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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

(Mark One)

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

For the quarterly period ended October 1, 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 1-4171

KELLOGG COMPANY

State of Incorporation Delaware IRS Employer Identification No.38-0710690

One Kellogg Square, P.O. Box 3599, Battle Creek, MI 49016-3599

Registrant s telephone number: 269-961-2000

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 x 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 shorter period that the registrant was required to submit and post such files).

Yes x No ¨

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

Common Stock outstanding as of October 29, 2011 359,150,227 shares

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KELLOGG COMPANY

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Part I FINANCIAL INFORMATION

Item 1. Financial Statements.

Kellogg Company and Subsidiaries

CONSOLIDATED BALANCE SHEET

(millions, except per share data)

	October 1, 2011 (unaudited)	January 1, 2011 *
Current assets		
Cash and cash equivalents	**$ 582**	$ 444
Accounts receivable, net	**1,302**	1,190
Inventories:		
Raw materials and supplies	**252**	224
Finished goods and materials in process	**761**	832
Deferred income taxes	**159**	110
Other prepaid assets	**122**	115
Total current assets	**3,178**	2,915
Property, net of accumulated depreciation of $4,858 and $4,690	**3,193**	3,128
Goodwill	**3,622**	3,628
Other intangibles, net of accumulated amortization of $48 and $47	**1,455**	1,456
Pension	**480**	333
Other assets	**335**	387
Total assets	**$ 12,263**	$ 11,847
Current liabilities		
Current maturities of long-term debt	**$**	$ 952
Notes payable	**737**	44
Accounts payable	**1,200**	1,149
Accrued advertising and promotion	**446**	405
Accrued income taxes	**18**	60
Accrued salaries and wages	**239**	153
Other current liabilities	**461**	421
Total current liabilities	**3,101**	3,184
Long-term debt	**5,300**	4,908
Deferred income taxes	**790**	697
Pension liability	**195**	265
Nonpension postretirement benefits	**191**	214
Other liabilities	**401**	425
Commitments and contingencies		

Equity		
Common stock, $.25 par value	**105**	105
Capital in excess of par value	**510**	495
Retained earnings	**6,644**	6,122
Treasury stock, at cost	**(3,050)**	(2,650)
Accumulated other comprehensive income (loss)	**(1,926)**	(1,914)
Total Kellogg Company equity	**2,283**	2,158
Noncontrolling interests	**2**	(4)
Total equity	**2,285**	2,154
Total liabilities and equity	**$ 12,263**	$ 11,847

* Condensed from audited financial statements.
Refer to Notes to Consolidated Financial Statements.

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Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF INCOME

(millions, except per share data)

	Quarter ended		Year-to-date period ended	
(Results are unaudited)	**October 1, 2011**	October 2, 2010	**October 1, 2011**	October 2, 2010
Net sales	**$ 3,312**	$ 3,157	**$10,183**	$9,537
Cost of goods sold	**1,962**	1,788	**5,969**	5,438
Selling, general and administrative expense	**886**	828	**2,635**	2,438
Operating profit	**464**	541	**1,579**	1,661
Interest expense	**58**	62	**178**	188
Other income (expense), net	**(9)**	1	**(10)**	9
Income before income taxes	**397**	480	**1,391**	1,482
Income taxes	**107**	143	**394**	427
Net income	**$ 290**	$ 337	**$997**	$1,055
Net income (loss) attributable to noncontrolling interests		(1)	**(2)**	(3)
Net income attributable to Kellogg Company	**$ 290**	$ 338	**$999**	$1,058
Per share amounts:				
Basic	**$ 0.81**	$ 0.91	**$2.75**	$2.80
Diluted	**$ 0.80**	$ 0.90	**$2.73**	$2.78
Dividends per share	**$ 0.430**	$ 0.405	**$1.240**	$1.155
Average shares outstanding:				
Basic	**360**	373	**363**	378
Diluted	**363**	376	**365**	381
Actual shares outstanding at period end			**359**	368

Refer to Notes to Consolidated Financial Statements.

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Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF EQUITY

(millions)

	Common stock		Capital in excess of	Retained	Treasury stock		Accumulated other comprehensive	Total Kellogg Company	Non-controlling	Total	Total comprehensive
(unaudited)	shares	amount	par value	earnings	shares	amount	income (loss)	equity	interests	equity	income (loss)
Balance, January 2, 2010	419	$105	$ 472	$5,481	38	$(1,820)	$ (1,966)	$ 2,272	$ 3	$ 2,275	
Common stock repurchases					21	(1,057)		(1,057)		(1,057)	
Net income (loss)				1,247				1,247	(7)	1,240	$ 1,240
Dividends				(584)				(584)		(584)	
Other comprehensive income							52	52		52	52
Stock compensation			19					19		19	
Stock options exercised and other			4	(22)	(5)	227		209		209	
Balance, January 1, 2011	419	$105	$ 495	$6,122	54	$(2,650)	$ (1,914)	$ 2,158	$ (4)	$ 2,154	$ 1,292
Common stock repurchases					13	(688)		(688)		(688)	
Acquisition of noncontrolling interest			(8)					(8)	8		
Net income (loss)				999				999	(2)	997	997
Dividends				(452)				(452)		(452)	
Other comprehensive income							(12)	(12)		(12)	(12)
Stock compensation			17					17		17	
Stock options exercised and other			6	(25)	(6)	288		269		269	
Balance, October 1, 2011	**419**	**$105**	**$ 510**	**$6,644**	**61**	**$(3,050)**	**$ (1,926)**	**$ 2,283**	**$ 2**	**$ 2,285**	**$ 985**

Refer to Notes to Consolidated Financial Statements.

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Kellogg Company and Subsidiaries

CONSOLIDATED STATEMENT OF CASH FLOWS

(millions)

(unaudited)	Year-to-date period ended **October 1, 2011**	October 2, 2010
Operating activities		
Net income	**$997**	$1,055
Adjustments to reconcile net income to operating cash flows:		
Depreciation and amortization	**270**	265
Deferred income taxes	**(2)**	(53)
Other	**133**	116
Postretirement benefit plan contributions	**(187)**	(45)
Changes in operating assets and liabilities:		
Trade receivables	**(224)**	(125)
Inventories	**43**	(43)
Accounts payable	**51**	68
Accrued income taxes	**85**	63
Accrued interest expense	**14**	(18)
Accrued and prepaid advertising, promotion and trade allowances	**25**	33
Accrued salaries and wages	**86**	(161)
All other current assets and liabilities	**(22)**	(76)
Net cash provided by operating activities	**1,269**	1,079
Investing activities		
Additions to properties	**(392)**	(252)
Other	**11**	2
Net cash used in investing activities	**(381)**	(250)
Financing activities		
Net issuances of notes payable	**689**	547
Issuances of long-term debt	**397**	
Reductions of long-term debt	**(946)**	(1)
Net issuances of common stock	**265**	178
Common stock repurchases	**(693)**	(907)
Cash dividends	**(452)**	(435)
Other	**10**	7
Net cash used in financing activities	**(730)**	(611)
Effect of exchange rate changes on cash and cash equivalents	**(20)**	7
Increase in cash and cash equivalents	**138**	225
Cash and cash equivalents at beginning of period	**444**	334
Cash and cash equivalents at end of period	**$582**	$559

Refer to Notes to Consolidated Financial Statements.

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Notes to Consolidated Financial Statements

for the quarter ended October 1, 2011 (unaudited)

Note 1 Accounting Policies

Basis of presentation

The unaudited interim financial information of Kellogg Company (the Company) included in this report reflects normal recurring adjustments that management believes are necessary for a fair statement of the results of operations, financial position, equity and cash flows for the periods presented. This interim information should be read in conjunction with the financial statements and accompanying notes contained on pages 27 to 57 of the Company s 2010 Annual Report on Form 10-K.

The condensed balance sheet data at January 1, 2011 was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States. The results of operations for the quarterly period ended October 1, 2011 are not necessarily indicative of the results to be expected for other interim periods or the full year.

Accounting standards to be adopted in future periods

In September 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2011-08, Testing Goodwill for Impairment, allowing entities the option to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. Under ASU No. 2011-08, an entity would not be required to calculate the fair value of a reporting unit unless the entity determines, based on a qualitative assessment, that it is more likely than not that its fair value is less than its carrying amount. ASU No. 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. The Company will consider early adoption of ASU 2011-08 in connection with its annual goodwill impairment evaluation in the fourth quarter of 2011.

In June 2011, the FASB issued ASU No. 2011-05, Presentation of Comprehensive Income, requiring most entities to present items of net income and other comprehensive income either in one continuous statement referred to as the statement of comprehensive income or in two separate, but consecutive, statements of net income and other comprehensive income. The update does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. ASU No. 2011-05 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011 and should be applied retrospectively. Early adoption is permitted. The Company will be adopting ASU 2011-05 at the beginning of its 2012 fiscal year.

Note 2 Goodwill and other intangible assets

Changes in the carrying amount of goodwill for the quarter ended October 1, 2011 are presented in the following table.

Carrying amount of goodwill

(millions)	North America	Europe	Latin America	Asia Pacific (a)	Consolidated
January 1, 2011	$3,539	$62	$	$27	$3,628
Currency translation adjustment		(5)		(1)	(6)
October 1, 2011	**$3,539**	**$57**	**$**	**$26**	**$3,622**

(a) Includes Australia, Asia and South Africa.

Intangible assets subject to amortization

	Gross carrying amount		Accumulated amortization	
(millions)	**October 1, 2011**	January 1, 2011	**October 1, 2011**	January 1, 2011
Trademarks	**$19**	$19	**$17**	$16
Other	**41**	41	**31**	31
Total	**$60**	$60	**$48**	$47

For intangible assets in the preceding table, amortization was less than $1 million for each of the current and prior year comparable quarters. The currently estimated aggregate annual amortization expense for full-year 2011 and each of the four succeeding fiscal years is approximately $2 million.

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Intangible assets not subject to amortization

	Total carrying amount	
(millions)	**October 1, 2011**	January 1, 2011
Trademarks	**$ 1,443**	$ 1,443

Note 3 Exit or disposal activities

The Company views its continued spending on cost-reduction activities as part of its ongoing operating principles to provide greater visibility in achieving its long-term profit growth targets. Initiatives undertaken are currently expected to recover cash implementation costs within a five-year period of completion. Upon completion (or as each major stage is completed in the case of multi-year programs), the project begins to deliver cash savings and/or reduced depreciation.

2011 activities

During 2011, the Company incurred exit costs related to ongoing programs which will result in cost of goods sold (COGS) and selling, general and administrative (SGA) expense savings.

Total charges incurred during the quarter and year-to-date periods ended October 1, 2011 and October 2, 2010 were as follows:

	Quarter ended, October 1, 2011			Quarter ended, October 2, 2010		
(millions)	**COGS program**	**SGA programs**	**Total**	COGS program	SGA programs	Total
Employee severance	**$1**	**$1**	**$2**	$	$1	$1
Other cash costs (a)	**1**		**1**		1	1
Asset write-offs	**1**		**1**			
Retirement benefits (b)		**6**	**6**		5	5
Total	**$3**	**$7**	**$10**	$	$7	$7

(a) Includes cash costs for equipment removal and relocation.
(b) Pension plan curtailment losses and special termination benefits.

	Year-to-date period ended, October 1, 2011			Year-to-date period ended, October 2, 2010		
(millions)	**COGS program**	**SGA programs**	**Total**	COGS program	SGA programs	Total
Employee severance	**$ 5**	**$ 1**	**$ 6**	$ 2	$ 2	$ 4
Other cash costs (a)	**1**		**1**		6	6
Asset write-offs	**2**		**2**			
Retirement benefits (b)		**12**	**12**	1	5	6
Total	**$ 8**	**$13**	**$21**	$ 3	$13	$16

(a) Includes cash costs for equipment removal and relocation.
(b) Pension plan curtailment losses and special termination benefits.

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Total program costs incurred through October 1, 2011 were as follows:

(millions)	Total program costs through October 1, 2011 COGS program	SGA programs	Total
Employee severance	**$23**	**$21**	**$44**
Other cash costs (a)	**7**	**15**	**22**
Asset write-offs	**3**		**3**
Retirement benefits (b)	**3**	**17**	**20**
Total	**$36**	**$53**	**$89**

(a) Includes cash costs for equipment removal and relocation.
(b) Pension plan curtailment losses and special termination benefits.

In 2009, the Company commenced various COGS related cost reduction programs. Refer to page 36 of the Company s 2010 Annual Report on Form 10-K for further information on these initiatives. Costs impacted the following operating segments during the quarter and year-to-date periods ended October 1, 2011 and October 2, 2010.

	COGS program			
	Quarter ended		Year-to-date period ended	
(millions)	**October 1, 2011**	October 2, 2010	**October 1, 2011**	October 2, 2010
North America	**$**	$	**$**	$1
Europe	**3**		**8**	2
Total	**$ 3**	$	**$ 8**	$3

These costs represent employee severance and other cash costs associated with the elimination of hourly and salaried positions, as well as non-cash asset write offs at various global manufacturing facilities. To date, we have incurred $36 million in total exit costs for this program. The costs have impacted our operating segments, as follows (in millions): North America-$14; Europe-$21; and Asia Pacific-$1. Based on forecasted exchange rates, the Company currently expects to incur an additional $7 million in exit costs for this program during 2011.

In 2009, the Company commenced various SGA programs which resulted in an improvement in the efficiency and effectiveness of various support functions. Refer to page 37 of the Company s 2010 Annual Report on Form 10-K for further information on these initiatives. Costs for these programs impacted the following operating segments during the quarter and year-to-date periods ended October 1, 2011 and October 2, 2010 as follows:

	SGA programs			
	Quarter ended		Year-to-date period ended	
(millions)	**October 1, 2011**	October 2, 2010	**October 1, 2011**	October 2, 2010
North America	**$7**	$6	**$13**	$10
Europe		1		1
Asia Pacific (a)				2
Total	**$7**	$7	**$13**	$13

(a) Includes Australia, Asia and South Africa.

These costs represent severance and other cash costs associated with the elimination of positions. To date, we have incurred $53 million in exit costs for these programs. The costs have impacted our operating segments as follows (in millions): North America-$34; Europe-$15; Asia Pacific-$3; and Latin America-$1. Based on forecasted exchange rates, the Company currently expects to incur an additional $1 million in exit costs for these programs during 2011.

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Reserves for the COGS and SGA programs are primarily for employee severance and will be paid out by the end of 2011. The detail is as follows:

(millions)	Balance January 1, 2011	Accruals	Payments	**Balance October 1, 2011**
COGS program	$2	$5	$(6)	**$1**
SGA programs	3	1	(3)	**1**
Total	$5	$6	$(9)	**$2**

Note 4 Equity

Earnings per share

Basic earnings per share is determined by dividing net income attributable to Kellogg Company by the weighted average number of common shares outstanding during the period. Diluted earnings per share is similarly determined, except that the denominator is increased to include the number of additional common shares that would have been outstanding if all dilutive potential common shares had been issued. Dilutive potential common shares consist principally of employee stock options issued by the Company, and to a lesser extent, certain contingently issuable performance shares. Basic earnings per share is reconciled to diluted earnings per share in the following table. The total number of anti-dilutive potential common shares excluded from the reconciliation were 5 million and 4 million for the quarter and year-to-date periods ended October 1, 2011, respectively, and 9 million and 4 million for the quarter and year-to-date periods ended October 2, 2010, respectively.

Quarters ended October 1, 2011 and October 2, 2010:

(millions, except per share data)	**Net income attributable to Kellogg Company**	**Average shares outstanding**	**Earnings per share**
2011			
Basic	**$290**	**360**	**$0.81**
Dilutive potential common shares		**3**	**(0.01)**
Diluted	**$290**	**363**	**$0.80**
2010			
Basic	$338	373	$0.91
Dilutive potential common shares		3	(0.01)
Diluted	$338	376	$0.90

Year-to-date period ended October 1, 2011 and October 2, 2010:

(millions, except per share data)	**Net income attributable to Kellogg Company**	**Average shares outstanding**	**Earnings per share**
2011			
Basic	**$ 999**	**363**	**$2.75**
Dilutive potential common shares		**2**	**(0.02)**
Diluted	**$ 999**	**365**	**$2.73**
2010			
Basic	$1,058	378	$2.80
Dilutive potential common shares		3	(0.02)
Diluted	$1,058	381	$2.78

During the year-to-date period ended October 1, 2011, the Company issued 0.4 million shares to employees and directors under various benefit plans and stock purchase programs. Equity-based compensation is discussed further in Note 6.

On April 23, 2010, the Company s board of directors authorized a $2.5 billion three-year share repurchase program for 2010 through 2012. During the year-to-date period ended October 1, 2011, the Company repurchased 13 million shares of common stock for a total of $688 million. During the year-to-date period ended October 2, 2010, the Company repurchased 18 million shares of common stock for a total of $907 million.

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Comprehensive income

Comprehensive income includes net income and all other changes in equity during a period except those resulting from investments by or distributions to shareholders. Other comprehensive income for all periods presented consists of foreign currency translation adjustments, fair value adjustments associated with cash flow hedges and adjustments for net experience losses and prior service cost related to employee benefit plans.

During the first quarter of 2010, the Company amended its U.S. postretirement healthcare benefit plan, which resulted in a $17 million decrease of a deferred tax asset.

Quarter ended October 1, 2011:

(millions)	Pre-tax amount	Tax (expense) or benefit	After-tax amount
2011			
Net income			**$290**
Other comprehensive income:			
Foreign currency translation adjustments	**$(188)**	**$**	**(188)**
Cash flow hedges:			
Unrealized gain (loss) on cash flow hedges	**(1)**		**(1)**
Reclassification to net earnings	**1**		**1**
Postretirement and postemployment benefits:			
Amounts arising during the period:			
Net experience gain (loss)	**4**	**(2)**	**2**
Prior service credit (cost)	**1**		**1**
Reclassification to net earnings:			
Net experience loss	**33**	**(12)**	**21**
Prior service cost	**4**	**(1)**	**3**
	$(146)	**$(15)**	**(161)**
Total comprehensive income			**$129**

Quarter ended October 2, 2010:

(millions)	Pre-tax amount	Tax (expense) or benefit	After-tax amount
2010			
Net income			$337
Other comprehensive income:			
Foreign currency translation adjustments	$163	$	163
Cash flow hedges:			
Unrealized gain (loss) on cash flow hedges	(2)	1	(1)
Reclassification to net earnings	6	(1)	5
Postretirement and postemployment benefits:			
Amounts arising during the period:			
Net experience gain (loss)	(27)	8	(19)
Prior service credit (cost)	(2)		(2)
Reclassification to net earnings:			
Net experience loss	25	(8)	17
Prior service cost	3	(1)	2
	$166	$(1)	165
Total comprehensive income			$502

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Year-to-date period ended October 1, 2011:

(millions)	Pre-tax amount	Tax (expense) or benefit	After-tax amount
2011			
Net income			**$ 997**
Other comprehensive income:			
Foreign currency translation adjustments	**$(45)**	**$**	**(45)**
Cash flow hedges:			
Unrealized gain (loss) on cash flow hedges	**(36)**	**12**	**(24)**
Reclassification to net earnings	**(10)**	**4**	**(6)**
Postretirement and postemployment benefits:			
Amounts arising during the period:			
Net experience gain (loss)	**(9)**	**2**	**(7)**
Reclassification to net earnings:			
Net experience loss	**97**	**(34)**	**63**
Prior service cost	**10**	**(3)**	**7**
	$7	**$ (19)**	**(12)**
Total comprehensive income			**$985**

Year-to-date period ended October 2, 2010:

(millions)	Pre-tax amount	Tax (expense) or benefit	After-tax amount
2010			
Net income			$ 1,055
Other comprehensive income:			
Foreign currency translation adjustments	$5	$	5
Cash flow hedges:			
Unrealized gain (loss) on cash flow hedges	(41)	12	(29)
Reclassification to net earnings	37	(10)	27
Postretirement and postemployment benefits:			
Amounts arising during the period:			
Net experience gain (loss)	(12)	3	(9)
Prior service credit (cost)		(17)	(17)
Reclassification to net earnings:			
Net experience loss	76	(24)	52
Prior service cost	9	(3)	6
	$ 74	$(39)	35
Total comprehensive income			$1,090

Accumulated other comprehensive income (loss) as of October 1, 2011 and January 1, 2011 consisted of the following:

(millions)	**October 1, 2011**	January 1, 2011
Foreign currency translation adjustments	**$(834)**	$(789)
Cash flow hedges unrealized net gain (loss)	**(5)**	25
Postretirement and postemployment benefits:		
Net experience loss	**(1,019)**	(1,075)
Prior service cost	**(68)**	(75)

Total accumulated other comprehensive income (loss)	**$(1,926)**	$(1,914)

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Note 5 Debt

The following table presents the components of notes payable at October 1, 2011 and January 1, 2011:

(millions)	**October 1, 2011**		January 1, 2011	
	Principal amount	**Effective interest rate**	Principal amount	Effective interest rate
U.S. commercial paper	**$707**	**0.27%**	$	%
Bank borrowings	**30**		44	
Total	**$737**		$44	

In August 2011, the Company terminated interest rate swaps with notional amounts totaling $1.5 billion, which were designated as fair value hedges for (a) $750 million of its 4.25% fixed rate U.S. Dollar Notes due 2013 and (b) $750 million of its 5.125% fixed rate U.S. Dollar Notes due 2012 (collectively, the Notes). The interest rate swaps effectively converted the interest rate on the Notes from fixed to variable and the unrealized gain upon termination of $24 million will be amortized to interest expense over the remaining term of the Notes.

In May 2011, the Company issued $400 million of seven-year 3.25% fixed rate U.S. Dollar Notes, using the proceeds from these Notes for general corporate purposes including repayment of commercial paper. The Notes contain customary covenants that limit the ability of the Company and its restricted subsidiaries (as defined) to incur certain liens or enter into certain sale and lease-back transactions, as well as a change of control provision.

During the first quarter of 2011, the Company repaid its $946 million, ten-year 6.6% U.S. Dollar Notes at maturity with U.S. commercial paper.

In March 2011, the Company entered into an unsecured Four-Year Credit Agreement to replace its existing unsecured Five-Year Credit Agreement, which would have expired in November 2011. The Four-Year Credit Agreement allows the Company to borrow, on a revolving credit basis, up to $2.0 billion, to obtain letters of credit in an aggregate amount up to $75 million, U.S. swingline loans in an aggregate amount up to $200 million and European swingline loans in an aggregate amount up to $400 million and to provide a procedure for lenders to bid on short-term debt of the Company. The agreement contains customary covenants and warranties, including specified restrictions on indebtedness, liens, sale and leaseback transactions, and a specified interest coverage ratio. If an event of default occurs, then, to the extent permitted, the administrative agent may terminate the commitments under the credit facility, accelerate any outstanding loans under the agreement, and demand the deposit of cash collateral equal to the lender s letter of credit exposure plus interest.

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Note 6 Stock compensation

The Company uses various equity-based compensation programs to provide long-term performance incentives for its global workforce. Currently, these incentives consist principally of stock options, and to a lesser extent, executive performance shares and restricted stock grants. Additionally, the Company awards restricted stock to its non-employee directors. The interim information below should be read in conjunction with the disclosures included on pages 41 to 44 of the Company s 2010 Annual Report on Form 10-K.

The Company classifies pre-tax stock compensation expense in SGA expense principally within its corporate operations. For the periods presented, compensation expense for all types of equity-based programs and the related income tax benefit recognized were as follows:

	Quarter ended		Year-to-date period ended	
(millions)	**October 1, 2011**	October 2, 2010	**October 1, 2011**	October 2, 2010
Pre-tax compensation expense	**$8**	$ 1	**$30**	$24
Related income tax benefit	**$3**	$	**$11**	$ 8

As of October 1, 2011, total stock-based compensation cost related to non-vested awards not yet recognized was $53 million and the weighted-average period over which this amount is expected to be recognized was 2 years.

Stock options

During the year-to-date periods ended October 1, 2011 and October 2, 2010, the Company granted non-qualified stock options to eligible employees as presented in the following activity tables. Terms of these grants and the Company s methods for determining grant-date fair value of the awards were consistent with that described on pages 42 and 43 of the Company s 2010 Annual Report on Form 10-K.

Year-to-date period ended October 1, 2011:

Employee and director stock options	Shares (millions)	Weighted-average exercise price	Weighted-average remaining contractual term (yrs.)	Aggregate intrinsic value (millions)
Outstanding, beginning of period	**26**	**$47**		
Granted	**5**	**53**		
Exercised	**(6)**	**45**		
Forfeitures and expirations	**(1)**	**52**		
Outstanding, end of period	**24**	**$48**	**6.5**	**$121**
Exercisable, end of period	**16**	**$46**	**5.2**	**$108**

Year-to-date period ended October 2, 2010:

Employee and director stock options	Shares (millions)	Weighted-average exercise price	Weighted-average remaining contractual term (yrs.)	Aggregate intrinsic value (millions)

Outstanding, beginning of period	26	$45		
Granted	4	53		
Exercised	(4)	44		
Forfeitures and expirations				
Outstanding, end of period	26	$46	6.5	$129
Exercisable, end of period	20	$46	5.7	$104

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The weighted-average fair value of options granted was $7.59 per share for the year-to-date period ended October 1, 2011 and $7.90 per share for the year-to-date period ended October 2, 2010. The fair value was estimated using the following assumptions:

	Weighted-average expected volatility	Weighted-average expected term (years)	Weighted-average risk-free interest rate	Dividend yield
Grants within the year-to-date period ended October 1, 2011:	17%	6.98	3.07%	3.10%
Grants within the year-to-date period ended October 2, 2010:	20%	4.94	2.54%	2.80%

The total intrinsic value of options exercised was $59 million for the year-to-date period ended October 1, 2011 and $40 million for the year-to-date period ended October 2, 2010.

Performance shares

In the first quarter of 2011, the Company granted performance shares to a limited number of senior executive-level employees, which entitle these employees to receive a specified number of shares of the Company s common stock on the vesting date, provided cumulative three-year operating profit and internal net sales growth targets are achieved.

The 2011 target grant currently corresponds to approximately 225,000 shares, with a grant-date fair value of $48 per share. The actual number of shares issued on the vesting date could range from 0 to 200% of target, depending on actual performance achieved. Based on the market price of the Company s common stock at October 1, 2011, the maximum future value that could be awarded to employees on the vesting date for all outstanding performance share awards was as follows:

(millions)	**October 1, 2011**
2009 Award	**$18**
2010 Award	**$21**
2011 Award	**$24**

The 2008 performance share award, payable in stock, was settled at 69% of target in February 2011 for a total dollar

equivalent of $6 million.

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Note 7 Employee benefits

The Company sponsors a number of U.S. and foreign pension, other nonpension postretirement and postemployment plans to provide various benefits for its employees. These plans are described on pages 44 to 49 of the Company s 2010 Annual Report on Form 10-K. Components of Company plan benefit expense for the periods presented are included in the tables below.

Pension

	Quarter ended		Year-to-date period ended	
(millions)	**October 1, 2011**	October 2, 2010	**October 1, 2011**	October 2, 2010
Service cost	**$ 23**	$ 22	**$ 72**	$ 66
Interest cost	**52**	52	**157**	151
Expected return on plan assets	**(91)**	(82)	**(277)**	(238)
Amortization of unrecognized prior service cost	**4**	4	**11**	11
Recognized net loss	**27**	20	**79**	60
Settlement cost	**3**		**7**	
Total pension expense	**$ 18**	$ 16	**$ 49**	$ 50

Other nonpension postretirement

	Quarter ended		Year-to-date period ended	
(millions)	**October 1, 2011**	October 2, 2010	**October 1, 2011**	October 2, 2010
Service cost	**$ 6**	$ 5	**$ 17**	$ 15
Interest cost	**16**	16	**47**	48
Expected return on plan assets	**(22)**	(16)	**(66)**	(48)
Amortization of unrecognized prior service cost	**(1)**	(1)	**(2)**	(2)
Recognized net loss	**5**	4	**15**	13
Total postretirement benefit expense	**$ 4**	$ 8	**$ 11**	$ 26

Postemployment

	Quarter ended		Year-to-date period ended	
(millions)	**October 1, 2011**	October 2, 2010	**October 1, 2011**	October 2, 2010
Service cost	**$ 2**	$ 1	**$ 5**	$ 4
Interest cost	**1**	1	**3**	3
Recognized net loss	**1**	1	**3**	3
Total postemployment benefit expense	**$ 4**	$ 3	**$ 11**	$ 10

Company contributions to employee benefit plans are summarized as follows:

(millions)	Pension	Total

		Nonpension postretirement	
Quarter ended:			
October 1, 2011	**$ 1**	**$ 3**	**$ 4**
October 2, 2010	$ 6	$ 3	$ 9
Year-to-date period ended:			
October 1, 2011	**$176**	**$ 11**	**$187**
October 2, 2010	$ 35	$10	$ 45
Full year:			
Fiscal year 2011 (projected)	**$180**	**$15**	**$195**
Fiscal year 2010 (actual)	$350	$293	$643

Plan funding strategies may be modified in response to management s evaluation of tax deductibility, market conditions, and competing investment alternatives.

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Note 8 Income taxes

The consolidated effective tax rate for the quarter ended October 1, 2011, of 27% was lower than the prior year s rate of 30%. The consolidated effective tax rate for the year-to-date period ended October 1, 2011 was 28%, compared to the prior year-to-date period ended October 2, 2010 rate of 29%. The effective rate for the third quarter of 2011 benefited from a write off of an investment in a Latin America subsidiary as well as a decrease in the United Kingdom s statutory income tax rate.

As of October 1, 2011, the Company classified $12 million of unrecognized tax positions as a net current liability, representing several income tax positions under examination in various jurisdictions. Management s estimate of reasonably possible changes in unrecognized tax benefits during the next twelve months consists of the current liability balance, expected to be settled within one year, offset by $8 million of projected additions. Management is currently unaware of any issues under review that could result in significant additional payments, accruals or other material deviation in this estimate.

Following is a reconciliation of the Company s total gross unrecognized tax benefits for the year-to-date period ended October 1, 2011; $50 million of this total represents the amount that, if recognized, would affect the Company s effective income tax rate in future periods.

(millions)	
January 1, 2011	**$ 104**
Tax positions related to current year:	
Additions	**7**
Tax positions related to prior years:	
Additions	**8**
Reductions	**(16)**
Settlements	**(34)**
October 1, 2011	**$ 69**

The Company had the following amounts of income tax related interest accrued as of January 1, 2011 and October 1, 2011.

(millions)	
Interest accrued at January 1, 2011	$ 26
Reduction of interest expense recognized for the year-to-date period ended October 1, 2011	$ (2)
Interest accrued at October 1, 2011	$ 18

Note 9 Derivative instruments and fair value measurements

The Company is exposed to certain market risks such as changes in interest rates, foreign currency exchange rates, and commodity prices, which exist as a part of its ongoing business operations. Management uses derivative financial and commodity instruments, including futures, options, and swaps, where appropriate, to manage these risks. Instruments used as hedges must be effective at reducing the risk associated with the exposure being hedged and must be designated as a hedge at the inception of the contract.

The Company designates derivatives as cash flow hedges, fair value hedges, net investment hedges, and uses other contracts to reduce volatility in interest rates, foreign currency and commodities. As a matter of policy, the Company does not engage in trading or speculative hedging transactions.

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Total notional amounts of the Company s derivative instruments as of October 1, 2011 and January 1, 2011 were as follows:

(millions)	**October 1, 2011**	January 1, 2011
Foreign currency exchange contracts	**$1,011**	$1,075
Interest rate contracts	**200**	1,900
Commodity contracts	**251**	379
Total	**$1,462**	$3,354

Following is a description of each category in the fair value hierarchy and the financial assets and liabilities of the Company that were included in each category at October 1, 2011 and January 1, 2011, measured on a recurring basis.

Level 1 Financial assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market. For the Company, level 1 financial assets and liabilities consist primarily of commodity derivative contracts.

Level 2 Financial assets and liabilities whose values are based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability. For the Company, level 2 financial assets and liabilities consist of interest rate swaps and over-the-counter commodity and currency contracts.

The Company s calculation of the fair value of interest rate swaps is derived from a discounted cash flow analysis based on the terms of the contract and the interest rate curve. Over-the-counter commodity derivatives are valued using an income approach based on the commodity index prices less the contract rate multiplied by the notional amount. Foreign currency contracts are valued using an income approach based on forward rates less the contract rate multiplied by the notional amount. The Company s calculation of the fair value of level 2 financial assets and liabilities takes into consideration the risk of nonperformance, including counterparty credit risk.

Level 3 Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect management s own assumptions about the assumptions a market participant would use in pricing the asset or liability. The Company did not have any level 3 financial assets or liabilities as of October 1, 2011 or January 1, 2011.

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The following table presents assets and liabilities that were measured at fair value in the Consolidated Balance Sheet on a recurring basis as of October 1, 2011 and January 1, 2011:

	Level 1		Level 2		Total	
(millions)	**October 1, 2011**	January 1, 2011	**October 1, 2011**	January 1, 2011	**October 1, 2011**	January 1, 2011
Derivatives designated as hedging instruments:						
Assets:						
Foreign currency exchange contracts:						
Other prepaid assets	**$**	$	**$14**	$ 7	**$ 14**	$ 7
Interest rate contracts:						
Other prepaid assets				5		5
Other assets			**16**	69	**16**	69
Commodity contracts:						
Other prepaid assets	**2**	23			**2**	23
Total assets	**$ 2**	$ 23	**$ 30**	$ 81	**$ 32**	$ 104
Liabilities:						
Foreign currency exchange contracts:						
Other current liabilities	**$**	$	**$(15)**	$(27)	**$(15)**	$ (27)
Commodity contracts:						
Other current liabilities	**(12)**		**(10)**	(10)	**(22)**	(10)
Other liabilities			**(27)**	(29)	**(27)**	(29)
Total liabilities	**$(12)**	$	**$(52)**	$(66)	**$(64)**	$ (66)

The fair value of non designated hedging instruments as of October 1, 2011 and January 1, 2011 was immaterial.

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The effect of derivative instruments on the Consolidated Statement of Income for the quarters ended October 1, 2011 and October 2, 2010 was as follows:

Derivatives in fair value hedging relationships (millions)	Location of gain (loss) recognized in income	Gain (loss) recognized in income	
		October 1, 2011	October 2, 2010
Foreign currency exchange contracts	Other income (expense), net	**$ (9)**	$ 26

Derivatives in cash flow hedging relationships (millions)	Gain (loss) recognized in AOCI		Location of gain (loss) reclassified from AOCI	Gain (loss) reclassified from AOCI into income		Location of gain (loss) recognized in income (a)	Gain (loss) recognized in income(a)	
	October 1, 2011	October 2, 2010		**October 1, 2011**	October 2, 2010		**October 1, 2011**	October 2, 2010
Foreign currency exchange contracts	**$ 5**	$ 2	COGS	**$ (1)**	$ (8)	Other income (expense), net	**$ (1)**	$
Foreign currency exchange contracts	**2**	(2)	SGA expense		(1)	Other income (expense), net		
Interest rate contracts			Interest expense	**1**	(1)	N/A		
Commodity contracts	**(8)**	(2)	COGS	**(1)**	4	Other income (expense), net		
Total	**$ (1)**	$ (2)		**$ (1)**	$ (6)		**$ (1)**	$

Derivatives not designated as hedging instruments (millions)	Location of gain (loss) recognized in income	Gain (loss) recognized in income	
		October 1, 2011	October 2, 2010
Foreign currency exchange contracts	Other income (expense), net	**$ (1)**	$
Interest rate contracts	Interest expense	**$ 2**	$
Total		**$ 1**	$

(a) Includes the ineffective portion and amount excluded from effectiveness testing.

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The effect of derivative instruments on the Consolidated Statement of Income for the year-to-date periods ended October 1, 2011 and October 2, 2010 were as follows:

Derivatives in fair value hedging relationships (millions)	Location of gain (loss) recognized in income	Gain (loss) recognized in income	
		October 1, 2011	October 2, 2010
Foreign currency exchange contracts	Other income (expense), net	**$ 16**	$ (25)

Derivatives in cash flow hedging relationships (millions)	Gain (loss) recognized in AOCI		Location of gain (loss) reclassified from AOCI	Gain (loss) reclassified from AOCI into income		Location of gain (loss) recognized in income (a)	Gain (loss) recognized in income(a)	
	October 1, 2011	October 2, 2010		**October 1, 2011**	October 2, 2010		**October 1, 2011**	October 2, 2010
Foreign currency exchange contracts	**$ 2**	$ (10)	COGS	**$ (4)**	$ (21)	Other income (expense), net	**$ (2)**	$
Foreign currency exchange contracts			SGA expense		(1)	Other income (expense), net		
Interest rate contracts	**(13)**		Interest expense	**3**	(3)	N/A		
Commodity contracts	**(25)**	(31)	COGS	**11**	(12)	Other income (expense), net		(1)
Total	**$ (36)**	$ (41)		**$ 10**	$ (37)		**$ (2)**	$ (1)

Derivatives not designated as hedging instruments (millions)	Location of gain (loss) recognized in income	Gain (loss) recognized in income	
		October 1, 2011	October 2, 2010
Foreign currency exchange contracts	Other income (expense), net	**$**	$
Interest rate contracts	Interest expense	**$ (1)**	$
Total		**$ (1)**	$

(a) Includes the ineffective portion and amount excluded from effectiveness testing.

Contracts with certain of the Company s counterparties contain provisions requiring the Company to post collateral if the d