

AGILENT TECHNOLOGIES INC

Form 10-Q

September 07, 2011

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-Q**

(MARK ONE)

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

**FOR THE QUARTERLY PERIOD ENDED JULY 31, 2011**

**OR**

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

**FOR THE TRANSITION PERIOD FROM                      TO**

**COMMISSION FILE NUMBER: 001-15405**

# AGILENT TECHNOLOGIES, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

**DELAWARE**

(State or other jurisdiction of  
incorporation or organization)

**77-0518772**

(IRS employer  
Identification no.)

**5301 STEVENS CREEK BLVD.,  
SANTA CLARA, CALIFORNIA**  
(Address of principal executive offices)

**95051**  
(Zip Code)

Registrant's telephone number, including area code: **(408) 553-2424**

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by section 13 or 15(d) of the securities exchange act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer   
(do not check if a smaller reporting company)

Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

**CLASS**

**OUTSTANDING AT JULY 31, 2011**

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COMMON STOCK, \$0.01 PAR VALUE

347,214,336 SHARES

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(in millions, except per share amounts)

(Unaudited)

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2011	2010	2011	2010
Net revenue:				
Products	\$ 1,406	\$ 1,147	\$ 4,053	\$ 3,152
Services and other	285	237	834	716
Total net revenue	1,691	1,384	4,887	3,868
Costs and expenses:				
Cost of products	643	527	1,822	1,379
Cost of services and other	156	132	457	393
Total costs	799	659	2,279	1,772
Research and development	162	154	486	453
Selling, general and administrative	449	456	1,364	1,280
Total costs and expenses	1,410	1,269	4,129	3,505
Income from operations	281	115	758	363
Interest income	3	3	10	9
Interest expense	(20)	(24)	(63)	(69)
Gain on sale of network solutions division, net		127		127
Other income (expense), net	17	6	34	19
Income before taxes	281	227	739	449
Provision (benefit) for income taxes	(49)	22	16	57
Net income	\$ 330	\$ 205	\$ 723	\$ 392
Net income per share basic:	\$ 0.95	\$ 0.59	\$ 2.08	\$ 1.13
Net income per share diluted:	\$ 0.92	\$ 0.58	\$ 2.04	\$ 1.11
Weighted average shares used in computing net income per share:				
Basic	348	347	347	348
Diluted	357	352	355	352

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



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## AGILENT TECHNOLOGIES, INC.

## CONDENSED CONSOLIDATED BALANCE SHEET

(in millions, except par value and share amounts)

(Unaudited)

	July 31, 2011	October 31, 2010
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 3,101	\$ 2,649
Short-term restricted cash and cash equivalents		1,550
Accounts receivable, net	917	869
Inventory	897	716
Other current assets	308	385
Total current assets	5,223	6,169
Property, plant and equipment, net	1,000	980
Goodwill	1,580	1,456
Other intangible assets, net	462	494
Long-term investments	122	142
Other assets	366	455
Total assets	\$ 8,753	\$ 9,696
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 470	\$ 499
Employee compensation and benefits	348	395
Deferred revenue	424	358
Short-term debt		1,501
Other accrued liabilities	263	330
Total current liabilities	1,505	3,083
Long-term debt	2,168	2,190
Retirement and post-retirement benefits	226	477
Other long-term liabilities	654	710
Total liabilities	4,553	6,460
Contingencies (Note 13)		
Total equity:		
Stockholders' equity:		
Preferred stock; \$0.01 par value; 125 million shares authorized; none issued and outstanding		
Common stock; \$0.01 par value; 2 billion shares authorized; 590 million shares at July 31, 2011 and 579 million shares at October 31, 2010, issued	6	6
Treasury stock at cost; 243 million shares at July 31, 2011 and 233 million shares at October 31, 2010	(8,500)	(8,038)
Additional paid-in-capital	8,248	7,904
Retained earnings	4,167	3,444
Accumulated other comprehensive income (loss)	271	(88)
Total stockholders' equity	4,192	3,228
Non-controlling interest	8	8
Total equity	4,200	3,236
Total liabilities and equity	\$ 8,753	\$ 9,696

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

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## AGILENT TECHNOLOGIES, INC.

## CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions)

(Unaudited)

	Nine Months Ended July 31,	
	2011	2010
Cash flows from operating activities:		
Net income	\$ 723	\$ 392
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	190	135
Share-based compensation	58	51
Deferred taxes	30	(27)
Excess and obsolete inventory and inventory-related charges	20	21
Gain on divestitures, net		(125)
Other non-cash expenses, net	9	21
Changes in assets and liabilities:		
Accounts receivable	(31)	(109)
Inventory	(192)	(22)
Accounts payable	(36)	85
Employee compensation and benefits	(56)	(54)
Interest swap proceeds	31	
Other assets and liabilities	4	(23)
Net cash provided by operating activities	750	345
Cash flows from investing activities:		
Investments in property, plant and equipment	(138)	(87)
Proceeds from sale of property, plant and equipment	17	7
Proceeds from sale of investments	14	38
Proceeds from divestiture, net of cash divested		216
Acquisitions of businesses and intangible assets, net of cash acquired	(96)	(1,310)
Change in restricted cash and cash equivalents, net	1,545	5
Net cash provided by (used in) investing activities	1,342	(1,131)
Cash flows from financing activities:		
Issuance of common stock under employee stock plans	299	264
Repayment of debt	(1,500)	(29)
Issuance of senior notes		747
Debt issuance cost		(5)
Treasury stock repurchases	(462)	(359)
Net cash provided by (used in) financing activities	(1,663)	618
Effect of exchange rate movements	23	6
Net increase (decrease) in cash and cash equivalents	452	(162)
Cash and cash equivalents at beginning of period	2,649	2,479
Cash and cash equivalents at end of period	\$ 3,101	\$ 2,317

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



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**AGILENT TECHNOLOGIES, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(UNAUDITED)**

**1. OVERVIEW, BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Overview.* Agilent Technologies, Inc. ( we , Agilent or the company ), incorporated in Delaware in May 1999, is a measurement company, providing core bio-analytical and electronic measurement solutions to the life sciences, chemical analysis, communications and electronics industries.

Our fiscal year-end is October 31, and our fiscal quarters end on January 31, April 30 and July 31. Unless otherwise stated, all dates refer to our fiscal year and fiscal quarters.

*Acquisition of Varian, Inc.* On May 14, 2010, we completed our acquisition of Varian, Inc. ( Varian ) by means of a merger of one of our wholly-owned subsidiaries with and into Varian such that Varian became a wholly-owned subsidiary of Agilent. We financed the purchase price of Varian using the proceeds from our September 2009 offering of senior notes and other existing cash. The Varian merger has been accounted for in accordance with the authoritative accounting guidance and the results of Varian are included in Agilent 's consolidated financial statements from the date of merger. For additional details related to the acquisition of Varian, see Note 3, Acquisition of Varian .

*Basis of Presentation.* We have prepared the accompanying financial data for the three and nine months ended July 31, 2011 and 2010 pursuant to the rules and regulations of the Securities and Exchange Commission ( SEC ). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles ( GAAP ) in the U.S. have been condensed or omitted pursuant to such rules and regulations. The following discussion should be read in conjunction with our 2010 Annual Report on Form 10-K.

In the opinion of management, the accompanying condensed consolidated financial statements contain all normal and recurring adjustments necessary to present fairly our condensed consolidated balance sheet as of July 31, 2011 and October 31, 2010, condensed consolidated statement of operations for the three and nine months ended July 31, 2011 and 2010, and condensed consolidated statement of cash flows for the nine months ended July 31, 2011 and 2010.

The preparation of condensed consolidated financial statements in accordance with GAAP in the U.S. requires management to make estimates and assumptions that affect the amounts reported in our condensed consolidated financial statements and accompanying notes. Management bases its estimates on historical experience and various other assumptions believed to be reasonable. Although these estimates are based on management 's best knowledge of current events and actions that may impact the company in the future, actual results may be different from the estimates. Our critical accounting policies are those that affect our financial statements materially and involve difficult, subjective or complex judgments by management. Those policies are revenue recognition, inventory valuation, share-based compensation, retirement and post-retirement benefit plan assumptions, goodwill and purchased intangible assets, restructuring and asset impairment charges and accounting

for income taxes.

*Reclassifications.* Certain prior year financial statement amounts have been reclassified to conform to the current year presentation with no impact on previously reported net income.

*Update to Significant Accounting Policies.* With the exception of the adoption of the new accounting pronouncements related to revenue recognition, which are discussed below, there have been no material changes to our significant accounting policies, as compared to the significant accounting policies described in our Annual Report on Form 10-K for the fiscal year ended October 31, 2010.

*Revenue Recognition for Arrangements with Multiple Deliverables.* On November 1, 2010, we adopted an accounting update regarding revenue recognition for multiple deliverable arrangements and an accounting update for certain revenue arrangements that include software elements.

We adopted the above accounting updates on a prospective basis for applicable transactions originating or materially modified after November 1, 2010. The amended update for multiple deliverable arrangements did not change the units of accounting for our revenue transactions, and most products and services qualify as separate units of accounting. Under the previous guidance for multiple deliverable arrangements with software elements, we typically applied the residual method to allocate revenue if we were unable to determine vendor specific objective evidence of fair value or verifiable objective evidence of fair value for the delivered element but were able to obtain fair value for any undelivered elements.

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The adoption of the amended revenue recognition rules did not significantly change the timing of revenue recognition and did not have a material impact on our consolidated financial statements for the three and nine months ended July 31, 2011. We cannot reasonably estimate the effect of adopting these standards on future financial periods as the impact will vary depending on the nature and volume of new or materially modified sales arrangements in any given period.

Our multiple-element arrangements are generally comprised of a combination of measurement instruments, installation or other start-up services and/or software and/or support or services. Hardware and software elements are typically delivered at the same time and revenue is recognized upon delivery once title and risk of loss pass to the customer. Delivery of installation, start-up services and other services varies based on the complexity of the equipment, staffing levels in a geographic location and customer preferences, and can range from a few days to a few months. Service revenue is deferred and recognized over the contractual period or as services are rendered and accepted by the customer. Revenue from the sale of software products that are not required to deliver the tangible product's essential functionality are accounted for under software revenue recognition rules which require vendor specific objective evidence (VSOE) of fair value to allocate revenue in a multiple element arrangement. Our arrangements generally do not include any provisions for cancellation, termination, or refunds that would significantly impact recognized revenue.

We have evaluated the deliverables in our multiple-element arrangements and concluded that they are separate units of accounting if the delivered item or items have value to the customer on a standalone basis and for an arrangement that includes a general right of return relative to the delivered item(s), delivery or performance of the undelivered item(s) is considered probable and substantially in our control. We allocate revenue to each element in our multiple-element arrangements based upon their relative selling prices. We determine the selling price for each deliverable based on a selling price hierarchy. The selling price for a deliverable is based on VSOE if available, third-party evidence (TPE) if VSOE is not available, or estimated selling price (ESP) if neither VSOE nor TPE is available. Revenue allocated to each element is then recognized when the basic revenue recognition criteria for that element have been met.

We use VSOE of selling price in the selling price allocation in all instances where it exists. VSOE of selling price for products and services is determined when a substantial majority of the selling prices fall within a reasonable range when sold separately. TPE of selling price can be established by evaluating largely interchangeable competitor products or services in standalone sales to similarly situated customers. As our products contain a significant element of proprietary technology and the solution offered differs substantially from that of competitors, it is difficult to obtain the reliable standalone competitive pricing necessary to establish TPE. ESP represents the best estimate of the price at which we would transact a sale if the product or service were sold on a standalone basis. We determine ESP for a product or service by using historical selling prices which reflect multiple factors including, but not limited to customer type, geography, market conditions, competitive landscape, gross margin objectives and pricing practices. The determination of ESP is made through consultation with and approval by management. We may modify or develop new pricing practices and strategies in the future. As these pricing strategies evolve, we may modify our pricing practices in the future, which may result in changes in ESP. The aforementioned factors may result in a different allocation of revenue to the deliverables in multiple element arrangements from the current fiscal quarter, which may change the pattern and timing of revenue recognition for these elements but will not change the total revenue recognized for the arrangement.

*Fair Value of Financial Instruments.* The carrying values of certain of our financial instruments including cash and cash equivalents, restricted cash and cash equivalents, accounts receivable, accounts payable, short-term debt, accrued compensation and other accrued liabilities approximate fair value because of their short maturities. The fair value of long-term equity investments is determined using quoted market prices for those securities when available. For those long-term equity investments accounted for under the cost method, their carrying value approximates their estimated fair value. The fair value of our long-term debt exceeds the carrying value by approximately 7 percent as of July 31, 2011. The fair value of foreign currency contracts used for hedging purposes is estimated internally by using inputs tied to active markets. See also Note 9, Fair Value Measurements for additional information on the fair value of financial instruments.

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*Goodwill and Purchased Intangible Assets.* We review goodwill for impairment annually as of September 30 and whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable in accordance with the authoritative guidance. The circumstances that could trigger a goodwill impairment could include, but are not limited to, the following items to the extent that management believes the occurrence of one or more would make it more likely than not that we would fail the first step of the goodwill impairment test (as described in the next paragraph): significant adverse change in legal factors or in the business climate, an adverse action or assessment by a regulator, unanticipated competition, a loss of key personnel, a more-likely-than-not expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed of, a portion of a reporting unit's goodwill has been included in the carrying amounts of a business that will be disposed or if our market capitalization is below our net book value.

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The provisions of authoritative guidance require that we perform a two-step impairment test on goodwill. In the first step, we compare the fair value of each reporting unit to its carrying value. The second step (if necessary) measures the amount of impairment by applying fair-value-based tests to the individual assets and liabilities within each reporting unit. As defined in the authoritative guidance, a reporting unit is an operating segment, or one level below an operating segment. Accordingly, we have aggregated components of an operating segment that have similar economic characteristics into our reporting units. At the time of an acquisition, we assign goodwill to the reporting unit that is expected to benefit from the synergies of the combination. Agilent has three reporting units, which are the same as our operating segments: life sciences, chemical analysis and electronic measurement.

The process of evaluating the potential impairment of goodwill is highly subjective and requires significant judgment, as our businesses operate in a number of markets and geographical regions. We determine the fair value of our reporting units based on an income approach, whereby we calculate the fair value of each reporting unit based on the present value of estimated future cash flows, which are formed by evaluating historical trends, current budgets, operating plans and industry data. We evaluate the reasonableness of the fair value calculations of our reporting units by reconciling the total of the fair values of all of our reporting units to our total market capitalization, taking into account an appropriate control premium. We then compare the carrying value of our reporting units to the fair value calculations based on the income approach noted above.

If the estimated fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is not impaired and the second step of the impairment test is not necessary. If the carrying amount of a reporting unit exceeds its estimated fair value, then the second step of the goodwill impairment test must be performed. The second step of the goodwill impairment test compares the implied fair value of the reporting unit's goodwill with its goodwill carrying amount to measure the amount of impairment, if any. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit's assets and liabilities in a manner similar to a purchase price allocation, with any residual fair value allocated to goodwill. If the carrying value of a reporting unit's goodwill exceeds its implied fair value, an impairment loss is recognized in an amount equal to that excess. Estimates of the future cash flows associated with the businesses are critical to these assessments. Changes in these estimates based on changed economic conditions or business strategies could result in material impairment charges in future periods.

Purchased intangible assets consist primarily of acquired developed technologies, proprietary know-how, trademarks, and customer relationships and are amortized using the straight-line method over estimated useful lives ranging from 6 months to 15 years. In process research and development (IPR&D) is initially capitalized at fair value as an intangible asset with an indefinite life and assessed for impairment thereafter. When the IPR&D project is complete, it is reclassified as an amortizable purchased intangible asset and is amortized over its estimated useful life. If an IPR&D project is abandoned, Agilent will record a charge for the value of the related intangible asset to Agilent's consolidated statement of operations in the period it is abandoned.

## 2. NEW ACCOUNTING PRONOUNCEMENTS

In October 2009, the FASB amended revenue recognition guidance for arrangements with multiple deliverables. The guidance eliminates the residual method of revenue recognition and allows the use of management's best estimate of selling price for individual elements of an arrangement when vendor specific objective evidence (VSOE), or third-party evidence (TPE) is unavailable. The FASB also amended the scope of existing software revenue recognition accounting. Tangible products containing software components and non-software components that function together to deliver the product's essential functionality would be scoped out of the accounting guidance on software and accounted for based on other appropriate revenue recognition guidance. We adopted both of the above guidance effective November 1, 2010 on a prospective basis. The adoption of the amended revenue recognition rules did not have a material impact on our consolidated financial statements. See Note 1, Overview, Basis of Presentation and Summary of Significant Accounting Policies for additional information.

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In January 2010, the FASB issued guidance that requires new disclosures for fair value measurements and provides clarification for existing disclosure requirements. The guidance is effective for interim and annual periods beginning after December 15, 2009, except for gross presentation of activity in level 3 which is effective for annual periods beginning after December 15, 2010, and for interim periods in those years. We adopted the guidance for new disclosures for fair value measurements and clarification for existing disclosure requirements as of February 1, 2010 and there was no material impact on our consolidated financial statements. Additionally, we will adopt the guidance regarding level 3 activity on November 1, 2011 and we do not expect there to be a material impact to our consolidated financial statements. See Note 9, Fair Value Measurements for additional information on the fair value of financial instruments.

In April 2010, the FASB issued guidance on defining a milestone and determining when it may be appropriate to apply the milestone method of revenue recognition for research or development transactions. The guidance is effective on a prospective basis for milestones achieved in fiscal years, and interim periods within those years, beginning on or after June 15, 2010, with early adoption permitted. We adopted the guidance in the first quarter of 2011 and there was no material impact on our consolidated financial statements.

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In May 2011, the FASB amended fair value measurement and disclosure guidance to achieve convergence with IFRS. The amended guidance modifies the measurement of fair value, clarifies verbiage, and changes disclosure or other requirements in US GAAP and IFRS. The guidance is effective during interim and annual periods beginning after December 15, 2011. We do not expect a material impact on our consolidated financial statements due to the adoption of this guidance.

In June 2011, the FASB issued guidance related to the presentation of comprehensive income. The guidance aims to improve the comparability, consistency, and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. The guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. We expect to make presentational changes to our consolidated financial statements upon adoption of this guidance, but as this guidance impacts disclosure requirements only, its adoption will not have a material impact on our consolidated financial statements.

### 3. ACQUISITION OF VARIAN

On May 14, 2010, we completed the previously announced acquisition of Varian through the merger of Varian and Cobalt Acquisition Corp., a direct wholly-owned subsidiary of Agilent under the Merger Agreement, dated July 26, 2009. As a result of the merger, Varian has become a wholly-owned subsidiary of Agilent. Accordingly, the results of Varian are included in Agilent's consolidated financial statements from the date of the merger.

The consideration paid was approximately \$1,507 million, comprising \$52 cash per share of Varian's outstanding common stock. We also paid \$17 million to acquire Varian's vested in-the-money stock options at \$52 cash per share less their exercise price. In addition we paid \$12 million for Varian's non-vested in-the-money stock options at \$52 cash per share less their exercise price, and Varian's non-vested restricted stock awards and non-vested performance shares, each at 100 percent of target and at \$52 cash per share. In accordance with the authoritative accounting guidance, settlement of the non-vested awards is considered to be for the performance of post combination services and is therefore stock-based compensation expensed immediately after acquisition. Agilent funded the acquisition using the proceeds from our September 2009 offering of senior notes and other existing cash.

The Varian merger was accounted for in accordance with the authoritative accounting guidance. The acquired assets and assumed liabilities were recorded by Agilent at their estimated fair values. Agilent determined the estimated fair values with the assistance of appraisals or valuations performed by independent third party specialists, discounted cash flow analyses, quoted market prices where available, and estimates made by management. We expect to realize operational and cost synergies, leverage the existing sales channels and product development resources, and utilize the assembled workforce. The company expects the combined entity to achieve significant savings in corporate and divisional overhead costs. The company also anticipates opportunities for growth through expanded geographic and customer segment diversity and the ability to leverage additional products and capabilities. These factors, among others, contributed to a purchase price in excess of the estimated fair value of Varian's net identifiable assets acquired, and, as a result, we have recorded goodwill in connection with this transaction.

Goodwill acquired was allocated to our operating segments and reporting units as a part of the purchase price allocation. We do not expect the goodwill recognized to be deductible for income tax purposes. Any impairment charges made in the future associated with goodwill will not be tax deductible.

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The purchase price was allocated to the estimated fair values of the assets acquired and liabilities assumed on the closing date of May 14, 2010. For the completed purchase price allocation refer to Note 3 of Agilent's 2010 Form 10-K.

The following represents unaudited pro forma operating results as if Varian had been included in the company's condensed consolidated statements of operations as of the beginning of the fiscal year presented (in millions, except per share amounts).

		<b>Three Months Ended</b>	<b>July 31, 2010</b>	<b>Nine Months Ended</b>	
Net revenue	\$		1,413	\$	4,292
Net income	\$		248	\$	338
Net income per share	basic	\$	0.71	\$	0.97
Net income per share	diluted	\$	0.70	\$	0.96

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The unaudited pro forma financial information assumes that the companies were combined as of November 1, 2009 and include business combination accounting effects from the acquisition including amortization charges from acquired intangible assets, reduction in revenue and increase in cost of sales due to the respective estimated fair value adjustments to deferred revenue and inventory, decrease to interest income for cash used in the acquisition, acquisition related transaction costs and tax related effects. The pro forma information as presented above is for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisition had taken place at the beginning of fiscal 2010.

The unaudited pro forma financial information for the three months ended July 31, 2010 combine the historical results of Agilent and Varian for the three months ended July 31, 2010. The unaudited pro forma financial information for the nine months ended July 31, 2010 combine the historical results of Agilent for the nine months ended July 31, 2010 and the historical results of Varian for the six months ended April 2, 2010 and the three months ended July 31, 2010.

4. SHARE-BASED COMPENSATION

Agilent accounts for share-based awards in accordance with the provisions of the revised accounting guidance which requires the measurement and recognition of compensation expense for all share-based payment awards made to our employees and directors including employee stock option awards, restricted stock units, employee stock purchases made under our employee stock purchase plan (ESPP) and performance share awards granted to selected members of our senior management under the long-term performance plan (LTPP) based on estimated fair values.

The impact on our results for share-based compensation was as follows:

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2011	2010	2011	2010
	(in millions)			
Cost of products and services	\$ 3	\$ 3	\$ 13	\$ 11
Research and development	2	2	8	8
Selling, general and administrative	11	8	39	32
Total share-based compensation expense	\$ 16	\$ 13	\$ 60	\$ 51

At July 31, 2011 there was no share-based compensation capitalized within inventory. The windfall tax benefit realized from exercised stock options and similar awards was not material for the three and nine months ended July 31, 2011 and 2010. During the nine months ended July 31, 2010, we reversed approximately \$3 million of expense for the cancellation of non-vested awards related to the separation of a senior executive.

The following assumptions were used to estimate the fair value of the options and LTPP grants. We had no LTPP and employee stock options granted during the three months ended July 31, 2011.

Three Months Ended

Nine Months Ended

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	2011	July 31, 2010	2011	July 31, 2010
<b>Stock Option Plans:</b>				
Weighted average risk-free interest rate		2.1%	1.5%	2.2%
Dividend yield		0%	0%	0%
Weighted average volatility		36%	35%	37%
Expected life		4.4 yrs	5.8 yrs	4.4 yrs
<b>LTPP:</b>				
Volatility of Agilent shares		39%	40%	39%
Volatility of selected peer-company shares		20%-80%	20%-76%	20%-80%
Price-wise correlation with selected peers		53%	55%	53%

The fair value of share-based awards for employee stock option awards was estimated using the Black-Scholes option pricing model. Shares granted under the LTPP were valued using a Monte Carlo simulation model. Both the Black-Scholes and Monte Carlo simulation fair value models require the use of highly subjective and complex assumptions, including the option's expected life and the price volatility of the underlying stock. The estimated fair value of restricted stock unit awards is determined based on the market

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price of Agilent's common stock on the date of grant. The ESPP allows eligible employees to purchase shares of our common stock at 85 percent of the purchase price and uses the purchase date to establish the fair market value.

We use historical volatility to estimate the expected stock price volatility assumption for employee stock option awards. In reaching the conclusion, we have considered many factors including the extent to which our options are currently traded and our ability to find traded options in the current market with similar terms and prices to the options we are valuing. For the grants awarded under the 2009 stock plan after November 1, 2010, we increased the period available to retirement eligible employees to exercise their options from three years at retirement date to the full contractual term of ten years. In developing our estimated life of our employee stock options of 5.8 years, we considered the historical option exercise behavior of our executive employees who were granted the majority of the options in the annual grants made during the first quarter of 2011, which we believe is representative of future behavior.

## 5. PROVISION FOR INCOME TAXES

For the three and nine months ended July 31, 2011, we recorded an income tax benefit of \$49 million and an income tax provision of \$16 million, respectively, compared to an income tax provision of \$22 million and \$57 million, respectively, for the same periods last year. The income tax benefit and provision for the three and nine months ended July 31, 2011, respectively, includes net discrete tax benefits of \$72 million and \$55 million, respectively and are primarily associated with the recognition of previously unrecognized tax benefits and the reversal of the related interest accruals due to the reassessment of certain foreign uncertain tax positions. The income tax provision for the nine months ended July 31, 2011 also includes a \$29 million out of period adjustment to reduce the carrying value of certain U.K. deferred tax assets, which was recorded in the prior quarter ended April 30, 2011. The overstatement of these deferred tax assets resulted in an overstatement of the U.K. valuation allowance release in the fourth quarter of 2010.

The income tax provision for the three and nine months ended July 31, 2010 includes a net discrete tax expense netting to zero and \$3 million, respectively, relating primarily to tax settlements and lapses of statutes of limitations.

Without considering interest and penalties, the effective tax rate reflects taxes in all jurisdictions except the U.S. and foreign jurisdictions in which income tax expense or benefit continues to be offset by adjustments to valuation allowances. As of July 31, 2011 we intend to maintain partial or full valuation allowances in these jurisdictions until sufficient positive evidence exists to support its reversal. We currently have a valuation allowance of \$334 million of which \$269 million relates to U.S. jurisdictions. Due to improvements in the U.S. operating results over the past three years, management believes a reasonable possibility exists that, within the next year, sufficient positive evidence may become available to reach a conclusion that a significant portion of the U.S. valuation allowance will no longer be needed.

In the U.S., tax years remain open back to the year 2006 for federal income tax purposes and the year 2000 for state purposes. In other major jurisdictions where we conduct business, the tax years generally remain open back to the year 2003. With these jurisdictions and the U.S., it is possible that there could be significant changes to our unrecognized tax benefits in the next twelve months due to either the expiration of a statute of limitation or a tax audit settlement. Because of the uncertainty as to the timing of a potential settlement or the completion of tax audits, an estimate cannot be made of the range of tax increases or decreases that could occur in the next twelve months.

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In December 2010, Agilent reached an agreement with the Internal Revenue Service (IRS) for tax years 2003-2005. In addition, Agilent and the IRS reached an agreement on transfer pricing issues covering years 2003-2007. Tax adjustments resulting from these agreements were offset by applying available net operating losses and tax credit carry forwards. Agilent's U.S. federal income tax returns for 2006 through 2007 are currently under audit by the IRS. As a result of these agreements with the IRS and agreements with other tax jurisdictions, unrecognized tax benefits were reduced from \$656 million at October 31, 2010 to \$489 million at July 31, 2011.

### 6. NET INCOME PER SHARE

The following is a reconciliation of the numerators and denominators of the basic and diluted net income per share computations for the periods presented below:

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2011	2010	2011	2010
	(in millions)			
<b>Numerator:</b>				
Net income	\$ 330	\$ 205	\$ 723	\$ 392
<b>Denominators:</b>				
Basic weighted-average shares	348	347	347	348
Potentially dilutive common stock equivalents stock options and other employee stock plans	9	5	8	4
Diluted weighted-average shares	357	352	355	352

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The dilutive effect of share-based awards is reflected in diluted net income per share by application of the treasury stock method, which includes consideration of unamortized share-based compensation expense and the dilutive effect of in-the-money options and non-vested restricted stock units. Under the treasury stock method, the amount the employee must pay for exercising stock options and unamortized share-based compensation expense are assumed proceeds to be used to repurchase hypothetical shares. An increase in the fair market value of the company's common stock can result in a greater dilutive effect from potentially dilutive awards.

For the three and nine months ended July 31, 2011, no options to purchase shares were excluded from the calculation of diluted earnings per share. For the three and nine months ended July 31, 2011 the average stock price was \$49 and \$44, respectively. For the three and nine months ended July 31, 2010, options to purchase 11 million shares with a weighted average exercise price of \$34 were excluded from the calculation of diluted earnings per share as their effect was anti-dilutive. For the three and nine months ended July 31, 2010 the average stock price was \$31.

7. INVENTORY

	July 31, 2011	(in millions)		October 31, 2010
Finished goods	\$	441	\$	338
Purchased parts and fabricated assemblies		456		378
Inventory	\$	897	\$	716

8. GOODWILL AND OTHER INTANGIBLE ASSETS

The following table presents goodwill balances and the movements for each of our reportable segments during the nine months ended July 31, 2011:

	Life Sciences		Chemical Analysis		Electronic Measurement		Total	
	(in millions)							
Goodwill as of October 31, 2010	\$	311	\$	747	\$	398	\$	1,456
Goodwill arising from acquisitions		53		11				64
Foreign currency translation impact and other adjustments		5		15		40		60
Goodwill as of July 31, 2011	\$	369	\$	773	\$	438	\$	1,580

The components of other intangibles as of July 31, 2011 and October 31, 2010 are shown in the table below:

	Gross Carrying Amount	Purchased Other Intangible Assets Accumulated Amortization and Impairments	Net Book Value
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(in millions)

**As of October 31, 2010:**

Purchased technology	\$	466	\$	176	\$	290
Backlog		12		12		
Trademark/Tradenname		39		13		26
Customer relationships		236		77		159
Total amortizable intangible assets	\$	753	\$	278	\$	475
In-Process R&D		19				19
Total	\$	772	\$	278	\$	494

**As of July 31, 2011:**

Purchased technology	\$	505	\$	231	\$	274
Backlog		12		12		
Trademark/Tradenname		40		19		21
Customer relationships		252		104		148
Total amortizable intangible assets	\$	809	\$	366	\$	443
In-Process R&D		19				19
Total	\$	828	\$	366	\$	462

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During the three and nine months ended July 31, 2011, we recorded additions to goodwill of zero and \$64 million, respectively, relating to the purchase of three businesses. We also recorded a \$27 million adjustment to goodwill during the three months ended July 31, 2011 in the electronic measurement segment relating to deferred taxes from a prior acquisition. During the three and nine months ended July 31, 2011, we recorded additions to other intangibles of zero and \$42 million, respectively, related to the purchase of three businesses. We also recorded \$14 million of foreign exchange translation impact to other intangibles for the nine months ended July 31, 2011.

Amortization of intangible assets was \$29 million and \$85 million for the three and nine months ended July 31, 2011 and \$27 million and \$46 million for the same periods in the prior year. During the three and nine months ended July 31, 2011, we recorded zero and \$3 million of impairments of other intangibles related to an exited business. Future amortization expense related to existing purchased intangible assets is estimated to be \$27 million for the remainder of 2011, \$95 million for 2012, \$78 million for 2013, \$67 million for 2014, \$57 million for 2015, \$50 million for 2016, and \$88 million thereafter.

## 9. FAIR VALUE MEASUREMENTS

The authoritative guidance defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, we consider the principal or most advantageous market and assumptions that market participants would use when pricing the asset or liability.

### *Fair Value Hierarchy*

The guidance establishes a fair value hierarchy that prioritizes the use of inputs used in valuation techniques into three levels. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. There are three levels of inputs that may be used to measure fair value:

*Level 1-* applies to assets or liabilities for which there are quoted prices in active markets for identical assets or liabilities.

*Level 2-* applies to assets or liabilities for which there are inputs other than quoted prices included within level 1 that are observable, either directly or indirectly, for the asset or liability such as: quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in less active markets; or other inputs that can be derived principally from, or corroborated by, observable market data.

*Level 3-* applies to assets or liabilities for which there are unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of the assets or liabilities.

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*Assets and Liabilities Measured at Fair Value on a Recurring Basis*

Assets and liabilities measured at fair value on a recurring basis as of July 31, 2011 were as follows:

	July 31, 2011	Fair Value Measurement at July 31, 2011 Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1) (in millions)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>				
Short-term				
Cash equivalents (money market funds)	\$ 1,404	\$ 1,404	\$	\$
Derivative instruments (foreign exchange contracts)	23		23	
Long-term				
Trading securities	51	51		
Derivative instruments (interest rate contracts)	15		15	
Available-for-sale investments	2	2		
Total assets measured at fair value	\$ 1,495	\$ 1,457	\$ 38	\$
<b>Liabilities:</b>				
Short-term				
Derivative instruments (foreign exchange contracts)	\$ 14	\$	\$ 14	\$
Long-term				
Deferred compensation liability	49		49	
Total liabilities measured at fair value	\$ 63	\$	\$ 63	\$

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Our money market funds, trading securities investments, and available-for-sale investments are generally valued using quoted market prices and therefore are classified within level 1 of the fair value hierarchy. Our derivative financial instruments are classified within level 2, as there is not an active market for each hedge contract, but the inputs used to calculate the value of the instruments are tied to active markets. Our deferred compensation liability is classified as level 2 because although the values are not directly based on quoted market prices, the inputs used in the calculations are observable.

Trading securities and deferred compensation liability are reported at fair value, with gains or losses resulting from changes in fair value recognized currently in net income. Investments designated as available-for-sale and certain derivative instruments are reported at fair value, with unrealized gains and losses, net of tax, included in stockholders' equity. Realized gains and losses from the sale of these instruments are recorded in net income.

For assets measured at fair value using significant unobservable inputs (level 3), the following table summarizes the change in balances during the three and nine months ended July 31, 2011 and 2010:

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2011	2010	2011	2010
	(in millions)			
Balance, beginning of period	\$	\$	1	\$ 6
Realized losses related to amortization of premium				(1)
Realized losses related to investment impairments				
Sales			(1)	(3)
Transfers into level 3				
Transfers out of level 3				(2)
Balance, end of period	\$	\$	\$	\$
Total losses included in net income attributable to change in unrealized losses relating to assets still held at the reporting date, reported in interest and other income, net	\$	\$	\$	\$ (1)

*Impairment of Investments.* All of our investments, excluding trading securities, are subject to periodic impairment review. The impairment analysis requires significant judgment to identify events or circumstances that would likely have a significant adverse effect on the future value of the investment. We consider various factors in determining whether an impairment is other-than-temporary, including the severity and duration of the impairment, forecasted recovery, the financial condition and near-term prospects of the investee, and our ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value. There were no other than temporary impairments for investments for the three and nine months ended July 31, 2011 and 2010.

***Assets and Liabilities Measured at Fair Value on a Non-Recurring Basis***

For assets measured at fair value on a non-recurring basis, the following table summarizes the impairments included in net income during the three and nine months ended July 31, 2011 and 2010:

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	Three Months Ended		Nine Months Ended	
	2011	July 31, 2010	2011	July 31, 2010
Long-lived assets held and used	\$	3	\$	7
Long-lived assets held for sale				14

(in millions)

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For the three months ended July 31, 2011, long-lived assets held and used with a carrying value of \$4 million were written down to their fair value of \$1 million. For the nine months ended July 31, 2011 long-lived assets held and used with a carrying value of \$8 million were written down to their fair value of \$1 million. For the three months ended July 31, 2011, there were no impairments of long-lived assets held for sale. For the nine months ended July 31, 2011 long-lived assets held for sale with a carrying value of \$4 million were written down to their fair value of \$3 million. Impairments of long-lived assets held and used were zero for the three months ended July 31, 2010. For the nine months ended July 31, 2010, long-lived assets held and used with a carrying value of \$29 million were written down to their fair value of \$23 million. Impairments of long-lived assets held for sale were zero for the three months ended July 31, 2010. For the nine months ended July 31, 2010, long-lived assets held for sale with a carrying value of \$30 million were written down to their fair value of \$16 million. Fair value for the impaired long-lived assets was measured using level 2 inputs and impairments were included in net income for the period stated.

10. DERIVATIVES

We are exposed to foreign currency exchange rate fluctuations and interest rate changes in the normal course of our business. As part of risk management strategy, we use derivative instruments, primarily forward contracts, purchased options, and interest rate swaps, to hedge economic and/or accounting exposures resulting from changes in foreign currency exchange rates and interest rates.

*Fair Value Hedges*

We are exposed to interest rate risk due to the mismatch between the interest expense we pay on our loans at fixed rates and the variable rates of interest we receive from cash, cash equivalents and other short-term investments. We have issued long-term debt in U.S. dollars at fixed interest rates based on the market conditions at the time of financing. We believe that the fair value of our fixed rate debt changes when the underlying market rates of interest change, and we may use interest rate swaps to modify such market risk. The interest rate swaps effectively change our fixed interest rate payments to U.S. dollar LIBOR-based variable interest expense to match the floating interest income from our cash, cash equivalents and other short term investments. By entering into these interest rate swaps we are also hedging the movements in the fair value of the fixed-rate debt on our balance sheet. However, not all of our fixed rate debt's fair value is hedged in this manner, and in the future we may choose to terminate previously executed swaps. For derivative instruments that are designated and qualify as fair value hedges, we recognize the gain or loss on the derivative instrument, as well as the offsetting loss or gain on the hedged item attributable to the hedged risk, in interest expense, in the consolidated statement of operations. These fair value hedges are 100 percent effective, and there is no impact on earnings due to hedge ineffectiveness. The fair value of the swaps is recorded on the consolidated balance sheet at each period end, with an offsetting entry in senior notes. As of July 31, 2011, there were 9 interest rate swap contracts designated as fair value hedges associated with our 2012 and 2020 senior notes. The notional amount of these interest rate swap contracts, receive-fixed/pay-variable, was \$750 million. On November 25, 2008, we terminated two interest rate swap contracts associated with our 2017 senior notes that represented the notional amount of \$400 million. The asset value, including interest receivable, upon termination was approximately \$43 million and the amount to be amortized at July 31, 2011 was \$32 million. On June 6, 2011, we also terminated five interest rate swap contracts associated with our 2015 senior notes that represented the notional amount of \$500 million. The asset value, including interest accrual, upon termination was approximately \$31 million and the amount to be amortized at July 31, 2011 was \$26 million. The proceeds from all such terminated interest rate swaps are recorded as operating cash flows and the gain is being deferred and amortized over the remaining life of the respective senior notes. On Aug 9, 2011, we terminated five interest rate swap contracts related to our 2020 senior notes that represented the notional amount of \$500 million. The asset value, including interest receivable, upon termination for these contracts was approximately \$34 million.

*Cash Flow Hedges*

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We enter into foreign exchange contracts to hedge our forecasted operational cash flow exposures resulting from changes in foreign currency exchange rates. These foreign exchange contracts, carried at fair value, have maturities between one and twelve months. These derivative instruments are designated and qualify as cash flow hedges under the criteria prescribed in the authoritative guidance. The changes in the value of the effective portion of the derivative instrument are recognized in accumulated other comprehensive income. Amounts associated with cash flow hedges are reclassified to cost of sales in the consolidated statement of operations when either the forecasted transaction occurs or it becomes probable that the forecasted transaction will not occur. Changes in the fair value of the ineffective portion of derivative instruments are recognized in cost of sales in the consolidated statement of operations in the current period.

### *Other Hedges*

Additionally, we enter into foreign exchange contracts to hedge monetary assets and liabilities that are denominated in currencies other than the functional currency of our subsidiaries. These foreign exchange contracts are carried at fair value and do not qualify for hedge accounting treatment and are not designated as hedging instruments. Changes in value of the derivative are

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recognized in other income (expense) in the consolidated statement of operations, in the current period, along with the offsetting foreign currency gain or loss on the underlying assets or liabilities.

Our use of derivative instruments exposes us to credit risk to the extent that the counterparties may be unable to meet the terms of the agreement. We do, however, seek to mitigate such risks by limiting our counterparties to major financial institutions which are selected based on their credit ratings and other factors. We have established policies and procedures for mitigating credit risk that include establishing counterparty credit limits, monitoring credit exposures, and continually assessing the creditworthiness of counterparties.

All of our derivative agreements contain threshold limits to the net liability position with counterparties and are dependent on our corporate credit rating determined by the major credit rating agencies. If our corporate credit rating were to fall below investment grade, the counterparties to the derivative instruments may request collateralization on derivative instruments in net liability positions.

The aggregate fair value of all derivative instruments with credit-risk-related contingent features that were in a net liability position as of July 31, 2011, was approximately \$3 million. The credit-risk-related contingent features underlying these agreements had not been triggered as of July 31, 2011.

There were 127 foreign exchange forward contracts and 7 foreign exchange option contracts open as of July 31, 2011 and designated as cash flow hedges. There were 200 foreign exchange forward contracts open as of July 31, 2011 not designated as hedging instruments. The aggregated U.S. Dollar notional amounts by currency and designation as of July 31, 2011 were as follows:

Currency	Derivatives in Cash Flow Hedging Relationships		Option Contracts Buy/(Sell) (in millions)	Derivatives Not Designated as Hedging Instruments Forward Contracts Buy/(Sell)
	Forward Contracts Buy/(Sell)	Option Contracts Buy/(Sell)		
Euro	\$ (98)	\$		\$ 211
British Pound	(30)			146
Canadian Dollar	(48)			22
Australian Dollars	47			41
Malaysian Ringgit	144			42
Japanese Yen	(36)	(120)		21
Other	(5)			50
	\$ (26)	\$ (120)	\$	533

The gross fair values and balance sheet location of derivative instruments held in the condensed consolidated balance sheet as of July 31, 2011 and October 31, 2010 were as follows:

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Asset Derivatives		Fair Values of Derivative Instruments				Liability Derivatives	
		Fair Value		Fair Value			
Balance Sheet Location	July 31, 2011	October 31, 2010	Balance Sheet Location	July 31, 2011	October 31, 2010		
(in millions)							
<b>Derivatives designated as hedging instruments:</b>							
<i>Fair value hedges</i>							
Interest rate contracts							
Other assets	\$ 15	\$ 61	Other long-term liabilities	\$	\$		
<i>Cash flow hedges</i>							
Foreign exchange contracts							
Other current assets	\$ 10	\$ 13	Other accrued liabilities	\$ 7	\$ 15		
	\$ 25	\$ 74		\$ 7	\$ 15		
<b>Derivatives not designated as hedging instruments:</b>							
Foreign exchange contracts							
Other current assets	\$ 13	\$ 11	Other accrued liabilities	\$ 7	\$ 7		
	\$ 13	\$ 11		\$ 7	\$ 7		
Total derivatives	\$ 38	\$ 85		\$ 14	\$ 22		

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The effect of derivative instruments for foreign exchange and interest rate swap contracts designated as hedging instruments and not designated as hedging instruments in our condensed consolidated statement of operations were as follows:

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2011	2010	2011	2010
(in millions)				
<b>Derivatives designated as hedging instruments:</b>				
<i>Fair Value Hedges</i>				
Gain (loss) on interest rate swap contracts, including interest accrual, recognized in interest expense	\$ 32	\$ 41	\$ 4	\$ 57
Gain (loss) on hedged item, recognized in interest expense	\$ (26)	\$ (37)	\$ 18	\$ (44)
<i>Cash Flow Hedges</i>				
Gain (loss) recognized in accumulated other comprehensive income	\$ 2	\$ (5)	\$	\$ 6
Gain (loss) reclassified from accumulated other comprehensive income into cost of sales	\$ (1)	\$ 3	\$ (3)	\$ 6
<b>Derivatives not designated as hedging instruments:</b>				
Gain (loss) recognized in other income (expense)	\$	\$ (2)	\$ 28	\$ (25)

The estimated net amount of existing gain at July 31, 2011 that is expected to be reclassified from other comprehensive income to the cost of sales within the next twelve months is \$2 million.

## 11. RESTRUCTURING COSTS, ASSET IMPAIRMENTS AND OTHER SPECIAL CHARGES

Our 2005 restructuring program, announced in the fourth quarter of 2005, is largely complete. The remaining obligations under this and previous plans relate primarily to lease obligations that are expected to be satisfied over approximately the next year.

Our 2009 restructuring program, the ( FY 2009 Plan ), announced in the first half of 2009, was conceived in response to deteriorating economic conditions and was designed to deliver sufficient savings to enable our businesses to reach their profitability targets throughout the cycle. Workforce reduction payments, primarily severance, were largely complete in fiscal year 2010. Lease payments should primarily be complete by the end of fiscal 2014.

A summary of total restructuring activity and other special charges is shown in the table below:

	Workforce Reduction	Consolidation of Excess Facilities	(in millions)		Special Charges related to Inventory	Total
Balance as of October 31, 2010	\$ 8	\$ 26	\$	1	\$	35

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Income statement expense		1		1		2
Asset impairments/inventory charges						
Cash payments		(8)		(8)	(1)	(17)
<b>Balance as of July 31, 2011</b>	\$	1	\$	19	\$	20

The restructuring and other special accruals for all plans, which totaled \$20 million at July 31, 2011, are recorded in other accrued liabilities and other long-term liabilities on the condensed consolidated balance sheet. These balances reflect estimated future cash outlays.

A summary of the charges in the condensed consolidated statement of operations resulting from all restructuring plans is shown below:

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	Three Months Ended July 31,				Nine Months Ended July 31,				
	2011		2010		2011		2010		
	(in millions)								
Cost of products and services	\$		\$		1	\$		\$	7
Research and development					1				2
Selling, general and administrative		2		4		2		47	
Total restructuring, asset impairments and other special charges	\$	2	\$	6	\$	2	\$	56	

## 12. RETIREMENT PLANS AND POST RETIREMENT PENSION PLANS

*Components of net periodic costs.* For the three and nine months ended July 31, 2011 and 2010, our net pension and post retirement benefit costs were comprised of the following:

	Pensions								U.S. Post Retirement Benefit Plans			
	U.S. Plans		Non-U.S. Plans				U.S. Post Retirement Benefit Plans					
	2011	2010	Three Months Ended July 31,				2011	2010				
	(in millions)											
Service cost benefits earned during the period	\$	10	\$	10	\$	8	\$	7	\$	1	\$	1
Interest cost on benefit obligation		7		7		18		17		4		6
Expected return on plan assets		(11)		(10)		(24)		(21)		(5)		(5)
Amortization and deferrals:												
Actuarial loss		1		2		10		8		3		4
Prior service cost		(3)		(3)				(1)		(9)		(4)
Total net plan costs	\$	4	\$	6	\$	12	\$	10	\$	(6)	\$	2

	Pensions								U.S. Post Retirement Benefit Plans			
	U.S. Plans		Non-U.S. Plans				U.S. Post Retirement Benefit Plans					
	2011	2010	Nine Months Ended July 31,				2011	2010				
	(in millions)											
Service cost benefits earned during the period	\$	31	\$	30	\$	24	\$	23	\$	3	\$	3
Interest cost on benefit obligation		21		21		53		52		17		20
Expected return on plan assets		(33)		(30)		(70)		(64)		(15)		(15)
Amortization and deferrals:												
Actuarial loss		3		5		29		28		10		12
Prior service cost		(9)		(9)				(1)		(18)		(12)
Total net plan costs	\$	13	\$	17	\$	36	\$	38	\$	(3)	\$	8

As of April 1, 2011, we approved changes to our U.S. Post-Retirement Benefit Plan. In connection with these changes, we reduced our Accumulated Prospective Benefit Obligation by \$194 million with the offset going to accumulated other comprehensive income. The prior service credit will be amortized over the future working lifetime of all participants in the plan which is approximately 9 years.

We contributed approximately zero to our U.S. defined benefit plans and \$17 million to our non-U.S. defined benefit plans during the three months ended July 31, 2011 and \$33 million and \$51 million, respectively, for the nine months ended July 31, 2011. We contributed less than \$1 million to our U.S. defined benefit plans and \$12 million to our non-U.S. defined benefit plans during the three months ended July 31, 2010 and \$32 million and \$34 million, respectively, for the nine months ended July 31, 2010. We expect to contribute approximately zero to our U.S. defined benefit plans and \$16 million to our non-U.S. defined benefit plans during the remainder of 2011.

### 13. WARRANTIES AND CONTINGENCIES

#### *Warranties*

We accrue for standard warranty costs based on historical trends in warranty charges as a percentage of net product shipments. The accrual is reviewed regularly and periodically adjusted to reflect changes in warranty cost estimates. Estimated warranty charges

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are recorded within cost of products at the time products are sold. The standard warranty accrual balances are held in other accrued and other long-term liabilities on our condensed consolidated balance sheet. Our warranty terms typically extend for one year from the date of delivery.

A summary of the standard warranty accrual activity is shown in the table below:

	FY 2011	(in millions)	FY 2010
Beginning balance as of November 1,	\$	45	\$ 28
Reserve acquired upon close of Varian acquisition			13
Accruals for warranties issued during the period		48	41
Changes in estimates		6	(2)
Settlements made during the period		(50)	(41)
Ending balance as of July 31,	\$	49	\$ 39

**Contingencies**

We are involved in lawsuits, claims, investigations and proceedings, including patent, commercial and environmental matters. We record a provision for a liability when management believes that it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. There are no matters pending that we believe are reasonably possible of being material in relation to our business, consolidated financial condition, results of operations or cash flows.

**14. SHORT-TERM DEBT AND SHORT-TERM RESTRICTED CASH & CASH EQUIVALENTS****Credit Facility**

On May 11, 2007, we entered into a five-year credit agreement, which provides for a \$300 million unsecured credit facility that will expire on May 11, 2012. On September 8, 2009, we entered into an Accession Agreement, increasing the credit facility from \$300 million to \$330 million. The company may use amounts borrowed under the facility for general corporate purposes. As of July 31, 2011 the company has no borrowings outstanding under the facility. We were in compliance with the covenants for the credit facility during the three and nine months ended July 31, 2011.

**World Trade Debt**

We satisfied the financing obligation of World Trade in its entirety on December 10, 2010 using the proceeds of our senior notes issued in July 2010 and existing cash on our balance sheet.

*Short-Term Restricted Cash & Cash Equivalents*

As of October 31, 2010, \$1,550 million was reported as short-term restricted cash and cash equivalents in our consolidated balance sheet which was held in commercial paper maintained in connection with our World Trade repurchase obligation. This restricted cash, held by one of our wholly-owned subsidiaries, has been reclassified to cash and cash equivalents following the December 10, 2010 settlement of the World Trade repurchase obligation.

## 15. LONG-TERM DEBT

*Senior Notes*

The following table summarizes the company's senior notes and the related interest rate swaps:

	July 31, 2011			October 31, 2010		
	Amortized Principal	Swap	Total	Amortized Principal	Swap	Total
	(in millions)					
2012 Senior Notes	\$ 250	\$ 4	\$ 254	\$ 250	\$ 6	\$ 256
2013 Senior Notes	250		250	249		249
2015 Senior Notes	499	26	525	499	37	536
2017 Senior Notes	598	32	630	598	35	633
2020 Senior Notes	498	11	509	498	18	516
Total	\$ 2,095	\$ 73	\$ 2,168	\$ 2,094	\$ 96	\$ 2,190

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All notes issued are unsecured and rank equally in right of payment with all of Agilent's other senior unsecured indebtedness. There have been no changes to the principal, maturity, interest rates and interest payment terms of the senior notes in the three and nine months ended July 31, 2011 as compared to the senior notes described in our Annual Report on Form 10-K for the fiscal year ended October 31, 2010.

On November 25, 2008, we terminated two interest rate swap contracts associated with our 2017 senior notes that represented the notional amount of \$400 million. The asset value, including interest receivable, upon termination was approximately \$43 million and the amount to be amortized at July 31, 2011 was \$32 million. The gain is being deferred and amortized to interest expense over the remaining life of the senior notes.

On June 6, 2011, we terminated our interest rate swap contracts related to our 2015 senior notes that represented the notional amount of \$500 million. The asset value, including interest receivable, upon termination for these contracts was approximately \$31 million and the amount to be amortized at July 31, 2011 was \$26 million. The gain is being deferred and amortized to interest expense over the remaining life of the senior notes.

Upon the closing of the offering of the 2012 senior notes, we entered into interest rate swaps with an aggregate notional amount of \$250 million. Also concurrent with issuing the 2020 senior notes in July 2010, we entered into interest rate swaps with an aggregate notional amount of \$500 million. Under the interest rate swaps, we will receive fixed-rate interest payments and will make payments based on the U.S. dollar LIBOR plus 258 basis points and 179 basis points with respect to the 2012 and 2020 senior notes, respectively. The economic effect of these swaps will be to convert the fixed-rate interest expense on the senior notes to a variable LIBOR-based interest rate. The hedging relationship qualifies for the shortcut method of assessing hedge effectiveness, and consequently we do not expect any ineffectiveness during the life of the swap and any movement in the value of the swap would be reflected in the movement in fair value of the senior notes. At July 31, 2011, the fair value of the swaps on 2012 and 2020 senior notes was an asset of \$15 million, with a corresponding increase in the carrying value of senior notes.

On August 9, 2011, we terminated our interest rate swap contracts related to our 2020 senior notes that represented the notional amount of \$500 million. The asset value, including interest receivable, upon termination for these contracts was approximately \$34 million. The gain will be deferred and amortized to interest expense over the remaining life of the senior notes.

16. COMPREHENSIVE INCOME

The following table presents the components of comprehensive income:

	<b>Three Months Ended July 31,</b>	
	<b>2011</b>	<b>2010</b>
	<b>(in millions)</b>	
Net income	\$ 330	\$ 205
Other comprehensive income:		
Change in unrealized gain on investments		(2)
Change in unrealized gain and loss on derivative instruments	2	(5)
	1	(3)

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Reclassification of (gains) and losses into earnings related to derivative instruments			
Foreign currency translation		(9)	11
Change in deferred net pension cost		3	13
Deferred taxes		(4)	
Comprehensive income	\$	323	\$ 219

	Nine Months Ended July 31,			
	2011	(in millions)		2010
Net income	\$	723	\$	392
Other comprehensive income:				
Change in unrealized gain on investments		(5)		2
Change in unrealized gain and loss on derivative instruments				6
Reclassification of (gains) and losses into earnings related to derivative instruments		3		(6)
Foreign currency translation		147		(43)
Change in deferred net pension cost		225		9
Deferred taxes		(11)		(8)
Comprehensive income	\$	1,082	\$	352

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17. STOCK REPURCHASE PROGRAM

On November 19, 2009 our Board of Directors approved a share-repurchase program to reduce or eliminate dilution of basic outstanding shares in connection with issuances of stock under the company's equity incentive plans. The share-repurchase program does not require the company to acquire a specific number of shares and may be suspended or discontinued at any time. There is no fixed termination date for the new share-repurchase program. For the three and nine months ended July 31, 2011, we repurchased 4 million shares for \$192 million and 10 million shares for \$462 million, respectively. For the three and nine months ended July 31, 2010, we repurchased 3 million shares for \$94 million and 11 million shares for \$359 million, respectively. All such shares and related costs are held as treasury stock and accounted for using the cost method.

18. SEGMENT INFORMATION

*Description of segments.* We are a measurement company, providing core bio-analytical and electronic measurement solutions to the life sciences, chemical analysis, communications and electronics industries. The three operating segments were determined based primarily on how the chief operating decision maker views and evaluates our operations. Operating results are regularly reviewed by the chief operating decision maker to make decisions about resources to be allocated to the segment and to assess its performance. Other factors, including market separation and customer specific applications, go-to-market channels, products and services and manufacturing are considered in determining the formation of these operating segments.

A description of our three reportable segments is as follows:

Our life sciences business provides application-focused solutions that include instruments, software, consumables, and services that enable customers to identify, quantify and analyze the physical and biological properties of substances and products. Key product categories in life sciences include: DNA and RNA microarrays and associated scanner, software, and reagents; microfluidics-based sample analysis systems; liquid chromatography (LC) systems, columns and components; liquid chromatography mass spectrometry (LCMS) systems; capillary electrophoresis systems; laboratory software and informatics systems; bio-reagents and related products; laboratory automation and robotic systems, dissolution testing; Nuclear Magnetic Resonance (NMR) and Magnetic Resonance Imaging (MRI) systems along with X-Ray Crystallography, and services and support for the aforementioned products.

Our chemical analysis business provides application-focused solutions that include instruments, software, consumables, and services that enable customers to identify, quantify and analyze the physical and biological properties of substances and products. Key product categories in chemical analysis include: gas chromatography (GC) systems, columns and components; gas chromatography mass spectrometry (GC-MS) systems; inductively coupled plasma mass spectrometry (ICP-MS) products; spectroscopy products; software and data systems; vacuum pumps and measurement technologies; services and support for the aforementioned products.

Our electronic measurement business provides electronic measurement instruments and systems, software design tools and related services that are used in the design, development, manufacture, installation, deployment and operation of electronics equipment, and microscopy products. Related services include start-up assistance, instrument productivity and application services and instrument calibration and repair. We also offer customization, consulting and optimization services throughout the customer's product lifecycle.

A significant portion of the segments' expenses arise from shared services and infrastructure that we have historically provided to the segments in order to realize economies of scale and to efficiently use resources. These expenses, collectively called corporate charges, include costs of centralized research and development, legal, accounting, real estate, insurance services, information technology services, treasury and other corporate infrastructure expenses. Charges are allocated to the segments, and the allocations have been determined on a basis that we consider to be a reasonable reflection of the utilization of services provided to or benefits received by the segments.

The following tables reflect the results of our reportable segments under our management reporting system. These results are not necessarily in conformity with U.S. GAAP. The performance of each segment is measured based on several metrics, including adjusted income from operations. These results are used, in part, by the chief operating decision maker in evaluating the performance of, and in allocating resources to, each of the segments.

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The profitability of each of the segments is measured after excluding restructuring and asset impairment charges, investment gains and losses, interest income, interest expense, acquisition and integration costs, non-cash amortization and other items as noted in the reconciliations below.

	Life Sciences	Chemical Analysis	Electronic Measurement	Total
	(in millions)			
<b>Three months ended July 31, 2011:</b>				
Total segment revenue	\$ 453	\$ 383	\$ 856	\$ 1,692
Varian acquisition deferred revenue fair value adjustment	\$ (1)	\$ (1)	\$ (1)	\$ (1)
Total net revenue	\$ 453	\$ 382	\$ 856	\$ 1,691
Segment income from operations	\$ 60	\$ 79	\$ 204	\$ 343
<b>Three months ended July 31, 2010:</b>				
Total segment revenue	\$ 374	\$ 329	\$ 692	\$ 1,395
Varian acquisition deferred revenue fair value adjustment	\$ (10)	\$ (1)	\$ (1)	\$ (11)
Total net revenue	\$ 364	\$ 328	\$ 692	\$ 1,384
Segment income from operations	\$ 56	\$ 69	\$ 127	\$ 252
	Life Sciences	Chemical Analysis	Electronic Measurement	Total
	(in millions)			
<b>Nine months ended July 31, 2011:</b>				
Total segment revenue	\$ 1,321	\$ 1,113	\$ 2,461	\$ 4,895
Varian acquisition deferred revenue fair value adjustment	\$ (4)	\$ (4)	\$ (4)	\$ (8)
Total net revenue	\$ 1,317	\$ 1,109	\$ 2,461	\$ 4,887
Segment income from operations	\$ 169	\$ 216	\$ 551	\$ 936
<b>Nine months ended July 31, 2010:</b>				
Total segment revenue	\$ 1,048	\$ 811	\$ 2,020	\$ 3,879
Varian acquisition deferred revenue fair value adjustment	\$ (10)	\$ (1)	\$ (1)	\$ (11)
Total net revenue	\$ 1,038	\$ 810	\$ 2,020	\$ 3,868
Segment income from operations	\$ 159	\$ 193	\$ 285	\$ 637

The following table reconciles reportable segments' income from operations to Agilent's total enterprise income before taxes:

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2011	2010	2011	2010
	(in millions)			
Total reportable segments' income from operations	\$ 343	\$ 252	\$ 936	\$ 637
Restructuring related costs	(2)	(6)	(2)	(56)
Transformational initiatives	(11)	(14)	(33)	(29)
Amortization of Intangibles	(29)	(28)	(85)	(47)
Acquisition and integration costs	(11)	(50)	(39)	(77)
Varian acquisition related fair value adjustments	(1)	(33)	(8)	(33)
Other	(8)	(6)	(11)	(32)
Interest income	3	3	10	9

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Interest expense		(20)		(24)		(63)		(69)
Gain on sale of network solutions division, net				127				127
Other income (expense), net		17		6		34		19
Income before taxes, as reported	\$	281	\$	227	\$	739	\$	449

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The following table reflects segment assets under our management reporting system. Segment assets include allocations of corporate assets, including deferred tax assets, goodwill, other intangibles and other assets. Unallocated assets primarily consist of cash, cash equivalents, accumulated amortization of other intangibles and the valuation allowance relating to deferred tax assets.

	Life Sciences	Chemical Analysis	Electronic Measurement	Total
	(in millions)			
<b>Assets:</b>				
As of July 31, 2011	\$ 1,855	\$ 1,748	\$ 2,167	\$ 5,770
As of October 31, 2010	\$ 1,564	\$ 1,635	\$ 2,245	\$ 5,444

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (UNAUDITED)**

The following discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto included elsewhere in this Form 10-Q and our Annual Report on Form 10-K. This report contains forward-looking statements including, without limitation, statements regarding trends, seasonality, cyclicalities and growth in, and drivers of, the markets we sell into, our strategic direction, our future effective tax rate and tax valuation allowance, earnings from our foreign subsidiaries, remediation activities, new product and service introductions, the ability of our products to meet market needs, changes to our manufacturing processes, the use of contract manufacturers, the impact of local government regulations on our ability to pay vendors or conduct operations, our liquidity position, our ability to generate cash from operations, growth in our businesses, our investments, the potential impact of adopting new accounting pronouncements, our financial results, our purchase commitments, our contributions to our pension plans, the selection of discount rates and recognition of any gains or losses for our benefit plans, our cost-control activities, savings anticipated from our restructuring programs, uncertainties relating to Federal and Drug Administration (FDA) and other regulatory approvals, the integration of our Varian acquisition and other transactions, our stock repurchase program, our transition to lower-cost regions, the existence, length or timing of an economic recovery that involve risks and uncertainties. Our actual results could differ materially from the results contemplated by these forward-looking statements due to various factors, including those discussed below in **Risks, Uncertainties and Other Factors That May Affect Future Results** and elsewhere in this Form 10-Q.

**Basis of Presentation**

The financial information presented in this Form 10-Q is not audited and is not necessarily indicative of our future consolidated financial position, results of operations or cash flows. Our fiscal year-end is October 31, and our fiscal quarters end on January 31, April 30 and July 31. Unless otherwise stated, all dates refer to our fiscal year and fiscal periods.

**Executive Summary**

Agilent is the world's premier measurement company, providing core bio-analytical and electronic measurement solutions to the life sciences, chemical analysis, communications and electronics industries.

Total orders for the three and nine months ended July 31, 2011 were \$1,687 million and \$5,017 million, respectively, an increase of 13 percent and 24 percent, respectively, above the same periods last year with each business segment showing order growth in the three and nine months when compared to the same periods last year. Due to the close date of the Varian acquisition which occurred on May 14, 2010, we have excluded the first two weeks of May of this fiscal year when we compare periods without the Varian acquisition. The increase in orders in the three months ended July 31, 2011 attributable to our acquisitions accounted for 2 percentage points of order growth when compared to the same period last year. The increase in orders in the nine months ended July 31, 2011 attributable to our acquisitions, less orders attributable to our divestitures, accounted for 7 percentage points of order growth when compared to the same period last year.

Net revenue of \$1,691 million and \$4,887 million for the three and nine months ended July 31, 2011, increased 22 percent and 26 percent, respectively, above the same periods last year. The revenue increase attributable to our acquisitions accounted for 2 percentage points of revenue increase for the three months ended July 31, 2011 when compared to the same period last year. The revenue increase attributable to our

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acquisitions, less revenue attributable to our divestitures, accounted for 6 percentage points of revenue increase for the nine months ended July 31, 2011 when compared to the same period last year. Revenue growth in the life sciences business, for the three and nine months ended July 31, 2011, was led by demand for products in pharmaceutical and biotechnology markets when compared to the same periods last year. Revenue growth in the chemical analysis business for the three and nine months ended July 31, 2011, was led by strong growth in the petrochemical markets when compared to the same periods last year. Within electronic measurement, we saw strong year-over-year revenue growth from general purpose end-markets in the three and nine months ended July 31, 2011 when compared to the same periods last year. Also within electronic measurement, we saw strong year-over-year revenue growth in the communications test businesses in the three and nine months ended July 31, 2011 when compared to the same periods last year. Revenue growth within the communication test business was higher than in general purpose test with strong wireless manufacturing revenue growth in the three and nine months ended July 31, 2011.

Net income for the three and nine months ended July 31, 2011 was \$330 million and \$723 million, respectively, compared to \$205 million and \$392 million, respectively, for the corresponding periods last year. In the nine months ended July 31, 2011, we generated \$750 million of cash from operations, compared with \$345 million generated in the same period last year.

On May 14, 2010, we completed our acquisition of Varian by means of a merger of one of our wholly-owned subsidiaries with and into Varian such that Varian became a wholly-owned subsidiary of Agilent. We financed the purchase price of Varian using the

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proceeds from our September 2009 offering of senior notes and other existing cash. The Varian merger has been accounted for in accordance with the authoritative accounting guidance and the results of Varian are included in Agilent's consolidated financial statements from the date of merger. For additional details related to the acquisition of Varian, see Note 3, Acquisition of Varian.

Looking forward, we will continue integrating Varian's order fulfillment systems and processes into Agilent and our priority is to focus on revenue and cost synergies, as well as increase technology sharing between our businesses. As a result of the integration of Varian into Agilent, we are expecting to achieve \$100 million in net cost savings. Approximately 1/3 of the net cost savings will be generated within general and administrative expenses by the end of this fiscal year and the remaining savings within the costs of products and services by the end of fiscal 2013.

**Critical Accounting Policies and Estimates**

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our condensed consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles (GAAP) in the U.S. The preparation of condensed consolidated financial statements in conformity with GAAP in the U.S. requires management to make estimates, judgments and assumptions that affect the amounts reported in our condensed consolidated financial statements and accompanying notes. Our critical accounting policies are those that affect our financial statements materially and involve difficult, subjective or complex judgments by management. Those policies are revenue recognition, inventory valuation, share-based compensation, retirement and post-retirement benefit plan assumptions, goodwill and purchased intangible assets, restructuring and asset impairment charges, and accounting for income taxes, a number of which are described in the following paragraphs. Management bases its estimates on historical experience and various other assumptions believed to be reasonable. Although these estimates are based on management's best knowledge of current events and actions that may impact the company in the future, actual results may be different from the estimates.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used or changes in the accounting estimate that are reasonably likely to occur could materially change the financial statements.

*Revenue recognition.* We enter into agreements to sell products (hardware or software), services, and other arrangements (multiple element arrangements) that include combinations of products and services. Revenue from product sales, net of trade discounts and allowances, is recognized provided that persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable, and collectability is reasonably assured. Delivery is considered to have occurred when title and risk of loss have transferred to the customer. Revenue is reduced for estimated product returns, when appropriate. For sales that include customer-specified acceptance criteria, revenue is recognized after the acceptance criteria have been met. For products that include installation, if the installation meets the criteria to be considered a separate element, product revenue is recognized upon delivery, and recognition of installation revenue occurs when the installation is complete. Otherwise, neither the product nor the installation revenue is recognized until the installation is complete. Revenue from services is deferred and recognized over the contractual period or as services are rendered and accepted by the customer. We allocate revenue to each element in our multiple-element arrangements based upon their relative selling prices. We determine the selling price for each deliverable based on a selling price hierarchy. The selling price for a deliverable is based on our vendor specific objective evidence (VSOE) if available, third-party evidence (TPE) if VSOE is not available, or estimated selling price (ESP) if neither VSOE nor TPE is available. Revenue from the sale of software products that are not required to deliver the tangible product's essential functionality are accounted for under software revenue recognition rules. Revenue allocated to each element is then recognized when the basic revenue recognition criteria for that element have been met. The amount of product revenue recognized is affected by our judgments as to whether an arrangement includes multiple elements.

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We use VSOE of selling price in the selling price allocation in all instances where it exists. VSOE of selling price for products and services is determined when a substantial majority of the selling prices fall within a reasonable range when sold separately. TPE of selling price can be established by evaluating largely interchangeable competitor products or services in standalone sales to similarly situated customers. As our products contain a significant element of proprietary technology and the solution offered differs substantially from that of competitors, it is difficult to obtain the reliable standalone competitive pricing necessary to establish TPE. ESP represents the best estimate of the price at which we would transact a sale if the product or service were sold on a standalone basis. We determine ESP for a product or service by using historical selling prices which reflect multiple factors including, but not limited to customer type, geography, market conditions, competitive landscape, gross margin objectives and pricing practices. The determination of ESP is made through consultation with and approval by management. We may modify or develop new pricing practices and strategies in the future. As these pricing strategies evolve, we may modify our pricing practices in the future, which may result in changes in ESP. The aforementioned factors may result in a different allocation of revenue to the deliverables in multiple element arrangements from the current fiscal quarter, which may change the pattern and timing of revenue recognition for these elements but will not change the total revenue recognized for the arrangement.

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*Share-based compensation.* We estimate the stock price volatility using the historical volatility of Agilent's stock options over the most recent historical period equivalent to the expected life of stock options. In reaching this conclusion, we have considered many factors including the extent to which our options are currently traded and our ability to find traded options in the current market with similar terms and prices to the options we are valuing. A 10 percent increase in our estimated historical volatility from 35 percent to 45 percent for our most recent employee stock option grant would generally increase the value of an award and the associated compensation cost by approximately 23 percent if no other factors were changed. In estimating the expected life of our options granted we considered the historical option exercise behavior of our executive employees, which we believe is representative of future behavior.

*Goodwill and purchased intangible assets.* Agilent reviews goodwill for impairment annually during our fourth fiscal quarter and whenever events or changes in circumstances indicate the carrying value may not be recoverable. As defined in the authoritative guidance, a reporting unit is an operating segment, or one level below an operating segment. We have aggregated components of an operating segment that have similar economic characteristics into our reporting units. We have three reporting units for goodwill impairment testing purposes: life sciences, chemical analysis and electronic measurement. We test goodwill for possible impairment by first determining the fair value of the related reporting unit and comparing this value to the recorded net assets of the reporting unit, including goodwill.

The process of evaluating the potential impairment of goodwill is highly subjective and requires significant judgment, as our businesses operate in a number of markets and geographical regions. We determine the fair value of our reporting units based on an income approach, whereby we calculate the fair value of each reporting unit based on the present value of estimated future cash flows, which are formed by evaluating historical trends, current budgets, operating plans and industry data. We evaluate the reasonableness of the fair value calculations of our reporting units by reconciling the total of the fair values of all of our reporting units to our total market capitalization, taking into account an appropriate control premium. We then compare the carrying value of our reporting units to the fair value calculations based on the income approach. Estimates of the future cash flows associated with the businesses are critical to these assessments. The assumptions used in the fair value calculation change from year to year and include revenue growth rates, operating margins, risk adjusted discount rates and future economic and market conditions. Changes in these assumptions based on changed economic conditions or business strategies could result in material impairment charges in future periods.

The circumstances that could trigger a goodwill impairment could include, but are not limited to, the following items to the extent that management believes the occurrence of one or more would make it more likely than not that we would fail step 1 of the goodwill impairment test: significant adverse change in legal factors or in the business climate, an adverse action or assessment by a regulator, unanticipated competition, a loss of key personnel, a more-likely-than-not expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed of, a portion of a reporting unit's goodwill has been included in the carrying amounts of a business that will be disposed of or if our market capitalization is below our net book value.

The results of our test for goodwill impairment, as of September 30, 2010, showed that the estimated fair values of our life sciences, chemical analysis and electronic measurement reporting units exceeded their carrying values in excess of \$1 billion for each reporting unit. A 1 percent increase in the discount rate lowered the fair value by approximately 15 percent. There was no impairment of goodwill during the three and nine months ended July 31, 2011 or for the year ended October 31, 2010. We continue to assess the overall environment to determine if we would trigger and fail step 1 of the goodwill impairment test.

Purchased intangible assets consist primarily of acquired developed technologies, proprietary know-how, trademarks, and customer relationships and are amortized using the straight-line method over estimated useful lives ranging from 6 months to 15 years. In process research and development (IPR&D) is initially capitalized at fair value as an intangible asset with an indefinite life and assessed for impairment thereafter. When the IPR&D project is complete, it is reclassified as an amortizable purchased intangible asset and is amortized over its estimated useful life. If an IPR&D project is abandoned, Agilent will record a charge for the value of the related intangible asset to Agilent's consolidated

statement of operations in the period it is abandoned.

We continually monitor events and changes in circumstances that could indicate carrying amounts of long-lived assets, including purchased intangible assets, may not be recoverable. When such events or changes in circumstances occur, we assess the recoverability of long-lived assets by determining whether the carrying value of such assets will be recovered through undiscounted expected future cash flows. If the total of the undiscounted future cash flows is less than the carrying amount of those assets, we recognize an impairment loss based on the excess of the carrying amount over the fair value of the assets. We impaired \$3 million and \$7 million of purchased intangibles and fixed assets in the three and nine months ended July 31, 2011, respectively, mainly related to cessation of portions of certain businesses and vacating certain leasehold improvements.

*Accounting for income taxes.* We must make certain estimates and judgments in determining income tax expense for financial statement purposes. These estimates and judgments occur in the calculation of tax credits, benefits and deductions, and in the calculation of certain tax assets and liabilities which arise from differences in the timing of recognition of revenue and expense for tax

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and financial statement purposes, as well as interest and penalties related to uncertain tax positions. Significant changes to these estimates may result in an increase or decrease to our tax provision in a subsequent period.

Significant management judgment is also required in determining whether deferred tax assets will be realized in full or in part. When it is more likely than not that all or some portion of specific deferred tax assets such as net operating losses or foreign tax credit carryforwards will not be realized, a valuation allowance must be established for the amount of the deferred tax assets that cannot be realized. We consider all available positive and negative evidence on a jurisdiction-by-jurisdiction basis when assessing whether it is more likely than not that deferred tax assets are recoverable. We consider evidence such as our past operating results, the existence of cumulative losses in recent years and our forecast of future taxable income. At July 31, 2011, we provided a partial valuation allowance for our U.S. deferred tax assets and either a full or partial valuation allowance on certain foreign deferred tax assets. We intend to maintain a partial or full valuation allowance in these jurisdictions until sufficient positive evidence exists to support its reversal.

Due to improvements in the U.S. operating results over the past three years, management believes a reasonable possibility exists that, within the next year, sufficient positive evidence may become available to reach a conclusion that a significant portion of the U.S. valuation allowance will no longer be needed.

We have not provided for all U.S. federal income and foreign withholding taxes on the undistributed earnings of some of our foreign subsidiaries because we intend to reinvest such earnings indefinitely. Should we decide to remit this income to the U.S. in a future period, our provision for income taxes may increase materially in that period.

The calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax law and regulations in a multitude of jurisdictions. Although the guidance on the accounting for uncertainty in income taxes prescribes the use of a recognition and measurement model, the determination of whether an uncertain tax position has met those thresholds will continue to require significant judgment by management. If the ultimate resolution of tax uncertainties is different from what is currently estimated, a material impact on income tax expense could result.

**Adoption of New Pronouncements**

See Note 2, New Accounting Pronouncements, to the condensed consolidated financial statements for a description of new accounting pronouncements.

**Restructuring Costs, Asset Impairments and Other Charges**

Our 2009 restructuring program, announced in the first half of 2009, was conceived in response to deteriorating economic conditions and was designed to deliver sufficient savings to enable our businesses to reach their profitability targets throughout the cycle. Workforce reduction payments, primarily severance, were largely complete in fiscal year 2010. Lease payments should primarily be complete by the end of fiscal 2014.

## Foreign Currency

Our revenues, costs and expenses, and monetary assets and liabilities are exposed to changes in foreign currency exchange rates as a result of our global operating and financing activities. We hedge revenues, expenses and balance sheet exposures that are not denominated in the functional currencies of our subsidiaries on a short term and anticipated basis. We do experience some fluctuations within individual lines of the condensed consolidated statement of operations and balance sheet because our hedging program is not designed to offset the currency movements in each category of revenues, expenses, monetary assets and liabilities. Our hedging program is designed to hedge currency movements on a relatively short-term basis (rolling twelve month period). Therefore, we are exposed to currency fluctuations over the longer term.

## Results from Operations

### Orders and Net Revenue

	Three Months Ended July 31,		Nine Months Ended July 31,		Year over Year Change	
	2011	2010	2011	2010	Three Months	Nine Months
	(in millions)					
Orders	\$ 1,687	\$ 1,491	\$ 5,017	\$ 4,057	13%	24%
Net revenue:						
Products	\$ 1,406	\$ 1,147	\$ 4,053	\$ 3,152	23%	29%
Services and other	285	237	834	716	20%	16%
Total net revenue	\$ 1,691	\$ 1,384	\$ 4,887	\$ 3,868	22%	26%

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Net revenue of \$1,691 million and \$4,887 million for the three and nine months ended July 31, 2011, increased 22 percent and 26 percent, respectively, above the same periods last year. Due to the close date of the Varian acquisition which occurred on May 14, 2010, we have excluded the first two weeks of May of this fiscal year when we compare periods without the Varian acquisition. The revenue increase attributable to our acquisitions accounted for 2 percentage points of revenue increase for the three months ended July 31, 2011 when compared to the same period last year. The revenue increase attributable to our acquisitions, less revenue attributable to our divestitures, accounted for 6 percentage points of revenue increase for the nine months ended July 31, 2011 when compared to the same period last year. Revenue growth in the life sciences business, for the three and nine months ended July 31, 2011, was led by demand for products in pharmaceutical and biotechnology markets when compared to the same periods last year. Revenue growth in the chemical analysis business for the three and nine months ended July 31, 2011, was led by strong growth in the petrochemical markets when compared to the same periods last year. Within electronic measurement, revenue from general purpose end-markets improved in the three and nine months ended July 31, 2011 when compared to the same periods last year. Also within electronic measurement, the communications test businesses improved in the three and nine months ended July 31, 2011 when compared to the same periods last year. Revenue growth within the communication test business was higher than in general purpose test with strong wireless manufacturing revenue growth in the three and nine months ended July 31, 2011. For the three and nine months ended July 31, 2011 Agilent's segment revenue was \$1,692 million and \$4,895 million, respectively, an increase of 21 percent and 26 percent, respectively, when compared to the same periods last year. Note 18, Segment Information, shows a reconciliation between segment revenue and net revenue.

Services and other revenue include revenue generated from servicing our installed base of products, warranty extensions and consulting. Services and other revenue increased 20 percent and 16 percent in the three and nine months ended July 31, 2011, respectively, when compared to the same periods last year. The increase in services and other revenue attributable to our acquisitions accounted for 1 percentage point of revenue increase in the three months ended July 31, 2011. The increase in services and other revenue attributable to our acquisitions, less service and other revenue attributable to our divestitures, accounted for 2 percentage points of revenue increase in the nine months ended July 31, 2011. The service and other revenue growth is lower than product revenue growth due to only a proportion of product sales attracting service contracts, the recognition of warranty revenue over an extended period and a portion of the revenue being driven more by the previously installed base than current period product sales.

**Operating Results**

	Three Months Ended July 31,		Nine Months Ended July 31,		Year over Year Change	
	2011	2010	2011	2010	Three Months	Nine Months
Total gross margin	52.7%	52.4%	53.4%	54.2%		(1)ppt
Operating margin	16.6%	8.3%	15.5%	9.4%	8ppts	6ppts
<b>(in millions)</b>						
Research and development	\$ 162	\$ 154	\$ 486	\$ 453	5%	7%
Selling, general and administrative	\$ 449	\$ 456	\$ 1,364	\$ 1,280	(2)%	7%

Total gross margin for the three months ended July 31, 2011 was flat compared to the same period last year. Total gross margin for the nine months ended July 31, 2011 showed a 1 percentage point decrease compared to the same period last year. The decrease in gross margins in the nine months ended July 31, 2011 was mostly due to the unfavorable impact of the Varian acquisition (including fair value adjustments). Operating margins have increased 8 percentage points and 6 percentage points for the three and nine months ended July 31, 2011, respectively, compared to the same periods last year. The increase in operating margin is due to higher volume, reduction in restructuring expenses, benefits from our previously completed restructuring program which were offset by the impact of the Varian acquisition and higher variable and incentive pay.

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Research and development expenses increased 5 percent and 7 percent for the three and nine months ended July 31, 2011, respectively, compared to the same periods last year. Increased expenditures, compared to the same period last year, were mostly due to the Varian acquisition, higher variable and incentive pay and the unfavorable impact of currency movements. We remain committed to invest about 10 percent of revenues in research and development and have focused our development efforts on key strategic opportunities in order to align our business with available markets and position ourselves to capture market share.

Selling, general and administrative expenses decreased 2 percent for the three months ended July 31, 2011 compared to the same period last year. Selling, general and administrative expenses increased 7 percent for the nine months ended July 31, 2011

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compared to the same period last year. The decrease in expenses for the three months ended July 31, 2011 compared with the same period last year were largely the result of reduced acquisition and integration related costs offset by the unfavorable impact of currency movements. Increased expenses in the nine months were due to the Varian acquisition, higher variable and incentive pay and the unfavorable impact of currency movements offset by the impact of decreased restructuring expenses and costs associated with divested businesses.

At July 31, 2011, our headcount was approximately the same as at July 31, 2010.

**Provision for Income Taxes**

For the three and nine months ended July 31, 2011, we recorded an income tax benefit of \$49 million and an income tax provision of \$16 million, respectively, compared to an income tax provision of \$22 million and \$57 million, respectively, for the same periods last year. The income tax benefit and provision for the three and nine months ended July 31, 2011, respectively, includes net discrete tax benefits of \$72 million and \$55 million, respectively and are primarily associated with the recognition of previously unrecognized tax benefits and the reversal of the related interest accruals due to the reassessment of certain foreign uncertain tax positions. The income tax provision for the nine months ended July 31, 2011 also includes a \$29 million out of period adjustment to reduce the carrying value of certain U.K. deferred tax assets, which was recorded in the prior quarter ended April 30, 2011. The overstatement of these deferred tax assets resulted in an overstatement of the U.K. valuation allowance release in the fourth quarter of 2010.

The income tax provision for the three and nine months ended July 31, 2010 includes a net discrete tax expense netting to zero and \$3 million, respectively, relating primarily to tax settlements and lapses of statutes of limitations.

Without considering interest and penalties, the effective tax rate reflects taxes in all jurisdictions except the U.S. and foreign jurisdictions in which income tax expense or benefit continues to be offset by adjustments to valuation allowances. As of July 31, 2011 we intend to maintain partial or full valuation allowances in these jurisdictions until sufficient positive evidence exists to support its reversal. We currently have a valuation allowance of \$334 million of which \$269 million relates to U.S. jurisdictions. Due to improvements in the U.S. operating results over the past three years, management believes a reasonable possibility exists that, within the next year, sufficient positive evidence may become available to reach a conclusion that a significant portion of the U.S. valuation allowance will no longer be needed.

At July 31, 2011, our estimate of the annual effective tax rate, including discrete items was 5 percent. The effective income tax rate including discrete items, for the three and nine months ended July 31, 2011 was an income tax benefit of 17 percent and an income tax provision of 2 percent, respectively. The company determines its interim tax provision using an estimated annual effective tax rate methodology except in jurisdictions where the company anticipates or has a year-to-date ordinary loss for which no tax benefit can be recognized. In these jurisdictions, tax expense is computed based on an actual or discrete method. Our effective tax rate is affected by research tax credits, the expected level of other tax benefits, the effects of business acquisitions and dispositions, the impact of changes to valuation allowances, changes in other comprehensive income, as well as changes in the mix of income and losses in the jurisdictions in which we operate that have varying statutory rates.

In the U.S., tax years remain open back to the year 2006 for federal income tax purposes and the year 2000 for state purposes. In other major jurisdictions where we conduct business, the tax years generally remain open back to the year 2003. With these jurisdictions and the U.S., it is

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possible that there could be significant changes to our unrecognized tax benefits in the next twelve months due to either the expiration of a statute of limitation or a tax audit settlement. Because of the uncertainty as to the timing of a potential settlement or the completion of tax audits, an estimate cannot be made of the range of tax increases or decreases that could occur in the next twelve months.

In December 2010, Agilent reached an agreement with the Internal Revenue Service (IRS) for tax years 2003-2005. In addition, Agilent and the IRS reached an agreement on transfer pricing issues covering years 2003-2007. Tax adjustments resulting from these agreements were offset by applying available net operating losses and tax credit carry forwards. Agilent's U.S. federal income tax returns for 2006 through 2007 are currently under audit by the IRS. As a result of these agreements with the IRS and agreements with other tax jurisdictions, unrecognized tax benefits were reduced from \$656 million at October 31, 2010 to \$489 million at July 31, 2011.

### Segment Overview

Agilent is a measurement company providing core bio-analytical and electronic measurement solutions to the life sciences, chemical analysis, communications and electronics industries. Agilent has three primary businesses focused on the life sciences market, the chemical analysis market and the electronic measurement market.

Table of Contents**Life Sciences**

Our life sciences business provides application-focused solutions that include instruments, software, consumables, and services that enable customers to identify, quantify and analyze the physical and biological properties of substances and products. Key product categories in life sciences include: DNA and RNA microarrays and associated scanner, software, and reagents; microfluidics-based sample analysis systems; liquid chromatography (LC) systems, columns and components; liquid chromatography mass spectrometry (LC-MS) systems; capillary electrophoresis systems; laboratory software and informatics systems; bio-reagents and related products; laboratory automation and robotic systems, dissolution testing; Nuclear Magnetic Resonance (NMR) and Magnetic Resonance Imaging (MRI) systems along with X-Ray crystallography, and services and support for the aforementioned products.

**Orders and Net Revenue**

	Three Months Ended July 31,		Nine Months Ended July 31,		Year over Year Change		
	2011	2010	2011	2010	Three Months	Nine Months	
	(in millions)						
Orders	\$ 445	\$ 391	\$ 1,366	\$ 1,058	14%	29%	
Net revenue	\$ 453	\$ 374	\$ 1,321	\$ 1,048	21%	26%	

Life sciences orders for the three and nine months ended July 31, 2011 increased 14 percent and 29 percent, respectively, when compared to the same periods last year. Excluding the impact of the Varian acquisition, the Hycor divestiture and our recent acquisitions of Biocius and Lab901, orders for the three and nine months ended July 31, 2011 grew 11 percent and 15 percent, respectively, when compared to the same periods last year. Due to the close date of the Varian acquisition which occurred on May 14, 2010, we have excluded the first two weeks of May of this fiscal year when we compare periods without the Varian acquisition. Order results were led by strength in the LC-MS, automation, informatics, consumables, and services portfolios. We saw solid performance in key products, such as the LC/Triple Quadrupole (QQQ) system, SureSelect Complete, and OpenLab software suite. Geographically, excluding the impact of Varian and other recent acquisitions, orders grew 1 percent in the Americas, grew 27 percent in Europe, declined 4 percent in Japan, and grew 13 percent in other Asia Pacific for the three months ended July 31, 2011, when compared to the same period last year. The Americas region was affected by softness in academia and government spending, while Europe benefited from strong order volume in NMR magnets and SureSelect Complete. Excluding acquisitions and the Hycor divestiture, orders grew 10 percent in the Americas, 18 percent in Europe, 4 percent in Japan, and 20 percent in other Asia Pacific for the nine months ended July 31, 2011, when compared to the same period last year.

Life sciences revenues for the three and nine months ended July 31, 2011 increased 21 percent and 26 percent, respectively, when compared to the same periods last year. Excluding the impact of the Varian acquisition, the Hycor divestiture and other recent acquisitions, revenues for the three and nine months ended July 31, 2011 grew 18 percent and 14 percent, respectively, when compared to the same periods last year. Foreign currency movements for the three and nine months ended July 31, 2011 had a favorable currency impact of 6 and 3 percentage points on the growth in revenues, respectively, when compared to the same period last year. Revenue growth was led by the LC, LC-MS, informatics, automation, genomics, consumables, and services portfolios, along with Research Products including NMR and MRI. Geographically, excluding the impact of Varian and other recent acquisitions, revenues grew 22 percent in the Americas, 7 percent in Europe, 19 percent in Japan, and 28 percent in other Asia Pacific for the three months ended July 31, 2011, when compared to the same period last year. Growth in the Americas was helped by an expanded sales channel selling a broader portfolio of products to our customers. Excluding the impact of the Varian acquisition, the Hycor divestiture and other recent acquisitions, revenues grew 16 percent in the Americas, 7 percent in Europe, 10 percent in Japan, and 23 percent in other Asia Pacific for the nine months ended July 31, 2011, when compared to the same period last year.

Good revenue growth momentum continued this quarter in the pharmaceutical and biotech, academic and government, as well as in other applied markets such as petrochemical. Despite budget restrictions in most large pharmaceutical companies, technology refresh programs continue to drive traditional replacement business to move to the latest technologies. In the academic and government market, metabolomics continue to be a strong area of interest and next generation sequencing is very active. In the petrochemical applied market, petroleum and chemical industries are expected to continue profitability improvements and to reinvest in their business.

Looking forward, we expect reasonable momentum in markets such as pharmaceutical and biotech to drive further demand in our instruments and application solutions. With our life sciences sales channel coverage model, we continue to focus on global academic and government accounts. The life sciences business also remains focused on expanding our application portfolio. The Lab901 acquisition will allow us to address the demand for higher automation and throughput for DNA and protein analysis. With the

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acquisition of Biocius Life Sciences and its RapidFire high-throughput mass spectrometry drug-screening technology platform, we are well positioned will allow us to expand our reach within the pharmaceutical market.

In addition, our strategic focus is to pursue the successful integration of the Varian expanded life sciences product portfolio, including complementary products in liquid chromatography, mass spectrometry, consumables, new offerings in dissolution testing, and magnetic resonance (NMR, MRI). We are focusing on improving the Research Product Division growth and profitability. Progress has been made in filling service and sales positions. Additionally, supply chain and manufacturing support have been added and factories are being modified to meet future growth and cost goals.

**Operating Results**

	Three Months Ended July 31,		Nine Months Ended July 31,		Year over Year Change	
	2011	2010	2011	2010	Three Months	Nine Months
Gross margin	51.3%	53.8%	52.2%	54.4%	(3)ppts	(2)ppts
Operating margin	13.2%	14.9%	12.8%	15.2%	(2)ppts	(2)ppts
<b>(in millions)</b>						
Research and development	\$ 44	\$ 37	\$ 131	\$ 103	19%	27%
Selling, general and administrative	\$ 129	\$ 108	\$ 390	\$ 308	19%	27%

Gross margins for products and services for the three and nine months ended July 31, 2011 decreased 3 percentage points and 2 percentage points, respectively, compared to the same periods last year. For the three months ended July 31, 2011, the decrease was due to higher logistics costs, higher consumables costs, and unfavorable product mix. For the nine months ended July 31, 2011, higher production costs in Research Products, including NMR and MRI, higher logistics costs, and higher consumables costs were the main factors for the decrease.

Research and development expenses for the three and nine months ended July 31, 2011, increased 19 percent and 27 percent, respectively, compared to the same periods last year. Increases during these periods were due to acquisitions (Varian, Lab901, and Biocius) and continued investments in new product development.

Selling, general and administrative expenses for the three and nine months ended July 31, 2011 increased 19 percent and 27 percent, respectively, compared to the same periods last year. For the three months ended July 31, 2011, the increase was due to acquisitions (Varian, Lab901, and Biocius), higher commissions, and investments in sales channel coverage partially offset by lower discretionary spending. For the nine months ended July 31, 2011, the increase was due to acquisitions, higher commissions, and investments in sales channel coverage partially offset by the Hycor divestiture.

Operating margins for products and services for the three and nine months ended July 31, 2011 decreased 2 percentage points in both periods compared to the same periods last year. Factors which led to operating margin variances for these periods are collectively highlighted in the above discussions on gross margins, research and development expenses, and selling, general and administrative expenses.

*Income from Operations*

Income from operations for the three and nine months ended July 31, 2011 increased \$4 million and \$10 million, respectively, on a corresponding revenue increase of \$79 million and \$273 million. The resultant year-over-year operating margin incremental was 5 percent and 4 percent for these periods, respectively. Excluding the impact of Varian and other recent acquisitions, the year-over-year operating margin incremental for the three and nine months ended July 31, 2011 were approximately 15 percent and 32 percent, respectively.

**Chemical Analysis**

Our chemical analysis business provides application-focused solutions that include instruments, software, consumables, and services that enable customers to identify, quantify and analyze the physical and biological properties of substances and products. Key product categories in chemical analysis include: gas chromatography (GC) systems, columns and components; gas

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chromatography mass spectrometry (GC-MS) systems; inductively coupled plasma mass spectrometry (ICP-MS) instruments; atomic absorption (AA) instruments; inductively coupled plasma optical emission spectrometry (ICP-OES) instruments; software and data systems; vacuum pumps and measurement technologies; services and support for our products.

**Orders and Net Revenue**

	Three Months Ended July 31,		Nine Months Ended July 31,		Year over Year Change	
	2011	2010	2011	2010	Three Months	Nine Months
	(in millions)					
Orders	\$ 400	\$ 350	\$ 1,168	\$ 823	14%	42%
Net revenue	\$ 383	\$ 329	\$ 1,113	\$ 811	17%	37%

Chemical analysis orders for the three and nine months ended July 31, 2011 increased 14 percent and 42 percent, respectively, when compared to the same periods last year. Excluding the Varian and A2 Technologies Inc. acquisitions, orders for the three and nine months ended July 31, 2011 grew 9 percent and 14 percent, respectively, when compared to the same periods last year. Due to the close date of the Varian acquisition which occurred on May 14, 2010, we have excluded the first two weeks of May of this fiscal year when we compare periods without the Varian acquisition. Order results were led by solid performance in the GC, GC-MS, AA, ICP-OES instruments, along with consumables and services. Growth in the services and support business was driven by strength in compliance and preventive maintenance services, and continued growth in multi-vendor business. Continued strength in replacement cycle purchasing drove solid order performance in instruments such as the 7890A GC, autosampler and 5975 series GC-MS. Orders were also strong in 7000 series GC Triple Quadrupole (QQQ) as customers continue to invest in new technology, particularly in the food and environmental markets. Geographically, excluding the impact of the Varian and A2 Technologies acquisitions, orders were flat in the Americas, grew 5 percent in Europe, grew 5 percent in Japan, and grew 23 percent in other Asia Pacific for the three months ended July 31, 2011 when compared to the same period last year. Europe has softened due to Western Europe economic concerns, while China was a major growth driver. Excluding the impact of the Varian and A2 Technologies acquisitions, orders grew 9 percent in the Americas, grew 12 percent in Europe, declined 1 percent in Japan, and grew 27 percent in other Asia Pacific for the nine months ended July 31, 2011 when compared to the same period last year.

Chemical analysis revenues for the three and nine months ended July 31, 2011 increased 17 percent and 37 percent, respectively, when compared to the same periods last year. Excluding the Varian and A2 Technologies acquisitions, revenues for the three and nine months ended July 31, 2011 grew 11 percent and 10 percent, respectively, when compared to the same periods last year. Foreign currency movements for the three and nine months ended July 31, 2011 had an favorable currency impact of 7 and 3 percentage points on the growth in revenues, respectively, when compared to the same period last year. Revenue growth was led by the GC, GC-MS, ICP-MS, and Vacuum portfolios, along with services. Geographically, excluding the impact of the acquisitions, revenues grew 1 percent in the Americas, declined 2 percent in Europe, grew 27 percent in Japan, and grew 34 percent in other Asia Pacific for the three months ended July 31, 2011 when compared to the same period last year. Unexpectedly strong results in the Americas from the same quarter last year due to the Gulf of Mexico oil spill activity and United States government stimulus spending negatively impacted year over year comparisons. Excluding the Varian and A2 Technologies acquisitions, revenues grew 8 percent in the Americas, grew 5 percent in Europe, declined 2 percent in Japan, and grew 23 percent in other Asia Pacific for the nine months ended July 31, 2011 when compared to the same period last year.

Growth in core end markets continues. The energy, chemical, and food markets remain strong, while the environmental market is particularly strong in China. In the petrochemical market, petroleum and chemical industries are expected to take advantage of their strong financial position to replace aging instrumentation and acquire new capabilities. In the food market, the demand to export safe and high quality food in emerging markets, especially China, remains robust. Globalization of the food supply generates business risk for food producers, and our instruments help mitigate that risk. The demand continues to drive increased testing capacity and instrument purchases in all product categories, consumables, and services. In the environmental market, discovery of emerging contaminants continues to be important research to protect the public health in

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mature geographies while demand for safe drinking water is strong in emerging economies. Both factors drive increased instrument purchases, especially high end mass spectrometry instruments.

Looking forward, we will continue to focus on the successful integration of Varian. With Varian, our chemical analysis product portfolio has new offerings in spectroscopy and vacuum technologies, complementary mass spectrometry products, and an expanded consumables portfolio which are being leveraged globally with an integrated sales team. We are focusing on improvements in profitability of the Varian portfolio by refreshing products and leveraging our Asia supply chain. In addition to driving value from our acquisitions, we continue to focus on expanding our core product and service offerings with a particular focus on expanding our leadership position in developing countries.

Table of Contents**Operating Results**

	Three Months Ended July 31,		Nine Months Ended July 31,		Year over Year Change	
	2011	2010	2011	2010	Three Months	Nine Months
Gross margin	50.7%	52.7%	50.7%	53.9%	(2)ppts	(3)ppts
Operating margin	20.6%	21.0%	21.4%	23.8%	ppts	(2)ppts
<b>(in millions)</b>						
Research and development	\$ 23	\$ 20	\$ 69	\$ 47	12%	47%
Selling, general and administrative	\$ 93	\$ 84	\$ 279	\$ 197	10%	41%

Gross margins for products and services for the three and nine months ended July 31, 2011 decreased 2 percentage points and 3 percentage points, respectively, compared to the same periods last year. Decreases for these periods were due to the impact of the Varian portfolio, higher logistics costs, and unfavorable currency movements.

Research and development expenses for the three and nine months ended July 31, 2011 increased 12 percent and 47 percent, respectively, compared to the same periods last year. Increases during these periods were due to the Varian acquisition and investments in product R&D to support ongoing portfolio enhancement and expansion.

Selling, general and administrative expenses for the three and nine months ended July 31, 2011 increased 10 percent and 41 percent, respectively, compared to the same periods last year. For the three months ended July 31, 2011, increases were due primarily to the Varian and A2 Technologies acquisitions, higher commissions, and investments in sales channel coverage partially offset by lower discretionary spending. For the nine months ended July 31, 2011, increases were due to the Varian acquisition, higher commissions, and investments in sales channel coverage.

Operating margin for products and services for the three months ended July 31, 2011 was relatively flat compared to the same period last year. Operating margin for products and services for the nine months ended July 31, 2011 decreased 2 percentage points compared to the same period last year. Factors which led to operating margin variances for these periods are collectively highlighted in the above discussions on gross margins, research and development expenses, and selling, general and administrative expenses.

**Income from Operations**

Income from operations for the three and nine months ended July 31, 2011 increased \$10 million and \$23 million, respectively, on a corresponding revenue increase of \$54 million and \$302 million. The resultant year-over-year operating margin incremental was 19 percent and 8 percent for these periods, respectively. Excluding the impact of the Varian and A2 Technologies acquisitions, the year-over-year operating margin incremental for the three and nine months ended July 31, 2011 were approximately 32 percent and 29 percent, respectively.

**Electronic Measurement**

Our electronic measurement business provides electronic measurement instruments and systems, software design tools and related services that are used in the design, development, manufacture, installation, deployment and operation of electronics equipment, and microscopy products. Related services include start-up assistance, instrument productivity and application services and instrument calibration and repair. We also offer customization, consulting and optimization services throughout the customer's product lifecycle.

***Orders and Net Revenue***

<b>Three Months Ended</b>		<b>Nine Months Ended</b>		<b>Year over Year Change</b>	
<b>July 31,</b>		<b>July 31,</b>		<b>Three</b>	<b>Nine</b>
<b>2011</b>	<b>2010</b>	<b>2011</b>			