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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549



FORM 10-K

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

For the Fiscal Year Ended December 31, 2013

Commission File Number 1-4949

CUMMINS INC.

Indiana  
(State of Incorporation)

35-0257090  
(IRS Employer Identification No.)

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

Telephone (812) 377-5000

Securities registered pursuant to Section 12(b) of the Act:

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

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

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

The aggregate market value of the voting stock held by non-affiliates was approximately \$20.3 billion at June 30, 2013. This value includes all shares of the registrant's common stock, except for treasury shares.

As of January 31, 2014, there were 186,682,826 shares outstanding of \$2.50 par value common stock.

**Documents Incorporated by Reference**

Portions of the registrant's definitive Proxy Statement for its 2014 annual meeting of shareholders, which will be filed with the Securities and Exchange Commission on Schedule 14A within 120 days after the end of 2013, will be incorporated by reference in Part III of this Form 10-K to the extent indicated therein upon such filing.

**Website Access to Company's Reports**

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

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**CUMMINS INC. AND SUBSIDIARIES**  
**TABLE OF CONTENTS**

<u>PART</u>	<u>ITEM</u>	<u>PAGE</u>
	<a href="#"><u>Cautionary Statements Regarding Forward-Looking Information</u></a>	<a href="#"><u>3</u></a>
I	<a href="#"><u>1</u></a>	<a href="#"><u>5</u></a>
	<a href="#"><u>Business</u></a>	<a href="#"><u>5</u></a>
	<a href="#"><u>Overview</u></a>	<a href="#"><u>5</u></a>
	<a href="#"><u>Operating Segments</u></a>	<a href="#"><u>5</u></a>
	<a href="#"><u>Engine Segment</u></a>	<a href="#"><u>5</u></a>
	<a href="#"><u>Components Segment</u></a>	<a href="#"><u>6</u></a>
	<a href="#"><u>Power Generation Segment</u></a>	<a href="#"><u>8</u></a>
	<a href="#"><u>Distribution Segment</u></a>	<a href="#"><u>9</u></a>
	<a href="#"><u>Joint Ventures, Alliances and Non-Wholly-Owned Subsidiaries</u></a>	<a href="#"><u>10</u></a>
	<a href="#"><u>Supply</u></a>	<a href="#"><u>12</u></a>
	<a href="#"><u>Patents and Trademarks</u></a>	<a href="#"><u>12</u></a>
	<a href="#"><u>Seasonality</u></a>	<a href="#"><u>13</u></a>
	<a href="#"><u>Largest Customers</u></a>	<a href="#"><u>13</u></a>
	<a href="#"><u>Backlog</u></a>	<a href="#"><u>13</u></a>
	<a href="#"><u>Research and Development Expense</u></a>	<a href="#"><u>13</u></a>
	<a href="#"><u>Environmental Sustainability</u></a>	<a href="#"><u>14</u></a>
	<a href="#"><u>Environmental Compliance</u></a>	<a href="#"><u>14</u></a>
	<a href="#"><u>Employees</u></a>	<a href="#"><u>15</u></a>
	<a href="#"><u>Available Information</u></a>	<a href="#"><u>15</u></a>
	<a href="#"><u>Executive Officers of the Registrant</u></a>	<a href="#"><u>16</u></a>
1A	<a href="#"><u>Risk Factors</u></a>	<a href="#"><u>17</u></a>
1B	<a href="#"><u>Unresolved Staff Comments</u></a>	<a href="#"><u>24</u></a>
2	<a href="#"><u>Properties</u></a>	<a href="#"><u>25</u></a>
3	<a href="#"><u>Legal Proceedings</u></a>	<a href="#"><u>26</u></a>
4	<a href="#"><u>Mine Safety Disclosures</u></a>	<a href="#"><u>26</u></a>
II	<a href="#"><u>5</u></a>	<a href="#"><u>27</u></a>
	<a href="#"><u>6</u></a>	<a href="#"><u>29</u></a>
	<a href="#"><u>7</u></a>	<a href="#"><u>30</u></a>
	<a href="#"><u>7A</u></a>	<a href="#"><u>64</u></a>
	<a href="#"><u>8</u></a>	<a href="#"><u>66</u></a>
	<a href="#"><u>9</u></a>	<a href="#"><u>122</u></a>
	<a href="#"><u>9A</u></a>	<a href="#"><u>122</u></a>
	<a href="#"><u>9B</u></a>	<a href="#"><u>122</u></a>
III	<a href="#"><u>10</u></a>	<a href="#"><u>122</u></a>
	<a href="#"><u>11</u></a>	<a href="#"><u>122</u></a>
	<a href="#"><u>12</u></a>	<a href="#"><u>123</u></a>
	<a href="#"><u>13</u></a>	<a href="#"><u>123</u></a>
	<a href="#"><u>14</u></a>	<a href="#"><u>123</u></a>
IV	<a href="#"><u>15</u></a>	<a href="#"><u>123</u></a>
	<a href="#"><u>Signatures</u></a>	<a href="#"><u>124</u></a>
	<a href="#"><u>Cummins Inc. Exhibit Index</u></a>	<a href="#"><u>125</u></a>

## [Table of Contents](#)

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

### **CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING INFORMATION**

Certain parts of this annual report contain forward-looking statements intended to qualify for the safe harbors from liability established by the Private Securities Litigation Reform Act of 1995. Forward-looking statements include those that are based on current expectations, estimates and projections about the industries in which we operate and management's beliefs and assumptions. Forward-looking statements are generally accompanied by words such as "anticipates," "expects," "forecasts," "intends," "plans," "believes," "seeks," "estimates," "could," "should" or words of similar meaning. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which we refer to as "future factors," which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. Some future factors that could cause our results to differ materially from the results discussed in such forward-looking statements are discussed below and shareholders, potential investors and other readers are urged to consider these future factors carefully in evaluating forward-looking statements. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. Future factors that could affect the outcome of forward-looking statements include the following:

- a sustained slowdown or significant downturn in our markets;
- a slowdown in infrastructure development;
- unpredictability in the adoption, implementation and enforcement of emission standards around the world;
- the actions of, and income from, joint ventures and other investees that we do not directly control;
- changes in the engine outsourcing practices of significant customers;
- a downturn in the North American truck industry or financial distress of a major truck customer;
- a major customer experiencing financial distress;
- any significant problems in our new engine platforms;
- supply shortages and supplier financial risk, particularly from any of our single-sourced suppliers;
- variability in material and commodity costs;
- product recalls;
- competitor pricing activity;
- increasing competition, including increased global competition among our customers in emerging markets;
- exposure to information technology security threats and sophisticated "cyber attacks;"
- political, economic and other risks from operations in numerous countries;
- changes in taxation;
- global legal and ethical compliance costs and risks;
- aligning our capacity and production with our demand;
- product liability claims;
- the development of new technologies;
- obtaining additional customers for our new light-duty diesel engine platform and avoiding any related write-down in our investments in such platform;
- increasingly stringent environmental laws and regulations;
- foreign currency exchange rate changes;
- the price and availability of energy;
- the performance of our pension plan assets;
- labor relations;
- changes in accounting standards;

- our sales mix of products;

## [Table of Contents](#)

- protection and validity of our patent and other intellectual property rights;
- technological implementation and cost/financial risks in our increasing use of large, multi-year contracts;
- the cyclical nature of some of our markets;
- the outcome of pending and future litigation and governmental proceedings;
- continued availability of financing, financial instruments and financial resources in the amounts, at the times and on the terms required to support our future business;
- the consummation and integration of the planned acquisitions of our partially-owned United States and Canadian distributors; and
- other risk factors described in Item IA under the caption "Risk Factors."

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

## PART I

### ITEM 1. Business

#### OVERVIEW

Cummins Inc. was founded in 1919 as a corporation in Columbus, Indiana, as one of the first diesel engine manufacturers. We are a global power leader that designs, manufactures, distributes and services diesel and natural gas engines and engine-related component products, including filtration, aftertreatment, turbochargers, fuel systems, controls systems, air handling systems and electric power generation systems. We sell our products to original equipment manufacturers (OEMs), distributors and other customers worldwide. We serve our customers through a network of over 600 company-owned and independent distributor locations and over 6,800 dealer locations in more than 190 countries and territories.

#### OPERATING SEGMENTS

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

#### Engine Segment

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

	Years ended December 31,		
	2013	2012	2011
Percent of consolidated net sales <sup>(1)</sup>	47 %	50 %	52 %
Percent of consolidated EBIT <sup>(1)</sup>	48 %	54 %	53 %

<sup>(1)</sup> Measured before intersegment eliminations

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

- Engines with a displacement range of 2.8 to 91 liters and horsepower ranging from 49 to 4,200;
- New parts and service, as well as remanufactured parts and engines, through our extensive distribution network and
- The newly developed light-duty diesel engine, which will be sold through the recreational vehicle, pick-up, bus and certain medium-duty truck markets.

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

- **Heavy-duty truck** - We manufacture diesel engines that range from 310 to 600 horsepower serving global heavy-duty truck customers worldwide.
- **Medium-duty truck and bus** - We manufacture medium-duty diesel engines ranging from 200 to 450 horsepower serving medium-duty and inter-city delivery truck customers worldwide, with key markets including North America, Latin America, Europe and Mexico. We also provide diesel or natural gas engines for school buses, transit buses and shuttle buses worldwide, with key markets including North America, Europe, Latin America and Asia.
- **Light-duty automotive and RV** - We manufacture 320 to 385 horsepower diesel engines for Chrysler Group, LLC's (Chrysler) heavy-duty chassis cab and pickup trucks and 200 to 600 horsepower diesel engines for Class A motor homes (RVs), primarily in North America.

- **Industrial** - We provide mid-range, heavy-duty and high-horsepower engines that range from 49 to 4,200 horsepower for a wide variety of equipment in the construction, agricultural, mining, rail, government, oil and gas, power generation and commercial and recreational marine applications throughout the world. Across these markets we have major customers in North America, Europe/Middle East/Africa (EMEA), China, Korea, Japan, Latin America, India, Russia, Southeast Asia, South Pacific and Mexico.

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

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

## Components Segment

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

	Years ended December 31,		
	2013	2012	2011
Percent of consolidated net sales <sup>(1)</sup>	21 %	19 %	18 %
Percent of consolidated EBIT <sup>(1)</sup>	24 %	18 %	18 %

<sup>(1)</sup> Measured before intersegment eliminations

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

Our Components segment is organized around the following businesses:

- **Emission solutions** - Our emission solutions business is a global leader in designing, manufacturing and integrating aftertreatment technology and solutions for the commercial on- and off-highway medium-duty, heavy-duty and high-horsepower engine markets. Our emission solutions business develops and produces various emission solutions, including custom engineering systems and integrated controls, oxidation catalysts, particulate filters, oxides of nitrogen (NOx) reduction systems such as selective catalytic reduction and NOx adsorbers and engineered components such as dosers and sensors. Our emission solutions business primarily serves markets in North America, Europe, Brazil, Russia, Australia and China and serves both OEM and engine first fit and retrofit customers.
- **Turbo technologies** - Our turbo technologies business designs, manufactures and markets turbochargers for light-duty, mid-range, heavy-duty and high-horsepower diesel markets with manufacturing facilities in five countries and sales and distribution worldwide. Our turbo technologies business provides critical air handling technologies for engines, including variable geometry turbochargers, to meet challenging performance requirements and worldwide emission standards. Our turbo technologies business primarily serves markets in North America, Europe, Asia and Brazil.

- **Filtration** - Our filtration business designs and manufactures filtration, coolant and chemical products. Our filtration business offers over 8,000 products including air filters, fuel filters, fuel water separators, lube filters, hydraulic filters, coolant, diesel exhaust fluid, fuel additives and other filtration systems to OEMs, dealers/distributors and end users. Our filtration business supports a wide customer base in a diverse range of markets including on-highway, off-highway, oil and gas, agriculture, construction, power generation, marine, industrial and light-duty trucks. We produce and sell globally recognized Fleetguard® branded products in over 160 countries including countries in North America, Europe, South America, Asia, Australia and Africa. Fleetguard products are available through thousands of distribution points worldwide.
- **Fuel systems** - Our fuel systems business designs and manufactures new and replacement fuel systems primarily for heavy-duty on-highway diesel engine applications and also remanufactures fuel systems.

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

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

On July 18, 2012, we acquired the doser technology business assets from Hilite Germany GmbH (Hilite) in a \$176 million cash transaction. The acquisition was accounted for as a business combination with the majority of the purchase price being allocated to goodwill and technology and customer related intangible assets. The results of the acquired entity for 2012 and 2013 were included in the Components operating segment.

During 2011, we sold certain assets and liabilities of our exhaust business, which manufactured exhaust products and select components for emission systems for a variety of applications not core to our other product offerings, and our light-duty filtration business, which manufactured light-duty automotive and industrial filtration solutions. Both of these businesses were historically included in our Components segment. See Note 2, "ACQUISITIONS AND DIVESTITURES," to our *Consolidated Financial Statements* for additional detail.

### Power Generation Segment

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

	Years ended December 31,		
	2013	2012	2011
Percent of consolidated net sales <sup>(1)</sup>	14%	15%	16%
Percent of consolidated EBIT <sup>(1)</sup>	10%	12%	14%

<sup>(1)</sup> Measured before intersegment eliminations

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

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



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

- **Power products** - Our power products business manufactures generators for commercial and consumer applications ranging from two kilowatts (kW) to one megawatt (MW) under the Cummins Power Generation and Cummins Onan brands.
- **Power systems** - Our power systems business manufactures and sells diesel fuel-based generator sets over one MW, paralleling systems and transfer switches for critical protection and distributed generation applications. We also offer integrated systems that consist of generator sets, power transfer and paralleling switchgear for applications such as data centers, health care facilities and waste water treatment plants.
- **Alternators** - Our alternator business (formally called generator technologies prior to the fourth quarter of 2013) designs, manufactures, sells and services A/C generator/alternator products internally as well as to other generator set assemblers. Our products are sold under the Stamford, AVK and Markon brands and range in output from 0.6 kilovolt-amperes (kVA) to 30,000 kVA.
- **Power Solutions** - Our power solutions business provides natural gas fuel-based turnkey solutions for distributed generation and energy management applications in the range of 300-2000 kW products. The business also serves a global rental account for diesel and gas generator sets.

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

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

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

### Distribution Segment

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

	Years ended December 31,		
	2013	2012	2011
Percent of consolidated net sales <sup>(1)</sup>	18%	16%	14%
Percent of consolidated EBIT <sup>(1)</sup>	18%	16%	15%

<sup>(1)</sup> Measured before intersegment eliminations

Our Distribution segment consists of 27 company-owned and 15 joint venture distributors that service and distribute the full range of our products and services to end-users at over 400 locations in approximately 80 distribution territories. Our company-owned distributors are located in key markets, including North America, Australia, Europe, the Middle East, India, China, Africa, Russia, Japan, Brazil, Singapore and Central America, while our joint venture distributors are located in key markets, including North America, South America, Africa, China, Thailand, Singapore and Vietnam.

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

- Parts and filtration,
- Power generation,
- Engines and
- Service.

The Distribution segment is organized into five primary geographic regions:

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

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

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

In addition to managing our involvement with our wholly-owned and partially-owned distributors, our Distribution segment is responsible for managing the performance and capabilities of our independent distributors. Our Distribution segment serves a highly diverse customer base with approximately 44 percent of its 2013 sales being generated from new engines and power generation equipment, compared to 45 percent in 2012, with its remaining sales generated by parts and filtration and service revenue.

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

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

On September 17, 2013, we announced our intention to acquire the equity that we do not already own in most of our partially-owned United States and Canadian distributors over the next three to five years.

In December 2013, we acquired the remaining 35 percent interest in Cummins Western Canada LP (Western Canada) from the former principal for consideration of approximately \$34 million. This entity was previously consolidated and, as a result, the acquisition was not treated as a business combination but as an equity transaction. This acquisition was made in accordance with our planned strategy.

In May 2013, we acquired the remaining 67 percent interest in Cummins Rocky Mountain LLC (Rocky Mountain) from the former principal for consideration of approximately \$62 million in cash and an additional \$74 million in cash paid to creditors to eliminate all debt related to the entity. The acquisition was accounted for as a business combination, with the results of the acquired entity included in the Distribution operating segment in the second quarter of 2013.

In January 2013, we acquired an additional 29.99 percent interest in Cummins Northwest LLC (Northwest) from the former principal for consideration of approximately \$18 million. We formed a new partnership with a new distributor principal. We owned 79.99 percent of Northwest and the new distributor principal owned 20.01 percent. The acquisition was accounted for as a business combination, with the results of the acquired entity included in the Distribution operating segment in the first quarter of 2013. In July 2013, we acquired the remaining 20.01 percent from the former distributor principal for an additional \$4 million.

In July 2012, we acquired an additional 45 percent interest in Cummins Central Power from the former principal for consideration of approximately \$20 million. The acquisition was accounted for as a business combination, with the results of the acquired entity included in the Distribution operating segment in the third quarter of 2012.

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

**JOINT VENTURES, ALLIANCES AND NON-WHOLLY-OWNED SUBSIDIARIES**

We have entered into a number of joint venture agreements and alliances with business partners around the world. Our joint ventures are either distribution or manufacturing entities. We also own controlling interests in non-wholly-owned manufacturing and distribution subsidiaries. Five entities, in which we own more than a 50 percent equity interest, are consolidated in our Distribution segment results as well as several manufacturing joint ventures in the other operating segments.

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

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

Our equity income from these investees was as follows:

In millions	Years ended December 31,					
	2013		2012		2011	
<b>Distribution Entities</b>						
North American distributors	\$ 129	40 %	\$ 147	42 %	\$ 134	36 %
Komatsu Cummins Chile, Ltda.	25	8 %	26	8 %	22	6 %
All other distributors	1	— %	4	1 %	4	1 %
<b>Manufacturing Entities</b>						
Dongfeng Cummins Engine Company, Ltd.	63	19 %	52	15 %	80	21 %
Chongqing Cummins Engine Company, Ltd.	58	18 %	61	18 %	68	18 %
Beijing Foton Cummins Engine Co., Ltd. (Heavy-duty)	(21)	(6) %	(13)	(4) %	(6)	(2) %
Beijing Foton Cummins Engine Co., Ltd. (Light-duty)	17	5 %	5	1 %	(7)	(2) %
Shanghai Fleetguard Filter Co., Ltd.	13	4 %	13	4 %	15	4 %
Tata Cummins, Ltd.	5	2 %	11	3 %	14	4 %
Cummins Westport, Inc.	4	1 %	14	4 %	14	4 %
All other manufacturers	31	9 %	27	8 %	37	10 %
Cummins share of net income <sup>(1)</sup>	<u>\$ 325</u>	<u>100 %</u>	<u>\$ 347</u>	<u>100 %</u>	<u>\$ 375</u>	<u>100 %</u>

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

**Distribution Entities**

- **North American Distributors** - As of December 31, 2013, our distribution channel in North America included nine unconsolidated partially-owned distributors. Our equity interests in these nonconsolidated entities ranged from 37 percent to 50 percent. We also had more than a 50 percent ownership interest in three partially owned distributors which we consolidate. While each distributor is a separate legal entity, the business of each is substantially the same as that of our wholly-owned distributors based in other parts of the world. All of our distributors, irrespective of their legal structure or ownership, offer the full range of our products and services to customers and end-users in their respective markets.
- **Komatsu Cummins Chile, Ltda.** - Komatsu Cummins Chile, Ltda. is a joint venture with Komatsu America Corporation. The joint venture is a distributor that offers the full range of our products and services to customers and end-users in the Chilean and Peruvian markets.

Our distribution agreements with independent and partially-owned distributors generally have a renewable three-year term and are restricted to specified territories. Our distributors develop and maintain a network of dealers with which we have no direct relationship. Our distributors are permitted to sell other, noncompetitive products only with our consent. We license all of our distributors to use our name and logo in connection with the sale and service of our products, with no right to assign or sublicense the trademarks, except to authorized dealers, without our consent. Products are sold to the distributors at standard domestic or international distributor net prices, as applicable. Net prices are wholesale prices we establish to permit our distributors an adequate margin on their sales. Subject to local laws, we can generally refuse to renew these agreements upon expiration or terminate them upon written notice for inadequate sales, change in principal ownership and certain other reasons. Distributors also have the right to terminate the agreements upon 60-day notice without cause, or 30-day notice for cause. Upon termination or failure to renew, we are required to purchase the distributor's current inventory, signage and special tools, and may, at our option purchase other assets of the distributor, but are under no obligation to do so.

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

## Manufacturing Entities

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

- **Chongqing Cummins Engine Company, Ltd.** -Chongqing Cummins Engine Company, Ltd. (CCEC) is a joint venture in China with Chongqing Machinery and Electric Co. Ltd. This joint venture manufactures several models of our heavy-duty and high-horsepower diesel engines, primarily serving the industrial and stationary power markets in China.
- **Dongfeng Cummins Engine Company, Ltd.** -Dongfeng Cummins Engine Company, Ltd. (DCEC) is a joint venture in China with Dongfeng Automotive Co. Ltd., a subsidiary of Dongfeng Motor Corporation (Dongfeng), one of the largest medium-duty and heavy-duty truck manufacturers in China. DCEC produces Cummins 4- to 13-liter mechanical engines, full-electric diesel engines, with a power range from 125 to 545 horsepower, and natural gas engines.
- **Beijing Foton Cummins Engine Co., Ltd.** -Beijing Foton Cummins Engine Co., Ltd. is a joint venture in China with Beiqi Foton Motor Co., Ltd., a commercial vehicle manufacturer, which consists of two distinct lines of business, a light-duty business and a heavy-duty business. The light-duty business produces ISF 2.8 liter and ISF 3.8 liter families of our high performance light-duty diesel engines in Beijing. These engines are used in light-duty commercial trucks, pickup trucks, buses, multipurpose and sport utility vehicles with main markets in China, Brazil and Russia. Certain types of marine, small construction equipment and industrial applications are also served by these engine families. The heavy-duty business has been in the development stage for the past several years but is scheduled to start the production of ISG 10.5 liter and ISG 11.8 liter families of our high performance heavy-duty diesel engines in the second quarter of 2014 in Beijing. These engines will be used in heavy-duty commercial trucks in China and subsequently in world wide markets. Certain types of construction equipment and industrial applications will also be served by these engine families in the future.
- **Shanghai Fleetguard Filter Co., Ltd.** -Shanghai Fleetguard Filter Co., Ltd. is a joint venture in China with Dongfeng that manufactures filtration systems.
- **Cummins Westport, Inc.** -Cummins Westport, Inc. is a joint venture in Canada with Westport Innovations Inc. to market and sell automotive spark-ignited natural gas engines and to participate in joint technology projects on low-emission technologies.
- **Tata Cummins, Ltd.** -Tata Cummins, Ltd. is a joint venture in India with Tata Motors Ltd., the largest automotive company in India and a member of the Tata group of companies. This joint venture manufactures engines in India for use in trucks manufactured by Tata Motors, as well as for various industrial and power generation applications.

- **Komatsu manufacturing alliances** - Komatsu manufacturing alliances consists of two manufacturing joint ventures and one design joint venture including Komatsu Cummins Engine Company (KCEC) in Japan and Cummins Komatsu Engine Company (CKEC) in the United States (U.S.) with Komatsu Ltd. These joint ventures manufacture Cummins-designed medium-duty engines in Japan and Komatsu-designed high-horsepower engines in the U.S. The industrial engine design joint venture is located in Japan.
- **Cummins-Scania XPI Manufacturing, LLC** - Cummins-Scania XPI Manufacturing, LLC is a joint venture in the United States with Scania Holding, Inc. This joint venture manufactures several models of advanced fuel systems for heavy-duty and midrange diesel engines.
- **Cummins Olayan Energy Ltd.** - Cummins Olayan Energy Ltd. is a joint venture in the Kingdom of Saudi Arabia with General Contracting Company to operate certain rental power generation equipment, which is primarily utilized within the Kingdom of Saudi Arabia.
- **Guangxi Cummins Industrial Power Co., Ltd.** - Guangxi Cummins Industrial Power Co., Ltd. is a joint venture in China with Guangxi LiuGong Machinery Co. This joint venture manufactures 6.7 liter and 9.3 liter diesel engines for use in various construction equipment.

#### **Non-Wholly-Owned Subsidiary**

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

#### **SUPPLY**

The performance of the end-to-end supply chain, extending through to our suppliers, is foundational to our ability to meet customers' expectations and support long-term growth. We are committed to having a robust strategy for how we select and manage our suppliers to enable a market focused supply chain. This requires us to continuously evaluate and upgrade our supply base, as necessary, to ensure we are meeting the needs of our customers.

We have a strategic sourcing policy that guides decisions on what we make internally, what we purchase externally and when we establish supplier partnerships to provide the lowest total cost and highest supply chain performance. Today we machine and assemble strategic components used in our engines and power generation units, including blocks, heads, turbochargers, connecting rods, camshafts, crankshafts, filters, alternators and fuel systems. We source externally purchased material and manufactured components from global leading suppliers both domestically and internationally. Many key suppliers are managed through long-term supply agreements that assure capacity, delivery, quality and cost requirements are met over an extended period. Approximately 60 to 70 percent of the direct material in our product designs are single sourced to external suppliers. Although we elected to source a relatively high proportion of our total raw materials and components from single suppliers, we have an established annual sourcing strategy process and risk assessment procedures to evaluate risk. These processes are leading us to increase our use of dual and parallel sourcing to both minimize risk and increase supply chain responsiveness.

Other important elements of our sourcing strategy include:

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

#### **PATENTS AND TRADEMARKS**

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

## **SEASONALITY**

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

## **LARGEST CUSTOMERS**

We have thousands of customers around the world and have developed long-standing business relationships with many of them. PACCAR is our largest customer, accounting for approximately 12 percent of our consolidated net sales in 2013, compared to approximately 13 percent in 2012 and 12 percent in 2011. We have long-term supply agreements with PACCAR for our heavy-duty ISX 15 liter and ISX 11.9 liter engines and our ISL 9 liter mid-range engine. While a significant number of our sales to PACCAR are under long-term supply agreements, these agreements provide for particular engine requirements for specific vehicle models and not a specific volume of engines. PACCAR is our only customer accounting for more than 10 percent of our net sales in 2013. The loss of this customer or a significant decline in the production level of PACCAR vehicles that use our engines would have an adverse effect on our results of operations and financial condition. We have been an engine supplier to PACCAR for over 69 years. A summary of principal customers for each operating segment is included in our segment discussion.

In addition to our agreement with PACCAR, we have long-term heavy-duty engine supply agreements with Navistar and Volvo Trucks North America and long-term mid-range supply agreements with Daimler Trucks North America, Navistar, MAN and Ford. We also have an agreement with Chrysler to supply engines for its Ram trucks. In our off-highway markets, we have various engine and component supply agreements ranging across our midrange and high-horsepower businesses with Komatsu Ltd., as well as various joint ventures and other license agreements in our Engine, Component and Distribution segments. Collectively, our net sales to these eight customers, including PACCAR, was approximately 36 percent of our consolidated net sales in 2013, compared to approximately 35 percent in 2012 and 33 percent in 2011. Excluding PACCAR, net sales to any single customer were less than 7 percent of our consolidated net sales in 2013, compared to less than 8 percent in 2012 and less than 6 percent in 2011. These agreements contain standard purchase and sale agreement terms covering engine and engine parts pricing, quality and delivery commitments, as well as engineering product support obligations. The basic nature of our agreements with OEM customers is that they are long-term price and operations agreements that help assure the availability of our products to each customer through the duration of the respective agreements. Agreements with most OEMs contain bilateral termination provisions giving either party the right to terminate in the event of a material breach, change of control or insolvency or bankruptcy of the other party.

## **BACKLOG**

Our 2013 lead times for the majority of our businesses improved from their 2012 levels. While we have supply agreements with some truck and off-highway equipment OEMs, most of our business is transacted through open purchase orders. These open orders are historically subject to month-to-month releases and are subject to cancellation on reasonable notice without cancellation charges and therefore are not considered firm. As of December 31, 2013, we did not have any significant backlogs.

## **RESEARCH AND DEVELOPMENT EXPENSE**

In 2013, we decreased our research, development and engineering expenses slightly as we continued to invest in future critical technologies and products. We will continue to make investments to improve our current technologies, continue to meet the future emission requirements around the world and improve fuel economy.

Our research and development program is focused on product improvements, innovations and cost reductions for our customers. Research and development expenditures include salaries, contractor fees, building costs, utilities, administrative expenses and allocation of corporate costs and are expensed, net of contract reimbursements, when incurred. From time to time, we enter into agreements with customers to fund a portion of the research and development costs of a particular project. We generally account for these reimbursements as an offset to the related research and development expenditure. Research and development expenses, net of contract reimbursements, were \$700 million in 2013, \$721 million in 2012 and \$621 million in 2011. Contract reimbursements were \$76 million in 2013, \$86 million in 2012 and \$75 million in 2011.

For 2011, approximately \$1 million, or less than 1 percent, of our research and development expenditures were directly related to compliance with 2010 Environmental Protection Agency (EPA) emission standards. For 2013, 2012 and 2011, approximately \$15 million, \$101 million and \$104 million, or 2 percent, 14 percent and 17 percent, respectively, of our research and development expenditures were directly related to compliance with 2013 EPA emission standards. For 2013, approximately \$32 million, or 5 percent, of our research and development expenditures was directly related to compliance with 2017 EPA emission standards.

## **ENVIRONMENTAL SUSTAINABILITY**

Our 10 Environmental Sustainability principles attempt to positively impact the environment through the products that we make, how we use our facilities and manage our supply chain and how we improve the communities where we live and work. Using these guiding principles and with the input of key stakeholder areas, our Corporate Action Committee for Environmental Sustainability in 2013 developed the Company's first Global Environmental Sustainability Plan to more fully integrate environmental stewardship across all of our businesses and functions. We continue to invest significantly in our products to further reduce emissions and increase efficiency. We attempt to work collaboratively with customers to improve their fuel economy, reduce their carbon footprints and conserve other resources. Over the past five years, we believe that we have reduced company-wide water usage intensity by approximately 47 percent, U.S.-wide process-derived hazardous waste generation by approximately 56 percent and company-wide landfill waste by approximately 21 percent, all normalized to total work hours. As part of the U.S. Department of Energy's Better Buildings, Better Plants program, we have pledged to achieve a 25 percent energy intensity (energy use adjusted for sales) reduction by 2015; at the end of 2012, we had achieved a 34 percent reduction. We also have articulated our positions on key public policy issues and on a wide range of environmental issues. We are actively engaged with regulatory, industry and other stakeholder groups around the world as greenhouse gas and fuel efficiency standards become more prevalent globally. For the ninth consecutive year, we were named to the Dow Jones World Sustainability Index, which recognizes the top 10 percent of the world's largest 2,500 companies in economic, environmental and social leadership. Our Sustainability Report for 2012/2013 and prior reports as well as an addendum of more detailed environmental data is available on our website at [www.cummins.com](http://www.cummins.com), although such report and addendum are not incorporated into this Form 10-K.

## **ENVIRONMENTAL COMPLIANCE**

### **Product Environmental Compliance**

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

### **EU and EPA Engine Certifications**

The current on-highway emission standards came into effect in the EU on January 1, 2013 (Euro VI) and on January 1, 2010 for the EPA. To meet the more stringent heavy-duty on-highway emission standards, we used an evolution of our proven selective catalytic reduction (SCR) and exhaust gas recirculation (EGR) technology solutions and refined them for the EU and EPA certified engines to maintain power and torque with substantial fuel economy improvement and maintenance intervals comparable with our previous compliant engines. We offer a complete lineup of on-highway engines to meet the near-zero emission standards. Mid-range and heavy-duty engines for EU and EPA require NOx aftertreatment. NOx reduction is achieved by an integrated technology solution comprised of the XPI High Pressure Common Rail fuel system, SCR technology, next-generation cooled EGR, advanced electronic controls, proven air handling and the Cummins Diesel Particulate Filter (DPF). The EU, EPA, and CARB have certified that our engines meet the current emission requirements. Emission standards in international markets, including Japan, Mexico, Australia, Brazil, Russia, India and China are becoming more stringent. We believe that our experience in meeting the EU and EPA emission standards leaves us well positioned to take advantage of opportunities in these markets as the need for emission control capability grows.

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

#### **Other Environmental Statutes and Regulations**

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

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

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

#### **EMPLOYEES**

As of December 31, 2013, we employed approximately 47,900 persons worldwide. Approximately 15,650 of our employees worldwide are represented by various unions under collective bargaining agreements that expire between 2014 and 2016.

#### **AVAILABLE INFORMATION**

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

Our internet site is [www.cummins.com](http://www.cummins.com). You can access our Investors and Media webpage through our internet site, by clicking on the heading "Investors and Media" followed by the "Investor Relations" link. We make available, free of charge, on or through our Investors and Media webpage, our proxy statements, annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports filed or furnished pursuant to the Securities Exchange Act of 1934 or the Securities Act of 1933, as amended, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC.

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



**EXECUTIVE OFFICERS OF THE REGISTRANT**

Following are the names and ages of our executive officers, their positions with us as of January 31, 2014, and summaries of their backgrounds and business experience:

<b>Name and Age</b>	<b>Present Cummins Inc. position and year appointed to position</b>	<b>Principal position during the past five years other than Cummins Inc. position currently held</b>
N. Thomas Linebarger (51)	Chairman of the Board of Directors and Chief Executive Officer (2012)	President and Chief Operating Officer (2008-2011)
Sharon R. Barner (56)	Vice President—General Counsel (2012)	Partner—Law firm of Foley & Lardner (2011-2012) Deputy Under Secretary of Commerce—Intellectual Property and Deputy Director of the United States Patent and Trademark Office (2009-2011) Partner—Law firm of Foley & Lardner (1996-2009)
Pamela L. Carter (64)	Vice President and President—Distribution Business (2007)	
Steven M. Chapman (59)	Group Vice President—China and Russia (2009)	Vice President—Emerging Markets and Businesses (2005-2009)
Jill E. Cook (50)	Vice President—Human Resources (2003)	
Richard J. Freeland (56)	Vice President and President—Engine Business (2010)	Vice President and President—Components Group (2008-2010)
Richard E. Harris (61)	Vice President—Chief Investment Officer (2008)	
Mark A. Levett (64)	Vice President—Corporate Responsibility and Chief Executive Officer - Cummins Foundation (2013)	General Manager and Vice President—High Horsepower (1999-2013)
Marsha L. Hunt (50)	Vice President—Corporate Controller (2003)	
Marya M. Rose (51)	Vice President—Chief Administrative Officer (2011)	Vice President—General Counsel and Corporate Secretary (2001-2011)
Livingston L. Satterthwaite (53)	Vice President and President—Power Generation (2008)	
Anant J. Talaulicar (52)	Vice President and President—Components Group (2010), Vice President and Managing Director—India ABO (2004)	Chairman and Managing Director—Cummins India Ltd. (2003-present)
John C. Wall (62)	Vice President—Chief Technical Officer (2000)	
Patrick J. Ward (50)	Vice President—Chief Financial Officer (2008)	
Lisa M. Yoder (50)	Vice President—Global Supply Chain & Manufacturing (2011)	Vice President—Corporate Supply Chain (2010-2011), Executive Director—Supply Chain & Operations-Power Generation (2007-2010)

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

**ITEM 1A. Risk Factors**

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

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

Global economic uncertainty continued throughout 2013 as we experienced declining or relatively flat demand in many global markets. If the global economy or some of our significant markets encounter a sustained slowdown; depending upon the length, duration and severity of such a slowdown, our results of operations, financial condition and cash flow would almost certainly be materially adversely affected. Specifically, our revenues would likely decrease, we may be forced to consider further restructuring actions, we may need to increase our allowance for doubtful accounts, our days sales outstanding may increase and we could experience impairments to assets of certain of our businesses.

***A slowdown in infrastructure development could adversely affect our business.***

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

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

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

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

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

Our net income includes significant equity, royalty and interest income from investees that we do not directly control. For 2013, we recognized \$361 million of equity, royalty and interest income from investees, compared to \$384 million in 2012. The majority of our equity, royalty and interest income from investees is from our unconsolidated North American distributors and from two of our joint ventures in China, Dongfeng Cummins Engine Company, Ltd. (DCEC) and Chongqing Cummins Engine Company, Ltd. (CCEC). Our equity ownership interests in our unconsolidated North American distributors ranged from 50 percent to 50 percent at December 31, 2013. We have percent equity ownership interests in DCEC and CCEC. As a result, although a significant percentage of our net income is derived from these unconsolidated entities, we do not unilaterally control their management or their operations, which puts a substantial portion of our net income at risk from the actions or inactions of these entities. A significant reduction in the level of contribution by these entities to our net income would likely have a material adverse effect on our results of operations.

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

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

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

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

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

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

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

During 2013, we single sourced approximately 60 to 70 percent of the total types of parts in our product designs. Any delay in our suppliers' deliveries may adversely affect our operations at multiple manufacturing locations, forcing us to seek alternative supply sources to avoid serious disruptions. Delays may be caused by factors affecting our suppliers, including capacity constraints, labor disputes, economic downturns, availability of credit, the impaired financial condition of a particular supplier, suppliers' allocations to other purchasers, weather emergencies, natural disasters or acts of war or terrorism. Any extended delay in receiving critical supplies could impair our ability to deliver products to our customers and our results of operations.

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

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

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

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

***Failure to successfully integrate the planned acquisitions of the equity we do not already own of our partially-owned United States and Canadian distributors could have an adverse impact on our realization of expected benefits to our financial condition and results of operations.***

The completion of our plan to acquire all of the equity we do not already own of our partially-owned United States and Canadian distributors (each, an "Acquisition," and collectively, the "Acquisitions"), is subject to various risks, including, among other things, our ability to realize the full extent of the incremental revenue, earnings, cash flow, cost savings and other benefits that we expect to realize as a result of the completion of the Acquisitions within the anticipated time frame, or at all; the costs that are expected to be incurred in connection with evaluating, negotiating, consummating and integrating the Acquisitions; the ability of management to focus adequate time and attention on evaluating, negotiating, consummating and integrating the Acquisitions; and diversion of management's attention from base strategies and objectives, both during and after the acquisition process. Further, as with all merger and acquisition activity, there can be no assurance that we will be able to negotiate, consummate and integrate the Acquisitions in accordance with our plans. Those persons holding the third-party ownership of our partially-owned United States and Canadian distributors may not agree to our acquisition proposals, including the terms and conditions thereof, and may claim that our proposals to exercise certain contractual rights that we have with respect to acquiring such distributors may violate applicable state franchise and distributor laws, which may prohibit, delay or otherwise adversely affect the consummation of such Acquisitions on terms and conditions that are less favorable to us than we currently anticipate, or not at all.

***After completion of the Acquisitions, we may fail to realize the expected enhanced revenue, earnings, cash flow, cost savings and other benefits.***

The financial success of the Acquisitions will depend, in substantial part, on our ability to successfully combine our business with the businesses of our partially-owned United States and Canadian distributors, transition operations and realize the expected enhanced revenue, earnings, cash flow, cost savings and other benefits from such Acquisitions. While we currently believe that these enhanced revenue, earnings, cash flow, cost savings and other benefits estimates are achievable, it is possible that we will be unable to achieve these objectives within the anticipated time frame, or at all. Our enhanced revenue, earnings, cash flow, cost savings and other benefits estimates also depend on our ability to execute and integrate the Acquisitions in a manner that permits those benefits to be realized. If these estimates turn out to be incorrect or we are not able to execute our integration strategy successfully, the anticipated enhanced revenue, earnings, cash flow, cost savings and other benefits, resulting from the Acquisitions may not be realized fully, or at all, or may take longer to realize than expected.

Specifically, issues that must be addressed in integration in order to realize the anticipated benefits and costs savings of the Acquisitions include, among other things:

- maintaining and improving management and employee engagement, morale, motivation and productivity;
- recruiting and retaining executives and key employees;
- retaining and strengthening relationships with existing customers and attracting new customers;
- conforming standards, controls, procedures and policies, business cultures and compensation structures among the companies;
- consolidating and streamlining corporate and administrative infrastructures;
- consolidating sales, customer service and marketing operations;
- identifying and eliminating redundant and underperforming operations and assets;
- integrating the distribution, sales, customer service and administrative support activities among the companies;
- integrating information technology systems, including those systems managing data security for sensitive employee, customer and vendor information, and diverse network applications across the companies;

## [Table of Contents](#)

- managing the broadened competitive landscape, including responding to the actions taken by competitors in response to the Acquisitions;
- coordinating geographically dispersed organizations;
- managing the additional business risks of businesses that we have not previously directly managed; and
- managing tax costs or inefficiencies associated with integrating our operations following completion of the Acquisitions.

Delays encountered in the process of integrating the Acquisitions could negatively impact our revenues, expenses, operating results, cash flow and financial condition after completion of the Acquisitions, including through the loss of current customers or suppliers. Although significant benefits, such as enhanced revenue, earnings, cash flow and cost savings, are expected to result from the Acquisitions, there can be no assurance that we will realize any of these anticipated benefits after completion of any or all of the Acquisitions.

Additionally, significant costs are expected to be incurred in connection with the integration of the Acquisitions. We continue to assess the magnitude of these costs and additional unanticipated costs may be incurred, including costs associated with assuming our partially-owned United States and Canadian distributors' exposure to outstanding and anticipated legal claims and other liabilities. Although we believe that the elimination of duplicative costs, as well as the realization of other synergies and efficiencies related to the integration of the Acquisitions, will offset incremental integration-related costs over time, no assurances can be given that this net benefit will be achieved in the near term, or at all. In addition, the process of integrating the operations of our partially-owned United States and Canadian distributors may distract management and employees from delivering against base strategies and objectives, which could negatively impact other segments of our business following the completion of the Acquisitions.

Furthermore, the Acquisitions and the related integration efforts, could result in the departure of key managers and employees, and we may fail to identify managerial resources to fill both executive-level and lower-level managerial positions and replace key employees, including those who oversee customer relationships, any of which could have a negative impact on our business, and, prior to the completion of the Acquisitions, the businesses of our partially-owned United States and Canadian distributors.

***The completion of the Acquisitions may be subject to the receipt of certain required clearances or approvals from governmental entities that could prevent or delay their completion or impose conditions that could have an adverse effect on us.***

Completion of each of the Acquisitions may be conditioned upon the receipt of certain governmental clearances or approvals, including, but not limited to, the expiration or termination of any applicable waiting periods under U.S. competition and trade laws with respect to such Acquisitions as well as applicable state regulations and restrictions. There can be no assurance that these clearances and approvals will be obtained, and, additionally, government authorities from which these clearances and approvals are required may impose conditions on the completion of any, or all, of the Acquisitions or require changes to their respective terms. If, in order to obtain any clearances or approvals required to complete any of the Acquisitions, we become subject to any material conditions after completion of any of such Acquisitions, our business and results of operations after completion of any of such Acquisitions may be adversely affected.

***We face significant competition in the markets we serve.***

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

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

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

***We are exposed to, and may be adversely affected by, information technology security threats and sophisticated "cyber attacks."***

We rely on our information technology systems and networks in connection with various of our business activities. Some of these networks and systems are managed by third party service providers and are not under our direct control. Our operations routinely involve receiving, storing, processing and transmitting sensitive information pertaining to our business, customers, dealers, suppliers, employees and other sensitive matters. Information technology security threats, including security breaches, computer malware and other "cyber attacks" are increasing in both frequency and sophistication. These threats could create financial liability, subject us to legal or regulatory sanctions or damage our reputation with customers, dealers, suppliers and other stakeholders. We continuously seek to maintain a robust program of information security and controls, but the impact of a material information technology event could have a material adverse effect on our competitive position, reputation, results of operations, financial condition and cash flow.

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

Approximately 52 percent of our net sales for 2013 and 53 percent in 2012 were attributable to customers outside the U.S. Accordingly, our business is subject to the political, economic and other risks that are inherent in operating in numerous countries. These risks include:

- the difficulty of enforcing agreements and collecting receivables through foreign legal systems;
- trade protection measures and import or export licensing requirements;
- the imposition of taxes on foreign income and tax rates in certain foreign countries that exceed those in the U.S.;
- the imposition of tariffs, exchange controls or other restrictions;
- difficulty in staffing and managing widespread operations and the application of foreign labor regulations;
- required compliance with a variety of foreign laws and regulations;
- and
- changes in general economic and political conditions in countries where we operate, particularly in emerging markets.

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

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

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

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

Due to the international scope of our operations, we are subject to a complex system of commercial and trade regulations around the world. Recent years have seen an increase in the development and enforcement of laws regarding trade compliance and anti-corruption such as the U.S. Foreign Corrupt Practices Act and similar laws from other countries. Our numerous foreign subsidiaries, affiliates and joint venture partners are governed by laws, rules and business practices that differ from those of the U.S. The activities of these entities may not comply with U.S. laws or business practices or our Code of Business Conduct. Violations of these laws may result in severe criminal or civil sanctions, could disrupt our business, and result in an adverse effect on our reputation, business and results of operations or financial condition. We cannot predict the nature, scope or effect of future regulatory requirements to which our operations might be subject or the manner in which existing laws might be administered or interpreted.

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

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

***Our business is exposed to risks of product liability claims.***

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

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

We began development of a new North American light-duty diesel engine platform in July 2006 to be used in a variety of on- and off-highway applications. Since that time, and as of December 31, 2013, we have capitalized investments of approximately \$242 million. Market uncertainty due to the global recession resulted in some customers delaying or cancelling their vehicle programs, while others remained active. In August 2013, we reached an agreement to supply Nissan Motor Co. Ltd. with our light-duty diesel engine beginning in 2015, however, if customer expectations or volume projections deteriorate from our current expected levels and we do not identify new customers, we may need to recognize an impairment charge and write the assets down to net realizable value.

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

Our plants and operations are subject to increasingly stringent environmental laws and regulations in all of the countries in which we operate, including laws and regulations governing air emission, discharges to water and the generation, handling, storage, transportation, treatment and disposal of waste materials. While we believe that we are in compliance in all material respects with these environmental laws and regulations, there can be no assurance that we will not be adversely impacted by costs, liabilities or claims with respect to existing or subsequently acquired operations, under either present laws and regulations or those that may be adopted or imposed in the future. We are also subject to laws requiring the cleanup of contaminated property. If a release of hazardous substances occurs at or from any of our current or former properties or at a landfill or another location where we have disposed of hazardous materials, we may be held liable for the contamination and the amount of such liability could be material.

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

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

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

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

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

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

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

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

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

As of December 31, 2013, we employed approximately 47,900 persons worldwide. Approximately 15,650 of our employees worldwide are represented by various unions under collective bargaining agreements that expire between 2014 and 2016. While we have no reason to believe that we will be materially impacted by work stoppages or other labor matters, there can be no assurance that future issues with our labor unions will be resolved favorably or that we will not encounter future strikes, work stoppages, or other types of conflicts with labor unions or our employees. Any of these consequences may have an adverse effect on us or may limit our flexibility in dealing with our workforce. In addition, many of our customers and suppliers have unionized work forces. Work stoppages or slow-downs experienced by our customers or suppliers could result in slow-downs or closures that would have a material adverse effect on our results of operations, financial condition and cash flow.



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

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

**ITEM 1B. Unresolved Staff Comments**

None.

**ITEM 2. Properties**

**Manufacturing Facilities**

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

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

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

**Distribution Facilities**

The principal distribution facilities used by our Distribution and Engine segments are located in the following locations:

Segment	U.S. Facilities	Facilities Outside the U.S.
<b>Distribution</b>	<b>Alaska:</b> Anchorage <b>Colorado:</b> Commerce City, Henderson <b>Kansas:</b> Wichita <b>Massachusetts:</b> Dedham <b>Missouri:</b> Kansas City <b>Nebraska:</b> Omaha <b>New Mexico:</b> Farmington <b>New York:</b> Bronx <b>Oregon:</b> Portland <b>Pennsylvania:</b> Bristol, Harrisburg <b>Utah:</b> Salt Lake City <b>Washington:</b> Renton, Spokane	<b>Australia:</b> Scoresby <b>Germany:</b> Gross Gerau <b>India:</b> Pune <b>Japan:</b> Tokyo <b>Korea:</b> Chonan <b>Russia:</b> Moscow <b>Singapore:</b> Singapore SG <b>South Africa:</b> Johannesburg <b>U.K.:</b> Wellingborough <b>United Arab Emirates:</b> Dubai
<b>Engine</b>	<b>Tennessee:</b> Memphis	<b>Belgium:</b> Rumst <b>Singapore:</b> Singapore

**Headquarters and Other Offices**

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

U.S. Facilities	Facilities Outside the U.S.
<b>Indiana:</b> Columbus, Indianapolis <b>Tennessee:</b> Nashville <b>Washington DC</b>	<b>China:</b> Beijing, Shanghai, Wuhan <b>India:</b> Pune <b>U.K.:</b> Staines, Stockton

**ITEM 3. Legal Proceedings**

We are subject to numerous lawsuits and claims arising out of the ordinary course of our business, including actions related to product liability; personal injury; the use and performance of our products; warranty matters; patent, trademark or other intellectual property infringement; contractual liability; the conduct of our business; tax reporting in foreign jurisdictions; distributor termination; workplace safety; and environmental matters. We also have been identified as a potentially responsible party at multiple waste disposal sites under U.S. federal and related state environmental statutes and regulations and may have joint and several liability for any investigation and remediation costs incurred with respect to such sites. We have denied liability with respect to many of these lawsuits, claims and proceedings and are vigorously defending such lawsuits, claims and proceedings. We carry various forms of commercial, property and casualty, product liability and other forms of insurance; however, such insurance may not be applicable or adequate to cover the costs associated with a judgment against us with respect to these lawsuits, claims and proceedings. We do not believe that these lawsuits are material individually or in the aggregate. While we believe we have also established adequate accruals for our expected future liability with respect to pending lawsuits, claims and proceedings, where the nature and extent of any such liability can be reasonably estimated based upon then presently available information, there can be no assurance that the final resolution of any existing or future lawsuits, claims or proceedings will not have a material adverse effect on our business, results of operations, financial condition or cash flows.

We conduct significant business operations in Brazil that are subject to the Brazilian federal, state and local labor, social security, tax and customs laws. While we believe we comply with such laws, they are complex, subject to varying interpretations and we are often engaged in litigation regarding the application of these laws to particular circumstances.

**ITEM 4. Mine Safety Disclosures**

Not Applicable.

**PART II**

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

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

(b) Use of proceeds—not applicable.

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

Period	Issuer Purchases of Equity Securities			
	(a) Total Number of Shares Purchased <sup>(1)</sup>	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs <sup>(2)</sup>
September 30 - November 3, 2013	1,983	\$ 130.06	—	75,555
November 4 - December 1, 2013	718,347	129.21	715,963	72,140
December 2 - December 31, 2013	7,776	135.07	—	62,796
Total	728,106	\$ 129.28	715,963	

<sup>(1)</sup> Shares purchased represent shares under our Key Employee Stock Investment Plan established in 1969 (there is no maximum repurchase limitation in this plan) and the 2012 Board of Directors authorized \$1 billion share repurchase program.

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

In February 2011, the Board of Directors authorized the acquisition of an additional \$1 billion of our common stock beginning in 2011. In 2013, we completed this authorization, purchasing the remaining \$226 million or 2.0 million shares. We acquired \$256 million or 2.6 million shares and \$518 million or 5.3 million shares in 2012 and 2011, respectively.

In December 2012, the Board of Directors authorized the acquisition of an additional \$1 billion of our common stock upon completion of the 2011 repurchase program. In 2013, we acquired \$155 million or 1.3 million shares of our common stock leaving \$845 million available for purchase under this new authorization at December 31, 2013.

During the fourth quarter of 2013, we repurchased 12,143 shares from employees in connection with the Key Employee Stock Investment Plan which allows certain employees, other than officers, to purchase shares of common stock on an installment basis up to an established credit limit. Loans are issued for five-year terms at a fixed interest rate established at the date of purchase and may be refinanced after its initial five-year period for an additional five-year period. Participants must hold shares for a minimum of six months from date of purchase and after shares are sold must wait six months before another share purchase may be made. We hold participants' shares as security for the loans and would, in effect repurchase shares if the participant defaulted in repayment of the loan. There is no maximum amount of shares that we may purchase under this plan.

**Performance Graph (Unaudited)**

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

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

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



ASSUMES \$100 INVESTED ON DEC. 31, 2008  
 ASSUMES DIVIDENDS REINVESTED  
 FISCAL YEAR ENDING DEC. 31, 2013

**ITEM 6. Selected Financial Data**

The selected financial information presented below for each of the last five years ended December 31, beginning with 2013, was derived from our *Consolidated Financial Statements*. This information should be read in conjunction with our *Consolidated Financial Statements* and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

In millions, except per share amounts	2013	2012	2011	2010	2009
<b>For the years ended December 31,</b>					
Net sales	\$ 17,301	\$ 17,334	\$ 18,048	\$ 13,226	\$ 10,800
<i>U.S. percentage of sales</i>	48%	47%	41%	36%	48%
<i>Non-U.S. percentage of sales</i>	52%	53%	59%	64%	52%
Gross margin	4,383	4,508	4,589	3,168	2,169
Research, development and engineering expenses	713	728	629	414	362
Equity, royalty and interest income from investees	361	384	416	351	214
Interest expense	41	32	44	40	35
Net income attributable to Cummins Inc. <sup>(1)</sup>	1,483	1,645	1,848	1,040	428
Earnings per share attributable to Cummins Inc.					
Basic	\$ 7.93	\$ 8.69	\$ 9.58	\$ 5.29	\$ 2.17
Diluted	7.91	8.67	9.55	5.28	2.16
Cash dividends declared per share	2.25	1.80	1.325	0.875	0.70
Net cash provided by operating activities	\$ 2,089	\$ 1,532	\$ 2,073	\$ 1,006	\$ 1,137
Capital expenditures	676	690	622	364	310
<b>At December 31,</b>					
Cash and cash equivalents	\$ 2,699	\$ 1,369	\$ 1,484	\$ 1,023	\$ 930
Total assets	14,728	12,548	11,668	10,402	8,816
Long-term debt <sup>(2)</sup>	1,672	698	658	709	637
Total equity <sup>(3)</sup>	7,870	6,974	5,831	4,996	4,020

<sup>(1)</sup> For the year ended December 31, 2012, consolidated net income included \$52 million of restructuring and other charges (\$35 million after-tax), a \$6 million gain (\$4 million after-tax) related to adjustments from our 2011 divestitures and a \$20 million charge (\$12 million after-tax) related to legal matters. For the year ended December 31, 2011, consolidated net income included a \$68 million gain (\$37 million after-tax) related to the disposition of certain assets and liabilities of our exhaust business and a \$53 million gain (\$33 million after-tax) recorded for the disposition of certain assets and liabilities of our light-duty filtration business, both from the Components segment, and a \$38 million gain (\$24 million after-tax) related to flood damage recoveries from the insurance settlement related to a June 2008 flood in Southern Indiana. For the year ended December 31, 2010, consolidated net income included \$32 million in Brazil tax recoveries (\$21 million after-tax) and \$2 million in flood damage expenses. For the year ended December 31, 2009, consolidated net income included \$99 million in restructuring and other charges (\$65 million after-tax) and a gain of \$12 million related to flood damage recoveries.

<sup>(2)</sup> In September 2013, we issued \$1 billion of senior unsecured debt.

<sup>(3)</sup> In 2013, 2012, 2011 and 2010, we recorded non-cash charges (credits) to equity of \$(102) million, \$83 million, \$96 million and \$(125) million, respectively, to record net actuarial losses (gains) associated with the valuation of our pension plans. These losses (gains) include the effects of market conditions on our pension trust assets and the effects of economic factors on the valuation of the pension liability.

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

### ORGANIZATION OF INFORMATION

The following Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) was prepared to provide the reader with a view and perspective of our business through the eyes of management and should be read in conjunction with our *Consolidated Financial Statements* and the accompanying notes to those financial statements. Our MD&A is presented in the following sections:

- Executive Summary and Financial Highlights
- 2014 Outlook
- Results of Operations
- Restructuring and Other Charges
- Operating Segment Results
- Liquidity and Capital Resources
- Contractual Obligations and Other Commercial Commitments
- Application of Critical Accounting Estimates
- Recently Adopted Accounting Pronouncements

### EXECUTIVE SUMMARY AND FINANCIAL HIGHLIGHTS

We are a global power leader that designs, manufactures, distributes and services diesel and natural gas engines and engine-related component products, including filtration, aftertreatment, turbochargers, fuel systems, controls systems, air handling systems and electric power generation systems. We sell our products to original equipment manufacturers (OEMs), distributors and other customers worldwide. We have long-standing relationships with many of the leading manufacturers in the markets we serve, including PACCAR Inc, Daimler Trucks North America, Chrysler Group, LLC (Chrysler), Volvo AB, Komatsu, Navistar International Corporation, Aggreko plc, Ford Motor Company and MAN Nutzfahrzeuge AG. We serve our customers through a network of over 600 company-owned and independent distributor locations and over 6,800 dealer locations in more than 190 countries and territories.

Our reportable operating segments consist of the following: Engine, Components, Power Generation and Distribution. This reporting structure is organized according to the products and markets each segment serves and allows management to focus its efforts on providing enhanced service to a wide range of customers. The Engine segment produces engines and parts for sale to customers in on-highway and various industrial markets. Our engines are used in trucks of all sizes, buses and recreational vehicles, as well as in various industrial applications, including construction, mining, agriculture, marine, oil and gas, rail and military equipment. The Components segment sells filtration products, aftertreatment systems, turbochargers and fuel systems. The Power Generation segment is an integrated provider of power systems, which sells engines, generator sets and alternators. The Distribution segment includes wholly-owned and partially-owned distributorships engaged in wholesaling engines, generator sets and service parts, as well as performing service and repair activities on our products and maintaining relationships with various OEMs throughout the world.

Our financial performance depends, in large part, on varying conditions in the markets we serve, particularly the on-highway, construction and general industrial markets. Demand in these markets tends to fluctuate in response to overall economic conditions. Our sales may also be impacted by OEM inventory levels and production schedules and stoppages. Economic downturns in markets we serve generally result in reductions in sales and pricing of our products. As a worldwide business, our operations are also affected by currency, political, economic and regulatory matters, including adoption and enforcement of environmental and emission standards, in the countries we serve. As part of our growth strategy, we invest in businesses in certain countries that carry high levels of these risks such as China, Brazil, India, Mexico, Russia and countries in the Middle East and Africa. At the same time, our geographic diversity and broad product and service offerings have helped limit the impact from a drop in demand in any one industry or customer or the economy of any single country on our consolidated results.

Worldwide revenues in 2013 were down slightly compared to 2012, as global economic uncertainty continued during the period. International revenues declined by 4 percent with sales down or relatively flat in most international markets primarily due to declines in the off-highway mining market with reduced unit shipments of 37 percent, reduced demand in the international power generation markets and unfavorable foreign currency fluctuations. These declines were partially offset by an increase in Components segment sales reflecting a full year of sales from Hilite Germany GmbH (Hilite), which was acquired in the third quarter of 2012 and growth in the construction and medium-duty Brazilian truck markets, resulting in higher engine and component demand. Revenue in the U.S. and Canada improved by 3 percent, which reflected the consolidation of three partially-owned North American distributors since June 2012 and improved demand within the Components segment emission solutions business from on-highway OEM and aftermarket products and medium-duty truck customers. Revenues also increased in the Power Generation segment power products business as the result of increased demand in North America. These increases were mostly offset by reduced demand in the on-highway heavy-duty truck and medium-duty bus markets, as well as the off-highway mining and oil and gas markets to which unit shipments declined 15 percent, 25 percent, 30 percent and 37 percent, respectively, compared to last year.

Slow growth in the U.S. economy continued to suppress business capital expenditures in 2013, thus impacting demand for truck and power generation equipment. The governments of China and India have tried to control inflation through tight monetary policies in the form of rising interest rates and tightening access to credit. Brazil began to tighten its monetary policies in the second half of 2013. Tightening monetary policies could create headwinds in our end markets. The European economy remains stagnant and uncertain; however, demand for engines and components in Euro zone countries stabilized somewhat during 2013. Although we do not have any significant direct exposure to European sovereign debt, we generated approximately 8 percent of our net sales from Euro zone countries in both 2013 and 2012.

The following table contains sales and EBIT (defined as earnings before interest expense, taxes and noncontrolling interests) results by operating segment for the years ended December 31, 2013 and 2012. Refer to the section titled "Operating Segment Results" for a more detailed discussion of net sales and EBIT by operating segment including the reconciliation of segment EBIT to income before taxes.

### Operating Segments

In millions	2013			2012			Percent change 2013 vs. 2012	
	Sales	Percent of Total	EBIT	Sales	Percent of Total	EBIT	Sales	EBIT
Engine	\$ 10,013	58 %	\$ 1,041	\$ 10,733	62 %	\$ 1,248	(7)%	(17)%
Components	4,342	25 %	527	4,012	23 %	426	8 %	24 %
Power Generation	3,031	18 %	218	3,268	19 %	285	(7)%	(24)%
Distribution	3,749	22 %	388	3,277	19 %	369	14 %	5 %
Intersegment eliminations	(3,834)	(23)%	—	(3,956)	(23)%	—	(3)%	—
Non-segment	—	—	(14)	—	—	(25)	—	(44)%
<b>Total</b>	<b>\$ 17,301</b>	<b>100 %</b>	<b>\$ 2,160</b>	<b>\$ 17,334</b>	<b>100 %</b>	<b>\$ 2,303</b>	<b>—</b>	<b>(6)%</b>

Net income attributable to Cummins Inc. for 2013 was \$1,483 million, or \$7.91 per diluted share, on sales of \$17.3 billion, compared to 2012 net income attributable to Cummins Inc. of \$1,645 million, or \$8.67 per diluted share, on sales of \$17.3 billion. The decrease in income and earnings per share was driven mainly by lower gross margins, lower equity, royalty and interest income from investees, higher operating expenses and a higher effective tax rate of 25.1 percent versus 23.5 percent in 2012. Diluted earnings per share for 2013 benefited \$0.06 from lower shares outstanding, primarily due to purchases under the stock repurchase program.

In December 2013, we acquired the remaining 35 percent interest in Cummins Western Canada LP (Western Canada) for a total consideration of \$34 million. In May 2013, we acquired the remaining 67 percent interest in Cummins Rocky Mountain LLC (Rocky Mountain) for total consideration of approximately \$136 million. In January 2013, we acquired an additional 29.99 percent interest in Cummins Northwest LLC (Northwest), followed by the remaining 20.01 percent interest in July 2013, for total consideration of approximately \$22 million.

We generated \$2.1 billion of operating cash flows in 2013, compared to \$1.5 billion in 2012. Refer to the section titled "Operating Activities" in the "Liquidity and Capital Resources" section for a discussion of items impacting cash flows.



## [Table of Contents](#)

In February 2011, the Board of Directors approved a share repurchase program and authorized the acquisition of up to \$1 billion of our common stock. In June 2013, we repurchased the remaining \$226 million of common stock to complete this authorization. In December 2012, the Board of Directors authorized the acquisition of up to \$1 billion of additional common stock upon completion of the 2011 repurchase plan. We purchased \$155 million of common stock during 2013 under this new plan.

In July 2013, the Board of Directors authorized a dividend increase of 25 percent from \$0.50 per share to \$0.625 per share on a quarterly basis effective in the third quarter. Our debt to capital ratio (capital is defined as debt plus equity) at December 31, 2013, was 18.1 percent, compared to 10.0 percent at December 31, 2012. As of the date of filing of this Annual Report on Form 10-K, we had an 'A' credit rating with a 'Stable' outlook from Standard & Poor's Rating Services, an 'A' credit rating and a 'Stable' outlook from Fitch Ratings and an 'A3' credit rating with a 'Stable' outlook from Moody's Investors Service, Inc. In addition to our \$2.8 billion in cash and marketable securities on hand, we have sufficient access to our credit facilities, if necessary, to meet currently anticipated investment and funding needs.

On September 16, 2013, we filed an automatic shelf registration for an undetermined amount of debt and equity securities. In September 2013, we issued \$1 billion aggregate principal amount of senior notes consisting of \$500 million aggregate principal amount of 3.65% senior unsecured notes due in 2023 and \$500 million aggregate principal amount of 4.875% senior unsecured notes due in 2043.

On September 17, 2013, we announced our intention to acquire the equity that we do not already own in most of our partially-owned United States and Canadian distributors over the next three to five years.

Our global pension plans, including our unfunded and non-qualified plans, were 107 percent funded at year-end 2013. Our U.S. qualified plan, which represents approximately 55 percent of the worldwide pension obligation, was 121 percent funded and our United Kingdom (U.K.) plan was 106 percent funded. Asset returns in 2013 for the U.S. qualified plan was 7.6 percent while the year-end 2013 discount rate was 4.8 percent, up 0.85 percentage points from the 2012 discount rate of 3.95 percent. We expect to contribute \$205 million of cash to our global pension plans in 2014. We do not have a required minimum pension contribution obligation for our U.S. plans in 2014. We expect pension and other postretirement benefit cost in 2014 to decrease by approximately \$36 million pre-tax, or \$0.12 per diluted share, when compared to 2013. Refer to application of critical accounting estimates within MD&A and Note 12, "PENSION AND OTHER POSTRETIREMENT BENEFITS," to the *Consolidated Financial Statements*, for additional information concerning our pension and other post-retirement benefit plans.

## 2014 OUTLOOK

### Near-Term

The global economy continued to experience uncertainty throughout 2013, negatively impacting many international and some North American markets. These impacts were partially offset by improvements in North America primarily due to Distribution segment sales related to the consolidation of three partially-owned North American distributors since June 2012 and improved demand within the Components segment emission solutions business for on-highway OEM and aftermarket products. Economies in emerging markets, including China and India slowed during 2013 which negatively impacted a number of our end markets, especially the off-highway mining market and the power generation markets.

We currently expect the following positive trends in 2014:

- Market share gains in the North America medium-duty truck market are expected to continue in 2014 and should positively impact sales in both the Engine and Components segments.
- We plan to continue acquiring our partially-owned North American distributors, which will increase our Distribution segment revenues.
- The new Euro VI regulations, effective January 1, 2014, are expected to positively impact sales for aftertreatment products and increase our customer base in Europe.

We currently expect the following challenges to our business that may reduce our revenue and earnings potential in 2014:

- Power generation markets are expected to remain weak.
- Demand in most end markets in India is expected to remain weak.
- Demand in certain European markets could remain weak due to continued economic uncertainty.
- Growth in emerging markets could be negatively impacted if emission regulations are not strictly enforced.

## [Table of Contents](#)

- Foreign currency volatility could continue to put pressure on earnings.
- North American oil and gas markets are expected to remain weak.
- Domestic and international mining markets could continue to deteriorate if commodity prices weaken.

### **Long-Term**

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

- tightening emissions controls across the world;
- infrastructure needs in emerging markets;
- energy availability and cost issues and
- globalization of industries like ours.

**RESULTS OF OPERATIONS**

In millions (except per share amounts)	Years ended December 31,			Favorable/(Unfavorable)			
	2013	2012	2011	2013 vs. 2012		2012 vs. 2011	
				Amount	Percent	Amount	Percent
<b>NET SALES</b>	\$ 17,301	\$ 17,334	\$ 18,048	\$ (33)	— %	\$ (714)	(4)%
Cost of sales	12,918	12,826	13,459	(92)	(1)%	633	5 %
<b>GROSS MARGIN</b>	<b>4,383</b>	4,508	4,589	(125)	(3)%	(81)	(2)%
<b>OPERATING EXPENSES AND INCOME</b>							
Selling, general and administrative expenses	1,920	1,900	1,837	(20)	(1)%	(63)	(3)%
Research, development and engineering expenses	713	728	629	15	2 %	(99)	(16)%
Equity, royalty and interest income from investees	361	384	416	(23)	(6)%	(32)	(8)%
Gain on sale of businesses	—	6	121	(6)	(100)%	(115)	(95)%
Other operating income (expense), net	(10)	(16)	21	6	(38)%	(37)	NM
<b>OPERATING INCOME</b>	<b>2,101</b>	2,254	2,681	(153)	(7)%	(427)	(16)%
Interest income	27	25	34	2	8 %	(9)	(26)%
Interest expense	41	32	44	(9)	(28)%	12	27 %
Other income (expense), net	32	24	—	8	33 %	24	100 %
<b>INCOME BEFORE INCOME TAXES</b>	<b>2,119</b>	2,271	2,671	(152)	(7)%	(400)	(15)%
Income tax expense	531	533	725	2	— %	192	26 %
<b>CONSOLIDATED NET INCOME</b>	<b>1,588</b>	1,738	1,946	(150)	(9)%	(208)	(11)%
Less: Net income attributable to noncontrolling interests	105	93	98	(12)	(13)%	5	5 %
<b>NET INCOME ATTRIBUTABLE TO CUMMINS INC.</b>	<b>\$ 1,483</b>	\$ 1,645	\$ 1,848	\$ (162)	(10)%	\$ (203)	(11)%
<b>Diluted earnings per common share attributable to Cummins Inc.</b>	<b>\$ 7.91</b>	\$ 8.67	\$ 9.55	\$ (0.76)	(9)%	\$ (0.88)	(9)%

"NM" - not meaningful information

Percent of sales	2013	2012	2011	Favorable/(Unfavorable)Percentage Points	
				2013 vs. 2012	2012 vs. 2011
Gross margin	25.3%	26.0%	25.4%	(0.7)	0.6
Selling, general and administrative expenses	11.1%	11.0%	10.2%	(0.1)	(0.8)
Research, development and engineering expenses	4.1%	4.2%	3.5%	0.1	(0.7)

**2013 vs. 2012**

*Net Sales*

Net sales decreased slightly versus 2012 and was primarily driven by the following:

- Engine segment sales decreased by 7 percent due to lower demand in the power generation markets, weaker demand in the North American heavy-duty truck markets and continued weakness in industrial demand, primarily in off-high-way mining markets.
- Power Generation segment sales decreased by 7 percent due to lower demand in the power solutions business, primarily in the U.K., and lower demand in the power systems and the alternators businesses in international markets, partially offset by improvements in the North American power product business.
- Foreign currency fluctuations unfavorably impacted sales by 1 percent.

The decreases were partially offset by the following:

- Distribution segment sales increased by 14 percent primarily due to incremental sales in 2013 related to the consolidation of partially-owned North American distributors since June 2012.

## [Table of Contents](#)

- Components segment sales increased by 8 percent due to increased sales within the emission solutions business, mainly related to improved on-highway OEM and aftermarket demand in North America, a full year of sales from Hilite which was acquired in the third quarter of 2012, 2013 pre-buy activity in anticipation of the Euro VI emission standards and growth in the medium-duty Brazilian truck market resulting in improved aftertreatment demand.

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

Sales to international markets (excluding the U.S. and Canada) were 48 percent of total net sales in 2013, compared with 49 percent of total net sales in 2012.

### **Gross Margin**

Gross margin decreased by \$125 million and as a percentage of sales decreased by 0.7 percentage points. The decrease in gross margin as a percentage of sales was primarily due to a decline in demand for high-horsepower engines and gensets, partially offset by improved price realization, lower material and commodity costs and the absence of 2012 restructuring charges of \$29 million.

The provision for warranties issued, excluding campaigns, as a percentage of sales was 2.1 percent in both 2013 and 2012. A more detailed discussion of margin by segment is presented in the "OPERATING SEGMENT RESULTS" section.

### **Selling, General and Administrative Expenses**

Selling, general and administrative expenses increased primarily due to incremental costs in 2013 related to the acquisition of partially owned North American distributors since June 2012. These costs primarily contributed to increased compensation and related expenses of \$52 million and increased variable compensation of \$5 million, partially offset by lower consulting of \$24 million, the absence of 2012 restructuring charges of \$20 million and reduced discretionary spending. Higher compensation expense was primarily due to increased headcount to support our strategic growth initiatives. Compensation and related expenses include salaries and fringe benefits. Overall, selling, general and administrative expenses, as a percentage of sales, increased to 11.1 percent in 2013 from 11.0 percent in 2012.

### **Research, Development and Engineering Expenses**

Research, development and engineering expenses decreased primarily due to lower consulting of \$30 million and decreased engineering program spending of \$23 million, partially offset by increases of \$44 million in compensation related expenses. Higher compensation expense was primarily due to increased headcount to support our strategic growth initiatives. Compensation and related expenses include salaries and fringe benefits. Research, development and engineering expenses in 2012 also included restructuring charges of \$3 million. Overall, research, development and engineering expenses, as a percentage of sales, decreased to 4.1 percent in 2013 from 4.2 percent in 2012. Research activities continue to focus on development of new products to meet future emission standards around the world and improvements in fuel economy performance.

### **Equity, Royalty and Interest Income From Investees**

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

<b>In millions</b>	<b>2013 vs. 2012</b>	
	<b>Increase/(Decrease)</b>	
North American distributors	\$	(18)
Cummins Westport, Inc.		(10)
Beijing Foton Cummins Engine Co., Ltd. (Heavy-duty)		(8)
Beijing Foton Cummins Engine Co., Ltd. (Light-duty)		12
Tata Cummins, Ltd.		(6)
Dongfeng Cummins Engine Company, Ltd.		11
All other		(3)
Cummins share of net income		(22)
Royalty and interest income		(1)
Equity, royalty and interest income from investees	\$	(23)

[Table of Contents](#)

The decreases above were primarily due to the consolidation of the partially-owned North American distributors acquired in 2013, unfavorable warranty accruals at Cummins Westport, Inc., an impairment charge of an equity investment within the Power Generation segment and additional start-up costs at Beijing Foton Cummins Engine Co., Ltd. (Heavy-duty), partially offset by increased demand at Beijing Foton Cummins Engine Co., Ltd (Light-duty) and Dongfeng Cummins Engine Company, Ltd.

As we execute our plan to acquire partially-owned distributors over the next three to five years, equity earnings for our North American distributors will continue to decrease. See Note 2, "ACQUISITIONS AND DIVESTITURES," to the *Consolidated Financial Statements* for further information.

**Gain on Sale of Businesses**

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

**Other Operating Income (Expense), Net**

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

In millions	Years ended December 31,	
	2013	2012
Loss on write off of assets	\$ (14)	\$ (6)
Amortization of intangible assets	(11)	(8)
Royalty expense	(4)	(3)
Legal matters	(2)	(20)
Gain (loss) on sale of fixed assets	1	4
Royalty income	20	18
Other, net	—	(1)
Total other operating income (expense), net	\$ (10)	\$ (16)

**Interest Income**

Interest income was relatively flat compared to 2012.

**Interest Expense**

Interest expense increased primarily due to the \$1 billion debt issuance in September 2013. Interest expense will increase in future periods as a result of this issuance.

**Other Income (Expense), Net**

Other income (expense), net was as follows:

In millions	Years ended December 31,	
	2013	2012
Gain (loss) on marketable securities, net	\$ 13	\$ 3
Gain on fair value adjustment for consolidated investee <sup>(1)</sup>	12	7
Change in cash surrender value of corporate owned life insurance	12	5
Dividend income	5	7
Gain on sale of equity investment	—	13
Bank charges	(10)	(15)
Foreign currency gains (losses), net	(27)	(14)
Other, net	27	18
Total other income (expense), net	\$ 32	\$ 24

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

### ***Income Tax Expense***

Our income tax rates are generally less than the 35 percent U.S. statutory income tax rate primarily because of lower taxes on foreign earnings and research tax credits. Our effective tax rate for 2013 was 25.1 percent compared to 23.5 percent for 2012. As a result of a restructuring of our foreign operations in 2013, our 2013 effective tax rate was approximately 1% less than it would have been without restructuring. On January 2, 2013, the American Taxpayer Relief Act of 2012 was signed into law and reinstated the research tax credit back to 2012. As tax law changes are accounted for in the period of enactment, we recognized a \$28 million discrete tax benefit in the first quarter of 2013. We also recognized a discrete tax expense of \$17 million in the first quarter which primarily related to the write-off of a deferred tax asset deemed unrecoverable. Also included in 2013 is a third quarter discrete net tax expense of \$7 million primarily related to U.S. federal tax return true-up adjustments and third quarter enactment of U.K. tax law changes. Additionally, our effective tax rate for 2013 also included a fourth quarter discrete net tax benefit of \$21 million primarily due to the release of U.S. deferred tax liabilities related to prior years unremitted income of certain Indian and Mexican subsidiaries now considered to be permanently reinvested, as well as adjustments to our income tax accounts principally based on our 2012 state tax return filings. Our 2012 income tax provision included a one-time \$134 million tax benefit which resulted from tax planning strategies and tax return elections made with respect to our U.K. operations.

We evaluate the recoverability of our deferred tax assets each quarter by assessing the likelihood of future profitability and available tax planning strategies that could be implemented to realize our net deferred tax assets. At December 31, 2013, we recorded net deferred tax assets of \$177 million. These assets included \$187 million for the value of tax loss and credit carryforwards. A valuation allowance of \$101 million was recorded to reduce the tax assets to the net value management believed was more likely than not to be realized. In the event our operating performance deteriorates, future assessments could conclude that a larger valuation allowance will be needed to further reduce the deferred tax assets.

We expect our 2014 effective tax rate to be 28.5 percent excluding any discrete items that may arise. The research tax credit expired December 31, 2013, and has not yet been renewed by Congress. If the research credit is reinstated during 2014, we would anticipate the 2014 effective tax rate to be reduced to 27 percent. The increase in the effective tax rate from 2013 to 2014 is attributable primarily to one-time tax benefits in 2013 that will not repeat in 2014, as well as other changes in tax legislation in the U.S. and proposed changes in the U.K. that will unfavorably impact our 2014 effective tax rate.

In September 2013, the Internal Revenue Service released final tangible personal property regulations regarding the deduction and capitalization of expenditures related to tangible property. The new rules will become effective for taxable years beginning on or after January 1, 2014. While we are still finalizing our analysis, we do not believe that these regulations will have a material impact on our *Consolidated Financial Statements*.

### ***Noncontrolling Interests***

Noncontrolling interests eliminate the income or loss attributable to non-Cummins ownership interests in our consolidated entities. Noncontrolling interests in income of consolidated subsidiaries increased reflecting our minority's share of higher profits of \$7 million at Cummins Western Canada LP, \$6 million at Wuxi Cummins Turbo Technologies Co. Ltd. and \$4 million due to the acquisition of a majority interest in Cummins Central Power LLC (Central Power) in the third quarter of 2012. The increases were partially offset by a total decrease of \$8 million at Cummins India Ltd.

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

Net income and diluted earnings per share attributable to Cummins Inc. decreased primarily due to lower gross margin as a percentage of sales, mainly driven by unfavorable product mix and lower volumes, particularly in the Engine segment and Power Generation segment, a higher effective tax rate of 25.1 percent versus 23.5 percent in 2012, lower equity, royalty and interest income from investees, mainly due to the acquisition of the North American distributors, and higher selling, general and administrative expenses. These decreases were partially offset by lower research, development and engineering expenses. Diluted earnings per share for 2013 benefited \$0.06 from lower shares outstanding, primarily due to purchases under the stock repurchase program.

## **2012 vs. 2011**

### ***Net Sales***

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

- Engine segment sales decreased by 5 percent due to weakness in industrial demand, especially in international construction markets, and lower volumes in the Brazilian medium-duty truck market, which were partially offset by growth in the North American on-highway markets in the first half of the year, led by the heavy-duty business.
- Foreign currency fluctuations unfavorably impacted sales by 2 percent.
- Power Generation segment sales decreased by 7 percent due to lower demand in the alternators, power solutions and power systems businesses, which were partially offset by growing demand in the power product business, especially in North America.
- Components segment sales, excluding acquisitions, decreased by 2 percent due to \$126 million of sales in 2011 related to assets sold in 2011 and lower demand in the turbo technologies, filtration and fuel systems businesses, which were partially offset by higher demand in the emission solutions business, primarily in North America and Brazil.

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

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

Sales to international markets (excluding the U.S. and Canada) were 49 percent of total net sales in 2012, compared with 56 percent of total net sales in 2011.

### ***Gross Margin***

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

The provision for warranties issued as a percentage of sales was 2.1 percent in both 2012 and 2011. A more detailed discussion of margin by segment is presented in the "OPERATING SEGMENT RESULTS" section.

### ***Selling, General and Administrative Expenses***

Selling, general and administrative expenses increased primarily due to higher consulting of \$45 million, restructuring and other charges of \$20 million and an increase of \$19 million in compensation and related expenses, which were partially offset by reduced discretionary spending in the second half of the year. Higher compensation expense was primarily due to increased headcount to support our strategic growth initiatives launched prior to a number of markets unexpectedly slowing in mid-2012. Compensation and related expenses include salaries, fringe benefits and variable compensation. Variable compensation related to 2012 performance decreased \$87 million over variable compensation related to 2011 performance. In the third quarter of 2012, we implemented a number of cost reduction initiatives to align our cost structure with the slowdown in demand at several of our key markets in the second half of the year. Overall, selling, general and administrative expenses, as a percentage of sales, increased to 11.0 percent in 2012 from 10.2 percent in 2011.

### ***Research, Development and Engineering Expenses***

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

**Equity, Royalty and Interest Income From Investees**

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

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

The decreases above were primarily due to lower sales in China at Dongfeng Cummins Engine Company, Ltd. and Chongqing Cummins Engine Company, Ltd., which were partially offset by growth in North American distributors and higher sales at Beijing Foton Cummins Engine Co., Ltd. (Light-duty).

**Gain on Sale of Businesses**

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

Sales for this business were \$62 million in 2011 (through closing). Income before income taxes for this business were approximately \$9 million in 2011 (through closing).

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

Sales for this business were \$64 million in 2011 (through closing). Income before income taxes for this business were approximately \$13 million in 2011 (through closing).

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

**Other Operating Income (Expense), Net**

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

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



**Interest Income**

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

**Interest Expense**

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

**Other Income (Expense), Net**

Other income (expense), net was as follows:

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

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

**Income Tax Expense**

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

**Noncontrolling Interests**

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

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

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

**RESTRUCTURING AND OTHER CHARGES**

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

Employee termination and severance costs were recorded based on approved plans developed by the businesses and corporate management which specified positions to be eliminated, benefits to be paid under existing severance plans or statutory requirements and the expected timetable for completion of the plan. Estimates of restructuring were made based on information available at the time charges were recorded.

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

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

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

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

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

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

At December 31, 2013, of the approximately 1,300 employees affected by this plan, substantially all terminations have been completed.

## [Table of Contents](#)

The table below summarizes the activity and balance of accrued restructuring charges, which is included in "Other accrued expenses" in our *Consolidated Balance Sheets* for the years ended December 31, 2012 and 2013.

In millions	
2012 Restructuring charges <sup>(1)</sup>	\$ 50
Cash payments for 2012 actions	(25)
Balance at December 31, 2012	25
Cash payments for 2012 actions	(22)
Change in estimate <sup>(2)</sup>	(3)
Balance at December 31, 2013	\$ —

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

(2) Due to the inherent uncertainty involved in calculating the initial estimates, the actual amounts paid for such activities differed slightly from the amounts initially recorded. We have adjusted the previous estimates accordingly.

## OPERATING SEGMENT RESULTS

Our reportable operating segments consist of the following: Engine, Components, Power Generation and Distribution. This reporting structure is organized according to the products and markets each segment serves and allows management to focus its efforts on providing enhanced service to a wide range of customers. The Engine segment produces engines and parts for sale to customers in on-highway and various industrial markets. Our engines are used in trucks of all sizes, buses and recreational vehicles, as well as in various industrial applications, including construction, mining, agriculture, marine, oil and gas, rail and military equipment. The Components segment sells filtration products, aftertreatment, turbochargers and fuel systems. The Power Generation segment is an integrated provider of power systems which sells engines, generator sets and alternators. The Distribution segment includes wholly-owned and partially-owned distributorships engaged in wholesaling engines, generator sets and service parts, as well as performing service and repair activities on our products and maintaining relationships with various OEMs throughout the world.

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

The accounting policies of our operating segments are the same as those applied in our *Consolidated Financial Statements*. We prepared the financial results of our operating segments on a basis that is consistent with the manner in which we internally disaggregate financial information to assist in making internal operating decisions. We have allocated certain common costs and expenses, primarily corporate functions, among segments differently than we would for stand-alone financial information prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). These include certain costs and expenses of shared services, such as information technology, human resources, legal and finance. We also do not allocate debt-related items, actuarial gains or losses, prior service costs or credits, changes in cash surrender value of corporate owned life insurance, flood damage gains or losses, divestiture gains or losses or income taxes to individual segments. Segment EBIT may not be consistent with measures used by other companies.

Following is a discussion of operating results for each of our business segments.



- Industrial market sales decreased primarily due to a 36 percent reduction in global mining shipments as a result of lower commodity prices and a 37 percent decline in engine shipments to North American oil and gas markets, partially offset by increased shipments to the Western European construction markets as a result of the pre-buy activity in 2013 ahead of the Tier IV emission regulations beginning in the first quarter of 2014.
- Foreign currency fluctuations unfavorably impacted sales.

The decreases above were partially offset by the following:

- Medium-duty truck engine sales increased due to market share gains in the North American medium-duty truck market and improved demand in the Brazilian and European truck markets. The improved sales in Brazil were primarily due to lower sales in the first half of 2012 as the result of the implementation of the Euro V emission regulations beginning in the first quarter of 2012.

Total on-highway-related sales for 2013 were 62 percent of total engine segment sales, compared to 59 percent in 2012.

**Segment EBIT**

Engine segment EBIT decreased versus 2012, primarily due to lower gross margin, partially offset by lower research, development and engineering expenses and higher equity, royalty and interest income from investees. Engine segment EBIT for 2012 included restructuring and other charges of \$20 million in the fourth quarter of 2012. Major components of EBIT and related changes to segment EBIT and EBIT as a percentage of sales were as follows:

In millions	Year ended December 31, 2013 vs. 2012		
	Favorable/(Unfavorable) Change		
	Amount	Percent	Percentage point change as a percent of sales
Gross margin	\$ (237)	(10)%	(0.7)
Selling, general and administrative expenses	1	— %	(0.5)
Research, development and engineering expenses	17	4 %	(0.2)
Equity, royalty and interest income from investees	9	7 %	0.2

The decrease in gross margin versus 2012 was primarily due to unfavorable product mix and lower high-horsepower volumes, partially offset by improved price realization, decreased material and commodity costs and favorable foreign currency fluctuations. The decrease in selling, general and administrative expenses was primarily due to lower discretionary spending and the absence of restructuring charges incurred in 2012, partially offset by increased headcount. The decrease in research, development and engineering expenses was primarily due to lower discretionary spending in 2013, partially offset by increases in new product development spending and increased headcount to support our strategic growth initiatives. The increase in equity, royalty and interest income from investees was primarily due to increased earnings at Beijing Foton Cummins Engine Co., Ltd. within the light-duty business and Dongfeng Cummins Engine Company, Ltd, partially offset by decreased earnings at Cummins Westport, Inc. and larger losses at Beijing Foton Cummins Engine Company, Ltd. (Heavy-duty) in anticipation of production in the second quarter of 2014.

**2012 vs. 2011**

**Sales**

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

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

[Table of Contents](#)

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

The decreases above were partially offset by the following:

- Heavy-duty truck engine sales increased due to growth in the North American on-highway markets in the first half of the year, primarily as a result of the replacement of aging fleets.
- Light-duty automotive and RV sales increased primarily due to a 37 percent improvement in units shipped to Chrysler.

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

**Segment EBIT**

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

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

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

**Components Segment Results**

Financial data for the Components segment was as follows:

In millions	Years ended December 31,			Favorable/(Unfavorable)			
				2013 vs. 2012		2012 vs. 2011	
	2013	2012	2011	Amount	Percent	Amount	Percent
External sales	\$ 3,151	\$ 2,809	\$ 2,886	\$ 342	12 %	\$ (77)	(3)%
Intersegment sales	1,191	1,203	1,177	(12)	(1)%	26	2 %
Total sales	4,342	4,012	4,063	330	8 %	(51)	(1)%
Depreciation and amortization	96	82	73	(14)	(17)%	(9)	(12)%
Research, development and engineering expenses	218	213	175	(5)	(2)%	(38)	(22)%
Equity, royalty and interest income from investees	28	29	31	(1)	(3)%	(2)	(6)%
Interest income	3	3	5	—	— %	(2)	(40)%
Segment EBIT	527	426	470	101	24 %	(44)	(9)%
					Percentage Points		Percentage Points
Segment EBIT as a percentage of total sales	12.1 %	10.6 %	11.6 %		1.5		(1.0)

Sales for our Components segment by business were as follows:

In millions	Years ended December 31,			Favorable/(Unfavorable)			
	2013	2012	2011	2013 vs. 2012		2012 vs. 2011	
				Amount	Percent	Amount	Percent
Emission solutions	1,791	1,415	1,262	376	27 %	153	12 %
Turbo technologies	1,115	1,106	1,223	9	1 %	(117)	(10)%
Filtration	1,028	1,048	1,113	(20)	(2)%	(65)	(6)%
Fuel systems	408	443	465	(35)	(8)%	(22)	(5)%
Total sales	<u>\$ 4,342</u>	<u>\$ 4,012</u>	<u>\$ 4,063</u>	<u>\$ 330</u>	<u>8 %</u>	<u>\$ (51)</u>	<u>(1)%</u>

### 2013 vs. 2012

#### *Sales*

Components segment sales increased versus 2012 primarily due to increased sales within the emission solutions business, mainly related to the following:

- improved on-highway OEM and aftermarket demand in North America,
- the impact of our 2012 acquisition of Hilite experienced in Western Europe, which resulted in \$77 million of related incremental sales in 2013 compared to 2012,
- Western European pre-buy activity in anticipation of the Euro VI emission standards beginning in the first quarter of 2014 and
- growth in the medium-duty Brazilian truck market which resulted in improved aftertreatment demand.

The increases above were partially offset by the following:

- Foreign currency fluctuations unfavorably impacted sales results.
- Fuel systems business sales decreased primarily due to lower demand in North American on-highway markets and lower demand in Europe, partially offset by increased aftermarket demand.

#### *Segment EBIT*

Components segment EBIT increased versus 2012, primarily due to higher gross margin. Components segment EBIT for 2012 included restructuring and other charges of \$6 million in the fourth quarter. Major components of EBIT and related changes to segment EBIT and EBIT as a percentage of sales were as follows:

In millions	Year ended December 31, 2013 vs. 2012		
	Favorable/(Unfavorable) Change		
	Amount	Percent	Percentage point change as a percent of sales
Gross margin	\$ 112	13 %	0.9
Selling, general and administrative expenses	7	3 %	0.7
Research, development and engineering expenses	(5)	(2)%	0.3
Equity, royalty and interest income from investees	(1)	(3)%	(0.1)

The increase in gross margin was primarily due to higher volumes in the emission solutions business and lower material and commodity costs in several businesses, partially offset by increased product coverage costs and unfavorable foreign currency fluctuations. The decrease in selling, general and administrative expenses was primarily due to lower discretionary spending in 2013, partially offset by increased compensation and variable compensation expense. The increase in research, development and engineering expenses was primarily due to increased headcount to support our strategic growth initiatives and new product development spending, partially offset by lower consulting expenses.

**2012 vs. 2011*****Acquisition***

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

***Excluding Acquisition***

Selected financial information for our Components segment excluding the impact of the acquisition on 2012 sales and EBIT was as follows:

In millions	Years ended December 31,		Favorable/(Unfavorable)	
			2012 vs. 2011	
	2012	2011	Amount	Percent
<b>Excluding acquisition</b>				
Total sales	\$ 3,966	\$ 4,063	\$ (97)	(2)%
Segment EBIT	434	470	(36)	(8)%
<b>Percentage Points</b>				
Segment EBIT as a percentage of total sales	10.9%	11.6%		(0.7)

***Sales***

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

- Turbo technologies business sales decreased primarily due to a decline in OEM sales in Europe and China, reduced aftermarket demand and unfavorable foreign currency fluctuations, which were partially offset by higher OEM demand in North America in the first half of the year.
- Foreign currency fluctuations unfavorably impacted sales results.
- Filtration business sales decreased primarily as a result of the disposition of certain assets and liabilities of our light-duty filtration business and our exhaust business in 2011 and unfavorable foreign currency fluctuations. Disposition related sales were \$71 million in 2011. The decreases were partially offset by increased aftermarket demand in the first half of the year.
- Fuel systems business sales decreased primarily due to lower European demand and reduced aftermarket demand, which were partially offset by improved demand in North American on-highway markets in the first half of the year.

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



### Segment EBIT

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

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

### Segment EBIT Excluding Acquisition

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

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

### Power Generation Segment Results

Financial data for the Power Generation segment was as follows:

In millions	Years ended December 31,			Favorable/(Unfavorable)			
	2013	2012	2011	2013 vs. 2012		2012 vs. 2011	
	Amount	Amount	Amount	Amount	Percent	Amount	Percent
External sales	\$ 2,154	\$ 2,163	\$ 2,492	\$ (9)	— %	\$ (329)	(13)%
Intersegment sales	877	1,105	1,006	(228)	(21)%	99	10 %
Total sales	3,031	3,268	3,498	(237)	(7)%	(230)	(7)%
Depreciation and amortization	50	47	42	(3)	(6)%	(5)	(12)%
Research, development and engineering expenses	73	76	54	3	4 %	(22)	(41)%
Equity, royalty and interest income from investees	32	40	47	(8)	(20)%	(7)	(15)%
Interest income	6	9	8	(3)	(33)%	1	13 %
Segment EBIT	218	285	373	(67)	(24)%	(88)	(24)%
				Percentage Points		Percentage Points	
Segment EBIT as a percentage of total sales	7.2%	8.7%	10.7%	(1.5)		(2.0)	

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

- **Power products** - Our power products business manufactures generators for commercial and consumer applications ranging from two kilowatts (kW) to one megawatt (MW) under the Cummins Power Generation and Cummins Onan brands.
- **Power systems** - Our power systems business manufactures and sells diesel fuel-based generator sets over one MW, paralleling systems and transfer switches for critical protection and distributed generation applications. We also offer integrated systems that consist of generator sets, power transfer and paralleling switchgear for applications such as data centers, health care facilities and waste water treatment plants.
- **Alternators** - Our alternator business (formally called generator technologies prior to the fourth quarter of 2013) designs, manufactures, sells and services A/C generator/alternator products internally as well as to other generator set assemblers. Our products are sold under the Stamford, AVK and Markon brands and range in output from 0.6 kilovolt-amperes (kVA) to 30,000 kVA.
- **Power solutions** - Our power solutions business provides natural gas fuel-based turnkey solutions for distributed generation and energy management applications in the range of 300-2000 kW products. The business also serves a global rental account for diesel and gas generator sets.

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

In millions	Years ended December 31,			Favorable/(Unfavorable)			
	2013	2012	2011	2013 vs. 2012		2012 vs. 2011	
	Amount	Amount	Amount	Amount	Percent	Amount	Percent
Power products	\$ 1,725	\$ 1,654	\$ 1,636	\$ 71	4 %	\$ 18	1 %
Power systems	656	757	815	(101)	(13)%	(58)	(7)%
Alternators	496	566	673	(70)	(12)%	(107)	(16)%
Power solutions	154	291	374	(137)	(47)%	(83)	(22)%
Total sales	\$ 3,031	\$ 3,268	\$ 3,498	\$ (237)	(7)%	\$ (230)	(7)%

**2013 vs. 2012**

**Sales**

Power Generation segment sales decreased versus 2012, primarily due to lower demand in the power solutions and power systems businesses. The following are the primary drivers by business:

- Power solutions sales decreased primarily due to lower volumes in the U.K., partially offset by increased sales in Asia.
- Power systems sales decreased primarily due to reduced demand in India, the Middle East, China, Asia and Russia, partially offset by increased sales in Western Europe.
- Alternators sales decreased primarily due to demand reductions in Europe, the U.K. and India.

The decreases above were partially offset by power products as sales increased primarily due to higher volumes in North America and improved price realization. These increases were partially offset by demand reductions in India and Asia and unfavorable foreign currency fluctuations.

**Segment EBIT**

Power Generation segment EBIT decreased versus 2012, primarily due to lower gross margin, partially offset by lower selling, general and administrative expenses. Power Generation segment EBIT for 2013 included an \$8 million legal settlement in the third quarter and an \$8 million impairment charge for the write-off of an equity method investment in the fourth quarter, while segment EBIT for 2012 included restructuring and other charges of \$12 million in the fourth quarter. Major components of EBIT and related changes to segment EBIT and EBIT as a percentage of sales were as follows:

Year ended December 31, 2013 vs. 2012

In millions	Favorable/(Unfavorable) Change		
	Amount	Percent	Percentage point change as a percent of sales
Gross margin	\$ (70)	(11)%	(0.9)
Selling, general and administrative expenses	14	4 %	(0.3)
Research, development and engineering expenses	3	4 %	(0.1)
Equity, royalty and interest income from investees	(8)	(20)%	(0.1)

The decrease in gross margin versus 2012 was due to lower volumes, partially offset by improved price realization and favorable foreign currency fluctuations. The decreases in selling, general and administrative expenses and research, development and engineering expenses were primarily due to the absence of restructuring charges incurred in the fourth quarter of last year and lower discretionary spending to align with slowing demand in key markets. The decrease in equity, royalty and interest income from investees was due to an \$8 million impairment charge of an equity method investment in the fourth quarter of 2013.

**2012 vs. 2011**

**Sales**

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

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

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

**Segment EBIT**

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

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

The decrease in gross margin versus 2011 was due to lower volumes, unfavorable foreign currency fluctuations, higher material costs, increased product coverage and restructuring and other charges, which were partially offset by improved price realization. The increase in selling, general and administrative expenses was primarily due to increased headcount to support our strategic growth initiatives, partially offset by lower discretionary spending in the second half of 2012 to align with slowing demand in key markets. The increase in research, development and engineering expenses was primarily due to increased headcount to support our strategic growth initiatives and new product development spending. Equity, royalty and interest income from investees decreased primarily due to lower profitability at Cummins Olayan Energy Ltd. and Chongqing Cummins Engine Company, Ltd.



**2013 vs. 2012****Sales**

Distribution segment sales increased versus 2012 primarily due to \$507 million of incremental sales in 2013 related to the acquisition of partially-owned North American distributors since June 2012. The acquisition-related sales by product were as follows:

- \$236 million for the parts and filtration business,
- \$94 million for the engine business,
- \$117 million for the power generation business, and
- \$60 million for the service business.

These increases were partially offset by decreased engine product sales, primarily due to a significant slowdown in the North American oil and gas markets, and by unfavorable foreign currency fluctuations. Excluding acquisition related sales, all other changes by product line were relatively flat versus 2012.

**Segment EBIT**

Major components of EBIT and related changes to segment EBIT and EBIT as a percentage of sales were as follows:

In millions	Year ended December 31, 2013 vs. 2012		
	Favorable/(Unfavorable) Change		
	Amount	Percent	Percentage point change as a percent of sales
Gross margin	\$ 86	13 %	(0.4)
Selling, general and administrative expenses	(41)	(8)%	0.9
Equity, royalty and interest income from investees	(23)	(12)%	(1.3)

Distribution segment EBIT increased versus 2012, primarily due to higher gross margin as a result of the acquisition and consolidation of partially owned North American distributors in 2013. This increase was partially offset by unfavorable foreign currency fluctuations, higher selling, general and administrative expenses and lower equity, royalty and interest income from investees as a result of the acquisitions. Amortization of intangible assets related to these acquisitions also negatively impacted EBIT for 2013. These acquisitions resulted in a \$12 million gain related to the remeasurement of our pre-existing ownership interest in 2013, compared to a \$7 million gain related to the remeasurement of our pre-existing 35 percent ownership in Central Power in 2012. Distribution segment EBIT also included restructuring and other charges of \$14 million in the fourth quarter of 2012.

**2012 vs. 2011****Sales**

The 2012 Central Power acquisition related sales by product were \$61 million for the parts and filtration business, \$52 million for the engine business, \$28 million for the power generation business, and \$18 million for the service business. Distribution segment sales, excluding acquisition related sales of \$159 million, increased versus 2011 due to higher demand in the parts and filtration, power generation and service businesses, partially offset by lower demand in the engine business. The following were the primary drivers by line of business:

- Parts and filtration product sales increased primarily due to higher demand in North and Central America and the Middle East.
- Power generation product sales increased primarily due to growth in East Asia and improved demand in the South Pacific, which were partially offset by a reduction in nonrecurring project-related sales in the Middle East.
- Service revenue increased primarily due to higher demand from mining customers in the South Pacific and higher volumes in East Asia and Europe.

The increases above were partially offset by the following:

- Foreign currency fluctuations unfavorably impacted sales results.

- Engine product sales decreased primarily due to a significant slowdown in the North American oil and gas markets and lower demand in Europe as a result of pre-buy activity in the second half of 2011 ahead of the 2012 emissions change for certain construction engines, which were partially offset by growth in East Asia.

**Segment EBIT**

Distribution segment EBIT decreased versus 2011, primarily due to higher selling, general and administrative expenses and higher research, development and engineering expenses, which were partially offset by higher equity, royalty and interest income from investees and higher gross margin. Distribution segment EBIT for 2012 included restructuring and other charges of \$14 million in the fourth quarter. Major components of EBIT and related changes to segment EBIT and EBIT as a percentage of sales were as follows:

In millions	Year ended December 31, 2012 vs. 2011		
	Favorable/(Unfavorable) Change		
	Amount	Percent	Percentage point change as a percent of sales
<b>Including acquisitions</b>			
Gross margin	\$ 11	2 %	(1.2)
Selling, general and administrative expenses	(46)	(10)%	(0.3)
Research, development and engineering expenses	(3)	(100)%	(0.1)
Equity, royalty and interest income from investees	16	9 %	—
<b>Excluding acquisitions</b>			
Gross margin	(18)	(3)%	(1.1)
Selling, general and administrative expenses	(23)	(5)%	(0.4)

**Segment EBIT Excluding Acquisitions**

The decrease in gross margin versus 2011 was primarily due to unfavorable foreign currency impacts, unfavorable variations in geographic mix and restructuring and other charges, which were partially offset by higher volumes in most products. The increase in selling, general and administrative expenses was primarily due to increased headcount to support our strategic growth initiatives launched prior to a number of markets unexpectedly slowing in mid-2012, partially offset by decreased variable compensation expense and lower discretionary spending in the second half of 2012. The increase in research, development and engineering expenses was mainly due to increased headcount to support our strategic growth initiatives. The increase in equity, royalty and interest income from investees was primarily due to increased income from North American distributors.

**Reconciliation of Segment EBIT to Income Before Income Taxes**

The table below reconciles the segment information to the corresponding amounts in the *Consolidated Statements of Income*.

In millions	Years ended December 31,		
	2013	2012	2011
Total segment EBIT	\$ 2,174	\$ 2,328	\$ 2,613
Non-segment EBIT <sup>(1)</sup>	(14)	(25)	102
Total EBIT	2,160	2,303	2,715
Less: Interest expense	41	32	44
Income before income taxes	\$ 2,119	\$ 2,271	\$ 2,671

(1) Includes intersegment sales and profit in inventory eliminations and unallocated corporate expenses. The year ended December 31, 2012, included a \$6 million gain (\$4 million after-tax) related to adjustments from our 2011 divestitures and a \$20 million charge (\$12 million after-tax) related to legal matters. The year ended December 31, 2011, included a \$68 million gain (\$37 million after-tax) and a \$53 million gain (\$33 million after-tax) related to the Component segment sales of certain assets and liabilities from our exhaust and light-duty filtration businesses, respectively, and a \$38 million gain (\$24 million after-tax) related to the insurance settlement regarding the June 2008 flood in Southern Indiana. The gains and losses have been excluded from segment results as they were not considered in our evaluation of operating results for the years ended December 31, 2012 and 2011.

(2) Depreciation and amortization as shown on a segment basis excludes the amortization of debt discount and deferred costs that are included in the *Consolidated Statements of Income* as "Interest expense."

## LIQUIDITY AND CAPITAL RESOURCES

### Management's Assessment of Liquidity

Our financial condition and liquidity remain strong. Our solid balance sheet and credit ratings enable us to have ready access to credit and the capital markets.

As a well-known seasoned issuer, we filed an automatic shelf registration for an undetermined amount of debt and equity securities with the Securities and Exchange Commission on September 16, 2013. Under this shelf registration we may offer, from time to time, debt securities, common stock, preferred and preference stock, depository shares, warrants, stock purchase contracts and stock purchase units.

In September 2013, we issued \$1 billion aggregate principal amount of senior notes consisting of \$500 million aggregate principal amount of 3.65% senior unsecured notes due in 2023 and \$500 million aggregate principal amount of 4.875% senior unsecured notes due in 2043. We received net proceeds of \$979 million. The senior notes pay interest semi-annually on April 1 and October 1, commencing on April 1, 2014. The indenture governing the senior notes contains covenants that, among other matters, limit (i) our ability to consolidate or merge into, or sell, assign, convey, lease, transfer or otherwise dispose of all or substantially all of our and our subsidiaries' assets to another person, (ii) our and certain of our subsidiaries' ability to create or assume liens and (iii) our and certain of our subsidiaries' ability to engage in sale and leaseback transactions. We currently anticipate using a portion of the net proceeds from the sale of the notes for the planned acquisitions of the equity that we do not already own in our partially-owned United States and Canadian distributors, as well as for general corporate purposes. We plan to spend approximately \$400 million to \$500 million on distributor acquisitions and refinancings in 2014.

We assess our liquidity in terms of our ability to generate adequate cash to fund our operating, investing and financing activities. We generate significant ongoing cash flow, which has been used, in part, to fund capital expenditures, pay dividends on our common stock, fund repurchases of common stock and make acquisitions. Cash provided by operations is our principal source of liquidity. As of December 31, 2013, other sources of liquidity included:

- cash and cash equivalents of \$2.7 billion, of which approximately 53 percent was located in the U.S. and 47 percent was located outside the U.S., primarily in the U.K., China and Singapore,
- marketable securities of \$150 million, which were located in India and the U.S. and the majority of which could be liquidated into cash within a few days,
- revolving credit facility with \$1.7 billion available, net of outstanding letters of credit and
- international and other domestic short-term credit facilities with \$310 million available.

We believe our liquidity provides us with the financial flexibility needed to fund working capital, capital expenditures, projected pension obligations, dividend payments, common stock repurchases, acquisitions and debt service obligations. We continue to generate cash from operations in the U.S. and maintain access to \$1.7 billion of our revolver as noted above.

Our revolving credit agreement provides us with a \$1.75 billion unsecured revolving credit facility, the proceeds of which are to be used for our general corporate purposes. See Note 10, "DEBT" to our *Consolidated Financial Statements* for further information. The credit agreement includes one financial covenant: a leverage ratio. The required leverage ratio, which measures the sum of total debt plus securitization financing to consolidated earnings before interest, taxes, depreciation and amortization (EBITDA) for the four fiscal quarters may not exceed 3.25 to 1.0. At December 31, 2013, our leverage ratio was 0.70 to 1.0.

A significant portion of our cash flows is generated outside the U.S. As of December 31, 2013, the total of cash, cash equivalents and marketable securities held by foreign subsidiaries was \$1.4 billion, the vast majority of which was located in the U.K., China, Singapore and India. The geographic location of our cash and marketable securities aligns well with our business growth strategy. We manage our worldwide cash requirements considering available funds among the many subsidiaries through which we conduct our business and the cost effectiveness with which those funds can be accessed. As a result, we do not anticipate any local liquidity restrictions to preclude us from funding our targeted expansion or operating needs with local resources.

If we distribute our foreign cash balances to the U.S. or to other foreign subsidiaries, we could be required to accrue and pay U.S. taxes. For example, we would be required to accrue and pay additional U.S. taxes if we repatriated cash from certain foreign subsidiaries whose earnings we have asserted are permanently reinvested outside of the U.S. Foreign earnings for which we assert permanent reinvestment outside the U.S. consist primarily of earnings of our China and U.K. domiciled subsidiaries. At present, we do not foresee a need to repatriate any earnings from these subsidiaries for which we have asserted

[Table of Contents](#)

permanent reinvestment. However, to help fund cash needs of the U.S. or other international subsidiaries as they arise, we repatriate available cash from certain foreign subsidiaries whose earnings are not permanently reinvested when it is cost effective to do so. Earnings generated after 2011 from our China operations are considered permanently reinvested, while earnings generated prior to 2012, for which U.S. deferred tax liabilities have been recorded, are expected to be repatriated in future years.

The maturity schedule of our existing long-term debt does not require significant cash outflows in the intermediate term. Required annual principal payments range from \$8 million to \$82 million over each of the next five years.

### Working Capital Summary

We fund our working capital with cash from operations and short-term borrowings when necessary. Various assets and liabilities, including short-term debt, can fluctuate significantly from month to month depending on short-term liquidity needs. As a result, working capital is a prime focus of management attention.

In millions	2013	2012	Change 2013 vs 2012	
			Amount	Percent
Cash and cash equivalents	\$ 2,699	\$ 1,369	\$ 1,330	97 %
Marketable securities	150	247	(97)	(39)%
Accounts and notes receivable, net	2,649	2,475	174	7 %
Inventories	2,381	2,221	160	7 %
Prepaid expenses and other current assets	760	855	(95)	(11)%
Current assets	8,639	7,167	1,472	21 %
Current maturity of long-term debt, accounts and loans payable	1,625	1,416	209	15 %
Current portion of accrued product warranty	360	386	(26)	(7)%
Accrued compensation, benefits and retirement costs	433	400	33	8 %
Taxes payable (including taxes on income)	99	173	(74)	(43)%
Other accrued expenses	851	761	90	12 %
Current liabilities	3,368	3,136	232	7 %
Working capital	\$ 5,271	\$ 4,031		
Current ratio	2.57	2.29		
Days' sales in receivables	54	53		
Inventory turnover	5.4	5.7		

Current assets increased 21 percent compared to 2012, primarily due to increases in cash and cash equivalents as a result of the \$1 billion debt issuance in September 2013, accounts and notes receivable and inventories, partially offset by a decline in marketable securities and a decline in other current assets (primarily related to refundable income taxes received in the first quarter of 2013).

Current liabilities increased 7 percent compared to 2012, primarily due to an increase in accounts payable trade and an increase in other accrued expenses, partially offset by a decrease in taxes payable.

Inventory turnover decreased 0.3 turns compared to 2012. The decrease was primarily due to inventory acquired as part of the acquisitions of Rocky Mountain and Northwest in 2013.

### Cash Flows

Cash and cash equivalents increased \$1,330 million during the year ended December 31, 2013, compared to a decrease of \$115 million during the comparable period in 2012. The change in cash and cash equivalents was as follows:



**Operating Activities**

In millions	Years ended December 31,			Change	
	2013	2012	2011	2013 vs. 2012	2012 vs. 2011
Consolidated net income	\$ 1,588	\$ 1,738	\$ 1,946	\$ (150)	\$ (208)
Restructuring and other charges and credits, net of cash payments	(25)	27	—	(52)	27
Depreciation and amortization	407	361	325	46	36
Gain on sale of businesses	—	(6)	(121)	6	115
Gain on sale of equity investment	—	(13)	—	13	(13)
Gain on fair value adjustment for consolidated investees	(12)	(7)	—	(5)	(7)
Deferred income taxes	100	116	85	(16)	31
Equity in income of investees, net of dividends	(62)	(15)	(23)	(47)	8
Pension contributions in excess of expense	(82)	(68)	(131)	(14)	63
Other post-retirement benefits payments in excess of expense	(25)	(21)	(31)	(4)	10
Stock-based compensation expense	37	36	42	1	(6)
Excess tax benefits on stock-based awards	(13)	(14)	(5)	1	(9)
Translation and hedging activities	17	—	4	17	(4)
Changes in current assets and liabilities, net of acquisitions and divestitures					
Accounts and notes receivable	(148)	87	(350)	(235)	437
Inventories	(46)	(32)	(225)	(14)	193
Other current assets	212	(60)	(21)	272	(39)
Accounts payable	163	(256)	208	419	(464)
Accrued expenses	(246)	(514)	234	268	(748)
Changes in other liabilities and deferred revenue	211	214	139	(3)	75
Other, net	13	(41)	(3)	54	(38)
Net cash provided by operating activities	<u>\$ 2,089</u>	<u>\$ 1,532</u>	<u>\$ 2,073</u>	<u>\$ 557</u>	<u>\$ (541)</u>

**2013 vs. 2012**

Net cash provided by operating activities increased versus 2012 primarily due to favorable working capital fluctuations, partially offset by lower consolidated net income and lower dividends received from equity investees. During 2013, the net increase in working capital resulted in a cash outflow of \$65 million compared to a cash outflow of \$775 million in 2012. This change of \$710 million was primarily driven by an increase in accounts payable due to timing differences, lower net tax payments of \$311 million due to the receipt of income tax refunds in 2013, which were partially offset by tax payments, and a smaller decrease in accrued expenses, partially offset by an increase in accounts and notes receivable in 2013 as a result of higher sales in the fourth quarter of 2013 versus 2012.

**Pensions**

The funded status of our pension plans is dependent upon a variety of variables and assumptions including return on invested assets, market interest rates and levels of voluntary contributions to the plans. In 2013, the investment return on our U.S. pension trust was 7.6 percent while our U.K. pension trust return was 10.9 percent. Approximately 77 percent of our pension plan assets are invested in highly liquid investments such as fixed income and equity securities. The remaining 23 percent of our plan assets are invested in less liquid, but market valued investments, including real estate, private equity and insurance contracts. We made \$169 million of pension contributions in 2013, including \$112 million of voluntary contributions. Claims and premiums for other postretirement benefits approximated \$48 million, net of reimbursements, in 2013. These contributions and payments include payments from our funds either to increase pension plan assets or to make direct payments to plan participants. We anticipate making total contributions of \$205 million to our defined benefit pension plans in 2014. Expected contributions to our defined benefit pension plans in 2014 will meet or exceed the current funding requirements.

**2012 vs. 2011**

Net cash provided by operating activities decreased versus 2011 primarily due to unfavorable working capital fluctuations and lower consolidated net income, which were partially offset by a lower non-cash gain on disposition of certain assets and liabilities of our exhaust business and our light-duty filtration business in 2012. During 2012, the net increase in working capital resulted in a cash outflow of \$775 million compared to a cash outflow of \$154 million in 2011. This change of \$621 million was primarily driven by lower accrued expenses and a decrease in accounts payable, as volumes dropped in the second half of the year, and higher cash tax payments of approximately \$159 million. These were partially offset by a decrease in accounts and notes receivable and a smaller increase in inventory in 2012.

**Investing Activities**

In millions	Years ended December 31,			Change	
	2013	2012	2011	2013 vs. 2012	2012 vs. 2011
Capital expenditures	\$ (676)	\$ (690)	\$ (622)	\$ 14	\$ (68)
Investments in internal use software	(64)	(87)	(60)	23	(27)
Proceeds from disposals of property, plant and equipment	14	11	8	3	3
Investments in and advances to equity investees	(42)	(70)	(81)	28	11
Acquisitions of businesses, net of cash acquired	(147)	(215)	—	68	(215)
Proceeds from sale of businesses, net of cash sold	—	10	199	(10)	(189)
Investments in marketable securities—acquisitions	(418)	(561)	(729)	143	168
Investments in marketable securities—liquidations	525	585	750	(60)	(165)
Proceeds from sale of equity investment	—	23	—	(23)	23
Purchases of other investments	(40)	—	—	(40)	—
Cash flows from derivatives not designated as hedges	1	12	(18)	(11)	30
Other, net	1	—	1	1	(1)
Net cash used in investing activities	\$ (846)	\$ (982)	\$ (552)	\$ 136	\$ (430)

**2013 vs. 2012**

Net cash used in investing activities decreased versus 2012 primarily due to lower net investments in marketable securities, lower cash investments in acquisitions of businesses and lower investments in and advances to equity investees, partially offset by purchases of corporate owned life insurance.

On September 17, 2013, we announced our intention to acquire the equity that we do not already own in most of our partially-owned United States and Canadian distributors over the next three to five years. We plan to spend approximately \$400 million to \$500 million on distributor acquisitions and refinancing in 2014.

Capital expenditures were \$676 million in 2013 compared to \$690 million in 2012. Despite the challenging economies around the world, we continue to invest in new product lines and targeted capacity expansions. We plan to spend between \$700 million and \$800 million in 2014 as we continue with product launches and facility improvements and prepare for future emission standards. Over 50 percent of our capital expenditures are expected to be invested outside of the U.S. in 2014. As of December 31, 2013, we have committed to invest an additional \$52 million in existing joint ventures, of which the entire amount is expected to be funded in 2014.

**2012 vs. 2011**

Net cash used in investing activities increased versus 2011 primarily due to cash investments for the acquisitions of Hilite and Central Power, proceeds from the 2011 disposition of certain assets and liabilities of our exhaust business and light-duty filtration business, which did not repeat in 2012, and increased capital expenditures.

**Financing Activities**

In millions	Years ended December 31,			Change	
	2013	2012	2011	2013 vs. 2012	2012 vs. 2011
Proceeds from borrowings	\$ 1,004	\$ 64	\$ 127	\$ 940	\$ (63)
Payments on borrowings and capital lease obligations	(90)	(145)	(237)	55	92
Net borrowings under short-term credit agreements	(3)	11	6	(14)	5
Distributions to noncontrolling interests	(75)	(62)	(56)	(13)	(6)
Dividend payments on common stock	(420)	(340)	(255)	(80)	(85)
Repurchases of common stock	(381)	(256)	(629)	(125)	373
Excess tax benefits on stock-based awards	13	14	5	(1)	9
Other, net	4	20	14	(16)	6
Net cash provided by (used in) financing activities	\$ 52	\$ (694)	\$ (1,025)	\$ 746	\$ 331

**2013 vs. 2012**

In September 2013, we issued \$1 billion aggregate principal amount of senior notes consisting of \$500 million aggregate principal amount of 3.65% senior unsecured notes due in 2023 and \$500 million aggregate principal amount of 4.875% senior unsecured notes due in 2043. Net proceeds from the issuance were \$979 million.

Net cash provided by financing activities increased versus 2012 primarily due to proceeds from the issuance of senior notes and lower payments on borrowings and capital lease obligations, partially offset by higher repurchases of common stock and higher dividend payments.

Our total debt was \$1.7 billion as of December 31, 2013, compared with \$775 million as of December 31, 2012. Total debt as a percent of our total capital, including total long-term debt, was 18.1 percent at December 31, 2013, compared with 10.0 percent at December 31, 2012.

**2012 vs. 2011**

Net cash used in financing activities decreased versus 2011 primarily due to significantly lower repurchases of common stock and decreased payments on borrowings and capital lease obligations, which were partially offset by higher dividend payments and decreased proceeds from borrowings.

Our total debt was \$775 million as of December 31, 2012, compared with \$783 million as of December 31, 2011. Total debt as a percent of our total capital, including total long-term debt, was 10.0 percent at December 31, 2012, compared with 11.8 percent at December 31, 2011.

**Repurchase of Common Stock**

In December 2007, the Board of Directors authorized the acquisition of up to \$500 million of our common stock, which was completed in February 2011. Repurchases under this plan by year were as follows:

In millions (except per share amounts)	Shares Purchased	Average Cost Per Share	Total Cost of Repurchases	Remaining Authorized Capacity
2008	2.3	\$ 55.49	\$ 128	372
2009	0.4	46.52	20	352
2010	3.5	68.57	241	111
2011	1.1	104.47	111	—
Total	7.3		\$ 500	

In February 2011, the Board of Directors approved a new share repurchase program and authorized the acquisition of up to \$1 billion of our common stock upon completion of the \$500 million program. Under this authorization, we repurchased \$518 million of shares in 2011 and \$256 million of shares in 2012. In December 2012, the Board of Directors authorized the acquisition of up to \$1 billion of additional common stock upon completion of the 2011 repurchase plan. In 2013, we made the following quarterly purchases under the repurchase programs indicated:

In millions (except per share amounts) For each quarter ended	Shares Purchased	Average Cost Per Share	Total Cost of Repurchases	Remaining Authorized Capacity
<b>February 2011, \$1 billion repurchase program</b>				
March 31	—	\$ —	\$ —	\$ 226
June 30	2.0	113.44	226	—
Subtotal	2.0	\$ 113.44	\$ 226	\$ —
<b>December 2012, \$1 billion repurchase program</b>				
June 30	0.6	\$ 107.74	\$ 63	\$ 937
September 29	—	—	—	937
December 31	0.7	129.18	92	845
Subtotal	1.3	119.54	\$ 155	\$ 845
Total	3.3	\$ 115.85	\$ 381	\$ 845

**Quarterly Dividends**

In July 2013, the Board of Directors authorized a 25 percent increase to our quarterly cash dividend on our common stock from \$0.50 per share to \$0.625 per share. In July 2012, the Board of Directors authorized a 25 percent increase to our quarterly cash dividend on our common stock from \$0.40 per share to \$0.50 per share. In July 2011, the Board of Directors approved a 52 percent increase to our quarterly cash dividend on our common stock from \$0.2625 per share to \$0.40 per share. Cash dividends per share paid to common shareholders for the last three years were as follows:

	Quarterly Dividends		
	2013	2012	2011
First quarter	\$ 0.50	\$ 0.40	\$ 0.2625
Second quarter	0.50	0.40	0.2625
Third quarter	0.625	0.50	0.40
Fourth quarter	0.625	0.50	0.40
Total	\$ 2.25	\$ 1.80	\$ 1.325

Total dividends paid to common shareholders in 2013, 2012 and 2011 were \$420 million, \$340 million and \$255 million respectively. Declaration and payment of dividends in the future depends upon our income and liquidity position, among other factors, and is subject to declaration by our Board of Directors, who meet quarterly to consider our dividend payment. We expect to fund dividend payments with cash from operations.

**Credit Ratings**

A number of our contractual obligations and financing agreements, such as our revolving credit facility have restrictive covenants and/or pricing modifications that may be triggered in the event of downward revisions to our corporate credit rating. There were no downgrades of our credit ratings in 2013 that have impacted these covenants or pricing modifications. In October 2012, Fitch Ratings upgraded our ratings to 'A' and changed our outlook to stable. In April 2013, Moody's Investors Service, Inc. raised our rating to 'A3' and changed our outlook to stable. Standard & Poor's Rating Services, Fitch Ratings and Moody's Investors Service, Inc. confirmed our credit ratings as 'A', 'A' and 'A3', respectively, subsequent to the third quarter issuance of \$1 billion in senior notes.

Credit ratings are not recommendations to buy, are subject to change and each rating should be evaluated independently of any other rating. In addition, we undertake no obligation to update disclosures concerning our credit ratings, whether as a result of new information, future events or otherwise. Our ratings and outlook from each of the credit rating agencies as of the date of filing are shown in the table below.

Credit Rating Agency	Senior L-T Debt Rating	Outlook
Standard & Poor's Rating Services	A	Stable
Fitch Ratings	A	Stable
Moody's Investors Service, Inc.	A3	Stable

**CONTRACTUAL OBLIGATIONS AND OTHER COMMERCIAL COMMITMENTS**

A summary of payments due for our contractual obligations and commercial commitments, as of December 31, 2013, is shown in the tables below:

**Contractual Cash Obligations**

In millions	2014	2015-2016	2017-2018	After 2018	Total
Loans payable	\$ 17	\$ —	\$ —	\$ —	\$ 17
Long-term debt and capital lease obligations <sup>(1)</sup>	149	327	194	3,091	3,761
Operating leases	171	189	98	111	569
Capital expenditures	350	104	—	—	454
Purchase commitments for inventory	578	—	—	—	578
Other purchase commitments	215	117	20	13	365
Pension funding <sup>(2)</sup>	88	93	—	—	181
Other postretirement benefits	43	79	69	207	398
Total	\$ 1,611	\$ 909	\$ 381	\$ 3,422	\$ 6,323

<sup>(1)</sup> Includes principal payments and expected interest payments based on the terms of the obligations

<sup>(2)</sup> We are contractually obligated in the U.K. to fund \$88 million in 2014 and \$93 million in 2015; however, our expected total pension contributions for 2014, including the U.K., is approximately \$205 million.

The contractual obligations reported above exclude our unrecognized tax benefits of \$169 million as of December 31, 2013. We are not able to reasonably estimate the period in which cash outflows relating to uncertain tax contingencies could occur. See Note 4, "INCOME TAXES," to the *Consolidated Financial Statements* for further details.

Our other commercial commitments as of December 31, 2013, are as follows

**Other Commercial Commitments**

In millions	2014	2015-2016	2017-2018	After 2018	Total
Standby letters of credit under revolving credit agreements	\$ 23	\$ —	\$ —	\$ —	\$ 23
International and other domestic letters of credit	34	8	4	3	49
Performance and excise bonds	61	5	—	—	66
Guarantees, indemnifications and other commitments	6	—	—	—	6
Total	\$ 124	\$ 13	\$ 4	\$ 3	\$ 144

**APPLICATION OF CRITICAL ACCOUNTING ESTIMATES**

A summary of our significant accounting policies is included in Note 1, "SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES" of our *Consolidated Financial Statements* which discusses accounting policies that we have selected from acceptable alternatives.

Our *Consolidated Financial Statements* are prepared in accordance with GAAP which often requires management to make judgments, estimates and assumptions regarding uncertainties that affect the reported amounts presented and disclosed in the financial statements. Management reviews these estimates and assumptions based on historical experience, changes in business conditions and other relevant factors they believe to be reasonable under the circumstances. In any given reporting period, our actual results may differ from the estimates and assumptions used in preparing our *Consolidated Financial Statements*.

Critical accounting estimates are defined as follows: the estimate requires management to make assumptions about matters that were highly uncertain at the time the estimate was made; different estimates reasonably could have been used; or if changes in the estimate are reasonably likely to occur from period to period and the change would have a material impact on our financial condition or results of operations. Our senior management has discussed the development and selection of our accounting policies, related accounting estimates and the disclosures set forth below with the Audit Committee of our Board of Directors. We believe our critical accounting estimates include those addressing the estimation of liabilities for warranty programs, accounting for income taxes and pension benefits.

## Warranty Programs

We estimate and record a liability for base warranty programs at the time our products are sold. Our estimates are based on historical experience and reflect management's best estimates of expected costs at the time products are sold and subsequent adjustment to those expected costs when actual costs differ. As a result of the uncertainty surrounding the nature and frequency of product recall programs, the liability for such programs is recorded when we commit to a recall action or when a recall becomes probable and estimable, which generally occurs when it is announced. Our warranty liability is generally affected by component failure rates, repair costs and the point of failure within the product life cycle. Future events and circumstances related to these factors could materially change our estimates and require adjustments to our liability. New product launches require a greater use of judgment in developing estimates until historical experience becomes available. Product specific experience is typically available four or five quarters after product launch, with a clear experience trend evident eight quarters after launch. We generally record warranty expense for new products upon shipment using a preceding product's warranty history and a multiplicative factor based upon preceding similar product experience and new product assessment until sufficient new product data is available for warranty estimation. We then use a blend of actual new product experience and preceding product historical experience for several subsequent quarters, and new product specific experience thereafter. Note 11, "PRODUCT WARRANTY LIABILITY," to our *Consolidated Financial Statements* contains a summary of the activity in our warranty liability account for 2013 and 2012 including adjustments to pre-existing warranties.

## Accounting for Income Taxes

We determine our income tax expense using the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax effects of temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax benefits of tax loss and credit carryforwards are also recognized as deferred tax assets. We evaluate the recoverability of our deferred tax assets each quarter by assessing the likelihood of future profitability and available tax planning strategies that could be implemented to realize our net deferred tax assets. At December 31, 2013, we recorded net deferred tax assets of \$177 million. These assets included \$187 million for the value of tax loss and credit carryforwards. A valuation allowance of \$101 million was recorded to reduce the tax assets to the net value management believed was more likely than not to be realized. In the event our operating performance deteriorates, future assessments could conclude that a larger valuation allowance will be needed to further reduce the deferred tax assets. In addition, we operate within multiple taxing jurisdictions and are subject to tax audits in these jurisdictions. These audits can involve complex issues, which may require an extended period of time to resolve. We reduce our net tax assets for the estimated additional tax and interest that may result from tax authorities disputing uncertain tax positions we have taken and we believe we have made adequate provision for income taxes for all years that are subject to audit based upon the latest information available. A more complete description of our income taxes and the future benefits of our tax loss and credit carryforwards is disclosed in Note 4, "INCOME TAXES," to our *Consolidated Financial Statements*.

## Pension Benefits

We sponsor a number of pension plans primarily in the U.S. and the U.K. and to a lesser degree in various other countries. In the U.S. and the U.K. we have several major defined benefit plans that are separately funded. We account for our pension programs in accordance with employers' accounting for defined benefit pension and other postretirement plans under GAAP. GAAP requires that amounts recognized in financial statements be determined using an actuarial basis. As a result, our pension benefit programs are based on a number of statistical and judgmental assumptions that attempt to anticipate future events and are used in calculating the expense and liability related to our plans each year at December 31. These assumptions include discount rates used to value liabilities, assumed rates of return on plan assets, future compensation increases, employee turnover rates, actuarial assumptions relating to retirement age, mortality rates and participant withdrawals. The actuarial assumptions we use may differ significantly from actual results due to changing economic conditions, participant life span and withdrawal rates. These differences may result in a material impact to the amount of net periodic pension cost to be recorded in our *Consolidated Financial Statements* in the future.

The expected long-term return on plan assets is used in calculating the net periodic pension cost. We considered several factors in developing our expected rate of return on plan assets. The long-term rate of return considers historical returns and expected returns on current and projected asset allocations and is generally applied to a five-year average market value of return. Projected returns are based primarily on broad, publicly traded fixed income and equity indices and forward-looking estimates of active portfolio and investment management. As of December 31, 2013, based upon our target asset allocations, it is anticipated that our U.S. investment policy will generate an average annual return over the 10-year projection period equal to or in excess of 7.5 percent approximately 30 percent of the time while returns of 8.0 percent or greater are anticipated 25 percent of the time. We expect additional positive returns from active investment management. The 2013 one-year return of 7.6 percent, combined with the very favorable returns in 2012, has eliminated the significant deterioration in pension assets

experienced in 2008 as a result of the credit crisis and related market recession. Based on the historical returns and forward-looking return expectations, we believe an investment return assumption of 7.5 percent per year in 2014 for U.S. pension assets is reasonable.

The methodology used to determine the rate of return on pension plan assets in the U.K. was based on establishing an equity-risk premium over current long-term bond yields adjusted based on target asset allocations. As of December 31, 2013, based upon our target asset allocations, it is anticipated that our U.K. investment policy will generate an average annual return over the 20-year projection period equal to or in excess of 5.6 percent approximately 50 percent of the time while returns of 6.5 percent or greater are anticipated 25 percent of the time. We expect additional positive returns from active investment management. The one-year return for our U.K. plan was 10.9 percent for 2013, and similar to our U.S. plan, the 2008 market related deterioration in our plan assets has been eliminated. Our strategy with respect to our investments in pension plan assets is to be invested with a long-term outlook. Therefore, the risk and return balance of our asset portfolio should reflect a long-term horizon. Based on the historical returns and forward-looking return expectations, we believe an investment return assumption of 5.8 percent in 2014 for U.K. pension assets is reasonable. Our pension plan asset allocations at December 31, 2013 and 2012 and target allocation for 2014 are as follows:

Investment description	U.S. Plans			U.K. Plans		
	Target Allocation	Percentage of Plan Assets at December 31,		Target Allocation	Percentage of Plan Assets at December 31,	
	2014	2013	2012	2014	2013	2012
Fixed income	64.0%	57.0%	47.5%	45.0%	43.7%	46.0%
Equity securities	22.0%	35.5%	40.1%	30.5%	43.2%	43.0%
Real estate/other	14.0%	7.5%	12.4%	24.5%	13.1%	11.0%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

The differences between the actual return on plan assets and expected long-term return on plan assets are recognized in the asset value used to calculate net periodic expense over five years. The table below sets forth the expected return assumptions used to develop our pension cost for the period 2011-2013 and our expected rate of return for 2014.

	Long-term Expected Return Assumptions			
	2014	2013	2012	2011
U.S. plans	7.50%	8.00%	8.00%	8.00%
U.K. plans	5.80%	5.80%	6.50%	7.00%

A lower expected rate of return will increase our net periodic pension cost and reduce profitability.

GAAP for pensions offers various acceptable alternatives to account for the differences that eventually arise between the estimates used in the actuarial valuations and the actual results. It is acceptable to delay or immediately recognize these differences. Under the delayed recognition alternative, changes in pension obligation (including those resulting from plan amendments) and changes in the value of assets set aside to meet those obligations are not recognized in net periodic pension cost as they occur but are recognized initially in comprehensive income and subsequently amortized as components of net periodic pension cost systematically and gradually over future periods. In addition to this approach, GAAP also allows immediate recognition of actuarial gains or losses. Immediate recognition introduces volatility in financial results. We have chosen to delay recognition and amortize actuarial differences over future periods. If we adopted the immediate recognition approach, we would record a loss of \$838 million (\$579 million after-tax) from cumulative actuarial net losses for our U.S. and U.K. pension plans.

The difference between the expected return and the actual return on plan assets is deferred from recognition in our results of operations and, under certain circumstances such as when the difference exceeds 10 percent of the market value of plan assets or the projected benefit obligation (PBO), amortized over future years of service. This is also true of changes to actuarial assumptions. As of December 31, 2013, we had net pension actuarial losses of \$478 million and \$361 million for the U.S. and U.K. pension plans, respectively. Under GAAP, the actuarial gains and losses are recognized and recorded in accumulated other comprehensive loss. Net actuarial gains increased our shareholders' equity by \$102 million (after-tax) in 2013. The gains were due to a liability gain from a higher U.S. discount rate and improved plan asset performance for the U.K. plan, partially offset by U.K. liability losses from a higher inflation assumption and a lower discount rate. As these amounts exceed 10 percent of our PBO, the excess is amortized over the average remaining service lives of participating employees.

The table below sets forth the net periodic pension cost for the period 2011-2013 and our expected cost for 2014.

In millions	2014	2013	2012	2011
Net periodic pension cost	\$ 57	\$ 87	\$ 64	\$ 68

We expect 2014 net periodic pension cost to decrease significantly over 2013, due to reduced loss amortizations resulting from improved U.S. asset performance and a higher discount rate. The increase in periodic pension cost in 2013 compared to 2012 was due to unfavorable impacts of higher service cost due to increased headcount, decreased discount rates and lower expected asset returns for our U.K. plan as we de-risk plan trust assets moving toward more conservative investments. The decrease in periodic pension cost in 2012 compared to 2011 was due to improved returns on assets and strong contributions in 2011. Another key assumption used in the development of the net periodic pension cost is the discount rate. The weighted average discount rates used to develop our net periodic pension cost are set forth in the table below.

	Discount Rates			
	2014	2013	2012	2011
U.S. plans	4.83%	3.97%	4.82%	5.42%
U.K. plans	4.60%	4.70%	5.20%	5.80%

Changes in the discount rate assumptions will impact the interest cost component of the net periodic pension cost calculation.

The discount rate enables us to state expected future cash payments for benefits as a present value on the measurement date. The guidelines for setting this rate are discussed in GAAP which suggests the use of a high-quality corporate bond rate. We used bond information provided by Moody's Investor Service Inc., Standard & Poor's Rating Services, Fitch Ratings and Dominion Bond Rating. All bonds used to develop our hypothetical portfolio in the U.S. and U.K. were high-quality, non-callable bonds (Aa or better) as of December 31, 2013, by at least two of the bond rating agencies. The average yield of this hypothetical bond portfolio was used as the benchmark for determining the discount rate to be used to value the obligations of the plans subject to GAAP for pensions and other postretirement benefits.

Our model called for projected payments until current participants have received payment of benefits over a period of approximately 80 years in the U.S. and U.K. For both countries, our model matches the present value of the plan's projected benefit payments to the market value of the theoretical settlement bond portfolio. A single equivalent discount rate is determined to align the present value of the required cash flow with the value of the bond portfolio. The resulting discount rate is reflective of both the current interest rate environment and the plan's distinct liability characteristics.

The table below sets forth the estimated impact on our 2014 net periodic pension cost relative to a change in the discount rate and a change in the expected rate of return on plan assets.

In millions	Impact on Pension Cost Increase/(Decrease)
Discount rate used to value liabilities	
0.25 percent increase	\$ (11)
0.25 percent decrease	10
Expected rate of return on assets	
1 percent increase	(38)
1 percent decrease	38

The above sensitivities reflect the impact of changing one assumption at a time. A higher discount rate decreases the plan obligations and decreases our net periodic pension cost. A lower discount rate increases the plan obligations and increases our net periodic pension cost. It should be noted that economic factors and conditions often affect multiple assumptions simultaneously and the effects of changes in key assumptions are not necessarily linear. Note 12, "PENSION AND OTHER POSTRETIREMENT BENEFITS," to our *Consolidated Financial Statements* provides a summary of our pension benefit plan activity, the funded status of our plans and the amounts recognized in our *Consolidated Financial Statements*.



## RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

In February 2013, the Financial Accounting Standards Board (FASB) amended its standards on comprehensive income by requiring disclosure in the footnotes of information about amounts reclassified out of accumulated other comprehensive income by component. Specifically, the amendment requires disclosure of the line items on net income in which the item was reclassified only if it is reclassified to net income in its entirety in the same reporting period. It also requires cross reference to other disclosures for amounts that are not reclassified in their entirety in the same reporting period. The new rules became effective for us beginning January 1, 2013 and were adopted prospectively in accordance with the standard. The standard resulted in new disclosures in NOTE 16, "OTHER COMPREHENSIVE INCOME (LOSS)."

In December 2011, the FASB amended its standards related to offsetting assets and liabilities. This amendment requires entities to disclose both gross and net information about certain instruments and transactions eligible for offset in the statement of financial position and certain instruments and transactions subject to an agreement similar to a master netting agreement. This information enables users of the financial statements to understand the effect of those arrangements on our financial position. The new rules became effective on January 1, 2013. In January 2013, the FASB further amended this standard to limit its scope to derivatives, repurchase and reverse repurchase agreements, securities borrowings and lending transactions. This standard resulted in new disclosures in NOTE 21, "DERIVATIVES."

### ITEM 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to financial risk resulting from volatility in foreign exchange rates, commodity prices and interest rates. This risk is closely monitored and managed through the use of financial derivative instruments including foreign currency forward contracts, commodity swap contracts, commodity zero-cost collars and interest rate swaps. As stated in our policies and procedures, financial derivatives are used expressly for hedging purposes and under no circumstances are they used for speculative purposes. When material, we adjust the value of our derivative contracts for counter-party or our credit risk. None of our derivative instruments are subject to collateral requirements. Substantially all of our derivative contracts are subject to master netting arrangements which provide us with the option to settle certain contracts on a net basis when they settle on the same day with the same currency. In addition, these arrangements provide for a net settlement of all contracts with a given counterparty in the event that the arrangement is terminated due to the occurrence of default or a termination event.

Further information regarding financial instruments and risk management is contained in NOTE 21, "DERIVATIVES," to our *Consolidated Financial Statements*.

The following describes our risk exposures and provides the results of a sensitivity analysis performed as of December 31, 2013. The sensitivity analysis assumes instantaneous, parallel shifts in foreign currency exchange rates and commodity prices.

#### Foreign Exchange Rates

As a result of our international business presence, we are exposed to foreign currency exchange risks. We transact business in foreign currencies and, as a result, our income experiences some volatility related to movements in foreign currency exchange rates. To help manage our exposure to exchange rate volatility, we use foreign currency forward contracts on a regular basis to hedge forecasted intercompany and third-party sales and purchases denominated in non-functional currencies. Our internal policy allows for managing anticipated foreign currency cash flows for up to one year. These foreign currency forward contracts are designated and qualify as foreign currency cash flow hedges under GAAP. The effective portion of the unrealized gain or loss on the forward contract is deferred and reported as a component of "Accumulated other comprehensive loss" (AOCL). When the hedged forecasted transaction (sale or purchase) occurs, the unrealized gain or loss is reclassified into income in the same line item associated with the hedged transaction in the same period or periods during which the hedged transaction affects income. The ineffective portion of the hedge, if any, is recognized in current income during the period of change. As of December 31, 2013, the amount we expect to reclassify from AOCL to income over the next year is an unrealized net gain of \$4 million. For the years ended December 31, 2013 and 2012, there were no circumstances that would have resulted in the discontinuance of a foreign currency cash flow hedge.

To minimize the income volatility resulting from the remeasurement of net monetary assets and payables denominated in a currency other than the functional currency, we enter into foreign currency forward contracts, which are considered economic hedges. The objective is to offset the gain or loss from remeasurement with the gain or loss from the fair market valuation of the forward contract. These derivative instruments are not designated as hedges under GAAP.

As of December 31, 2013, the potential gain or loss in the fair value of our outstanding foreign currency contracts, assuming a hypothetical 10 percent fluctuation in the currencies of such contracts, would be approximately \$35 million. The sensitivity analysis of the effects of changes in foreign currency exchange rates assumes the notional value to remain constant for the next 12 months. The analysis ignores the impact of foreign exchange movements on our competitive position and potential changes in sales levels. It should be noted that any change in the value of the contracts, real or hypothetical, would be significantly offset by an inverse change in the value of the underlying hedged items (see Note 21, "DERIVATIVES," to our *Consolidated Financial Statements*).

### Interest Rate Risk

We are exposed to market risk from fluctuations in interest rates. We manage our exposure to interest rate fluctuations through the use of interest rate swaps. The objective of the swaps is to more effectively balance our borrowing costs and interest rate risk.

In November 2005, we entered into an interest rate swap to effectively convert our \$250 million debt issue, due in 2028, from a fixed rate of 7.125 percent to a floating rate based on a LIBOR spread. The terms of the swap mirror those of the debt, with interest paid semi-annually. This swap qualifies as a fair value hedge under GAAP. The gain or loss on this derivative instrument as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in current income as "Interest expense." The following table summarizes these gains and losses for the years presented below:

In millions	For the years ended December 31,			
	2013		2012	
	Gain/(Loss) on Swaps	Gain/(Loss) on Borrowings	Gain/(Loss) on Swaps	Gain/(Loss) on Borrowings
Interest expense	\$ (39)	\$ 39	\$ 6	\$ (6)

### Commodity Price Risk

We are exposed to fluctuations in commodity prices due to contractual agreements with component suppliers. In order to protect ourselves against future price volatility and, consequently, fluctuations in gross margins, we periodically enter into commodity swap contracts with designated banks to fix the cost of certain raw material purchases with the objective of minimizing changes in inventory cost due to market price fluctuations. Certain commodity swap contracts are derivative contracts that are designated as cash flow hedges under GAAP. We also have commodity swap contracts that represent an economic hedge, but are not designated for hedge accounting and are marked to market through earnings. For those contracts that qualify for hedge accounting, the effective portion of the unrealized gain or loss is deferred and reported as a component of AOCL. When the hedged forecasted transaction (purchase) occurs, the unrealized gain or loss is reclassified into income in the same line item associated with the hedged transaction in the same period or periods during which the hedged transaction affects income. The ineffective portion of the hedge, if any, is recognized in current income in the period in which the ineffectiveness occurs. As of December 31, 2013, we expect to reclassify an unrealized netloss of \$4 million from AOCL to income over the next year. Our internal policy allows for managing these cash flow hedges for up to three years.

As of December 31, 2013, the potential gain or loss related to the outstanding commodity swap contracts, assuming a hypothetical 10 percent fluctuation in the price of such commodities, was \$9 million. The sensitivity analysis of the effects of changes in commodity prices assumes the notional value to remain constant for the next 12 months. The analysis ignores the impact of commodity price movements on our competitive position and potential changes in sales levels. It should be noted that any change in the value of the swap contracts, real or hypothetical, would be significantly offset by an inverse change in the value of the underlying hedged items (see Note 21, "DERIVATIVES," to the *Consolidated Financial Statements*).

**ITEM 8. Financial Statements and Supplementary Data**

**Index to Financial Statements**

- **Management's Report to Shareholders**
- **Report of Independent Registered Public Accounting Firm**
- **Consolidated Statements of Income for the years ended December 31, 2013, 2012 and 2011**
- **Consolidated Statements of Comprehensive Income for the years ended December 31, 2013, 2012 and 2011**
- **Consolidated Balance Sheets at December 31, 2013 and 2012**
- **Consolidated Statements of Cash Flows for the years ended December 31, 2013, 2012 and 2011**
- **Consolidated Statements of Changes in Equity for the years ended December 31, 2013, 2012 and 2011**
- **Notes to Consolidated Financial Statements**

NOTE 1	SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
NOTE 2	ACQUISITIONS AND DIVESTITURES
NOTE 3	INVESTMENTS IN EQUITY INVESTEEES
NOTE 4	INCOME TAXES
NOTE 5	MARKETABLE SECURITIES
NOTE 6	FAIR VALUE OF FINANCIAL INSTRUMENTS
NOTE 7	INVENTORIES
NOTE 8	PROPERTY, PLANT AND EQUIPMENT
NOTE 9	GOODWILL AND OTHER INTANGIBLE ASSETS
NOTE 10	DEBT
NOTE 11	PRODUCT WARRANTY LIABILITY
NOTE 12	PENSION AND OTHER POSTRETIREMENT BENEFITS
NOTE 13	OTHER LIABILITIES AND DEFERRED REVENUE
NOTE 14	COMMITMENTS AND CONTINGENCIES
NOTE 15	SHAREHOLDERS' EQUITY
NOTE 16	OTHER COMPREHENSIVE INCOME (LOSS)
NOTE 17	STOCK INCENTIVE AND STOCK OPTION PLANS
NOTE 18	NONCONTROLLING INTEREST
NOTE 19	RESTRUCTURING AND OTHER CHARGES
NOTE 20	EARNINGS PER SHARE
NOTE 21	DERIVATIVES
NOTE 22	OPERATING SEGMENTS
NOTE 23	SUBSEQUENT EVENT

- **Selected Quarterly Financial Data (Unaudited)**

## MANAGEMENT'S REPORT TO SHAREHOLDERS

### Management's Report on Financial Statements and Practices

The accompanying *Consolidated Financial Statements* of Cummins Inc. were prepared by management, which is responsible for their integrity and objectivity. The statements were prepared in accordance with generally accepted accounting principles and include amounts that are based on management's best judgments and estimates. The other financial information included in the annual report is consistent with that in the financial statements.

Management also recognizes its responsibility for conducting our affairs according to the highest standards of personal and corporate conduct. This responsibility is characterized and reflected in key policy statements issued from time to time regarding, among other things, conduct of its business activities within the laws of the host countries in which we operate, within The Foreign Corrupt Practices Act and potentially conflicting interests of its employees. We maintain a systematic program to assess compliance with these policies.

To comply with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002, we designed and implemented a structured and comprehensive compliance process to evaluate our internal control over financial reporting across the enterprise.

### Management's Report on Internal Control Over Financial Reporting

The management of Cummins Inc. is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and preparation of our *Consolidated Financial Statements* for external purposes in accordance with accounting principles generally accepted in the United States of America.

Management assessed the effectiveness of our internal control over financial reporting and concluded it was effective as of December 31, 2013. In making its assessment, management utilized the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control—Integrated Framework (1992).

The effectiveness of our internal control over financial reporting as of December 31, 2013, has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which appears herein.

### Officer Certifications

Please refer to Exhibits 31(a) and 31(b) attached to this report for certifications required under Section 302 of the Sarbanes-Oxley Act of 2002.

\_\_\_\_\_  
/s/ N. THOMAS LINEBARGER  
*Chairman and Chief Executive Officer*

\_\_\_\_\_  
/s/ PATRICK J. WARD  
*Vice President and Chief Financial Officer*

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of Cummins Inc.:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Cummins Inc. and its subsidiaries at December 31, 2013 and 2012 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2013 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control—Integrated Framework* (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying "Management's Report on Internal Control Over Financial Reporting." Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

Indianapolis, Indiana

February 18, 2014

**CUMMINS INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**

In millions, except per share amounts	Years ended December 31,		
	2013	2012	2011
<b>NET SALES</b> <sup>(a)</sup>	<b>\$ 17,301</b>	<b>\$ 17,334</b>	<b>\$ 18,048</b>
Cost of sales	<b>12,918</b>	12,826	13,459
<b>GROSS MARGIN</b>	<b>4,383</b>	4,508	4,589
<b>OPERATING EXPENSES AND INCOME</b>			
Selling, general and administrative expenses	<b>1,920</b>	1,900	1,837
Research, development and engineering expenses	<b>713</b>	728	629
Equity, royalty and interest income from investees (Note 3)	<b>361</b>	384	416
Gain on sale of businesses (Note 2)	<b>—</b>	6	121
Other operating income (expense), net	<b>(10)</b>	(16)	21
<b>OPERATING INCOME</b>	<b>2,101</b>	2,254	2,681
Interest income	<b>27</b>	25	34
Interest expense (Note 10)	<b>41</b>	32	44
Other income (expense), net	<b>32</b>	24	—
<b>INCOME BEFORE INCOME TAXES</b>	<b>2,119</b>	2,271	2,671
Income tax expense (Note 4)	<b>531</b>	533	725
<b>CONSOLIDATED NET INCOME</b>	<b>1,588</b>	1,738	1,946
Less: Net income attributable to noncontrolling interests	<b>105</b>	93	98
<b>NET INCOME ATTRIBUTABLE TO CUMMINS INC.</b>	<b>\$ 1,483</b>	<b>\$ 1,645</b>	<b>\$ 1,848</b>
<b>EARNINGS PER COMMON SHARE ATTRIBUTABLE TO CUMMINS INC. (Note 20)</b>			
Basic	<b>\$ 7.93</b>	\$ 8.69	\$ 9.58
Diluted	<b>\$ 7.91</b>	\$ 8.67	\$ 9.55

<sup>(a)</sup> Includes sales to nonconsolidated equity investees of \$2,319 million, \$2,427 million and \$2,594 million for the years ended December 31, 2013, 2012 and 2011, respectively.

*The accompanying notes are an integral part of our Consolidated Financial Statements.*

**CUMMINS INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

In millions	Years ended December 31,		
	2013	2012	2011
<b>CONSOLIDATED NET INCOME</b>	<b>\$ 1,588</b>	<b>\$ 1,738</b>	<b>\$ 1,946</b>
Other comprehensive income (loss), net of tax (Note 16)			
Foreign currency translation adjustments	(46)	29	(147)
Unrealized gain (loss) on derivatives	(1)	20	(32)
Change in pension and other postretirement defined benefit plans	183	(70)	(78)
Unrealized gain (loss) on marketable securities	1	2	1
Total other comprehensive income (loss), net of tax	137	(19)	(256)
<b>COMPREHENSIVE INCOME</b>	<b>1,725</b>	<b>1,719</b>	<b>1,690</b>
Less: Comprehensive income attributable to noncontrolling interest	76	86	60
<b>COMPREHENSIVE INCOME ATTRIBUTABLE TO CUMMINS INC.</b>	<b>\$ 1,649</b>	<b>\$ 1,633</b>	<b>\$ 1,630</b>

*The accompanying notes are an integral part of our Consolidated Financial Statements.*

**CUMMINS INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**

In millions, except par value	December 31,	
	2013	2012
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 2,699	\$ 1,369
Marketable securities (Note 5)	150	247
Total cash, cash equivalents and marketable securities	2,849	1,616
Accounts and notes receivable, net		
Trade and other	2,362	2,235
Nonconsolidated equity investees	287	240
Inventories (Note 7)	2,381	2,221
Prepaid expenses and other current assets	760	855
Total current assets	8,639	7,167
Long-term assets		
Property, plant and equipment, net (Note 8)	3,156	2,724
Investments and advances related to equity method investees (Note 3)	931	897
Goodwill (Note 9)	461	445
Other intangible assets, net (Note 9)	357	369
Prepaid pensions (Note 12)	514	182
Other assets	670	764
Total assets	\$ 14,728	\$ 12,548
<b>LIABILITIES</b>		
Current liabilities		
Loans payable (Note 10)	\$ 17	\$ 16
Accounts payable (principally trade)	1,557	1,339
Current maturities of long-term debt (Note 10)	51	61
Current portion of accrued product warranty (Note 11)	360	386
Accrued compensation, benefits and retirement costs	433	400
Deferred revenue	285	215
Taxes payable (including taxes on income)	99	173
Other accrued expenses	566	546
Total current liabilities	3,368	3,136
Long-term liabilities		
Long-term debt (Note 10)	1,672	698
Pensions (Note 12)	232	244
Postretirement benefits other than pensions (Note 12)	356	432
Other liabilities and deferred revenue (Note 13)	1,230	1,064
Total liabilities	6,858	5,574
Commitments and contingencies (Note 14)	—	—
<b>EQUITY</b>		
Cummins Inc. shareholders' equity (Note 15)		
Common stock, \$2.50 par value, 500 shares authorized, 222.3 and 222.4 shares issued	2,099	2,058
Retained earnings	8,406	7,343
Treasury stock, at cost, 35.6 and 32.6 shares	(2,195)	(1,830)
Common stock held by employee benefits trust, at cost, 1.3 and 1.5 shares	(16)	(18)
Accumulated other comprehensive loss (Note 16)		
Defined benefit postretirement plans	(611)	(794)
Other	(173)	(156)
Total accumulated other comprehensive loss	(784)	(950)
Total Cummins Inc. shareholders' equity	7,510	6,603
Noncontrolling interests (Note 18)	360	371
Total equity	7,870	6,974
Total liabilities and equity	\$ 14,728	\$ 12,548

*The accompanying notes are an integral part of our Consolidated Financial Statements.*



**CUMMINS INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

In millions	Years ended December 31,		
	2013	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Consolidated net income	\$ 1,588	\$ 1,738	\$ 1,946
Adjustments to reconcile consolidated net income to net cash provided by operating activities			
Restructuring and other charges and credits, net of cash payments (Note 19)	(25)	27	—
Depreciation and amortization	407	361	325
Gain on sale of businesses (Note 2)	—	(6)	(121)
Gain on sale of equity investment	—	(13)	—
Gain on fair value adjustment for consolidated investees (Note 2)	(12)	(7)	—
Deferred income taxes (Note 4)	100	116	85
Equity in income of investees, net of dividends	(62)	(15)	(23)
Pension contributions in excess of expense (Note 12)	(82)	(68)	(131)
Other post-retirement benefits payments in excess of expense (Note 12)	(25)	(21)	(31)
Stock-based compensation expense	37	36	42
Excess tax benefits on stock-based awards	(13)	(14)	(5)
Translation and hedging activities	17	—	4
	(65)	(775)	(154)
Changes in current assets and liabilities, net of acquisitions and divestitures (Note 1)			
Changes in other liabilities and deferred revenue	211	214	139
Other, net	13	(41)	(3)
Net cash provided by operating activities	2,089	1,532	2,073
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Capital expenditures	(676)	(690)	(622)
Investments in internal use software	(64)	(87)	(60)
Proceeds from disposals of property, plant and equipment	14	11	8
Investments in and advances to equity investees	(42)	(70)	(81)
Acquisitions of businesses, net of cash acquired (Note 2)	(147)	(215)	—
Proceeds from sale of businesses, net of cash sold (Note 2)	—	10	199
Investments in marketable securities—acquisitions	(418)	(561)	(729)
Investments in marketable securities—liquidations (Note 5)	525	585	750
Proceeds from sale of equity investment	—	23	—
Purchases of other investments	(40)	—	—
Cash flows from derivatives not designated as hedges	1	12	(18)
Other, net	1	—	1
Net cash used in investing activities	(846)	(982)	(552)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Proceeds from borrowings (Note 10)	1,004	64	127
Payments on borrowings and capital lease obligations	(90)	(145)	(237)
Net borrowings under short-term credit agreements	(3)	11	6
Distributions to noncontrolling interests	(75)	(62)	(56)
Dividend payments on common stock (Note 15)	(420)	(340)	(255)
	(381)	(256)	(629)
Repurchases of common stock			
Excess tax benefits on stock-based awards	13	14	5
Other, net	4	20	14
Net cash provided by (used in) financing activities	52	(694)	(1,025)
<b>EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>	35	29	(35)
Net increase (decrease) in cash and cash equivalents	1,330	(115)	461
Cash and cash equivalents at beginning of year	1,369	1,484	1,023
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	\$ 2,699	\$ 1,369	\$ 1,484

*The accompanying notes are an integral part of our Consolidated Financial Statements.*

**CUMMINS INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**

In millions	Common Stock	Additional paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Common Stock Held in Trust	Total Cummins Inc. Shareholders' Equity	Noncontrolling Interests	Total Equity
<b>BALANCE AT DECEMBER 31, 2010</b>	\$ 554	\$ 1,380	\$ 4,445	\$ (720)	\$ (964)	\$ (25)	\$ 4,670	\$ 326	\$ 4,996
Net income			1,848				1,848	98	1,946
Other comprehensive income (loss)				(218)			(218)	(38)	(256)
Issuance of shares	1	13					14	—	14
Employee benefits trust activity		25				3	28	—	28
Acquisition of shares					(629)		(629)	—	(629)
Cash dividends on common stock			(255)				(255)	—	(255)
Distribution to noncontrolling interests							—	(56)	(56)
Stock option exercises					6		6	—	6
Other shareholder transactions		28					28	9	37
<b>BALANCE AT DECEMBER 31, 2011</b>	\$ 555	\$ 1,446	\$ 6,038	\$ (938)	\$ (1,587)	\$ (22)	\$ 5,492	\$ 339	\$ 5,831
Net income			1,645				1,645	93	1,738
Other comprehensive income (loss)				(12)			(12)	(7)	(19)
Issuance of shares	1	6					7	—	7
Employee benefits trust activity		27				4	31	—	31
Acquisition of shares					(256)		(256)	—	(256)
Cash dividends on common stock			(340)				(340)	—	(340)
Distribution to noncontrolling interests							—	(76)	(76)
Stock option exercises					13		13	—	13
Other shareholder transactions		23					23	22	45
<b>BALANCE AT DECEMBER 31, 2012</b>	\$ 556	\$ 1,502	\$ 7,343	\$ (950)	\$ (1,830)	\$ (18)	\$ 6,603	\$ 371	\$ 6,974
Net income			1,483				1,483	105	1,588
Other comprehensive income (loss)				166			166	(29)	137
Issuance of shares		8					8	—	8
Employee benefits trust activity		24				2	26	—	26
Acquisition of shares					(381)		(381)	—	(381)
Cash dividends on common stock			(420)				(420)	—	(420)
Distribution to noncontrolling interests							—	(75)	(75)
Stock option exercises		1			16		17	—	17
Other shareholder transactions		8					8	(12)	(4)
<b>BALANCE AT DECEMBER 31, 2013</b>	\$ 556	\$ 1,543	\$ 8,406	\$ (784)	\$ (2,195)	\$ (16)	\$ 7,510	\$ 360	\$ 7,870

*The accompanying notes are an integral part of our Consolidated Financial Statements.*

**CUMMINS INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations**

Cummins Inc. was founded in 1919 as a corporation in Columbus, Indiana, as one of the first diesel engine manufacturers. We are a global power leader that designs, manufactures, distributes and services diesel and natural gas engines and engine-related component products, including filtration, aftertreatment, turbochargers, fuel systems, controls systems, air handling systems and electric power generation systems. We sell our products to original equipment manufacturers (OEMs), distributors and other customers worldwide. We serve our customers through a network of over 600 company-owned and independent distributor locations and over 6,800 dealer locations in more than 190 countries and territories.

**Principles of Consolidation**

Our *Consolidated Financial Statements* include the accounts of all wholly-owned and majority-owned domestic and foreign subsidiaries where our ownership is more than 50 percent of outstanding equity interests except for majority-owned subsidiaries that are considered variable interest entities (VIEs) where we are not deemed to have a controlling financial interest. In addition, we also consolidate, regardless of our ownership percentage, VIEs for which we are deemed to have a controlling financial interest. Intercompany balances and transactions are eliminated in consolidation. Where our ownership interest is less than 100 percent, the noncontrolling ownership interests are reported in our *Consolidated Balance Sheets*. The noncontrolling ownership interest in our income, net of tax, is classified as "Net income attributable to noncontrolling interests" in our *Consolidated Statements of Income*.

Certain amounts for 2012 and 2011 have been reclassified to conform to the current classifications.

We have variable interests in several businesses accounted for under the equity method of accounting that are deemed to be VIEs and are subject to the provisions of accounting principles generally accepted in the United States of America (GAAP) for variable interest entities. Most of these VIEs are unconsolidated and as such are included in the summary of disclosures in NOTE 3, "INVESTMENTS IN EQUITY INVESTEES." The VIEs, including the consolidated VIEs, are not material individually or in the aggregate to our *Consolidated Balance Sheets* or *Consolidated Statements of Income*.

**Investments in Equity Investees**

We use the equity method to account for our investments in joint ventures, affiliated companies and alliances in which we have the ability to exercise significant influence, generally represented by equity ownership or partnership equity of at least 20 percent but not more than 50 percent. Generally, under the equity method, original investments in these entities are recorded at cost and subsequently adjusted by our share of equity in income or losses after the date of acquisition. Investment amounts in excess of our share of an investee's net assets are amortized over the life of the related asset creating the excess. If the excess is goodwill, then it is not amortized. Equity in income or losses of each investee is recorded according to our level of ownership; if losses accumulate, we record our share of losses until our investment has been fully depleted. If our investment has been fully depleted, we recognize additional losses only when we are the primary funding source. We eliminate (to the extent of our ownership percentage) in our *Consolidated Financial Statements* the profit in inventory held by our equity method investees that has not yet been sold to a third-party. Our investments are classified as "Investments and advances related to equity method investees" in our *Consolidated Balance Sheets*. Our share of the results from joint ventures, affiliated companies and alliances is reported in our *Consolidated Statements of Income* as "Equity, royalty and interest income from investees," and is reported net of all applicable income taxes.

Our foreign equity investees are presented net of applicable foreign income taxes in our *Consolidated Statements of Income*. The vast majority of our United States (U.S.) equity investees are partnerships (non-taxable), thus there is no difference between gross or net of tax presentation as the investees are not taxed. See NOTE 3, "INVESTMENTS IN EQUITY INVESTEES," for additional information.

## Use of Estimates in the Preparation of the Financial Statements

Preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect reported amounts presented and disclosed in our *Consolidated Financial Statements*. Significant estimates and assumptions in these *Consolidated Financial Statements* require the exercise of judgment and are used for, but not limited to, allowance for doubtful accounts, estimates of future cash flows and other assumptions associated with goodwill and long-lived asset impairment tests, useful lives for depreciation and amortization, warranty programs, determination of discount and other rate assumptions for pension and other postretirement benefit costs, restructuring costs, income taxes and deferred tax valuation allowances, lease classification and contingencies. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be different from these estimates.

## Revenue Recognition

We recognize revenue, net of estimated costs of returns, allowances and sales incentives, when it is realized or realizable, which generally occurs when:

- Persuasive evidence of an arrangement exists,
- The product has been shipped and legal title and all risks of ownership have been transferred,
- The sales price is fixed or determinable and
- Payment is reasonably assured.

Products are generally sold on open account under credit terms customary to the geographic region of distribution. We perform ongoing credit evaluations of our customers and generally do not require collateral to secure our accounts receivable. For engines, service parts, service tools and other items sold to independent distributors and to partially-owned distributors accounted for under the equity method, revenues are recorded when title and risk of ownership transfers. This transfer is based on the agreement in effect with the respective distributor, which in the U.S. and most international locations, generally occurs when the products are shipped. To the extent of our ownership percentage, margins on sales to distributors accounted for under the equity method are deferred until the distributor sells the product to unrelated parties.

We provide various sales incentives to both our distribution network and our OEM customers. These programs are designed to promote the sale of our product in the channel or encourage the usage of our products by OEM customers. Sales incentives primarily fall into three categories:

- Volume rebates,
- Market share rebates and
- Aftermarket rebates.

For volume rebates, we provide certain customers with rebate opportunities for attaining specified volumes during a particular quarter or year. We accrue for the expected amount of these rebates at the time of the original sale and update our accruals quarterly based on our best estimate of the volume levels the customer will reach during the measurement period. For market share rebates, we provide certain customers with rebate opportunities based on the percentage of their production that utilizes our product. These rebates are typically measured either quarterly or annually and are accrued at the time of the original sale based on the current market shares, with adjustments made as the level changes. For aftermarket rebates we provide incentives to promote sales to certain dealers and end-markets. These rebates are typically paid on a quarterly, or more frequent, basis and estimates are made at the end of each quarter as to the amount yet to be paid. These estimates are based on historical experience with the particular program. The incentives are classified as a reduction in sales in our *Consolidated Statements of Income*.

Rights of return do not exist for the majority of our sales, other than for quality issues. We do offer certain return rights in our aftermarket business, where some aftermarket customers are permitted to return small amounts of parts and filters each year and in our power generation business, which sells portable generators to retail customers. An estimate of future returns is accrued at the time of sale based on historical return rates.

## **Foreign Currency Transactions and Translation**

We translate assets and liabilities of foreign entities to U.S. dollars, where the local currency is the functional currency, at year-end exchange rates. We translate income and expenses to U.S. dollars using weighted-average exchange rates for the year. We record adjustments resulting from translation in a separate component of accumulated other comprehensive income (loss) and include the adjustments in net income only upon sale, loss of controlling financial interest or liquidation of the underlying foreign investment.

Foreign currency transaction gains and losses are included in current net income. For foreign entities where the U.S. dollar is the functional currency, including those operating in highly inflationary economies when applicable, we remeasure non-monetary balances and the related income statement using historical exchange rates. We include in income the resulting gains and losses, including the effect of derivatives in our *Consolidated Statements of Income*, which combined with transaction gains and losses amounted to a net loss of \$27 million in 2013, net loss of \$14 million in 2012 and net loss of \$14 million in 2011.

## **Derivative Instruments**

We make use of derivative instruments in foreign exchange, commodity price and interest rate hedging programs. Derivatives currently in use are foreign currency forward contracts, commodity swap contracts, commodity zero-cost collars and an interest rate swap. These contracts are used strictly for hedging and not for speculative purposes.

Due to our international business presence, we are exposed to foreign currency exchange risk. We transact in foreign currencies and have significant assets and liabilities denominated in foreign currencies. Consequently, our income experiences some volatility related to movements in foreign currency exchange rates. In order to benefit from global diversification and after considering naturally offsetting currency positions, we enter into foreign currency forward contracts to minimize our existing exposures (recognized assets and liabilities) and hedge forecasted transactions.

We are exposed to fluctuations in commodity prices due to contractual agreements with component suppliers. In order to protect ourselves against future price volatility and, consequently, fluctuations in gross margins, we periodically enter into commodity swap contracts with designated banks to fix the cost of certain raw material purchases with the objective of minimizing changes in inventory cost due to market price fluctuations.

We record all derivatives at fair value in our financial statements. NOTE 21, "DERIVATIVES," provides further information on our hedging strategy and accounting for derivative financial instruments.

## **Income Tax Accounting**

We determine our income tax expense using the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax effects of temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax benefits of tax loss and credit carryforwards are also recognized as deferred tax assets. We evaluate the recoverability of our deferred tax assets each quarter by assessing the likelihood of future profitability and available tax planning strategies that could be implemented to realize our net deferred tax assets. A valuation allowance is recorded to reduce the tax assets to the net value management believes is more likely than not to be realized. In the event our operating performance deteriorates, future assessments could conclude that a larger valuation allowance will be needed to further reduce the deferred tax assets. In addition, we operate within multiple taxing jurisdictions and are subject to tax audits in these jurisdictions. These audits can involve complex issues, which may require an extended period of time to resolve. We reduce our net tax assets for the estimated additional tax and interest that may result from tax authorities disputing uncertain tax positions we have taken and we believe we have made adequate provision for income taxes for all years that are subject to audit based upon the latest information available. A more complete description of our income taxes and the future benefits of our tax loss and credit carryforwards is disclosed in NOTE 4, "INCOME TAXES."

## **Cash and Cash Equivalents**

Cash equivalents are defined as short-term, highly liquid investments with an original maturity of 90 days or less at the time of purchase. The carrying amounts reflected in our *Consolidated Balance Sheets* for cash and cash equivalents approximate fair value due to the short-term maturity of these investments.

**Statements of Cash Flows-Supplemental Disclosures**

In millions	Years ended December 31,		
	2013	2012	2011
<b>Changes in current assets and liabilities, net of acquisitions and divestitures</b>			
Accounts and notes receivable	\$ (148)	\$ 87	\$ (350)
Inventories	(46)	(32)	(225)
Other current assets	212	(60)	(21)
Accounts payable	163	(256)	208
Accrued expenses	(246)	(514)	234
<b>Total</b>	<b>\$ (65)</b>	<b>\$ (775)</b>	<b>\$ (154)</b>
Cash payments for income taxes, net of refunds	\$ 380	\$ 691	\$ 532
Cash payments for interest, net of capitalized interest	\$ 30	\$ 32	\$ 47

**Marketable Securities**

We account for marketable securities in accordance with GAAP for investments in debt and equity securities. We determine the appropriate classification of all marketable securities as "held-to-maturity," "available-for-sale" or "trading" at the time of purchase, and re-evaluate such classifications at each balance sheet date. At December 31, 2013 and 2012, all of our investments were classified as available-for-sale.

Available-for-sale (AFS) securities are carried at fair value with the unrealized gain or loss, net of tax, reported in other comprehensive income. Unrealized losses considered to be "other-than-temporary" are recognized currently in income. The cost of securities sold is based on the specific identification method. The fair value of most investment securities is determined by currently available market prices. Where quoted market prices are not available, we use the market price of similar types of securities that are traded in the market to estimate fair value. See NOTE 5, "MARKETABLE SECURITIES," for a detailed description of our investments in marketable securities.

**Accounts Receivable and Allowance for Doubtful Accounts**

Trade accounts receivable are recorded at the invoiced amount, which approximates net realizable value, and generally do not bear interest. The allowance for doubtful accounts is our best estimate of the amount of probable credit losses in our existing accounts receivable. We determine the allowance based on our historical collection experience and by performing an analysis of our accounts receivable in light of the current economic environment. We review our allowance for doubtful accounts on a regular basis. In addition, when necessary, we provide an allowance for the full amount of specific accounts deemed to be uncollectible. Account balances are charged off against the allowance in the period in which we determine that it is probable the receivable will not be recovered. The allowance for doubtful accounts balances for the years ended December 31, 2013 and 2012 were \$14 million and \$13 million, respectively.

**Inventories**

Our inventories are stated at the lower of cost or market. For the years ended December 31, 2013 and 2012, approximately 14 percent and 14 percent, respectively, of our consolidated inventories (primarily heavy-duty and high-horsepower engines and parts) were valued using the last-in, first-out (LIFO) cost method. The cost of other inventories is generally valued using the first-in, first-out (FIFO) cost method. Our inventories at interim and year-end reporting dates include estimates for adjustments related to annual physical inventory results and for inventory cost changes under the LIFO cost method. Due to significant movements of partially-manufactured components and parts between manufacturing plants, we do not internally measure, nor do our accounting systems provide, a meaningful segregation between raw materials and work-in-process. See NOTE 7, "INVENTORIES," for additional information.

**Property, Plant and Equipment**

We record property, plant and equipment, inclusive of assets under capital leases, at cost. We depreciate the cost of the majority of our equipment using the straight-line method with depreciable lives ranging from 20 to 40 years for buildings and 3 to 20 years for machinery, equipment and fixtures. Capital lease amortization is recorded in depreciation expense. We expense normal maintenance and repair costs as incurred. Depreciation expense totaled \$318 million, \$287 million and \$264 million for the years ended December 31, 2013, 2012 and 2011, respectively. See NOTE 8, "PROPERTY, PLANT AND EQUIPMENT," for additional information.

## Long-Lived Assets

We review our long-lived assets for possible impairment whenever events or circumstances indicate that the carrying value of an asset or asset group may not be recoverable. We assess the recoverability of the carrying value of the long-lived assets at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities. An impairment of a long-lived asset or asset group exists when the expected future pre-tax cash flows (undiscounted and without interest charges) estimated to be generated by the asset or asset group is less than its carrying value. If these cash flows are less than the carrying value of such asset or asset group, an impairment loss is measured based on the difference between the estimated fair value and carrying value of the asset or asset group. Assumptions and estimates used to estimate cash flows in the evaluation of impairment and the fair values used to determine the impairment are subject to a degree of judgment and complexity. Any changes to the assumptions and estimates resulting from changes in actual results or market conditions from those anticipated may affect the carrying value of long-lived assets and could result in a future impairment charge.

## Goodwill

Under GAAP for goodwill, we have the option to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value as a basis for determining whether it is necessary to perform an annual two-step goodwill impairment test. The two-step impairment test is now only required if an entity determines through this qualitative analysis that it is more likely than not that the fair value of the reporting unit is less than its carrying value. In addition, carrying value of goodwill must be tested for impairment on an interim basis in certain circumstances where impairment may be indicated. When we are required or opt to perform the two-step impairment test, the fair value of each reporting unit is estimated by discounting the after tax future cash flows less requirements for working capital and fixed asset additions. Our reporting units are generally defined as one level below an operating segment. However, there were two situations where we have aggregated two or more components which share similar economic characteristics and thus are aggregated into a single reporting unit for testing purposes. These two situations are described further below. This analysis has resulted in the following reporting units for our goodwill testing:

- Within our Components segment, our emission solutions and filtration businesses have been aggregated into a single reporting unit.
- Also within our Components segment, our turbo technologies business is considered a separate reporting unit.
- Within our Power Generation segment, our alternators business is considered a separate reporting unit.
- Within our Engine segment, our new and recon parts business is considered a separate reporting unit. This reporting unit is in the business of selling new parts and remanufacturing and reconditioning engines and certain engine components.
- Our Distribution segment is considered a single reporting unit as it is managed geographically and all regions share similar economic characteristics and provide similar products and services.

No other reporting units have goodwill. Our valuation method requires us to make projections of revenue, operating expenses, working capital investment and fixed asset additions for the reporting units over a multi-year period. Additionally, management must estimate a weighted-average cost of capital, which reflects a market rate, for each reporting unit for use as a discount rate. The discounted cash flows are compared to the carrying value of the reporting unit and, if less than the carrying value, a separate valuation of the goodwill is required to determine if an impairment loss has occurred. In addition, we also perform a sensitivity analysis to determine how much our forecasts can fluctuate before the fair value of a reporting unit would be lower than its carrying amount. We performed the required procedures as of the end of our fiscal third quarter and determined that our goodwill was not impaired. At December 31, 2013, our recorded goodwill was \$461 million, approximately 87 percent of which resided in the emission solutions plus filtration reporting unit. For this reporting unit, the fair value exceeded its carrying value by a substantial margin when we last performed step one of the two-step impairment test. Changes in our projections or estimates, a deterioration of our operating results and the related cash flow effect or a significant increase in the discount rate could decrease the estimated fair value of our reporting units and result in a future impairment of goodwill. See NOTE 9, "GOODWILL AND OTHER INTANGIBLE ASSETS," for additional information.

## **Software**

We capitalize certain costs for software that are developed or obtained for internal use. Software costs are amortized on a straight-line basis over their estimated useful lives generally ranging from 3 to 12 years. Software assets are reviewed for impairment when events or circumstances indicate that the carrying value may not be recoverable over the remaining lives of the assets. Upgrades and enhancements are capitalized if they result in significant modifications that enable the software to perform tasks it was previously incapable of performing. Software maintenance, training, data conversion and business process reengineering costs are expensed in the period in which they are incurred. See NOTE 9, "GOODWILL AND OTHER INTANGIBLE ASSETS," for additional information.

## **Warranty**

We charge the estimated costs of warranty programs, other than product recalls, to income at the time products are shipped to customers. We use historical experience of warranty programs to develop the estimated liability for our various warranty programs. As a result of the uncertainty surrounding the nature and frequency of product recall programs, the liability for such programs is recorded when we commit to a recall action or when a recall becomes probable and estimable, which generally occurs when it is announced. The liability for these programs is reflected in the provision for warranties issued. We review and assess the liability for these programs on a quarterly basis. We also assess our ability to recover certain costs from our suppliers and record a receivable from the supplier when we believe a recovery is probable.

In addition, we sell extended warranty coverage on most of our engines. The revenue collected is initially deferred and is recognized as revenue in proportion to the costs expected to be incurred in performing services over the contract period. We compare the remaining deferred revenue balance quarterly to the estimated amount of future claims under extended warranty programs and provide an additional accrual when the deferred revenue balance is less than expected future costs. See NOTE 11, "PRODUCT WARRANTY LIABILITY," for additional information.

## **Research and Development**

Our research and development program is focused on product improvements, innovations and cost reductions for our customers. Research and development expenditures include salaries, contractor fees, building costs, utilities, administrative expenses and allocation of corporate costs and are expensed, net of contract reimbursements, when incurred. From time to time, we enter into agreements with customers to fund a portion of the research and development costs of a particular project. We generally account for these reimbursements as an offset to the related research and development expenditure. Research and development expenses, net of contract reimbursements, were \$700 million in 2013, \$721 million in 2012 and \$621 million in 2011. Contract reimbursements were \$76 million in 2013, \$86 million in 2012 and \$75 million in 2011.

## **Related Party Transactions**

In accordance with the provisions of various joint venture agreements, we may purchase products and components from our joint ventures, sell products and components to our joint ventures and our joint ventures may sell products and components to unrelated parties. Joint venture transfer prices may differ from normal selling prices. Certain joint venture agreements transfer product at cost, some transfer product on a cost-plus basis, and others transfer product at market value. Our related party sales are presented on the face of our *Consolidated Statements of Income*. Our related party purchases were not material to our financial position or results of operations.

## **RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS**

In February 2013, the Financial Accounting Standards Board (FASB) amended its standards on comprehensive income by requiring disclosure in the footnotes of information about amounts reclassified out of accumulated other comprehensive income by component. Specifically, the amendment requires disclosure of the line items on net income in which the item was reclassified only if it is reclassified to net income in its entirety in the same reporting period. It also requires cross reference to other disclosures for amounts that are not reclassified in their entirety in the same reporting period. The new rules became effective for us beginning January 1, 2013 and were adopted prospectively in accordance with the standard. The standard resulted in new disclosures in NOTE 16, "OTHER COMPREHENSIVE INCOME (LOSS)."

In December 2011, the FASB amended its standards related to offsetting assets and liabilities. This amendment requires entities to disclose both gross and net information about certain instruments and transactions eligible for offset in the statement of financial position and certain instruments and transactions subject to an agreement similar to a master netting agreement. This information enables users of the financial statements to understand the effect of those arrangements on our financial position. The new rules became effective on January 1, 2013. In January 2013, the FASB further amended this standard to limit its scope to derivatives, repurchase and reverse repurchase agreements, securities borrowings and lending transactions. This standard resulted in new disclosures in NOTE 21, "DERIVATIVES."



**NOTE 2. ACQUISITIONS AND DIVESTITURES****Acquisitions**

On September 17, 2013, we announced our intention to acquire the equity that we do not already own in most of our partially-owned United States and Canadian distributors over the next three to five years.

**Cummins Western Canada LP**

In December 2013, we acquired the remaining 35 percent interest in Cummins Western Canada LP (Western Canada) from the former principal for consideration of approximately \$34 million. This entity was previously consolidated and, as a result, the acquisition was not treated as a business combination but as an equity transaction. This acquisition was made in accordance with our planned strategy.

**Cummins Rocky Mountain LLC**

In May 2013, we acquired the remaining 67 percent interest in Cummins Rocky Mountain LLC (Rocky Mountain) from the former principal for consideration of approximately \$62 million in cash and an additional \$74 million in cash paid to creditors to eliminate all debt related to the entity. The purchase price was approximately \$136 million as presented below. The intangible assets are primarily customer related and are being amortized over periods ranging from one to four years. The acquisition was accounted for as a business combination, with the results of the acquired entity included in the Distribution operating segment beginning in the second quarter of 2013.

Distribution segment results also included a \$5 million gain, as we were required to re-measure our pre-existing 33 percent ownership interest in Rocky Mountain to fair value in accordance with GAAP. Net sales for Rocky Mountain were \$384 million for the year ended December 31, 2012. This amount is not fully incremental to Cummins Inc. as the amount would be reduced by the elimination of sales to the previously unconsolidated entity. Approximately \$13 million of the \$14 million deferred purchase price was distributed in 2013. The remaining balance is expected to be paid in 2014.

The final purchase price allocation as of December 31, 2013, was as follows:

<b>In millions</b>	
Accounts receivable	\$ 48
Inventory	100
Fixed assets	34
Intangible assets	8
Goodwill	10
Other assets	8
Current liabilities	(41)
Total business valuation	167
Fair value of pre-existing 33 percent interest	(31)
Purchase price	<u>\$ 136</u>

**Cummins Northwest LLC**

In January 2013, we acquired an additional 29.99 percent interest in Cummins Northwest LLC (Northwest) from the former principal for consideration of approximately \$18 million. We formed a new partnership with a new distributor principal. We owned 79.99 percent of Northwest and the new distributor principal owned 20.01 percent. The acquisition was accounted for as a business combination, with the results of the acquired entity included in the Distribution segment beginning in the first quarter of 2013. Distribution segment results also included a \$7 million gain, as we were required to re-measure our pre-existing 50 percent ownership interest in Northwest to fair value in accordance with GAAP. The transaction generated \$3 million of goodwill. Net sales for Northwest were \$137 million for the year ended December 31, 2012. This amount is not fully incremental to Cummins Inc. as the amount would be reduced by the elimination of sales to the previously unconsolidated entity.

In July 2013, we acquired the remaining 20.01 percent from the former distributor principal for an additional \$4 million. Since the entity was already consolidated, this was accounted for as an equity transaction.

**Hilite Germany GmbH**

In July 2012, we purchased the doser technology and business assets from Hilite Germany GmbH (Hilite) in a cash transaction. Dosers are products that enable compliance with emission standards in certain aftertreatment systems and complement our current product offerings. The purchase price was \$176 million and is summarized below. There was no contingent consideration associated with this transaction. During 2012, we expensed approximately \$4 million of acquisition related costs.

The acquisition of Hilite was accounted for as a business combination, with the results of the acquired entity and the goodwill included in the Components operating segment beginning in the third quarter of 2012. The majority of the purchase price was allocated to technology and customer related intangible assets and goodwill, most of which is expected to be fully deductible for tax purposes. We expect the Hilite acquisition to strengthen our aftertreatment product offerings. This acquisition enhances our technical capabilities and keeps us in a strong position to meet the needs of current customers and grow into new markets, especially as an increasing number of regions around the world adopt tougher emission standards.

Intangible assets by asset class, including weighted average amortization life, were as follows:

Dollars in millions	Purchase price allocation	Weighted average amortization life in years
Technology	\$ 52	10.6
Customer	23	4.5
License arrangements	8	6.0
Total intangible assets	\$ 83	8.5

The purchase price was allocated as follows:

In millions	
Inventory	\$ 5
Fixed assets	5
Intangible assets	83
Goodwill	91
Liabilities	(8)
Total purchase price	\$ 176

Net sales for Hilite were \$104 million for 2012, of which \$46 million was included in our *Consolidated Statements of Income* and represented less than 1 percent of consolidated sales, and \$77 million in 2011.

**Cummins Central Power LLC**

In July 2012, we acquired an additional 45 percent interest in Cummins Central Power LLC (Central Power) from the former principal for consideration of approximately \$20 million. The acquisition was accounted for as a business combination, with the results of the acquired entity included in the Distribution operating segment beginning in the third quarter of 2012. Distribution segment results also included a \$7 million gain, as we were required to re-measure our pre-existing 35 percent ownership interest in Central Power to fair value in accordance with GAAP. Net sales for Central Power were \$242 million in 2012, of which \$115 million was included in our *Consolidated Statements of Income* and represented less than 1 percent of consolidated sales, and \$209 million in 2011.

**Divestitures****Exhaust Business**

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

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

**Light-Duty Filtration Business**

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

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

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

**NOTE 3. INVESTMENTS IN EQUITY INVESTEES**

Investments in and advances to equity investees and our ownership percentage was as follows:

In millions	Ownership %	December 31,	
		2013	2012
Dongfeng Cummins Engine Company, Ltd.	50%	\$ 135	\$ 113
Komatsu alliances	20-50%	132	132
North American distributors	37-50%	114	139
Beijing Foton Cummins Engine Co., Ltd. <sup>(1)</sup>	50%	103	107
Cummins-Scania XPI Manufacturing, LLC	50%	71	65
Chongqing Cummins Engine Company, Ltd.	50%	67	58
Tata Cummins, Ltd.	50%	50	52
Cummins Olayan Energy	49%	34	34
Shanghai Fleetguard Filter Co., Ltd.	50%	33	31
Guangxi Cummins Industrial Power Co., Ltd.	50%	26	30
Other	Various	166	136
Total		\$ 931	\$ 897

<sup>(1)</sup> Includes both the Light-duty and the Heavy-duty businesses.

Equity, royalty and interest income from investees, net of applicable taxes, was as follows:

In millions	Years ended December 31,		
	2013	2012	2011
<b>Distribution Entities</b>			
North American distributors	\$ 129	\$ 147	\$ 134
Komatsu Cummins Chile, Ltda.	25	26	22
All other distributors	1	4	4
<b>Manufacturing Entities</b>			
Dongfeng Cummins Engine Company, Ltd.	63	52	80
Chongqing Cummins Engine Company, Ltd.	58	61	68
Beijing Foton Cummins Engine Co., Ltd. (Heavy-duty)	(21)	(13)	(6)
Beijing Foton Cummins Engine Co., Ltd. (Light-duty)	17	5	(7)
Shanghai Fleetguard Filter Co., Ltd.	13	13	15
Tata Cummins, Ltd.	5	11	14
Cummins Westport, Inc.	4	14	14
All other manufacturers	31	27	37
Cummins share of net income	325	347	375
Royalty and interest income	36	37	41
Equity, royalty and interest income from investees	\$ 361	\$ 384	\$ 416

## Distribution Entities

We have an extensive worldwide distributor and dealer network through which we sell and distribute our products and services. Generally, our distributors are divided by geographic region with some of our distributors being wholly-owned by Cummins, some partially-owned and the majority independently owned. We consolidate all wholly-owned distributors and partially-owned distributors where we are the primary beneficiary and account for other partially-owned distributors using the equity method of accounting.

- **North American Distributors** - As of December 31, 2013, our distribution channel in North America included 9 unconsolidated partially-owned distributors. Our equity interests in these nonconsolidated entities ranged from 37 percent to 50 percent. We also had more than a 50 percent ownership interest in three partially owned distributors which we consolidate. While each distributor is a separate legal entity, the business of each is substantially the same as that of our wholly-owned distributors based in other parts of the world. All of our distributors, irrespective of their legal structure or ownership, offer the full range of our products and services to customers and end-users in their respective markets.
- **Komatsu Cummins Chile, Ltda.** - Komatsu Cummins Chile, Ltda. is a joint venture with Komatsu America Corporation. The joint venture is a distributor that offers the full range of our products and services to customers and end-users in the Chilean and Peruvian markets.

We also have 50 percent equity interests in five other international distributors.

We are contractually obligated to repurchase new engines, parts and components, special tools and signage from our North American distributors following an ownership transfer or termination of the distributor. In addition, in certain cases where we own a partial interest in a distributor, we are obligated to purchase the other equity holders' interests if certain events occur (such as the death or resignation of the distributor principal or a change in control of Cummins Inc.). The purchase price of the equity interests is determined based on the fair value of the distributor's assets. Outside of North America, repurchase obligations and practices vary by region. All distributors that are partially-owned are considered to be related parties in our *Consolidated Financial Statements*.

## Manufacturing Entities

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

- **Chongqing Cummins Engine Company, Ltd.** - Chongqing Cummins Engine Company, Ltd. (CCEC) is a joint venture in China with Chongqing Machinery and Electric Co. Ltd. This joint venture manufactures several models of our heavy-duty and high-horsepower diesel engines, primarily serving the industrial and stationary power markets in China.
- **Dongfeng Cummins Engine Company, Ltd.** - Dongfeng Cummins Engine Company, Ltd. (DCEC) is a joint venture in China with Dongfeng Automotive Co. Ltd., a subsidiary of Dongfeng Motor Corporation (Dongfeng), one of the largest medium-duty and heavy-duty truck manufacturers in China. DCEC produces Cummins 4- to 13-liter mechanical engines, full-electric diesel engines, with a power range from 125 to 545 horsepower, and natural gas engines.

- **Beijing Foton Cummins Engine Co., Ltd.** -Beijing Foton Cummins Engine Co., Ltd. is a joint venture in China with Beiqi Foton Motor Co., Ltd., a commercial vehicle manufacturer, which consists of two distinct lines of business, a light-duty business and a heavy-duty business. The light-duty business produces ISF 2.8 liter and ISF 3.8 liter families of our high performance light-duty diesel engines in Beijing. These engines are used in light-duty commercial trucks, pickup trucks, buses, multipurpose and sport utility vehicles with main markets in China, Brazil and Russia. Certain types of marine, small construction equipment and industrial applications are also served by these engine families. The heavy-duty business has been in the development stage for the past several years but is scheduled to start the production of ISG 10.5 liter and ISG 11.8 liter families of our high performance heavy-duty diesel engines in the second quarter of 2014 in Beijing. These engines will be used in heavy-duty commercial trucks in China and subsequently in world wide markets. Certain types of construction equipment and industrial applications will also be served by these engine families in the future.
- **Shanghai Fleetguard Filter Co., Ltd.** -Shanghai Fleetguard Filter Co., Ltd. is a joint venture in China with Dongfeng that manufactures filtration systems.
- **Cummins Westport, Inc.** -Cummins Westport, Inc. is a joint venture in Canada with Westport Innovations Inc. to market and sell automotive spark-ignited natural gas engines and to participate in joint technology projects on low-emission technologies.
- **Tata Cummins, Ltd.** - Tata Cummins, Ltd. is a joint venture in India with Tata Motors Ltd., the largest automotive company in India and a member of the Tata group of companies. This joint venture manufactures engines in India for use in trucks manufactured by Tata Motors, as well as for various industrial and power generation applications.
- **Komatsu manufacturing alliances** - Komatsu manufacturing alliances consists of two manufacturing joint ventures and one design joint venture including Komatsu Cummins Engine Company (KCEC) in Japan and Cummins Komatsu Engine Company (CKEC) in the United States (U.S.) with Komatsu Ltd. These joint ventures manufacture Cummins-designed medium-duty engines in Japan and Komatsu-designed high-horsepower engines in the U.S. The industrial engine design joint venture is located in Japan.
- **Cummins-Scania XPI Manufacturing, LLC** - Cummins-Scania XPI Manufacturing, LLC is a joint venture in the United States with Scania Holding, Inc. This joint venture manufactures several models of advanced fuel systems for heavy-duty and midrange diesel engines.
- **Cummins Olayan Energy Ltd.** -Cummins Olayan Energy Ltd. is a joint venture in the Kingdom of Saudi Arabia with General Contracting Company to operate certain rental power generation equipment, which is primarily utilized within the Kingdom of Saudi Arabia.
- **Guangxi Cummins Industrial Power Co., Ltd.** -Guangxi Cummins Industrial Power Co., Ltd. is a joint venture in China with Guangxi LiuGong Machinery Co. This joint venture manufactures 6.7 liter and 9.3 liter diesel engines for use in various construction equipment.

**Equity Investee Financial Summary**

We have approximately \$482 million in our investment account at December 31, 2013, that represents cumulative undistributed income in our equity investees. Dividends received from our unconsolidated equity investees were \$271 million, \$329 million and \$341 million in 2013, 2012 and 2011, respectively. Summary financial information for our equity investees was as follows:

In millions	As of and for the years ended December 31,		
	2013	2012	2011
Net sales	\$ 7,799	\$ 8,296	\$ 8,659
Gross margin	1,719	1,870	1,948
Net income	690	747	788
Cummins share of net income	\$ 325	\$ 347	\$ 375
Royalty and interest income	36	37	41
Total equity, royalty and interest from investees	\$ 361	\$ 384	\$ 416
Current assets	\$ 2,742	\$ 2,843	
Non-current assets	1,794	1,588	
Current liabilities	(2,090)	(2,039)	
Non-current liabilities	(541)	(431)	
Net assets	\$ 1,905	\$ 1,961	
Cummins share of net assets	\$ 967	\$ 886	

**NOTE 4. INCOME TAXES**

In millions	Years ended December 31,		
	2013	2012	2011
Income before income taxes			
U.S. income	\$ 1,058	\$ 998	\$ 881
Foreign income	1,061	1,273	1,790
Total	\$ 2,119	\$ 2,271	\$ 2,671

Income tax expense consists of the following:

In millions	Years ended December 31,		
	2013	2012	2011
Current			
U.S. federal and state	\$ 239	\$ 118	\$ 116
Foreign	192	299	524
Total current	431	417	640
Deferred			
U.S. federal and state	67	108	69
Foreign	33	8	16
Total deferred	100	116	85
Income tax expense	\$ 531	\$ 533	\$ 725

A reconciliation of the statutory U.S. federal income tax rate to the effective tax rate was as follows:

	Years ended December 31,		
	2013	2012	2011
Statutory U.S. federal income tax rate	35.0 %	35.0 %	35.0 %
State income tax, net of federal effect	0.2	1.0	0.4
Research tax credits	(3.7)	(0.4)	(4.7)
Differences in rates and taxability of foreign subsidiaries and joint ventures	(6.0)	(12.1)	(4.6)
Other, net	(0.4)	—	1.0
Effective tax rate	25.1 %	23.5 %	27.1 %

Our income tax rates are generally less than the 35 percent U.S. statutory income tax rate primarily because of lower taxes on foreign earnings and research tax credits. As a result of a restructuring of our foreign operations in 2013, our 2013 effective tax rate is approximately 1 percent less than it would have been without restructuring. On January 2, 2013, the American Taxpayer Relief Act of 2012 was signed into law and reinstated the research tax credit back to 2012. As tax law changes are accounted for in the period of enactment, we recognized a \$28 million discrete tax benefit in the first quarter of 2013. We also recognized a discrete tax expense of \$17 million in the first quarter which primarily related to the write-off of a deferred tax asset deemed unrecoverable. Also included in 2013 is a third quarter discrete net tax expense of \$7 million, primarily related to U.S. federal tax return true-up adjustments and third quarter enactment of U.K. tax law changes. Additionally, our effective tax rate for 2013 included a fourth quarter discrete net tax benefit of \$21 million primarily due to the release of U.S. deferred tax liabilities related to prior years unremitted income of certain Indian and Mexican subsidiaries now considered to be permanently reinvested, as well as adjustments to our income tax accounts principally based on our 2012 state tax return filings. Our 2012 income tax provision included a one-time \$134 million tax benefit which resulted from tax planning strategies and tax return elections made with respect to our U.K. operations.

In September 2013, the Internal Revenue Service released final tangible personal property regulations regarding the deduction and capitalization of expenditures related to tangible property. The new rules will become effective for taxable years beginning on or after January 1, 2014. While we are still finalizing our analysis, we do not believe that these regulations will have a material impact on our *Consolidated Financial Statements*.

Retained earnings of our U.K. domiciled subsidiaries and certain Singapore, German, Indian and Mexican subsidiaries are considered to be permanently reinvested. During 2013, we released \$12 million of U.S. deferred tax liabilities related to prior years unremitted income of certain Indian and Mexican subsidiaries considered to be permanently reinvested starting in 2013. In addition, earnings of our China operations generated after December 31, 2011, are considered to be permanently reinvested. U.S. deferred tax is not provided on these permanently reinvested earnings. Our permanently reinvested foreign earnings are expected to be used for items such as capital expenditures and to fund joint ventures outside of the U.S. The total permanently reinvested retained earnings and related cumulative translation adjustment balances for these entities were \$3.1 billion, \$2.3 billion and \$1.5 billion for the years ended December 31, 2013, 2012, and 2011, respectively. These amounts were determined primarily based on book retained earnings balances for these subsidiaries translated at historical rates. The determination of the deferred tax liability related to these retained earnings and cumulative translation adjustment balances which are considered to be permanently reinvested outside the U.S. is not practicable. We may periodically repatriate a portion of these earnings to the extent we can do so essentially tax-free or at minimal tax cost.

For our remaining subsidiary companies and joint ventures outside the U.S., we provide for the additional taxes that would be due upon the dividend distribution of the income of those foreign subsidiaries and joint ventures assuming the full utilization of foreign tax credits. Deferred tax liabilities on unremitted earnings of foreign subsidiaries and joint ventures, including those in China generated in years prior to 2012, were \$201 million and \$213 million at December 31, 2013 and 2012, respectively. We have \$709 million of retained earnings and related cumulative translation adjustments in our China operations generated prior to December 31, 2011 for which we have provided a U.S. deferred tax liability of \$151 million. We anticipate that these earnings will be distributed to the U.S. within the next five years.

Income before income taxes included equity income of foreign joint ventures of \$203 million, \$192 million and \$234 million for the years ended December 31, 2013, 2012 and 2011, respectively. This equity income is recorded net of foreign taxes. Additional U.S. income taxes of \$13 million, \$9 million and \$49 million for the years ended December 31, 2013, 2012 and 2011, respectively, were provided for the additional U.S. taxes that will ultimately be due upon the distribution of the foreign joint venture equity income.

Carryforward tax benefits and the tax effect of temporary differences between financial and tax reporting that give rise to net deferred tax assets were as follows:

In millions	December 31,	
	2013	2012
<b>Deferred tax assets</b>		
U.S. federal and state carryforward benefits	\$ 124	\$ 115
Foreign carryforward benefits	63	50
Employee benefit plans	328	369
Warranty and marketing expenses	332	308
Accrued expenses	70	75
Other	51	78
Gross deferred tax assets	968	995
Valuation allowance	(101)	(95)
Total deferred tax assets	867	900
<b>Deferred tax liabilities</b>		
Property, plant and equipment	(304)	(218)
Unremitted income of foreign subsidiaries and joint ventures	(201)	(213)
Employee benefit plans	(158)	(47)
Other	(27)	(26)
Total deferred tax liabilities	(690)	(504)
Net deferred tax assets	\$ 177	\$ 396

Our 2013 U.S. federal and state carryforward benefits include \$124 million of state credit and net operating loss carryforward benefits that begin to expire in 2014. Our foreign carryforward benefits include \$63 million of net operating loss carryforwards that begin to expire in 2014. A valuation allowance is recorded to reduce the gross deferred tax assets to an amount we believe is more likely than not to be realized. The valuation allowance increased in 2013 by a net \$6 million and increased in 2012 by a net \$24 million. The valuation allowance is primarily attributable to the uncertainty regarding the realization of a portion of the U.S. state and foreign net operating loss and tax credit carryforward benefits. Prepaid and other current assets include deferred tax assets of \$232 million and \$232 million for the years ended December 31, 2013 and 2012, respectively. In addition, prepaid and other current assets include refundable income taxes of \$152 million and \$240 million for the years ended December 31, 2013 and 2012, respectively. Other assets include deferred tax assets of \$61 million and \$177 million for the years ended December 31, 2013 and 2012, respectively. In addition, other assets include \$59 million of long-term refundable income taxes for the year ended December 31, 2013. Other liabilities and deferred revenue included deferred tax liabilities of \$116 million and \$13 million for the years ended December 31, 2013 and 2012, respectively.



A reconciliation of unrecognized tax benefits was as follows:

<b>In millions</b>	
Balance at December 31, 2010	\$ 85
Additions based on tax positions related to the current year	5
Additions based on tax positions related to the prior years	44
Reductions for tax positions related to prior years	(3)
Reductions for tax positions relating to settlements with taxing authorities	(39)
Reductions for tax positions relating to lapse of statute of limitations	(6)
Balance at December 31, 2011	86
Additions based on tax positions related to the current year	4
Additions based on tax positions related to the prior years	57
Reductions for tax positions related to prior years	(2)
Balance at December 31, 2012	145
Additions based on tax positions related to the current year	10
Additions based on tax positions related to the prior years	21
Reductions for tax positions related to prior years	(6)
Reductions for tax positions relating to lapse of statute of limitations	(1)
Balance at December 31, 2013	<u>\$ 169</u>

Included in the December 31, 2013 and 2012, balances are \$107 million and \$87 million related to tax positions that, if recognized, would favorably impact the effective tax rate in future periods. Also, we had accrued interest expense related to the unrecognized tax benefits of \$3 million, \$2 million and \$7 million as of December 31, 2013, 2012 and 2011, respectively. We recognize potential accrued interest and penalties related to unrecognized tax benefits in income tax expense. For the years ended December 31, 2013, 2012 and 2011, we recognized \$1 million, \$(3) million and \$(15) million in net interest expense, respectively. In 2011, as a result of the settlement of certain tax positions with tax authorities in China, we reduced our liability for unrecognized tax benefits by \$39 million and the related net accrued interest of \$16 million. The \$39 million reduction was fully offset by adjustments to other income tax balance sheet accounts resulting in zero net income statement impact. As the settlement with the tax authorities included no interest or penalties being incurred, we recognized a \$16 million income tax benefit in 2011 from the release of the accrued interest previously recorded related to the unrecognized tax benefits that were settled.

Audit outcomes and the timing of audit settlements are subject to significant uncertainty. Although we believe that adequate provision has been made for such issues, there is the possibility that the ultimate resolution of such issues could have an adverse effect on our earnings. Conversely, if these issues are resolved favorably in the future, the related provision would be reduced, thus having a positive impact on earnings. We do not expect any significant change to our unrecognized tax benefits within the next year.

As a result of our global operations, we file income tax returns in various jurisdictions including U.S. federal, state and foreign jurisdictions. We are routinely subject to examination by taxing authorities throughout the world, including Australia, Belgium, Brazil, Canada, China, France, India, Mexico, the U.K. and the U.S. With few exceptions, our U.S. federal, major state and foreign jurisdictions are no longer subject to income tax assessments for years before 2010. We expect the U.S. examinations related to tax years 2011-2012 will commence during 2014.

**NOTE 5. MARKETABLE SECURITIES**

A summary of marketable securities, all of which are classified as current, was as follows:

In millions	December 31,					
	2013			2012		
	Cost	Gross unrealized gains/(losses)	Estimated fair value	Cost	Gross unrealized gains/(losses)	Estimated fair value
Available-for-sale						
Debt mutual funds <sup>(1)</sup>	\$ 99	\$ 2	\$ 101	\$ 139	\$ 3	\$ 142
Bank debentures	2	—	2	45	—	45
Certificates of deposit	22	—	22	47	—	47
Government debt securities-non-U.S.	3	(1)	2	3	—	3
Corporate debt securities	—	—	—	1	—	1
Equity securities and other <sup>(2)</sup>	10	13	23	—	9	9
Total marketable securities	\$ 136	\$ 14	\$ 150	\$ 235	\$ 12	\$ 247

<sup>(1)</sup> Contractual maturities are only applicable to debt mutual funds that utilize a Level 2 fair value.

<sup>(2)</sup> In the first quarter of 2013, we realized a \$9 million gain on the sale of equity securities.

The proceeds from sales and maturities of marketable securities and gross realized gains from the sale of AFS securities were as follows:

In millions	2013	2012	2011
Proceeds from sales and maturities of marketable securities	\$ 525	\$ 585	\$ 750
Gross realized gains from the sale of available-for-sale securities <sup>(1)</sup>	14	3	3

<sup>(1)</sup> Gross realized losses from the sale of available-for-sale securities were immaterial.

At December 31, 2013, the fair value of AFS investments in debt securities by contractual maturity was as follows:

Maturity date	Fair value (in millions)
1 year or less	\$ 50
1 - 5 years	4
5 - 10 years	1
Total	\$ 55

**NOTE 6. FAIR VALUE OF FINANCIAL INSTRUMENTS**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). We utilize market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable. We primarily apply the market approach for recurring fair value measurements and utilize the best available information. Accordingly, we utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. We are able to classify fair value balances based on the observability of those inputs. The fair value hierarchy prioritizes the inputs used to measure fair value giving the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). At December 31, 2013, we did not have any Level 3 financial assets or liabilities, other than those in our pension plan (see NOTE 12, "PENSION AND OTHER POSTRETIREMENT BENEFITS").

The majority of the assets and liabilities we carry at fair value are AFS securities and derivatives. The fair value of AFS securities are derived from Level 1 or Level 2 inputs. The predominance of market inputs are actively quoted and can be validated through external sources, including brokers, market transactions and third-party pricing services. The fair value measurement of derivatives are valued primarily using Level 2 inputs. Many of our derivative contracts are valued utilizing publicly available pricing data of contracts with similar terms. In other cases, the contracts are valued using current spot market data adjusted for the appropriate current forward curves provided by external financial institutions. We participate in commodity swap contracts, commodity zero-cost collar contracts, currency forward contracts and interest rate swaps. When material, we adjust the values of our derivative contracts for counter-party or our credit risk. There were no transfers into or out of Levels 2 or 3 during 2013.

The following table summarizes our financial instruments recorded at fair value in our *Consolidated Balance Sheets* at December 31, 2013:

In millions	Fair Value Measurements Using			Total
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
<b>Available-for-sale debt securities</b>				
Debt mutual funds	\$ 72	\$ 29	\$ —	\$ 101
Bank debentures	—	2	—	2
Certificates of deposit	—	22	—	22
Government debt securities-non-U.S.	—	2	—	2
<b>Available-for-sale equity securities</b>				
Information technology industry	23	—	—	23
<b>Derivative assets</b>				
Interest rate contracts	—	49	—	49
Foreign currency forward contracts	—	11	—	11
<b>Total assets</b>	<b>\$ 95</b>	<b>\$ 115</b>	<b>\$ —</b>	<b>\$ 210</b>
<b>Derivative liabilities</b>				
Commodity swap contracts	—	5	—	5
Foreign currency forward contracts	—	5	—	5
<b>Total liabilities</b>	<b>\$ —</b>	<b>\$ 10</b>	<b>\$ —</b>	<b>\$ 10</b>

The substantial majority of our assets were valued utilizing a market approach. A description of the valuation techniques and inputs used for our level 2 fair value measures was as follows:

- *Debt mutual funds*— Assets in Level 2 consist of exchange traded mutual funds that lack sufficient trading volume to be classified at Level 1. The fair value measure for these investments is the daily net asset value published on a regulated governmental website. Daily quoted prices are available from the issuing brokerage and are used on a test basis to corroborate this Level 2 input.
- *Bank debentures and Certificates of deposit*— These investments provide us with a fixed rate of return and generally range in maturity from six months to three years. The counter-parties to these investments are reputable financial institutions with investment grade credit ratings. Since these instruments are not tradable and must be settled directly by us with the respective financial institution, our fair value measure is the financial institutions' month-end statement.
- *Government debt securities-non-U.S. and Corporate debt securities*— The fair value measure for these securities are broker quotes received from reputable firms. These securities are infrequently traded on a national stock exchange and these values are used on a test basis to corroborate our Level 2 input measure.
- *Foreign currency forward contracts*— The fair value measure for these contracts are determined based on forward foreign exchange rates received from third-party pricing services. These rates are based upon market transactions and are periodically corroborated by comparing to third-party broker quotes.

[Table of Contents](#)

- *Commodity swap contracts*— The fair value measure for these contracts are current spot market data adjusted for the appropriate current forward curves provided by external financial institutions. The current spot price is the most significant component of this valuation and is based upon market transactions. We use third-party pricing services for the spot price component of this valuation which is periodically corroborated by market data from broker quotes.
- *Commodity zero cost collar contracts*— We utilize the month-end statement from the issuing financial institution as our fair value measure for this investment. We corroborate this valuation through the use of a third-party pricing service for similar assets and liabilities.
- *Interest rate contracts*— We currently have only one interest rate contract. We utilize the month-end statement from the issuing financial institution as our fair value measure for this investment. We corroborate this valuation through the use of a third-party pricing service for similar assets and liabilities.

The following tables summarize our financial instruments recorded at fair value in our *Consolidated Balance Sheets* at December 31, 2012:

In millions	Fair Value Measurements Using			Total
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
<b>Available-for-sale debt securities</b>				
Debt mutual funds	\$ 100	\$ 42	\$ —	\$ 142
Bank debentures	—	45	—	45
Certificates of deposit	—	47	—	47
Government debt securities-non-U.S.	—	3	—	3
Corporate debt securities	—	1	—	1
<b>Available-for-sale equity securities</b>				
Financial services industry	9	—	—	9
<b>Derivative assets</b>				
Interest rate contracts	—	88	—	88
Foreign currency forward contracts	—	3	—	3
Commodity swap contracts	—	1	—	1
Commodity zero cost collar contracts	—	1	—	1
Total assets	\$ 109	\$ 231	\$ —	\$ 340
<b>Derivative liabilities</b>				
Commodity swap contracts	—	2	—	2
Commodity zero cost collar contracts	—	1	—	1
Total liabilities	\$ —	\$ 3	\$ —	\$ 3

**Fair Value of Other Financial Instruments**

Based on borrowing rates currently available to us for bank loans with similar terms and average maturities, considering our risk premium, the fair value and carrying value of total debt, including current maturities, was as follows:

In millions	December 31,	
	2013	2012
Fair value of total debt	\$ 1,877	\$ 926
Carrying value of total debt	1,740	775

The carrying values of all other receivables and liabilities approximated fair values (derived from Level 2 inputs).

**NOTE 7. INVENTORIES**

Inventories are stated at the lower of cost or market. Inventories included the following:

In millions	December 31,	
	2013	2012
Finished products	\$ 1,487	\$ 1,393
Work-in-process and raw materials	1,005	939
Inventories at FIFO cost	2,492	2,332
Excess of FIFO over LIFO	(111)	(111)
Total inventories	\$ 2,381	\$ 2,221

**NOTE 8. PROPERTY, PLANT AND EQUIPMENT**

Details of our property, plant and equipment balance were as follows:

In millions	December 31,	
	2013	2012
Land and buildings	\$ 1,427	\$ 1,228
Machinery, equipment and fixtures	4,174	3,910
Construction in process <sup>(1)</sup>	809	738
Property, plant and equipment, gross	6,410	5,876
Less: Accumulated depreciation	(3,254)	(3,152)
Property, plant and equipment, net	\$ 3,156	\$ 2,724

<sup>(1)</sup> Construction in process included \$188 million in 2013 and \$175 million in 2012 related to our future light-duty diesel engine platform.

**NOTE 9. GOODWILL AND OTHER INTANGIBLE ASSETS**

The following table summarizes the changes in the carrying amount of goodwill for 2013 and 2012:

In millions	Components	Distribution	Power Generation	Engine	Total
Balance at December 31, 2011	\$ 311	\$ 10	\$ 12	\$ 6	\$ 339
Acquisitions	91	9	—	—	100
Translation and other	6	—	—	—	6
Balance at December 31, 2012	408	19	12	6	445
Acquisitions	—	13	—	—	13
Translation and other	3	(1)	1	—	3
Balance at December 31, 2013	\$ 411	\$ 31	\$ 13	\$ 6	\$ 461

Intangible assets that have finite useful lives are amortized over their estimated useful lives. The following table summarizes our other intangible assets with finite useful lives that are subject to amortization:

In millions	December 31,	
	2013	2012
Software	\$ 494	\$ 495
Less: Accumulated amortization	(218)	(218)
Net software	276	277
Trademarks, patents and other	135	140
Less: Accumulated amortization	(54)	(48)
Net trademarks, patents and other	81	92
Total	\$ 357	\$ 369

Amortization expense for software and other intangibles totaled \$86 million, \$64 million, and \$57 million for the years ended December 31, 2013, 2012 and 2011, respectively. Internal and external software costs (excluding those related to research, re-engineering and training), trademarks and patents are amortized generally over a 3 to 12 year period. The projected amortization expense of our intangible assets, assuming no further acquisitions or dispositions, was as follows:

In millions	For the years ended				
	2014	2015	2016	2017	2018
Projected amortization expense	\$ 74	\$ 78	\$ 72	\$ 51	\$ 27

**NOTE 10. DEBT**

**Loans Payable**

Loans payable at December 31, 2013 and 2012 were \$17 million and \$16 million, respectively, and consisted primarily of notes payable to financial institutions. The weighted-average interest rate for notes payable, bank overdrafts and current maturities of long-term debt at December 31, 2013, 2012 and 2011, was as follows:

	December 31,		
	2013	2012	2011
Weighted average interest rate	2.59	3.21	4.19

**Interest**

For the years ended December 31, 2013, 2012 and 2011, total interest incurred was \$48 million, \$39 million and \$48 million, respectively, and interest capitalized was \$7 million, \$7 million and \$4 million, respectively.

**Revolving Credit Facility**

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

The credit facility matures on November 9, 2017. Amounts payable under our revolving credit facility will rank pro rata with all of our unsecured, unsubordinated indebtedness. Up to \$200 million under our credit facility is available for swingline loans denominated in U.S. dollars. Advances under the facility bear interest at (i) a base rate or (ii) a rate equal to the LIBOR Rate plus an applicable margin based on the credit ratings of our outstanding senior unsecured long-term debt. Based on our current long-term debt ratings, the applicable margin on LIBOR rate loans was 0.875 percent per annum as of December 31, 2013. Advances under the facility may be prepaid without premium or penalty, subject to customary breakage costs.

The credit agreement includes various covenants, including, among others, maintaining a leverage ratio of no more than 3.25 to 1.0. As of December 31, 2013, we were in compliance with the covenants.

There were no outstanding borrowings under this facility at December 31, 2013. A reconciliation of the maximum capacity of our revolver to the amount available under the facility was as follows:

In millions	Revolving Credit Capacity at December 31, 2013
Maximum credit capacity of the revolving credit facility	\$ 1,750
Less: Letters of credit against revolving credit facility	23
Amount available for borrowing under the revolving credit facility	\$ 1,727

As of December 31, 2013, we also had \$310 million available for borrowings under our international and other domestic credit facilities. Commitments against the other domestic and international short-term facilities were \$17 million as of December 31, 2013 and \$16 million at the end of 2012.

**Long-term Debt**

In millions	December 31,	
	2013	2012
<b>Long-term debt</b>		
Export financing loan, 4.5%, due 2013	\$ —	\$ 23
Senior notes, 3.65%, due 2023	500	—
Debentures, 6.75%, due 2027	58	58
Debentures, 7.125%, due 2028	250	250
Senior notes, 4.875%, due 2043	500	—
Debentures, 5.65%, due 2098 (effective interest rate 7.48%)	165	165
Credit facilities related to consolidated joint ventures	92	88
Other	65	69
	<b>1,630</b>	653
Unamortized discount	(48)	(35)
Fair value adjustments due to hedge on indebtedness	49	88
Capital leases	92	53
Total long-term debt	<b>1,723</b>	759
Less: Current maturities of long-term debt	(51)	(61)
Long-term debt	<b>\$ 1,672</b>	\$ 698

Principal payments required on long-term debt during the next five years are as follows:

In millions	Required Principal Payments				
	2014	2015	2016	2017	2018
Payment	\$ 51	\$ 55	\$ 82	\$ 8	\$ 17

As a well-known seasoned issuer, we filed an automatic shelf registration for an undetermined amount of debt and equity securities with the Securities and Exchange Commission on September 16, 2013. Under this shelf registration we may offer, from time to time, debt securities, common stock, preferred and preference stock, depositary shares, warrants, stock purchase contracts and stock purchase units.

In September 2013, we issued \$1 billion aggregate principal amount of senior notes consisting of \$500 million aggregate principal amount of 3.65% senior unsecured notes due in 2023 and \$500 million aggregate principal amount of 4.875% senior unsecured notes due in 2043. We received net proceeds of \$979 million. The senior notes pay interest semi-annually on April 1 and October 1, commencing on April 1, 2014. The indenture governing the senior notes contains covenants that, among other matters, limit (i) our ability to consolidate or merge into, or sell, assign, convey, lease, transfer or otherwise dispose of all or substantially all of our and our subsidiaries' assets to another person, (ii) our and certain of our subsidiaries' ability to create or assume liens and (iii) our and certain of our subsidiaries' ability to engage in sale and leaseback transactions.

Interest on the 6.75% debentures is payable on February 15 and August 15 each year.

Interest on the \$250 million 7.125% debentures and \$165 million 5.65% debentures is payable on March 1 and September 1 of each year. The debentures are unsecured and are not subject to any sinking fund requirements. We can redeem the 7.125% debentures and the 5.65% debentures at any time prior to maturity at the greater of par plus accrued interest or an amount designed to ensure that the debenture holders are not penalized by the early redemption.

During 2010, two of our wholly-owned Brazilian subsidiaries entered into a loan agreement for a loan in local currency in an amount equivalent to US\$50 million, at drawdown, at a fixed rate of 4.5% to finance its exports over the next three years. The principal of the loan had a two-year grace period and began amortizing in 2012 and was completed in 2013.

Our debt agreements contain several restrictive covenants. The most restrictive of these covenants applies to our revolving credit facility which will upon default, among other things, limit our ability to incur additional debt or issue preferred stock, enter into sale-leaseback transactions, sell or create liens on our assets, make investments and merge or consolidate with any other person. In addition, we are subject to a maximum debt-to-EBITDA ratio financial covenant. As of December 31, 2013, we were in compliance with all of the covenants under our borrowing agreements.

**NOTE 11. PRODUCT WARRANTY LIABILITY**

We charge the estimated costs of warranty programs, other than product recalls, to income at the time products are shipped to customers. We use historical claims experience to develop the estimated liability. We review product recall programs on a quarterly basis and, if necessary, record a liability when we commit to an action, or when they become probable and estimable, which is reflected in the provision for warranties issued line. We also sell extended warranty coverage on several engines. A tabular reconciliation of the product warranty liability, including the deferred revenue related to our extended warranty coverage and accrued recall programs was as follows:

In millions	December 31,	
	2013	2012
Balance, beginning of year	\$ 1,088	\$ 1,014
Provision for warranties issued	431	415
Deferred revenue on extended warranty contracts sold	189	210
Payments	(427)	(416)
Amortization of deferred revenue on extended warranty contracts	(115)	(103)
Changes in estimates for pre-existing warranties	(35)	(33)
Foreign currency translation	(2)	1
Balance, end of year	\$ 1,129	\$ 1,088

Warranty related deferred revenue, supplier recovery receivables and the long-term portion of the warranty liability on our *Consolidated Balance Sheets* were as follows:

In millions	December 31,		Balance Sheet Location
	2013	2012	
Deferred revenue related to extended coverage programs			
Current portion	\$ 145	\$ 111	Deferred revenue
Long-term portion	349	309	Other liabilities and deferred revenue
Total	\$ 494	\$ 420	
Receivables related to estimated supplier recoveries			
Current portion	\$ 5	\$ 7	Trade and other receivables
Long-term portion	5	6	Other assets
Total	\$ 10	\$ 13	
Long-term portion of warranty liability	\$ 275	\$ 282	Other liabilities and deferred revenue

**NOTE 12. PENSION AND OTHER POSTRETIREMENT BENEFITS**

**Pension Plans**

We sponsor several contributory and noncontributory pension plans covering substantially all employees. Generally, hourly employee pension benefits are earned based on years of service and compensation during active employment while future benefits for salaried employees are determined using a cash balance formula. However, the level of benefits and terms of vesting may vary among plans. Pension plan assets are administered by trustees and are principally invested in fixed income securities and equity securities. It is our policy to make contributions to our various qualified plans in accordance with statutory and contractual funding requirements and any additional contributions we determine are appropriate.

***Obligations, Assets and Funded Status***

Benefit obligation balances presented below reflect the projected benefit obligation (PBO) for our pension plans. The changes in the benefit obligations, the various plan assets, the funded status of the plans and the amounts recognized in our *Consolidated Balance Sheets* for our significant pension plans were as follows:



In millions	Qualified and Non-Qualified Pension Plans			
	U.S. Plans		U.K. Plans	
	2013	2012	2013	2012
<b>Change in benefit obligation</b>				
Benefit obligation at the beginning of the year	\$ 2,454	\$ 2,243	\$ 1,269	\$ 1,128
Service cost	70	58	21	21
Interest cost	93	103	57	59
Actuarial losses (gains)	(193)	207	96	52
Benefits paid from fund	(150)	(148)	(50)	(41)
Benefits paid directly by employer	(13)	(10)	—	—
Exchange rate changes	—	—	37	52
Curtailed gain	—	—	—	(2)
Other	—	1	(1)	—
Benefit obligation at end of year	\$ 2,261	\$ 2,454	\$ 1,429	\$ 1,269
<b>Change in plan assets</b>				
Fair value of plan assets at beginning of year	\$ 2,327	\$ 2,091	\$ 1,324	\$ 1,200
Actual return on plan assets	168	284	142	88
Employer contributions	100	100	56	22
Benefits paid	(150)	(148)	(50)	(41)
Exchange rate changes	—	—	44	55
Fair value of plan assets at end of year	\$ 2,445	\$ 2,327	\$ 1,516	\$ 1,324
Funded status (including underfunded and nonfunded plans) at end of year	\$ 184	\$ (127)	\$ 87	\$ 55
<b>Amounts recognized in consolidated balance sheets</b>				
Prepaid pensions - long-term assets	\$ 427	\$ 127	\$ 87	\$ 55
Accrued compensation, benefits and retirement costs - current liabilities	(11)	(10)	—	—
Pensions - long-term liabilities	(232)	(244)	—	—
Net amount recognized	\$ 184	\$ (127)	\$ 87	\$ 55
<b>Amounts recognized in accumulated other comprehensive loss consist of:</b>				
Net actuarial loss	\$ 478	\$ 734	\$ 361	\$ 349
Prior service credit	(1)	(1)	—	—
Net amount recognized	\$ 477	\$ 733	\$ 361	\$ 349

In addition to the pension plans in the above table, we also maintain less significant defined benefit pension plans primarily in 4 other countries outside of the U.S. and the U.K. that comprise approximately 2 percent and 4 percent of our pension plan assets and obligations, respectively. These plans are reflected in "Other liabilities and deferred revenue" on our *Consolidated Balance Sheets*.

The following table presents information regarding total accumulated benefit obligation, PBO's and underfunded pension plans that are included in the preceding table:

In millions	Qualified and Non-Qualified Pension Plans			
	U.S. Plans		U.K. Plans	
	2013	2012	2013	2012
Total accumulated benefit obligation	\$ 2,231	\$ 2,417	\$ 1,309	\$ 1,167
Plans with accumulated benefit obligation in excess of plan assets				
Accumulated benefit obligation	212	216	—	—
Plans with projected benefit obligation in excess of plan assets				
Projected benefit obligation	243	254	—	—

**Components of Net Periodic Pension Cost**

The following table presents the net periodic pension cost under our plans:

In millions	Qualified and Non-Qualified Pension Plans					
	U.S. Plans			U.K. Plans		
	2013	2012	2011	2013	2012	2011
Service cost	\$ 70	\$ 58	\$ 51	\$ 21	\$ 21	\$ 20
Interest cost	93	103	109	57	59	58
Expected return on plan assets	(167)	(157)	(151)	(72)	(81)	(74)
Amortization of prior service (credit) cost	(1)	(1)	(1)	—	1	3
Recognized net actuarial loss	62	47	39	24	14	14
Net periodic pension cost	\$ 57	\$ 50	\$ 47	\$ 30	\$ 14	\$ 21

Other changes in benefit obligations and plan assets recognized in other comprehensive income in 2013, 2012 and 2011 were as follows:

In millions	2013	2012	2011
Amortization of prior service (cost) credit	\$ 1	\$ (1)	\$ (2)
Recognized actuarial loss	(86)	(61)	(53)
Incurred prior service cost	—	1	1
Incurred actuarial (gain) loss	(168)	124	138
Foreign exchange translation adjustments	10	16	—
Total recognized in other comprehensive income	\$ (243)	\$ 79	\$ 84
Total recognized in net periodic pension cost and other comprehensive income	\$ (156)	\$ 143	\$ 152

The amount in accumulated other comprehensive loss expected to be recognized as a component of net periodic pension cost during the next fiscal year is a net actuarial loss of \$57 million.

**Assumptions**

The table below presents various assumptions used in determining the pension benefit obligation for each year and reflects weighted-average percentages for the various plans as follows:

	Qualified and Non-Qualified Pension Plans			
	U.S. Plans		U.K. Plans	
	2013	2012	2013	2012
Discount rate	4.83%	3.97%	4.60%	4.70%
Compensation increase rate	4.91%	4.90%	4.50%	4.00%

The table below presents various assumptions used in determining the net periodic pension cost and reflects weighted-average percentages for the various plans as follows:

	Qualified and Non-Qualified Pension Plans					
	U.S. Plans			U.K. Plans		
	2013	2012	2011	2013	2012	2011
Discount rate	3.97%	4.82%	5.42%	4.70%	5.20%	5.80%
Expected return on plan assets	8.00%	8.00%	8.00%	5.80%	6.50%	7.00%
Compensation increase rate	4.91%	4.00%	4.00%	4.00%	4.25%	4.50%

**Plan Assets**

Our investment policies in the U.S. and U.K. provide for the rebalancing of assets to maintain our long-term strategic asset allocation. We are committed to its long-term strategy and do not attempt to time the market given empirical evidence that asset allocation is more critical than individual asset or investment manager selection. Rebalancing of the assets has and continues to occur. The rebalancing is critical to having the proper weighting of assets to achieve the expected total portfolio returns. We believe that our portfolio is highly diversified and does not have any significant exposure to concentration risk. The plan assets for our defined benefit pension plans do not include any of our common stock.

**U.S. Plan Assets**

For the U.S. qualified pension plans, our assumption for the expected return on assets was 8.0 percent in 2013. Projected returns are based primarily on broad, publicly traded equity and fixed income indices and forward-looking estimates of active portfolio and investment management. We expect additional positive returns from this active investment management. Based on the historical returns and forward-looking return expectations, we have elected to use an assumption of 7.5 percent per year beginning in 2014.

The primary investment objective is to exceed, on a net-of-fee basis, the rate of return of a policy portfolio comprised of the following:

Asset Class	Target	Range
U.S. equities	9.0%	+/-5.0%
Non-U.S. equities	3.0%	+/-3.0%
Global equities	10.0%	+/-3.0%
Total equities	22.0%	
Real estate	7.0%	+3.0/-7.0%
Private equity	7.0%	+3.0/-7.0%
Fixed income	64.0%	+/-5.0%
Total	100.0%	

The fixed income component is structured to represent a custom bond benchmark that will closely hedge the change in the value of our liabilities. This component is structured in such a way that its benchmark covers approximately 95 percent of the plan's exposure to changes in its discount rate (AA corporate bond yields). In order to achieve a hedge on more than the targeted 64 percent of plan assets invested in fixed income securities, our Benefits Policy Committee (BPC) permits the fixed income managers, other managers or the custodian/trustee to utilize derivative securities, as part of a liability driven investment strategy to further reduce the plan's risk of declining interest rates. However, all managers hired to manage assets for the trust are prohibited from using leverage unless specifically discussed with the BPC and approved in their guidelines.

**U.K. Plan Assets**

For the U.K. qualified pension plans, our assumption for the expected return on assets was 5.8 percent in 2013. The methodology used to determine the rate of return on pension plan assets in the U.K. was based on establishing an equity-risk premium over current long-term bond yields adjusted based on target asset allocations. Our strategy with respect to our investments in these assets is to be invested in a suitable mixture of return-seeking assets (equities and real estate) and liability matching assets (bonds) with a long-term outlook. Therefore, the risk and return balance of our U.K. asset portfolio should reflect a long-term horizon. To achieve these objectives we have established the following targets:

Asset Class	Target	Range
Global equities	30.5%	+2.5/-5.0%
Real estate	7.5%	+2.5/-5.0%
Re-insurance	5.0%	+2.5/-5.0%
Private equity	7.5%	+2.5/-5.0%
Corporate credit instruments	4.5%	+2.5/-4.5%
Fixed income	45.0%	+5.5/-2.0%
Total	100.0%	

As part of our strategy in the U.K. we have not prohibited the use of any financial instrument, including derivatives. Based on the above discussion, we have elected to use our assumption of 5.8 percent per year beginning in 2014.

**Fair Value of U.S. Plan Assets**

The fair values of U.S. pension plan assets by asset category were as follows:

In millions	Fair Value Measurements as of December 31, 2013			Total
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
<b>Equities</b>				
U.S.	\$ 96	\$ 375	\$ —	\$ 471
Non-U.S.	143	138	—	281
<b>Fixed Income</b>				
Government debt	325	455	—	780
Corporate debt				
U.S.	279	244	—	523
Non-U.S.	64	—	—	64
Asset/mortgaged backed securities	12	—	—	12
Net cash equivalents <sup>(1)</sup>	36	—	—	36
Derivative instruments <sup>(2)</sup>	—	2	—	2
Private equity and real estate <sup>(3)</sup>	—	—	296	296
<b>Total</b>	<b>\$ 955</b>	<b>\$ 1,214</b>	<b>\$ 296</b>	<b>\$ 2,465</b>
Pending trade/purchases/sales				(28)
Accruals <sup>(4)</sup>				8
<b>Total</b>				<b>\$ 2,445</b>

In millions	Fair Value Measurements as of December 31, 2012			Total
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
<b>Equities</b>				
U.S.	\$ 113	\$ 542	\$ —	\$ 655
Non-U.S.	177	127	—	304
<b>Fixed Income</b>				
Government debt	475	132	—	607
Corporate debt				
U.S.	203	191	—	394
Non-U.S.	42	—	—	42
Asset/mortgaged backed securities	13	—	—	13
Net cash equivalents <sup>(1)</sup>	35	—	—	35
Private equity and real estate <sup>(3)</sup>	—	—	286	286
<b>Total</b>	<b>\$ 1,058</b>	<b>\$ 992</b>	<b>\$ 286</b>	<b>\$ 2,336</b>
Pending trade/purchases/sales				(16)
Accruals <sup>(4)</sup>				7
<b>Total</b>				<b>\$ 2,327</b>

(1) Cash equivalents include commercial paper, short-term government/agency, mortgage and credit instruments.

(2) Derivative instruments include interest rate swaps, foreign currency forward contracts and credit default swaps.

(3) The instruments in private equity and real estate funds, for which quoted market prices are not available, are valued at their estimated fair value as determined by applicable investment managers or by audited financial statement of the funds.

(4) Interest or dividends that had not been settled as of the year ended December 31.

The reconciliation of Level 3 assets was as follows:

In millions	Fair Value Measurements as of December 31, Using Significant Unobservable Inputs (Level 3)		
	Private Equity	Real Estate	Total
Balance at December 31, 2011	\$ 147	\$ 119	\$ 266
Actual return on plan assets			
Unrealized (losses) gains on assets still held at the reporting date	15	9	24
Purchases, sales and settlements, net	(6)	2	(4)
Balance at December 31, 2012	156	130	286
Actual return on plan assets			
Unrealized (losses) gains on assets still held at the reporting date	20	10	30
Purchases, sales and settlements, net	(23)	3	(20)
Balance at December 31, 2013	\$ 153	\$ 143	\$ 296

#### Fair Value of U.K. Plan Assets

In July 2012, the U.K. pension plan purchased an insurance contract that will guarantee payment of specified pension liabilities. The contract defers payment for 10 years. This is included in the table below in Level 3 at a value of \$440 million at December 31, 2013 and \$424 million at December 31, 2012.

The fair values of U.K. pension plan assets by asset category were as follows:

In millions	Fair Value Measurements as of December 31, 2013			
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
<b>Equities</b>				
U.S.	\$ —	\$ 270	\$ —	\$ 270
Non-U.S.	—	328	—	328
<b>Fixed Income</b>				
Government debt	—	120	—	120
Corporate debt non-U.S.	—	138	—	138
Net cash equivalents <sup>(1)</sup>	13	—	—	13
Derivative instruments <sup>(2)</sup>	—	24	—	24
Re-insurance	—	66	—	66
Private equity, real estate & insurance <sup>(3)</sup>	—	—	557	557
<b>Total</b>	\$ 13	\$ 946	\$ 557	\$ 1,516

In millions	Fair Value Measurements as of December 31, 2012			
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
<b>Equities</b>				
U.S.	\$ —	\$ 251	\$ —	\$ 251
Non-U.S.	—	325	—	325
<b>Fixed Income</b>				
Government debt	—	191	—	191
Net cash equivalents <sup>(1)</sup>	10	—	—	10
Re-insurance	—	61	—	61
Private equity, real estate & insurance <sup>(3)</sup>	—	—	486	486
<b>Total</b>	\$ 10	\$ 828	\$ 486	\$ 1,324

(1) Cash equivalents include commercial paper, short-term government/agency, mortgage and credit instruments.

(2) Derivative instruments include interest rate swaps, foreign currency forward contracts and credit default swaps.

(3) The instruments in private equity and real estate funds, for which quoted market prices are not available, are valued at their estimated fair value as determined by applicable investment managers or by audited financial statement of the funds.

The reconciliation of Level 3 assets was as follows:

In millions	Fair Value Measurements as of December 31, Using Significant Unobservable Inputs (Level 3)			
	Insurance	Real Estate	Private Equity	Total
Balance at December 31, 2011	\$ —	\$ 33	\$ 14	\$ 47
Actual return on plan assets				
Unrealized (losses) gains on assets still held at the reporting date	13	1	1	15
Purchases, sales and settlements, net	411	—	13	424
Balance at December 31, 2012	424	34	28	486
Actual return on plan assets				
Unrealized (losses) gains on assets still held at the reporting date	29	2	5	36
Purchases, sales and settlements, net	(13)	33	15	35
Balance at December 31, 2013	\$ 440	\$ 69	\$ 48	\$ 557

#### Level 3 Assets

The investments in an insurance contract, private equity and real estate funds, for which quoted market prices are not available, are valued at their estimated fair value as determined by applicable investment managers or by quarterly financial statements of the funds. These financial statements are audited at least annually. In conjunction with our investment consultant, we monitor the fair value of the insurance contract as periodically reported by our insurer and their counterparty risk. The fair value of all real estate properties, held in the partnerships, are valued at least once per year by an independent professional real estate valuation firm. Fair value generally represents the fund's proportionate share of the net assets of the investment partnerships as reported by the general partners of the underlying partnerships. Some securities with no readily available market are initially valued at cost, utilizing independent professional valuation firms as well as market comparisons with subsequent adjustments to values which reflect either the basis of meaningful third-party transactions in the private market or the fair value deemed appropriate by the general partners of the underlying investment partnerships. In such instances, consideration is also given to the financial condition and operating results of the issuer, the amount that the investment partnerships can reasonably expect to realize upon the sale of the securities and any other factors deemed relevant. The estimated fair values are subject to uncertainty and therefore may differ from the values that would have been used had a ready market for such investments existed and such differences could be material.

#### *Estimated Future Contributions and Benefit Payments*

We plan to contribute approximately \$205 million to our defined benefit pension plans in 2014. The table below presents expected future benefit payments under our pension plans:

In millions	Qualified and Non-Qualified Pension Plans					
	2014	2015	2016	2017	2018	2019 - 2023
Expected benefit payments	\$ 225	\$ 228	\$ 235	\$ 238	\$ 244	\$ 1,271

#### *Other Pension Plans*

We also sponsor defined contribution plans for certain hourly and salaried employees. Our contributions to these plans were \$66 million, \$74 million and \$72 million for the years ended December 31, 2013, 2012 and 2011.

#### **Other Postretirement Benefits**

Our other postretirement benefit plans provide various health care and life insurance benefits to eligible employees, who retire and satisfy certain age and service requirements, and their dependents. The plans are contributory and contain cost-sharing features such as caps, deductibles, coinsurance and spousal contributions. Employer contributions are limited by formulas in each plan. Retiree contributions for health care benefits are adjusted annually and we reserve the right to change benefits covered under these plans. There were no plan assets for the postretirement benefit plans as our policy is to fund benefits and expenses for these plans as claims and premiums are incurred.

**Obligations and Funded Status**

Benefit obligation balances presented below reflect the accumulated postretirement benefit obligations (APBO) for our other postretirement benefit plans. The changes in the benefit obligations, the funded status of the plans and the amounts recognized in our *Consolidated Balance Sheets* for our significant other postretirement benefit plans were as follows:

In millions	2013	2012
<b>Change in benefit obligation</b>		
Benefit obligation at the beginning of the year	\$ 478	\$ 483
Interest cost	17	21
Plan participants' contributions	10	8
Plan amendments	—	(4)
Actuarial losses (gains)	(49)	21
Benefits paid directly by employer	(58)	(51)
Benefit obligation at end of year	<u>\$ 398</u>	<u>\$ 478</u>
<b>Funded status at end of year</b>		
	<u>\$ (398)</u>	<u>\$ (478)</u>
<b>Amounts recognized in consolidated balance sheets</b>		
Accrued compensation, benefits and retirement costs - current liabilities	\$ (42)	\$ (46)
Postretirement benefits other than pensions-long-term liabilities	(356)	(432)
Net amount recognized	<u>\$ (398)</u>	<u>\$ (478)</u>
<b>Amounts recognized in accumulated other comprehensive loss consist of:</b>		
Net actuarial loss	\$ 27	\$ 83
Prior service credit	(5)	(6)
Net amount recognized	<u>\$ 22</u>	<u>\$ 77</u>

In addition to the other postretirement plans in the above table, we also maintain less significant postretirement plans in four other countries outside the U.S. that comprise less than 5 percent of our postretirement obligations. These plans are reflected in "Other liabilities and deferred revenue" in our *Consolidated Balance Sheets*.

**Components of Net Periodic Other Postretirement Benefits Cost**

The following table presents the net periodic other postretirement benefits cost under our plans:

In millions	2013	2012	2011
Interest cost	\$ 17	\$ 21	\$ 24
Amortization of prior service credit	—	(5)	(8)
Recognized net actuarial loss	6	3	—
Other	—	1	1
Net periodic other postretirement benefit cost	<u>\$ 23</u>	<u>\$ 20</u>	<u>\$ 17</u>

Other changes in benefit obligations recognized in other comprehensive income in 2013, 2012 and 2011 were as follows:

In millions	2013	2012	2011
Amortization of prior service credit	\$ —	\$ 5	\$ 8
Recognized actuarial loss	(6)	(3)	—
Incurred actuarial (gain) loss	(49)	20	16
Incurred prior service credit	—	(4)	—
Other	—	(1)	—
Total recognized in other comprehensive income	<u>\$ (55)</u>	<u>\$ 17</u>	<u>\$ 24</u>
Total recognized in net periodic other postretirement benefit cost and other comprehensive income	<u>\$ (32)</u>	<u>\$ 37</u>	<u>\$ 41</u>

The amount in accumulated other comprehensive loss expected to be recognized as a component of net periodic other postretirement benefit cost during the next fiscal year is zero.

**Assumptions**

The table below presents assumptions used in determining the other postretirement benefit obligation for each year and reflects weighted-average percentages for our other postretirement plans as follows:

	2013	2012
Discount rate	4.55%	3.70%

The table below presents assumptions used in determining the net periodic other postretirement benefits cost and reflects weighted-average percentages for the various plans as follows:

	2013	2012	2011
Discount rate	3.70%	4.70%	5.20%

Our consolidated other postretirement benefit obligation is determined by application of the terms of health care and life insurance plans, together with relevant actuarial assumptions and health care cost trend rates. For measurement purposes, a 7.50 percent annual rate of increase in the per capita cost of covered health care benefits was assumed in 2013. The rate is assumed to decrease on a linear basis to 5.00 percent through 2019 and remain at that level thereafter. An increase in the health care cost trends of 1 percent would increase our APBO by \$19 million as of December 31, 2013 and the net periodic other postretirement benefit cost for 2014 by \$1 million. A decrease in the health care cost trends of 1 percent would decrease our APBO by \$16 million as of December 31, 2013 and the net periodic other postretirement benefit cost for 2014 by \$1 million.

**Estimated Benefit Payments**

The table below presents expected benefit payments under our other postretirement benefit plans:

In millions	2014	2015	2016	2017	2018	2019 - 2023
Expected benefit payments	\$ 43	\$ 41	\$ 38	\$ 36	\$ 33	\$ 140

**NOTE 13. OTHER LIABILITIES AND DEFERRED REVENUE**

Other liabilities and deferred revenue included the following:

In millions	December 31,	
	2013	2012
Deferred revenue	\$ 414	\$ 368
Accrued warranty	275	282
Accrued compensation	184	168
Other long-term liabilities	357	246
Other liabilities and deferred revenue	<u>\$ 1,230</u>	<u>\$ 1,064</u>

**NOTE 14. COMMITMENTS AND CONTINGENCIES**

We are subject to numerous lawsuits and claims arising out of the ordinary course of our business, including actions related to product liability; personal injury; the use and performance of our products; warranty matters; patent, trademark or other intellectual property infringement; contractual liability; the conduct of our business; tax reporting in foreign jurisdictions; distributor termination; workplace safety; and environmental matters. We also have been identified as a potentially responsible party at multiple waste disposal sites under U.S. federal and related state environmental statutes and regulations and may have joint and several liability for any investigation and remediation costs incurred with respect to such sites. We have denied liability with respect to many of these lawsuits, claims and proceedings and are vigorously defending such lawsuits, claims and proceedings. We carry various forms of commercial, property and casualty, product liability and other forms of insurance; however, such insurance may not be applicable or adequate to cover the costs associated with a judgment against us with respect to these lawsuits, claims and proceedings. We do not believe that these lawsuits are material individually or in the aggregate. While we believe we have also established adequate accruals for our expected future liability with respect to pending lawsuits, claims and proceedings, where the nature and extent of any such liability can be reasonably estimated based upon then presently available information, there can be no assurance that the final resolution of any existing or future lawsuits, claims or proceedings will not have a material adverse effect on our business, results of operations, financial condition or cash flows.



We conduct significant business operations in Brazil that are subject to the Brazilian federal, state and local labor, social security, tax and customs laws. While we believe we comply with such laws, they are complex, subject to varying interpretations and we are often engaged in litigation regarding the application of these laws to particular circumstances.

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

#### **U.S. Distributor Commitments**

Our distribution agreements with independent and partially-owned distributors generally have a renewable three-year term and are restricted to specified territories. Our distributors develop and maintain a network of dealers with which we have no direct relationship. Our distributors are permitted to sell other, noncompetitive products only with our consent. We license all of our distributors to use our name and logo in connection with the sale and service of our products, with no right to assign or sublicense the trademarks, except to authorized dealers, without our consent. Products are sold to the distributors at standard domestic or international distributor net prices, as applicable. Net prices are wholesale prices we establish to permit our distributors an adequate margin on their sales. Subject to local laws, we can generally refuse to renew these agreements upon expiration or terminate them upon written notice for inadequate sales, change in principal ownership and certain other reasons. Distributors also have the right to terminate the agreements upon 60-day notice without cause, or 30-day notice for cause. Upon termination or failure to renew, we are required to purchase the distributor's current inventory, signage and special tools and may, at our option purchase other assets of the distributor, but are under no obligation to do so.

#### **Other Guarantees and Commitments**

In addition to the matters discussed above, from time to time we periodically enter into other guarantee arrangements, including guarantees of non-U.S. distributor financing, residual value guarantees on equipment under operating leases and other miscellaneous guarantees of third-party obligations. As of December 31, 2013, the maximum potential loss related to these other guarantees was \$6 million. The liability related to these guarantees was less than \$1 million.

We have arrangements with certain suppliers that require us to purchase minimum volumes or be subject to monetary penalties. The penalty amounts are less than our purchase commitments and essentially allow the supplier to recover their tooling costs in most instances. As of December 31, 2013, if we were to stop purchasing from each of these suppliers, the aggregate amount of the penalty would be approximately \$107 million, of which \$62 million relates to a contract with an engine parts supplier that extends to 2016. These arrangements enable us to secure critical components. We do not currently anticipate paying any penalties under these contracts.

We have guarantees with certain customers that require us to satisfactorily honor contractual or regulatory obligations, or compensate for monetary losses related to nonperformance. These performance bonds and other performance-related guarantees were \$66 million and \$70 million as of December 31, 2013 and 2012, respectively.

#### **Indemnifications**

Periodically, we enter into various contractual arrangements where we agree to indemnify a third-party against certain types of losses. Common types of indemnities include:

- product liability and license, patent or trademark indemnifications.
- asset sale agreements where we agree to indemnify the purchaser against future environmental exposures related to the asset sold and
- any contractual agreement where we agree to indemnify the counter-party for losses suffered as a result of a misrepresentation in the contract.

We regularly evaluate the probability of having to incur costs associated with these indemnities and accrue for expected losses that are probable. Because the indemnifications are not related to specified known liabilities and due to their uncertain nature, we are unable to estimate the maximum amount of the potential loss associated with these indemnifications.

#### **Joint Venture Commitments**

As of December 31, 2013, we have committed to invest an additional \$52 million in existing joint ventures, of which the entire \$52 million is expected to be funded in 2014.

**Leases**

We lease certain manufacturing equipment, facilities, warehouses, office space and equipment, aircraft and automobiles for varying periods under lease agreements. Most of the leases are non-cancelable operating leases with fixed rental payments, expire over the next 10 years and contain renewal provisions. Rent expense under these leases was as follows:

In millions	December 31,		
	2013	2012	2011
Rent expense	\$ 186	\$ 176	\$ 166

The following is a summary of the leased property under capital leases by major classes:

In millions	Asset balances at December 31,	
	2013	2012
Building	\$ 103	\$ 66
Equipment	97	110
Other	16	15
Less: Accumulated depreciation	(96)	(103)
Total	\$ 120	\$ 88

Following is a summary of the future minimum lease payments due under capital and operating leases, including leases in our rental business, with terms of more than one year at December 31, 2013, together with the net present value of the minimum payments due under capital leases:

In millions	Capital Leases	Operating Leases
2014	\$ 20	\$ 171
2015	20	111
2016	18	78
2017	11	57
2018	9	41
After 2018	48	111
Total minimum lease payments	\$ 126	\$ 569
Interest	(34)	
Present value of net minimum lease payments	\$ 92	

In addition, we have subleased certain facilities under operating leases to third parties. The future minimum lease payments due from lessees under those arrangements are \$1 million per year for the years 2014 through 2016.

**NOTE 15. SHAREHOLDERS' EQUITY****Preferred and Preference Stock**

We are authorized to issue one million shares each of zero par value preferred and preference stock with preferred shares being senior to preference shares. We can determine the number of shares of each series, and the rights, preferences and limitations of each series. At December 31, 2013, there was no preferred or preference stock outstanding.

## Common Stock

Changes in shares of common stock, treasury stock and common stock held in trust for employee benefit plans are as follows:

In millions	Common Stock	Treasury Stock	Common Stock Held in Trust
Balance at December 31, 2010	221.8	24.0	2.1
Shares acquired	—	6.4	—
Shares issued	0.4	(0.2)	—
Employee benefits trust activity	—	—	(0.3)
Balance at December 31, 2011	222.2	30.2	1.8
Shares acquired	—	2.6	—
Shares issued	0.4	(0.2)	—
Employee benefits trust activity	—	—	(0.3)
Other shareholder transactions	(0.2)	—	—
Balance at December 31, 2012	222.4	32.6	1.5
Shares acquired	—	3.3	—
Shares issued	0.1	(0.3)	—
Employee benefits trust activity	—	—	(0.2)
Other shareholder transactions	(0.2)	—	—
Balance at December 31, 2013	222.3	35.6	1.3

## Treasury Stock

Shares of common stock repurchased by us are recorded at cost as treasury stock and result in a reduction of shareholders' equity in our *Consolidated Balance Sheets*. Treasury shares may be reissued as part of our stock-based compensation programs. When shares are reissued, we use the weighted-average cost method for determining cost. The gains between the cost of the shares and the issuance price are added to additional paid-in-capital. The losses are deducted from additional paid-in capital to the extent of the gains. Thereafter, the losses are deducted from retained earnings. Treasury stock activity for the three-year period ended December 31, 2013, consisting of shares issued and repurchased is presented in our *Consolidated Statements of Changes in Equity*:

In February 2011, the Board of Directors approved a share repurchase program and authorized the acquisition of up to \$1 billion of our common stock, which was completed in June 2013. In December 2012, the Board of Directors authorized the acquisition of up to \$1 billion of our common stock upon completion of the 2011 repurchase program. In 2013, we made the following quarterly purchases under the repurchase programs indicated:

In millions (except per share amounts) For each quarter ended	2013 Shares Purchased	Average Cost Per Share	Total Cost of Repurchases	Remaining Authorized Capacity
<b>February 2011, \$1 billion repurchase program</b>				
March 31	—	\$ —	\$ —	226
June 30	2.0	113.44	226	—
Subtotal	2.0	113.44	226	—
<b>December 2012, \$1 billion repurchase program</b>				
June 30	0.6	107.74	63	937
September 29	—	—	—	937
December 31	0.7	129.18	92	845
Subtotal	1.3	119.54	155	845
Total	3.3	\$ 115.85	\$ 381	\$ 845

## Quarterly Dividends

In July 2013, the Board of Directors authorized a dividend increase of 25 percent from \$0.50 per share to \$0.625 per share on a quarterly basis effective in the third quarter. In July 2012, the Board of Directors authorized a 25 percent increase to our quarterly cash dividend on our common stock from \$0.40 per share to \$0.50 per share. In July 2011, the Board of Directors approved a 52 percent increase to our quarterly cash dividend on our common stock from \$0.2625 per share to \$0.40 per share. Cash dividends per share paid to common shareholders for the last three years were as follows:

	Quarterly Dividends		
	2013	2012	2011
First quarter	\$ 0.50	\$ 0.40	\$ 0.2625
Second quarter	0.50	0.40	0.2625
Third quarter	0.625	0.50	0.40
Fourth quarter	0.625	0.50	0.40
Total	\$ 2.25	\$ 1.80	\$ 1.325

Total dividends paid to common shareholders in 2013, 2012 and 2011 were \$420 million, \$340 million and \$255 million, respectively. Declaration and payment of dividends in the future depends upon our income and liquidity position, among other factors, and is subject to declaration by our Board of Directors, who meet quarterly to consider our dividend payment. We expect to fund dividend payments with cash from operations.

## Employee Benefits Trust

In 1997, we established the Employee Benefits Trust (EBT) funded with common stock for use in meeting our future obligations under employee benefit and compensation plans. The primary sources of cash for the EBT are dividends received on unallocated shares of our common stock held by the EBT. The EBT may be used to fund matching contributions to employee accounts in the 401(k) Retirement Savings Plan (RSP) made in proportion to employee contributions under the terms of the RSP. In addition, we may direct the trustee to sell shares of the EBT on the open market to fund other non-qualified employee benefit plans. Matching contributions charged to income for the years ended December 31, 2013, 2012 and 2011 were \$24 million, \$27 million and \$28 million, respectively.

**NOTE 16. OTHER COMPREHENSIVE INCOME (LOSS)**

Following are the changes in accumulated other comprehensive income (loss) by component

In millions	Change in pensions and other postretirement defined benefit plans	Foreign currency translation adjustment	Unrealized gain (loss) on marketable securities	Unrealized gain (loss) on derivatives	Total attributable to Cummins Inc.	Noncontrolling interests	Total
Balance at December 31, 2010	\$ (646)	\$ (90)	\$ 4	\$ 12	\$ (720)		
Other comprehensive income before reclassifications							
Before tax amount	(155)	(121)	3	(26)	(299)	\$ (39)	\$ (338)
Tax (provision) benefit	46	13	—	11	70	—	70
After tax amount	(109)	(108)	3	(15)	(229)	(39)	(268)
Amounts reclassified from accumulated other comprehensive income <sup>(1)</sup>	31	—	(3)	(17)	11	1	12
Net current period other comprehensive income (loss)	(78)	(108)	—	(32)	(218)	\$ (38)	\$ (256)
Balance at December 31, 2011	\$ (724)	\$ (198)	\$ 4	\$ (20)	\$ (938)		
Other comprehensive income before reclassifications							
Before tax amount	\$ (164)	\$ 51	\$ 6	\$ 16	\$ (91)	\$ (8)	\$ (99)
Tax (provision) benefit	54	(14)	(2)	(4)	34	—	34
After tax amount	(110)	37	4	12	(57)	(8)	(65)
Amounts reclassified from accumulated other comprehensive income <sup>(1)</sup>	40	—	(3)	8	45	1	46
Net current period other comprehensive income (loss)	(70)	37	1	20	(12)	\$ (7)	\$ (19)
Balance at December 31, 2012	\$ (794)	\$ (161)	\$ 5	\$ —	\$ (950)		
Other comprehensive income before reclassifications							
Before tax amount	206	(31)	16	(6)	185	\$ (28)	\$ 157
Tax (provision) benefit	(87)	13	(9)	3	(80)	—	(80)
After tax amount	119	(18)	7	(3)	105	(28)	77
Amounts reclassified from accumulated other comprehensive income <sup>(1)(2)</sup>	64	—	(5)	2	61	(1)	60
Net current period other comprehensive income (loss)	183	(18)	2	(1)	166	\$ (29)	\$ 137
Balance at December 31, 2013	\$ (611)	\$ (179)	\$ 7	\$ (1)	\$ (784)		

<sup>(1)</sup>Amounts are net of tax.

<sup>(2)</sup>See reclassifications out of accumulated other comprehensive income (loss) disclosure for details.

[Table of Contents](#)

Following are the items reclassified out of accumulated other comprehensive income (loss) and the related tax effects:

In millions (Gain)/Loss Components	For the year ended, December 31, 2013	Statement of Income Location
Realized (gain) loss on marketable securities	\$ (13)	Other income (expense), net
Income tax expense	7	Income tax expense
Net realized (gain) loss on marketable securities	(6)	
Realized (gain) loss on derivatives		
Foreign currency forward contracts	2	Net sales
Commodity swap contracts	1	Cost of sales
Total before taxes	3	
Income tax expense	(1)	Income tax expense
Net realized (gain) loss on derivatives	2	
Change in pension and other postretirement defined benefit plans		
Recognized actuarial loss	95	(1)
Total before taxes	95	
Income tax expense	(31)	Income tax expense
Net change in pensions and other postretirement defined benefit plans	64	
Total reclassifications for the period	\$ 60	

(1) These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note 12).

**NOTE 17. STOCK INCENTIVE AND STOCK OPTION PLANS**

In May 2012, our shareholders approved the 2012 Omnibus Plan (the Plan), which replaced and succeeded the 2003 Stock Incentive Plan. The Plan allows for the granting of equity awards covering up to 3.5 million shares to executives, employees and non-employee directors. Awards available for grant under the Plan include, but are not limited to, stock options, stock appreciation rights, performance shares and other stock awards. Shares issued under the Plan may be newly issued shares or reissued treasury shares.

Stock options are generally granted with a strike price equal to the fair market value of the stock on the date of grant, a life of 10 years and a two-year vesting period. The strike price may be higher than the fair value of the stock on the date of the grant, but cannot be lower. Compensation expense is recorded on a straight-line basis over the vesting period beginning on the grant date. The compensation expense is based on the fair value of each option grant using the Black-Scholes option pricing model. Options granted to employees eligible for retirement under our retirement plan are fully expensed as of the grant date.

Stock options are also awarded through the Key Employee Stock Investment Plan (KESIP) which allows certain employees, other than officers, to purchase shares of common stock on an installment basis up to an established credit limit. Fifty stock options are granted for every even block of 100 KESIP shares purchased by the employee. The options granted through the KESIP program are considered awards under the Plan and are vested immediately. Compensation expense for stock options granted through the KESIP program is recorded based on the fair value of each option grant using the Black-Scholes option pricing model.

Performance shares are granted as target awards and are earned based on our return on equity (ROE) performance. A payout factor has been established ranging from 0 to 200 percent of the target award based on our actual ROE performance. Shares have a three-year performance period. Employees leaving the company prior to the end of the three-year performance period forfeit shares granted to them. The fair value of the award is equal to the average market price, adjusted for the present value of dividends over the vesting period, of our stock on the grant date. Compensation expense is recorded ratably over the period beginning on the grant date until the shares become unrestricted and is based on the amount of the award that is expected to be earned under the plan formula, adjusted each reporting period based on current information.

[Table of Contents](#)

Restricted common stock is awarded from time to time at no cost to certain employees. Participants are entitled to cash dividends and voting rights. Restrictions limit the sale or transfer of the shares during a defined period. Generally, one-third of the shares become vested and free from restrictions after two years and one-third of the shares issued become vested and free from restrictions each year thereafter on the anniversary of the grant date, provided the participant remains an employee. The fair value of the award is equal to the average market price of our stock on the grant date. Compensation expense is determined at the grant date and is recognized over the four-year restriction period on a straight-line basis.

Compensation expense (net of estimated forfeitures) related to our share-based plans for the year ended December 31, 2013, 2012 and 2011, was approximately \$34 million, \$35 million and \$40 million, respectively. The excess tax benefit/(deficiency) associated with our share-based plans for the years ended December 31, 2013, 2012 and 2011, was \$13 million, \$14 million and \$5 million, respectively. The total unrecognized compensation expense (net of estimated forfeitures) related to nonvested awards was approximately \$34 million at December 31, 2013, and is expected to be recognized over a weighted-average period of less than one year.

The tables below summarize the activity in the Plan:

	Options	Weighted-average Exercise Price	Weighted-average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in millions)
Balance at December 31, 2010	1,073,595	\$ 37.92		
Granted	316,159	115.71		
Exercised	(134,520)	23.93		
Forfeited	(12,197)	57.68		
Balance at December 31, 2011	1,243,037	59.02		
Granted	321,945	119.34		
Exercised	(241,815)	31.73		
Forfeited	(13,999)	67.86		
Balance at December 31, 2012	1,309,168	78.80		
Granted	<b>432,370</b>	<b>112.07</b>		
Exercised	<b>(265,528)</b>	<b>40.48</b>		
Forfeited	<b>(13,674)</b>	<b>105.19</b>		
Balance at December 31, 2013	<b>1,462,336</b>	<b>\$ 95.35</b>	<b>7.33</b>	<b>\$ 66</b>
Exercisable, December 31, 2011	721,210	\$ 38.75	6.25	\$ 38
Exercisable, December 31, 2012	785,869	\$ 51.40	6.26	\$ 44
<b>Exercisable, December 31, 2013</b>	<b>758,936</b>	<b>\$ 76.85</b>	<b>5.94</b>	<b>\$ 48</b>

The weighted-average grant date fair value of options granted during the years ended December 31, 2013, 2012 and 2011, was \$48.00, \$54.25 and \$51.23, respectively. The total intrinsic value of options exercised during the years ended December 31, 2013, 2012 and 2011, was approximately \$22 million, \$19 million and \$12 million, respectively.

The weighted-average grant date fair value of performance and restricted shares was as follows:

Nonvested	Performance Shares		Restricted Shares	
	Shares	Weighted-average Fair Value	Shares	Weighted-average Fair Value
Balance at December 31, 2010	481,771	\$ 45.10	69,890	\$ 51.94
Granted	229,436	86.65	13,555	108.51
Vested	(178,653)	48.03	(1,600)	42.61
Forfeited	(7,163)	59.15	—	—
Balance at December 31, 2011	525,391	62.05	81,845	61.49
Granted	325,590	89.92	3,150	91.68
Vested	(194,484)	25.46	(22,766)	52.16
Forfeited	(26,413)	91.94	—	—
Balance at December 31, 2012	630,084	86.49	62,229	66.43
Granted	<b>176,649</b>	<b>106.40</b>	<b>7,506</b>	<b>114.56</b>
Vested	<b>(303,882)</b>	<b>61.48</b>	<b>(26,901)</b>	<b>62.03</b>
Forfeited	<b>(26,938)</b>	<b>85.07</b>	<b>(10,293)</b>	<b>65.41</b>
Balance at December 31, 2013	<b>475,913</b>	<b>\$ 109.93</b>	<b>32,541</b>	<b>\$ 81.49</b>

The total fair value of performance shares vested during the years ended December 31, 2013, 2012 and 2011 was \$35 million, \$24 million and \$17 million, respectively. The total fair value of restricted shares vested was \$3 million, \$3 million and less than \$1 million for the years ended December 31, 2013, 2012 and 2011, respectively.

The fair value of each option grant was estimated on the grant date using the Black-Scholes option pricing model with the following assumptions:

	Years ended December 31,		
	2013	2012	2011
Expected life (years)	5	5	5
Risk-free interest rate	0.79%	1.05%	1.87%
Expected volatility	56.59%	58.98%	55.39%
Dividend yield	1.55%	1.30%	1.30%

*Expected life*—The expected life of employee stock options represents the weighted-average period the stock options are expected to remain outstanding based upon our historical data.

*Risk-free interest rate*—The risk-free interest rate assumption is based upon the observed U.S. treasury security rate appropriate for the expected life of our employee stock options.

*Expected volatility*—The expected volatility assumption is based upon the weighted-average historical daily price changes of our common stock over the most recent period equal to the expected option life of the grant, adjusted for activity which is not expected to occur in the future.

*Dividend yield*—The dividend yield assumption is based on our history and expectation of dividend payouts.

#### NOTE 18. NONCONTROLLING INTEREST

Noncontrolling interests in the equity of consolidated subsidiaries were as follows:

In millions	December 31,	
	2013	2012
Cummins India Ltd.	\$ 252	\$ 260
Wuxi Cummins Turbo Technologies Co. Ltd.	81	75
Other	27	36
Total	<b>\$ 360</b>	<b>\$ 371</b>



**NOTE 19. RESTRUCTURING AND OTHER CHARGES**

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

Employee termination and severance costs were recorded based on approved plans developed by the businesses and corporate management which specified positions to be eliminated, benefits to be paid under existing severance plans or statutory requirements and the expected timetable for completion of the plan. Estimates of restructuring were made based on information available at the time charges were recorded.

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

<b>In millions</b>	<b>Year ended December 31, 2012</b>
Workforce reductions	\$ 49
Exit activities	1
Other	2
Restructuring and other charges	<u>\$ 52</u>

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

<b>In millions</b>	<b>Year ended December 31, 2012</b>
Engine	\$ 20
Distribution	14
Power Generation	12
Components	6
Restructuring and other charges	<u>\$ 52</u>

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

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

At December 31, 2013, of the approximately 1,300 employees affected by this plan, substantially all terminations have been completed.

[Table of Contents](#)

The table below summarizes the activity and balance of accrued restructuring charges, which is included in "Other accrued expenses" in our *Consolidated Balance Sheets* for the years ended December 31, 2012 and 2013.

In millions	
2012 Restructuring charges <sup>(1)</sup>	\$ 50
Cash payments for 2012 actions	(25)
Balance at December 31, 2012	25
Cash payments for 2012 actions	(22)
Change in estimate <sup>(2)</sup>	(3)
Balance at December 31, 2013	\$ —

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

(2) Due to the inherent uncertainty involved in calculating the initial estimates, the actual amounts paid for such activities differed slightly from the amounts initially recorded. We have adjusted the previous estimates accordingly.

**NOTE 20. EARNINGS PER SHARE**

We calculate basic earnings per share (EPS) of common stock by dividing net income attributable to Cummins Inc. by the weighted-average number of common shares outstanding for the period. The calculation of diluted EPS assumes the issuance of common stock for all potentially dilutive share equivalents outstanding. We exclude shares of common stock held in the EBT (see Note 15, "SHAREHOLDERS' EQUITY") from the calculation of the weighted-average common shares outstanding until those shares are distributed from the EBT to the RSP. Following are the computations for basic and diluted earnings per share:

Dollars in millions, except per share amounts	Years ended December 31,		
	2013	2012	2011
Net income attributable to Cummins Inc.	\$ 1,483	\$ 1,645	\$ 1,848
Weighted-average common shares outstanding			
Basic	186,994,382	189,286,821	192,972,211
Dilutive effect of stock compensation awards	423,459	381,883	625,667
Diluted	187,417,841	189,668,704	193,597,878
Earnings per common share attributable to Cummins Inc.			
Basic	\$ 7.93	\$ 8.69	\$ 9.58
Diluted	7.91	8.67	9.55

The weighted-average diluted common shares outstanding for 2013, 2012 and 2011 excludes the effect of 359,641, 453,893 and 177,460 weighted-average shares, respectively, of common stock options, since such options had an exercise price in excess of the monthly average market value of our common stock during that year.

**NOTE 21. DERIVATIVES**

We are exposed to financial risk resulting from volatility in foreign exchange rates, commodity prices and interest rates. This risk is closely monitored and managed through the use of financial derivative instruments including foreign currency forward contracts, commodity swap contracts, commodity zero-cost collars and interest rate swaps. As stated in our policies and procedures, financial derivatives are used expressly for hedging purposes and under no circumstances are they used for speculative purposes. When material, we adjust the value of our derivative contracts for counter-party or our credit risk. None of our derivative instruments are subject to collateral requirements. Substantially all of our derivative contracts are subject to master netting arrangements which provide us with the option to settle certain contracts on a net basis when they settle on the same day with the same currency. In addition, these arrangements provide for a net settlement of all contracts with a given counterparty in the event that the arrangement is terminated due to the occurrence of default or a termination event.

**Foreign Exchange Rates**

As a result of our international business presence, we are exposed to foreign currency exchange risks. We transact business in foreign currencies and, as a result, our income experiences some volatility related to movements in foreign currency exchange rates. To help manage our exposure to exchange rate volatility, we use foreign currency forward contracts on a regular basis to hedge forecasted intercompany and third-party sales and purchases denominated in non-functional currencies. Our internal policy allows for managing anticipated foreign currency cash flows for up to one year. These foreign currency forward contracts are designated and qualify as foreign currency cash flow hedges under GAAP. The effective portion of the unrealized gain or loss on the forward contract is deferred and reported as a component of "Accumulated other comprehensive loss" (AOCL). When the hedged forecasted transaction (sale or purchase) occurs, the unrealized gain or loss is reclassified into income in the same line item associated with the hedged transaction in the same period or periods during which the hedged transaction affects income. The ineffective portion of the hedge, if any, is recognized in current income during the period of change. As of December 31, 2013, the amount we expect to reclassify from AOCL to income over the next year is an unrealized net gain of \$4 million. For the years ended December 31, 2013 and 2012, there were no circumstances that would have resulted in the discontinuance of a foreign currency cash flow hedge.

To minimize the income volatility resulting from the remeasurement of net monetary assets and payables denominated in a currency other than the functional currency, we enter into foreign currency forward contracts, which are considered economic hedges. The objective is to offset the gain or loss from remeasurement with the gain or loss from the fair market valuation of the forward contract. These derivative instruments are not designated as hedges under GAAP.

The table below summarizes our outstanding foreign currency forward contracts. Only the U.S. dollar forward contracts are designated and qualify for hedge accounting as of each period presented below. The currencies in this table represent 94 percent and 95 percent of the notional amounts of contracts outstanding as of December 31, 2013 and 2012.

Currency denomination	Notional amount in millions	
	December 31, 2013	December 31, 2012
United States Dollar (USD)	98	110
British Pound Sterling (GBP)	170	227
Euro (EUR)	32	28
Singapore Dollar (SGD)	—	3
Indian Rupee (INR)	3,118	1,943
Japanese Yen (JPY)	1,357	384
Canadian Dollar (CAD)	14	59
South Korea Won (KRW)	21,855	35,266
Chinese Renmimbi (CNY)	331	45
Brazilian Real (BRL)	79	—

**Commodity Price Risk**

We are exposed to fluctuations in commodity prices due to contractual agreements with component suppliers. In order to protect ourselves against future price volatility and, consequently, fluctuations in gross margins, we periodically enter into commodity swap contracts with designated banks to fix the cost of certain raw material purchases with the objective of minimizing changes in inventory cost due to market price fluctuations. Certain commodity swap contracts are derivative contracts that are designated as cash flow hedges under GAAP. We also have commodity swap contracts that represent an economic hedge, but are not designated for hedge accounting and are marked to market through earnings. For those contracts that qualify for hedge accounting, the effective portion of the unrealized gain or loss is deferred and reported as a component of AOCL. When the hedged forecasted transaction (purchase) occurs, the unrealized gain or loss is reclassified into income in the same line item associated with the hedged transaction in the same period or periods during which the hedged transaction affects income. The ineffective portion of the hedge, if any, is recognized in current income in the period in which the ineffectiveness occurs. As of December 31, 2013, we expect to reclassify an unrealized netloss of \$4 million from AOCL to income over the next year. Our internal policy allows for managing these cash flow hedges for up to three years.

The following table summarizes our outstanding commodity swap contracts that were entered into to hedge the cost of certain raw material purchases:

Dollars in millions Commodity	December 31, 2013			December 31, 2012		
	Notional Amount	Quantity		Notional Amount	Quantity	
Copper	\$ —	—	(1)	\$ 24	3,025 metric tons	(1)
Platinum	61	41,403 troy ounces	(2)	71	45,126 troy ounces	(2)
Palladium	16	21,790 troy ounces	(2)	10	14,855 troy ounces	(2)

(1)A metric ton is a measurement of mass equal to 1,000 kilograms.

(2)A troy ounce is a measurement of mass equal to approximately 31 grams.

In 2012, we began to use a combination of call and put option contracts for copper in net-zero-cost collar arrangements (zero-cost collars) that establish ceiling and floor prices for copper. These contracts are used strictly for hedging and not for speculative purposes. For these zero-cost collars, if the average price of the copper during the calculation period is within the call and put price, the zero-cost collar contracts expire at no cost to us. If the price falls below the floor, the counter-party to the collar receives the difference from us and if the price rises above the ceiling, the counter-party pays the difference to us. We believe that these zero-cost collars will act as economic hedges; however we have chosen not to designate them as hedges for accounting purposes.

The following table summarizes our outstanding commodity zero-cost collar contracts that were entered into to hedge the cost of copper purchases:

	December 31,			
	2013		2012	
Average cap	\$	7,639	\$	8,196
Average floor		6,978		7,005
Quantity in metric tons <sup>(1)</sup>		5,421		4,100

(1) A metric ton is a measurement of mass equal to 1,000 kilograms.

### Interest Rate Risk

We are exposed to market risk from fluctuations in interest rates. We manage our exposure to interest rate fluctuations through the use of interest rate swaps. The objective of the swaps is to more effectively balance our borrowing costs and interest rate risk.

In November 2005, we entered into an interest rate swap to effectively convert our \$250 million debt issue, due in 2028, from a fixed rate of 7.125 percent to a floating rate based on a LIBOR spread. The terms of the swap mirror those of the debt, with interest paid semi-annually. This swap qualifies as a fair value hedge under GAAP. The gain or loss on this derivative instrument as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in current income as "Interest expense." The following table summarizes these gains and losses for the years presented below:

In millions Income Statement Classification	For the years ended December 31,			
	2013		2012	
	Gain/(Loss) on Swaps	Gain/(Loss) on Borrowings	Gain/(Loss) on Swaps	Gain/(Loss) on Borrowings
Interest expense	\$ (39)	\$ 39	\$ 6	\$ (6)

### Cash Flow Hedging

The following table summarizes the effect on our *Consolidated Statements of Income* for derivative instruments classified as cash flow hedges for the years ended December 31, 2013 and 2012 presented below. The table does not include amounts related to ineffectiveness as it was not material for the periods presented.

In millions	Location of Gain/(Loss) Reclassified into Income (Effective Portion)	For the years ended December 31,			
		Amount of Gain/(Loss) Recognized in AOCL on Derivative (Effective Portion)		Amount of Gain/(Loss) Reclassified from AOCL into Income (Effective Portion)	
		2013	2012	2013	2012
<b>Derivatives in Cash Flow Hedging Relationships</b>					
Foreign currency forward contracts	Net sales	\$ 1	\$ 8	\$ (2)	\$ (2)
Commodity swap contracts	Cost of sales	(7)	8	(1)	(9)
Total		\$ (6)	\$ 16	\$ (3)	\$ (11)

**Derivatives Not Designated as Hedging Instruments**

The following table summarizes the effect on our *Consolidated Statements of Income* for derivative instruments that are not classified as hedges for the years ended December 31, 2013 and 2012.

In millions	Location of Gain/(Loss) Recognized in Income on Derivatives	Amount of Gain/(Loss) Recognized in Income on Derivatives			
		For the years ended December 31,			
		2013		2012	
<b>Derivatives Not Designated as Hedging Instruments</b>					
Foreign currency forward contracts	Cost of sales	\$	(1)	\$	(4)
Foreign currency forward contracts	Other income (expense), net		3		11
Commodity zero-cost collars	Cost of sales		(2)		1

**Fair Value Amount and Location of Derivative Instruments**

The following tables summarize the location and fair value of derivative instruments on our *Consolidated Balance Sheets*:

In millions	Derivative Assets		
	Fair Value		Balance Sheet Location
	December 31, 2013	December 31, 2012	
<b>Derivatives designated as hedging instruments</b>			
Interest rate contract	\$ 49	\$ 88	Other assets
Foreign currency forward contracts	5	2	Prepaid expenses and other current assets
Commodity swap contracts	—	1	Prepaid expenses and other current assets
Total derivatives designated as hedging instruments	\$ 54	\$ 91	
<b>Derivatives not designated as hedging instruments</b>			
Foreign currency forward contracts	6	1	Prepaid expenses and other current assets
Commodity zero-cost collars	—	1	Other assets
Total derivatives not designated as hedging instruments	\$ 6	\$ 2	
Total derivative assets	\$ 60	\$ 93	

In millions	Derivative Liabilities		
	Fair Value		Balance Sheet Location
	December 31, 2013	December 31, 2012	
<b>Derivatives designated as hedging instruments</b>			
Commodity swap contracts	\$ 5	\$ 2	Other accrued expenses
Total derivatives designated as hedging instruments	\$ 5	\$ 2	
<b>Derivatives not designated as hedging instruments</b>			
Commodity zero-cost collars	—	1	Other accrued expenses
Foreign currency forward contracts	5	—	Other accrued expenses
Total derivatives not designated as hedging instruments	\$ 5	\$ 1	
Total derivative liabilities	\$ 10	\$ 3	

We have elected to present our derivative contracts on a gross basis in our *Consolidated Balance Sheets*. Had we chosen to present on a net basis, we would have derivatives in a net asset position of \$53 million and derivatives in a net liability position of \$3 million.

## NOTE 22. OPERATING SEGMENTS

Operating segments under GAAP are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision-maker, or decision-making group, in deciding how to allocate resources and in assessing performance. Cummins' chief operating decision-maker (CODM) is the Chief Executive Officer.

Our reportable operating segments consist of the following: Engine, Components, Power Generation and Distribution. This reporting structure is organized according to the products and markets each segment serves and allows management to focus its efforts on providing enhanced service to a wide range of customers. The Engine segment produces engines and parts for sale to customers in on-highway and various industrial markets. Our engines are used in trucks of all sizes, buses and recreational vehicles, as well as in various industrial applications, including construction, mining, agriculture, marine, oil and gas, rail and military equipment. The Components segment sells filtration products, aftertreatment systems, turbochargers and fuel systems. The Power Generation segment is an integrated provider of power systems, which sells engines, generator sets and alternators. The Distribution segment includes wholly-owned and partially-owned distributorships engaged in wholesaling engines, generator sets and service parts, as well as performing service and repair activities on our products and maintaining relationships with various OEMs throughout the world.

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

The accounting policies of our operating segments are the same as those applied in our *Consolidated Financial Statements*. We prepared the financial results of our operating segments on a basis that is consistent with the manner in which we internally disaggregate financial information to assist in making internal operating decisions. We have allocated certain common costs and expenses, primarily corporate functions, among segments differently than we would for stand-alone financial information prepared in accordance with GAAP. These include certain costs and expenses of shared services, such as information technology, human resources, legal and finance. We also do not allocate debt-related items, actuarial gains or losses, prior service costs or credits, changes in cash surrender value of corporate owned life insurance, flood damage gains or losses, divestiture gains or losses or income taxes to individual segments. Segment EBIT may not be consistent with measures used by other companies.

Summarized financial information regarding our reportable operating segments at December 31, is shown in the table below:

In millions	Engine	Components	Power Generation	Distribution	Non-segment Items <sup>(1)</sup>	Total
<b>2013</b>						
External sales	\$ 8,270	\$ 3,151	\$ 2,154	\$ 3,726	\$ —	\$ 17,301
Intersegment sales	1,743	1,191	877	23	(3,834)	—
Total sales	10,013	4,342	3,031	3,749	(3,834)	17,301
Depreciation and amortization <sup>(2)</sup>	205	96	50	54	—	405
Research, development and engineering expenses	416	218	73	6	—	713
Equity, royalty and interest income from investees	136	28	32	165	—	361
Interest income	16	3	6	2	—	27
Segment EBIT	1,041	527	218	388	(14)	2,160
Net assets	4,323	1,885	1,801	1,637	—	9,646
Investments and advances to equity investees	419	140	110	262	—	931
Capital expenditures	372	141	106	57	—	676
<b>2012</b>						
External sales	\$ 9,101	\$ 2,809	\$ 2,163	\$ 3,261	\$ —	\$ 17,334
Intersegment sales	1,632	1,203	1,105	16	(3,956)	—
Total sales	10,733	4,012	3,268	3,277	(3,956)	17,334
Depreciation and amortization <sup>(2)</sup>	192	82	47	34	—	355
Research, development and engineering expenses	433	213	76	6	—	728
Equity, royalty and interest income from investees	127	29	40	188	—	384
Interest income	11	3	9	2	—	25
Segment EBIT <sup>(3)</sup>	1,248	426	285	369	(25)	2,303
Net assets	3,373	1,830	1,582	1,392	—	8,177
Investments and advances to equity investees	401	127	88	281	—	897
Capital expenditures	399	134	95	62	—	690
<b>2011</b>						
External sales	\$ 9,649	\$ 2,886	\$ 2,492	\$ 3,021	\$ —	\$ 18,048
Intersegment sales	1,658	1,177	1,006	23	(3,864)	—
Total sales	11,307	4,063	3,498	3,044	(3,864)	18,048
Depreciation and amortization <sup>(2)</sup>	181	73	42	25	—	321
Research, development and engineering expenses	397	175	54	3	—	629
Equity, royalty and interest income from investees	166	31	47	172	—	416
Interest income	18	5	8	3	—	34
Segment EBIT	1,384	470	373	386	102	2,715
Net assets	3,167	1,467	1,547	1,123	—	7,304
Investments and advances to equity investees	398	123	79	238	—	838
Capital expenditures	339	141	87	55	—	622

(1) Includes intersegment sales and profit in inventory eliminations and unallocated corporate expenses. There were no significant unallocated corporate expenses for the year ended December 31, 2013. The year ended December 31, 2012, included a \$6 million gain (\$4 million after-tax) related to adjustments from our 2011 divestitures and a \$20 million charge (\$12 million after-tax) related to legal matters. The year ended December 31, 2011, included a \$68 million gain (\$37 million after-tax) and a \$53 million gain (\$33 million after-tax) related to the Component segment sales of certain assets and liabilities from our exhaust and light-duty filtration businesses, respectively, and a \$38 million gain (\$24 million after-tax) related to the insurance settlement regarding the June 2008 flood in Southern Indiana. The gains and losses have been excluded from segment results as they were not considered in our evaluation of operating results for the years ended December 31, 2012 and 2011.

(2) Depreciation and amortization as shown on a segment basis excludes the amortization of debt discount and deferred costs that are included in the *Consolidated Statements of Income* as "Interest expense."

(3) Segment EBIT included restructuring and other charges for each business segment of \$20 million (Engine), \$6 million (Components), \$12 million (Power Generation) and \$14 million (Distribution). See NOTE 19, "RESTRUCTURING AND OTHER CHARGES," for additional detail.

(4) Distribution segment EBIT for the year ended December 31, 2013, included a \$7 million gain and \$5 million gain for the fair value adjustment resulting from the acquisitions of a controlling interest in Northwest and Rocky Mountain, respectively. Distribution segment EBIT for the year ended December 31, 2012, included a \$7 million gain on the fair value adjustment resulting from the acquisition of a controlling interest in Central Power. See NOTE 2, "ACQUISITIONS AND DIVESTITURES," for additional detail.

A reconciliation of our segment information to the corresponding amounts in the *Consolidated Statements of Income* is shown in the table below:

In millions	Years ended December 31,		
	2013	2012	2011
Total EBIT	\$ 2,160	\$ 2,303	\$ 2,715
Less: Interest expense	41	32	44
Income before income taxes	\$ 2,119	\$ 2,271	\$ 2,671

In millions	December 31,		
	2013	2012	2011
Net assets for operating segments	\$ 9,646	\$ 8,177	\$ 7,304
Liabilities deducted in arriving at net assets	5,103	4,913	4,832
Pension and other postretirement benefit adjustments excluded from net assets	(346)	(977)	(928)
Deferred tax assets not allocated to segments	292	410	435
Debt-related costs not allocated to segments	33	25	25
Total assets	\$ 14,728	\$ 12,548	\$ 11,668

The tables below present certain segment information by geographic area. Net sales attributed to geographic areas were based on the location of the customer. Long-lived assets include property, plant and equipment, net of depreciation, investments and advances to equity investees and other assets, excluding deferred tax assets.

In millions	Years ended as of December 31,		
	2013	2012	2011
<i>Net Sales</i>			
United States	\$ 8,382	\$ 8,107	\$ 7,354
China	1,194	1,056	1,452
Brazil	882	798	1,286
India	630	757	859
Mexico	556	692	631
United Kingdom	453	660	727
Canada	655	642	653
Other foreign countries	4,549	4,622	5,086
Total net sales	\$ 17,301	\$ 17,334	\$ 18,048

In millions	Years ended as of December 31,		
	2013	2012	2011
<i>Long-lived assets</i>			
United States	\$ 2,606	\$ 2,440	\$ 2,218
China	646	589	520
India	330	243	203
United Kingdom	319	339	318
Brazil	172	170	151
Netherlands	138	130	111
Mexico	87	77	72
Germany	69	49	47
Canada	68	69	64
Korea	37	37	27
Turkey	28	29	19
Romania	27	15	10
Australia	18	25	34
Singapore	17	16	9
United Arab Emirates	15	16	14
France	13	13	13
Other foreign countries	34	33	32
Total long-lived assets	\$ 4,624	\$ 4,290	\$ 3,862



Our largest customer is PACCAR Inc. Worldwide sales to this customer were \$2,085 million in 2013, \$2,232 million in 2012 and \$2,144 million in 2011, representing 12 percent, 13 percent and 12 percent, respectively, of our consolidated net sales. No other customer accounted for more than 10 percent of consolidated net sales.

**NOTE 23. SUBSEQUENT EVENT**

**Acquisition of Cummins Mid-South LLC**

On February 15, 2014, we acquired the remaining 62.2 percent interest in Cummins Mid-South LLC (Mid-South) from the former distributor principal for consideration of approximately \$46 million in cash and an additional \$61 million paid to creditors to eliminate all debt related to the entity, or total consideration of \$107 million, subject to customary purchase price adjustments.

The acquisition will be accounted for as a business combination and the results of the acquired entity will be included in the Distribution operating segment beginning with the first quarter of 2014. As a result of this transaction, first quarter 2014 Distribution segment results are expected to include a gain of approximately \$6 million, related to the remeasurement of our pre-existing ownership interest in Mid-South.

**SELECTED QUARTERLY FINANCIAL DATA  
UNAUDITED**

In millions, except per share amounts	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	2013			
Net sales	\$ 3,922	\$ 4,525	\$ 4,266	\$ 4,588
Gross margin	957	1,153	1,109	1,164
Net income attributable to Cummins Inc.	282	414	355	432
Net earnings per share attributable to Cummins Inc.—basic <sup>(1)</sup>	\$ 1.50	\$ 2.20	\$ 1.91	\$ 2.33
Net earnings per share attributable to Cummins Inc.—diluted	1.49	2.20	1.90	2.32
Cash dividends per share	0.50	0.50	0.625	0.625
Stock price per share				
High	\$ 122.54	\$ 122.32	\$ 136.50	\$ 141.39
Low	109.19	103.41	107.51	122.52
2012				
Net sales	\$ 4,472	\$ 4,452	\$ 4,118	\$ 4,292
Gross margin	1,198	1,210	1,042	1,058
Net income attributable to Cummins Inc. <sup>(2)</sup>	455	469	352	369
Net earnings per share attributable to Cummins Inc.—basic	\$ 2.39	\$ 2.47	\$ 1.87	\$ 1.96
Net earnings per share attributable to Cummins Inc.—diluted <sup>(1)</sup>	2.38	2.47	1.86	1.95
Cash dividends per share	0.40	0.40	0.50	0.50
Stock price per share				
High	\$ 129.51	\$ 123.34	\$ 105.63	\$ 109.78
Low	90.37	88.31	82.20	85.88

<sup>(1)</sup> Earnings per share in each quarter is computed using the weighted-average number of shares outstanding during that quarter while earnings per share for the full year is computed using the weighted-average number of shares outstanding during the year. Thus, the sum of the four quarters earnings per share may not equal the full year earnings per share.

<sup>(2)</sup> In the second quarter of 2012, we recorded a \$6 million gain (\$4 million after-tax) or \$0.02 per share related to adjustments to our 2011 divestitures.

In the fourth quarter of 2012, we recorded a \$52 million restructuring charge (\$35 million after-tax) or \$0.19 per share and a \$20 million charge (\$12 million after-tax) or \$0.07 per share related to legal matters.

At December 31, 2013, there were approximately 3,905 holders of record of Cummins Inc.'s \$2.50 par value common stock.

**ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**ITEM 9A. Controls and Procedures**

**Evaluation of Disclosure Controls and Procedures**

As of the end of the period covered by this Annual Report on Form 10-K, our management evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of the design and operation of our disclosure controls and procedures as defined in Exchange Act Rules 13a-15(e) and 15d-15(e). Based upon that evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Annual Report on Form 10-K.

**Changes in Internal Control over Financial Reporting**

There has been no change in our internal control over financial reporting during the quarter ended December 31, 2013, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Management's Report on Internal Control Over Financial Reporting**

The information required by Item 9A relating to Management's Annual Report on Internal Control Over Financial Reporting and Attestation Report of the Registered Public Accounting Firm is incorporated herein by reference to the information set forth under the captions "Management's Report on Internal Control Over Financial Reporting" and "Report of Independent Registered Public Accounting Firm," respectively, under Item 8.

**ITEM 9B. Other Information**

None.

**PART III**

**ITEM 10. Directors, Executive Officers and Corporate Governance**

The information required by Item 10 is incorporated by reference to the relevant information under the captions "Corporate Governance," "Election of Directors" and "Other Information—Section 16(a) Beneficial Ownership Reporting Compliance" in our 2014 Proxy Statement, which will be filed within 120 days after the end of 2013. Information regarding our executive officers may be found in Part 1 of this annual report under the caption "Executive Officers of the Registrant." Except as otherwise specifically incorporated by reference, our Proxy Statement is not deemed to be filed as part of this annual report.

**ITEM 11. Executive Compensation**

The information required by Item 11 is incorporated by reference to the relevant information under the caption "Executive Compensation" in our 2014 Proxy Statement, which will be filed within 120 days after the end of 2013.

**ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

Information concerning our equity compensation plans as of December 31, 2013, is as follows:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights <sup>(1)</sup>	Weighted-average exercise price of outstanding options, warrants and rights <sup>(2)</sup>	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in the first column)
Equity compensation plans approved by security holders	1,970,790	\$ 95.35	2,978,599
Equity compensation plans not approved by security holders	—	—	—
<b>Total</b>	<b>1,970,790</b>	<b>\$ 95.35</b>	<b>2,978,599</b>

<sup>(1)</sup> The number is comprised of 1,462,336 stock options, 475,913 performance shares and 32,541 restricted shares. Refer to NOTE 17, "STOCK INCENTIVE AND STOCK OPTION PLANS," to the *Consolidated Financial Statements* for a description of how options and shares are rewarded.

<sup>(2)</sup> The weighted-average exercise price relates only to the 1,462,336 stock options. Performance and restricted shares do not have an exercise price and, therefore, are not included in this calculation.

The remaining information required by Item 12 is incorporated by reference to the relevant information under the caption "Stock Ownership of Directors, Management and Others" in our 2014 Proxy Statement, which will be filed within 120 days after the end of 2013.

**ITEM 13. Certain Relationships, Related Transactions and Director Independence**

The information required by Item 13 is incorporated by reference to the relevant information under the captions "Corporate Governance" and "Other Information—Related Party Transactions" in our 2014 Proxy Statement, which will be filed within 120 days after the end of 2013.

**ITEM 14. Principal Accounting Fees and Services**

The information required by Item 14 is incorporated by reference to the relevant information under the caption "Selection of Independent Public Accountants" in our 2014 Proxy Statement, which will be filed within 120 days after the end of 2013.

**PART IV****ITEM 15. Exhibits and Financial Statement Schedules**

(a) The following *Consolidated Financial Statements* and schedules filed as part of this report can be found in Item 8 "Financial Statements and Supplementary Data":

- **Management's Report to Shareholders**
- **Report of Independent Registered Public Accounting Firm**
- ***Consolidated Statements of Income* for the years ended December 31, 2013, 2012 and 2011**
- ***Consolidated Statements of Comprehensive Income* for the years ended December 31, 2013, 2012 and 2011**
- ***Consolidated Balance Sheets* at December 31, 2013 and 2012**
- ***Consolidated Statements of Cash Flows* for the years ended December 31, 2013, 2012 and 2011**
- ***Consolidated Statements of Changes in Equity* for the years ended December 31, 2013, 2012 and 2011**
- ***Notes to Consolidated Financial Statements***
- ***Selected Quarterly Financial Data (Unaudited)***

(b) See Exhibit Index at the end of this Annual Report on Form 10-K.



**CUMMINS INC.  
EXHIBIT INDEX**

Exhibit No.	Description of Exhibit
3 (a)	Restated Articles of Incorporation, as amended (incorporated by reference to Exhibit 3(a) to Cummins Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 28, 2009).
3 (b)	By-laws, as amended and restated effective as of May 8, 2012 (incorporated by reference to Exhibit 3(b) to Cummins Inc.'s Quarterly Report on Form 10-Q for the quarter ended July 1, 2012).
4 (a)	Indenture, dated as of September 16, 2013, by and between Cummins Inc. and U.S. Bank National Association (incorporated by reference to Exhibit 4.3 to the Registration Statement on Form S-3 filed with the SEC on September 26, 2013 (Registration Statement No. 333-191189)).
4 (b)	First Supplemental Indenture, dated as of September 24, 2013, between Cummins Inc. and U.S. Bank National Association (incorporated by reference to Exhibit 4.1 of the Current Report on 8-K, filed by Cummins Inc. with the SEC on September 24, 2013 (File No. 001-04949)).
4 (c)	Second Supplemental Indenture, dated as of September 24, 2013, between Cummins Inc. and U.S. Bank National Association (incorporated by reference to Exhibit 4.2 of the Current Report on 8-K, filed by Cummins Inc. with the SEC on September 24, 2013 (File No. 001-04949)).
10 (a)#	2003 Stock Incentive Plan, as amended (incorporated by reference to Exhibit 10(a) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2009).
10 (b)#	Target Bonus Plan (incorporated by reference to Exhibit 10(b) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2009).
10 (c)#	Deferred Compensation Plan, as amended (incorporated by reference to Exhibit 10(c) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2012).
10 (d)#	Supplemental Life Insurance and Deferred Income Plan, as amended (incorporated by reference to Exhibit 10(d) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2011).
10 (e)#	Credit Agreement, dated as of November 9, 2012, by and among Cummins Inc., Cummins Ltd., Cummins Power Generation Ltd., Cummins Generator Technologies Limited, certain other subsidiaries referred to therein and the Lenders party thereto. (incorporated by reference to Exhibit 10.1 to Cummins Inc.'s Current Report on Form 8-K dated November 9, 2012).
10 (f)#	Deferred Compensation Plan for Non-Employee Directors, as amended (filed herewith).
10 (g)#	Excess Benefit Retirement Plan, as amended (incorporated by reference to Exhibit 10(g) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2011).
10 (h)#	Employee Stock Purchase Plan, as amended (incorporated by reference to Annex B to Cummins Inc.'s definitive proxy statement filed with the Securities and Exchange Commission on Schedule 14A on March 27, 2012 (File No. 001-04949)).
10 (i)#	Longer Term Performance Plan (incorporated by reference to Exhibit 10(i) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2009).
10 (j)#	2006 Executive Retention Plan, as amended (incorporated by reference to Exhibit 10(j) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2011).
10 (k)#	Senior Executive Target Bonus Plan (incorporated by reference to Exhibit 10(k) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2009).
10 (l)#	Senior Executive Longer Term Performance Plan (incorporated by reference to Exhibit 10(l) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2009).
10 (m)#	Form of Stock Option Agreement under the 2003 Stock Incentive Plan (incorporated by reference to Exhibit 10(m) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2009).
10 (n)#	Form of Performance Share Award Agreement under the 2003 Stock Incentive Plan (incorporated by reference to Exhibit 10(n) to Cummins Inc.'s Annual Report on Form 10-K for the year ended December 31, 2009).
10 (o)#	2012 Omnibus Incentive Plan (incorporated by reference to Annex A to Cummins Inc.'s definitive proxy statement filed with the Securities and Exchange Commission on Schedule 14A on March 27, 2012 (File No. 001-04949)).
10 (p)#	Form of Stock Option Agreement under the 2012 Omnibus Incentive Plan (filed herewith).
10 (q)#	Key Employee Stock Investment Plan (incorporated by reference to Exhibit 4.3 to Cummins Inc.'s Registration Statement on Form S-8 on November 6, 2012 (File No. 333-184786)).
12	Calculation of Ratio of Earnings to Fixed Charges (filed herewith).
21	Subsidiaries of the Registrant (filed herewith).
23	Consent of PricewaterhouseCoopers LLP (filed herewith).
24	Powers of Attorney (filed herewith).
31 (a)	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31 (b)	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32	Certifications Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).
101 .INS	XBRL Instance Document.
101 .SCH	XBRL Taxonomy Extension Schema Document.
101 .CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101 .DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101 .LAB	XBRL Taxonomy Extension Label Linkbase Document.
101 .PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

# A management contract or compensatory plan or arrangement.

**CUMMINS INC. DEFERRED COMPENSATION PLAN  
FOR NON-EMPLOYEE DIRECTORS**

As Amended and Restated as of October 14, 2013

**TABLE OF CONTENTS**

	<b><u>Page</u></b>
<b>Article I</b> RESTATEMENT AND PURPOSE	1
Section 1.01. Restatement and Application	1
Section 1.02. Application of Restatement	1
Section 1.03. Purpose	1
Section 1.04. Funding	1
<b>Article II</b> DEFINITIONS AND INTERPRETATION	1
Section 2.01 Definitions	1
Section 2.02 Rules of Interpretation	5
<b>Article III</b> PARTICIPATION	6
Section 3.01. Commencement of Participation	6
Section 3.02. Cessation of Participation	6
<b>Article IV</b> ELECTIONS TO DEFER	6
Section 4.01. General Provisions	6
Section 4.02. Election Form	7
<b>Article V</b> DEFERRED COMPENSATION ACCOUNTS	7
Section 5.01. Establishment of Deferred Cash Accounts	7
Section 5.02. Establishment of Deferred Stock Account	7
Section 5.03. Separate Accounts for Grandfathered Amounts	8
<b>Article VI</b> ADJUSTMENTS TO DEFERRED CASH ACCOUNTS	8
<b>Article VII</b> PAYMENT OF DEFERRED AMOUNTS	9
Section 7.01. Timing of Payments	9
Section 7.02. Form of Payment	9
Section 7.03. Amount of Installment Payments	9
Section 7.04. Death Benefits	10
Section 7.05. Payments Upon a Change of Control	10
Section 7.06. Payments on Account of Unforeseeable Emergency	10
Section 7.07. Designating a Beneficiary	10
<b>Article VIII</b> ADMINISTRATION OF PLAN	11
Section 8.01. Powers and Responsibilities of the Administrator	11
Section 8.02. Indemnification	12
Section 8.03. Claims and Claims Review Procedure	12
<b>Article IX</b> GROSS-UP PAYMENTS	13
<b>Article X</b> AMENDMENT AND TERMINATION	14



<b>Article XI MISCELLANEOUS</b>	14
Section 11.01. Obligations of the Company	14
Section 11.02. Employment Rights	14
Section 11.03. Non-Alienation	14
Section 11.04. Tax Withholding	15
Section 11.05. Other Plans	15
Section 11.06. Liability of Affiliated Employers	15

**CUMMINS INC. DEFERRED COMPENSATION PLAN FOR  
NON-EMPLOYEE DIRECTORS**

**ARTICLE I  
RESTATEMENT AND PURPOSE**

**Section 1.01. Restatement and Application.** Cummins Inc. established the Deferred Compensation Plan for Non-Employee Directors of Cummins Inc. ("Plan"), effective April 5, 1994, and it has amended the Plan since that time. The Plan was last amended and restated effective October 15, 2012. The Plan is again amended and restated effective October 14, 2013, to incorporate certain changes to the terms of the Plan.

**Section 1.02. Application of Restatement.** This document shall apply to all amounts deferred or vested under the Plan after 2004 and any earnings credited with respect to such amounts. It does not apply to any amount deferred and vested on or before December 31, 2004, or any earnings credited under the Plan with respect to such amounts (together, "Grandfathered Amounts"), and Grandfathered Amounts shall continue to be governed by the terms and conditions of the Plan as in effect on December 31, 2007; provided, however, the person or persons entitled to receive any remaining portion of a Participant's Accounts after his death shall be determined pursuant to this document, provided that the Participant's death occurs after 2004.

**Section 1.03. Purpose.** The sole purpose of this Plan is to provide non-employee directors of the Company with an opportunity to defer Compensation from the Company in accordance with the terms and conditions set forth herein.

**Section 1.04. Funding.** The Company has established the Trust to hold assets for the provision of certain benefits under the Plan as well as other employer benefits. Assets of the Trust are subject to the claims of the Company's and any Affiliated Employer's general creditors, and no Participant shall have any interest in any assets of the Trust or the Company other than as a general creditor of the Company.

**ARTICLE II  
DEFINITIONS AND INTERPRETATION**

**Section 2.01. Definitions.** When the first letter of a word or phrase is capitalized herein and the word or phrase is not otherwise defined, the word or phrase shall have the meaning specified below:

- (a) "Account" means, with respect to a Participant, his Deferred Cash Account or Deferred Stock Account. Where the context permits, "Account" also means the amount credited to such Account. To the extent necessary to administer the Plan, a separate sub-account may be created for each Payment Year to which is credited the amounts deferred during such Payment Year.
- (b) "Administrator" means the Company's Benefits Policy Committee or such other person that the Board designates as Administrator. To the extent that the Administrator delegates a duty or responsibility to an agent, the term "Administrator" shall include such agent.
- (c) "Affiliated Employer" means (i) a member of a controlled group of corporations (as defined in Code Section 414(b)) of which the Company is a member or (ii) an unincorporated trade or business under common control (as defined in Code Section 414(d)) with the Company.
- (d) "Affirmation of Domestic Partnership" means an Applicable Form for affirming the relationship between a Participant and his Domestic Partner.
- (e) "Applicable Form" means a form provided by the Administrator for making an election or designation under the Plan. To the extent permitted by the Administrator, an Applicable Form may be provided and/or an election or designation made electronically.
- (f) "Beneficiary" means the person or entity entitled to receive a Participant's death benefits under Section 7.04, if any, remaining after the Participant's death. A Participant's Beneficiary shall be determined as provided in Section 7.07.
- (g) "Benefit Claim" means a request or claim for a benefit under the Plan, including a claim for greater benefits than have been paid.
- (h) "Board" or "Board of Directors" means the Company's Board of Directors or, where the context so permits, its designee.

- (i) "Cash Deferrals" means the cash portion of eligible Compensation deferred by a Director pursuant to the Plan.
- (j) "Change of Control" means the occurrence of any of the following:
  - (1) there shall be consummated (A) any consolidation or merger of the Company in which the Company is not the continuing or surviving corporation or pursuant to which shares of the Company's common stock would be converted in whole or in part into cash or other securities or property, other than a merger of the Company in which the holders of the Company's common stock immediately before the merger have substantially the same proportionate ownership of common stock of the surviving corporation immediately after the merger, or (B) any sale, lease, exchange or transfer (in one transaction or a series of related transactions) of all or substantially all of the assets of the Company, or
  - (2) the liquidation or dissolution of the Company, or
  - (3) any 'person' (as such term is used in Sections 13(d)(3) and 14(d)(2) of the Securities Exchange Act of 1934, as amended ('the Exchange Act')), other than the Company or a subsidiary thereof or any employee benefit plan sponsored by the Company or a subsidiary thereof or a corporation owned, directly or indirectly, by the shareholders of the Company in substantially the same proportions as their ownership of stock of the Company, shall become the beneficial owners (within the meaning of Rule 13d-3 under the Exchange Act) of securities of the Company representing 25% or more of the combined voting power of the Company's then outstanding securities ordinarily (and apart from rights accruing in special circumstances) having the right to vote in the election of directors, as a result of a tender or exchange offer, open market purchases, privately negotiated purchases, or otherwise, or
  - (4) at any time during a period of two consecutive years, individuals who at the beginning of such period constituted the Board of Directors shall cease for any reason to constitute at least a majority thereof, unless the election or the nomination for election by the Company's stockholders of each new director during such two-year period was approved by a vote of at least two-thirds (2/3) of the directors then still in office who were directors at the beginning of such two-year period, or
  - (5) any other event shall occur that would be required to be reported in response to Item 6(e) (or any successor provision) of Schedule 14A or Regulation 14A promulgated under the Exchange Act.

Notwithstanding the preceding provisions, an event or series of events shall not constitute a Change of Control unless the event or series of events qualifies as a change in the ownership or effective control of the corporation or in the ownership of a substantial portion of the assets of the corporation within the meaning of Code Section 409A(a)(2)(A) (v).

- (k) "Code" means the Internal Revenue Code of 1986, as amended from time to time.
- (l) "Company" means Cummins Inc.
- (m) "Compensation" means all fees, whether paid in cash or shares of the Company's common stock, earned as a Director, and fees to be received for serving as a chairperson or member or for attending a meeting of a Board committee; provided, however, Compensation does not include any consulting fees earned by the Director.
- (n) "Deferred Cash Account" means the bookkeeping account established by the Company for a Participant under Section 5.01.
- (o) "Deferred Stock Account" means the bookkeeping account established by the Company for a Participant under Section 5.02.
- (p) "Denial" or "Denied" means a denial, reduction, termination, or failure to provide or make payment (in whole or in part) of a Plan benefit.
- (q) "Designated Distribution Date" means the date on which distribution of a Payment Year's sub-account is to commence as elected pursuant to Section 4.02(c) or Section 4.01(d), as applicable. Except as otherwise provided in Section 4.02 or permitted by the Administrator, a Participant's Designated Distribution Date must be a specified Quarterly Distribution Date occurring at least two years after the end of the calendar year for which the deferral is made.

- (r) "Designated Form" means the method of distribution of the Participant's Account as elected pursuant to Section 4.02(b) or Section 4.01(d), as applicable.
- (s) "Director" means a member of the Company's Board of Directors who is not an officer or employee of the Company.
- (t) "Domestic Partner" means a person of the same or opposite sex (i) with whom the Participant has a single, dedicated relationship and has shared the same permanent residence for at least six months, (ii) who is not married to another person or part of another domestic partner relationship and is at least age 18, (iii) who, with the Participant, is mutually responsible for the other's welfare, (iv) who, with the Participant, intends for their relationship to be permanent, (v) who is not so closely related to the Participant as to preclude marriage under state law, and (vi) for whom there is an Affirmation of Domestic Partnership on file with the Administrator. In determining whether the requirements of clauses (i) through (v) of the preceding sentence have been satisfied, the Administrator may rely on the Affirmation of Domestic Partnership filed with the Administrator.
- (u) "Domestic Relations Order" has the meaning specified in Code Section 414(p)(1)(B).
- (v) "Grandfathered Amount" has the meaning specified in Section 1.02.
- (w) "Non-Grandfathered Amount" means a benefit under the Plan that is not a Grandfathered Amount.
- (x) "Participant" means a Director who agrees to make deferrals under the Plan and to be bound by the provisions of the Plan on a form provided by the Company, and who is, or whose Beneficiaries are, entitled to benefits under the Plan. Once an individual has become a Participant pursuant to the preceding sentence, he shall remain a Participant until his entire benefit under the Plan has been distributed.
- (y) "Payment Year" means a Director's annual term of service, which is the period beginning on the day after an annual shareholders meeting of the Company and ending on the date of the subsequent year's annual shareholders meeting.
- (z) "Plan" means the "Cummins Inc. Deferred Compensation Plan for Non-Employee Directors," as set out in this document and as it may be amended from time to time.
- (aa) "Quarterly Distribution Date" means March 15, June 15, September 15, or December 15.
- (bb) "Spouse" means, as of the date of a Participant's death, (i) the person to whom the Participant is married in accordance with applicable law of the jurisdiction in which the Participant resides, or (ii) in the case of a Participant not described in clause (i), the Participant's Domestic Partner.
- (cc) "Stock Deferrals" means the stock portion of eligible Compensation deferred by a Director pursuant to the Plan.
- (dd) "Terminates Service," "Termination of Service," or any variation thereof refers to a separation from service within the meaning of Code Section 409A(a)(2)(A) (i) for a reason other than the Director's death.
- (ee) "Trust" means the grantor trust established by the Company to hold assets for the provision of certain benefits under the Plan as well as other employer benefits.
- (ff) "Trustee" means the Trustee of the Trust.
- (gg) "Unforeseeable Emergency" has the meaning given to such term by Code Section 409A and the guidance thereunder. In general, the term means a severe financial hardship to the Participant resulting from an illness or accident of the Participant, the Participant's spouse, the Participant's beneficiary or a dependent (as defined in Code Section 152(a)) of the Participant; loss of the Participant's property due to casualty; or other similar extraordinary and unforeseeable circumstances arising from events beyond the control of the Participant.

**Section 2.02. Rules of Interpretation.**

- (a) The Plan is intended to comply with Code Section 409A, and it shall be interpreted and administered in accordance with such intent. Except as provided in the preceding sentence or as otherwise expressly provided herein, the Plan shall be construed, enforced, and administered, and the validity thereof determined, in accordance with the internal laws of the State of Indiana without regard to conflict of law principles, and the following provisions of this Section.
- (b) Words used herein in the masculine shall be construed to include the feminine, where appropriate, and *vice versa*, and words used herein in the singular or plural shall be construed to include the plural or singular, where appropriate.
- (c) Headings and subheadings are used for convenience of reference only and shall not affect the interpretation of any provision hereof.

(d) If any provision of the Plan shall be held to violate the Code or be illegal or invalid for any other reason, that provision shall be deemed null and void, but the invalidation of that provision shall not otherwise affect the Plan.

(e) Reference to any provision of the Code or other law shall be deemed to include a reference to the successor of such provision.

### **ARTICLE III PARTICIPATION**

**Section 3.01. Commencement of Participation.** The Board or its designee shall provide each Director with a copy or summary of the Plan and the forms needed to make Cash Deferrals or Stock Deferrals under the Plan. Any such Director shall become a Participant only after completing such forms and making such elections as the Board may prescribe, including an agreement to be bound by all terms of the Plan and all determinations of the Administrator or the Board.

**Section 3.02. Cessation of Participation.** A Participant shall continue to be eligible to make deferrals under the Plan until the Participant ceases to be an eligible Director. Termination of participation shall be effective as of the date on which the Director both Terminates Service and his entire interest in the Plan has been distributed.

### **ARTICLE IV ELECTIONS TO DEFER**

#### **Section 4.01. General Provisions.**

(a) A Director newly elected to the Board may elect to defer his or her Compensation attributable to services performed for the balance of the Payment Year in which he or she was elected. The election to defer Compensation may be made until 6:00 P.M. of the day of the Board meeting at which the Director is so elected (the time zone of location of said Board meeting shall control).

(b) Before December 31 of any year, an incumbent Director may elect to defer all or a portion of his Compensation for services as a Director during any Payment Year(s) beginning in a later calendar year, in which case the elected deferrals shall be deferred and credited to a bookkeeping sub-account or sub-accounts for the applicable Payment Year established pursuant to the terms of the Plan.

(c) A Participant may change an existing deferral election with respect to future Compensation only by filing a new election form pursuant to Subsection (b), in which case the change shall be effective with respect to the Participant's Compensation for services as a Director during the Payment Year beginning after the calendar year in which the election was filed (and later Payment Years, as elected by the Participant).

(d) A Participant may change the Designated Distribution Date and/or Designated Form for a Payment Year's sub-account only by filing an Applicable Form with the Administrator that meets the following requirements: the Participant's election change shall (i) not be effective until 12 months after it is filed with the Administrator, (ii) be valid only if it defers the payment of the relevant sub-account for a period of not less than five years from the date it otherwise would have been made, and (iii) if the election relates to a payment at a specified time or pursuant to a specified schedule, be valid only if it is made at least 12 months before the date the payment is scheduled to be paid.

(e) A Participant may change the investment option(s) stipulated for crediting earnings on his or her Account pursuant to Section 5.02(c) and Article VI of the Plan and such procedures as are prescribed by the Administrator.

(f) A Participant may change his or her designation of Beneficiary(ies) at any time by filing a new election form with the Administrator.

**Section 4.02 Election Form.** A Director may make an election to defer amounts under the Plan by filing with the Administrator an Applicable Form within the applicable time as specified in Section 4.01 above. A completed election form shall stipulate:

(a) The percentage of the cash portion of eligible Compensation and the common stock portion of eligible Compensation to be deferred.

(b) The method of distribution of the Participant's Account. The Participant may elect to receive payment of his Account in either (i) one lump sum payment or (ii) a specified number of annual installments, not to exceed 15. A Participant may elect a different form of distribution for each Payment Year's sub-account.

- (c) The date on which distribution is to commence, subject to the provisions of Article VII.
- (d) The optional rate(s) for crediting earnings on Cash Deferrals.

**ARTICLE V**  
**DEFERRED COMPENSATION ACCOUNT'S**

**Section 5.01. Establishment of Deferred Cash Accounts.** At the time of a Participant's initial election to make Cash Deferrals pursuant to Article IV, the Company shall establish a bookkeeping account (known as the Deferred Cash Account) for such Participant to record his interest under the Plan attributable to Cash Deferrals. Cash Deferrals made by a Participant for a Payment Year shall be credited to the Deferred Cash Account as of the last day of the Payment Year, and the Account shall be adjusted as provided in Article VI.

**Section 5.02. Establishment of Deferred Stock Account**

(a) At the time of a Participant's initial election to make Stock Deferrals pursuant to Article IV, the Company shall establish a bookkeeping account (known as the Deferred Stock Account) for such Participant to record his interest under the Plan attributable to Stock Deferrals. Stock Deferrals made by a Participant for a Payment Year (rounded up to the next whole share) shall be credited to the Deferred Stock Account as of the last day of the Payment Year. Any part of the stock portion of a Director's Compensation not covered by a Stock Deferral election shall be paid to the Director in accordance with the terms of the Cummins Inc. 2012 Omnibus Incentive Plan (or any successor plan thereto) and the applicable award thereunder.

(b) The Deferred Stock Account shall also be credited with an amount equivalent to the dividends that would have been paid on an equal number of outstanding shares of the Company's common stock then credited to the Participant's Deferred Stock Account. Such amount shall be credited as of the payment date of such dividend and converted into an additional number of whole and partial deferred shares as of such date (based on the average of the closing prices of such stock for the 20 consecutive trading days immediately preceding such date). Such additional deferred shares shall thereafter be treated in the same manner as any other shares credited to the Participant's Deferred Stock Account.

(c) Upon either (i) a Participant reaching age 70, or (ii) commencement of distribution of the Participant's Account, the Participant may elect to allocate all or any portion of the value of Participant's Deferred Stock Account into the other available investment options under the Plan. The Participant may choose more than one investment option in such minimum increments as are prescribed by the Administrator.

Such election must be made in writing no later than the beginning of the year one year prior to the year in which either (i) age 70 is attained, or (ii) the first annual installment from the Account which is to be affected by the election is made.

The value of the stock units affected by this election shall be determined by multiplying the number of stock units so affected by the 90-day average closing price of the Common Stock of the Company on the New York Stock Exchange covering the 90 trading days immediately preceding the date the investment diversification election is submitted by the Participant to the Administrator. After the initial diversification is made, a Participant may change the investment election once per month (beginning after the initial diversification election) or at other times prescribed by the Administrator.

(d) The number and kinds of shares standing to the credit of a Participant's Deferred Stock Account shall be appropriately adjusted from time to time, as determined by the Administrator in its discretion, in the event of changes in the Company's outstanding common stock by reason of stock dividends, stock splits, spinoffs, or other distributions of assets (other than normal cash dividends), recapitalizations, reorganizations, mergers, consolidations, combinations, exchanges, or other relevant changes in the Company's corporate structure or capitalization. Notwithstanding the foregoing, if the Company shall subdivide the shares of common stock or the Company shall declare a dividend payable in shares of common stock, and if no action is taken by the Administrator, then the adjustments contemplated by this subsection (d) that are proportionate shall nevertheless automatically be made as of the date of such subdivision of the shares or dividend in shares.

**Section 5.03. Separate Accounts for Grandfathered Amounts.** The Company shall separately account for Grandfathered Amounts and Non-Grandfathered Amounts.

**ARTICLE VI**  
**ADJUSTMENTS TO DEFERRED CASH ACCOUNTS**

As of the last day of each calendar month, the Company shall credit the Participant's Deferred Cash Account with an earnings factor. The earnings factor will equal the amount the Participant's Deferred Cash Account would have earned if it had been invested in the investment options determined from time to time by the Company. The Participant is permitted to select the investment option(s) used to determine the earnings factor and may change the selection once per month or at other times as prescribed by the Administrator. The Participant may choose more than one investment option in such minimum increments as are prescribed by the Administrator. The Company reserves the right to change or amend any of the investment options at any time. The Company is under no obligation to acquire or provide any of the investments designated by a Participant, and any investments actually made by the Company will be made solely in the name of the Company and will remain the property of the Company. The crediting of an earnings factor shall occur so long as there is a balance in the Participant's Deferred Cash Account, regardless of whether the Participant has Terminated Service.

**ARTICLE VII**  
**PAYMENT OF DEFERRED AMOUNTS**

**Section 7.01. Timing of Payments.** Each Payment Year's sub-account within a Participant's Deferred Cash Account and Deferred Stock Account shall be paid (or commence distribution, if paid in installments) to the Participant (or the Participant's Beneficiary, if the Participant is deceased) on the earliest to occur of the following:

- (a) the Participant's death as described in Section 7.04;
- (b) the first business day of the calendar quarter following the Participant's Termination of Service;
- (c) a Change of Control as described in Section 7.05; or
- (d) the Designated Distribution Date for the Payment Year's sub-account.

**Section 7.02. Form of Payment.** All distributions from a Participant's Deferred Cash Account shall be paid in cash. All distributions from a Participant's Deferred Stock Account shall be paid in shares of Company common stock (other than any fractional share which shall be paid in cash) and such shares shall be issued under, and subject to, the Cummins Inc. 2012 Omnibus Incentive Plan (or a successor plan thereto); provided that, to the extent the allocation election described in Section 5.02(c) has been made, the amount so allocated shall be paid in cash.

**Section 7.03. Amount of Installment Payments.**

(a) The amount of each annual cash installment from a Payment Year's sub-account within a Participant's Deferred Cash Account or a Participant's Deferred Stock Account (to the extent the allocation election described in Section 5.02(c) has been made) shall be determined by dividing the credit balance in such sub-account as of the distribution date by the number of installments then remaining unpaid (including the installment for which the calculation is being made). The credit balance in the Payment Year's sub-account within the Participant's Deferred Cash Account or Deferred Stock Account shall be reduced by the amount of each distribution out of such Account.

(b) The number of shares distributed in each annual installment from a Payment Year's sub-account within a Participant's Deferred Stock Account (to the extent allocated to stock units) shall be determined by dividing the number of stock units in such sub-account as of the distribution date by the number of installments then remaining unpaid (including the installment for which the calculation is being made), with the number to be distributed rounded up to the next whole share. The number of stock units in the Payment Year's sub-account within the Participant's Deferred Stock Account shall be reduced by the number of shares included in each installment. The value of any partial share remaining on the date of the final installment from such sub-account shall be paid in cash.

**Section 7.04. Death Benefits.** Notwithstanding anything to the contrary herein, in the event of the Participant's death, payment of the entire balance in the Participant's Deferred Cash Account and Deferred Stock Account shall be made to the Participant's designated Beneficiary(ies) in a single lump sum payment within 90 days following the Participant's death.

**Section 7.05. Payments Upon a Change of Control.** Notwithstanding anything to the contrary herein, upon a Change of Control, the balance in each Participant's Deferred Cash Account and Deferred Stock Account shall

be paid to the Participant (or, if the Participant is deceased, Beneficiary) in a single lump sum payment. Such payment shall be made on the date of the Change of Control.

**Section 7.06. Payments on Account of Unforeseeable Emergency** . Notwithstanding anything to the contrary in Section 7.01, if a Participant demonstrates to the satisfaction of the Chairman of the Board and the Chair of the Compensation Committee of the Board (together, the "Chairs") that he or she has incurred an Unforeseeable Emergency, the amount reasonably necessary to satisfy the emergency need (including any amounts necessary to pay any income taxes or penalties reasonably anticipated to result from the distribution), as determined by the Chairs, shall be distributed to the Participant as soon as administratively feasible after the decision of the Chairs; provided that, in determining whether an Unforeseeable Emergency has been incurred and the amount reasonably necessary to satisfy the emergency need, the Chairs shall take into consideration, among other things, all amounts available to the Participant under the Cummins Inc. and Affiliates Retirement and Savings Plans ("RSP") (including by obtaining a loan under the RSP). If the Chairs grant a request for withdrawal pursuant to this Section, the Administrator shall prospectively cancel the Participant's existing deferral elections, and the Chairs shall take into account the additional compensation that is available as a result of the cancellation of those elections in determining the amount reasonably necessary to satisfy the Participant's emergency need.

**Section 7.07. Designating a Beneficiary**

(a) The Participant may designate a Beneficiary only by filing a completed Applicable Form with the Administrator during his life. The Participant's proper filing of a Beneficiary designation shall cancel all prior Beneficiary designations. If the Participant does not designate a Beneficiary, or if all properly designated Beneficiaries die before the Participant, then payment of the balance in the Participant's Deferred Cash Account and Deferred Stock Account shall be made to the Participant's estate in the event of the Participant's death.

(b) The following rules shall determine the apportionment of payments due under the Plan among Beneficiaries in the event of the Participant's death:

- (1) If any Beneficiary designated by the Participant as a "Direct Beneficiary" dies before the Participant, his or her interest and the interest of his or her heirs in any payments under the Plan shall terminate and the percentage share of the remaining Beneficiaries designated as Direct Beneficiaries shall be increased on a pro rata basis. If no such Beneficiary survives the Participant, the Participant's entire interest in the Plan shall pass to any Beneficiary designated as a "Contingent Beneficiary."
- (2) If any Beneficiary designated by the Participant as a "Contingent Beneficiary" dies before the Participant, his or her interest and the interest of his or her heirs in any payments under the Plan shall terminate and the percentage share of the remaining Beneficiaries designated as Contingent Beneficiaries shall be increased on a pro rata basis.
- (3) If any Beneficiary dies after the Participant, but before payment is made to such Beneficiary, then the payment shall be made to the Beneficiary's estate.

**ARTICLE VIII  
ADMINISTRATION OF PLAN**

**Section 8.01. Powers and Responsibilities of the Administrator.**

(a) The Administrator shall have full responsibility and discretionary authority to control and manage the operation and administration of the Plan. The Administrator is authorized to accept service of legal process on behalf of the Plan. To the fullest extent permitted by applicable law, any action taken by the Administrator pursuant to a reasonable interpretation of the Plan shall be binding and conclusive on all persons claiming benefits under the Plan, except to the extent that a court of competent jurisdiction determines that such action was arbitrary or capricious.

(b) The Administrator's discretionary powers include, but are not limited to, the following:

- (1) to interpret Plan documents, decide all questions of eligibility, determine whether a Participant has Terminated Service, determine the amount, manner, and timing of distributions under the Plan, and resolve any claims for benefits;
- (2) to prescribe procedures to be followed by a Participant, Beneficiary, or other person applying for benefits;



- (3) to appoint or employ persons to assist in the administration of the Plan and any other agents as it deems advisable;
- (4) to adopt such rules as it deems necessary or appropriate;  
and
- (5) to maintain and keep adequate records concerning the Plan, including sufficient records to determine each Participant's eligibility to participate and his interest in the Plan, and its proceedings and acts in such form and detail as it may decide.

**Section 8.02. Indemnification.** The Company shall indemnify and hold harmless the Administrator, any person serving on a committee that serves as Administrator, and any officer, employee, or director of the Company or any Affiliated Employer to whom any duty or power relating to the administration of the Plan has been properly delegated from and against any cost, expense, or liability arising out of any act or omission in connection with the Plan, unless arising out of such person's own fraud or bad faith.

**Section 8.03. Claims and Claims Review Procedure.**

(a) All Benefit Claims must be made in accordance with procedures established by the Administrator from time to time. A Benefit Claim and any appeal thereof may be filed by the claimant or his authorized representative.

(b) The Administrator shall provide the claimant with written or electronic notice of its approval or Denial of a properly filed Benefit Claim within 90 days after receiving the claim, unless special circumstances require an extension of the decision period. If special circumstances require an extension of the time for processing the claim, the initial 90-day period may be extended for up to an additional 90 days. If an extension is required, the Administrator shall provide written notice of the required extension before the end of the initial 90-day period, which notice shall (i) specify the circumstances requiring an extension and (ii) the date by which the Administrator expects to make a decision.

(c) If a Benefit Claim is Denied, the Administrator shall provide the claimant with written or electronic notice containing (i) the specific reasons for the Denial, (ii) references to the applicable Plan provisions on which the Denial is based, (iii) a description of any additional material or information needed and why such material or information is necessary, and (iv) a description of the applicable review process and time limits.

(d) A claimant may appeal the Denial of a Benefit Claim by filing a written appeal with the Administrator within 60 days after receiving notice of the Denial. The claimant's appeal shall be deemed filed on receipt by the Administrator. If a claimant does not file a timely appeal, the Administrator's decision shall be deemed final, conclusive, and binding on all persons.

(e) The Administrator shall provide the claimant with written or electronic notice of its decision on appeal within 60 days after receipt of the claimant's appeal request, unless special circumstances require an extension of this time period. If special circumstances require an extension of the time to process the appeal, the processing period may be extended for up to an additional 60 days. If an extension is required, the Administrator shall provide written notice of the required extension to the claimant before the end of the original 60-day period, which shall specify the circumstances requiring an extension and the date by which the Administrator expects to make a decision. If the Benefit Claim is Denied on appeal, the Administrator shall provide the claimant with written or electronic notice containing a statement that the claimant is entitled to receive, upon request and free of charge, reasonable access to and copies of all documents, records, and other information relevant to the Benefit Claim, as well as the specific reasons for the Denial on appeal and references to the applicable Plan provisions on which the Denial is based. The Administrator's decision on appeal shall be final, conclusive, and binding on all persons.

**ARTICLE IX  
GROSS-UP PAYMENTS**

If payment of the lump sum value of the Deferred Amounts pursuant to Section 7.05 ("Accelerated Payment") causes the Accelerated Payment and any other payments made in connection with a Change of Control (together with the Accelerated Payment, the "Total Payments") to be subject to the tax ("Excise Tax") imposed by Code Section 4999, the Company shall pay to the Participant an additional amount ("Gross-Up Payment") such that the net amount retained by the Participant, after deduction of any Excise Tax paid or payable (and not grossed-up under a similar provision of another plan or program sponsored by the Company) on the lump sum and such other Total Payments and any federal, state, and local income tax and Excise Tax upon the payment provided for by this Article, shall be equal to the Accelerated Payment and such other Total Payments. If any of such other Total Payments are subject to the Excise Tax without regard to the Accelerated Payment, a Gross-Up Payment shall be made, but shall be limited to the increase in the Excise Tax (plus any federal, state, and local income tax and Excise Tax on such Gross-Up Payment) arising solely as a result of the Accelerated Payment.

For purposes of determining whether any of the payments described above will be subject to the Excise Tax and the amount of such Excise Tax, (i) any other payments or benefits received or to be received by the Participant in connection with a Change of Control, whether payable pursuant to the terms of the Plan or any other plan, arrangement, or agreement with the Company, its successors, any person whose actions result in a change in control of the Company or any corporation affiliated (or which, as a result of the completion of a transaction causing a change of control, will become affiliated) with the Company within the meaning of Code Section 1504 shall be treated as "parachute payments" within the meaning of Code Section 280G(b)(2), and all "excess parachute payments" within the meaning of Code Section 280G(b)(1) shall be treated as subject to the Excise Tax, unless in the opinion of tax counsel selected by the Company's independent auditors, the payments (in whole or in part) do not constitute parachute payments, or such excess parachute payments (in whole or in part) represent reasonable compensation for services actually rendered within the meaning of Code Section 280G(b)(4) either in their entirety or in excess of the base amount within the meaning of Code Section 280G(b)(3), or are otherwise not subject to the Excise Tax, (ii) the amount of the payments that shall be treated as subject to the Excise Tax shall be equal to the lesser of (A) the total amount of the payments or (B) the amount of excess parachute payments within the meaning of Code Section 280G(b)(1) (after applying clause (i), above), and (iii) the value of any non-cash benefits or any deferred payment or benefit shall be determined by the Company's independent auditors and acceptable to the Participant in accordance with the principles of Code Sections 280G(d)(3) and (4). In the event that the Excise Tax is subsequently determined to be less than the amount taken into account hereunder at the time of payment, the Participant shall repay to the Company at the time that the amount of such reduction in Excise Tax is finally determined the portion of the Gross-Up Payment attributable to such reduction (plus the portion of the Gross-Up Payment attributable to the Excise Tax and federal and state and local income tax imposed on the Gross-Up Payment being repaid by the Participant if such repayment results in a reduction in Excise Tax and/or a federal and state and local income tax deduction) plus interest on the amount of such repayment at the rate provided in Code Section 1274(d). In the event that the Excise Tax is determined to exceed the amount taken into account hereunder at the time of the Gross-Up Payment (including by reason of any payment the existence or amount of which cannot be determined at the time of the Gross-Up Payment), the Company shall make an additional Gross-Up Payment in respect of such excess (plus any interest payable with respect to such excess) at the time that the amount of such excess is finally determined.

To the extent that earlier payment is not required by the preceding provisions of this Section, the Company's payment pursuant to this Section shall be made not later than the end of the calendar year next following the calendar year in which the Participant remits the related taxes.

## **ARTICLE X AMENDMENT AND TERMINATION**

The Plan shall continue in force with respect to any Participant until the completion of any payments due hereunder. The Company may, however, at any time, amend the Plan to provide that no additional benefits shall accrue with respect to any Participant under the Plan; provided, however, that no such amendment shall (i) deprive any Participant or Beneficiary of any benefit that accrued under the Plan before the adoption of such amendment; (ii) result in an acceleration of benefit payments in violation of Code Section 409A and the guidance thereunder, or (iii) result in any other violation of Section 409A or the guidance thereunder. The Company may also, at any time, amend the Plan retroactively or otherwise, if and to the extent that it deems such action appropriate in light of government regulations or other legal requirements.

## **ARTICLE XI MISCELLANEOUS**

**Section 11.01. Obligations of the Company.** The only obligation of the Company or any Affiliated Employer hereunder shall be a contractual obligation to make payments to Participants, Spouses, or other Beneficiaries entitled to benefits provided for herein when due, and only to the extent that such payments are not made from the Trust.

**Section 11.02. Employment Rights.** Nothing contain herein shall confer any right on a Participant to be continued in the service of the Company or affect the Participant's right to participate in and receive benefits under and in accordance with any pension, profit-sharing, incentive compensation, or other benefit plan or program of the Company or any Affiliated Employer.

**Section 11.03. Non-Alienation.** Except as otherwise required by a Domestic Relations Order, no right or interest of a Participant, Spouse, or other Beneficiary under this Plan shall be subject to voluntary or involuntary alienation, assignment, or transfer of any kind.

**Section 11.04. Tax Withholding.** The Company or the Trustee may withhold from any distribution hereunder amounts that the Company or the Trustee deems necessary to satisfy federal, state, or local tax withholding requirements (or make other arrangements satisfactory to the Company or Trustee with regard to such taxes).

**Section 11.05. Other Plans.** Amounts and benefits paid under the Plan shall not be considered compensation to the Participant for purposes of computing any benefits to which he may be entitled under any other pension or retirement plan maintained by the Company or any Affiliated Employer.

**Section 11.06. Liability of Affiliated Employers.** If any payment to be made under the Plan is to be made on account of a Participant who is or was employed by an Affiliated Employer, the cost of such payment shall be borne in such proportion as the Company and the Affiliated Employer agree.

This Amendment and Restatement of the Cummins Inc. Deferred Compensation Plan for Non-Employee Directors has been signed by the Company's duly authorized officer, acting on behalf of the Company, on this 14<sup>th</sup> day of October, 2013.

**CUMMINS INC.**

By: /s/ Jill E. Cook  
Title: Vice President - Human Resources

**CUMMINS INC.  
2012 OMNIBUS INCENTIVE PLAN  
STOCK OPTION AGREEMENT**

You have been granted an option (this “Option”) to purchase shares of the common stock, par value \$2.50 per share (the “Common Stock”), of Cummins Inc. (the “Company”) pursuant to the Company’s 2012 Omnibus Incentive Plan (the “Plan”) and this Stock Option Award Agreement (this “Option Agreement”). This Option is granted under and governed by the terms and conditions of the Plan and this Option Agreement. Capitalized terms used but not defined in this Option Agreement shall have the meaning set forth in the Plan.

Detailed information regarding [\_\_\_\_\_] can be found in your [\_\_\_\_\_].

Type of Option:  Incentive Stock Option  
 Nonqualified Stock Option

Term: This Option shall expire on the tenth anniversary of the Grant Date (the “Expiration Date”), unless terminated earlier pursuant to the terms of this Option Agreement or the Plan. Upon termination or expiration of this Option, all your rights hereunder shall cease.

Vesting: *[For non-KESIP options]* [This Option will vest on [\_\_\_\_\_].] *[For KESIP options]* [ This Option is immediately vested in full on the Grant Date.]

Termination of Employment: *[For non-KESIP options]* [If your employment or service with the Company and its Affiliates terminates by reason of your death, your Disability (defined as eligibility for benefits under the Company’s Long Term Disability Plan) or your Retirement, this Option will become fully vested on the date of such termination.]  
The following conditions apply in the event that your employment or service with the Company and its Affiliates is terminated prior to the Expiration Date of this Option. In no event, however, will the time periods described herein extend the term of this Option beyond its Expiration Date or beyond the date this Option is otherwise cancelled or terminates pursuant to the provisions of the Plan.

*a. Termination As a Result of Death.* If your employment or service terminates by reason of your death (at a time when you could not have been terminated for Cause), then your estate or your beneficiary, or such other person or persons as may acquire your rights under this Option by will or by the laws of descent and distribution, may exercise this Option until the first anniversary of such termination of employment or service (or until such longer or shorter period as the Administrator may in its sole discretion determine).

*b. Termination As a Result of Retirement or Disability.* If your employment or service terminates by reason of your Retirement or Disability (at a time when you could not have been terminated for Cause), then you may exercise this Option until the fifth anniversary of such termination of employment or service (or until such longer or shorter period as the Administrator may in its sole discretion determine).

c. *Termination Other than As a Result of Death, Retirement or Disability.* If your employment or service terminates other than by reason of your death, Disability or Retirement, then this Option shall automatically terminate immediately on the date of such termination.

d. *Determination of Cause After Termination.* Notwithstanding the foregoing, if after your employment or service terminates the Company determines that it could have terminated you for Cause had all relevant facts been known at the time of your termination, then the Company may terminate this Option immediately upon such determination, and you will be prohibited from exercising this Option thereafter. In such event, you will be notified of the termination of this Option.

If the date this Option terminates as specified above (other than as a result of a termination for Cause) falls on a day on which the stock market is not open for trading or on a date on which you are prohibited by Company policy (such as an insider trading policy) from exercising the Option, the termination date shall be automatically extended to the first available trading day following the original termination date, but not beyond the Expiration Date.

Manner of Exercise:

You may exercise this Option only if it has not been forfeited or has not otherwise expired, and only to the extent this Option has vested. To exercise this Option, you must comply with such exercise and notice procedures as the Administrator may establish from time to time. A properly completed notice of stock option exercise (or such other notice as is prescribed) will become effective upon receipt of the notice and any required payment by the Company (or its designee); provided that the Company may suspend exercise of the Option pending its determination of whether your employment will be or could have been terminated for Cause and if such a determination is made, your notice of stock option exercise (or such other notice as is prescribed) will automatically be rescinded.

If, following your death, your beneficiary or heir, or such other person or persons as may acquire your rights under this Option by will or by the laws of descent and distribution, wishes to exercise this Option, such person must contact the Company and prove to the Company's satisfaction that such person has the right and is entitled to exercise this Option.

Your ability to exercise this Option, or the manner of exercise or payment of withholding taxes, may be restricted by the Company if required by applicable law or by the Company's trading policies as in effect from time to time.

Restrictions on Resale

By accepting this Option, you agree not to sell any shares of Common Stock acquired under this Option at a time when applicable laws, Company policies or an agreement between the Company and its underwriters prohibit a sale.

Transferability:

You may not transfer or assign this Option for any reason, other than by will or the laws of descent and distribution, or to a spouse or lineal descendant (a "Family Member"), a trust for the exclusive benefit of Family Members or a partnership or other entity in which all the beneficial owners are Family Members, or as otherwise set forth in the Plan. Any attempted transfer or assignment of this Option, other than as set forth in the preceding sentence or the Plan, will be null and void.

Market Stand-Off:

In connection with any underwritten public offering by the Company of its equity securities pursuant to an effective registration statement filed under the Securities Act of 1933, as amended (the “Securities Act”), you agree that you shall not directly or indirectly sell, make any short sale of, loan, hypothecate, pledge, offer, grant or sell any option or other contract for the purchase of, purchase any option or other contract for the sale of, or otherwise dispose of or transfer or agree to engage in any of the foregoing transactions with respect to, any Shares acquired under this Option without the prior written consent of the Company and the Company’s underwriters. Such restriction shall be in effect for such period of time following the date of the final prospectus for the offering as may be requested by the Company or such underwriters. In no event, however, shall such period exceed one hundred eighty (180) days.

Recoupment; Rescission of Exercise

If the Committee determines that recoupment of incentive compensation paid to you pursuant to this Option is required under any law or any recoupment policy of the Company, then this Option will terminate immediately on the date of such determination to the extent required by such law or recoupment policy, any prior exercise of this Option may be deemed to be rescinded, and the Committee may recoup any such incentive compensation in accordance with such recoupment policy or as required by law. The Company shall have the right to offset against any other amounts due from the Company to you the amount owed by you hereunder and any exercise price and withholding amount tendered by you with respect to any such incentive compensation.

Restrictions on Exercise, Issuance and Transfer of Shares:

*a. General.* No individual may exercise this Option, and no shares of Common Stock subject to this Option will be issued, unless and until the Company has determined to its satisfaction that such exercise and issuance will comply with all applicable federal and state securities laws, rules and regulations of the Securities and Exchange Commission, rules of any stock exchange on which shares of Common Stock of the Company may then be traded, or any other applicable laws. In addition, if required by underwriters for the Company, you agree to enter into a lock-up agreement with respect to any shares of Common Stock acquired or to be acquired under this Option.

*b. Securities Laws.* You acknowledge that you are acquiring this Option, and the right to purchase the shares of Common Stock subject to this Option, for investment purposes only and not with a view toward resale or other distribution thereof to the public which would be in violation of the Securities Act. You agree and acknowledge with respect to any shares of Common Stock that have not been registered under the Securities Act, that: (i) you will not sell or otherwise dispose of such shares of Common Stock, except as permitted pursuant to a registration statement declared effective under the Securities Act and qualified under any applicable state securities laws, or in a transaction which in the opinion of counsel for the Company is exempt from such required registration, and (ii) that a legend containing a statement to such effect will be placed on the certificates evidencing such shares of Common Stock. Further, as additional conditions to the issuance of the shares of Common Stock subject to this Option, you agree (with such agreement being binding upon any of your beneficiaries, heirs, legatees and/or legal representatives) to do the following prior to any issuance of such shares of Common Stock: (i) to execute and deliver to the Company such investment representations and warranties as are required by the Company; (ii) to enter into a restrictive stock transfer agreement if required by the Board; and (iii) to take or refrain from taking such other actions as counsel for the Company may deem necessary or appropriate for compliance with the Securities Act, and any other applicable federal or state securities laws, regardless of whether the shares of Common Stock have at that time been registered under the Securities Act, or otherwise qualified under any applicable state securities laws.

Miscellaneous:

- ◆ This Option Agreement may be amended only by written consent signed by both you and the Company, unless the amendment is not to your detriment or the amendment is otherwise permitted without your consent by the Plan.
- ◆ The failure of the Company to enforce any provision of this Option Agreement at any time shall in no way constitute a waiver of such provision or of any other provision hereof.
- ◆ You will have none of the rights of a shareholder of the Company with respect to this Option until Shares are transferred to you upon exercise of the Option.
- ◆ In the event any provision of this Option Agreement is held illegal or invalid for any reason, such illegality or invalidity shall not affect the legality or validity of the remaining provisions of this Option Agreement, and this Option Agreement shall be construed and enforced as if the illegal or invalid provision had not been included in this Option Agreement.
- ◆ As a condition to the grant of this Option, you agree (with such agreement being binding upon your legal representatives, guardians, legatees or beneficiaries) that this Option Agreement shall be interpreted by the Committee and that any interpretation by the Committee of the terms of this Option Agreement or the Plan, and any determination made by the Committee pursuant to this Option Agreement or the Plan, shall be final, binding and conclusive.
- ◆ This Option Agreement may be executed in counterparts.

BY ELECTRONICALLY SIGNING AND AGREEING TO THIS STOCK OPTION AGREEMENT, YOU AGREE TO ALL OF THE TERMS AND CONDITIONS DESCRIBED HEREIN AND IN THE PLAN. YOU ALSO ACKNOWLEDGE HAVING READ THIS AGREEMENT AND THE PLAN.

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[Name]  
[Title]

**CUMMINS INC. AND SUBSIDIARIES**  
**COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES**

In millions	2013	2012	2011	2010	2009
<b>Earnings</b>					
Income before income taxes <sup>(1)</sup>	\$ 2,119	\$ 2,271	\$ 2,671	\$ 1,617	\$ 640
Add					
Fixed charges	112	104	106	95	87
Amortization of capitalized interest	1	2	2	3	5
Distributed income of equity investees	271	329	341	178	215
Less					
Equity in earnings of investees	325	347	375	321	196
Capitalized interest	7	7	4	5	6
Earnings before fixed charges	<u>\$ 2,171</u>	<u>\$ 2,352</u>	<u>\$ 2,741</u>	<u>\$ 1,567</u>	<u>\$ 745</u>
<b>Fixed charges</b>					
Interest expense <sup>(2)</sup>	\$ 41	\$ 32	\$ 44	\$ 40	\$ 35
Capitalized interest	7	7	4	5	6
Amortization of debt discount and deferred costs	2	6	2	1	2
Interest portion of rental expense <sup>(3)</sup>	62	59	56	49	44
Total fixed charges	<u>\$ 112</u>	<u>\$ 104</u>	<u>\$ 106</u>	<u>\$ 95</u>	<u>\$ 87</u>
Ratio of earnings to fixed charges <sup>(4)</sup>	19.4	22.6	25.9	16.5	8.6

<sup>(1)</sup> For the year ended December 31, 2012, consolidated net income included \$52 million of restructuring and other charges, a \$6 million gain related to adjustments from our 2011 divestitures and a \$20 million charge related to legal matters. For the year ended December 31, 2011, consolidated net income included a \$68 million gain related to the disposition of certain assets and liabilities of our exhaust business and a \$53 million gain recorded for the disposition of certain assets and liabilities of our light-duty filtration business, both from the Components segment, and a \$38 million gain related to flood damage recoveries from the insurance settlement related to a June 2008 flood in Southern Indiana. For the year ended December 31, 2010, consolidated net income included \$32 million in Brazil tax recoveries and \$2 million in flood damage expenses. For the year ended December 31, 2009, consolidated net income included \$99 million in restructuring and other charges and a gain of \$12 million related to flood damage recoveries.

<sup>(2)</sup> The interest amount in the table above does not include interest expense associated with uncertain tax positions. In September 2013, we issued \$1 billion of senior unsecured debt.

<sup>(3)</sup> Amounts represent those portions of rent expense that are reasonable approximations of interest costs.

<sup>(4)</sup> We have not issued preferred stock. Therefore, the ratio of earnings to combined fixed charges and preferred stock dividends are the same as the ratios presented above.



**CUMMINS INC.**  
**SUBSIDIARIES OF THE REGISTRANT**

<b>Entity Name</b>	<b>Country or State of Organization</b>
35601 Yukon, Inc.	Canada
665217 B.C. Ltd.	Canada
968392 Alberta Ltd.	Canada
Center of Excellence Singapore Pte. Ltd.	Singapore
Cherry Island Renewable Energy, LLC	Delaware
CIFC Worldwide Partner C.V.	The Netherlands
CMI Africa Holdings BV	The Netherlands
CMI CGT Holdings LLC	Indiana
CMI Foreign Holdings B.V.	The Netherlands
CMI Global Equity Holdings B.V.	The Netherlands
CMI Global Equity Holdings C.V.	The Netherlands
CMI Global Holdings B.V.	The Netherlands
CMI Global Partner 2 C.V.	The Netherlands
CMI Global Partners B.V.	The Netherlands
CMI International Finance Partner 1 LLC	Indiana
CMI International Finance Partner 2 LLC	Indiana
CMI International Finance Partner 3 LLC	Indiana
CMI International Finance Partner 4 LLC	Indiana
CMI International Finance Partner 5 LLC	Indiana
CMI Mexico LLC	Indiana
CMI PGI Holdings LLC`	Indiana
CMI PGI International Holdings LLC	Indiana
CMI Turkish Holdings B.V.	The Netherlands
CMI UK Finance LP	United Kingdom
CMI UK Financing LP	United Kingdom
Coil Systems GmbH	Germany
Consolidated Diesel Company	North Carolina
Consolidated Diesel of North Carolina Inc.	North Carolina
Consolidated Diesel, Inc.	Delaware
Cummins (China) Investment Co. Ltd.	China
Cummins Afrique de l'Quest	Senegal
Cummins Americas, Inc.	Indiana
Cummins Angola Ltd.	Angola
Cummins Argentina-Servicios Mineros S.A.	Argentina
Cummins Asia Pacific Pte. Ltd.	Singapore
Cummins Aust Technologies Pty. Ltd.	Australia
Cummins Austria GmbH	Austria
Cummins Belgium N.V.	Belgium
Cummins Botswana (Pty.) Ltd.	Botswana
Cummins Brasil Ltda.	Brazil
Cummins Canada Limited	Canada

Cummins Caribbean LLC	Puerto Rico
Cummins CDC Holding Inc.	Indiana
Cummins Central Power, LLC	Nebraska
Cummins Centroatamerica Holding S.de R.L.	Panama
Cummins Child Development Center, Inc.	Indiana
Cummins Colombia S.A.S.	Colombia
Cummins Comercializadora S. de R.L. de C.V.	Mexico
Cummins Corporation	Indiana
Cummins Cote d'Ivoire SARL	Cote d'Ivoire
Cummins CV Member LLC	Indiana
Cummins Czech Republic s.r.o.	Czech Republic
Cummins Deutschland GmbH	Germany
Cummins Diesel International Ltd.	Barbados
Cummins Distribution Holdeco Inc.	Indiana
Cummins East Asia Research & Development Co. Ltd.	China
Cummins Eastern Marine, Inc.	Canada
Cummins EMEA Holdings Limited	United Kingdom
Cummins Emission Solutions (China) Co., Ltd.	China
Cummins Emission Solutions Inc.	Indiana
Cummins Emissions Solutions (Pty.) Ltd.	South Africa
Cummins Energetica Ltda.	Brazil
Cummins Energy Solutions Business Europe NV/SA	Belgium
Cummins Energy Solutions Business Iberia	Spain
Cummins Engine (Beijing) Co. Ltd.	China
Cummins Engine (Shanghai) Co. Ltd.	China
Cummins Engine (Shanghai) Trading & Services Co. Ltd.	China
Cummins Engine Holding Co., Inc.	Indiana
Cummins Engine IP, Inc.	Delaware
Cummins Engine Venture Corporation	Indiana
Cummins Filter Co. Ltd.	Korea
Cummins Filtration (Shanghai) Co. Ltd.	China
Cummins Filtration GmbH	Germany
Cummins Filtration Inc.	Indiana
Cummins Filtration International Corp.	Indiana
Cummins Filtration IP, Inc.	Delaware
Cummins Filtration SARL	France
Cummins Filtration Trading (Shanghai) Co., Ltd.	China
Cummins Filtros Ltda.	Brazil
Cummins Fuel Systems (Wuhan) Co. Ltd.	China
Cummins Generator Technologies Americas Inc.	Pennsylvania
Cummins Generator Technologies Australia Pty. Ltd.	Australia
Cummins Generator Technologies Co., Ltd.	China
Cummins Generator Technologies Germany GmbH	Germany
Cummins Generator Technologies India Ltd.	India
Cummins Generator Technologies Italy SRL	Italy
Cummins Generator Technologies Limited	United Kingdom

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Cummins Generator Technologies Norway	Norway
Cummins Generator Technologies Romania S.A.	Romania
Cummins Generator Technologies Singapore Pte Ltd.	Singapore
Cummins Generator Technologies Spain S.A.	Spain
Cummins Ghana Limited	Ghana
Cummins Ghana Mining Limited	Ghana
Cummins Global Financing LP	United Kingdom
Cummins Global Technologies LLP	United Kingdom
Cummins Grupo Comercial Y. de Servicios, S. de R.L. de C.V.	Mexico
Cummins Grupo Industrial S. de R.L. de C.V.	Mexico
Cummins Holland B.V.	The Netherlands
Cummins Hong Kong Ltd.	Hong Kong
Cummins India Ltd.	India
Cummins Intellectual Property, Inc.	Delaware
Cummins International Finance LLC	Indiana
Cummins International Holdings Coopertief U.A.	The Netherlands
Cummins International Holdings LLC	Colorado
Cummins International Holdings LLC	Indiana
Cummins Italia S.P.A.	Italy
Cummins Japan Ltd.	Japan
Cummins Korea Co. Ltd.	Korea
Cummins LLC Member, Inc.	Delaware
Cummins LLP	Kazakhstan
Cummins Ltd.	United Kingdom
Cummins Makina Sanayi ve Ticaret Limited Sirketi	Turkey
Cummins Middle East FZE	Dubai
Cummins Mobility Services Inc.	Indiana
Cummins Mongolia Investment LLC	Mongolia
Cummins Mozambique Ltd.	Mozambique
Cummins Natural Gas Engines, Inc.	Delaware
Cummins New Zealand Limited	New Zealand
Cummins Nigeria Ltd.	Nigeria
Cummins Norte de Colombia S.A.S.	Colombia
Cummins North Africa Regional Office SARL	Morocco
Cummins Northeast, LLC	Delaware
Cummins Northwest LLC	Washington
Cummins Norway AS	Norway
Cummins NV	Belgium
Cummins PGI Holdings Ltd.	United Kingdom
Cummins Power Generation (China) Co., Ltd.	China
Cummins Power Generation (S) Pte. Ltd.	Singapore
Cummins Power Generation (U.K.) Limited	United Kingdom
Cummins Power Generation Deutschland GmbH	Germany
Cummins Power Generation Inc.	Delaware
Cummins Power Generation Limited	United Kingdom
Cummins Power Generation Mali S.A.	South Africa

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Cummins Power Systems LLC	Delaware
Cummins PowerGen IP, Inc.	Delaware
Cummins PowerRent Comercio e Locacao, Ltda.	Brazil
Cummins Research and Technology India Ltd.	India
Cummins Rocky Mountain LLC	Colorado
Cummins Rocky Mountain S. de R.L. de C.V.	Mexico
Cummins Romania Srl	Romania
Cummins S. de R.L. de C.V.	Mexico
Cummins Sales and Service Korea Co., Ltd.	Korea
Cummins Sales and Service Philippines Inc.	Philippines
Cummins Sales and Service Singapore Pte. Ltd.	Singapore
Cummins Sales and Service (Thailand) Co. Ltd.	Thailand
Cummins Scott & English Malaysia Sdn. Bhd.	Malaysia
Cummins Sinai ve Otomotiv Urunleri Sanayi ve Ticaret Limited Sirketi	Turkey
Cummins South Africa (Pty.) Ltd.	South Africa
Cummins South Pacific Pty. Limited	Australia
Cummins Spain, S.L.	Spain
Cummins Sweden AB	Sweden
Cummins Technologies India Limited	India
Cummins Trade Receivables, LLC	Delaware
Cummins Turbo Technologies B.V.	The Netherlands
Cummins Turbo Technologies Limited	United Kingdom
Cummins U.K. Holdings Ltd.	United Kingdom
Cummins U.K. Pension Plan Trustee Ltd.	United Kingdom
Cummins UK Holdings LLC	Indiana
Cummins Vendas e Servicos de Motores e Geradores Ltda.	Brazil
Cummins Venture Corporation	Delaware
Cummins West Africa Limited	Nigeria
Cummins Western Canada L.P.	Canada
Cummins (Xiangfan) Machining Co. Ltd.	China
Cummins Zambia Ltd.	Zambia
Cummins Zimbabwe Pvt. Ltd.	Zimbabwe
Cummins-Scania High Pressure Injection, LLC	Delaware
CWC General Partner Ltd.	Canada
Distribuidora Cummins Centroamerica Costa Rica, S.de R.L.	Costa Rica
Distribuidora Cummins Centroamerica El Salvador, S.de R.L.	El Salvador
Distribuidora Cummins Centroamerica Honduras, S.de R.L.	Honduras
Distribuidora Cummins de Panama, S. de R.L.	Panama
Distribuidora Cummins S.A.	Argentina
Distribuidora Cummins S.A. Sucursal Bolivia	Bolivia
Distribuidora Cummins Sucursal Paraguay SRL	Paraguay
Dynamo Insurance Company, Inc.	Vermont
Industria e Comercio Cummins Ltda.	Brazil
Markon Engineering Company Ltd.	United Kingdom
Newage Engineers GmbH	Germany
Newage Ltd. (U.K.)	United Kingdom

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Newage Machine Tools Ltd.	United Kingdom
OOO Cummins	Russia
Petbow Limited	United Kingdom
Power Group International (Overseas Holdings) B.V.	Holland
Power Group International (Overseas Holdings) Ltd.	United Kingdom
Power Group International Ltd.	United Kingdom
Shanghai Cummins Trading Co., Ltd.	China
Shenzhen Chongfa Cummins Engine Co., Ltd.	Hong Kong
Turbo Drive Ltd.	Hong Kong
Worldwide Partner CV Member LLC	Indiana
Wuxi Cummins Turbo Technologies Co. Ltd.	China
Xiangfan Fleetguard Exhaust System Company, Ltd.	China

**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We hereby consent to the incorporation by reference in the Registration Statements on Form S-3 (No. 333-191189) and Form S-8 (Nos. 003-46097, 033-56115, 333-67391, 333-123368, 333-172650, 333-181927 and 333-184786) of Cummins Inc. of our report dated February 18, 2014 relating to the financial statements and the effectiveness of internal control over financial reporting, which appears in this Form 10-K.

/s/ PRICEWATERHOUSECOOPERS LLP

PricewaterhouseCoopers LLP

Indianapolis, Indiana

February 18, 2014

CUMMINS INC.

2013 Form 10-K

POWER OF ATTORNEY

I hereby legally appoint each of Patrick J. Ward and Marsha L. Hunt as my attorneys-in-fact and agents, with full power of substitution and re-substitution, to sign on my behalf the Annual Report on Form 10-K, and any and all amendments thereto, of Cummins Inc. (the "Company") for the Company's year ended December 31, 2013 and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, and to do anything else that said attorneys-in-fact and agents or any of them, or his or her substitute or substitutes, may lawfully do or cause to be done consistent herewith.

Dated: February 11, 2014

/s/ ROBERT J. BERNHARD

Robert J. Bernhard

Director

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**CUMMINS INC.**

**2013 Form 10-K**

**POWER OF ATTORNEY**

I hereby legally appoint each of Patrick J. Ward and Marsha L. Hunt as my attorneys-in-fact and agents, with full power of substitution and re-substitution, to sign on my behalf the Annual Report on Form 10-K, and any and all amendments thereto, of Cummins Inc. (the "Company") for the Company's year ended December 31, 2013 and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, and to do anything else that said attorneys-in-fact and agents or any of them, or his or her substitute or substitutes, may lawfully do or cause to be done consistent herewith.

Dated: February 11, 2014

/s/ FRANKLIN R. CHANG-DIAZ

Franklin R. Chang-Diaz

*Director*

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**CUMMINS INC.**

**2013 Form 10-K**

**POWER OF ATTORNEY**

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Dated: February 11, 2014

/s/ STEPHEN DOBBS

Stephen Dobbs

*Director*

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**CUMMINS INC.**

**2013 Form 10-K**

**POWER OF ATTORNEY**

I hereby legally appoint each of Patrick J. Ward and Marsha L. Hunt as my attorneys-in-fact and agents, with full power of substitution and re-substitution, to sign on my behalf the Annual Report on Form 10-K, and any and all amendments thereto, of Cummins Inc. (the "Company") for the Company's year ended December 31, 2013 and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, and to do anything else that said attorneys-in-fact and agents or any of them, or his or her substitute or substitutes, may lawfully do or cause to be done consistent herewith.

Dated: February 11, 2014

/s/ ROBERT K. HERDMAN

Robert K. Herdman

*Director*

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**CUMMINS INC.**

**2013 Form 10-K**

**POWER OF ATTORNEY**

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Dated: February 11, 2014

/s/ ALEXIS M. HERMAN

Alexis M. Herman

*Director*

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**CUMMINS INC.**

**2013 Form 10-K**

**POWER OF ATTORNEY**

I hereby legally appoint each of Patrick J. Ward and Marsha L. Hunt as my attorneys-in-fact and agents, with full power of substitution and re-substitution, to sign on my behalf the Annual Report on Form 10-K, and any and all amendments thereto, of Cummins Inc. (the "Company") for the Company's year ended December 31, 2013 and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, and to do anything else that said attorneys-in-fact and agents or any of them, or his or her substitute or substitutes, may lawfully do or cause to be done consistent herewith.

Dated: February 11, 2014

/s/ WILLIAM I. MILLER

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William I. Miller

Director

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**CUMMINS INC.**

**2013 Form 10-K**

**POWER OF ATTORNEY**

I hereby legally appoint each of Patrick J. Ward and Marsha L. Hunt as my attorneys-in-fact and agents, with full power of substitution and re-substitution, to sign on my behalf the Annual Report on Form 10-K, and any and all amendments thereto, of Cummins Inc. (the "Company") for the Company's year ended December 31, 2013 and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, and to do anything else that said attorneys-in-fact and agents or any of them, or his or her substitute or substitutes, may lawfully do or cause to be done consistent herewith.

Dated: February 11, 2014

/s/ GEORGIA R. NELSON

Georgia R. Nelson

*Director*

Certification

I, N. Thomas Linebarger, certify that:

1. I have reviewed this report on Form 10-K of Cummins Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the periods covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the periods in which the report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: February 18, 2014

/s/ N. THOMAS LINEBARGER

N. Thomas Linebarger

*Chairman and Chief Executive Officer*

Certification

I, Patrick J. Ward, certify that:

1. I have reviewed this report on Form 10-K of Cummins Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the periods covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the periods in which the report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: February 18, 2014

/s/ PATRICK J. WARD

Patrick J. Ward

*Vice President and Chief Financial Officer*

**Cummins Inc.**  
**CERTIFICATION PURSUANT TO**  
**18 U.S.C. SECTION 1350,**  
**AS ADOPTED PURSUANT TO**

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Cummins Inc. (the "Company") on Form 10-K for the period ended December 31, 2013, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, N. Thomas Linebarger, Chairman and Chief Executive Officer of the Company, and Patrick J. Ward, Vice President and Chief Financial Officer, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934;  
and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

February 18, 2014

/s/ N. THOMAS LINEBARGER

N. Thomas Linebarger  
*Chairman and Chief Executive Officer*

February 18, 2014

/s/ PATRICK J. WARD

Patrick J. Ward  
*Vice President and Chief Financial Officer*