FLOWSERVE CORP
Form 10-Q
July 27, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2011**

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM __________ to __________.**

Commission File No. 1-13179
FLOWSERVE CORPORATION
(Exact name of registrant as specified in its charter)

New York	**31-0267900**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5215 N. O Connor Blvd., Suite 2300, Irving, Texas	**75039**
(Address of principal executive offices)	(Zip Code)

(972) 443-6500
(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. þ Yes o 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). þ Yes o 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 accelerated filer, large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (do not check if a smaller reporting company)
Smaller reporting company o		

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

As of July 21, 2011, there were 55,736,107 shares of the issuer s common stock outstanding.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

FLOWSERVE CORPORATION
(Unaudited)

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Amounts in thousands, except per share data)	Three Months Ended June 30, 2011	2010
Sales	$ 1,125,752	$ 961,096
Cost of sales	(756,414)	(617,731)
Gross profit	369,338	343,365
Selling, general and administrative expense	(232,983)	(201,330)
Net earnings from affiliates	3,751	3,994
Operating income	140,106	146,029
Interest expense	(9,534)	(8,682)
Interest income	394	406
Other income (expense), net	5,985	(12,304)
Earnings before income taxes	136,951	125,449
Provision for income taxes	(38,227)	(33,645)
Net earnings, including noncontrolling interests	98,724	91,804
Less: Net loss (earnings) attributable to noncontrolling interests	8	(157)
Net earnings attributable to Flowserve Corporation	$ 98,732	$ 91,647
Net earnings per share attributable to Flowserve Corporation common shareholders:		
Basic	$ 1.77	$ 1.64
Diluted	1.76	1.62
Cash dividends declared per share	$ 0.32	$ 0.29

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Amounts in thousands)	Three Months Ended June 30, 2011	2010
Net earnings, including noncontrolling interests	$ 98,724	$ 91,804
Other comprehensive income (expense):		
Foreign currency translation adjustments, net of tax	27,318	(60,771)
Pension and other postretirement effects, net of tax	854	1,242
Cash flow hedging activity, net of tax	(677)	1,230
Other comprehensive income (expense)	27,495	(58,299)

Comprehensive income, including noncontrolling interests	126,219	33,505
Comprehensive loss (income) attributable to noncontrolling interests	4	(65)
Comprehensive income attributable to Flowserve Corporation	$ 126,223	$ 33,440

See accompanying notes to condensed consolidated financial statements.

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FLOWSERVE CORPORATION
(Unaudited)

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Amounts in thousands, except per share data)	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Sales	$ 2,122,959	$ 1,920,002
Cost of sales	(1,405,926)	(1,228,327)
Gross profit	717,033	691,675
Selling, general and administrative expense	(455,622)	(412,570)
Net earnings from affiliates	8,948	9,099
Operating income	270,359	288,204
Interest expense	(18,139)	(17,677)
Interest income	883	740
Other income (expense), net	14,474	(33,837)
Earnings before income taxes	267,577	237,430
Provision for income taxes	(71,857)	(65,420)
Net earnings, including noncontrolling interests	195,720	172,010
Less: Net earnings attributable to noncontrolling interests	(5)	(142)
Net earnings attributable to Flowserve Corporation	$ 195,715	$ 171,868
Net earnings per share attributable to Flowserve Corporation common shareholders:		
Basic	$ 3.51	$ 3.08
Diluted	3.48	3.04
Cash dividends declared per share	$ 0.64	$ 0.58

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Amounts in thousands)	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Net earnings, including noncontrolling interests	$ 195,720	$ 172,010
Other comprehensive income (expense):		
Foreign currency translation adjustments, net of tax	76,121	(98,358)
Pension and other postretirement effects, net of tax	459	4,161
Cash flow hedging activity, net of tax	(429)	1,785
Other comprehensive income (expense)	76,151	(92,412)
Comprehensive income, including noncontrolling interests	271,871	79,598
Comprehensive income attributable to noncontrolling interests	(432)	(105)

Comprehensive income attributable to Flowserve Corporation	$ 271,439	$ 79,493

See accompanying notes to condensed consolidated financial statements.

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FLOWSERVE CORPORATION
(Unaudited)
CONDENSED CONSOLIDATED BALANCE SHEETS

(Amounts in thousands, except per share data)	**June 30, 2011**	**December 31, 2010**
ASSETS		
Current assets:		
Cash and cash equivalents	$ 221,312	$ 557,579
Accounts receivable, net of allowance for doubtful accounts of $20,073 and $18,632, respectively	1,000,702	839,566
Inventories, net	1,090,575	886,731
Deferred taxes	133,855	131,996
Prepaid expenses and other	143,178	107,872
Total current assets	2,589,622	2,523,744
Property, plant and equipment, net of accumulated depreciation of $737,037 and $682,715, respectively	593,233	581,245
Goodwill	1,035,372	1,012,530
Deferred taxes	23,508	24,343
Other intangible assets, net	147,057	147,112
Other assets, net	174,484	170,936
Total assets	$ 4,563,276	$ 4,459,910
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$ 479,221	$ 571,021
Accrued liabilities	781,799	817,837
Debt due within one year	55,697	51,481
Deferred taxes	17,572	16,036
Total current liabilities	1,334,289	1,456,375
Long-term debt due after one year	464,463	476,230
Retirement obligations and other liabilities	433,064	414,272
Shareholders equity:		
Common shares, $1.25 par value	73,664	73,664
Shares authorized 120,000		
Shares issued 58,931 and 58,931, respectively		
Capital in excess of par value	605,076	613,861
Retained earnings	2,008,272	1,848,680
	2,687,012	2,536,205
Treasury shares, at cost 3,779 and 3,872 shares, respectively	(301,346)	(292,210)
Deferred compensation obligation	10,138	9,533
Accumulated other comprehensive loss	(74,787)	(150,506)

Total Flowserve Corporation Shareholders Equity	2,321,017	2,103,022
Noncontrolling interest	10,443	10,011
Total equity	2,331,460	2,113,033
Total liabilities and equity	$ 4,563,276	$ 4,459,910

See accompanying notes to condensed consolidated financial statements.

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FLOWSERVE CORPORATION
(Unaudited)
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands)	Six Months Ended June 30, 2011	2010
Cash flows Operating activities:		
Net earnings, including noncontrolling interests	$ 195,720	$ 172,010
Adjustments to reconcile net earnings to net cash used by operating activities:		
Depreciation	44,373	42,426
Amortization of intangible and other assets	6,850	4,804
Amortization of deferred loan costs	1,449	2,121
Net gain on disposition of assets	(595)	(170)
Excess tax benefits from stock-based compensation arrangements	(5,021)	(10,238)
Stock-based compensation	16,271	15,087
Net earnings from affiliates, net of dividends received	1,623	(6,999)
Change in assets and liabilities:		
Accounts receivable, net	(121,537)	(36,174)
Inventories, net	(161,296)	(63,800)
Prepaid expenses and other	(32,670)	(1,739)
Other assets, net	(6,091)	385
Accounts payable	(114,811)	(67,601)
Accrued liabilities and income taxes payable	(75,279)	(123,789)
Retirement obligations and other liabilities	11,000	2,662
Net deferred taxes	2,219	18,319
Net cash flows used by operating activities	(237,795)	(52,696)
Cash flows Investing activities:		
Capital expenditures	(48,498)	(25,232)
Proceeds from disposal of assets	3,735	2,890
Payments for acquisitions, net of cash acquired	(890)	-
Affiliate investing activity, net	-	5,073
Net cash flows used by investing activities	(45,653)	(17,269)
Cash flows Financing activities:		
Excess tax benefits from stock-based compensation arrangements	5,021	10,238
Payments on long-term debt	(12,500)	(2,841)
Borrowings under other financing arrangements	4,348	1,932
Repurchase of common shares	(26,025)	(23,100)
Payments of dividends	(33,977)	(31,172)
Proceeds from stock option activity	224	5,471
Dividends paid to noncontrolling interests	-	(259)
Sale of shares to noncontrolling interests	-	533
Net cash flows used by financing activities	(62,909)	(39,198)

Effect of exchange rate changes on cash	10,090	(41,655)
Net change in cash and cash equivalents	(336,267)	(150,818)
Cash and cash equivalents at beginning of period	557,579	654,320
Cash and cash equivalents at end of period	$ 221,312	$ 503,502

See accompanying notes to condensed consolidated financial statements.

FLOWSERVE CORPORATION
(Unaudited)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Accounting Policies

Basis of Presentation

The accompanying condensed consolidated balance sheet as of June 30, 2011, the related condensed consolidated statements of income and comprehensive income for the three and six months ended June 30, 2011 and 2010, and the condensed consolidated statements of cash flows for the six months ended June 30, 2011 and 2010, of Flowserve Corporation, are unaudited. In management s opinion, all adjustments comprising normal recurring adjustments necessary for a fair presentation of such condensed consolidated financial statements have been made.

The accompanying condensed consolidated financial statements and notes in this Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2011 (Quarterly Report) are presented as permitted by Regulation S-X and do not contain certain information included in our annual financial statements and notes thereto. Accordingly, the accompanying condensed consolidated financial information should be read in conjunction with the consolidated financial statements presented in our Annual Report on Form 10-K for the year ended December 31, 2010 (2010 Annual Report).

Ongoing Events in North Africa, Middle East and Japan Ongoing political and economic conditions in North Africa have caused us to experience shipment delays to this region. We estimate that the shipments to this region that have been delayed resulted in lost or delayed opportunities for operating income of $2.5 million and $5.1 million for the three months and six months ended June 30, 2011, respectively. We are closely monitoring the conditions in the Middle East and North Africa and, while there are many potential outcomes in each individual country that are difficult to estimate, based on current facts and circumstances as we understand them, it is possible that delayed shipments and bookings could continue throughout the remainder of the year. If the current conditions in North Africa persist, we estimate that the unfavorable impact on bookings through the end of 2011 could approximate $25 million. The preponderance of our physical assets in the region are located in the Kingdom of Saudi Arabia and the United Arab Emirates and have, to date, not been affected by the unrest elsewhere in the region.

We continue to assess the conditions and potential adverse impacts of the earthquake and tsunami in Japan earlier in the year, in particular as they relate to our customers and suppliers in the impacted regions, as well as announced and potential regulatory impacts to the global nuclear power market. We did not experience any significant adverse impacts due to shipment delays, collection issues or supply chain disruptions during the first half of 2011; however, we have experienced a small amount of lost or delayed bookings in the region in the second quarter and anticipate we could continue to experience lost or delayed bookings in the region through the end of 2011. We are also closely monitoring the effects of the Japan crisis on the global nuclear power industry. While it is difficult to estimate the effect of the Fukushima plant shutdown on the global nuclear power market, we believe that there has been a related reduction in orders in the second quarter that could continue throughout 2011, which may affect both bookings and sales in the second half of 2011.

Venezuela As previously disclosed in our 2009 and 2010 Annual Reports, effective January 11, 2010, the Venezuelan government devalued its currency (Bolivar) and moved to a two-tier exchange structure. The official exchange rate moved from 2.15 to 4.30 Bolivars to the United States (U.S.) dollar for non-essential items and to 2.60 Bolivars to the U.S. dollar for essential items. Additionally, effective January 1, 2010, Venezuela was designated as hyperinflationary, and as a result, we began to use the U.S. dollar as our functional currency in Venezuela. On December 30, 2010, the Venezuelan government announced its intention to eliminate the favorable essential items rate effective January 1, 2011. Our operations in Venezuela generally consist of a service center that both imports equipment and parts from certain of our other locations for resale to third parties within Venezuela and performs service and repair activities. Our Venezuelan subsidiary s sales for the six months ended June 30, 2011 and 2010 and total assets at June 30, 2011 represented approximately 1% or less of our consolidated sales and total assets for the same periods.

Although approvals by Venezuela s Commission for the Administration of Foreign Exchange have slowed, we have historically been able to remit dividends and other payments at the official rate, and we currently anticipate doing so in the future. Accordingly, we used the official rate of 4.30 Bolivars to the U.S. dollar for re-measurement of our Venezuelan financial statements into U.S. dollars for all periods presented. As a result of the currency devaluation, we recognized a net loss of $8.6 million during the six months ended June 30, 2010. The loss was reported in other income (expense), net in our condensed consolidated statement of income and resulted in no tax benefit. The elimination of the favorable essential items rate, effective January 1, 2011, had no impact on our consolidated financial position or results of operations for the three and six months ended June 30, 2011.

We have evaluated the carrying value of related assets and concluded that there is no current impairment. We are continuing to assess and monitor the ongoing impact of the currency devaluation on our Venezuelan operations and imports into the market, including the Venezuelan subsidiary s ability to remit cash for dividends and other payments at the official rate, the future ability of our imported products to be classified as essential items and the ability to recover exchange losses, as well as further actions of the Venezuelan government and economic conditions in Venezuela that may adversely impact our future consolidated financial condition or results of operations.

Accounting Policies

Effective January 1, 2011, we adopted Accounting Standards Update (ASU) No. 2009-13, Revenue Recognition (Accounting Standards Codification (ASC) 605): Multiple-Deliverable Revenue Arrangements a consensus of the Financial Accounting Standards Board (FASB) Emerging Issues Task Force, which resulted in expanded disclosure requirements regarding our revenue recognition policy (see Revenue Recognition below). Our adoption of ASU No. 2009-13, effective January 1, 2011, had no impact on our consolidated financial condition or results of operations.

Except for the incremental revenue recognition policy disclosure included below, no other changes have occurred to our significant accounting policies in the six months ended June 30, 2011. Our significant accounting policies are detailed in Note 1 to our consolidated financial statements included in our 2010 Annual Report.

Revenue Recognition

Revenues for product sales are recognized when the risks and rewards of ownership are transferred to the customers, which is typically based on the contractual delivery terms agreed to with the customer and fulfillment of all but inconsequential or perfunctory actions. In addition, our policy requires persuasive evidence of an arrangement, a fixed or determinable sales price and reasonable assurance of collectability. We defer the recognition of revenue when advance payments are received from customers before performance obligations have been completed and/or services have been performed. Freight charges billed to customers are included in sales and the related shipping costs are included in cost of sales in our condensed consolidated statements of income. Our contracts typically include cancellation provisions that require customers to reimburse us for costs incurred up to the date of cancellation, as well as any contractual cancellation penalties.

We enter into certain contracts with multiple deliverables that may include any combination of designing, developing, manufacturing, modifying, installing and commissioning of flow management equipment and providing services related to the performance of such products. Delivery of these products and services typically occurs within a one to two-year period, although many arrangements, such as book and ship type orders, have a shorter timeframe for delivery. We aggregate or separate deliverables into units of accounting based on whether the deliverable(s) have standalone value to the customer and when no general right of return exists. Contract value is allocated ratably to the units of accounting in the arrangement based on their relative selling prices determined as if the deliverables were sold separately.

Revenues for long-term contracts, including separate units of accounting from multiple-deliverable contracts, that exceed certain internal thresholds regarding the size, complexity and duration of the project and provide for the receipt of progress billings from the customer are recorded on the percentage of completion method with progress measured on a cost-to-cost basis. Percentage of completion revenue represented approximately 8% of our consolidated sales for the three and six months ended June 30, 2011 and 2010.

Revenue on service and repair contracts is recognized after services have been agreed to by the customer and rendered. Revenues generated under fixed fee service and repair contracts are recognized on a ratable basis over the term of the contract. These contracts can range in duration, but generally extend for up to five years. Revenue on fixed fee service contracts represented approximately 1% of our consolidated sales for the three and six months ended June 30, 2011 and 2010.

In certain instances, we provide guaranteed completion dates under the terms of our contracts. Failure to meet contractual delivery dates can result in late delivery penalties or non-recoverable costs. In instances where the payment of such costs are deemed to be probable, we perform a project profitability analysis, accounting for such costs as a reduction of realizable revenues, which could potentially cause estimated total project costs to exceed projected total revenues realized from the project. In such instances, we would record reserves to cover such excesses in the period they are determined. In circumstances where the total projected revenues still exceed total projected costs, the incurrence of unrealized incentive fees or non-recoverable costs generally reduces profitability of the project at the time of subsequent revenue recognition. Our reported results would change if different estimates were used for contract costs or if different estimates were used for contractual contingencies.

Accounting Developments

Pronouncements Implemented

In January 2010, the FASB issued ASU No. 2010-06, Fair Value Measurements and Disclosures (ASC 820): Improving Disclosures about Fair Value Measurements, which requires additional disclosures on transfers in and out of Level I and Level II and on activity for Level III fair value measurements. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures of Level III activity, which are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. Our adoption of the Level I and II disclosure guidance, effective January 1, 2010, and Level III disclosure guidance, effective January 1, 2011, had no material impact on our consolidated financial condition or results of operations.

In September 2009, the FASB issued ASU No. 2009-13, Revenue Recognition (ASC 605): Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force, which addresses the accounting for multiple-deliverable arrangements to enable vendors to account for products or services separately rather than as a combined unit and requires expanded revenue recognition policy disclosures. This amendment addresses how to separate deliverables and how to measure and allocate arrangement consideration to one or more units of accounting. As noted above, our adoption of ASU No. 2009-13, effective January 1, 2011, had no impact on our consolidated financial condition or results of operations.

In December 2010, the FASB issued ASU No. 2010-28, Intangibles Goodwill and Other (ASC 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts a consensus of the FASB Emerging Issues Task Force, which modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. This amendment requires an entity to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists and to consider whether there are any adverse qualitative factors indicating that an impairment may exist. Our adoption of ASU No. 2010-28, effective January 1, 2011, had no impact on our consolidated financial condition or results of operations.

In December 2010, the FASB issued ASU No. 2010-29, Business Combinations (ASC 805): Disclosure of Supplementary Pro Forma Information for Business Combinations a consensus of the FASB Emerging Issues Task Force, which specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. This amendment also expands the supplemental pro forma disclosures under ASC 805 to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. Our adoption of ASU No. 2010-29, effective January 1, 2011, had no material impact on our consolidated financial condition or results of operations.

Pronouncements Not Yet Implemented

In June 2011, the FASB issued ASU No. 2011-05, Comprehensive Income (ASC 220): Presentation of Comprehensive Income, which specifies that an entity has the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. This amendment requires an entity to present on the face of the financial statements reclassification adjustments for items that are reclassified from other comprehensive income to net income. ASU No. 2011-05 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. We do not expect the adoption of ASU No. 2011-05 to have a material impact on our consolidated financial condition and results of operations. The presentation and disclosure requirements shall be applied retrospectively for all periods presented.

2. Acquisition

Valbart Srl

As discussed in Note 2 to our consolidated financial statements included in our 2010 Annual Report, effective July 16, 2010, we acquired for inclusion in Flow Control Division (FCD), Valbart Srl (Valbart), a privately-owned Italian valve manufacturer, for $199.4 million, which included $33.8 million of existing Valbart net debt (third party debt less cash on hand) that was repaid at closing. Valbart manufactures trunnion-mounted ball valves used primarily in upstream and midstream oil and gas applications, and its acquisition is intended to improve our ability to provide a more complete valve portfolio to oil and gas projects. Valbart generated approximately 81 million ($104 million, at then-current exchange rates) in sales (unaudited) during its fiscal year ended May 31, 2010. No pro forma information was provided due to immateriality.

3. Stock-Based Compensation Plans

We established the Flowserve Corporation Equity and Incentive Compensation Plan (the 2010 Plan) effective January 1, 2010. This shareholder-approved plan authorizes the issuance of up to 2,900,000 shares of our common stock in the form of incentive stock options, non-statutory stock options, restricted shares, restricted share units and performance-based units (collectively referred to as Restricted Shares), stock appreciation rights and bonus stock. Of the 2,900,000 shares of common stock authorized under the 2010 Plan, 2,420,536 remain available for issuance as of June 30, 2011. In addition to the 2010 Plan, we also maintain the Flowserve Corporation 2004 Stock Compensation Plan (the 2004 Plan), which was established on April 21, 2004. The 2004 Plan authorized the issuance of up to 3,500,000 shares of common stock through grants of Restricted Shares, stock options and other equity-based awards. Of the 3,500,000 shares of common stock authorized under the 2004 Plan, 474,622 remain available for issuance as of June 30, 2011.

We recorded stock-based compensation expense of $5.2 million ($7.7 million pre-tax) and $4.7 million ($6.9 million pre-tax) for the three months ended June 30, 2011 and 2010, respectively. We recorded stock-based compensation expense of $11.0 million ($16.3 million pre-tax) and $10.3 million ($15.2 million pre-tax) for the six months ended June 30, 2011 and 2010, respectively.

Stock Options Information related to stock options issued to officers, other employees and directors under all plans described in Note 5 to our consolidated financial statements included in our 2010 Annual Report is presented in the following table:

	Six Months Ended June 30, 2011			
	Shares	Weighted Average Exercise Price	Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in millions)
Number of shares under option:				
Outstanding January 1, 2011	68,071	$ 40.48		
Exercised	(11,900)	34.57		
Outstanding June 30, 2011	56,171	$ 41.73	4.0	$ 3.8
Exercisable June 30, 2011	56,171	$ 41.73	4.0	$ 3.8

No options were granted during the six months ended June 30, 2011 or 2010. No stock options vested during the three or six months ended June 30, 2011 or 2010. The fair value of each option award was estimated on the date of grant using the Black-Scholes option pricing model.

As of June 30, 2011, we had no unrecognized compensation cost related to outstanding unvested stock option awards. The total intrinsic value of stock options exercised during the three months ended June 30, 2011 and 2010, was less than $1 million and $1.9 million, respectively. The total intrinsic value of stock options exercised during the six months ended June 30, 2011 and 2010 was $3.8 million and $7.9 million, respectively.

Restricted Shares Awards of Restricted Shares are valued at the closing market price of our common stock on the date of grant. The unearned compensation is amortized to compensation expense over the vesting period of the restricted shares. We had unearned compensation of $42.3 million and $31.6 million at June 30, 2011 and December 31, 2010, respectively, which is expected to be recognized over a weighted-average period of 1.4 years. These amounts will be recognized into net earnings in prospective periods as the awards vest. The total fair value of Restricted Shares vested during the three months ended June 30, 2011 and 2010 was $1.2 million and $1.7 million, respectively. The total fair value of Restricted Shares vested during the six months ended June 30, 2011 and 2010 was

$34.8 million and $31.6 million, respectively.

The following table summarizes information regarding Restricted Shares:

	Six Months Ended June 30, 2011		
	Shares		Weighted Average Grant-Date Fair Value
Number of unvested shares:			
Outstanding - January 1, 2011	1,259,377	$	77.05
Granted	216,644		130.51
Vested	(392,869)		88.68
Cancelled	(25,186)		77.58
Outstanding - June 30, 2011	1,057,966	$	83.67

Unvested Restricted Shares outstanding as of June 30, 2011, includes 434,000 units with performance-based vesting provisions. Performance-based units are issuable in common stock and vest upon the achievement of pre-defined performance targets, primarily based on our average annual return on net assets over a three-year period as compared with the same measure for a defined peer group for the same period. Most units were granted in three annual grants since January 1, 2009 and have a vesting percentage between 0% and 200% depending on the achievement of the specific performance targets. Compensation expense is recognized ratably over a cliff vesting period of 36 months, based on the fair market value of our common stock on the date of grant, as adjusted for anticipated forfeitures. During the performance period, earned and unearned compensation expense is adjusted based on changes in the expected achievement of the performance targets. Vesting provisions range from 0 to 844,000 shares based on performance targets. As of June 30, 2011, we estimate vesting of approximately 745,000 shares based on expected achievement of performance targets.

4. Derivative Instruments and Hedges

Our risk management and derivatives policy specifies the conditions under which we may enter into derivative contracts. See Notes 1 and 6 to our consolidated financial statements included in our 2010 Annual Report and Note 7 of this Quarterly Report for additional information on our purpose for entering into derivatives not designated as hedging instruments and our overall risk management strategies. We enter into forward exchange contracts to hedge our cash flow risks associated with transactions denominated in currencies other than the local currency of the oper