External sales	**$ 2,163**	$ 2,492	$ 2,150	$ (329)	(13)%	$ 342	16%
Intersegment sales	**1,105**	1,006	769	99	10%	237	31%
Total sales	**3,268**	3,498	2,919	(230)	(7)%	579	20%
Depreciation and amortization	**47**	42	41	(5)	(12)%	(1)	(2)%
Research, development and engineering expenses	**76**	54	36	(22)	(41)%	(18)	(50)%
Equity, royalty and interest income from investees	**40**	47	35	(7)	(15)%	12	34%
Interest income	**9**	8	5	1	13%	3	60%
Segment EBIT	**285**	373	299	(88)	(24)%	74	25%

				Percentage Points	Percentage Points
Segment EBIT as a percentage of total sales	**8.7%**	10.7%	10.2%	(2.0)	0.5

In the first quarter of 2012, our Power Generation segment reorganized its reporting structure to include the following businesses:

Power products Our power products business manufactures generators for commercial and consumer applications ranging from two kilowatts (kW) to one megawatt (MW) under the Cummins Power Generation and Cummins Onan brands.

Power systems Our power systems business manufactures and sells diesel fuel-based generator sets over one MW, paralleling systems and transfer switches for critical protection and distributed generation applications. We also offer integrated systems that consist of generator sets, power transfer and paralleling switchgear for applications such as data centers, health care facilities and waste water treatment plants.

Generator technologies Our generator technologies business designs, manufactures, sells and services A/C generator/alternator products internally as well as to other generator set assemblers. Our products are sold under the Stamford, AVK and Markon brands and range in output from 0.6 kilovolt-amperes (kVA) to 30,000 kVA.

Power solutions Our power solutions business provides natural gas fuel-based turnkey solutions for distributed generation and energy management applications in the range of 300-2000 kW products. The business also serves the oil and gas segment and a global rental account for diesel and gas generator sets.

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Sales for our Power Generation segment by business (including 2011 and 2010 reorganized balances) were as follows:

	Years ended December 31,			Favorable/(Unfavorable)			
				2012 vs. 2011		2011 vs. 2010	
In millions	2012	2011	2010	Amount	Percent	Amount	Percent
Power products	**$ 1,654**	$ 1,636	$ 1,465	$ 18	1%	$ 171	12%
Power systems	**757**	815	616	(58)	(7)%	199	32%
Generator technologies	**566**	673	550	(107)	(16)%	123	22%
Power solutions	**291**	374	288	(83)	(22)%	86	30%
Total sales	**$ 3,268**	$ 3,498	$ 2,919	$ (230)	(7)%	$ 579	20%

2012 vs. 2011

Sales

Power Generation segment sales decreased versus 2011, primarily due to lower demand in the generator technologies, power solutions and power systems businesses. The following are the primary drivers by business:

Generator technologies sales decreased primarily due to demand reductions in Europe and Asia and unfavorable foreign currency fluctuations.

Power solutions sales decreased primarily due to lower volumes in Europe, Africa, Russia and Asia.

Power systems sales decreased primarily due to lower volumes in the Middle East, North America and Latin America and unfavorable foreign currency fluctuations, which were partially offset by stronger demand in Asia and improved price realization.

The decreases above were partially offset by power products as sales increased primarily due to higher volumes in North America and Western Europe and improved price realization. These increases were partially offset by demand reductions in China, the U.K., Latin America and Eastern Europe and unfavorable foreign currency fluctuations.

Segment EBIT

Power Generation segment EBIT decreased versus 2011, primarily due to lower gross margin, higher research, development and engineering expenses, lower equity, royalty and interest income from investees and higher selling, general and administrative expenses. Power Generation segment EBIT for 2012 included restructuring and other charges of $12 million in the fourth quarter. Changes in Power Generation segment EBIT and EBIT as a percentage of sales were as follows:

	Year ended December 31, 2012 vs. 2011 Favorable/(Unfavorable) Change		
In millions	Amount	Percent	Percentage point change as a percent of sales
Gross margin	$ (60)	(9)%	(0.4)
Selling, general and administrative expenses	(6)	(2)%	(0.8)
Research, development and engineering expenses	(22)	(41)%	(0.8)
Equity, royalty and interest income from investees	(7)	(15)%	(0.1)

The decrease in gross margin versus 2011 was due to lower volumes, unfavorable foreign currency fluctuations, higher material costs, increased product coverage and restructuring and other charges,

which were partially offset by improved price realization. The increase in selling, general and administrative expenses was primarily due to increased headcount to support our strategic growth initiatives, partially offset by lower discretionary spending in the second half of 2012 to align with slowing demand in key markets. The increase in research, development and engineering expenses was primarily due to increased headcount to support our strategic growth initiatives and new product development spending. Equity, royalty and interest income from investees decreased primarily due to lower profitability at Cummins Olayan and CCEC.

2011 vs. 2010

Sales

Power Generation segment sales increased in all businesses, versus 2010, primarily due to increased demand in the power systems, power products and generator technologies businesses. The following are the primary drivers by business:

Power systems sales increased due to stronger demand in North America, the Middle East, China and Latin American markets and improved price realization.

Power products sales increased due to stronger demand in most regions, particularly in Asia, North America, the Middle East and Latin America, improved price realization, new product introductions and favorable foreign currency impacts.

Generator technologies sales increased due to improved price realization, stronger demand in most regions, especially Western Europe, Asia and the U.K., and favorable foreign currency impacts.

Power solutions sales increased due to our largest customer expanding its gas genset rental fleet and overall general market growth in the power solutions business mainly in Europe, the Middle East and Africa.

Segment EBIT

Power Generation segment EBIT increased versus 2010, primarily due to higher gross margins, partially offset by higher selling, general and administrative expenses and research, development and engineering expenses. Changes in Power Generation segment EBIT and EBIT as a percentage of sales were as follows:

	Year ended December 31, 2011 vs. 2010 Favorable/(Unfavorable) Change		
In millions	**Amount**	**Percent**	**Percentage point change as a percent of sales**
Gross margin	$ 135	25%	0.7
Selling, general and administrative expenses	(56)	(22)%	(0.2)
Research, development and engineering expenses	(18)	(50)%	(0.3)
Equity, royalty and interest income from investees	12	34%	0.1

The increase in gross margin was due to higher volumes and improved price realization, which was partially offset by increased commodity and material costs. The increases in selling, general and administrative expenses and research, development and engineering expenses were primarily due to increased headcount to support our strategic growth initiatives. Equity, royalty and interest income from investees increased at CCEC primarily as a result of improved power generation markets in China.

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Distribution Segment Results

Financial data for the Distribution segment was as follows:

				Favorable/(Unfavorable)			
	Years ended December 31,			2012 vs. 2011		2011 vs. 2010	
In millions	**2012**	**2011**	**2010**	**Amount**	**Percent**	**Amount**	**Percent**
External sales	**$ 3,261**	$ 3,021	$ 2,311	$ 240	8%	$ 710	31%
Intersegment sales	**16**	23	13	(7)	(30)%	10	77%
Total sales	**3,277**	3,044	2,324	233	8%	720	31%
Depreciation and amortization	**34**	25	25	(9)	(36)%		
Research, development and engineering expenses	**6**	3	1	(3)	(100)%	(2)	NM
Equity, royalty and interest income from investees	**188**	172	132	16	9%	40	30%
Interest income	**2**	3	2				