

NAVISTAR INTERNATIONAL CORP  
Form 10-Q  
March 05, 2014  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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Form 10-Q

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(Mark One)

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

For the quarterly period ended January 31, 2014

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 1-9618

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NAVISTAR INTERNATIONAL CORPORATION  
(Exact name of registrant as specified in its charter)

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Delaware 36-3359573  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

2701 Navistar Drive, Lisle, Illinois 60532  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code (331) 332-5000

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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 Website, 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 definition of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

As of February 28, 2014, the number of shares outstanding of the registrant's common stock was 81,288,845, net of treasury shares.

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Disclosure Regarding Forward-Looking Statements

Information provided and statements contained in this report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended ("Securities Act"), Section 21E of the Securities Exchange Act of 1934, as amended ("Exchange Act"), and the Private Securities Litigation Reform Act of 1995. Such forward-looking statements only speak as of the date of this report and Navistar International Corporation assumes no obligation to update the information included in this report.

Such forward-looking statements include, but are not limited to, statements concerning:

- estimates we have made in preparing our financial statements;
- our development of new products and technologies;
- anticipated sales, volume, demand, and markets for our products;
- anticipated performance and benefits of our products and technologies, including our advanced clean engine solutions;
- our business strategies relating to, and our ability to meet, federal and state regulatory heavy-duty diesel emissions standards applicable to certain of our engines, including the timing and costs of compliance and consequences of noncompliance with such standards, as well as our ability to meet other federal, state and foreign regulatory requirements;
- our business strategies and long-term goals, and activities to accomplish such strategies and goals;
- our expectations to achieve the objectives of our "Drive-to-Deliver" turnaround plan, including: (i) leading vehicle uptime, (ii) creating a lean enterprise, (iii) generating future financial growth, and (iv) improving market share profitably;
- anticipated results from our Return-on-Invested-Capital ("ROIC") methodology and the benchmarking study to create a pathway to achieve profitability;
- anticipated results from the realignment of our leadership and management structure;
- anticipated benefits from acquisitions, strategic alliances, and joint ventures we complete;
- our expectations relating to the dissolution of our Blue Diamond Truck joint venture with Ford Motor Company ("Ford") expected in February 2015;
- our expectations and estimates relating to restructuring activities, including restructuring and integration charges and timing of cash payments related thereto, and operational flexibility, savings, and efficiencies from such restructurings;
- our expectations relating to the possible effects of anticipated divestitures and closures of businesses;
- our expectations relating to our cost-reduction actions, including our enterprise-wide reduction-in-force, and other actions to reduce discretionary spending;
- our expectations relating to our ability to service our long-term debt;
- our expectations relating to our retail finance receivables and retail finance revenues;
- our anticipated costs relating to the development of our emissions solutions products and other product modifications that may be required to meet other federal, state, and foreign regulatory requirements;
- our anticipated capital expenditures;
- our expectations relating to payments of taxes;
- our expectations relating to warranty costs;
- our expectations relating to interest expense;
- our expectations relating to impairment of goodwill and other assets;
- costs relating to litigation and similar matters;
- estimates relating to pension plan contributions and unfunded pension and postretirement benefits;
- trends relating to commodity prices; and
- anticipated trends, expectations, and outlook relating to matters affecting our financial condition or results of operations.

These statements often include words such as "believe," "expect," "anticipate," "intend," "plan," "estimate," or similar expressions. These statements are not guarantees of performance or results and they involve risks, uncertainties, and assumptions. Although we believe that these forward-looking statements are based on reasonable assumptions, there are many factors that could affect our actual financial results or results of operations and could cause actual results to

differ materially from those in the forward-looking statements. Factors that could cause or contribute to differences in our future financial results include those discussed in Item 1A, Risk Factors, included within our Annual Report on Form 10-K for the year ended October 31, 2013, which was filed on December 20, 2013, as well as those discussed elsewhere in this report. All future written and oral forward-looking statements by us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements contained herein or referred to above. Except for our ongoing obligations to disclose material information as required by the federal securities laws, we do not have any obligations or intention to release publicly any revisions to any forward-looking statements to reflect events or circumstances in the future or to reflect the occurrence of unanticipated events.

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Available Information

We are subject to the reporting and information requirements of the Exchange Act and as a result, are obligated to file annual, quarterly, and current reports, proxy statements, and other information with the United States ("U.S.") Securities and Exchange Commission ("SEC"). We make these filings available free of charge on our website (<http://www.navistar.com>) as soon as reasonably practicable after we electronically file them with, or furnish them to, the SEC. Information on our website does not constitute part of this Quarterly Report on Form 10-Q. In addition, the SEC maintains a website (<http://www.sec.gov>) that contains our annual, quarterly, and current reports, proxy and information statements, and other information we electronically file with, or furnish to, the SEC. Any materials we file with, or furnish to, the SEC may also be read and/or copied at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330.

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## PART I—Financial Information

## Item 1. Financial Statements

## Navistar International Corporation and Subsidiaries

## Consolidated Statements of Operations

(Unaudited)

	Three Months Ended January 31,	
(in millions, except per share data)	2014	2013
Sales and revenues		
Sales of manufactured products, net	\$2,169	\$2,598
Finance revenues	39	39
Sales and revenues, net	2,208	2,637
Costs and expenses		
Costs of products sold	2,014	2,286
Restructuring charges	3	2
Asset impairment charges	18	—
Selling, general and administrative expenses	239	285
Engineering and product development costs	90	111
Interest expense	82	74
Other expense (income), net	14	(38)
Total costs and expenses	2,460	2,720
Equity in loss of non-consolidated affiliates	—	(1)
Loss from continuing operations before income taxes	(252)	(84)
Income tax benefit (expense)	12	(15)
Loss from continuing operations	(240)	(99)
Income (loss) from discontinued operations, net of tax	1	(9)
Net loss	(239)	(108)
Less: Net income attributable to non-controlling interests	9	15
Net loss attributable to Navistar International Corporation	\$(248)	\$(123)
Amounts attributable to Navistar International Corporation common shareholders:		
Loss from continuing operations, net of tax	\$(249)	\$(114)
Income (loss) from discontinued operations, net of tax	1	(9)
Net loss	\$(248)	\$(123)
Earnings (loss) per share:		
Basic:		
Continuing operations	\$(3.07)	\$(1.42)
Discontinued operations	0.02	(0.11)
	\$(3.05)	\$(1.53)
Diluted:		
Continuing operations	\$(3.07)	\$(1.42)
Discontinued operations	0.02	(0.11)
	\$(3.05)	\$(1.53)
Weighted average shares outstanding:		
Basic	81.2	80.2

Diluted

81.2

80.2

See Notes to Condensed Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries  
 Consolidated Statements of Comprehensive Loss  
 (Unaudited)

(in millions)	Three Months Ended	
	January 31,	
	2014	2013
Net loss attributable to Navistar International Corporation	\$(248	) \$(123
Other comprehensive income (loss):		
Foreign currency translation adjustment	(62	) 17
Defined benefit plans, net of tax of \$0 in both periods	25	38
Total other comprehensive income (loss)	(37	) 55
Total comprehensive loss attributable to Navistar International Corporation	\$(285	) \$(68

See Notes to Condensed Consolidated Financial Statements

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Table of ContentsNavistar International Corporation and Subsidiaries  
Consolidated Balance Sheets

(in millions, except per share data)	January 31, 2014	October 31, 2013
ASSETS	(Unaudited)	
Current assets		
Cash and cash equivalents	\$ 549	\$ 755
Marketable securities	630	830
Trade and other receivables, net	553	737
Finance receivables, net	1,461	1,597
Inventories	1,382	1,210
Deferred taxes, net	74	72
Other current assets	249	258
Total current assets	4,898	5,459
Restricted cash	115	91
Trade and other receivables, net	28	29
Finance receivables, net	303	338
Investments in non-consolidated affiliates	75	77
Property and equipment (net of accumulated depreciation and amortization of \$2,465 and \$2,440, respectively)	1,700	1,741
Goodwill	170	184
Intangible assets (net of accumulated amortization of \$100 and \$97, respectively)	112	138
Deferred taxes, net	155	159
Other noncurrent assets	98	99
Total assets	\$ 7,654	\$ 8,315
LIABILITIES and STOCKHOLDERS' DEFICIT		
Liabilities		
Current liabilities		
Notes payable and current maturities of long-term debt	\$ 1,259	\$ 1,163
Accounts payable	1,430	1,502
Other current liabilities	1,564	1,596
Total current liabilities	4,253	4,261
Long-term debt	3,605	3,922
Postretirement benefits liabilities	2,531	2,564
Deferred taxes, net	25	33
Other noncurrent liabilities	1,117	1,136
Total liabilities	11,531	11,916
Redeemable equity securities	2	4
Stockholders' deficit		
Series D convertible junior preference stock	3	3
Common stock (86.8 shares issued, \$0.10 par value per share and 220 shares authorized, all at both dates)	9	9
Additional paid in capital	2,478	2,477
Accumulated deficit	(4,311)	(4,063)
Accumulated other comprehensive loss	(1,861)	(1,824)
Common stock held in treasury, at cost (5.6 and 6.3 shares, respectively)	(230)	(251)
Total stockholders' deficit attributable to Navistar International Corporation	(3,912)	(3,649)
Stockholders' equity attributable to non-controlling interests	33	44
Total stockholders' deficit	(3,879)	(3,605)

Total liabilities and stockholders' deficit	\$7,654	\$8,315
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See Notes to Condensed Consolidated Financial Statements

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Table of ContentsNavistar International Corporation and Subsidiaries  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

(in millions)	Three Months Ended	
	January 31, 2014	2013
Cash flows from operating activities		
Net loss	\$(239	) \$(108
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	55	89
Depreciation of equipment leased to others	31	11
Deferred taxes, including change in valuation allowance	(18	) (9
Asset impairment charges	18	—
Amortization of debt issuance costs and discount	14	16
Stock-based compensation	5	5
Provision for doubtful accounts, net of recoveries	2	1
Equity in loss of non-consolidated affiliates, net of dividends	2	3
Other non-cash operating activities	(9	) —
Changes in other assets and liabilities, exclusive of the effects of businesses acquired and disposed	46	58
Net cash provided by (used in) operating activities	(93	) 66
Cash flows from investing activities		
Purchases of marketable securities	(378	) (482
Sales or maturities of marketable securities	578	177
Net change in restricted cash and cash equivalents	(24	) 59
Capital expenditures	(21	) (72
Purchases of equipment leased to others	(49	) (32
Proceeds from sales of property and equipment	10	3
Investments in non-consolidated affiliates	(2	) —
Net cash provided by (used in) investing activities	114	(347
Cash flows from financing activities		
Proceeds from issuance of securitized debt	82	—
Principal payments on securitized debt	(94	) (190
Proceeds from issuance of non-securitized debt	47	25
Principal payments on non-securitized debt	(53	) (60
Net decrease in notes and debt outstanding under revolving credit facilities	(197	) (32
Principal payments under financing arrangements and capital lease obligations	(4	) (47
Debt issuance costs	(3	) (1
Proceeds from financed lease obligations	20	—
Issuance of common stock	—	14
Proceeds from exercise of stock options	16	1
Dividends paid by subsidiaries to non-controlling interest	(20	) (13
Net cash used in financing activities	(206	) (303
Effect of exchange rate changes on cash and cash equivalents	(21	) (6
Decrease in cash and cash equivalents	(206	) (590
Cash and cash equivalents at beginning of the period	755	1,087
Cash and cash equivalents at end of the period	\$549	\$497

See Notes to Condensed Consolidated Financial Statements



Table of ContentsNavistar International Corporation and Subsidiaries  
Consolidated Statements of Stockholders' Deficit  
(Unaudited)

(in millions)	Series D Convertible Junior Preference Stock	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Common Stock Held in Treasury, at cost	Stockholders' Equity Attributable to Non-controlling Interests	Total
Balance as of October 31, 2013	\$ 3	\$ 9	\$ 2,477	\$ (4,063 )	\$ (1,824 )	\$ (251 )	\$ 44	\$(3,605)
Net income (loss)				(248 )			9	(239 )
Total other comprehensive loss					(37 )			(37 )
Transfer from redeemable equity securities upon exercise or expiration of stock options			2					2
Stock-based compensation			4					4
Stock ownership programs			(5 )			21		16
Cash dividends paid to non-controlling interest							(20 )	(20 )
Balance as of January 31, 2014	\$ 3	\$ 9	\$ 2,478	\$ (4,311 )	\$ (1,861 )	\$ (230 )	\$ 33	\$(3,879)
Balance as of October 31, 2012	\$ 3	\$ 9	\$ 2,440	\$ (3,165 )	\$ (2,325 )	\$ (272 )	\$ 45	\$(3,265)
Net income (loss)				(123 )			15	(108 )
Total other comprehensive income					55			55
Transfer from redeemable equity securities upon exercise or expiration of stock options			1					1
Stock-based compensation			3					3
Stock ownership programs			(5 )			5		—
Cash dividends paid to non-controlling interest							(13 )	(13 )
October 2012 issuance of common stock, net of issuance cost and fees			14					14
Other					1		(1 )	—
Balance as of January 31, 2013	\$ 3	\$ 9	\$ 2,453	\$ (3,288 )	\$ (2,269 )	\$ (267 )	\$ 46	\$(3,313)

See Notes to Condensed Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries  
Notes to Condensed Consolidated Financial Statements  
(Unaudited)

1. Summary of Significant Accounting Policies

Organization and Description of the Business

Navistar International Corporation ("NIC"), incorporated under the laws of the State of Delaware in 1993, is a holding company whose principal operating entities are Navistar, Inc. and Navistar Financial Corporation ("NFC").

References herein to the "Company," "we," "our," or "us" refer collectively to NIC and its consolidated subsidiaries, including certain variable interest entities ("VIEs") of which we are the primary beneficiary.

Our fiscal year ends October 31. As such, all references to 2014 and 2013 contained within this Quarterly Report on Form 10-Q relate to our fiscal year, unless otherwise indicated.

We operate in four principal industry segments: North America Truck, North America Parts, Global Operations (collectively called "Manufacturing operations"), and Financial Services, which consists of NFC and our foreign finance operations (collectively called "Financial Services operations"). These segments are discussed in Note 13, Segment Reporting.

Basis of Presentation and Consolidation

The accompanying unaudited consolidated financial statements include the assets, liabilities, and results of operations of our Manufacturing operations, which include majority-owned dealers ("Dealcors"), and our Financial Services operations, including VIEs of which we are the primary beneficiary. The effects of transactions among consolidated entities have been eliminated to arrive at the consolidated amounts.

Certain reclassifications were made to prior periods' amounts to conform to the 2014 presentation, which relates to the realignment of our reporting segments that became effective during the fourth quarter of 2013.

We prepared the accompanying unaudited consolidated financial statements in accordance with United States ("U.S.") generally accepted accounting principles ("U.S. GAAP") for interim financial information and the instructions to the Quarterly Report on Form 10-Q and Article 10 of Regulation S-X issued by the U.S. Securities and Exchange Commission ("SEC"). Accordingly, they do not include all of the information and notes required by U.S. GAAP for comprehensive annual financial statements.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting policies described in our Annual Report on Form 10-K for the year ended October 31, 2013, which should be read in conjunction with the disclosures therein. In our opinion, these interim consolidated financial statements reflect all adjustments, consisting of normal recurring adjustments, necessary to present fairly the financial condition, results of operations, and cash flows for the periods presented. Operating results for interim periods are not necessarily indicative of annual operating results.

Variable Interest Entities

We have an interest in several VIEs, primarily joint ventures, established to manufacture or distribute products and enhance our operational capabilities. We have determined for certain of our VIEs that we are the primary beneficiary because we have the power to direct the activities of the VIE that most significantly impact the VIE's economic performance and have the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. Accordingly, we include in our consolidated financial statements the assets and liabilities and results of operations of those entities, even though we may not own a majority voting interest. The liabilities recognized as a result of consolidating these VIEs do not represent additional claims on our general assets; rather they represent claims against the specific assets of these VIEs. Assets of these entities are not readily available to satisfy claims against our general assets.

We are the primary beneficiary of our Blue Diamond Parts ("BDP") and Blue Diamond Truck ("BDT") joint ventures with Ford Motor Company ("Ford"). As a result, our Consolidated Balance Sheets include assets of \$201 million and \$323 million and liabilities of \$186 million and \$188 million as of January 31, 2014 and October 31, 2013, respectively, from BDP and BDT, including \$65 million and \$56 million of cash and cash equivalents, at the respective dates, which are not readily available to satisfy claims against our general assets. The creditors of BDP and BDT do not have recourse to our general credit. In December 2011, Ford notified the Company of its intention to

dissolve the BDT joint venture effective December 2014. In September 2013, we agreed with Ford to extend the BDT joint venture through February 2015. We do not expect the dissolution of the BDT joint venture to have a material impact on our consolidated financial statements.

Our Financial Services segment consolidates several VIEs. As a result, our Consolidated Balance Sheets include assets of \$946 million and \$989 million as of January 31, 2014 and October 31, 2013, respectively, and liabilities of \$752 million and \$778 million as of January 31, 2014 and October 31, 2013, respectively, all of which are involved in securitizations that are treated as



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Navistar International Corporation and Subsidiaries  
Notes to Condensed Consolidated Financial Statements—(Continued)  
(Unaudited)

asset-backed debt. In addition, our Consolidated Balance Sheets include assets of \$73 million and \$61 million and corresponding liabilities of \$58 million and \$49 million as of January 31, 2014 and October 31, 2013, respectively, which are related to other secured transactions that do not qualify for sale accounting treatment, and therefore, are treated as borrowings secured by operating and finance leases. Investors that hold securitization debt have a priority claim on the cash flows generated by their respective securitized assets to the extent that the related trusts are required to make principal and interest payments. Investors in securitizations of these entities have no recourse to our general credit.

We also have an interest in other VIEs, which we do not consolidate because we are not the primary beneficiary. Our financial support and maximum loss exposure relating to these non-consolidated VIEs are not material to our financial condition, results of operations, or cash flows.

We use the equity method to account for our investments in entities that we do not control under the voting interest or variable interest models, but where we have the ability to exercise significant influence over operating and financial policies. Equity in loss (income) of non-consolidated affiliates includes our share of the net income (loss) of these entities.

**Product Warranty Liability**

The following table presents accrued product warranty and deferred warranty revenue activity:

(in millions)	Three Months Ended	
	January 31,	
	2014	2013
Balance at beginning of period	\$1,349	\$1,118
Costs accrued and revenues deferred	71	111
Currency translation adjustment	(2	) —
Adjustments to pre-existing warranties <sup>(A)(B)</sup>	52	40
Payments and revenues recognized	(132	) (161
Balance at end of period	1,338	1,108
Less: Current portion	602	559
Noncurrent accrued product warranty and deferred warranty revenue	\$736	\$549

Adjustments to pre-existing warranties reflect changes in our estimate of warranty costs for products sold in prior periods. Such adjustments typically occur when claims experience deviates from historic and expected trends. Our (A) warranty liability is generally affected by component failure rates, repair costs, and the timing of failures. Future events and circumstances related to these factors could materially change our estimates and require adjustments to our liability. In addition, new product launches require a greater use of judgment in developing estimates until historical experience becomes available.

In the first quarter of 2014, we recorded adjustments for changes in estimates of \$52 million or \$0.64 per diluted share. In the first quarter of 2013, we recorded adjustments for changes in estimates of \$40 million or \$0.50 per diluted share. The impact of income taxes on the 2014 and 2013 adjustments is not material due to our deferred tax valuation allowances on our U.S. deferred tax assets

In the first quarter of 2013, we recognized \$13 million of charges for adjustments to pre-existing warranties for a specific warranty issue related to component parts from a supplier. Also during the first quarter of 2013, we (B) reached agreement for reimbursement from this supplier for this amount and other costs previously accrued. As a result of this agreement, we recognized a recovery of \$27 million within Costs of products sold and recorded a receivable within Other current assets.

**Extended Warranty Programs**

The amount of deferred revenue related to extended warranty programs was \$427 million and \$420 million at January 31, 2014 and October 31, 2013 respectively. Revenue recognized under our extended warranty programs was

\$27 million and \$29 million in the three months ended January 31, 2014 and 2013, respectively.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles ("GAAP") requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses for the periods presented. Significant estimates and assumptions are used for, but are not limited to, pension and other postretirement benefits, allowance for doubtful accounts, income tax contingency accruals and valuation allowances, product warranty accruals, asbestos and other product liability accruals, asset impairment charges, and litigation-related accruals. Actual results could differ from our estimates.

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Navistar International Corporation and Subsidiaries  
Notes to Condensed Consolidated Financial Statements—(Continued)  
(Unaudited)

Concentration Risks

Our financial condition, results of operations, and cash flows are subject to concentration risks related to concentrations of our union employees. As of January 31, 2014, approximately 5,700, or 64%, of our hourly workers and approximately 400, or 6%, of our salaried workers are represented by labor unions and are covered by collective bargaining agreements. Our current master collective bargaining agreement with the UAW will expire in October 2014. Our future operations may be affected by changes in governmental procurement policies, budget considerations, changing national defense requirements, and global, political, regulatory and economic developments in the U.S. and certain foreign countries (primarily Canada, Mexico, and Brazil).

Goodwill

Goodwill represents the excess of the cost of an acquired business over the amounts assigned to the net assets. Goodwill is not amortized but is tested for impairment at a reporting unit level on an annual basis or more frequently, if circumstances change or an event occurs that would more likely than not reduce the fair value of a reporting unit below its carrying amount.

Qualitative factors may be assessed to determine whether it is more likely than not that the fair value of the reporting unit is less than its carrying amount. If the qualitative assessment indicates that the carrying amount is more likely than not higher than the fair value, goodwill is tested for impairment based on a two-step test. The first step compares the fair value of a reporting unit with its carrying amount, including goodwill. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired, thus the second step of the impairment test is unnecessary. If the carrying amount of a reporting unit exceeds its fair value, the second step of the goodwill impairment test shall be performed to measure the amount of impairment loss, if any. The second step compares the implied fair value of reporting unit goodwill with the carrying amount of that goodwill. If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss shall be recognized in an amount equal to that excess.

Significant judgment is applied when goodwill is assessed for impairment. This judgment includes developing cash flow projections, selecting appropriate discount rates, identifying relevant market comparables, incorporating general economic and market conditions, and selecting an appropriate control premium. The income approach is based on discounted cash flows which are derived from internal forecasts and economic expectations for each respective reporting unit.

We have a goodwill balance of \$170 million as of January 31, 2014. During the first quarter of 2014, a Brazilian reporting unit with goodwill of \$132 million experienced declines in actual and forecasted results and cash flow. As a result of these factors as well as slower than expected growth in the Brazilian economy and a weakening of the Brazilian currency, we performed an impairment analysis in the first quarter. The income approach which is based on discounted cash flows which are derived from internal forecasts and economic expectations was used in the impairment analysis of the reporting unit. As a result of the goodwill impairment analysis, we determined that the goodwill was not impaired and that the fair value of the reporting unit exceeded its carrying amount by less than 10%. It is reasonably possible that within the next twelve months, we could recognize goodwill or other impairment charges, which could be material, if among other things, we experience adverse changes in our business including declines in profitability due to changes in volume, market pricing, cost, or the business environment.

Recently Issued and Adopted Accounting Standards

There are no recently issued accounting standards for which the Company expects a material impact on our financial statements. In addition, for the three months ended January 31, 2014, the Company has not adopted any new accounting guidance that has had a material impact on our consolidated financial statements.

2. Discontinued Operations and Other Divestitures

The Company is currently evaluating its portfolio of assets to validate their strategic and financial fit. To allow us to increase our focus on our North American core business, we are evaluating product lines, businesses, and engineering programs that fall outside of our core business. We are using Return on Invested Capital ("ROIC") methodology,

combined with an assessment of the strategic fit to our core business, to identify areas that are under-performing. For those areas under-performing, we are evaluating whether to fix, divest, or close, and expect to realize incremental benefits from these actions in the near future.

#### Discontinued Operations

In the first quarter of 2013, the Company completed the idling of the Workhorse Custom Chassis ("WCC") operations, and in the second quarter of 2013, we completed the divestiture of the WCC business for an immaterial amount. The operating results

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of the WCC operations are reported as discontinued operations in the Consolidated Statements of Operations for all periods presented.

Also in the first quarter of 2013, certain operations of the Monaco recreational vehicle ("RV") business ("Monaco") were determined to be held-for-sale. In May 2013, we divested substantially all of our interest in these operations of Monaco. The operating results of these operations of Monaco are reported as discontinued operations in the Consolidated Statements of Operations for all periods presented. The cash consideration from the divestiture was \$19 million. As a result of the divestiture, we impaired certain assets and recognized a loss totaling \$24 million.

WCC and Monaco were not material to the Company's Consolidated Balance Sheets or Condensed Consolidated Statements of Cash Flows and have not been reclassified in the respective financial statements.

The following table summarizes the discontinued operations activity in the Company's Consolidated Statements of Operations:

(in millions)	Three months ended	
	January 31, 2014	2013
Sales and revenues, net	\$—	\$34
Income (loss) before income taxes	\$1	\$(9 )
Income tax benefit (expense)	—	—
Income (loss) from discontinued operations, net of tax	\$1	\$(9 )

We generally use a centralized approach to cash management, financing of our Manufacturing operations, and general corporate related functions, and, accordingly, do not allocate debt, interest expense, or corporate overhead to our discontinued businesses. Any debt and related interest expense of a specific entity within a business is recorded by the respective entity.

#### Other Divestitures

##### Mahindra Joint Ventures

In 2006 and 2008, we formed two joint ventures with Mahindra & Mahindra Ltd. ("Mahindra") in India, which operated under the names of Mahindra Navistar Automotives Ltd. ("MNAL") and Mahindra-Navistar Engines Private Ltd. ("MNEPL") (collectively, the "Mahindra Joint Ventures"). In February 2013, the Company sold its stake in the Mahindra Joint Ventures to Mahindra for \$33 million. As a result of the divestiture, the Global Operations segment recognized a gain of \$26 million in 2013. As part of the transaction, the Company entered into licensing and service agreements with Mahindra.

#### 3. Restructurings and Impairments

Restructuring charges are recorded on restructuring plans that have been committed to by management and are, in part, based upon management's best estimates of future events. Changes to the estimates may require future adjustments to the restructuring liabilities. In the three months ended January 31, 2014 and 2013, the Company recognized Restructuring charges of \$3 million and \$2 million, respectively. In the three months ended January 31, 2014, the Company recognized Asset impairment charges of \$18 million.

#### Cost-Reductions and Other Strategic Initiatives

From time to time, we announced actions to control spending across the Company with targeted reductions of certain costs. We are focused on continued reductions in discretionary spending, including but not limited to reductions from efficiencies, and prioritizing or eliminating certain programs or projects.

We continue to focus on improving our core North America Truck and Parts businesses. We continue to evaluate our portfolio of assets, with the purpose of closing or divesting non-core/non-strategic businesses, and identifying opportunities to restructure our business and rationalize our Manufacturing operations in an effort to optimize our cost structure. The Company is currently evaluating its portfolio of assets to validate their strategic and financial fit. To allow us to increase our focus on our North America core businesses, we are evaluating product lines, businesses, and

engineering programs that fall outside of our core businesses. We are using ROIC, combined with an assessment of the strategic fit to our core businesses, to identify areas that are not performing to our expectations. For those areas, we are evaluating whether to fix, divest, or close. These actions could result in additional restructuring and other related charges in the future, including but not limited to; (i) impairments, (ii) costs for employee and contractor termination and other related benefits, and (iii) charges for pension and other postretirement contractual benefits and pension curtailments. These charges could be significant.

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As a result of our ongoing evaluation of our portfolio of assets to validate their strategic and financial fit, which led to the discontinuation of certain engineering programs related to products that were determined to be outside of our core operations or not performing to our expectations, the North America Truck segment recognized certain charges, which included (i) accelerated depreciation of certain assets of \$13 million in the first quarter of 2013, which impacted Cost of products sold in the Company's Consolidated Statements of Operations, and (ii) asset impairments of \$17 million in the third quarter of 2013.

In the first quarter of 2014, the Company concluded it had a triggering event related to potential sales of assets requiring assessment of impairment for certain intangible and long-lived assets in the North America Truck segment. As a result, certain amortizing intangible assets and long-lived assets were determined to be fully impaired, resulting in an impairment charge of \$18 million that was recognized in Asset impairment charges in the Company's Consolidated Statements of Operations. For more information, see Note 10, Fair value measurements.

**Voluntary separation program and reduction-in-force actions**

In the fourth quarter of 2012, the Company offered the majority of our U.S.-based non-represented salaried employees the opportunity to apply for a voluntary separation program ("VSP"). Along with the employees who chose to participate in the VSP, we used attrition and an involuntary reduction-in-force to eliminate additional positions in order to meet our targeted reductions goal. In addition to these actions in the U.S., our Brazilian operations utilized an involuntary reduction in force to eliminate positions.

In the fourth quarter of 2013, the Company leveraged efficiencies identified through redesigning our organizational structure and began implementing new cost-reduction initiatives, including an enterprise-wide reduction-in-force. As a result of these actions, the Company recognized restructuring charges of \$11 million in personnel costs for employee termination and related benefits, of which a portion was paid in 2013. The Company expects the remaining restructuring charges will be paid throughout 2014.

**Warrenville, Illinois Lease Vacancy**

In the second quarter of 2012, the Company vacated the premises of its former world headquarters in Warrenville, Illinois. The cash payments associated with the lease vacancy obligation are expected to be completed by the end of 2016.

**North American Manufacturing Restructuring Activities**

The Company continues to evaluate opportunities to restructure and rationalize its Manufacturing operations in an effort to optimize our cost structure.

**Chatham restructuring activities**

In the third quarter of 2011, the Company committed to close its Chatham, Ontario heavy truck plant, which had been idled since June 2009. Potential additional charges in future periods could range from \$20 million to \$70 million, primarily related to pension and postretirement costs and termination benefits, which are subject to employee negotiation and acceptance rates.

**Garland Facility closure**

In the fourth quarter of 2012, the Company committed to plans for the closure of its Garland, Texas truck manufacturing operations (the "Garland Facility"). Beginning in early 2013, the Company began transitioning production from the Garland Facility to other North America operations that produce similar models. In the second quarter of 2013, production at the Garland Facility ceased. In the first and second quarters of 2013, we recognized charges of \$12 million and \$8 million, respectively, for the acceleration of depreciation of certain assets related to the facility that impacted Cost of products sold in the Company's Consolidated Statements of Operations.

**Huntsville Facility**

In February 2014, the Company announced plans to consolidate its mid-range engine manufacturing footprint and relocate mid-range engine production from its Huntsville, Alabama, facility ("Huntsville Facility") to its Melrose Park, Illinois facility ("Melrose Park Facility"). As a result, in the first quarter of 2014, the North America Truck segment recognized restructuring charges of \$1 million for personnel costs related to employee terminations and \$2

million for inventory reserves related to the idled production equipment at the Huntsville Facility that impacted Cost of products sold in the Company's Consolidated Statements of Operations.



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**Restructuring Liability**

The following tables summarize the activity in the restructuring liability, which includes amounts related to discontinued operations and excludes pension and other postretirement contractual termination benefits:

(in millions)	Balance at October 31, 2013	Additions	Payments	Adjustments	Balance at January 31, 2014
Employee termination charges	\$15	\$2	\$(5 )	\$(1 )	\$11
Employee relocation costs	—	1	(1 )	—	—
Lease vacancy	18	—	(2 )	—	16
Other	1	—	(1 )	1	1
Restructuring liability	\$34	\$3	\$(9 )	\$—	\$28

  

(in millions)	Balance at October 31, 2012	Additions	Payments	Adjustments	Balance at January 31, 2013
Employee termination charges	\$ 72	\$—	\$(27 )	\$(2 )	\$43
Employee relocation costs	—	1	(1 )	—	—
Lease vacancy	17	1	(2 )	1	17
Other	—	1	—	—	1
Restructuring liability	\$ 89	\$3	\$(30 )	\$(1 )	\$61

**4. Finance Receivables**

Finance receivables are receivables of our Financial Services operations. Finance receivables generally consist of wholesale notes and accounts, as well as retail notes, finance leases and accounts. Total finance receivables reported on the Consolidated Balance Sheets are net of an allowance for doubtful accounts. Total assets of our Financial Services operations net of intercompany balances are \$2.2 billion and \$2.4 billion as of January 31, 2014 and October 31, 2013, respectively. Included in total assets are finance receivables of \$1.8 billion and \$1.9 billion as of January 31, 2014 and October 31, 2013, respectively. We have two portfolio segments of finance receivables based on the type of financing inherent to each portfolio. The retail portfolio segment represents loans or leases to end-users for the purchase or lease of vehicles. The wholesale portfolio segment represents loans to dealers to finance their inventory.

Our Finance receivables, net, consist of the following:

(in millions)	January 31, 2014	October 31, 2013
Retail portfolio	\$739	\$751
Wholesale portfolio	1,049	1,207
Total finance receivables	1,788	1,958
Less: Allowance for doubtful accounts	24	23
Total finance receivables, net	1,764	1,935
Less: Current portion, net <sup>(A)</sup>	1,461	1,597
Noncurrent portion, net	\$303	\$338

The current portion of finance receivables is computed based on contractual maturities. Actual cash collections (A) typically vary from the contractual cash flows because of prepayments, extensions, delinquencies, credit losses, and renewals.

**Securitizations**

Our Financial Services operations transfers wholesale notes, retail accounts receivable, retail notes, finance leases, and operating leases through special purpose entities ("SPEs"), which generally are only permitted to purchase these

assets, issue asset-backed securities, and make payments on the securities. In addition to servicing receivables, our continued involvement in the SPEs may include an economic interest in the transferred receivables and, in some cases, managing exposure to interest rates using interest rate swaps and interest rate caps. There were no transfers of finance receivables that qualified for sale accounting treatment as of January 31, 2014 and October 31, 2013, and as a result, the transferred finance receivables are included in our Consolidated Balance Sheets and the related interest earned is included in Finance revenues.

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We transfer eligible finance receivables into retail note owner trusts or wholesale note owner trusts in order to issue asset-backed securities. These trusts are VIEs of which we are determined to be the primary beneficiary and, therefore, the assets and liabilities of the trusts are included in our Consolidated Balance Sheets. The outstanding balance of finance receivables transferred into these VIEs was \$871 million and \$948 million as of January 31, 2014 and October 31, 2013, respectively. Other finance receivables related to secured transactions that do not qualify for sale accounting treatment were \$4 million as of both January 31, 2014 and October 31, 2013. For more information on assets and liabilities of consolidated VIEs and other securitizations accounted for as secured borrowings by our Financial Services segment, see Note 1, Summary of Significant Accounting Policies.

**Finance Revenues**

The following table presents the components of our Finance revenues:

(in millions)	Three Months Ended January 31,	
	2014	2013
Retail notes and finance leases revenue	\$17	\$21
Wholesale notes interest	18	20
Operating lease revenue	14	12
Retail and wholesale accounts interest	6	6
Gross finance revenues	55	59
Less: Intercompany revenues	(16	) (20
Finance revenues	\$39	\$39

**5. Allowance for Doubtful Accounts**

Our two portfolio segments, retail and wholesale, each consist of one class of receivable based on: (i) initial measurement attributes of the receivables, and (ii) the assessment and monitoring of risk and performance of the receivables. For more information, see Note 4, Finance Receivables.

The following tables present the activity related to our allowance for doubtful accounts for our retail portfolio segment, wholesale portfolio segment, and trade and other receivables:

(in millions)	Three Months Ended January 31, 2014			
	Retail Portfolio	Wholesale Portfolio	Trade and Other Receivables	Total
Allowance for doubtful accounts, at beginning of period	\$21	\$2	\$37	\$60
Provision for doubtful accounts, net of recoveries	4	—	2	6
Charge-off of accounts <sup>(A)</sup>	(2	) —	—	(2
Other <sup>(B)</sup>	(1	) —	(3	) (4
Allowance for doubtful accounts, at end of period	\$22	\$2	\$36	\$60
(in millions)	Three Months Ended January 31, 2013			
	Retail Portfolio	Wholesale Portfolio	Trade and Other Receivables	Total
Allowance for doubtful accounts, at beginning of period	\$27	\$—	\$24	\$51
Provision for doubtful accounts, net of recoveries	(1	) 2	—	1
Charge-off of accounts <sup>(A)</sup>	(3	) —	—	(3
Allowance for doubtful accounts, at end of period	\$23	\$2	\$24	\$49

(A) We repossess sold and leased vehicles on defaulted finance receivables and leases, and place them into Inventories. Losses recognized at the time of repossession and charged against the allowance for doubtful accounts

were less than \$1 million for both the three months ended January 31, 2014 and 2013.

(B) Amounts include currency translation.

The accrual of interest income is discontinued on certain impaired finance receivables. Impaired finance receivables include accounts with specific loss reserves and certain accounts that are on non-accrual status. In certain cases, we continue to collect payments on our impaired finance receivables.

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The following table presents information regarding impaired finance receivables:

(in millions)	January 31, 2014			October 31, 2013		
	Retail Portfolio	Wholesale Portfolio	Total	Retail Portfolio	Wholesale Portfolio	Total
Impaired finance receivables with specific loss reserves	\$ 14	\$ —	\$ 14	\$ 15	\$ —	\$ 15
Impaired finance receivables without specific loss reserves	1	—	1	1	—	1
Specific loss reserves on impaired finance receivables	5	—	5	6	—	6
Finance receivables on non-accrual status	13	—	13	10	—	10

For the impaired finance receivables in the retail portfolio as of January 31, 2014 and 2013, the average balances of those receivables were \$14 million during both the three months ended January 31, 2014 and 2013.

The Company uses the aging of its receivables as well as other inputs when assessing credit quality. The following table presents the aging analysis for finance receivables:

(in millions)	January 31, 2014			October 31, 2013		
	Retail Portfolio	Wholesale Portfolio	Total	Retail Portfolio	Wholesale Portfolio	Total
Current, and up to 30 days past due	\$686	\$ 1,044	\$1,730	\$699	\$ 1,204	\$ 1,903
30-90 days past due	40	4	44	44	2	46
Over 90 days past due	13	1	14	8	1	9
Total finance receivables	\$739	\$ 1,049	\$1,788	\$751	\$ 1,207	\$ 1,958

## 6. Inventories

The following table presents the components of Inventories:

(in millions)	January 31, 2014	October 31, 2013
Finished products	\$775	\$692
Work in process	101	58
Raw materials	506	460
Total inventories	\$1,382	\$1,210

## 7. Debt

(in millions)	January 31, 2014	October 31, 2013
Manufacturing operations		
Senior Secured Term Loan Credit Facility, as Amended, due 2017, net of unamortized discount of \$4 for both periods	\$693	\$693
8.25% Senior Notes, due 2021, net of unamortized discount of \$22 for both periods	1,178	1,178
3.00% Senior Subordinated Convertible Notes, due 2014, net of unamortized discount of \$19 and \$26, respectively	551	544
4.50% Senior Subordinated Convertible Notes, due 2018, net of unamortized discount of \$22 and \$23, respectively	178	177
Debt of majority-owned dealerships	46	48
Financing arrangements and capital lease obligations	70	77
Loan Agreement related to 6.5% Tax Exempt Bonds, due 2040	225	225
Promissory Note	18	20
Financed lease obligations	219	218
Other	34	39

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Total Manufacturing operations debt	3,212	3,219
Less: Current portion	662	658
Net long-term Manufacturing operations debt	\$2,550	\$2,561

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(in millions)	January 31, 2014	October 31, 2013
Financial Services operations		
Asset-backed debt issued by consolidated SPEs, at fixed and variable rates, due serially through 2019	\$752	\$778
Bank revolvers, at fixed and variable rates, due dates from 2014 through 2019	820	1,018
Commercial paper, at variable rates, program matures in 2015	22	21
Borrowings secured by operating and finance leases, at various rates, due serially through 2018	58	49
Total Financial Services operations debt	1,652	1,866
Less: Current portion	597	505
Net long-term Financial Services operations debt	\$1,055	\$1,361

## Financial Services Operations

In November 2013, Navistar Financial, S.A. de C.V., SOFOM, E.N.R, our Mexican financial services affiliate ("NFM") expanded its facility of five-year notes secured by retail finance receivables by selling an additional P\$800 million (the equivalent of US \$60 million at January 31, 2014).

In December 2013, International Truck Leasing Corporation, a special purpose, wholly-owned subsidiary of NFC, issued borrowings secured by operating and finance leases of \$21 million.

## 8. Postretirement Benefits

## Defined Benefit Plans

We provide postretirement benefits to a substantial portion of our employees and retirees. Costs associated with postretirement benefits include pension and postretirement health care expenses for employees, retirees, and surviving spouses and dependents. Generally, the pension plans are non-contributory. Our policy is to fund the pension plans in accordance with applicable U.S. and Canadian government regulations and to make additional contributions from time to time. For the three months ended January 31, 2014 and 2013, we contributed \$29 million and \$27 million, respectively, to our pension plans to meet regulatory funding requirements. We currently anticipate additional contributions of \$169 million to our pension plans during the remainder of 2014.

We primarily fund other post-employment benefit ("OPEB") obligations, such as retiree medical, in accordance with a 1993 Settlement Agreement (the "1993 Settlement Agreement"), which requires us to fund a portion of the plans' annual service cost to a retiree benefit trust (the "Base Trust"). The 1993 Settlement Agreement resolved a class action lawsuit originally filed in 1992 regarding the restructuring of the Company's then applicable retiree health care and life insurance benefits. Contributions for the three months ended January 31, 2014 and 2013, as well as anticipated contributions for the remainder of 2014, are not material.

## Components of Net Periodic Benefit Expense (Income)

Net postretirement benefits expense included in our Consolidated Statements of Operations is comprised of the following:

(in millions)	Three Months Ended January 31,			
	Pension Benefits		Health and Life Insurance Benefits	
	2014	2013	2014	2013
Service cost for benefits earned during the period	\$4	\$5	\$1	\$2
Interest on obligation	39	36	17	15
Amortization of cumulative loss	24	32	4	7
Amortization of prior service benefit	—	—	(1	) (1
Expected return on assets	(48	) (47	) (8	) (8
Net postretirement benefits expense	\$19	\$26	\$13	\$15

Defined Contribution Plans and Other Contractual Arrangements

Our defined contribution plans cover a substantial portion of domestic salaried employees and certain domestic represented employees. The defined contribution plans contain a 401(k) feature and provide most participants with a matching contribution from the Company. Effective February 1, 2013, the Company changed the timing for depositing the matching contributions to

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the end of the calendar year. Many participants covered by the plans receive annual Company contributions to their retirement accounts based on an age-weighted percentage of the participant's eligible compensation for the calendar year. Defined contribution expense pursuant to these plans was \$8 million and \$7 million in the three months ended January 31, 2014 and 2013, respectively.

In accordance with the 1993 Settlement Agreement, an independent Retiree Supplemental Benefit Trust (the "Supplemental Trust") was established. The Supplemental Trust, and the benefits it provides to certain retirees pursuant to a certain Retiree Supplemental Benefit Program under the 1993 Settlement Agreement ("Supplemental Benefit Program"), is not part of the Company's consolidated financial statements. The assets of the Supplemental Trust arise from three sources: (i) the Company's 1993 contribution to the Supplemental Trust of 25.5 million shares of our Class B common stock, which were subsequently sold by the Supplemental Trust prior to 2000, (ii) contingent profit-sharing contributions made by the Company pursuant to a certain Supplemental Benefit Trust Profit Sharing Plan ("Supplemental Benefit Profit Sharing Plan"), and (iii) net investment gains on the Supplemental Trust's assets, if any.

The Company's contingent profit sharing obligations under the Supplemental Benefits Profit Sharing Plan will continue until certain funding targets defined by the 1993 Settlement Agreement are met ("Profit Sharing Cessation"). Upon Profit Sharing Cessation, the Company would assume responsibility for (i) establishing the investment policy for the Supplemental Trust, (ii) approving or disapproving of certain additional supplemental benefits to the extent such benefits would result in higher expenditures than those contemplated upon the Profit Sharing Cessation, and (iii) making additional contributions to the Supplemental Trust as necessary to make up for investment and/or actuarial losses. We have recorded no profit sharing accruals based on the operating performance of the entities that are included in the determination of qualifying profits. For more information, see Note 12, Commitments and Contingencies, for a discussion of pending litigation regarding the Supplemental Benefit Profit Sharing Plan.

#### 9. Income Taxes

We compute on a quarterly basis an estimated annual effective tax rate considering ordinary income and related income tax expense. For all periods presented, U.S. and certain foreign results are excluded from ordinary income due to ordinary losses for which no benefit can be recognized. Ordinary income refers to income (loss) before income tax expense excluding significant unusual or infrequently occurring items. The tax effect of a significant unusual or infrequently occurring item is recorded in the interim period in which it occurs. Items included in income tax expense in the periods in which they occur include the tax effects of material restructurings and impairments, cumulative effect of changes in tax laws or rates, foreign exchange gains and losses, adjustments to uncertain tax positions, and adjustments to our valuation allowance due to changes in judgment regarding the ability to realize deferred tax assets in future years.

We have evaluated the need to maintain a valuation allowance for deferred tax assets based on our assessment of whether it is more likely than not that deferred tax benefits will be realized through the generation of future taxable income. Appropriate consideration is given to all available evidence, both positive and negative, in assessing the need for a valuation allowance. We continue to maintain a valuation allowance on our U.S. deferred tax assets, as well as certain foreign deferred tax assets, that we believe, on a more-likely-than-not basis, will not be realized. For all remaining deferred tax assets, while we believe that it is more likely than not that they will be realized, we believe that it is reasonably possible that additional deferred tax asset valuation allowances could be required in the next twelve months.

We recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the consolidated financial statements from such a position are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. As of January 31, 2014, the amount of liability for uncertain tax positions was \$64 million. If the unrecognized tax benefits are recognized, all but \$6 million would impact our effective tax rate. However, to the extent we continue to maintain a full valuation

allowance against certain deferred tax assets, the effect may be in the form of an increase in the deferred tax asset related to our net operating loss carry forward, which would be offset by a full valuation allowance.

We recognize interest and penalties related to uncertain tax positions as part of Income tax benefit (expense). For the three months ended January 31, 2014 and 2013, total interest and penalties related to our uncertain tax positions resulted in an income tax benefit of \$3 million and expense of \$4 million, respectively.

We have open tax years back to 2001 with various significant taxing jurisdictions including the U.S., Canada, Mexico, and Brazil. In connection with the examination of tax returns, contingencies may arise that generally result from differing interpretations of applicable tax laws and regulations as they relate to the amount, timing, or inclusion of revenues or expenses in taxable income, or the sustainability of tax credits to reduce income taxes payable. We believe we have sufficient accruals for

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our contingent tax liabilities. Annual tax provisions include amounts considered sufficient to pay assessments that may result from examinations of prior year tax returns, although actual results may differ. While it is probable that the liability for unrecognized tax benefits may increase or decrease during the next 12 months, we do not expect any such change would have a material effect on our financial condition, results of operations, or cash flows.

In the three months ended January 31, 2014, we reached a tax settlement with the State of Alabama, which resulted in the recording of a decrease to our uncertain tax positions of \$8 million. In the first quarter of 2013, we accrued \$12 million related to this matter, but later reduced our accrual by \$4 million in the fourth quarter of 2013 in anticipation of the settlement.

10. Fair Value Measurements

For assets and liabilities measured at fair value on a recurring and nonrecurring basis, a three-level hierarchy of measurements based upon observable and unobservable inputs is used to arrive at fair value. Observable inputs are developed based on market data obtained from independent sources, while unobservable inputs reflect our assumptions about valuation based on the best information available in the circumstances. Depending on the inputs, we classify each fair value measurement as follows:

• Level 1—based upon quoted prices for identical instruments in active markets,

• Level 2—based upon quoted prices for similar instruments, prices for identical or similar instruments in markets that are not active, or model-derived valuations, all of whose significant inputs are observable, and

• Level 3—based upon one or more significant unobservable inputs.

The following section describes key inputs and assumptions in our valuation methodologies:

**Cash Equivalents and Restricted Cash Equivalents**—We classify highly liquid investments, with an original maturity of 90 days or less, including U.S. Treasury bills, federal agency securities, and commercial paper, as cash equivalents. The carrying amounts of cash and cash equivalents and restricted cash approximate fair value because of the short-term maturity and highly liquid nature of these instruments.

**Marketable Securities**—Our marketable securities portfolios are classified as available-for-sale and primarily include investments in U.S. government securities and commercial paper with a maturity of greater than 90 days from the date of purchase. We use quoted prices from active markets to determine fair value.

**Derivative Assets and Liabilities**—We measure the fair value of derivatives assuming that the unit of account is an individual derivative transaction and that each derivative could be sold or transferred on a stand-alone basis. We classify within Level 2 our derivatives that are traded over-the-counter and valued using internal models based on observable market inputs. In certain cases, market data is not available and we estimate inputs such as in situations where trading in a particular commodity is not active. Measurements based upon these unobservable inputs are classified within Level 3. For more information regarding derivatives, see Note 11, Financial Instruments and Commodity Contracts.

**Guarantees**—We provide certain guarantees of payments and residual values to specific counterparties. Fair value of these guarantees is based upon internally developed models that utilize current market-based assumptions and historical data. We classify these liabilities within Level 3. For more information regarding guarantees, see Note 12, Commitments and Contingencies.

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The following table presents the financial instruments measured at fair value on a recurring basis:

(in millions)	January 31, 2014				October 31, 2013			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets								
Marketable securities:								
U.S. Treasury bills	\$281	\$—	\$—	\$281	\$396	\$—	\$—	\$396
Other	349	—	—	349	434	—	—	434
Derivative financial instruments:								
Foreign currency contracts	—	—	—	—	—	4	—	4
Interest rate caps	—	3	—	3	—	1	—	1
Total assets	\$630	\$3	\$—	\$633	\$830	\$5	\$—	\$835
Liabilities								
Derivative financial instruments:								
Foreign currency contracts	\$—	\$1	\$—	\$1	\$—	\$—	\$—	\$—
Guarantees	—	—	6	6	—	—	6	6
Total liabilities	\$—	\$1	\$6	\$7	\$—	\$—	\$6	\$6

The following table presents the changes for those financial instruments classified within Level 3 of the valuation hierarchy:

(in millions)	Three Months Ended January 31,			
	2014		2013	
	Guarantees	Commodity contracts	Guarantees	Commodity contracts
Balance at November 1	\$(6 )	\$—	\$(7 )	\$—
Transfers out of Level 3	—	—	—	—
Issuances	—	—	—	—
Settlements	—	—	—	—
Balance at January 31	\$(6 )	\$—	\$(7 )	\$—
Change in unrealized gains on assets and liabilities still held	\$—	\$—	\$—	\$—

The following table presents the financial instruments measured at fair value on a nonrecurring basis:

(in millions)	January 31, 2014	October 31, 2013
Level 2 financial instruments		
Carrying value of impaired finance receivables <sup>(A)</sup>	\$14	\$15
Specific loss reserve	(5 )	(6 )
Fair value	\$9	\$9

Certain impaired finance receivables are measured at fair value on a nonrecurring basis. An impairment charge is recorded for the amount by which the carrying value of the receivables exceeds the fair value of the underlying collateral, net of remarketing costs. Fair values of the underlying collateral are determined by reference to dealer vehicle value publications adjusted for certain market factors.

In the first quarter of 2014, the Company concluded it had a triggering event related to potential sales of assets requiring assessment of impairment for certain intangible and long-lived assets in the North America Truck segment. As a result, certain amortizing intangible assets and long-lived assets with a carrying value of \$18 million were determined to be fully impaired, resulting in an impairment charge of \$18 million, which was included in Asset impairment charges in the Company's Consolidated Statements of Operations. We utilized the market approach to

determine the fair values of these Level 2 assets.

In addition to the methods and assumptions we use for the financial instruments recorded at fair value as discussed above, we use the following methods and assumptions to estimate the fair value for our other financial instruments that are not marked to market on a recurring basis. The carrying amounts of Cash and cash equivalents, Restricted cash, and Accounts payable approximate fair values because of the short-term maturity and highly liquid nature of these instruments. Finance receivables generally consist of retail and wholesale accounts and retail and wholesale notes. The carrying amounts of Trade and other receivables and retail and wholesale accounts approximate fair values as a result of the short-term nature of the receivables. The carrying amounts of wholesale notes approximate fair values as a result of the short-term nature of the wholesale notes and their

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variable interest rate terms. The fair values of these financial instruments are classified as Level 1. Due to the nature of the aforementioned financial instruments, they have been excluded from the fair value amounts presented in the table below.

The fair values of our retail notes are estimated by discounting expected cash flows at estimated current market rates. The fair values of our retail notes are classified as Level 3 financial instruments.

The fair values of our debt instruments classified as Level 1 were determined using quoted market prices. Our Loan Agreement underlying the Tax Exempt Bonds is traded, but is illiquid, and as a result, is classified as Level 2. The fair values of our Level 3 debt instruments are generally determined using internally developed valuation techniques such as discounted cash flow modeling. Inputs such as discount rates and credit spreads reflect our estimates of assumptions that market participants would use in pricing the instrument and may be unobservable.

The following tables present the carrying values and estimated fair values of financial instruments:

(in millions)	As of January 31, 2014				Carrying Value
	Estimated Fair Value			Total	
	Level 1	Level 2	Level 3	Total	
Assets					
Retail notes	\$—	\$—	\$339	\$339	\$335
Notes receivable	—	—	12	12	70
Liabilities					
Debt:					
Manufacturing operations					
Senior Secured Term Loan Credit Facility, as Amended due 2017	—	—	723	723	693
8.25% Senior Notes, due 2021	1,264	—	—	1,264	1,178
3.0% Senior Subordinated Convertible Notes, due 2014 <sup>(A)</sup>	577	—	—	577	551
4.50% Senior Subordinated Convertible Notes, due 2018	—	—	199	199	178
Debt of majority-owned dealerships	—	—	46	46	46
Financing arrangements	—	—	39	39	67
Loan Agreement related to 6.5% Tax Exempt Bonds, due 2040	—	224	—	224	225
Promissory Note	—	—	18	18	18
Financed lease obligations	—	—	219	219	219
Other	—	—	31	31	34
Financial Services operations					
Asset-backed debt issued by consolidated SPEs, at various rates, due serially through 2019	—	—	746	746	752
Bank revolvers, at fixed and variable rates, due dates from 2014 through 2019	—	—	798	798	820
Commercial paper, at variable rates, program matures in 2015	22	—	—	22	22
Borrowings secured by operating and finance leases, at various rates, due serially through 2018	—	—	58	58	58

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(in millions)	As of October 31, 2013				Carrying Value
	Estimated Fair Value			Total	
	Level 1	Level 2	Level 3	Total	
Assets					
Retail notes	\$—	\$—	\$390	\$390	\$390
Notes receivable	—	—	13	13	14
Liabilities					
Debt:					
Manufacturing operations					
Senior Secured Term Loan Credit Facility, as Amended due 2017	—	—	720	720	693
8.25% Senior Notes, due 2021	1,274	—	—	1,274	1,178
3.0% Senior Subordinated Convertible Notes, due 2014 <sup>(A)</sup>	586	—	—	586	544
4.50% Senior Subordinated Convertible Notes, due 2018	—	—	203	203	177
Debt of majority-owned dealerships	—	—	48	48	48
Financing arrangements	—	—	44	44	73
Loan Agreement related to 6.5% Tax Exempt Bonds, due 2040	—	229	—	229	225
Promissory Note	—	—	20	20	20
Financed Lease Obligations	—	—	218	218	218
Other	—	—	36	36	39
Financial Services operations					
Asset-backed debt issued by consolidated SPEs, at various rates, due serially through 2019	—	—	775	775	778
Bank revolvers, at fixed and variable rates, due dates from 2014 through 2019	—	—	990	990	1,018
Commercial paper, at variable rates, program matures in 2015	21	—	—	21	21
Borrowings secured by operating and finance leases, at various rates, due serially through 2017	—	—	49	49	49

The carrying value represents the consolidated financial statement amount of the debt which excludes the (A) allocation of the conversion feature to equity, while the fair value is based on quoted market prices for the convertible note which includes the equity feature.

## 11. Financial Instruments and Commodity Contracts

### Derivative Financial Instruments

We use derivative financial instruments as part of our overall interest rate, foreign currency, and commodity risk management strategies to reduce our interest rate exposure, reduce exchange rate risk for transactional exposures denominated in currencies other than the functional currency, and minimize the effect of commodity price volatility. From time to time, we use foreign currency forward and option contracts to manage the risk of exchange rate movements that would affect the value of our foreign currency cash flows. Foreign currency exchange rate movements create a degree of risk by affecting the value of sales made and costs incurred in currencies other than the functional currency. From time to time, we also use commodity forward contracts to manage our exposure to variability in certain commodity prices. In 2009, in connection with the sale of our 3.00% Senior Subordinated Convertible Notes, due 2014 (the "2014 Convertible Notes"), we purchased call options for \$125 million. The call options are intended to minimize share dilution associated with the 2014 Convertible Notes. As the call options and warrants are indexed to our common stock, we recognized them in permanent equity in Additional paid in capital in the Company's Consolidated Balance Sheets, and will not recognize subsequent changes in fair value as long as the instruments remain classified as equity.

We generally do not enter into derivative financial instruments for speculative or trading purposes and did not during the three months ended January 31, 2014 and 2013. None of our derivatives qualified for hedge accounting treatment during the three months ended January 31, 2014 and 2013.

The majority of our derivative contracts are transacted under International Swaps and Derivatives Association ("ISDA") master agreements. Each agreement permits the net settlement of amounts owed in the event of default or certain other termination events. For derivative financial instruments, we have elected not to offset derivative positions in the balance sheet with the same counterparty under the same agreement. Certain of our derivative contracts contain provisions that require us to provide collateral if certain thresholds are exceeded. No collateral was provided at January 31, 2014 and at October 31, 2013. Collateral



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is generally not required to be provided by our counter-parties for derivative contracts. We manage exposure to counter-party credit risk by entering into derivative financial instruments with various major financial institutions that can be expected to fully perform under the terms of such instruments. We do not anticipate nonperformance by any of the counter-parties. Our exposure to credit risk in the event of nonperformance by the counter-parties is limited to those assets that have been recorded, but have not yet been received in cash. At January 31, 2014 and October 31, 2013, our exposure to the credit risk of others was \$3 million and \$5 million, respectively.

Our Financial Services operations may use interest rate swaps or interest rate caps from time to time to manage exposure to fluctuations in interest rates by limiting the amount of fixed rate finance receivables that are funded with variable rate debt. The Mexican Financial Services operation uses cross currency swaps to limit exposure to fluctuations in the value of the peso, as required under Mexican bank credit facilities.

The fair values of all derivatives are recorded as assets or liabilities on a gross basis in our Consolidated Balance Sheets. The following table presents the fair values of our derivatives and their respective balance sheet locations:

(in millions)	January 31, 2014		Liability Derivatives	
	Asset Derivatives		Location in	
	Location in	Fair Value	Consolidated Balance Sheets	Fair Value
Foreign currency contracts	Other current assets	\$—	Other current liabilities	\$1
Interest rate caps	Other current assets	3	Other noncurrent liabilities	—
Total fair value		\$3		\$1
(in millions)	October 31, 2013		Liability Derivatives	
	Asset Derivatives		Location in	
	Location in	Fair Value	Consolidated Balance Sheets	Fair Value
Foreign currency contracts	Other current assets	\$4	Other current liabilities	\$—
Interest rate caps	Other noncurrent assets	1	Other current liabilities	—
Total fair value		\$5		\$—

The following table presents the location and amount of loss (gain) recognized in our Consolidated Statements of Operations related to derivatives:

(in millions)	Location in Consolidated Statements of Operations	Three Months Ended January 31,	
		2014	2013
Cross currency swaps	Other expense (income), net	\$1	\$—
Interest rate caps	Interest expense	(1)	) —
Foreign currency contracts	Other expense (income), net	—	1
Total loss		\$—	\$1

**Foreign Currency Contracts**

During 2014 and 2013, we entered into foreign exchange forward and option contracts as economic hedges of anticipated cash flows denominated in Canadian Dollars, Brazilian Reals and Euros. All contracts were entered into to protect against the risk that the eventual cash flows resulting from certain transactions would be affected by changes in exchange rates between the U.S. dollar and the respective foreign currency.

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The following table presents the outstanding foreign currency contracts as of January 31, 2014 and October 31, 2013:

(in millions)	Currency	Notional Amount	Maturity
As of January 31, 2014			
Forward exchange contract	EUR	€ 20	April 2014
As of October 31, 2013			
Option collar contracts	EUR	€ 2	October 2013
Forward exchange contract	CAD	C\$ 90	October 2013
Option collar contract	CAD	C\$ 50	October 2013
Option collar contract	BRL	US\$25	October 2013

**Commodity Forward Contracts**

During 2014 and 2013, we entered into commodity forward contracts as economic hedges of our exposure to variability in commodity prices for diesel fuel and steel. As of January 31, 2014, we had outstanding diesel fuel contracts with aggregate notional values of \$6 million and outstanding steel contracts with aggregate notional values of \$11 million. The commodity forward contracts have maturity dates ranging from May 31, 2014 to July 31, 2014. As of October 31, 2013, we had outstanding diesel fuel contracts with aggregate notional values of \$2 million and outstanding steel contracts with aggregate notional values of \$11 million. All of these contracts were entered into to protect against the risk that the eventual cash flows related to purchases of the commodities will be affected by changes in prices.

**Interest-Rate Contracts**

From time to time, we enter into various interest-rate contracts, interest rate caps, and cross currency swaps. As of January 31, 2014 and October 31, 2013, the notional amount of our outstanding cross currency swaps was \$30 million and \$45 million, respectively. We are exposed to interest rate and exchange rate risk as a result of our borrowing activities. The objective of these contracts is to mitigate fluctuations in earnings, cash flows, and fair value of borrowings. Our Mexican financial services operation uses interest rate caps to protect against the potential of rising interest rates as required by the terms of its variable-rate asset-backed securities. As of January 31, 2014 and October 31, 2013, the notional amount of our outstanding interest rate caps was \$135 million and \$78 million, respectively.

**12. Commitments and Contingencies****Guarantees**

We occasionally provide guarantees that could obligate us to make future payments if the primary entity fails to perform under its contractual obligations. We have recognized liabilities for some of these guarantees in our Consolidated Balance Sheets as they meet the recognition and measurement provisions of U.S. GAAP. In addition to the liabilities that have been recognized, we are contingently liable for other potential losses under various guarantees. We do not believe that claims that may be made under such guarantees would have a material effect on our financial condition, results of operations, or cash flows.

In March 2010, we entered into an operating agreement, as amended, which contains automatic extensions and is subject to early termination provisions, with GE (the "GE Operating Agreement"). Under the terms of the GE Operating Agreement, as amended, GE is our preferred source of retail customer financing for equipment offered by us and our dealers in the U.S. We provide GE with a loss sharing arrangement for certain credit losses. Under the loss sharing arrangement we generally reimburse GE for credit losses in excess of the first 10% of the original value of a financed contract. The Company's exposure to loss is mitigated because receivables financed under the GE Operating Agreement are secured by the financed equipment. We do not carry the receivables financed under the GE Operating Agreement on our Consolidated Balance Sheets. There were \$1.4 billion of outstanding finance receivables at both January 31, 2014 and October 31, 2013 financed through the GE Operating Agreement and subject to the loss sharing arrangement. The related originations of these outstanding finance receivables were \$2.0 billion at both January 31, 2014 and October 31, 2013. Related to certain third-party equipment financings by GE and for which we have

accounted for as borrowings, we have recognized equipment leased to others of \$190 million and financed lease obligations of \$219 million included in our Consolidated Balance Sheets for the period ended January 31, 2014. Historically, our losses, representing the entire loss amount, on similar finance receivables, measured as a percentage of the average balance of the related finance receivable, ranged from 0.3% to 2.1%. While under limited circumstances NFC retains the right to originate retail customer financing, we expect retail finance receivables and retail finance revenues will continue to

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decline as our retail portfolio pays down. Based on our historic experience of losses on similar finance receivables and the nature of the loss sharing arrangement, we do not believe our share of losses related to balances currently outstanding will be material.

For certain independent dealers' wholesale inventory financed by third-party banks or finance companies, we provide limited repurchase agreements to the respective financing institution. The amount of losses related to these arrangements has not been material to our Consolidated Statements of Operations or Condensed Consolidated Statements of Cash Flows and the value of the guarantees and accruals recorded are not material to our Consolidated Balance Sheets.

We also have issued limited residual value guarantees in connection with various leases. The amounts of the guarantees are estimated and recorded. Our guarantees are contingent upon the fair value of the leased assets at the end of the lease term. The amount of losses related to these arrangements has not been material to our Consolidated Statements of Operations or Condensed Consolidated Statements of Cash Flows and the value of the guarantees and accruals recorded are not material to our Consolidated Balance Sheets.

We obtain certain stand-by letters of credit and surety bonds from third-party financial institutions in the ordinary course of business when required under contracts or to satisfy insurance-related requirements. As of January 31, 2014, the amount of stand-by letters of credit and surety bonds was \$203 million.

We extend credit commitments to certain truck fleet customers, which allow them to purchase parts and services from participating dealers. The participating dealers receive accelerated payments from us with the result that we carry the receivables and absorb the credit risk related to these customers. As of January 31, 2014, we have \$7 million of unused credit commitments outstanding under this program.

In addition, as of January 31, 2014, we have entered into various purchase commitments of \$187 million and contracts that have cancellation fees of \$49 million with various expiration dates through 2019.

In the ordinary course of business, we also provide routine indemnifications and other guarantees, the terms of which range in duration and often are not explicitly defined. We do not believe these will result in claims that would have a material impact on our financial condition, results of operations, or cash flows.

**Environmental Liabilities**

We have been named a potentially responsible party ("PRP"), in conjunction with other parties, in a number of cases arising under an environmental protection law, the Comprehensive Environmental Response, Compensation, and Liability Act, popularly known as the "Superfund" law. These cases involve sites that allegedly received wastes from current or former Company locations. Based on information available to us which, in most cases, consists of data related to quantities and characteristics of material generated at current or former Company locations, material allegedly shipped by us to these disposal sites, as well as cost estimates from PRPs and/or federal or state regulatory agencies for the cleanup of these sites, a reasonable estimate is calculated of our share of the probable costs, if any, and accruals are recorded in our consolidated financial statements. These accruals are generally recognized no later than upon completion of the remedial feasibility study and are not discounted to their present value. We review all accruals on a regular basis and believe that, based on these calculations, our share of the potential additional costs for the cleanup of each site will not have a material effect on our financial condition, results of operations, or cash flows. Two sites formerly owned by us: (i) Solar Turbines in San Diego, California, and (ii) the Canton Plant in Canton, Illinois; were identified as having soil and groundwater contamination. Two sites in Sao Paulo, Brazil, where we are currently operating, were identified as having soil and groundwater contamination. While investigations and cleanup activities continue at these and other sites, we believe that we have adequate accruals to cover costs to complete the cleanup of all sites.

We have accrued \$22 million for these and other environmental matters, which are included within Other current liabilities and Other noncurrent liabilities, as of January 31, 2014. The majority of these accrued liabilities are expected to be paid subsequent to 2014.

Along with other vehicle manufacturers, we have been subject to an increased number of asbestos-related claims in recent years. In general, these claims relate to illnesses alleged to have resulted from asbestos exposure from component parts found in older vehicles, although some cases relate to the alleged presence of asbestos in our facilities. In these claims, we are generally not the sole defendant, and the claims name as defendants numerous manufacturers and suppliers of a wide variety of products allegedly containing asbestos. We have strongly disputed these claims, and it has been our policy to defend against them vigorously. Historically, the actual damages paid out to claimants have not been material in any year to our financial condition,

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results of operations, or cash flows. It is possible that the number of these claims will continue to grow, and that the costs for resolving asbestos related claims could become significant in the future.

Legal Proceedings

Overview

We are subject to various claims arising in the ordinary course of business, and are party to various legal proceedings that constitute ordinary, routine litigation incidental to our business. The majority of these claims and proceedings relate to commercial, product liability, and warranty matters. In addition, from time to time we are subject to various claims and legal proceedings related to employee compensation, benefits, and benefits administration including, but not limited to, compliance with the Employee Retirement Income Security Act of 1974, as amended, and Department of Labor requirements. In our opinion, apart from the actions set forth below, the disposition of these proceedings and claims, after taking into account recorded accruals and the availability and limits of our insurance coverage, will not have a material adverse effect on our business or our financial condition, results of operations, or cash flows.

Profit Sharing Disputes

Pursuant to the 1993 Settlement Agreement, the program administrator and named fiduciary of the Supplemental Benefit Program is the Supplemental Benefit Program committee (the "Committee"), comprised of non-Company individuals. In August 2013, the Committee filed a motion for leave to amend its February 2013 complaint (which sought injunctive relief for the Company to provide certain information to which it was allegedly entitled under the Supplemental Benefit Profit Sharing Plan) and a proposed amended complaint (the "Profit Sharing Complaint") in the U.S. District Court for the Southern District of Ohio (the "Court"). Leave to file the Profit Sharing Complaint was granted by the Court in October 2013. In its Profit Sharing Complaint, the Committee alleges the Company breached the 1993 Settlement Agreement and violated ERISA by failing to properly calculate profit sharing contributions due under the Supplemental Benefit Profit Sharing Plan. The Committee seeks damages in excess of \$50 million, injunctive relief and reimbursement of attorneys' fees and costs. In October 2013, the Company filed a motion to dismiss the Profit Sharing Complaint and to compel the Committee to comply with the dispute resolution procedures set forth in the Supplemental Benefit Trust Profit Sharing Plan. The Company's motion is currently pending before the Court. In addition, various local bargaining units of the UAW have filed separate grievances pursuant to the profit sharing plans under various collective bargaining agreements in effect between the Company and the UAW that may have similar legal and factual issues as the Profit Sharing Complaint.

FATMA Notice

International Indústria de Motores da América do Sul Ltda. ("IIAA"), formerly known as Maxion International Motores S/A ("Maxion"), now a wholly owned subsidiary of the Company, received a notice in July 2010 from the State of Santa Catarina Environmental Protection Agency ("FATMA") in Brazil. The notice alleged that Maxion had sent wastes to a facility owned and operated by a company known as Natureza and that soil and groundwater contamination had occurred at the Natureza facility. The notice asserted liability against Maxion and assessed an initial penalty in the amount of R\$2 million (the equivalent of approximately US\$1 million at January 31, 2014), which is not due and final until all administrative appeals are exhausted. Maxion was one of numerous companies that received similar notices. IIAA filed an administrative defense in August 2010 and has not yet received a decision following that filing. IIAA disputes the allegations in the notice and intends to vigorously defend itself.

Lis Franco de Toledo, et. al. vs. Syntex do Brasil and IIAA

In 1973, Syntex do Brasil Industria e Comercio Ltda. ("Syntex"), a predecessor of IIAA, our Brazilian engine manufacturing subsidiary, which was formerly known as MWM International Industria de Motores da America do Sul Ltda ("MWM"), filed a lawsuit in Brazilian court against Dr. Lis Franco de Toledo and others (collectively, "Lis Franco"). Syntex claimed Lis Franco had improperly terminated a contract which provided for the transfer from Lis Franco to Syntex of a patent for the production of a certain vaccine. Lis Franco filed a counterclaim alleging that he was entitled to royalties under the contract. In 1975, the Brazilian court ruled in favor of Lis Franco, a decision which was affirmed on appeal in 1976. In 1984, while the case was still pending, Syntex' owner, Syntex Comercio e

Participacoes Ltda ("Syntex Parent") sold the stock of Syntex to MWM, and in connection with that sale Syntex Parent agreed to indemnify and hold harmless MWM for any and all liabilities of Syntex, including its prior pharmaceutical operations (which had been previously spun-off to another subsidiary wholly-owned by the Syntex Parent) and any payments that might be payable under the Lis Franco lawsuit. In the mid to late 1990s, Syntex Parent was merged with an entity known as Wyeth Industria Farmaceutica LTDA ("Wyeth").

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In 1999, Lis Franco amended its pleadings to add MWM to the lawsuit as a defendant. In 2000, Wyeth acknowledged to the Brazilian court its sole responsibility for amounts due in the Lis Franco lawsuit and MWM asked the court to be dismissed from that action. The judge denied that request. MWM appealed and lost.

In his pleadings, Lis Franco alleged that the royalties payable to him were approximately R\$42 million. MWM believed the appropriate amount payable was approximately R\$16 million. In December 2009, the court appointed expert responsible for the preparation of the royalty calculation filed a report with the court indicating royalty damages of approximately R\$70 million. MWM challenged the expert's calculation. In August 2010, the court asked the parties to consider the appointment of a new expert. MWM agreed with this request but Lis Franco objected and, in September 2010, the court accepted and ratified the expert's calculation as of May 2010 in the amount of R\$74 million and entered judgment against MWM.

In September 2010, MWM filed a motion for clarification of the decision which would suspend its enforcement. The Brazilian court denied this motion and MWM appealed the matter to the Rio de Janeiro State Court of Appeals (the "Court of Appeals"). In January 2011, the Court of Appeals granted the appeal and issued an injunction suspending the lower court's decision and judgment in favor of Lis Franco. In January 2011, MWM merged into IIAA and is now known as IIAA. An expert appointed by the Court of Appeals submitted his calculation report on October 24, 2011, and determined the amount to be R\$10.85 million. The parties submitted comments to such report in December 2011, the expert replied to these comments and ratified his previous report in May 2012, and the parties again submitted comments to the expert's reply. The expert reviewed these comments and submitted a complementary report in December 2012 which determined the amount to be R\$22 million. The parties submitted comments to the complementary report in January 2013. In May 2013, the Court of Appeals determined the damages amount to be R\$25 million (the equivalent of approximately US\$12 million at January 31, 2014). Wyeth, Lis Franco and MWM filed motions for clarification against such decision and in July 2013 the Court of Appeals denied all of these motions. MWM, Wyeth and Lis Franco filed a special appeal to the Brasilia Special Court of Appeals on August 20, 2013. The Brasilia Special Court of Appeals has not yet ruled on the special appeal.

In parallel, in May 2010, MWM filed a lawsuit in Sao Paulo, Brazil, against Wyeth seeking recognition that Wyeth is liable for any and all liabilities, costs, expenses, and payments related to the Lis Franco lawsuit. In September 2012, the Sao Paulo court ruled in favor of MWM and ordered Wyeth to pay, directly to the Estate of Lis Franco de Toledo and others and jointly with MWM, the amounts of the condemnation, to be determined at the end of the liquidation proceeding. The Sao Paulo court also ordered Wyeth to reimburse MWM for all expenses, including court costs and attorney fees associated with the case. The parties were notified of the decision in October 2012, to which MWM and Wyeth filed motions for clarification of certain issues, and in December 2012, the Sao Paulo court rejected both motions. In January 2013, Wyeth filed an appeal to the Sao Paulo court's December 2012 decision, and in April 2013, MWM filed an answer to the appeal. The appeal was rejected by the Court of Appeals on September 10, 2013. Wyeth filed a motion for clarification to the Court of Appeals. The motion was rejected by the Court of Appeals on November 5, 2013.

The parties are currently in settlement discussions with respect to these matters.

Westbrook vs. Navistar. et. al.

In April 2011, a False Claims Act qui tam complaint against Navistar, Inc., Navistar Defense, LLC, a wholly owned subsidiary of the Company ("Navistar Defense"), and unrelated third parties was unsealed by the United States District Court for the Northern District of Texas (the "Court"). The complaint was initially filed under seal in August 2010 by a qui tam relator ("Westbrook") on behalf of the federal government. The complaint alleged violations of the False Claims Act based on allegations that parts of vehicles delivered by Navistar Defense were not painted according to the contract specification, and improper activities in dealing with one of the vendors who painted certain of the vehicle parts. The complaint seeks monetary damages and civil penalties on behalf of the federal government, as well as costs and expenses. After the complaint was unsealed, the U.S. government notified the Court that it declined to intervene at that time. Navistar, Inc. was served with the complaint in July 2011, and a scheduling order and a revised



scheduling order was entered by the Court. In December 2011, the Court granted a motion by Navistar, Inc. and Navistar Defense, along with the other named defendants to judicially estop Westbrook and his affiliated company from participating in any recovery from the action, and to substitute his bankruptcy trustee (the "Trustee") as the only person with standing to pursue Westbrook's claims. In March 2012, the Court granted motions by Navistar, Inc., Navistar Defense, and the other named defendants to dismiss the complaint. The dismissal was without prejudice and the Trustee filed an amended complaint in April 2012. In May 2012, Navistar, Inc., Navistar Defense, and the other named defendants filed motions to dismiss the amended complaint. In addition, the parties jointly filed a motion to stay discovery pending resolution of the motions to dismiss. In July 2012, the Court granted all of the defendants' motions to dismiss with prejudice, dismissing all of the claims except the claim against Navistar Defense for retaliation and the claim against Navistar, Inc. for retaliation, which was dismissed without prejudice. Plaintiff was granted leave to file an amended complaint including only the retaliation claims against Navistar Defense and Navistar, Inc. The Trustee did not file a retaliation

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claim against Navistar, Inc. and voluntarily dismissed without prejudice the retaliation claim against Navistar Defense. The Trustee also filed a motion for reconsideration of the dismissal of the False Claims Act claims against Navistar Defense which the Court denied. The Court issued final judgment dismissing the matter in July 2012. Westbrook filed a notice of appeal to the Fifth Circuit Court of Appeals ("Fifth Circuit") in August 2012 as to the final judgment and the motion for reconsideration as to Navistar Defense only. The Trustee filed a separate notice of appeal to the Fifth Circuit in August 2012 as to several district court orders, including the December 2011 order holding the Trustee, not Westbrook, to be the proper party in the case. In December 2012, Navistar Defense's motion to dismiss Westbrook's appeal was denied "without prejudice to reconsideration by the oral argument panel" by the Fifth Circuit. The Fifth Circuit heard oral arguments on both appeals in November 2013 but has not yet issued a ruling on either appeal. Based on our assessment of the facts underlying the claims in the above action, we are unable to provide meaningful quantification of how the final resolution of these claims may impact our future consolidated financial condition, results of operations, or cash flows.

**EPA Notice of Violation**

In February 2012, Navistar, Inc. received a Notice of Violation ("NOV") from the U.S. Environmental Protection Agency ("EPA"). The NOV pertains to approximately 7,600 diesel engines which, according to the EPA, were produced by Navistar, Inc. in 2010 and, therefore, should have met the EPA's 2010 emissions standards. Navistar, Inc. previously provided information to the EPA showing that the engines were in fact produced in 2009. The NOV contains the EPA's conclusion that Navistar, Inc.'s alleged production of the engines in 2010 violated the Federal Clean Air Act. The NOV states that the EPA reserves the right to file an administrative complaint or to refer this matter to the U.S. Department of Justice with a recommendation that a civil complaint be filed in federal district court.

Based on our assessment of the facts underlying the NOV above, we are unable to provide meaningful quantification of how the final resolution of this matter may impact our future consolidated financial condition, results of operations or cash flows.

**CARB Notice of Violation**

In April 2013, Navistar, Inc. received a notice of violation and proposed settlement ("Notice") from the California Air Resources Board ("CARB"). The Notice alleges violations of the California regulations relating to verification of after-treatment devices and proposed civil penalties of approximately \$2.5 million, among other proposed settlement terms. Beginning in June 2013, the Company has made settlement offers to CARB and remains in discussions regarding this matter.

Based on our assessment of the facts underlying the Notice from CARB, we are unable to provide meaningful quantification of how the final resolution of this matter may impact our future consolidated financial condition, results of operations or cash flows.

**Shareholder Litigation**

In March 2013, a putative class action complaint, alleging securities fraud, was filed against us by the Construction Workers Pension Trust Fund - Lake County and Vicinity, on behalf of itself and all other similarly situated purchasers of our common stock between the period of November 3, 2010 and August 1, 2012. A second class action complaint was filed in April 2013 by the Norfolk County Retirement System, individually and on behalf of all other similarly situated purchasers of our common stock between the period of June 9, 2010 and August 1, 2012. A third class action complaint was filed in April 2013 by Jane C. Purnell FBO Purnell Family Trust, on behalf of itself and all other similarly situated purchasers of our common stock between the period of November 3, 2010 and August 1, 2012. Each complaint named us as well as Daniel C. Ustian, our former President and Chief Executive Officer, and Andrew J. Cederoth, our former Executive Vice President and Chief Financial Officer as defendants. These complaints (collectively, the "10b-5 Cases") contain similar factual allegations which include, among other things, that we violated the federal securities laws by knowingly issuing materially false and misleading statements concerning our financial condition and future business prospects and that we misrepresented and omitted material facts in filings with

the SEC concerning the timing and likelihood of EPA certification of our EGR technology to meet 2010 EPA emission standards. The plaintiffs in these matters seek compensatory damages and attorneys' fees, among other relief. In May 2013, an order was entered transferring and consolidating all cases before one judge and in July 2013, the Court appointed a lead plaintiff and lead plaintiff's counsel. The lead plaintiff filed a consolidated amended complaint in October 2013. The consolidated amended complaint enlarged the proposed class period to June 9, 2009 through August 1, 2012, and named fourteen additional current and former directors and officers as defendants. The defendants filed Motions to Dismiss on December 17, 2013. The plaintiff filed an Omnibus Opposition to Defendants' Motions to Dismiss, and a Motion to Strike on January 31, 2014. The defendants filed their opposition to the Motion to Strike on February 18, 2014 and filed a reply in support of their Motions to Dismiss on March 3, 2014.

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In March 2013, James Gould filed a derivative complaint on behalf of the Company against us and certain of our current and former directors and former officers. The complaint alleges, among other things, that certain of our current and former directors and former officers committed a breach of fiduciary duty, waste of corporate assets and were unjustly enriched in relation to similar factual allegations made in the 10b-5 Cases. The plaintiff in this matter seeks compensatory damages, certain corporate governance reforms, certain injunctive relief, disgorgement of the proceeds of certain defendants' profits from the sale of Company stock, and attorneys' fees, among other relief. Pursuant to a court order in May 2013, this matter has been stayed until the outcome of any motion to dismiss in the 10b-5 Cases. Each of these matters is pending in the United States District Court, Northern District of Illinois.

In August 2013, Abbie Griffin, filed a derivative complaint in the State of Delaware Court of Chancery, on behalf of the Company and all similarly situated stockholders, against the Company, as the nominal defendant, and certain of our current and former directors and former officers. The complaint alleges, among other things, that certain of our current and former directors and former officers committed a breach of fiduciary duty, in relation to similar factual allegations made in the 10b-5 Cases. The plaintiff in this matter seeks compensatory damages, certain corporate governance reforms, certain injunctive relief, and attorneys' fees, among other relief. Pursuant to a court order in August 2013, this matter has been stayed until the outcome of any motion to dismiss in the 10b-5 Cases.

Based on our assessment of the facts underlying these matters described above, we are unable to provide meaningful quantification of how the final resolution of these matters may impact our future consolidated financial condition, results of operations, or cash flows.

**Deloitte & Touche LLP**

In April 2011, the Company filed a complaint against Deloitte and Touche LLP ("Deloitte"). In December 2012, the parties reached a settlement. As a result of this settlement in the first quarter of 2013, the Company received cash proceeds of \$35 million, which were recorded as a gain to Other expense (income), net, in the Company's Consolidated Statements of Operations.

**Other**

**U.S. Securities and Exchange Commission ("SEC") Inquiry**

In June 2012, Navistar received an informal inquiry from the Chicago Office of the Enforcement Division of the SEC seeking a number of categories of documents for the periods dating back to November 1, 2010, relating to various accounting and disclosure issues. We received a formal order of private investigation in July 2012. We have received subsequent subpoenas from the SEC in connection with their inquiry, and we continue our full cooperation with the SEC in this matter. At this time, we are unable to predict the outcome of this matter or provide meaningful quantification of how the final resolution of this matter may impact our future consolidated financial condition, results of operations or cash flows.

**Non-Conformance Penalties**

In January 2012, the EPA promulgated the Interim Final Rule establishing non-conformance penalties ("NCPs") for heavy-duty diesel ("HDD") engines, and we began using NCPs for trucks using certain of our HDD engines in 2012. Also in January 2012, the EPA published a Notice of Proposed Rulemaking for a final NCP rule (the "Final Rule"), which proposed to make NCPs available in model years 2012 and later for emissions of NOx above the 0.20g limit for both medium and heavy HDD engines. The EPA promulgated the Final Rule for heavy HDD engines in September 2012. The Final Rule did not include NCPs for medium HDD engines. On December 11, 2013, the D.C. Circuit Court issued an opinion vacating the Final Rule. On February 10, 2014, the EPA filed a petition for panel rehearing asking the D.C. Circuit to reconsider that portion of its opinion vacating the Final Rule. The EPA's petition is currently pending. However, the Company did not plan to use the NCP rule to certify engines in model year 2014. A challenge to 2013 certificates under the Final Rule remains held in abeyance at the D.C. Circuit Court. In the three months ended January 31, 2014 and 2013, the North America Truck segment recorded charges totaling \$2 million and \$10 million, respectively, for NCPs for certain engine sales.



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## 13. Segment Reporting

The following is a description of our four reporting segments:

Our North America Truck segment manufactures and distributes Class 4 through 8 trucks, buses, and military vehicles under the International and IC Bus ("IC") brands, along with production of engines under the MaxxFace brand name, in the North America markets that include sales in the U.S., Canada, and Mexico. In an effort to strengthen and maintain our dealer network, this segment occasionally acquires and operates dealer locations for the purpose of transitioning ownership.

Our North America Parts segment provides customers with proprietary products needed to support the International commercial and military truck, IC Bus, MaxxFace engine lines, as well as our other product lines. Our North America Parts segment also provides a wide selection of other standard truck, trailer, and engine aftermarket parts. At January 31, 2014, this segment operated eleven regional parts distribution centers that provide 24-hour availability and shipment. Also included in the North America Parts segment are the operating results of BDP, which manages the sourcing, merchandising, and distribution of certain service parts we sell to Ford in North America.

Our Global Operations segment includes businesses that derive their revenue from outside our core North America markets and primarily consists of the IIAA (formerly MWM) engine and truck operations in Brazil and our export truck and parts businesses. The IIAA engine operations produce diesel engines, primarily under contract manufacturing arrangements, as well as under the MWM brand, for sale to OEMs in South America.

Our Financial Services segment provides retail, wholesale, and lease financing of products sold by the North America Truck and North America Parts segments and their dealers within the U.S. and Mexico, as well as financing for wholesale accounts and selected retail accounts receivable.

Corporate contains those items that are not included in our four segments.

## Segment Profit (Loss)

We define segment profit (loss) as Net income (loss) from continuing operations attributable to Navistar International Corporation excluding Income tax benefit (expense). The following tables present selected financial information for our reporting segments:

(in millions)	North America Truck	North America Parts	Global Operations	Financial Services <sup>(A)</sup>	Corporate and Eliminations	Total
Three Months Ended January 31, 2014						
External sales and revenues, net	\$1,277	\$597	\$295	\$39	\$—	\$2,208
Intersegment sales and revenues	88	10	8	16	(122)	—
Total sales and revenues, net	\$1,365	\$607	\$303	\$55	\$(122)	\$2,208
Income (loss) from continuing operations attributable to NIC, net of tax	\$(207)	\$104	\$(33)	\$23	\$(136)	\$(249)
Income tax benefit	—	—	—	—	12	12
Segment profit (loss)	\$(207)	\$104	\$(33)	\$23	\$(148)	\$(261)
Depreciation and amortization	\$58	\$4	\$8	\$10	\$6	\$86
Interest expense	—	—	—	17	65	82
Equity in income (loss) of non-consolidated affiliates	1	1	(2)	—	—	—
Capital expenditures <sup>(B)</sup>	12	4	3	1	1	21

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(in millions)	North America Truck	North America Parts	Global Operations	Financial Services <sup>(A)</sup>	Corporate and Eliminations	Total
Three Months Ended January 31, 2013						
External sales and revenues, net	\$1,538	\$669	\$391	\$39	\$—	\$2,637
Intersegment sales and revenues	127	18	15	20	(180)	—
Total sales and revenues, net	\$1,665	\$687	\$406	\$59	\$(180)	\$2,637
Income (loss) from continuing operations attributable to NIC, net of tax	\$(101)	\$117	\$(10)	\$22	\$(142)	\$(114)
Income tax expense	—	—	—	—	(15)	(15)
Segment profit (loss)	\$(101)	\$117	\$(10)	\$22	\$(127)	\$(99)
Depreciation and amortization	\$71	\$4	\$9	\$9	\$7	\$100
Interest expense	—	—	—	18	56	74
Equity in income (loss) of non-consolidated affiliates	2	1	(4)	—	—	(1)
Capital expenditures <sup>(B)</sup>	65	1	3	—	3	72
(in millions)	North America Truck	North America Parts	Global Operations	Financial Services	Corporate and Eliminations	Total
Segment assets, as of:						
January 31, 2014	\$2,309	\$701	\$994	\$2,243	\$1,407	\$7,654
October 31, 2013	2,250	716	1,162	2,355	1,832	8,315

(A) Total sales and revenues in the Financial Services segment include interest revenues of \$40 million and \$47 million for the three months ended January 31, 2014 and 2013, respectively.

(B) Exclusive of purchases of equipment leased to others.

## 14. Stockholders' Deficit

## October 2012 Issuance of Common Stock

In October 2012, the Company completed a public offering of 10,666,666 shares of NIC common stock at a price of \$18.75 per share and received proceeds, net of underwriting discounts, commissions, and offering expenses, of \$192 million. In connection with the public offering, in November 2012, the underwriters elected to exercise a portion of an over-allotment option and purchased an additional 763,534 shares of NIC common stock at a price of \$18.75 per share. The Company received proceeds from the exercise of the over-allotment, net of underwriting discounts and commissions, of \$14 million in the three months ended January 31, 2013.

## Accumulated Other Comprehensive Loss

The following table displays the changes in Accumulated other comprehensive loss, net of tax, by component from October 31, 2013 to January 31, 2014:

(in millions)	Foreign Currency Translation Adjustments	Defined Benefit Plan	Total
Balance as of October 31, 2013	\$(75)	\$(1,749)	\$(1,824)
Other comprehensive loss before reclassifications	(62)	(1)	(63)
Amounts reclassified out of accumulated other comprehensive loss	—	26	26
Net current-period other comprehensive income (loss)	(62)	25	(37)
Balance as of January 31, 2014	\$(137)	\$(1,724)	\$(1,861)





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The following table displays the amounts reclassified from Accumulated other comprehensive loss and the affected line item in the Consolidated Statements of Operations:

	Location in Consolidated Statements of Operations	Three months ended January 31, 2014
Defined benefit plans		
Amortization of prior service costs	Selling, general and administrative expenses	\$(1 )
Amortization of actuarial loss	Selling, general and administrative expenses	27
	Total before tax	26
	Tax benefit (expense)	—
	Net of tax	26
Total reclassifications for the period, net of tax		\$26

## 15. Earnings (Loss) Per Share Attributable to Navistar International Corporation

The following table presents the information used in the calculation of our basic and diluted income (loss) per share for continuing operations, discontinued operations, and net loss, all attributable to Navistar International Corporation:

(in millions, except per share data)	Three months ended January 31,	
	2014	2013
Numerator:		
Amounts attributable to Navistar International Corporation common stockholders:		
Loss from continuing operations, net of tax	\$(249 )	\$(114 )
Income (loss) from discontinued operations, net of tax	1	(9 )
Net loss	\$(248 )	\$(123 )
Denominator:		
Weighted average shares outstanding:		
Basic	81.2	80.2
Effect of dilutive securities	—	—
Diluted	81.2	80.2
Earnings (loss) per share attributable to Navistar International Corporation:		
Basic:		
Continuing operations	\$(3.07 )	\$(1.42 )
Discontinued operations	0.02	(0.11 )
	\$(3.05 )	\$(1.53 )
Diluted:		
Continuing operations	\$(3.07 )	\$(1.42 )
Discontinued operations	0.02	(0.11 )
	\$(3.05 )	\$(1.53 )

The conversion rate on our 2014 Convertible Notes is 19.891 shares of common stock per \$1,000 principal amount of 2014 Convertible Notes, equivalent to an initial conversion price of \$50.27 per share of common stock. In connection with the sale of the 2014 Convertible Notes, we sold warrants to various counterparties to purchase shares of our common stock from us at an exercise price of \$60.14 per share. The 2014 Convertible Notes and warrants are anti-dilutive when calculating diluted earnings per share when our average stock price is less than \$50.27 and \$60.14, respectively.

We also purchased call options in connection with the sale of the 2014 Convertible Notes, covering 11.3 million shares at an exercise price of \$50.27 per share, which are intended to minimize share dilution associated with the 2014 Convertible Notes; however under accounting guidance, these call options cannot be utilized to offset the dilution of the 2014 Convertible Notes for determining diluted earnings per share as they are anti-dilutive.

The conversion rate on our 4.50% Senior Subordinated Convertible Notes, due 2018 (the "2018 Convertible Notes"), is 17.1233 shares of common stock per \$1,000 principal amount of 2018 Convertible Notes, equivalent to an initial conversion price of

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approximately \$58.40 per share of common stock. The 2018 Convertible Notes are anti-dilutive when calculating diluted earnings per share when our average stock price is less than \$58.40.

The computation of diluted earnings per share also excludes outstanding options and other common stock equivalents in periods where inclusion of such potential common stock instruments would be anti-dilutive.

For the three months ended January 31, 2014 and 2013, no dilutive securities were included in the computation of diluted loss per share since they would have been anti-dilutive due to the net loss attributable to Navistar International Corporation. Additionally, certain securities would have been excluded from the computation of earnings per share, as our average stock price was less than their respective exercise prices. For the three months ended January 31, 2014 and 2013, the aggregate shares not included were 31 million and 28 million, respectively, of which 11.3 million shares were related to the warrants and 11.3 million shares were related to the 2014 Convertible Notes, as well as for the three months ended January 31, 2014, 3.4 million shares were related to the 2018 Convertible Notes.

16. Condensed Consolidating Guarantor and Non-guarantor Financial Information

The following tables set forth condensed consolidating balance sheets as of January 31, 2014 and 2013, and condensed consolidating statements of operations and condensed consolidating statements of comprehensive income (loss) for the three months ended January 31, 2014 and 2013, and condensed consolidating statements of cash flows for the three months ended January 31, 2014 and 2013.

The information is presented as a result of Navistar, Inc.'s guarantee, exclusive of its subsidiaries, of NIC's indebtedness under our 8.25% Senior Notes, due 2021, and obligations under our Loan Agreement related to the 6.5% Tax Exempt Bonds, due 2040. Navistar, Inc. is a direct wholly-owned subsidiary of NIC. None of NIC's other subsidiaries guarantee any of these notes or bonds. The guarantees are "full and unconditional", as those terms are used in Regulation S-X Rule 3-10, except that the guarantees will be automatically released in certain customary circumstances, such as when the subsidiary is sold or all of the assets of the subsidiary are sold, the capital stock is sold, when the subsidiary is designated as an "unrestricted subsidiary" for purposes of the respective indenture for each of the 8.25% Senior Notes, due 2021, and the 6.5% Tax Exempt Bonds, due 2040, upon liquidation or dissolution of the subsidiary or upon legal or covenant defeasance, or satisfaction and discharge of the notes. Separate financial statements and other disclosures concerning Navistar, Inc. have not been presented because management believes that such information is not material to investors. Within this disclosure only, "NIC" includes the financial results of the parent company only, with all of its wholly-owned subsidiaries accounted for under the equity method. Likewise, "Navistar, Inc.," for purposes of this disclosure only, includes the consolidated financial results of its wholly-owned subsidiaries accounted for under the equity method and its operating units accounted for on a consolidated basis. "Non-Guarantor Subsidiaries" includes the combined financial results of all other non-guarantor subsidiaries. "Eliminations and Other" includes all eliminations and reclassifications to reconcile to the consolidated financial statements. NIC files a consolidated U.S. federal income tax return that includes Navistar, Inc. and its U.S. subsidiaries. Navistar, Inc. has a tax allocation agreement ("Tax Agreement") with NIC which requires Navistar, Inc. to compute its separate federal income tax liability and remit any resulting tax liability to NIC. Tax benefits that may arise from net operating losses of Navistar, Inc. are not refunded to Navistar, Inc. but may be used to offset future required tax payments under the Tax Agreement. The effect of the Tax Agreement is to allow NIC, the parent company, rather than Navistar, Inc., to utilize current U.S. taxable losses of Navistar, Inc. and all other direct or indirect subsidiaries of NIC.

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## Condensed Consolidating Statement of Operations for the Three Months Ended January 31, 2014

(in millions)	NIC	Navistar, Inc.	Non-Guarantor Subsidiaries	Eliminations and Other	Consolidated
Sales and revenues, net	\$—	\$1,424	\$ 1,729	\$ (945 )	\$ 2,208
Costs of products sold	—	1,425	1,531	(942 )	2,014
Restructuring charges	—	2	1	—	3
Asset impairment charges	—	—	18	—	18
All other operating expenses (income)	36	241	159	(11 )	425
Total costs and expenses	36	1,668	1,709	(953 )	2,460
Equity in income (loss) of affiliates	(212 )	(11 )	(1 )	224 )	—
Income (loss) before income taxes	(248 )	(255 )	19 )	232	(252 )
Income tax benefit	—	7	5	—	12
Earnings (loss) from continuing operations	(248 )	(248 )	24 )	232	(240 )
Income from discontinued operations, net of tax	—	—	1	—	1
Net income (loss)	(248 )	(248 )	25 )	232	(239 )
Less: Net income attributable to non-controlling interests	—	—	9	—	9
Net income (loss) attributable to Navistar International Corporation	\$(248 )	\$(248 )	\$ 16	\$ 232	\$(248 )

## Condensed Consolidating Statement of Comprehensive Income (Loss) for the Three Months Ended January 31, 2014

(in millions)	NIC	Navistar, Inc.	Non-Guarantor Subsidiaries	Eliminations and Other	Consolidated
Net income (loss) attributable to Navistar International Corporation	\$(248 )	\$(248 )	\$ 16	\$ 232	\$(248 )
Other comprehensive income (loss):					
Foreign currency translation adjustment	(62 )	—	(62 )	62	(62 )
Defined benefit plans (net of tax of \$0 tax for all entities)	25	25	—	(25 )	25
Total other comprehensive income (loss)	(37 )	25	(62 )	37	(37 )
Total comprehensive income (loss) attributable to Navistar International Corporation	\$(285 )	\$(223 )	\$ (46 )	\$ 269	\$(285 )

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## Condensed Consolidating Balance Sheet as of January 31, 2014

(in millions)	NIC	Navistar, Inc.	Non-Guarantor Subsidiaries	Eliminations and Other	Consolidated
<b>Assets</b>					
Cash and cash equivalents	\$ 177	\$ 40	\$ 332	\$ —	\$ 549
Marketable securities	317	—	313	—	630
Restricted cash	18	4	93	—	115
Finance and other receivables, net	(1 )	138	2,214	(6 )	2,345
Inventories	—	773	621	(12 )	1,382
Investments in non-consolidated affiliates	(6,375 )	6,586	72	(208 )	75
Property and equipment, net	—	906	790	4	1,700
Goodwill	—	—	170	—	170
Deferred taxes, net	1	13	215	—	229
Other	34	162	267	(4 )	459
<b>Total assets</b>	<b>\$(5,829 )</b>	<b>\$ 8,622</b>	<b>\$ 5,087</b>	<b>\$ (226 )</b>	<b>\$ 7,654</b>
<b>Liabilities and stockholders' equity (deficit)</b>					
<b>Debt</b>					
Debt	\$ 2,133	\$ 994	\$ 1,741	\$ (4 )	\$ 4,864
Postretirement benefits liabilities	—	2,377	243	—	2,620
Amounts due to (from) affiliates	(7,396 )	11,182	(3,871 )	85	—
Other liabilities	3,344	632	147	—	—