

NAVISTAR INTERNATIONAL CORP

Form 10-Q

June 09, 2009

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**Form 10-Q**

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

For the quarterly period ended April 30, 2009

OR

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

For the transition period from To

Commission file number 1-9618

**NAVISTAR INTERNATIONAL CORPORATION**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of

**36-3359573**  
(I.R.S. Employer

incorporation or organization)

Identification No.)

**4201 Winfield Road, P.O. Box 1488,**

**Warrenville, Illinois**  
(Address of principal executive offices)

**60555**  
(Zip Code)

**Registrant's telephone number, including area code (630) 753-5000**

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

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

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

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

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

As of May 31, 2009, the number of shares outstanding of the registrant's common stock was 70,300,666, net of treasury shares.

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**Disclosure Regarding Forward-Looking Statements**

Information provided and statements contained in this report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended ( "Securities Act" ), Section 21E of the Securities Exchange Act of 1934, as amended ( "Exchange Act" ), and the Private Securities Litigation Reform Act of 1995. Such forward-looking statements only speak as of the date of this report and the Navistar International Corporation (the "Company" ) assumes no obligation to update the information included in this report. Such forward-looking statements include information concerning our possible or assumed future results of operations, including descriptions of our business strategy. These statements often include words such as believe, expect, anticipate, intend, plan, estimate, or similar expressions. statements are not guarantees of performance or results and they involve risks, uncertainties, and assumptions. For a further description of these factors, see Item 1A, *Risk Factors*, included within our Form 10-K for the year ended October 31, 2008, which was filed on December 30, 2008, and Item 1A, *Risk Factors*, included in this report. Although we believe that these forward-looking statements are based on reasonable assumptions, there are many factors that could affect our actual financial results or results of operations and could cause actual results to differ materially from those in the forward-looking statements. All future written and oral forward-looking statements by us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to above. Except for our ongoing obligations to disclose material information as required by the federal securities laws, we do not have any obligations or intention to release publicly any revisions to any forward-looking statements to reflect events or circumstances in the future or to reflect the occurrence of unanticipated events.

**Available Information**

We are subject to the reporting and information requirements of the Exchange Act and as a result, are obligated to file periodic reports, proxy statements, and other information with the United States Securities and Exchange Commission ( "SEC" ). We make these filings available free of charge on our website (<http://www.navistar.com>) as soon as reasonably practicable after we electronically file them with, or furnish them to, the SEC. The SEC

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maintains a website (<http://www.sec.gov>) that contains our annual, quarterly, and current reports, proxy and information statements, and other information we file electronically with the SEC. You can read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Room 1850, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Information on our website does not constitute part of this Quarterly Report on Form 10-Q.

**Table of Contents****PART I****Item 1. Condensed Consolidated Financial Statements**  
**Navistar International Corporation and Subsidiaries****Consolidated Statements of Operations****(Unaudited)**

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>April 30,</b>		<b>April 30,</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
<b>(in millions, except per share data)</b>				
<b>Sales and revenues</b>				
Sales of manufactured products, net	<b>\$ 2,741</b>	\$ 3,853	<b>\$ 5,636</b>	\$ 6,713
Finance revenues	<b>67</b>	96	<b>142</b>	190
Sales and revenues, net	<b>2,808</b>	3,949	<b>5,778</b>	6,903
<b>Costs and expenses</b>				
Costs of products sold	<b>2,295</b>	3,200	<b>4,618</b>	5,663
Restructuring charges	<b>(3)</b>		<b>55</b>	
Selling, general and administrative expenses	<b>300</b>	364	<b>676</b>	685
Engineering and product development costs	<b>130</b>	99	<b>238</b>	181
Interest expense	<b>57</b>	102	<b>150</b>	269
Other (income) expense, net	<b>22</b>	(4)	<b>(176)</b>	(5)
Total costs and expenses	<b>2,801</b>	3,761	<b>5,561</b>	6,793
Equity in income of non-consolidated affiliates	<b>14</b>	21	<b>31</b>	45
Income before income tax	<b>21</b>	209	<b>248</b>	155
Income tax benefit (expense)	<b>(9)</b>	2	<b>(2)</b>	(9)
<b>Net income</b>	<b>\$ 12</b>	\$ 211	<b>\$ 246</b>	\$ 146
<b>Basic earnings per share</b>	<b>\$ 0.16</b>	\$ 3.00	<b>\$ 3.45</b>	\$ 2.08
<b>Diluted earnings per share</b>	<b>\$ 0.16</b>	\$ 2.88	<b>\$ 3.44</b>	\$ 2.00
<b>Weighted average shares outstanding</b>				
Basic	<b>70.8</b>	70.3	<b>71.2</b>	70.3
Diluted	<b>71.3</b>	73.2	<b>71.5</b>	72.9

See Notes to Condensed Consolidated Financial Statements

**Table of Contents****Navistar International Corporation and Subsidiaries****Consolidated Balance Sheets**

(in millions, except per share data)	April 30, 2009 (Unaudited)	October 31, 2008
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 718	\$ 861
Marketable securities		2
Trade and other receivables, net	794	1,025
Finance receivables, net	1,655	1,789
Inventories	1,646	1,628
Deferred taxes, net	75	75
Other current assets	161	155
<b>Total current assets</b>	<b>5,049</b>	<b>5,535</b>
Restricted cash and cash equivalents	651	557
Trade and other receivables, net	33	31
Finance receivables, net	1,713	1,948
Investments in and advances to non-consolidated affiliates	154	156
Property and equipment (net of accumulated depreciation and amortization of \$1,698 and \$1,603, at the respective dates)	1,419	1,501
Goodwill	287	297
Intangible assets (net of accumulated amortization of \$84 and \$74, at the respective dates)	211	232
Deferred taxes, net	46	41
Other noncurrent assets	94	92
<b>Total assets</b>	<b>\$ 9,657</b>	<b>\$ 10,390</b>
<b>LIABILITIES, REDEEMABLE EQUITY SECURITIES, AND STOCKHOLDERS DEFICIT</b>		
<b>Liabilities</b>		
Current liabilities		
Notes payable and current maturities of long-term debt	\$ 579	\$ 665
Accounts payable	1,525	2,027
Other current liabilities	1,160	1,183
<b>Total current liabilities</b>	<b>3,264</b>	<b>3,875</b>
Long-term debt	5,070	5,409
Postretirement benefits liabilities	1,995	1,646
Deferred taxes, net	97	103
Other noncurrent liabilities	664	709
<b>Total liabilities</b>	<b>11,090</b>	<b>11,742</b>
<b>Redeemable equity securities</b>	<b>14</b>	<b>143</b>
<b>Stockholders deficit</b>		
Series D convertible junior preference stock	4	4
Common stock (\$0.10 par value per share, 110.0 shares authorized, 75.4 shares issued at both dates)	7	7
Additional paid in capital	2,104	1,966
Accumulated deficit	(2,146)	(2,392)
Accumulated other comprehensive loss	(1,252)	(943)
Common stock held in treasury, at cost (5.1 and 4.1 shares, at the respective dates)	(164)	(137)

<b>Total stockholders deficit</b>	<b>(1,447)</b>	<b>(1,495)</b>
<b>Total liabilities, redeemable equity securities, and stockholders deficit</b>	<b>\$ 9,657</b>	<b>\$ 10,390</b>

See Notes to Condensed Consolidated Financial Statements

**Table of Contents****Navistar International Corporation and Subsidiaries****Condensed Consolidated Statements of Cash Flows****(Unaudited)**

(in millions)	Six Months Ended	
	2009	2008
<b>Cash flows from operating activities</b>		
Net income	\$ 246	\$ 146
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	140	156
Depreciation of equipment held for or under lease	27	30
Deferred taxes	(2)	5
Amortization of debt issuance costs	8	10
Stock-based compensation	11	2
Provision for doubtful accounts	28	18
Impairment of goodwill and intangibles	7	
Equity in income of non-consolidated affiliates	(31)	(45)
Dividends from non-consolidated affiliates	47	29
(Gain) loss on sales of affiliates	1	(4)
(Gain) loss on sale of property and equipment	3	(2)
Loss on sale and impairment of repossessed vehicle inventory	15	4
Loss on sale of finance receivables	25	7
Restructuring charges	55	
Changes in other assets and liabilities	(93)	(35)
<b>Net cash provided by operating activities</b>	<b>487</b>	<b>321</b>
<b>Cash flows from investing activities</b>		
Purchases of marketable securities	(354)	(42)
Sales or maturities of marketable securities	356	11
Net change in restricted cash and cash equivalents	(96)	(316)
Capital expenditures	(77)	(103)
Purchase of equipment leased to others	(18)	(14)
Proceeds from sales of property and equipment	4	19
Investments and advances to non-consolidated affiliates	(14)	(4)
Proceeds from sales of affiliates	3	19
Other investing activities		(1)
<b>Net cash used in investing activities</b>	<b>(196)</b>	<b>(431)</b>
<b>Cash flows from financing activities</b>		
Proceeds from issuance of securitized debt	321	815
Principal payments on securitized debt	(658)	(980)
Proceeds from issuance of non-securitized debt	259	74
Principal payments on non-securitized debt	(362)	(8)
Net increase in notes and debt outstanding under revolving credit facilities	71	162
Principal payments under financing arrangements and capital lease obligations	(24)	(51)
Debt issuance costs	(2)	(7)
Stock repurchase	(29)	



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Net cash provided by (used in) financing activities	(424)	5
Effect of exchange rate changes on cash and cash equivalents	(10)	3
Decrease in cash and cash equivalents	(143)	(102)
Cash and cash equivalents at beginning of period	861	777
Cash and cash equivalents at end of the period	\$ 718	\$ 675

See Notes to Condensed Consolidated Financial Statements

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**Navistar International Corporation and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**1. Summary of significant accounting policies**

***Organization and Description of the Business***

Navistar International Corporation ( *NIC* ), incorporated under the laws of the state of Delaware in 1993, is a holding company whose principal operating subsidiaries are Navistar, Inc. and Navistar Financial Corporation ( *NFC* ). References herein to the Company, we, our, or us refer collectively to *NIC*, its subsidiaries, and certain variable interest entities ( *VIEs* ) of which we are the primary beneficiary. We operate in four principal industry segments: Truck, Engine, Parts (collectively called *manufacturing operations* ), and Financial Services. The Financial Services segment consists of *NFC* and our foreign finance operations (collectively called *financial services operations* ).

***Basis of Presentation and Consolidation***

The accompanying unaudited condensed consolidated financial statements include the assets, liabilities, and results of operations of our manufacturing operations, majority-owned dealers ( *Dealcors* ), wholly-owned financial services subsidiaries, and *VIEs* of which we are the primary beneficiary. The effects of transactions among consolidated entities have been eliminated to arrive at the consolidated amounts. Certain reclassifications were made to prior year amounts to conform to the 2009 presentation.

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

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting policies described in our Annual Report on Form 10-K for the year ended October 31, 2008 and should be read in conjunction with the disclosures therein. In our opinion, these interim financial statements reflect all adjustments, consisting of normal recurring adjustments, necessary to present fairly the financial condition, results of operations, and cash flows for the periods presented. Operating results for interim periods are not necessarily indicative of annual operating results.

***Variable Interest Entities***

We are the primary beneficiary of several *VIEs*, primarily joint ventures, established to manufacture or distribute products and enhance our operational capabilities. Our determination that we are the primary beneficiary of these entities is based upon the characteristics of our variable interests, which absorb the majority of the *VIEs* expected gains and losses. Accordingly, we include in our consolidated financial statements the assets and liabilities and results of operations of those entities, even though we may not own a majority voting interest. The liabilities recognized as a result of consolidating these *VIEs* do not represent additional claims on our general assets; rather they represent claims against the specific assets of the consolidated entities. Assets recognized as a result of consolidating these entities are not available to satisfy claims against our general assets.

Our Financial Services segment consolidates several *VIEs*. As a result, our consolidated balance sheets include assets of \$1.9 billion and \$2.2 billion and liabilities of \$1.7 billion and \$2.0 billion as of April 30, 2009 and October 31, 2008, respectively, from securitizations by *VIEs* that are treated as borrowings. In addition, our consolidated balance sheets include assets of \$751 million and \$727 million and related liabilities of \$633 million and \$632 million as of April 30, 2009 and October 31, 2008, respectively, from structures in which we

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**Navistar International Corporation and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**(Unaudited)**

transferred assets to consolidated special purpose entities ( SPEs ) that are not VIEs, which in turn arranged securitizations. Investors that hold on-balance sheet securitization debt have a priority claim on the cash flows generated by their respective securitized assets to the extent required to repay principal and interest. Investors in securitizations with these VIEs and SPEs have no recourse to the general credit of NIC or any other consolidated entity.

Our Financial Services segment does not consolidate a qualifying special purpose entity ( QSPE ) that is outside the scope of Financial Accounting Standards Board ( FASB ) Interpretation ( FIN ) No. 46(R), *Consolidation of Variable Interest Entities An Interpretation of ARB No. 51*, and a conduit since we are not its primary beneficiary. We obtain funds from the QSPE and conduit through consolidated SPEs, which transfer assets to the QSPE and conduit in securitizations. Portions of the transferred assets are accounted for as sales and accordingly those portions are not carried on our consolidated balance sheets. Our consolidated SPEs retain residual economic interests in the future cash flows of the securitized assets that are owned by the QSPE and conduit. We carry these interests as an asset, included in *Finance receivables, net* on our consolidated balance sheets. Retained interests are subordinated to the priority claims of investors in each respective securitization; our maximum loss exposure to the activities of the QSPE and conduit is limited to our retained interests. See Note 4, *Finance receivables*, for further discussion.

We are also involved with other VIEs, which we do not consolidate because we are not the primary beneficiary. Our determination that we are not the primary beneficiary of these entities is based upon the characteristics of our variable interests, which do not absorb the majority of the VIE s expected gains and losses. Our financial support and maximum loss exposure relating to these non-consolidated VIEs is not material to our financial condition, results of operations, or cash flows.

We use the equity method to account for our investments in entities that we do not control under the voting interest or variable interest models, but where we have the ability to exercise significant influence over operating and financial policies. Consolidated net income includes our share of the net earnings of these entities. As of April 30, 2009, we use the equity method to account for investments in 18 partially-owned affiliates, in which NIC or one of its subsidiaries is a shareholder, general or limited partner, or venturer, as applicable, including our 49 percent interest in Blue Diamond Parts ( BDP ), a VIE which we do not consolidate because we are not the primary beneficiary. See Note 6, *Investments in and advances to non-consolidated affiliates*, for further discussion.

***Out-Of-Period Adjustments***

Included in the results of operations for the three months and six months ended April 30, 2009 are certain out-of-period adjustments which represent corrections of prior-period errors. These errors primarily relate to overstatements of *Accounts payable* of \$9 million due to processing errors in our Truck segment that originated in the fourth quarter of 2008 and \$10 million due to errors in self-insurance reserve calculations and related intercompany transaction eliminations between our financial services operations and our manufacturing operations that originated primarily in periods prior to 2008. Correcting these errors, which were not material to any of the related periods, resulted in a \$19 million increase to net income for the three and six month periods ended April 30, 2009.

***Recently Adopted Accounting Standards***

As of January 31, 2009, we adopted FASB Staff Position ( FSP ) No. FAS 140-4 and FIN 46(R)-8, *Disclosures about Transfers of Financial Assets and Interests in Variable Interest Entities*. This FSP requires enhanced

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**Navistar International Corporation and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**(Unaudited)**

disclosures about a transferor's continuing involvement with transferred financial assets and an enterprise's involvement with VIEs and SPEs. We have complied with the disclosure requirements of this FSP as stated above and within Note 4, *Finance receivables*.

As of November 1, 2008, we adopted FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. The statement permits entities to choose to measure many financial instruments and certain other items at fair value. We elected to not measure any of our financial assets or financial liabilities at fair value that were not previously required to be measured at fair value; therefore, the adoption of this statement did not impact our condensed consolidated financial statements.

As of November 1, 2008, we adopted FASB Statement No. 157, *Fair Value Measurements*. The statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. In February 2008, the FASB issued FSPs that (i) deferred the effective date of this statement for one year for certain nonfinancial assets and nonfinancial liabilities and (ii) removed certain leasing transactions from the scope of the statement. There was no adjustment to *Accumulated deficit* as a result of our adoption of FASB Statement No. 157. The disclosures required by this statement are included in Note 8, *Fair value measurements*.

In March 2008, the FASB issued FASB Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities*. The statement amends and expands the disclosure requirements of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. FASB Statement No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The disclosures required by this statement are included in Note 11, *Financial instruments and commodity contracts*.

***Recently Issued Accounting Standards***

Accounting pronouncements issued by various standard setting and governmental authorities that have not yet become effective with respect to our consolidated financial statements are described below, together with our assessment of the potential impact they may have on our consolidated financial statements:

In April 2009, the FASB issued FSP 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*. This statement amends FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, to require disclosures about fair value of financial instruments for interim periods ending after June 15, 2009. Our effective date is July 31, 2009.

In April 2008, the FASB issued FSP No. FAS 142-3, *Determination of the Useful Life of Intangible Assets*, that amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, *Goodwill and Other Intangible Assets*. It is effective for financial statements issued for fiscal years beginning after December 15, 2008 and interim periods within those fiscal years and should be applied prospectively to intangible assets acquired after the effective date. Early adoption is not permitted. The FSP also requires expanded disclosure related to the determination of useful lives for intangible assets and should be applied to all intangible assets recognized as of, and subsequent to, the effective date. Our effective date is November 1, 2009. The impact of FSP No. FAS 142-3 will depend on the size and nature of acquisitions on or after November 1, 2009.

In February 2008, the FASB issued FSP No. FAS 157-2, *Effective Date of FASB Statement No. 157*, that permits companies to partially defer the effective date of FASB Statement No. 157 for one year for nonfinancial assets

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**Navistar International Corporation and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**(Unaudited)**

and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. FSP No. FAS 157-2 does not permit companies to defer recognition and disclosure requirements for financial assets and financial liabilities or for nonfinancial assets and nonfinancial liabilities that are remeasured at least annually. We have decided to defer adoption of FASB Statement No. 157 until November 1, 2009 for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in our consolidated financial statements on a nonrecurring basis. Our significant nonfinancial assets and liabilities that could be impacted by this deferral include assets and liabilities measured at fair value in a business combination as well as goodwill, tangible assets, and intangible assets tested for impairment. We are evaluating the potential impact on our consolidated financial statements, if any.

In December 2008, the FASB issued FSP No. FAS 132(R)-1, *Employers' Disclosures about Postretirement Benefit Plan Assets*, that provides guidance on an employer's disclosures about plan assets of a defined benefit pension or other postretirement plan. Our effective date is October 31, 2010.

In December 2007, the FASB issued FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements - An Amendment of ARB No. 51*, that clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity. It is effective for fiscal years and interim periods within those fiscal years, beginning on or after December 15, 2008. Our effective date is November 1, 2009. Upon adoption, our minority interests will be reported as a separate component of *Stockholders' deficit*.

In December 2007, the FASB issued FASB Statement No. 141(R), *Business Combinations*, that substantially changes the accounting for and reporting of business combinations including (i) expanding the definition of a business and a business combination, (ii) requiring all assets and liabilities of the acquired business, including goodwill and contingent consideration to be recorded at fair value on the acquisition date, (iii) requiring acquisition-related transaction and restructuring costs to be expensed rather than accounted for as acquisition costs, and (iv) requiring reversals of valuation allowances related to acquired deferred tax assets and changes to acquired income tax uncertainties to be recognized in earnings. FASB Statement No. 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. An entity may not apply the statement before that date. Our effective date is November 1, 2009. This statement will generally apply prospectively to business combinations for which the acquisition date is on or after that date; however, adjustments made to deferred tax asset valuation allowances arising from business combinations before the effective date are subject to the provisions of FASB Statement No. 141(R).

***Use of Estimates***

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

***Concentration Risks***

Our financial condition, results of operations, and cash flows are subject to concentration risks related to concentrations of union employees and two customers. As of April 30, 2009, approximately 6,000, or 63%, of

**Table of Contents****Navistar International Corporation and Subsidiaries****Notes to Condensed Consolidated Financial Statements (Continued)****(Unaudited)**

our hourly workers and approximately 760, or 10%, of our salaried workers are represented by labor unions and are covered by collective bargaining agreements. Our collective bargaining agreement with the National Automobile, Aerospace and Agricultural Implement Workers of Canada expires on June 30, 2009. As of April 30, 2009, approximately 800, or 8%, of our hourly workers and approximately 100, or 1%, of our salaried workers are covered by this collective bargaining agreement. See Note 16, *Segment reporting*, for discussion of customer concentrations. Additionally, our future operations may be affected by changes in governmental procurement policies, budget considerations, changing national defense requirements, and global, political, and economic developments in the U.S. and certain foreign countries (primarily Canada, Mexico, Brazil, and Argentina).

**Product Warranty Liability**

Accrued product warranty and deferred warranty revenue activity is as follows:

(in millions)	Six Months Ended April 30,	
	2009	2008
Balance, at beginning of period	\$ 602	\$ 677
Costs accrued and revenues deferred	102	100
Adjustments to pre-existing warranties <sup>(A)</sup>	78	5
Payments and revenues recognized	(180)	(174)
Warranty adjustment related to legal settlement <sup>(B)</sup>	(75)	
Balance, at end of period	\$ 527	\$ 608

(A) Adjustments to pre-existing warranties reflect changes in our estimate of warranty costs for products sold in prior periods. Such adjustments typically occur when claims experience deviates from historic and expected trends. The adjustments were \$61 million and \$78 million for the three months and six months ended April 30, 2009. The adjustments were \$0.86 per diluted share and \$1.09 per diluted share for the three months and six months ended April 30, 2009, respectively.

(B) See Note 2, *Ford settlement and related charges*, for a discussion regarding warranty adjustments related to the Ford Settlement. The amount of deferred revenue related to extended warranty programs was \$129 million at April 30, 2009 and October 31, 2008. Revenue recognized under our extended warranty programs was \$10 million and \$20 million for the three months and six months ended April 30, 2009, respectively, and \$12 million and \$23 million for the three months and six months ended April 30, 2008, respectively.

**2. Ford settlement and related charges**

In January 2009, we reached a settlement agreement with Ford Motor Company ( Ford ) where we agreed to settle our respective lawsuits against each other (the Ford Settlement ). The result of the Ford Settlement resolves all prior warranty claims, resolves the selling price for our engines going forward and allows Ford to pursue a separate strategy related to diesel engines in its products. Additionally, both companies agreed to end their current North America supply agreement for diesel engines as of December 31, 2009 (the agreement was otherwise set to expire July 2012). For additional information on the Ford Settlement, see Note 12, *Commitments and contingencies*.

In the third and fourth quarters of 2008, the Engine segment recognized \$395 million of charges for impairments of property and equipment and related charges associated with its asset groups in the VEE Business Unit. The



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impairment charges were the result of a reduction in demand from Ford for diesel engines produced by the VEE Business Unit and the expectation that Ford's demand for diesel engines would continue to be below previously anticipated levels.

In the first quarter of 2009, in connection with the Ford Settlement we received a \$200 million cash payment from Ford, which was recorded as a gain in *Other (income) expense, net*, and we reversed our previously recorded warranty liability of \$75 million, which was recorded as a reduction of *Costs of products sold*. With the changes in Ford's strategy, we announced our intentions to close our Indianapolis Engine Plant ( IEP ) and our Indianapolis Casting Corporation foundry ( ICC ) and the Engine segment recognized \$58 million of restructuring charges and \$27 million of other related charges. The restructuring charges consisted of \$21 million in personnel costs for employee termination and related benefits, \$16 million of charges for pension and other postretirement benefit contractual termination benefits and a pension curtailment, and \$21 million of other contractual costs. The other related charges consisted of \$21 million related to inventory valuation and low volume adjustments in *Costs of products sold* and \$6 million of indirect employee costs in *Selling, general and administrative expenses*. We expect the majority of the restructuring and other costs, excluding pension and other postretirement related costs, will be paid by the end of 2009, with the balance paid in 2010.

The following table summarizes the activity in the restructuring liability, which excludes \$16 million of charges for pension and other postretirement benefits, contractual termination benefits, and the pension curtailment for 2009:

(in millions)	Balance at October 31, 2008	Additions	Payments	Adjustments	Balance at April 30, 2009
Employee termination charges	\$	\$ 21	\$	\$ (3)	\$ 18
Other contractual costs		21			21
	\$	\$ 42	\$	\$ (3)	\$ 39

In the second quarter of 2009, the Engine segment recognized an additional \$41 million of other related charges primarily related to low volume adjustments of which \$17 million were recognized in *Costs of products sold* and \$24 million were recognized in *Other (income) expense, net*. In addition, \$6 million of indirect employee costs were reversed from *Selling, general and administrative expenses* due to revisions to reflect our expected results.

Due to the loss of the business with Ford, we continue to resolve commercial disputes with certain suppliers and to evaluate alternatives to improve our ongoing cost structure. Such actions may subject us to additional discrete charges in future periods, which could be material. Additionally as a part of the Ford Settlement, we expect to increase our interest in our Blue Diamond Truck ( BDT ) and BDP joint ventures with Ford to 75%. We are currently evaluating the appropriate accounting treatment for the transaction as it relates to the expected increased ownership of BDT and BDP.



**Table of Contents****Navistar International Corporation and Subsidiaries****Notes to Condensed Consolidated Financial Statements (Continued)****(Unaudited)****3. Allowance for doubtful accounts**

The activity related to our allowance for doubtful accounts for trade and other receivables and finance receivables is summarized as follows:

(in millions)	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
Balance, at beginning of period	\$ 109	\$ 107	\$ 113	\$ 101
Provision for doubtful accounts	26	6	28	18
Charge-off of accounts, net of recoveries	(13)	(20)	(19)	(26)
Balance, at end of period	\$ 122	\$ 93	\$ 122	\$ 93

Impaired finance receivables include accounts with specific loss reserves and accounts that are on non-accrual status. Most balances with specific loss reserves are also on a non-accrual status. In certain cases, we continue to collect payments on our impaired finance receivables.

Information regarding impaired finance receivables is as follows:

(in millions)	April 30,	As of October 31,
	2009	2008
Impaired finance receivables with specific loss reserves	\$ 59	\$ 56
Impaired finance receivables without specific loss reserves	4	4
Specific loss reserves on impaired finance receivables	28	21
Finance receivables on non-accrual status	65	61
Average balance of impaired finance receivables	61	47

**Repossessions**

We repossess sold and leased vehicles on defaulted finance receivables and leases, and place them into *Inventories*. We liquidate these repossessions to partially recover the credit losses in our portfolio. Losses recognized at the time of repossession and charged against the allowance for doubtful accounts were \$11 million and \$15 million for the three months and six months ended April 30, 2009, respectively, and \$12 million and \$16 million for the three months and six months ended April 30, 2008, respectively. Losses recognized upon the sale of repossessed vehicles were \$1 million and \$6 million for the three months and six months ended April 30, 2009, respectively, and \$4 million for the three months and six months ended April 30, 2008.

A summary of the activity related to repossessed vehicles is as follows:

Three Months Ended April 30,	Six Months Ended April 30,
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<b>(in millions)</b>	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Repossessed vehicles, at beginning of period	<b>\$ 37</b>	\$ 31	<b>\$ 45</b>	\$ 25
Repossessions	<b>21</b>	42	<b>36</b>	62
Liquidations	<b>(24)</b>	(25)	<b>(41)</b>	(39)
Impairments	<b>(3)</b>		<b>(9)</b>	
Repossessed vehicles, at end of period	<b>\$ 31</b>	\$ 48	<b>\$ 31</b>	\$ 48

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**Navistar International Corporation and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**(Unaudited)**

**4. Finance receivables**

Finance receivables are receivables of our financial services operations, which generally can be repaid or refinanced without penalty prior to contractual maturity. Total finance receivables reported on the consolidated balance sheets are net of an allowance for doubtful accounts.

The primary business of our financial services operations is to provide wholesale, retail, and lease financing for new and used trucks sold by us and our dealers and, as a result, our finance receivables and leases are concentrated in the trucking industry. On a geographic basis, there is not a disproportionate concentration of credit risk in any area of the U.S. or other countries where we have financial service operations. We retain as collateral an ownership interest in the equipment associated with leases and, on our behalf and the behalf of the various trusts, we maintain a security interest in equipment associated with generally all finance receivables.

All of the assets of our financial services operations are restricted through security agreements to benefit the creditors of the respective finance subsidiary. Total on-balance sheet assets of our financial services operations are \$4.6 billion and \$4.9 billion at April 30, 2009 and October 31, 2008, respectively. Included in total assets are on-balance sheet finance receivables of \$3.4 billion and \$3.7 billion at April 30, 2009 and October 31, 2008, respectively.

***Securizations***

Our financial services operations transfer wholesale notes, accounts receivable, retail notes, finance leases, and operating leases through SPEs which generally are only permitted to purchase these assets, issue asset-backed securities, and make payments on the securities. In addition to servicing receivables, our continued involvement in the SPEs includes an economic interest in the transferred receivables and managing exposure to interest rates using interest rate swaps, interest rate caps, and forward contracts. Certain sales of wholesale notes and accounts receivables are considered to be sales in accordance with FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, and are accounted for off-balance sheet. For sales that do qualify for off-balance sheet treatment, an initial gain (loss) is recorded at the time of the sale while servicing fees and excess spread income are recorded as revenue when earned over the life of the finance receivables.

We securitized finance receivables and investment in operating leases of \$309 million and \$321 million under secured borrowings for the three and six month periods ended April 30, 2009, respectively, and \$305 million and \$815 million for the three and six month periods ended April 30, 2008, respectively.

***Off-Balance Sheet Securizations***

We use an SPE that has in place a revolving wholesale note trust, which is a QSPE, which provides for the funding of eligible wholesale notes through an investor certificate and a variable funding certificate. The SPE owned \$738 million of wholesale notes and \$54 million of marketable securities as of April 30, 2009, and \$819 million of wholesale notes and \$95 million of marketable securities as of October 31, 2008. The QSPE holds \$99 million and \$97 million of wholesale notes with our Dealcors as of April 30, 2009 and October 31, 2008, respectively.

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Components of available wholesale note trust funding certificates were as follows:

(in millions)	Maturity	As of April 30, 2009	As of October 31, 2008
Investor certificate	February 2010	\$ 212	\$ 212
Variable funding certificate	October 2009	750	800
<b>Total wholesale note funding</b>		<b>\$ 962</b>	<b>\$ 1,012</b>

Unutilized funding related to the variable funding certificate was \$300 million and \$250 million at April 30, 2009 and October 31, 2008, respectively.

We use another SPE of which we are not the primary beneficiary. The SPE utilizes a \$100 million conduit funding arrangement which provides for the funding of eligible accounts receivables. The conduit matures in August 2009. The trust owned \$113 million of retail accounts and \$21 million of marketable securities as of April 30, 2009, and \$123 million of retail accounts and \$23 million of marketable securities as of October 31, 2008. There was \$86 million and \$52 million of unutilized funding at April 30, 2009 and October 31, 2008, respectively.

For sold receivables, wholesale notes balances past due over 60 days were \$3 million as of April 30, 2009 and October 31, 2008. There were no past due retail balances for the accounts receivable financing at either date. No credit losses on sold receivables were recorded for the three months and six months ended April 30, 2009 and 2008.

**Retained Interests in Off-Balance Sheet Securitizations**

The terms of receivable transfers generally require our financial services operations to provide credit enhancements in the form of excess seller's interests and/or cash reserves, which are owned by the trust and conduit. The maximum exposure under all credit enhancements was \$239 million and \$230 million as of April 30, 2009 and October 31, 2008, respectively.

Retained interests, which arise from the credit enhancements, represent the fair value of the excess of the cash flows from the assets held by the QSPE and conduit over the future payments of debt service to investors in the QSPE and conduit. The securitization agreements entitle us to these excess cash flows. Our retained interests are restricted assets that are subordinated to the interests of the investors in the QSPE and conduit. Our retained interests are recognized as an asset in *Finance receivables, net*.

The key economic assumptions and the sensitivity of the current fair values of residual cash flows comprising our retained interests to an immediate adverse change of 10 percent and 20 percent in each assumption are as follows:

(dollars in millions)	April 30, 2009	As of October 31, 2008	Fair Value Change at April 30, 2009 Adverse 10%	Adverse 20%

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Discount rate	<b>14.1 to 26.9%</b>	14.6 to 23.0%	\$ 2.5	\$ 4.9
Estimated credit losses	<b>0.0 to 0.24%</b>	0.0 to 0.24%	<b>0.1</b>	<b>0.1</b>
Payment speed (percent of portfolio per month)	<b>6.8 to 69.1%</b>	8.8 to 75.7%	<b>0.5</b>	<b>0.9</b>

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The lower end of the discount rate assumption range and the upper end of the payment speed assumption range were used to value the retained interests in the retail account securitization. No percentage for estimated credit losses were assumed for retail account securitizations as no losses have been incurred to date. The upper end of the discount rate assumption range and the lower end of the payment speed assumption range were used to value the retained interests in the wholesale note securitization facility.

The effect of a variation of a particular assumption on the fair value of the retained interests is calculated based upon changing one assumption at a time. Oftentimes however, changes in one factor may result in changes in another, which in turn could magnify or counteract these reported sensitivities.

**Finance Revenues**

Finance revenues derived from receivables that are both on and off-balance sheet consist of the following:

(in millions)	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
Finance revenues from on-balance sheet receivables:				
Retail notes and finance leases revenue	\$ 62	\$ 92	\$ 126	\$ 172
Operating leases revenue	5	6	11	11
Wholesale notes interest	3	7	11	15
Retail and wholesale accounts interest	5	8	10	16
Other income (loss)	2	(3)	2	2
Total finance revenues from on-balance sheet receivables	77	110	160	216
Revenues from off-balance sheet securitization:				
Fair value adjustments	10	2	29	5
Excess spread income	9	6	11	11
Servicing fees revenue	2	3	4	6
Losses on sale of finance receivables	(10)	(4)	(25)	(7)
Investment revenue			2	2
Securitization Income	11	7	21	17
Gross revenue from off-balance sheet securitization	88	117	181	233
Less: Intercompany revenues	(21)	(21)	(39)	(43)
Finance revenues	\$ 67	\$ 96	\$ 142	\$ 190

Cash flows from off-balance sheet securitization transactions are as follows:

Three Months Ended April 30,	Six Months Ended April 30,
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(in millions)	2009	2008	2009	2008
Proceeds from finance receivables	<b>\$ 898</b>	\$ 1,006	<b>\$ 1,940</b>	\$ 1,817
Servicing fees	<b>2</b>	5	<b>4</b>	8
Cash from net excess spread	<b>8</b>	10	<b>10</b>	15
Investment income		3	<b>1</b>	4
Net cash from securitization transactions	<b>\$ 908</b>	\$ 1,024	<b>\$ 1,955</b>	\$ 1,844

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The components of inventories are as follows:

<b>(in millions)</b>	<b>April 30, 2009</b>	<b>As of October 31, 2008</b>
Finished products	\$ 952	\$ 998
Work in process	265	219
Raw materials	386	359
Supplies	43	52
<b>Total inventories</b>	<b>\$ 1,646</b>	<b>\$ 1,628</b>

**6. Investments in and advances to non-consolidated affiliates**

*Investments in and advances to non-consolidated affiliates* is comprised of a 49 percent interest in BDP, a 51 percent interest in BDT, and sixteen other partially-owned affiliates. We do not control these affiliates, but have the ability to exercise significant influence over their operating and financial policies. Our ownership percentages in the sixteen other affiliates range from 10 percent to 51 percent. Our investment in these affiliates is an integral part of our operations, and we account for them using the equity method of accounting. As a part of the Ford Settlement, we expect to increase our interest in our BDT and BDP joint ventures with Ford to 75%. We are currently evaluating the appropriate accounting treatment for the transaction as it relates to the expected increase ownership of BDT and BDP.

Presented below is summarized financial information for BDP, which is considered a significant unconsolidated affiliate. BDP manages sourcing, merchandising, and distribution of various replacement parts.

<b>(in millions)</b>	<b>Three Months Ended April 30,</b>		<b>Six Months Ended April 30,</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Net service revenue	\$ 52	\$ 57	\$ 101	\$ 108
Net expenses	7	7	10	16
Income before tax expense	45	50	91	92
Net income	47	50	92	91

In April 2009, we entered into an agreement with Caterpillar Inc. ( Caterpillar ) for the purposes of establishing a joint venture to develop, manufacture, and distribute commercial trucks in regions outside of North America and India. Additionally, we expect to enter into a strategic alliance involving the development, design, manufacture, and sale of Caterpillar-branded heavy duty severe service trucks in North America. Upon completion of the joint venture agreement and formation of the joint venture, we expect to initially have a 50% ownership interest in the joint venture and expect to contribute approximately \$46 million as an initial capital contribution. Furthermore, we expect to provide up to an additional \$123 million of funding over the following three years. We did not make any capital contributions as of April 30, 2009.





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The following table summarizes our debt obligations:

<b>(in millions)</b>	<b>April 30, 2009</b>	<b>As of October 31, 2008</b>
<b>Manufacturing operations:</b>		
Facilities, due 2012	<b>\$ 1,330</b>	\$ 1,330
Debt of majority-owned dealerships	<b>145</b>	157
Financing arrangements and capital lease obligations	<b>287</b>	306
7.5% Senior Notes, due 2011, net of unamortized discount of less than \$1 million at both dates	<b>15</b>	15
9.95% Senior Notes, due 2011	<b>5</b>	6
Other	<b>17</b>	20
<b>Total manufacturing operations debt</b>	<b>1,799</b>	1,834
Less: Current portion	<b>(199)</b>	(195)
<b>Net long-term manufacturing operations debt</b>	<b>\$ 1,600</b>	\$ 1,639
<b>Financial services operations:</b>		
Asset-backed debt issued by consolidated SPEs, at variable rates, due serially through 2016	<b>\$ 1,732</b>	\$ 2,076
Bank revolvers, at fixed and variable rates, due dates from 2009 through 2013	<b>1,416</b>	1,370
Revolving retail warehouse facility, at variable rates, due 2010	<b>500</b>	500
Commercial paper, at variable rates, due 2009	<b>69</b>	162
Borrowings secured by operating and finance leases, at various rates, due serially through 2016	<b>133</b>	132
<b>Total financial services operations debt</b>	<b>3,850</b>	4,240
Less: Current portion	<b>(380)</b>	(470)
<b>Net long-term financial services operations debt</b>	<b>\$ 3,470</b>	\$ 3,770

**8. Fair value measurements**

On November 1, 2008, we adopted FASB Statement No. 157, *Fair Value Measurements*, as amended by FSP No. FAS 157-3, for assets and liabilities measured at fair value on a recurring basis. FASB Statement No. 157:

defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants at the measurement date, and establishes a framework for measuring fair value,

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establishes a hierarchy of fair value measurements based upon the observability of inputs used to value assets and liabilities,

requires consideration of nonperformance risk, and

expands disclosures about the methods used to measure fair value.

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**Navistar International Corporation and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements (Continued)**

**(Unaudited)**

FASB Statement No. 157 establishes a three-level hierarchy of measurements based upon the reliability of observable and unobservable inputs used to arrive at fair value. Observable inputs are independent market data, while unobservable inputs reflect our assumptions about valuation. Depending on the inputs, we classify each fair value measurement as follows:

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

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

Level 3 based upon one or more significant unobservable inputs.

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

*Cash Equivalents and Restricted Cash Equivalents.* We classify highly liquid investments, with a maturity of 90 days or less at the date of purchase, including U.S. Treasury bills, federal agency securities, and A-1 / P-1 (or higher) rated commercial paper, as cash equivalents. We use quoted prices where available and use a matrix of observable market-based inputs when quoted prices are unavailable.

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

*Wholesale Notes.* Wholesale notes are classified as held-for-sale and are valued at the lower of amortized cost or fair value on an aggregate basis. Amortized cost approximates fair values as a result of the short-term nature and variable interest terms inherent to wholesale notes.

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

*Retained Interests.* We retain certain interests in receivables sold in off-balance sheet securitization transactions. We estimate the fair value of retained interests using internal valuation models that incorporate market inputs and our own assumptions about future cash flows. The fair value of retained interests is estimated based on the present value of monthly collections on the sold finance receivables in excess of amounts accruing to investors and other obligations arising in securitization transactions. In addition to the amount of debt and collateral held by the securitization vehicle, the three key inputs that affect the valuation of the retained interests include credit losses, payment speed, and the discount rate. We classify these assets within Level 3. For more information regarding retained interest, see Note 4, *Finance receivables*.

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The following table presents the financial instruments measured at fair value on a recurring basis as of April 30, 2009:

(in millions)	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Derivative financial instruments	\$	\$ 2	\$ 47	\$ 49
Retained interests			239	239
Total assets	\$	\$ 2	\$ 286	\$ 288
<b>Liabilities</b>				
Derivative financial instruments	\$	\$ 50	\$ 50	\$ 100
Total liabilities	\$	\$ 50	\$ 50	\$ 100

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

(in millions)	Derivative Assets and Liabilities	Retained Interests
<b>Three Months Ended April 30, 2009</b>		
Balance at February 1, 2009	\$ (1)	\$ 199
Total gains (losses) (realized/unrealized)		
Included in earnings <sup>(A)</sup>	(5)	
Purchases, issuances, and settlements	3	40
Balance at April 30, 2009	\$ (3)	\$ 239
Change in unrealized gains (losses) on assets and liabilities still held	\$ (1)	\$

(in millions)	Derivative Assets and Liabilities	Retained Interests
<b>Six Months Ended April 30, 2009</b>		
Balance at November 1, 2008	\$ 1	\$ 230
Total gains (losses) (realized/unrealized)		
Included in earnings <sup>(A)</sup>	(7)	5
Purchases, issuances, and settlements	3	4

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Balance at April 30, 2009	\$	(3)	\$	239
Change in unrealized gains (losses) on assets and liabilities still held	\$	(3)	\$	5

(A) Net gains and (losses) on derivative assets for the three months and six months ended April 30, 2009, were (\$1) million and \$1 million, respectively, and are included in *Interest expense* and *Costs of products sold*. Losses on derivative liabilities for the three months and six months ended April 30, 2009 were \$4 million and \$8 million, respectively, and are included in *Interest expense* and *Costs of products sold*. For retained interests, gains recognized in the consolidated statement of operations are included in *Finance revenues*.

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The following table presents the financial instruments measured at fair value on a nonrecurring basis as of April 30, 2009:

(in millions)	Level 2
Finance receivables <sup>(A)</sup>	\$ 31

(A) Certain impaired finance receivables are measured at fair value on a nonrecurring basis. An impairment charge is recorded for the amount by which the carrying value of the receivables exceeds the fair value of the underlying collateral, net of remarketing costs. As of April 30, 2009, impaired receivables with a carrying amount of \$59 million had specific loss reserves of \$28 million and a fair value of \$31 million. Fair values of the underlying collateral are determined by reference to dealer vehicle value publications adjusted for certain market factors.

**9. Postretirement benefits****Defined Benefit Plans**

We provide postretirement benefits to a substantial portion of our employees. Costs associated with postretirement benefits include pension and postretirement health care expenses for employees, retirees, and surviving spouses and dependents. Generally, our pension plans are non-contributory. Our policy is to fund the pension plans in accordance with applicable U.S. and Canadian government regulations and to make additional contributions from time to time. For the three months and six months ended April 30, 2009, we contributed \$9 million and \$19 million, respectively, to our pension plans to meet regulatory minimum funding requirements. For the three months and six months ended April 30, 2008, we contributed \$14 million and \$21 million, respectively, to our pension plans to meet regulatory minimum funding requirements. We currently anticipate additional contributions of approximately \$18 million during the remainder of 2009.

Other post-employment benefit ( OPEB ) obligations, such as retiree medical, are generally funded in accordance with a 1993 restructured health and life legal settlement, which requires us to fund a portion of the plans' annual service cost. For the three months and six months ended April 30, 2009, we contributed \$1 million and \$2 million, respectively, to our OPEB plans to meet legal funding requirements. For the three months and six months ended April 30, 2008, we contributed \$1 million and \$2 million, respectively, to our OPEB plans to meet legal funding requirements. We currently anticipate additional contributions of approximately \$1 million during the remainder of 2009.

As discussed in Note 2, *Ford settlement and related charges*, the Company committed to close IEP and ICC. Our commitment to close the plants resulted in a charge of \$16 million during the first quarter of 2009 representing a plan curtailment and related contractual termination benefits. The plan curtailment also resulted in a plan remeasurement at January 31, 2009 increasing the Projected Benefit Obligation ( PBO ) by \$241 million. The discount rate used to measure the PBO was 6.5% at January 31, 2009 compared to 8.4% at October 31, 2008. All other significant assumptions remained unchanged from the October 31, 2008 measurement date. Actuarial losses for the three months ended January 31, 2009 of \$321 million, which were primarily due to the change in the discount rate and negative asset returns, were recognized as a charge to equity as a component of *Accumulated other comprehensive loss*.

In addition to the plan curtailment and related contractual termination benefits resulting from the Ford Settlement, the Company recognized an additional \$2 million of contractual termination benefits in the first quarter of 2009 related to the terminations of certain salaried employees in December 2008.

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On December 16, 2007, the majority of Company employees represented by the United Automobile, Aerospace and Agriculture Implement Workers of America ( UAW ) voted to ratify a new contract that will run through September 30, 2010. Among the changes from the prior contract was the cessation of annual lump sum payments that had been made to certain retirees. Prior to December 16, 2007, we accounted for these payments as a defined benefit plan based on the historical substance of the underlying arrangement. The elimination of these payments and other changes resulted in a net settlement and curtailment of the plan resulting in income of \$42 million, which is presented as a reduction of *Selling, general and administrative expenses* for the six months ended April 30, 2008.

**Components of Net Postretirement Benefits Expense (Income)**

Net postretirement benefits expense (income) included in our consolidated statements of operations is composed of the following:

	Three Months Ended April 30,				Six Months Ended April 30,			
	Pension Benefits		Health and Life Insurance Benefits		Pension Benefits		Health and Life Insurance Benefits	
(in millions)	2009	2008	2009	2008	2009	2008	2009	2008
Service cost for benefits earned during the period	\$ 4	\$ 6	\$ 1	\$ 3	\$ 8	\$ 12	\$ 3	\$ 6
Interest on obligation	57	56	29	28	117	112	58	57
Amortization of net cumulative losses	19	3			34	7	(1)	
Amortization of prior service cost (benefit)		1	(1)	(1)		1	(2)	(2)
Settlements and curtailments					6	(42)		(1)
Contractual termination benefits					9		3	
Premiums on pension insurance	1	1			1	1		
Less: Expected return on assets	(46)	(81)	(10)	(17)	(94)	(162)		