CSX CORP
Form 10-Q
October 17, 2018
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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 September 30, 2018
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
1-8022
CSX CORPORATION
(Exact name of registrant as specified in its charter)

Virginia		62-1051971
(State or other jurisdiction of incorporation or organization)		(I.R.S. Employer Identification No.)
500 Water Street, 15th Floor, Jacksonville, FL	32202	(904) 359-3200
(Address of principal executive offices)	(Zip Code)	(Telephone number, including area code)

No Change
(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes (X) No ( )
Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).
Yes (X) No ( )
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer", "accelerated filer” and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (check one)
Large Accelerated Filer (X) Accelerated Filer ( ) Non-accelerated Filer ( ) Smaller Reporting Company ( )
Emerging growth company ( )

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ( )

Indicate by a check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes ( ) No (X)
There were 844,420,361 shares of common stock outstanding on September 30, 2018 (the latest practicable date that is closest to the filing date).

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CSX CORPORATION

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS
CONSOLIDATED INCOME STATEMENTS (Unaudited)
(Dollars in millions, except per share amounts)

	Third Quarters		Nine Months	
	2018	2017	2018	2017
Revenue	$3,129	$2,743	$9,107	$8,545
Expense				
Labor and Fringe	695	725	2,060	2,271
Materials, Supplies and Other	474	523	1,425	1,590
Depreciation	334	331	986	978
Fuel	268	205	793	621
Equipment and Other Rents	89	109	302	313
Restructuring Charge (Note 1)	—	1	—	226
Equity Earnings of Affiliates	(24)	(19)	(79)	(48)
Total Expense	1,836	1,875	5,487	5,951
Operating Income	1,293	868	3,620	2,594
Interest Expense	(162)	(132)	(468)	(406)
Restructuring Charge - Non-Operating (Note 1)	—	—	—	(70)
Other Income - Net	19	14	54	41
Earnings Before Income Taxes	1,150	750	3,206	2,159
Income Tax Expense	(256)	(291)	(740)	(828)
Net Earnings	$894	$459	$2,466	$1,331
Per Common Share (Note 2)				
Net Earnings Per Share, Basic	$1.05	$0.51	$2.85	$1.45
Net Earnings Per Share, Assuming Dilution	$1.05	$0.51	$2.83	$1.45
Average Shares Outstanding (In millions)	850	902	866	916
Average Shares Outstanding, Assuming Dilution (In millions)	854	906	870	919
Cash Dividends Paid Per Common Share	$0.22	$0.20	$0.66	$0.58

CONDENSED CONSOLIDATED COMPREHENSIVE INCOME STATEMENTS (Unaudited)
(Dollars in millions, except per share amounts)

	Third Quarters		Nine Months	
	2018	2017	2018	2017
Total Comprehensive Earnings (Note 10)	$901	$467	$2,378	$1,410

Certain prior year data has been reclassified to conform to the current presentation.
See accompanying notes to consolidated financial statements.

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ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS
(Dollars in millions)

	(Unaudited) September 30, 2018	December 31, 2017
ASSETS		
Current Assets:		
Cash and Cash Equivalents	$ 663	$ 401
Short-term Investments	615	18
Accounts Receivable - Net (Note 11)	1,090	970
Materials and Supplies	283	372
Other Current Assets	133	154
Total Current Assets	2,784	1,915
Properties	44,485	44,324
Accumulated Depreciation	(12,614)	(12,560)
Properties - Net	31,871	31,764
Investment in Conrail	941	907
Affiliates and Other Companies	823	779
Other Long-term Assets	442	374
Total Assets	$ 36,861	$ 35,739
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts Payable	$ 982	$ 847
Labor and Fringe Benefits Payable	517	602
Casualty, Environmental and Other Reserves (Note 4)	110	108
Current Maturities of Long-term Debt (Note 7)	18	19
Income and Other Taxes Payable	166	157
Other Current Liabilities	151	161
Total Current Liabilities	1,944	1,894
Casualty, Environmental and Other Reserves (Note 4)	231	266
Long-term Debt (Note 7)	13,754	11,790
Deferred Income Taxes - Net	6,584	6,418
Other Long-term Liabilities	613	650
Total Liabilities	23,126	21,018
Shareholders' Equity:		
Common Stock, $1 Par Value	844	890
Other Capital	129	217
Retained Earnings	13,320	14,084
Accumulated Other Comprehensive Loss (Note 10)	(574)	(486)
Noncontrolling Interest	16	16
Total Shareholders' Equity	13,735	14,721
Total Liabilities and Shareholders' Equity	$ 36,861	$ 35,739

See accompanying notes to consolidated financial statements.

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ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED CASH FLOW STATEMENTS (Unaudited)
(Dollars in millions)

	Nine Months	
	2018	2017
OPERATING ACTIVITIES		
Net Earnings	$2,466	$1,331
Adjustments to Reconcile Net Earnings to Net Cash Provided by Operating Activities:		
Depreciation	986	978
Deferred Income Taxes	148	161
Gain on Property Dispositions	(122)	(5)
Equity Earnings of Affiliates	(79)	(48)
Restructuring Charge	—	296
Cash Payments for Restructuring Charge	(14)	(147)
Other Operating Activities	(13)	40
Changes in Operating Assets and Liabilities:		
Accounts Receivable	(97)	(78)
Other Current Assets	70	47
Accounts Payable	140	102
Income and Other Taxes Payable	19	180
Other Current Liabilities	(98)	4
Net Cash Provided by Operating Activities	3,406	2,861
INVESTING ACTIVITIES		
Property Additions	(1,240)	(1,462)
Proceeds from Property Dispositions	257	38
Purchase of Short-term Investments	(611)	(645)
Proceeds from Sales of Short-term Investments	15	957
Other Investing Activities	(8)	33
Net Cash Used In Investing Activities	(1,587)	(1,079)
FINANCING ACTIVITIES		
Long-term Debt Issued (Note 7)	2,000	850
Long-term Debt Repaid (Note 7)	(19)	(332)
Dividends Paid	(570)	(530)
Shares Repurchased	(2,816)	(1,763)
Accelerated Share Repurchase Pending Final Settlement (Note 2)	(100)	—
Other Financing Activities	(52)	(19)
Net Cash Used in Financing Activities	(1,557)	(1,794)
Net Increase (Decrease) in Cash and Cash Equivalents	262	(12)
CASH AND CASH EQUIVALENTS		
Cash and Cash Equivalents at Beginning of Period	401	603
Cash and Cash Equivalents at End of Period	$663	$591

Certain prior year data has been reclassified to conform to the current presentation.

See accompanying notes to consolidated financial statements.

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CSX CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1.Nature of Operations and Significant Accounting Policies

Background
CSX Corporation ("CSX"), together with its subsidiaries (the "Company"), based in Jacksonville, Florida, is one of the nation's leading transportation companies. The Company provides rail-based transportation services including traditional rail service and the transport of intermodal containers and trailers.

CSX's principal operating subsidiary, CSX Transportation, Inc. ("CSXT"), provides an important link to the transportation supply chain through its approximately 21,000 route mile rail network, which serves major population centers in 23 states east of the Mississippi River, the District of Columbia and the Canadian provinces of Ontario and Quebec. The Company's intermodal business links customers to railroads via trucks and terminals.

After a merger on July 1, 2017 with CSX Real Property, Inc., a former wholly-owned CSX subsidiary, CSXT is now responsible for the Company's real estate sales, leasing, acquisition and management and development activities. In addition, as substantially all real estate sales, leasing, acquisition and management and development activities are focused on supporting railroad operations, all results of these activities are included in operating income beginning in 2017. Previously, the results of these activities were classified as operating or non-operating based on the nature of the activity and were not material for any periods presented.

Other entities
In addition to CSXT, the Company's subsidiaries include CSX Intermodal Terminals, Inc. ("CSX Intermodal Terminals"), Total Distribution Services, Inc. ("TDSI"), Transflo Terminal Services, Inc. ("Transflo"), CSX Technology, Inc. ("CSX Technology") and other subsidiaries. CSX Intermodal Terminals owns and operates a system of intermodal terminals, predominantly in the eastern United States and also performs drayage services (the pickup and delivery of intermodal shipments) for certain customers and trucking dispatch operations. TDSI serves the automotive industry with distribution centers and storage locations. Transflo connects non-rail served customers to the many benefits of rail by transferring products from rail to trucks. The biggest Transflo markets are chemicals and agriculture, which include shipments of plastics and ethanol. CSX Technology and other subsidiaries provide support services for the Company.

Basis of Presentation
In the opinion of management, the accompanying consolidated financial statements contain all normal, recurring adjustments necessary to fairly present the following:

- Consolidated income statements for the quarter and nine months ended September 30, 2018 and September 30, 2017;
- Condensed consolidated comprehensive income statements for the quarter and nine months ended September 30, 2018 and September 30, 2017;
- Consolidated balance sheets at September 30, 2018 and December 31, 2017; and
- Consolidated cash flow statements for the nine months ended September 30, 2018 and September 30, 2017.

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(Unaudited)

NOTE 1. Nature of Operations and Significant Accounting Policies, continued

Pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"), certain information and disclosures normally included in the notes to the annual financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") have been omitted from these interim financial statements. CSX suggests that these financial statements be read in conjunction with the audited financial statements and the notes included in CSX's most recent annual report on Form 10-K and any subsequently filed current reports on Form 8-K.

Fiscal Year
Through the second quarter 2017, CSX followed a 52/53 week fiscal reporting calendar with the last day of each reporting period ending on a Friday. On July 7, 2017 the Board of Directors of CSX approved a change in the fiscal reporting calendar from a 52/53 week year ending on the last Friday of December to a calendar year ending on December 31 each year, effective beginning with fiscal third quarter 2017. Related to the change in the fiscal calendar:

- Fiscal year 2018 (January 1, 2018 through December 31, 2018) will contain 365 days, and fiscal year 2017 (December 31, 2016 through December 31, 2017) contained 366 days.
- Fiscal first quarter 2018 (January 1, 2018 through March 31, 2018) contained 90 days, and fiscal first quarter 2017 (December 31, 2016 through March 31, 2017) contained 91 days.
- Fiscal second quarter 2018 (April 1, 2018 through June 30, 2018) contained 91 days, and fiscal second quarter 2017 (April 1, 2017 through June 30, 2017) contained 91 days.
- Fiscal third quarter 2018 (July 1, 2018 through September 30, 2018) contained 92 days, and fiscal third quarter 2017 (July 1, 2017 through September 30, 2017) contained 92 days.

This change did not materially impact the comparability of the Company's financial results. Accordingly, the change to a calendar fiscal year was made on a prospective basis and operating results for prior periods were not adjusted. The Company was not required to file a transition report because this change was not deemed a change in fiscal year for purposes of reporting subject to Rule 13a-10 or Rule 15d-10 of the Securities Exchange Act of 1934 as the new fiscal year commenced with the end of the prior fiscal year end and within seven days of the prior fiscal year end.

Except as otherwise specified, references to "third quarter(s)" or "nine months" indicate CSX's fiscal periods ending September 30, 2018 and September 30, 2017, and references to "year-end" indicate the fiscal year ended December 31, 2017.

New Accounting Pronouncements
Pronouncements adopted in 2018
In February 2018, the Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which permits entities to reclassify tax effects stranded in accumulated other comprehensive income as a result of tax reform to retained earnings. Companies that elect to reclassify these amounts must reclassify stranded tax effects for all items accounted for in accumulated other comprehensive income. The Company adopted this standard update in first quarter 2018 and applied it prospectively. Adoption resulted in the reclassification of $107 million in tax effects related to employee benefit plans from accumulated other comprehensive loss, increasing retained earnings by the same amount.

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NOTE 1. Nature of Operations and Significant Accounting Policies, continued

In March 2017, the FASB issued ASU Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, which requires that only the service cost component of net periodic benefit costs be recorded as compensation cost in operating expense on the consolidated income statement. All other components of net periodic benefit cost (interest cost, expected return on plan assets, amortization of net loss, special termination benefits and settlement and curtailment effects) should be presented as non-operating charges on the consolidated income statement. If these non-operating charges are related to prior year restructuring activities, they are presented as restructuring charge - non-operating. Other non-operating charges are presented as other income - net. The Company adopted the provisions of this standard during first quarter 2018 and applied them retrospectively. The retrospective impact of adoption for third quarter and nine months 2017 is shown in the following table.

	Third Quarter 2017			Nine Months 2017		
(Dollars in millions)	As Previously Reported	Reclass	As Reclassified	As Previously Reported	Reclass	As Reclassified
Operating Expense:						
Labor and Fringe	$717	$ 8	$ 725	$2,249	$ 22	$ 2,271
Restructuring Charge	1	—	1	296	(70)	226
Non-Operating Income (Expense):						
Restructuring Charge - Non-Operating	$—	$ —	$ —	$—	$ (70)	$ (70)
Other Income - Net	6	8	14	19	22	41

In May 2014, the FASB issued ASU Revenue from Contracts with Customers, which supersedes previous revenue recognition guidance. The new standard requires that a company recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration the company expects to receive in exchange for those goods or services. In-depth reviews of commercial contracts were completed and changes to processes and internal controls to meet the standard's reporting and disclosure requirements were implemented. The Company adopted the guidance effective January 1, 2018 using the modified retrospective approach. The adoption did not affect the Company's financial condition, results of operations or liquidity. Disclosures related to the nature, amount and timing of revenue and cash flows arising from contracts with customers are included in Note 11, Revenues.

Pronouncements to be adopted
In February 2016, the FASB issued ASU, Leases, which will require lessees to recognize most leases on their balance sheets as a right-of-use asset with a corresponding lease liability, and lessors to recognize a net lease investment. Additional qualitative and quantitative disclosures will also be required. This standard update is effective for CSX beginning with the first quarter 2019 and the Company plans to adopt it using the cumulative-effect adjustment transition method approved by the FASB in July 2018. Changes to processes and internal controls to meet the standard's reporting and disclosure requirements have been identified and are being implemented. Software has been implemented that will assist in the recognition of additional assets and liabilities to be included on the balance sheet related to leases currently classified as operating leases with durations greater than twelve months, with certain allowable exceptions. In addition to lease agreements, service contracts and other agreements are also being reviewed to determine if they contain an embedded lease. The Company continues to evaluate the expected impact of this standard update on disclosures, but does not anticipate any material changes to operating results or liquidity as a result of right-of-use assets and corresponding lease liabilities that will be recorded.

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NOTE 1. Nature of Operations and Significant Accounting Policies, continued

In January 2018, the FASB issued ASU Leases - Land Easement Practical Expedient, which permits entities to forgo the evaluation of existing land easement arrangements to determine if they contain a lease as part of the adoption of the Leases ASU issued in February 2016. Accordingly, the Company's accounting treatment of existing land easements will not change. CSX will adopt this standard update concurrently with the Leases ASU issued in February 2016. New land easement arrangements, or modifications to existing arrangements, after the adoption of the standard update will still be evaluated to determine if they meet the definition of a lease.

In March 2017, the FASB issued ASU Simplifying the Test for Goodwill Impairment, which eliminates step two, the calculation of the implied fair value of goodwill, from the goodwill impairment test. Impairment will be quantified in step one of the test as the amount by which the carrying amount exceeds the fair value. This standard update is effective beginning first quarter 2020 and must be applied prospectively. The Company does not believe this standard update will have a material effect on its financial condition, results of operations or liquidity.

Restructuring Charge
The prior year restructuring charge includes costs related to the management workforce reduction program completed in 2017, reimbursement arrangements with MR Argent Advisor LLC ("Mantle Ridge") and the Company's former President and Chief Executive Officer, E. Hunter Harrison, the proration of equity awards and other advisory costs related to the leadership transition. Payments related to the 2017 restructuring charge were substantially complete as of March 31, 2018. For further details on the charge, see the Company's most recent annual report on Form 10-K.

During third quarter 2017, restructuring charge of $1 million was incurred for advisory fees related to shareholder matters. Expenses related to the management workforce reduction and other costs during the nine months 2017 are shown in the following table.

	Nine Months 2017		
(Dollars in millions)	As Previously Reported	Operating Restructuring Charge	Non-Operating Restructuring Charge
Severance and Pension	$144	$ 91	$ 53
Other Post-Retirement Benefits Curtailment	17	—	17
Employee Equity Awards Proration and Other	16	16	—
Subtotal Management Workforce Reduction	$177	$ 107	$ 70
Reimbursement Arrangements	84	84	—
Executive Equity Awards Proration	24	24	—
Advisory Fees Related to Shareholder Matters	11	11	—
Total Restructuring Charge	$296	$ 226	$ 70

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NOTE 2. Earnings Per Share

The following table sets forth the computation of basic earnings per share and earnings per share, assuming dilution:

	Third Quarters		Nine Months	
	2018	2017	2018	2017
Numerator (Dollars in millions):				
Net Earnings	$894	$459	$2,466	$1,331
Dividend Equivalents on Restricted Stock	—	—	—	(1)
Net Earnings, Attributable to Common Shareholders	$894	$459	$2,466	$1,330
Denominator (Units in millions):				
Average Common Shares Outstanding	850	902	866	916
Other Potentially Dilutive Common Shares	4	4	4	3
Average Common Shares Outstanding, Assuming Dilution	854	906	870	919
Net Earnings Per Share, Basic	$1.05	$0.51	$2.85	$1.45
Net Earnings Per Share, Assuming Dilution	$1.05	$0.51	$2.83	$1.45

Basic earnings per share is based on the weighted-average number of shares of common stock outstanding. Earnings per share, assuming dilution, is based on the weighted-average number of shares of common stock equivalents outstanding adjusted for the effects of common stock that may be issued as a result of potentially dilutive instruments. CSX's potentially dilutive instruments are made up of equity awards, which include long-term incentive awards and employee stock options.

The Earnings Per Share Topic in the FASB's ASC requires CSX to include additional shares in the computation of earnings per share, assuming dilution. The additional shares included in diluted earnings per share represent the number of shares that would be issued if all of the above potentially dilutive instruments were converted into CSX common stock.

When calculating diluted earnings per share, this rule requires CSX to include the potential shares that would be outstanding if all outstanding stock options were exercised. This number is different from outstanding stock options because it is offset by shares CSX could repurchase using the proceeds from these hypothetical exercises to obtain the common stock equivalent. Approximately seven thousand and 10 million of total average outstanding stock options for the third quarters ended September 30, 2018 and September 30, 2017, respectively, were excluded from the diluted earnings per share calculation because their effect was antidilutive.

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NOTE 2. Earnings Per Share, continued

Share Repurchases
In February 2018, the Company announced an increase to the $1.5 billion share repurchase program first announced in October 2017, bringing the total authorized to $5 billion. This program is expected to be completed by the end of first quarter 2019. During the third quarters of 2018 and 2017, the Company repurchased approximately $1.0 billion, or 15 million shares, and $1.0 billion, or 20 million shares, respectively. During the nine months of 2018 and 2017, the Company repurchased $2.8 billion, or 46 million shares, and $1.8 billion, or 35 million shares, respectively.

On July 19, 2018, the Company entered into an accelerated share repurchase agreement to repurchase shares of the Company’s common stock. Under this agreement, the Company made a prepayment of $500 million to a financial institution and received an initial delivery of 6 million shares valued at $400 million. The remaining balance of $100 million was settled through receipt of additional shares on October 11, 2018, with the final net number of shares calculated based on the volume-weighted average price of the Company's common stock over the term of the agreement, less a discount. Approximately 7 million total shares were repurchased under the agreement.

Under an accelerated share repurchase agreement executed in April 2018, the Company made a prepayment of $450 million to a financial institution and received an initial delivery of 6 million shares valued at $360 million. The remaining balance of $90 million was settled through receipt of additional shares in July 2018, with the final net number of shares calculated based on the volume-weighted average price of the Company's common stock over the term of the agreement, less a discount. Approximately 7 million total shares were repurchased under the agreement.

Under an accelerated share repurchase agreement executed in January 2018, the Company made a prepayment of $150 million to a financial institution and received an initial delivery of shares valued at $120 million. The remaining balance of $30 million was settled through receipt of additional shares in February 2018 with the final net number of shares calculated based on the volume-weighted average price of the Company's common stock over the term of the agreement, less a discount. Approximately 3 million total shares were repurchased under the agreement.

Management's assessment of market conditions and other factors guides the timing and volume of repurchases. Future share repurchases are expected to be funded by cash on hand, cash generated from operations and debt issuances. Shares are retired immediately upon repurchase. In accordance with the Equity Topic in the ASC, the excess of repurchase price over par value is recorded in retained earnings.

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(Unaudited)

NOTE 3. Share-Based Compensation

Under CSX's share-based compensation plans, awards consist of performance units, restricted stock awards, restricted stock units and stock options for management and stock grants for directors. Awards granted under the various programs are determined and approved by the Compensation Committee of the Board of Directors or, in certain circumstances, by the Chief Executive Officer for awards to management employees other than senior executives. The Board of Directors approves awards granted to CSX's non-management directors upon recommendation of the Governance Committee.

In May 2018, shareholders approved the 2018 CSX Employee Stock Purchase Plan ("ESPP") for the benefit of Company employees. The Company registered 4 million shares of common stock that may be issued pursuant to this plan. Under the ESPP, employees may contribute between 1% and 10% of base compensation, after-tax, to purchase up to $25,000 of CSX common stock per year. No shares will be issued under the ESPP until first quarter 2019.

Share-based compensation expense is measured using the fair value of the award on the grant date and is recognized on a straight-line basis over the service period of the respective award. Total pre-tax expense associated with share-based compensation and its related income tax benefit is shown in the table below. The year over year decrease in third quarter share-based compensation expense is primarily due to the prior year expense related to 9 million stock options granted in February 2017 to former President and CEO E. Hunter Harrison, which were forfeited upon his death in December 2017. Additionally, the decrease in nine months expense was also due to modifications to the terms of awards in the first and second quarters of 2017 (see Equity Award Modifications below).

	Third Quarters		Nine Months	
(Dollars in millions)	2018	2017	2018	2017
Share-Based Compensation Expense:				
Performance Units	$8	$3	$22	$41
Stock Options	4	14	10	47
Restricted Stock Units and Awards	1	2	4	11
Stock Awards for Directors	—	—	2	2
Total Share-Based Compensation Expense	$13	$19	$38	$101
Income Tax Benefit	$6	$12	$23	$41

Long-term Incentive Plan
In February 2018, the Company granted approximately 350 thousand performance units to certain employees under a new long-term incentive plan ("LTIP") for the years 2018 through 2020, which was adopted under the CSX Stock and Incentive Award Plan. During third quarter 2018, there were immaterial grants of performance units to certain members of management. No performance units were granted during third quarter 2017.

Payouts of performance units for the cycle ending with fiscal year 2020 will be based on the achievement of goals related to both operating ratio and free cash flow, in each case excluding non-recurring items as disclosed in the Company's financial statements. The final year operating ratio and cumulative free cash flow over the plan period will each comprise 50% of the payout and will be measured independently of the other.

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NOTE 3. Share-Based Compensation, continued

Grants were made in performance units, with each unit representing the right to receive one share of CSX common stock, and payouts will be made in CSX common stock. The payout range for participants will be between 0% and 200% of the target awards depending on Company performance against predetermined goals. Payouts for certain executive officers are subject to upward or downward adjustment by up to 25%, capped at an overall payout of 200%, based upon the Company's total shareholder return relative to specified comparable groups over the performance period. The fair value of the performance units awarded during the quarter and nine months ended September 30, 2018 was calculated using a Monte-Carlo simulation model with the following weighted-average assumptions:

	Third Quarter 2018	Nine Months 2018
Weighted-average assumptions used:		
Annual dividend yield	1.2 %	1.6 %
Risk-free interest rate	2.7 %	2.3 %
Annualized volatility	27.9 %	29.1 %
Expected life (in years)	2.3	2.9

Stock Options

Also, in February 2018, the Company granted approximately 950 thousand stock options along with the corresponding LTIP. The fair value of stock options on the date of grant was $14.55 per option which was calculated using the Black-Scholes valuation model. Stock options have been granted with ten-year terms and vest three years after the date of grant. The exercise price for stock options granted equals the closing market price of the underlying stock on the date of grant. These awards are time-based and are not based upon attainment of performance goals. During third quarter 2018, there were immaterial grants of stock options to certain members of management. No stock options awards were granted during third quarter 2017.

The fair values of all stock option awards during the quarter and nine months ended September 30, 2018 and September 30, 2017 were estimated at the grant date with the following weighted average assumptions:

	Third Quarters		Nine Months	
	2018	2017	2018	2017
Weighted-average grant date fair value	$20.52	$ —	$14.65	$12.83
Stock options valuation assumptions:				
Annual dividend yield	1.2 %	—%	1.5 %	1.5 %
Risk-free interest rate	2.8 %	—%	2.6 %	2.2 %
Annualized volatility	25.5 %	—%	27.0 %	27.1 %
Expected life (in years)	6.5	—	6.5	6.3
Other pricing model inputs:				
Weighted-average grant-date market price of CSX stock (strike price)	$74.84	$ —	$54.19	$49.60

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(Unaudited)

NOTE 3. Share-Based Compensation, continued

Restricted Stock Units
Finally, in February 2018, the Company granted approximately 85 thousand restricted stock units along with the corresponding LTIP. The restricted stock units vest three years after the date of grant. Participants receive cash dividend equivalents on the unvested shares during the restriction period. These awards are time-based and are not based upon attainment of performance goals. For information related to the Company's other outstanding long-term incentive compensation, see CSX's most recent annual report on Form 10-K. During third quarter 2018, there were immaterial grants of restricted stock units to certain members of management. No restricted stock units were granted during third quarter 2017.

Equity Award Modifications
In 2017, as part of an enhanced severance benefit under the management streamlining and realignment initiative discussed in Note 1, unvested performance units, restricted stock units and stock options for separated employees not eligible for retirement were permitted to vest on a pro-rata basis. Additionally, the terms of unvested equity awards for the former Chief Executive Officer, Michael J. Ward, and former President, Clarence W. Gooden, were modified prior to their retirements on March 6, 2017 to permit prorated vesting through May 31, 2018. These award modifications impacted approximately 70 employees and resulted in an increase to share-based compensation expense for revaluation of the affected awards of $31 million for the nine months ended September 30, 2017. The expense associated with these award modifications was included in the 2017 restructuring charge. No significant award modifications took place in 2018 or in third quarter 2017.

NOTE 4. Casualty, Environmental and Other Reserves

Personal injury and environmental reserves are considered critical accounting estimates due to the need for significant management judgment. Casualty, environmental and other reserves are provided for in the consolidated balance sheets as shown in the table below.

	September 30, 2018			December 31, 2017		
(Dollars in millions)	Current	Long-term	Total	Current	Long-term	Total
Casualty:						
Personal Injury	$42	$ 108	$150	$43	$ 125	$168
Occupational	7	47	54	6	54	60
Total Casualty	49	155	204	49	179	228
Environmental	37	52	89	31	59	90
Other	24	24	48	28	28	56
Total	$110	$ 231	$341	$108	$ 266	$374

These liabilities are accrued when reasonably estimable and probable in accordance with the Contingencies Topic in the ASC. Actual settlements and claims received could differ, and final outcomes of these matters cannot be predicted with certainty. Considering the legal defenses currently available, the liabilities that have been recorded and other factors, it is the opinion of management that none of these items individually, when finally resolved, will have a material adverse effect on the Company's financial condition, results of operations or liquidity. Should a number of these items occur in the same period, however, their combined effect could be material in that particular period.

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NOTE 4. Casualty, Environmental and Other Reserves, continued

Casualty
Casualty reserves of $204 million and $228 million as of September 30, 2018 and December 31, 2017, respectively, represent accruals for personal injury, occupational disease and occupational injury claims. During second quarter 2018, the Company increased its self-insured retention amount for these claims from $50 million to $75 million per occurrence for claims occurring on or after June 1, 2018. Currently, no individual claim is expected to exceed the self-insured retention amount. In accordance with the Contingencies Topic in the ASC, to the extent the value of an individual claim exceeds the self-insured retention amount, the Company would present the liability on a gross basis with a corresponding receivable for insurance recoveries. These reserves fluctuate based upon the timing of payments as well as changes in estimate. Actual results may vary from estimates due to the number, type and severity of the injury, costs of medical treatments and uncertainties in litigation. Most of the Company's casualty claims relate to CSXT unless otherwise noted below. Defense and processing costs, which historically have been insignificant and are anticipated to be insignificant in the future, are not included in the recorded liabilities.

Personal Injury
Personal injury reserves represent liabilities for employee work-related and third-party injuries. Work-related injuries for CSXT employees are primarily subject to the Federal Employers' Liability Act ("FELA"). CSXT retains an independent actuary to assist management in assessing the value of personal injury claims. An analysis is performed by the actuary quarterly and is reviewed by management. This analysis for the quarter resulted in an immaterial adjustment to the personal injury reserve. The methodology used by the actuary includes a development factor to reflect growth or reduction in the value of these personal injury claims based largely on CSXT's historical claims and settlement experience.

Occupational
Occupational reserves represent liabilities for occupational disease and injury claims. Occupational disease claims arise primarily from allegations of exposure to asbestos in the workplace. Occupational injury claims arise from allegations of exposure to certain other materials in the workplace, such as solvents, soaps, chemicals (collectively referred to as "irritants") and diesel fuels (like exhaust fumes) or allegations of chronic physical injuries resulting from work conditions, such as repetitive stress injuries.

Environmental
Environmental reserves were $89 million and $90 million as of September 30, 2018 and December 31, 2017, respectively. The Company is a party to various proceedings related to environmental issues, including administrative and judicial proceedings involving private parties and regulatory agencies. The Company has been identified as a potentially responsible party at approximately 216 environmentally impaired sites. Many of these are, or may be, subject to remedial action under the federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("CERCLA"), also known as the Superfund Law, or similar state statutes. Most of these proceedings arose from environmental conditions on properties used for ongoing or discontinued railroad operations. A number of these proceedings, however, are based on allegations that the Company, or its predecessors, sent hazardous substances to facilities owned or operated by others for treatment, recycling or disposal. In addition, some of the Company's land holdings were leased to others for commercial or industrial uses that may have resulted in releases of hazardous substances or other regulated materials onto the property and could give rise to proceedings against the Company.

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NOTE 4. Casualty, Environmental and Other Reserves, continued

In any such proceedings, the Company is subject to environmental clean-up and enforcement actions under the Superfund Law, as well as similar state laws that may impose joint and several liability for clean-up and enforcement costs on current and former owners and operators of a site without regard to fault or the legality of the original conduct. These costs could be substantial.

In accordance with the Asset Retirement and Environmental Obligations Topic in the ASC, the Company reviews its role with respect to each site identified at least quarterly, giving consideration to a number of factors such as:

- type of clean-up required;
- nature of the Company's alleged connection to the location (e.g., generator of waste sent to the site or owner or operator of the site);
- extent of the Company's alleged connection (e.g., volume of waste sent to the location and other relevant factors); and
- number, connection and financial viability of other named and unnamed potentially responsible parties at the location.

Based on the review process, the Company has recorded amounts to cover contingent anticipated future environmental remediation costs with respect to each site to the extent such costs are reasonably estimable and probable. The recorded liabilities for estimated future environmental costs are undiscounted. The liability includes future costs for remediation and restoration of sites as well as any significant ongoing monitoring costs, but excludes any anticipated insurance recoveries. Payments related to these liabilities are expected to be made over the next several years. Environmental remediation costs are included in materials, supplies and other on the consolidated income statements.

Currently, the Company does not possess sufficient information to reasonably estimate the amounts of additional liabilities, if any, on some sites until completion of future environmental studies. In addition, conditions that are currently unknown could, at any given location, result in additional exposure, the amount and materiality of which cannot presently be reasonably estimated. Based upon information currently available, however, the Company believes its environmental reserves accurately reflect the estimated cost of remedial actions currently required.

Other
Other reserves of $48 million and $56 million as of September 30, 2018 and December 31, 2017, respectively, include liabilities for various claims, such as property, automobile and general liability. Also included in other reserves are longshoremen disability claims related to a previously owned international shipping business (these claims are in runoff) as well as claims for current port employees.

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NOTE 5. Commitments and Contingencies

Insurance
The Company maintains numerous insurance programs with substantial limits for property damage (which includes business interruption) and third-party liability. A certain amount of risk is retained by the Company on each of the property and liability programs. The Company has a $50 million per occurrence retention for floods and named windstorms and a $25 million per occurrence retention for property losses other than floods and named windstorms. For claims occurring on or after June 1, 2018, the Company increased its self-insured retention for third-party liability claims from $50 million to $75 million per occurrence. While the Company believes its insurance coverage is adequate, future claims could exceed existing insurance coverage or insurance may not continue to be available at commercially reasonable rates.

Legal
The Company is involved in litigation incidental to its business and is a party to a number of legal actions and claims, various governmental proceedings and private civil lawsuits, including, but not limited to, those related to fuel surcharge practices, tax matters, environmental and hazardous material exposure matters, FELA and labor claims by current or former employees, other personal injury or property claims and disputes and complaints involving certain transportation rates and charges. Some of the legal proceedings include claims for compensatory as well as punitive damages and others are, or are purported to be, class actions. While the final outcome of these matters cannot be reasonably determined, considering, among other things, the legal defenses available and liabilities that have been recorded along with applicable insurance, it is currently the opinion of management that none of these pending items is likely to have a material adverse effect on the Company's financial condition, results of operations or liquidity. An unexpected adverse resolution of one or more of these items, however, could have a material adverse effect on the Company's financial condition, results of operations or liquidity in that particular period.
The Company is able to estimate a range of possible loss for certain legal proceedings for which a loss is reasonably possible in excess of reserves established. The Company has estimated this range to be $2 million to $118 million in aggregate at September 30, 2018. This estimated aggregate range is based upon currently available information and is subject to significant judgment and a variety of assumptions. Accordingly, the Company's estimate will change from time to time, and actual losses may vary significantly from the current estimate.

Fuel Surcharge Antitrust Litigation
In May 2007, class action lawsuits were filed against CSXT and three other U.S.-based Class I railroads alleging that the defendants' fuel surcharge practices relating to contract and unregulated traffic resulted from an illegal conspiracy in violation of antitrust laws. In November 2007, the class action lawsuits were consolidated in federal court in the District of Columbia, where they are now pending. The suit seeks treble damages allegedly sustained by purported class members as well as attorneys' fees and other relief. Plaintiffs are expected to allege damages at least equal to the fuel surcharges at issue.

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NOTE 5. Commitments and Contingencies, continued

In June 2012, the District Court certified the case as a class action. The decision was not a ruling on the merits of plaintiffs' claims, but rather a decision to allow the plaintiffs to seek to prove the case as a class. The defendant railroads petitioned the U.S. Court of Appeals for the D.C. Circuit for permission to appeal the District Court's class certification decision. In August 2013, the D.C. Circuit issued a decision vacating the class certification decision and remanded the case to the District Court to reconsider its class certification decision. On October 10, 2017, the District Court issued an order denying class certification. The U.S. Court of Appeals for the D.C. Circuit is reviewing the District Court's denial of class certification and held oral argument on September 28, 2018, with a decision yet to be issued. The District Court has delayed proceedings on the merits of the case pending the outcome of the class certification proceedings.

CSXT believes that its fuel surcharge practices were arrived at and applied lawfully and that the case is without merit. Accordingly, the Company intends to defend itself vigorously. However, penalties for violating antitrust laws can be severe, and resolution of this matter or an unexpected adverse decision on the merits could have a material adverse effect on the Company's financial condition, results of operations or liquidity in that particular period.

Environmental
CSXT is indemnifying Pharmacia LLC (formerly known as Monsanto Company) for certain liabilities associated with real estate located in Kearny, New Jersey along the Lower Passaic River (the “Property”). The Property, which was formerly owned by Pharmacia, is now owned by CSXT. CSXT's indemnification and defense duties arise with respect to several matters. The U.S. Environmental Protection Agency ("EPA"), using its CERCLA authority, seeks cleanup and removal costs and other damages associated with the presence of hazardous substances in the 17-mile Lower Passaic River Study Area (the "Study Area”). CSXT, on behalf of Pharmacia, and a significant number of other potentially responsible parties are together conducting a Remedial Investigation and Feasibility Study of the Study Area pursuant to an Administrative Settlement Agreement and Order on Consent with the EPA.

In March 2016, EPA issued its Record of Decision detailing the agency’s mandated remedial process for the lower 8 miles of the Study Area. Approximately 80 parties, including Pharmacia, are participating in an EPA-directed allocation process to assign responsibility for costs to be incurred implementing the remedy selected for the lower 8 miles of the Study Area. CSXT is participating in the allocation process on behalf of Pharmacia. At a later date, EPA will select a remedy for the remainder of the Study Area and is expected to again seek the participation of private parties to implement the selected remedy using EPA’s CERCLA authority to compel such participation, if necessary.

CSXT is also defending and indemnifying Pharmacia in a cooperative natural resource damages assessment process related to the Property. Based on currently available information, the Company does not believe any indemnification or remediation costs potentially allocable to CSXT with respect to the Property and the Study Area would be material to the Company's financial condition, results of operations or liquidity.

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NOTE 6. Employee Benefit Plans

The Company sponsors defined benefit pension plans principally for salaried, management personnel. CSX also sponsors a post-retirement medical plan and a life insurance plan that provide certain benefits to eligible employees hired prior to January 1, 2003. Independent actuaries compute the amounts of liabilities and expenses relating to these plans subject to the assumptions that the Company determines are appropriate based on historical trends, current market rates and future projections. These amounts are reviewed by management.

Only the service cost component of net periodic benefit costs is included in labor and fringe expense on the consolidated income statement. All other components of net periodic benefit cost are included in other income - net or, if related to prior year restructuring activities, in restructuring charge - non-operating.

(Dollars in millions)	Pension Benefits			
	Third Quarters		Nine Months	
	2018	2017	2018	2017
Service Cost Included in Labor and Fringe	$8	$8	$24	$28
Interest Cost	23	23	69	69
Expected Return on Plan Assets	(44)	(43)	(131)	(128)
Amortization of Net Loss	10	10	30	31
Total Income Included in Other Income - Net	(11)	(10)	(32)	(28)
Net Periodic Benefit Cost	$(3)	$(2)	$(8)	$—
Restructuring Charges - Non Operating[(a)]	—	—	—	57
Total (Income) Expense	$(3)	$(2)	$(8)	$57

(Dollars in millions)	Other Post-retirement Benefits			
	Third Quarters		Nine Months	
	2018	2017	2018	2017
Service Cost Included in Labor and Fringe	$—	$—	$1	$1
Interest Cost	2	2	5	6
Total Expense Included in Other Income - Net	2	2	5	6
Net Periodic Benefit Cost	$2	$2	$6	$7
Restructuring Charges - Non Operating[(a)]	—	—	—	13
Total Expense	$2	$2	$6	$20

(a) Charges related to special termination benefits and curtailment costs were the result of the management workforce reductions in first quarter 2017. See Restructuring Charge in Note 1, Nature of Operations and Significant Accounting Policies.

Qualified pension plan obligations are funded in accordance with regulatory requirements and with an objective of meeting or exceeding minimum funding requirements necessary to avoid restrictions on flexibility of plan operation and benefit payments. No contributions to the Company's qualified pension plans are required in 2018.

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NOTE 7. Debt and Credit Agreements

Total activity related to long-term debt as of the end of third quarter 2018 is shown in the table below. For fair value information related to the Company's long-term debt, see Note 9, Fair Value Measurements.

(Dollars in millions)	Current Portion	Long-term Portion	Total
Long-term debt as of December 31, 2017	$ 19	$ 11,790	$ 11,809
2018 activity:			
Long-term debt issued	—	2,000	2,000
Long-term debt repaid	(19)	—	(19)
Reclassifications	18	(18)	—
Discount, premium and other activity	—	(18)	(18)
Long-term debt as of September 30, 2018	$ 18	$ 13,754	$ 13,772

Debt Issuance

On February 20, 2018, CSX issued $800 million of 3.80% notes due 2028, $850 million of 4.30% notes due 2048, and $350 million of 4.65% notes due 2068. These notes are included in the consolidated balance sheets under long-term debt and may be redeemed by the Company at any time, subject to payment of certain make-whole premiums. The net proceeds will be used for general corporate purposes, which may include repurchases of CSX's common stock, capital investment, working capital requirements, improvements in productivity and other cost reductions at the Company's major transportation units.

Commercial Paper

On September 14, 2018, the Company established a commercial paper program, backed by the revolving credit facility, under which the Company may issue unsecured commercial paper notes up to a maximum aggregate principal amount of $1.0 billion outstanding at any one time. Proceeds from issuances of the notes are expected to be used for general corporate purposes. At September 30, 2018, the Company had no outstanding debt under the commercial paper program.

Credit Facility

CSX has a $1.0 billion unsecured, revolving credit facility backed by a diverse syndicate of banks. The facility allows same-day borrowings at floating (LIBOR-based) interest rates, plus a spread, depending upon CSX's senior unsecured debt ratings. LIBOR is the London Interbank Offered Rate which is a daily reference rate based on the interest rates at which banks offer to lend unsecured funds. This facility expires in May 2020, and at September 30, 2018, the Company had no outstanding balances under this facility.

Commitment fees and interest rates payable under the facility were similar to fees and rates available to comparably rated investment-grade borrowers. As of third quarter 2018, CSX was in compliance with all covenant requirements under this facility.

Receivables Securitization Facility

The Company has a receivables securitization facility with a three-year term scheduled to expire in September 2019. The purpose of this facility is to provide a low cost source of short-term liquidity of up to $200 million, depending on eligible receivables balances. At September 30, 2018, the Company had no outstanding balances under this facility.

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NOTE 8. Income Taxes

The effective tax rate decreased to 23.1% from 38.4% for the nine months ended September 30, 2018 and September 30, 2017, respectively, primarily as a result of the significant reduction in the federal corporate income tax rate effective January 1, 2018. During third quarter 2018, the Company filed its 2017 Federal Income Tax return which resulted in an immaterial adjustment to the deferred tax liability and tax expense. Accordingly, the Company's accounting for the federal rate reduction under the Tax Cuts and Jobs Act (“the Act”) is now complete. The Act has significant complexity and implementation guidance from the Internal Revenue Service and clarifications of state tax law, among other things, could impact the Company's accounting for provisions of the Act other than the federal rate reduction within the measurement period as defined in the SEC's Staff Accounting Bulletin No. 118 ("SAB 118"). As such, any resulting potential adjustments within the measurement period remain open under SAB 118. The Company does not believe potential adjustments in future periods would materially impact its financial condition or results of operations.

There have been no material changes to the balance of unrecognized tax benefits reported at December 31, 2017.

NOTE 9. Fair Value Measurements

The Financial Instruments Topic in the ASC requires disclosures about fair value of financial instruments in annual reports as well as in quarterly reports. For CSX, this statement applies to certain investments and long-term debt. Disclosure of the fair value of pension plan assets is only required annually. Also, this rule clarifies the definition of fair value for financial reporting, establishes a framework for measuring fair value and requires additional disclosures about the use of fair value measurements.

Various inputs are considered when determining the value of the Company's investments, pension plan assets and long-term debt. The inputs or methodologies used for valuing securities are not necessarily an indication of the risk associated with investing in these securities. These inputs are summarized in the three broad levels listed below.

- Level 1 - observable market inputs that are unadjusted quoted prices for identical assets or liabilities in active markets;
- Level 2 - other significant observable inputs (including quoted prices for similar securities, interest rates, credit risk, etc.); and
- Level 3 - significant unobservable inputs (including the Company's own assumptions about the assumptions market participants would use in determining the fair value of investments).

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NOTE 9. Fair Value Measurements, continued

The valuation methods described below may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Investments
The Company's investment assets, valued with assistance from a third-party trustee, consist of certificates of deposits, commercial paper, corporate bonds and government securities and are carried at fair value on the consolidated balance sheet per the Fair Value Measurements and Disclosures Topic in the ASC. There are several valuation methodologies used for those assets as described below.

- Certificates of Deposit and Commercial Paper (Level 2): Valued at amortized cost, which approximates fair value; and
- Corporate Bonds and Government Securities (Level 2): Valued using broker quotes that utilize observable market inputs.

The Company's investment assets are carried at fair value on the consolidated balance sheets as summarized in the following table. All of the inputs used to determine the fair value of the Company's investments are Level 2 inputs. The amortized cost basis of these investments was $705 million and $95 million as of September 30, 2018 and December 31, 2017, respectively.

(Dollars in Millions)	September 30, 2018	December 31, 2017
Certificates of Deposit and Commercial Paper	$ 610	$ —
Corporate Bonds	56	61
Government Securities	40	34
Total investments at fair value	$ 706	$ 95

These investments have the following maturities:

(Dollars in millions)	September 30, 2018	December 31, 2017
Less than 1 year	$ 615	$ 18
1 - 5 years	17	11
5 - 10 years	25	26
Greater than 10 years	49	40
Total investments at fair value	$ 706	$ 95

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NOTE 9. Fair Value Measurements, continued

Long-term Debt
Long-term debt is reported at carrying amount on the consolidated balance sheets and is the Company's only financial instrument with fair values significantly different from their carrying amounts. The majority of the Company's long-term debt is valued with assistance from an independent third party adviser that utilizes closing transactions, market quotes or market values of comparable debt. For those instruments not valued by the independent adviser, the fair value has been estimated by applying market rates of similar instruments to the scheduled contractual debt payments and maturities. These market rates are provided by the same independent adviser. All of the inputs used to determine the fair value of the Company's long-term debt are Level 2 inputs.

The fair value of outstanding debt fluctuates with changes in a number of factors. Such factors include, but are not limited to, interest rates, market conditions, credit ratings, values of similar financial instruments, size of the transaction, cash flow projections and comparable trades. Fair value will exceed carrying value when the current market interest rate is lower than the interest rate at which the debt was originally issued. The fair value of a company's debt is a measure of its current value under present market conditions. It does not impact the financial statements under current accounting rules. The fair value and carrying value of the Company's long-term debt is as follows:

(Dollars in millions)	September 30, 2018	December 31, 2017
Long-term Debt (Including Current Maturities):		
Fair Value	$ 14,173	$ 13,220
Carrying Value	13,772	11,809

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NOTE 10. Other Comprehensive Income (Loss)

CSX reports comprehensive earnings or loss in accordance with the Comprehensive Income Topic in the ASC in the Consolidated Comprehensive Income Statement. Total comprehensive earnings are defined as all changes in shareholders' equity during a period, other than those resulting from investments by and distributions to shareholders (e.g. issuance of equity securities and dividends). Generally, for CSX, total comprehensive earnings equal net earnings plus or minus adjustments for pension and other post-retirement liabilities. Total comprehensive earnings represent the activity for a period net of tax and were $901 million and $467 million for third quarters and $2.4 billion and $1.4 billion for nine months 2018 and 2017, respectively.

While total comprehensive earnings is the activity in a period and is largely driven by net earnings in that period, accumulated other comprehensive income or loss (“AOCI”) represents the cumulative balance of other comprehensive income, net of tax, as of the balance sheet date. For CSX, AOCI is primarily the cumulative balance related to pension and other post-retirement benefit adjustments and CSX's share of AOCI of equity method investees.

Changes in the AOCI balance by component are shown in the table below. Amounts reclassified in pension and other post-employment benefits to net earnings relate to the amortization of actuarial losses and are included in other income - net on the consolidated income statements. See Note 6, Employee Benefit Plans, for further information. Other primarily represents CSX's share of AOCI of equity method investees. Amounts reclassified in other to net earnings are included in equity earnings of affiliates on the consolidated income statements.

(Dollars in millions)	Pension and Other Post-Employment Benefits	Other	Accumulated Other Comprehensive Income (Loss)
Balance December 31, 2017, Net of Tax	$ (440)	$ (46)	$ (486)
Other Comprehensive Income (Loss)			
Loss Before Reclassifications	—	(2)	(2)
Amounts Reclassified to Net Earnings	31	(4)	27
Tax (Expense) Benefit	(7)	1	(6)
Reclassification of Stranded Tax Effects	(108)	1	(107)
Total Other Comprehensive Loss	(84)	(4)	(88)
Balance September 30, 2018, Net of Tax	$ (524)	$ (50)	$ (574)

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NOTE 11. Revenues

The Company's revenues are primarily derived from the transportation of freight as performance obligations that arise from its contracts with customers are satisfied. The following table presents the Company's revenues disaggregated by lines of business as they best depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors:

	Third Quarters		Nine Months	
(Dollars in millions)	2018	2017	2018	2017
Chemicals	$596	$546	$1,741	$1,664
Agricultural and Food Products	325	288	959	941
Automotive	300	269	934	892
Forest Products	223	181	633	567
Metals and Equipment	205	178	589	546
Minerals	137	120	388	362
Fertilizers	104	106	332	353
Total Merchandise	1,890	1,688	5,576	5,325
Domestic Coal	347	350	937	1,029
Export Coal	241	164	723	537
Total Coal	588	514	1,660	1,566
Domestic Intermodal	331	297	948	896
International Intermodal	169	149	491	432
Total Intermodal	500	446	1,439	1,328
Other	151	95	432	326
Total	$3,129	$2,743	$9,107	$8,545

Revenue Recognition
The Company generates revenue from freight billings under contracts with customers generally on a rate per carload, container or ton-basis based on origin to destination and commodities carried. The Company's performance obligation arises when it receives a bill of lading ("BOL") to transport a customer's commodities at a negotiated price contained in a transportation services agreement or a publicly disclosed tariff rate. Once a BOL is received, a contract is formed whereby the parties are committed to perform, collectability of consideration is probable and the rights of the parties, shipping terms and conditions, and payment terms are identified. A customer may submit several BOLs for transportation services at various times throughout a service agreement term but each shipment represents a distinct service that is a separately identified performance obligation.

The average transit time to complete a shipment is between 3 to 8 days and payments for transportation services are normally billed once a BOL is received and are generally due within 15 days after the invoice date. The Company recognizes revenue over transit time of freight as it moves from origin to destination. Revenue for services started but not completed at the reporting date is allocated based on the relative transit time in each reporting period, with the portion allocated for services subsequent to the reporting date considered remaining performance obligations.

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NOTE 11. Revenues, continued

The certain key estimates included in the recognition and measurement of revenue and related accounts receivable are as follows:

- Revenue associated with shipments in transit is recognized ratably over transit time and is based on average cycle times to move commodities and products from their origin to their final destination or interchange;
- Adjustments to revenue for billing corrections and billing discounts;
- Adjustments to revenue for overcharge claims filed by customers, which are based on historical payments to customers for rate overcharges as a percentage of total billing;
- Incentive-based refunds to customers, which are primarily volume-related, are recorded as a reduction to revenue on the basis of the projected liability (this estimate is based on historical activity, current volume levels and forecasted future volume).

Revenue related to interline transportation services that involve the services of another party, such as another railroad, is reported on a net basis. The portion of the gross amount billed to customers that is remitted by the Company to another party is not reflected as revenue.

Other revenue, which includes revenue from regional subsidiary railroads, demurrage, switching and other incidental charges, is recorded upon completion of the service and accounted for 5% of the Company's total revenue in the third quarter and for the nine months ended September 30, 2018. Revenue from regional subsidiary railroads includes shipments by railroads that the Company does not directly operate. Demurrage represents charges assessed when freight cars are held by a customer beyond a specified period of time. Switching revenue is primarily generated when the Company switches cars for a customer or another railroad.

During the third quarters of 2018 and 2017, revenue recognized from performance obligations related to prior periods (for example, due to changes in transaction price), was not material.

Remaining Performance Obligations
Remaining performance obligations represent the transaction price allocated to future reporting periods for freight services started but not completed at the reporting date. This includes the unearned portion of billed and unbilled amounts for cancellable freight shipments in transit. The Company expects to recognize the unearned portion of revenue for freight services in transit within one week of the reporting date. As of September 30, 2018, the Company had no material remaining performance obligations.

Contract Balances and Accounts Receivable
The timing of revenue recognition, billings and cash collections results in accounts receivable and customer advances and deposits (contract liabilities) on the consolidated balance sheets. The Company had no material contract assets, contract liabilities or deferred contract costs recorded on the consolidated balance sheet as of September 30, 2018.

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NOTE 11. Revenues, continued

The Company’s accounts receivable - net consists of freight and non-freight receivables, reduced by an allowance for doubtful accounts.

(Dollars in millions)	September 30, 2018	December 31, 2017
Freight Receivables	$ 887	$ 810
Freight Allowance for Doubtful Accounts	(17)	(17)
Freight Receivables, net	870	793
Non-Freight Receivables	230	186
Non-Freight Allowance for Doubtful Accounts	(10)	(9)
Non-Freight Receivables, net	220	177
Total Accounts Receivable, net	$ 1,090	$ 970

Freight receivables include amounts earned, billed and unbilled, and currently due from customers for transportation-related services. Non-freight receivables include amounts billed and unbilled and currently due related to government reimbursement receivables and other non-revenue receivables. The Company maintains an allowance for doubtful accounts to provide for the estimated amount of receivables that will not be collected. The allowance is based upon an assessment of customer creditworthiness, historical payment experience, the age of outstanding receivables and economic conditions. Impairment losses recognized on the Company’s accounts receivable were not material in the third quarters of 2018 and 2017.

NOTE 12. Summarized Consolidating Financial Data

In 2007, CSXT, a wholly-owned subsidiary of CSX Corporation, sold secured equipment notes maturing in 2023 in a registered public offering. CSX has fully and unconditionally guaranteed the notes. In connection with the notes, the Company is providing the following condensed consolidating financial information in accordance with SEC disclosure requirements. Each entity in the consolidating financial information follows the same accounting policies as described in the consolidated financial statements, except for the use of the equity method of accounting to reflect ownership interests in subsidiaries which are eliminated upon consolidation and the allocation of certain expenses of CSX incurred for the benefit of its subsidiaries. Condensed consolidating financial information for the obligor, CSXT, and parent guarantor, CSX, is shown in the following tables.

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CSX CORPORATION
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(Unaudited)

NOTE 12. Summarized Consolidating Financial Data, continued

Consolidating Income Statements
(Dollars in millions)

Third Quarter 2018	CSX Corporation	CSX Transportation	Eliminations and Other	Consolidated
Revenue	$ —	$ 3,110	$ 19	$ 3,129
Expense	(86)	1,952	(30)	1,836
Operating Income	86	1,158	49	1,293
Equity in Earnings of Subsidiaries	953	—	(953)	—
Interest (Expense) / Benefit	(190)	(11)	39	(162)
Other Income / (Expense) - Net	6	35	(22)	19
Earnings Before Income Taxes	855	1,182	(887)	1,150
Income Tax Benefit / (Expense)	39	(278)	(17)	(256)
Net Earnings	$ 894	$ 904	$ (904)	$ 894
Total Comprehensive Earnings	$ 901	$ 903	$ (903)	$ 901

Third Quarter 2017	CSX Corporation	CSX Transportation	Eliminations and Other	Consolidated
Revenue	$ —	$ 2,725	$ 18	$ 2,743
Expense	(129)	2,031	(27)	1,875
Operating Income	129	694	45	868
Equity in Earnings of Subsidiaries	472	—	(472)	—
Interest (Expense) / Benefit	(147)	(3)	18	(132)
Other Income / (Expense) - Net	1	19	(6)	14
Earnings Before Income Taxes	455	710	(415)	750
Income Tax Benefit / (Expense)	4	(277)	(18)	(291)
Net Earnings	$ 459	$ 433	$ (433)	$ 459
Total Comprehensive Earnings	$ 467	$ 433	$ (433)	$ 467

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CSX CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 12. Summarized Consolidating Financial Data, continued

Consolidating Income Statements
(Dollars in millions)

Nine Months 2018	CSX Corporation	CSX Transportation	Eliminations and Other	Consolidated
Revenue	$ —	$ 9,050	$ 57	$ 9,107
Expense	(248)	5,843	(108)	5,487
Operating Income	248	3,207	165	3,620
Equity in Earnings of Subsidiaries	2,653	—	(2,653)	—
Interest (Expense) / Benefit	(535)	(28)	95	(468)
Other Income / (Expense) - Net	16	87	(49)	54
Earnings Before Income Taxes	2,382	3,266	(2,442)	3,206
Income Tax (Expense) / Benefit	84	(776)	(48)	(740)
Net Earnings	$ 2,466	$ 2,490	$ (2,490)	$ 2,466
Total Comprehensive Earnings	$ 2,378	$ 2,484	$ (2,484)	$ 2,378

Nine Months 2017	CSX Corporation	CSX Transportation	Eliminations and Other	Consolidated
Revenue	$ —	$ 8,490	$ 55	$ 8,545
Expense	(171)	6,225	(103)	5,951
Operating Income	171	2,265	158	2,594
Equity in Earnings of Subsidiaries	1,506	—	(1,506)	—
Interest (Expense) / Benefit	(432)	(21)	47	(406)
Other Income / (Expense) - Net	6	(21)	(14)	(29)
Earnings Before Income Taxes	1,251	2,223	(1,315)	2,159
Income Tax (Expense) / Benefit	80	(844)	(64)	(828)
Net Earnings	$ 1,331	$ 1,379	$ (1,379)	$ 1,331
Total Comprehensive Earnings	$ 1,410	$ 1,378	$ (1,378)	$ 1,410

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CSX CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 12. Summarized Consolidating Financial Data, continued

Consolidating Balance Sheet
(Dollars in millions)

September 30, 2018	CSX Corporation	CSX Transportation	Eliminations and Other	Consolidated
ASSETS				
Current Assets				
Cash and Cash Equivalents	$ 537	$ 116	$ 10	$ 663
Short-term Investments	610	—	5	615
Accounts Receivable - Net	1	221	868	1,090
Receivable from Affiliates	960	5,256	(6,216)	—
Materials and Supplies	—	283	—	283
Other Current Assets	—	115	18	133
Total Current Assets	2,108	5,991	(5,315)	2,784
Properties	1	41,629	2,855	44,485
Accumulated Depreciation	(1)	(11,043)	(1,570)	(12,614)
Properties - Net	—	30,586	1,285	31,871
Investments in Conrail	—	—	941	941
Affiliates and Other Companies	(39)	846	16	823
Investments in Consolidated Subsidiaries	31,288	—	(31,288)	—
Other Long-term Assets	77	613	(248)	442
Total Assets	$ 33,434	$ 38,036	$ (34,609)	$ 36,861
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current Liabilities				
Accounts Payable	$ 189	$ 753	$ 40	$ 982
Labor and Fringe Benefits Payable	40	434	43	517
Payable to Affiliates	6,339	397	(6,736)	—
Casualty, Environmental and Other Reserves	—	97	13	110
Current Maturities of Long-term Debt	—	18	—	18
Income and Other Taxes Payable	(415)	542	39	166
Other Current Liabilities	1	148	2	151
Total Current Liabilities	6,154	2,389	(6,599)	1,944
Casualty, Environmental and Other Reserves	—	191	40	231
Long-term Debt	13,043	711	—	13,754
Deferred Income Taxes - Net	(99)	6,484	199	6,584
Other Long-term Liabilities	617	300	(304)	613
Total Liabilities	$ 19,715	$ 10,075	$ (6,664)	$ 23,126
Shareholders' Equity				
Common Stock, $1 Par Value	$ 844	$ 181	$ (181)	$ 844

Other Capital	129	5,096	(5,096	) 129
Retained Earnings	13,320	22,679	(22,679	) 13,320
Accumulated Other Comprehensive Loss	(574	) (11	) 11	(574)
Noncontrolling Interest	—	16	—	16
Total Shareholders' Equity	$ 13,719	$ 27,961	$ (27,945	) $ 13,735
Total Liabilities and Shareholders' Equity	$ 33,434	$ 38,036	$ (34,609	) $ 36,861

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CSX CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 12. Summarized Consolidating Financial Data, continued

Consolidating Balance Sheet
(Dollars in millions)

December 31, 2017	CSX Corporation	CSX Transportation	Eliminations and Other	Consolidated
ASSETS				
Current Assets				
Cash and Cash Equivalents	$ 274	$ 121	$ 6	$ 401
Short-term Investments	—	—	18	18
Accounts Receivable - Net	(1)	301	670	970
Receivable from Affiliates	1,226	3,517	(4,743)	—
Materials and Supplies	—	372	—	372
Other Current Assets	(1)	145	10	154
Total Current Assets	1,498	4,456	(4,039)	1,915
Properties	1	41,479	2,844	44,324
Accumulated Depreciation	(1)	(11,017)	(1,542)	(12,560)
Properties - Net	—	30,462	1,302	31,764
Investments in Conrail	—	—	907	907
Affiliates and Other Companies	(39)	800	18	779
Investment in Consolidated Subsidiaries	29,405	—	(29,405)	—
Other Long-term Assets	39	596	(261)	374
Total Assets	$ 30,903	$ 36,314	$ (31,478)	$ 35,739
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current Liabilities				
Accounts Payable	$ 105	$ 708	$ 34	$ 847
Labor and Fringe Benefits Payable	52	494	56	602
Payable to Affiliates	4,792	552	(5,344)	—
Casualty, Environmental and Other Reserves	—	95	13	108
Current Maturities of Long-term Debt	—	19	—	19
Income and Other Taxes Payable	(326)	455	28	157
Other Current Liabilities	5	153	3	161
Total Current Liabilities	4,628	2,476	(5,210)	1,894
Casualty, Environmental and Other Reserves	—	222	44	266
Long-term Debt	11,056	733	1	11,790
Deferred Income Taxes - Net	(130)	6,342	206	6,418
Other Long-term Liabilities	644	320	(314)	650
Total Liabilities	$ 16,198	$ 10,093	$ (5,273)	$ 21,018
Shareholders' Equity				
Common Stock, $1 Par Value	$ 890	$ 181	$ (181)	$ 890
Other Capital	217	5,096	(5,096)	217

Retained Earnings	14,084	20,933	(20,933)	14,084
Accumulated Other Comprehensive Loss	(486)	(5)	5	(486)
Noncontrolling Minority Interest	—	16	—	16
Total Shareholders' Equity	$ 14,705	$ 26,221	$ (26,205)	$ 14,721
Total Liabilities and Shareholders' Equity	$ 30,903	$ 36,314	$ (31,478)	$ 35,739

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CSX CORPORATION
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NOTE 12. Summarized Consolidating Financial Data, continued

Consolidating
Cash Flow
Statements
(Dollars in
millions)
Nine Months 2018