

PACCAR INC
Form 10-K
February 21, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d)

of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2017

Commission File No. 001-14817

PACCAR Inc

(Exact name of Registrant as specified in its charter)

Delaware 91-0351110
(State of incorporation) (I.R.S. Employer Identification No.)

777 - 106th Ave. N.E., Bellevue, WA 98004
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code (425) 468-7400

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, \$1 par value	The NASDAQ Global Select Market LLC

Securities registered pursuant to Section 12(g) of the Act: NONE

Edgar Filing: PACCAR INC - Form 10-K

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer", "smaller reporting company", and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer 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 check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The aggregate market value of the voting stock held by non-affiliates of the registrant as of June 30, 2017:

Common Stock, \$1 par value \$22.71 billion

The number of shares outstanding of the registrant's classes of common stock, as of January 31, 2018:

Common Stock, \$1 par value – 351,986,606 shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement for the annual stockholders meeting to be held on May 1, 2018 are incorporated by reference into Part III.

PACCAR Inc – FORM 10-K

INDEX

	Page
<u>PART I</u>	3
ITEM 1. <u>BUSINESS</u>	3
ITEM 1A. <u>RISK FACTORS</u>	7
ITEM 1B. <u>UNRESOLVED STAFF COMMENTS</u>	8
ITEM 2. <u>PROPERTIES</u>	9
ITEM 3. <u>LEGAL PROCEEDINGS</u>	9
ITEM 4. <u>MINE SAFETY DISCLOSURES</u>	9
<u>PART II</u>	10
ITEM 5. <u>MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	10
ITEM 6. <u>SELECTED FINANCIAL DATA</u>	12
ITEM 7. <u>MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	13
ITEM 7A. <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	37
ITEM 8. <u>FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>	38
ITEM 9. <u>CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>	80
ITEM 9A. <u>CONTROLS AND PROCEDURES</u>	80
ITEM 9B. <u>OTHER INFORMATION</u>	80
<u>PART III</u>	81
ITEM 10. <u>DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE</u>	81
ITEM 11. <u>EXECUTIVE COMPENSATION</u>	83
ITEM 12. <u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>	83
ITEM 13. <u>CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE</u>	83
ITEM 14. <u>PRINCIPAL ACCOUNTING FEES AND SERVICES</u>	83
<u>PART IV</u>	84
ITEM 15. <u>EXHIBITS, FINANCIAL STATEMENT SCHEDULES</u>	84
<u>SIGNATURES</u>	88

PART I

ITEM 1. BUSINESS.

(a) General Development of Business

PACCAR Inc (the Company or PACCAR), incorporated under the laws of Delaware in 1971, is the successor to Pacific Car and Foundry Company which was incorporated in Washington in 1924. The Company traces its predecessors to Seattle Car Manufacturing Company formed in 1905.

(b) Financial Information About Industry Segments and Geographic Areas

Information about the Company's industry segments and geographic areas in response to Items 101(b), (c)(1)(i), and (d) of Regulation S-K appears in Item 8, Note R, of this Form 10-K.

(c) Narrative Description of Business

PACCAR is a multinational company operating in three principal industry segments:

- (1) The Truck segment includes the design, manufacture and distribution of high-quality, light-, medium- and heavy-duty commercial trucks. Heavy-duty trucks have a gross vehicle weight (GVW) of over 33,000 lbs (Class 8) in North America and over 16 metric tonnes in Europe. Medium-duty trucks have a GVW ranging from 19,500 to 33,000 lbs (Class 6 to 7) in North America, and in Europe, light- and medium-duty trucks range between 6 to 16 metric tonnes. Trucks are configured with engine in front of cab (conventional) or cab-over-engine (COE).
- (2) The Parts segment includes the distribution of aftermarket parts for trucks and related commercial vehicles.
- (3) The Financial Services segment includes finance and leasing products and services provided to customers and dealers. PACCAR's finance and leasing activities are principally related to PACCAR products and associated equipment.

PACCAR's Other business includes the manufacturing and marketing of industrial winches.

TRUCKS

PACCAR's trucks are marketed under the Kenworth, Peterbilt and DAF nameplates. These trucks, which are built in three plants in the United States, three in Europe and one each in Australia, Brasil, Canada and Mexico, are used worldwide for over-the-road and off-highway hauling of commercial and consumer goods. The Company also manufactures engines, primarily for use in the Company's trucks, at its facilities in Columbus, Mississippi; Eindhoven, the Netherlands; and Ponta Grossa, Brasil. PACCAR competes in the North American Class 8 market, primarily with Kenworth and Peterbilt conventional models. These trucks are assembled at facilities in Chillicothe, Ohio; Denton, Texas; Renton, Washington; Ste. Therese, Canada and Mexicali, Mexico. PACCAR also competes in the North American Class 6 to 7 markets primarily with Kenworth and Peterbilt conventional models. These trucks are assembled at facilities in Ste. Therese, Canada and Mexicali, Mexico. PACCAR competes in the European light/medium market with DAF COE trucks assembled in the United Kingdom (U.K.) by Leyland, one of PACCAR's wholly owned subsidiaries, and participates in the European heavy market with DAF COE trucks assembled in the Netherlands and the U.K. PACCAR competes in the Brazilian heavy truck market with DAF models assembled at Ponta Grossa in the state of Paraná, Brasil. PACCAR competes in the Australian light and heavy truck markets with Kenworth conventional and COE models assembled at its facility at Bayswater in the state of Victoria, Australia, and DAF COE models assembled in the U.K. Commercial truck manufacturing comprises the largest segment of PACCAR's business and accounted for 76% of total 2017 net sales and revenues.

Substantially all trucks are sold to independent dealers. The Kenworth and Peterbilt nameplates are marketed and distributed by separate divisions in the U.S. and a foreign subsidiary in Canada. The Kenworth nameplate is also marketed and distributed by foreign subsidiaries in Mexico and Australia. The DAF nameplate is marketed and distributed worldwide by a foreign subsidiary headquartered in the Netherlands and is also marketed and distributed

by foreign subsidiaries in Brasil and Australia. The decision to operate as a subsidiary or as a division is incidental to PACCAR's Truck segment operations and reflects legal, tax and regulatory requirements in the various countries where PACCAR operates.

The Truck segment utilizes centrally managed purchasing, information technology, technical research and testing, treasury and finance functions. Some manufacturing plants in North America produce trucks for more than one nameplate, while other plants produce trucks for only one nameplate, depending on various factors. Best manufacturing practices within the Company are shared on a routine basis reflecting the similarity of the business models employed by each nameplate.

The Company's trucks have a reputation for high quality and are essentially custom products, most of which are ordered by dealers according to customer specifications. Some units are ordered by dealers for stocking to meet the needs of certain customers who require immediate delivery or for customers that require chassis to be fitted with specialized bodies. For a significant portion of the Company's truck operations, major components, such as engines, transmissions and axles, as well as a substantial percentage of other components, are purchased from component manufacturers pursuant to PACCAR and customer specifications. DAF, which is more vertically integrated, manufactures PACCAR engines and axles and a higher percentage of other components for its heavy truck models. The Company also manufactures engines at its Columbus, Mississippi facility. In 2017, the Company installed PACCAR engines in 41% of the Company's Kenworth and Peterbilt heavy duty trucks in the U.S. and Canada and substantially all of the DAF heavy-duty trucks sold throughout the world. Engines not manufactured by the Company are purchased from Cummins Inc. (Cummins). The Company purchased a significant portion of its transmissions from Eaton Corporation Plc. (Eaton) and ZF Friedrichshafen AG (ZF). The Company also purchased a significant portion of North America stampings used for cabs from Magna International Inc. (Magna). The Company has long-term agreements with Cummins, Eaton, ZF and Magna to provide for continuity of supply. A loss of supply from Cummins, Eaton, ZF or Magna, and the resulting interruption in the production of trucks, would have a material effect on the Company's results. Purchased materials and parts include raw materials, partially processed materials, such as castings, and finished components manufactured by independent suppliers. Raw materials, partially processed materials and finished components make up approximately 90% of the cost of new trucks. The value of major finished truck components manufactured by independent suppliers ranges from approximately 34% in Europe to approximately 87% in North America. In addition to materials, the Company's cost of sales includes labor and factory overhead, vehicle delivery and warranty. Accordingly, except for certain factory overhead costs such as depreciation, property taxes and utilities, the Company's cost of sales are highly correlated to sales.

The Company's DAF subsidiary purchases fully assembled cabs from a competitor, Renault V.I., for its European light-duty product line pursuant to a joint product development and long-term supply contract. Sales of trucks manufactured with these cabs amounted to approximately 3% of consolidated revenues in 2017. A short-term loss of supply, and the resulting interruption in the production of these trucks, would not have a material effect on the Company's results of operations. However, a loss of supply for an extended period of time would require the Company to either contract for an alternative source of supply or to manufacture cabs itself.

Other than these components, the Company is not limited to any single source for any significant component, although the sudden inability of a supplier to deliver components could have a temporary adverse effect on production of certain products. No significant shortages of materials or components were experienced in 2017. Manufacturing inventory levels are based upon production schedules, and orders are placed with suppliers accordingly.

Key factors affecting Truck segment earnings include the number of new trucks sold in the markets served and the margins realized on the sales. The Company's sales of new trucks are dependent on the size of the truck markets served and the Company's share of those markets. Truck segment sales and margins tend to be cyclical based on the level of overall economic activity, the availability of capital and the amount of freight being transported. The Company's costs for trucks consist primarily of material costs, which are influenced by the price of commodities such as steel, copper, aluminum and petroleum. The Company utilizes long-term supply agreements to reduce the variability of the unit cost of purchased materials and finished components. The Company's spending on research and development varies based on product development cycles and government requirements such as changes to diesel engine emissions and vehicle fuel efficiency standards in the various markets served. The Company maintains rigorous control of selling, general and administrative (SG&A) expenses and seeks to minimize such costs.

There are four principal competitors in the U.S. and Canada commercial truck market. The Company's share of the U.S. and Canadian Class 8 market was a record 30.7% of retail sales in 2017, and the Company's medium-duty market share was 17.1%. In Europe, there are six principal competitors in the commercial truck market, including parent

companies to two competitors of the Company in the U.S. In 2017, DAF had a 15.3% share of the European heavy-duty market and a 10.5% share of the light/medium market. These markets are highly competitive in price, quality and service. PACCAR is not dependent on any single customer for its sales. There are no significant seasonal variations in sales.

The Peterbilt, Kenworth and DAF nameplates are recognized internationally and play an important role in the marketing of the Company's truck products. The Company engages in a continuous program of trademark and trade name protection in all marketing areas of the world.

The Company's truck products are subject to noise, emission and safety regulations. Competing manufacturers are subject to the same regulations. The Company believes the cost of complying with these regulations will not be detrimental to its business.

The Company had a total production backlog of \$6.4 billion at the end of 2017. Within this backlog, orders scheduled for delivery within three months (90 days) are considered to be firm. The 90 day backlog approximated \$4.0 billion at December 31, 2017, \$2.1 billion at December 31, 2016 and \$2.8 billion at December 31, 2015. Production of the year-end 2017 backlog is expected to be substantially completed during 2018.

PARTS

The Parts segment includes the distribution of aftermarket parts for trucks and related commercial vehicles to over 2,100 Kenworth, Peterbilt and DAF dealers in 101 countries around the world. Aftermarket truck parts are sold and delivered to the Company's independent dealers through the Company's 18 strategically located parts distribution centers (PDCs) in the U.S., Canada, Europe, Australia, Mexico and Central and South America. Parts are primarily purchased from various suppliers and also manufactured by the Company. Aftermarket parts inventory levels are determined largely by anticipated customer demand and the need for timely delivery. The Parts segment accounted for 17% of total 2017 net sales and revenues.

Key factors affecting Parts segment earnings include the aftermarket parts sold in the markets served and the margins realized on the sales. Aftermarket parts sales are influenced by the total number of the Company's trucks in service and the average age and mileage of those trucks. To reflect the benefit the Parts segment receives from costs incurred by the Truck segment, certain factory overhead, research and development, engineering and SG&A expenses are allocated from the Truck segment to the Parts segment. The Company's cost for parts sold consists primarily of material costs, which are influenced by the price of commodities such as steel, copper, aluminum and petroleum. The Company utilizes long-term supply agreements to reduce the variability of the cost of parts sold. The Company maintains rigorous control of SG&A expenses and seeks to minimize such costs.

FINANCIAL SERVICES

PACCAR Financial Services (PFS) operates in 24 countries in North America, Europe, Australia and South America through wholly owned finance companies operating under the PACCAR Financial trade name. PFS also conducts full service leasing operations through operating divisions or wholly owned subsidiaries in North America, Germany and Australia under the PacLease trade name. Selected dealers in North America are franchised to provide full service leasing. PFS provides its franchisees with equipment financing and administrative support. PFS also operates its own full service lease outlets. PFS's retail loan and lease customers consist of small, medium and large commercial trucking companies, independent owner/operators and other businesses and acquire their PACCAR trucks principally from independent PACCAR dealers. PFS accounted for 7% of total net sales and revenues and 56% of total assets in 2017.

The Company's finance receivables are classified as dealer wholesale, dealer retail and customer retail segments. The dealer wholesale segment consists of truck inventory financing to independent PACCAR dealers. The dealer retail segment consists of loans and leases to participating dealers and franchises, which use the proceeds to fund their customers' acquisition of trucks and related equipment. The customer retail segment consists of loans and leases directly to customers for their acquisition of trucks and related equipment. Customer retail receivables are further segregated by fleet and owner/operator classes. The fleet class consists of customers operating more than five trucks. All others are considered owner/operators. Similar methods are employed to assess and monitor credit risk for each class.

Finance receivables are secured by the trucks and related equipment being financed or leased. The terms of loan and lease contracts generally range from three to five years depending on the type and use of equipment. Payment is required on dealer inventory financing when the floored truck is sold to a customer or upon maturity of the flooring loan, whichever comes first. Dealer inventory loans generally mature within one year.

The Company funds its financial services activities primarily from collections on existing finance receivables and borrowings in the capital markets. The primary sources of borrowings in the capital markets are commercial paper and medium-term notes issued in public and private offerings and, to a lesser extent, bank loans. An additional source of funds is loans from other PACCAR companies. PFS attempts to match the maturity and interest rate characteristics

of its debt with the maturity and interest rate characteristics of loans and leases.

Key factors affecting the earnings of the Financial Services segment include the volume of new loans and leases, the yield earned on the loans and leases, the costs of funding investments in loans and leases and the ability to collect the amounts owed to PFS. New loan and lease volume is dependent on the volume of new trucks sold by Kenworth, Peterbilt and DAF and the share of those truck sales that are financed by the Financial Services segment. The Company's Financial Services market share is influenced by the extent of competition in the financing market. PFS's primary competitors include commercial banks and independent finance and leasing companies.

The revenue earned on loans and leases depends on market interest and lease rates and the ability of PFS to differentiate itself from the competition by superior industry knowledge and customer service. Dealer inventory loans have variable rates with rates reset monthly based on an index pertaining to the applicable local market. Retail loan and lease contracts normally have fixed rates over the contract term. PFS obtains funds either through fixed rate borrowings or through variable rate borrowings, a portion of which have been effectively converted to fixed rate through the use of interest-rate contracts. This enables PFS to obtain a stable spread between the

cost of borrowing and the yield on fixed rate contracts over the contract term. Included in Financial Services cost of revenues is depreciation on equipment on operating leases. The amount of depreciation on operating leases principally depends on the acquisition cost of leased equipment, the term of the leases, which generally ranges from three to five years, and the residual value of the leases, which generally ranges from 30% to 60%. The margin earned is the difference between the revenues on loan and lease contracts and the direct costs of operation, including interest and depreciation.

PFS incurs credit losses when customers are unable to pay the full amounts due under loan and finance lease contracts. PFS takes a conservative approach to underwriting new retail business in order to minimize credit losses.

The ability of customers to pay their obligations to PFS depends on the state of the general economy, the extent of freight demand, freight rates and the cost of fuel, among other factors. PFS limits its exposure to any one customer, with no one customer or dealer balance representing over 5% of the aggregate portfolio assets. PFS generally requires a down payment and secures its interest in the underlying truck collateral and may require other collateral or guarantees. In the event of default, PFS will repossess the truck and sell it in the open market primarily through its dealer network as well as PFS used truck centers. PFS will also seek to recover any shortfall between the amounts owed and the amounts recovered from sale of the collateral. The amount of credit losses depends on the rate of default on loans and finance leases and, in the event of repossession, the ability to recover the amount owed from sale of the collateral which is affected by used truck prices. PFS's experience over the last fifty years financing truck sales has been that periods of economic weakness result in higher past dues and increased rates of repossession. Used truck prices also tend to fall during periods of economic weakness. As a result, credit losses tend to increase during periods of economic weakness. PFS provides an allowance for credit losses based on specifically identified customer risks and an analysis of estimated losses inherent in the portfolio, considering the amount of past due accounts, the trends of used truck prices and the economic environment in each of its markets.

Financial Services SG&A expenses consist primarily of personnel costs associated with originating and servicing the loan and lease portfolios. These costs vary somewhat depending on overall levels of business activity, but given the ongoing nature of servicing activities, tend to be relatively stable.

OTHER BUSINESSES

Other businesses include the manufacturing of industrial winches in two U.S. plants and marketing them under the Braden, Carco and Gearmatic nameplates. The markets for these products are highly competitive, and the Company competes with a number of well established firms. Sales of industrial winches were less than 1% of total net sales and revenues in 2017, 2016 and 2015.

The Braden, Carco and Gearmatic trademarks and trade names are recognized internationally and play an important role in the marketing of those products.

PATENTS

The Company owns numerous patents which relate to all product lines. Although these patents are considered important to the overall conduct of the Company's business, no patent or group of patents is considered essential to a material part of the Company's business.

REGULATION

As a manufacturer of highway trucks, the Company is subject to the National Traffic and Motor Vehicle Safety Act and Federal Motor Vehicle Safety Standards promulgated by the National Highway Traffic Safety Administration as

well as environmental laws and regulations in the United States, and is subject to similar regulations in all countries where it has operations and where its trucks are distributed. In addition, the Company is subject to certain other licensing requirements to do business in the United States and Europe. The Company believes it is in compliance with laws and regulations applicable to safety standards, the environment and other licensing requirements in all countries where it has operations and where its trucks are distributed.

Information regarding the effects that compliance with international, federal, state and local provisions regulating the environment have on the Company's capital and operating expenditures and the Company's involvement in environmental cleanup activities is included in Management's Discussion and Analysis of Financial Condition and Results of Operations and the Company's Consolidated Financial Statements in Items 7 and 8, respectively.

EMPLOYEES

On December 31, 2017, the Company had approximately 25,000 employees.

OTHER DISCLOSURES

The Company's filings on Forms 10-K, 10-Q and 8-K and any amendments to those reports can be found on the Company's website www.paccar.com free of charge as soon as practicable after the report is electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). The information on the Company's website is not incorporated by reference into this report. In addition, the Company's reports filed with the SEC can be found at www.sec.gov.

ITEM 1A. RISK FACTORS.

The following are significant risks which could have a material negative impact on the Company's financial condition or results of operations.

Business and Industry Risks

Commercial Truck Market Demand is Variable. The Company's business is highly sensitive to global and national economic conditions as well as economic conditions in the industries and markets it serves. Negative economic conditions and outlook can materially weaken demand for the Company's equipment and services. The yearly demand for commercial vehicles may increase or decrease more than overall gross domestic product in markets the Company serves, which are principally North America and Europe. Demand for commercial vehicles may also be affected by the introduction of new vehicles and technologies by the Company or its competitors.

Competition and Prices. The Company operates in a highly competitive environment, which could adversely affect the Company's sales and pricing. Financial results depend largely on the ability to develop, manufacture and market competitive products that profitably meet customer demand.

Production Costs and Supplier Capacity. The Company's products are exposed to variability in material and commodity costs. Commodity or component price increases and significant shortages of component products may adversely impact the Company's financial results or use of its production capacity. Many of the Company's suppliers also supply automotive manufacturers, and factors that adversely affect the automotive industry can also have adverse effects on these suppliers and the Company. Supplier delivery performance can be adversely affected if increased demand for these suppliers' products exceeds their production capacity. Unexpected events, including natural disasters, may increase the Company's cost of doing business or disrupt the Company's or its suppliers' operations.

Liquidity Risks, Credit Ratings and Costs of Funds. Disruptions or volatility in global financial markets could limit the Company's sources of liquidity, or the liquidity of customers, dealers and suppliers. A lowering of the Company's credit ratings could increase the cost of borrowing and adversely affect access to capital markets. The Company's Financial Services segment obtains funds for its operations from commercial paper, medium-term notes and bank debt. If the markets for commercial paper, medium-term notes and bank debt do not provide the necessary liquidity in the future, the Financial Services segment may experience increased costs or may have to limit its financing of retail and wholesale assets. This could result in a reduction of the number of vehicles the Company is able to produce and sell to customers.

The Financial Services Industry is Highly Competitive. The Company's Financial Services segment competes with banks, other commercial finance companies and financial services firms which may have lower costs of borrowing, higher leverage or market share goals that result in a willingness to offer lower interest rates, which may lead to decreased margins, lower market share or both. A decline in the Company's truck unit sales and a decrease in truck residual values due to lower used truck pricing are also factors which may affect the Company's Financial Services segment.

The Financial Services Segment is Subject to Credit Risk. The Financial Services segment is exposed to the risk of loss arising from the failure of a customer, dealer or counterparty to meet the terms of the loans, leases and derivative contracts with the Company. Although the financial assets of the Financial Services segment are secured by underlying equipment collateral, in the event a customer cannot meet its obligations to the Company, there is a risk that the value of the underlying collateral will not be sufficient to recover the amounts owed to the Company, resulting in credit losses.

Interest-Rate Risks. The Financial Services segment is subject to interest-rate risks, because increases in interest rates can reduce demand for its products, increase borrowing costs and potentially reduce interest margins. PFS uses derivative contracts to match the interest rate characteristics of its debt to the interest rate characteristics of its finance receivables in order to mitigate the risk of changing interest rates.

Information Technology. The Company relies on information technology systems, including the internet and other computer systems, which may be subject to disruptions during the process of upgrading or replacing software, databases or components; power outages; hardware failures; computer viruses; or outside parties attempting to disrupt the Company's business or gain unauthorized access to the Company's electronic data. The Company maintains protections to guard against such events. If the Company's computer systems were to be damaged, disrupted or breached, it could result in a negative impact on the Company's operating results and could also cause reputational damage, business disruption or the disclosure of confidential data.

Political, Regulatory and Economic Risks

Multinational Operations. The Company's global operations are exposed to political, economic and other risks and events beyond its control in the countries in which the Company operates. The Company may be adversely affected by political instabilities, fuel shortages or interruptions in utility or transportation systems, natural calamities, wars, terrorism and labor strikes. Changes in government monetary or fiscal policies and international trade policies may impact demand for the Company's products, financial results and competitive position. PACCAR's global operations are subject to extensive trade, competition and anti-corruption laws and regulations that could impose significant compliance costs.

Environmental Regulations. The Company's operations are subject to environmental laws and regulations that impose significant compliance costs. The Company could experience higher research and development and manufacturing costs due to changes in government requirements for its products, including changes in emissions, fuel, greenhouse gas or other regulations.

Litigation, Product Liability and Regulatory. The Company's products are subject to recall for environmental, performance and safety-related issues. Product recalls, lawsuits, regulatory actions or increases in the reserves the Company establishes for contingencies may increase the Company's costs and lower profits. Due to the international nature of the Company's business, some products are also subject to international trade regulations, including customs and import / export related laws and regulations, government embargoes and sanctions prohibiting sales to specific persons or countries, as well as anticorruption laws. The Company's reputation and its brand names are valuable assets, and claims or regulatory actions, even if unsuccessful or without merit, could adversely affect the Company's reputation and brand images because of adverse publicity.

Currency Exchange and Translation. The Company's consolidated financial results are reported in U.S. dollars, while significant operations are denominated in the currencies of other countries. Currency exchange rate fluctuations can affect the Company's assets, liabilities and results of operations through both translation and transaction risk, as reported in the Company's financial statements. The Company uses certain derivative financial instruments and localized production of its products to reduce, but not eliminate, the effects of foreign currency exchange rate fluctuations.

Accounting Estimates. In the preparation of the Company's financial statements in accordance with U.S. generally accepted accounting principles, management uses estimates and makes judgments and assumptions that affect asset and liability values and the amounts reported as income and expense during the periods presented. Certain of these estimates, judgments and assumptions, such as residual values on operating leases, the allowance for credit losses, warranty and the provision for income taxes, are particularly sensitive. If actual results are different from estimates used by management, they may have a material impact on the financial statements. For additional disclosures regarding accounting estimates, see "Critical Accounting Policies" under Item 7 of this Form 10-K.

Taxes. Changes in statutory income tax rates in the countries in which the Company operates impact the Company's effective tax rate. Changes to other taxes or the adoption of other new tax legislation could affect the Company's

provision for income taxes and related tax assets and liabilities.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

8

ITEM 2. PROPERTIES.

The Company and its subsidiaries own and operate manufacturing plants in five U.S. states, three countries in Europe, and in Australia, Brasil, Canada and Mexico. The Company also has 18 parts distribution centers, many sales and service offices, and finance and administrative offices which are operated in owned or leased premises in these and other locations. Facilities for product testing and research and development are located in Washington state and the Netherlands. The Company's corporate headquarters is located in owned premises in Bellevue, Washington. The Company considers all of the properties used by its businesses to be suitable for their intended purposes.

The Company invests in facilities, equipment and processes to provide manufacturing and warehouse capacity to meet its customers' needs and improve operating performance.

The following summarizes the number of the Company's manufacturing plants and parts distribution centers by geographical location within indicated industry segments:

	U.S	Canada	Australia	Mexico	Europe	Central and So. America
Truck	4	1	1	1	3	1
Parts	6	2	2	1	5	2
Other	2	—	—	—	—	—

ITEM 3. LEGAL PROCEEDINGS.

On July 19, 2016, the European Commission (EC) concluded its investigation of all major European truck manufacturers and reached a settlement with DAF. Following the settlement, claims and lawsuits have been filed against the Company, DAF and certain DAF subsidiaries and other truck manufacturers. Others may bring EC related claims and lawsuits against the Company or its subsidiaries. While the Company believes it has meritorious defenses, such claims and lawsuits will likely take a significant period of time to resolve. An adverse outcome of such proceedings could have a material impact on the Company's results of operations.

The Company and its subsidiaries are parties to various other lawsuits incidental to the ordinary course of business. Management believes that the disposition of such lawsuits will not materially affect the Company's business or financial condition.

ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable.

PART II

ITEM MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND
5. ISSUER PURCHASES OF EQUITY SECURITIES.

(a) Market Information, Holders, Dividends, Securities Authorized for Issuance Under Equity Compensation Plans and Performance Graph.

Market Information, Holders and Dividends.

Common stock of the Company is traded on the NASDAQ Global Select Market under the symbol PCAR. The table below reflects the range of trading prices as reported by The NASDAQ Stock Market LLC and cash dividends declared. There were 1,587 record holders of the common stock at December 31, 2017.

QUARTER	2017			2016		
	DIVIDEND DECLARED	STOCK PRICE HIGH	STOCK PRICE LOW	DIVIDEND DECLARED	STOCK PRICE HIGH	STOCK PRICE LOW
First	\$.24	\$70.12	\$64.61	\$.24	\$55.60	\$43.46
Second	.25	69.17	61.93	.24	60.86	48.17
Third	.25	73.29	62.72	.24	60.75	49.35
Fourth	.25	75.68	66.33	.24	68.50	53.38
Year-End Extra	1.20			.60		

The Company expects to continue paying regular cash dividends, although there is no assurance as to future dividends because they are dependent upon future earnings, capital requirements and financial conditions.

Securities Authorized for Issuance Under Equity Compensation Plans.

The following table provides information as of December 31, 2017 regarding compensation plans under which PACCAR equity securities are authorized for issuance.

	Number of Securities		
	Granted and to be Issued on Exercise of Outstanding Options and Other Rights	Weighted-average Exercise Price of Outstanding Options	Securities Available for Future Grant
Stock compensation plans approved by stockholders	4,645,617	\$ 51.57	14,019,387

All stock compensation plans have been approved by the stockholders.

The number of securities to be issued includes those issuable under the PACCAR Inc Long Term Incentive Plan (LTI Plan) and the Restricted Stock and Deferred Compensation Plan for Non-Employee Directors (RSDC Plan). Securities to be issued include 377,676 shares that represent deferred cash awards payable in stock. The weighted-average exercise price does not include the securities that represent deferred cash awards.

Securities available for future grant are authorized under the following two plans: (i) 13,207,080 shares under the LTI Plan, and (ii) 812,307 shares under the RSDC Plan.

Stockholder Return Performance Graph.

The following line graph compares the yearly percentage change in the cumulative total stockholder return on the Company's common stock, to the cumulative total return of the Standard & Poor's Composite 500 Stock Index and the return of the industry peer groups of companies identified in the graph (the "Peer Group Index") for the last five fiscal years ended December 31, 2017. Standard & Poor's has calculated a return for each company in the Peer Group Index weighted according to its respective capitalization at the beginning of each period with dividends reinvested on a monthly basis. Management believes that the identified companies and methodology used in the graph for the Peer Group Index provide a better comparison than other indices available. The Peer Group Index consists of AGCO Corporation, Caterpillar Inc., Cummins Inc., Dana Incorporated, Deere & Company, Eaton Corporation, Meritor Inc., Navistar International Corporation, Oshkosh Corporation, AB Volvo and CNH Industrial N.V. CNH Industrial N.V. is included from September 30, 2013, when it began trading on the New York Stock Exchange. The comparison assumes that \$100 was invested December 31, 2012, in the Company's common stock and in the stated indices and assumes reinvestment of dividends.

	2012	2013	2014	2015	2016	2017
PACCAR Inc	100	134.90	159.43	116.19	160.79	184.60
S&P 500 Index	100	132.39	150.51	152.59	170.84	208.14
Peer Group Index	100	116.35	111.61	87.57	124.93	190.50

(b) Use of Proceeds from Registered Securities.

Not applicable.

(c) Purchases of Equity Securities by the Issuer and Affiliated Purchasers.

On September 23, 2015, the Company's Board of Directors approved a plan to repurchase up to \$300 million of the Company's outstanding common stock. As of December 31, 2017, the Company repurchased 4.1 million shares for \$206.7 million under this plan. There were no repurchases under this plan for the year ended December 31, 2017.

ITEM 6. SELECTED FINANCIAL DATA.

	2017	2016	2015	2014	2013
	(millions except per share data)				
Truck, Parts and Other Net Sales and Revenues	\$18,187.5	\$15,846.6	\$17,942.8	\$17,792.8	\$15,948.9
Financial Services Revenues	1,268.9	1,186.7	1,172.3	1,204.2	1,174.9
Total Revenues	\$19,456.4	\$17,033.3	\$19,115.1	\$18,997.0	\$17,123.8
Net Income	\$1,675.2	\$521.7	\$1,604.0	\$1,358.8	\$1,171.3
Adjusted Net Income *	\$1,501.8	\$1,354.7			
Net Income Per Share:					
Basic	4.76	1.49	4.52	3.83	3.31
Diluted	4.75	1.48	4.51	3.82	3.30
Adjusted Diluted *	4.26	3.85			
Cash Dividends Declared Per Share	2.19	1.56	2.32	1.86	1.70
Total Assets:					
Truck, Parts and Other	10,237.9	8,444.1	8,855.2	8,701.5	9,095.4
Financial Services	13,202.3	12,194.8	12,254.6	11,917.3	11,630.1
Truck, Parts and Other Long-Term Debt					150.0
Financial Services Debt	8,879.4	8,475.2	8,591.5	8,230.6	8,274.2
Stockholders' Equity	8,050.5	6,777.6	6,940.4	6,753.2	6,634.3

* See Reconciliation of GAAP to Non-GAAP Financial Measures for 2017 and 2016 on page 33, and see Note M on pages 63-65 and Note K on pages 58-59.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.
OVERVIEW:

PACCAR is a global technology company whose Truck segment includes the design and manufacture of high-quality light-, medium- and heavy-duty commercial trucks. In North America, trucks are sold under the Kenworth and Peterbilt nameplates, in Europe, under the DAF nameplate and in Australia and South America, under the Kenworth and DAF nameplates. The Parts segment includes the distribution of aftermarket parts for trucks and related commercial vehicles. The Company's Financial Services segment derives its earnings primarily from financing or leasing PACCAR products in North America, Europe and Australia. The Company's Other business includes the manufacturing and marketing of industrial winches.

2017 Financial Highlights

- Worldwide net sales and revenues were a record \$19.46 billion in 2017 compared to \$17.03 billion in 2016.
- Truck sales were \$14.77 billion in 2017 compared to \$12.77 billion in 2016, reflecting higher truck deliveries in the U.S. and Canada, Europe and Australia.
- Parts sales were a record \$3.33 billion in 2017 compared to \$3.01 billion in 2016 reflecting higher demand in all markets.
- Financial Services revenues were \$1.27 billion in 2017 compared to \$1.19 billion in 2016. The increase was primarily revenues from higher average operating lease assets.
- In 2017, PACCAR earned net income for the 79th consecutive year. Net income of \$1.68 billion (\$4.75 per diluted share) includes a one-time net tax benefit of \$173.4 million from the Tax Cuts and Jobs Act ("the Tax Act"). Excluding this one-time net benefit, the Company earned adjusted net income (non-GAAP) of \$1.50 billion (\$4.26 per diluted share) in 2017. The operating results in 2017 reflect higher truck deliveries and record worldwide Parts segment sales and profit, partially offset by lower Financial Services segment results. Net income in 2016 was \$521.7 million (\$1.48 per diluted share). Excluding the \$833.0 million non-recurring EC charge, the Company earned adjusted net income (non-GAAP) of \$1.35 billion (\$3.85 per diluted share) in 2016. See Reconciliation of GAAP to Non-GAAP Financial Measures on page 33.
- Capital investments were \$433.1 million in 2017 compared to \$402.7 million in 2016, reflecting additional investments in the Company's manufacturing facilities, new product development and enhanced aftermarket support.
- After-tax return on beginning equity (ROE) was 24.7% in 2017, which includes the one-time net tax benefit of \$173.4 million from the Tax Act. Excluding the one-time net benefit, adjusted ROE (non-GAAP) was 22.2% in 2017. This compares to an ROE of 7.5% in 2016. Excluding the EC charge, adjusted ROE (non-GAAP) was 19.5% in 2016. See Reconciliation of GAAP to Non-GAAP Financial Measures on page 33.
- Research and development (R&D) expenses were \$264.7 million in 2017 compared to \$247.2 million in 2016.

The Company opened the PACCAR Innovation Center in Sunnyvale, California in the third quarter of 2017. The advanced technology research and development center coordinates next-generation product development and identifies emerging technologies to enhance future vehicle performance. Technology areas of focus include advanced driver assistance systems, artificial intelligence, vehicle connectivity and powertrain electrification.

In the third quarter of 2017, the Company launched a new proprietary 12-speed automated transmission in North America, the lightest transmission for Class 8 on-highway vehicles. The PACCAR automated transmission is designed to complement the superior performance of PACCAR MX engines and PACCAR axles. The transmission reduces vehicle weight by up to 105 pounds, enhances low-speed maneuverability through excellent gear ratio

coverage, and contributes to increased customer uptime with its industry-leading 750,000 mile oil change interval.

The Company is constructing a new 160,000 square-foot Parts distribution center in Toronto, Canada. The \$35 million facility is expected to open in mid-2018. PACCAR Parts opened new distribution centers in Brisbane, Australia and Panama City, Panama during the fourth quarter of 2017.

The Company's Dynacraft division is constructing a new 130,000 square-foot manufacturing facility in McKinney, Texas to manufacture components and subassemblies such as battery cables, door assemblies and air conditioning assemblies for Kenworth and Peterbilt trucks. The facility will support Peterbilt's operations in Denton, Texas and manufacture PACCAR's new 20,000-pound front axle for Peterbilt and Kenworth Class 8 trucks.

The Company's Kenworth division will collaborate with the PACCAR Technical Center and the Company's DAF division to launch its U.S. Department of Energy (DOE) SuperTruck II program. The five-year project will utilize the Kenworth T680 with a 76-inch sleeper and the fuel-efficient PACCAR MX-13 engine with the goal to double Class 8 vehicle freight efficiency and achieve greenhouse gas emissions requirements effective in 2021, 2024 and 2027.

Beginning in the first quarter of 2018, the Company's DAF division will participate in a two-year truck platooning trial organized by the United Kingdom Department for Transport. The trial is organized to demonstrate that wirelessly-linked truck combinations, or platoons, can deliver improved efficiency to the transportation industry by lowering fuel consumption, reducing CO2 emissions, improving traffic flow and contributing to increased road safety.

Truck Outlook

Truck industry retail sales in the U.S. and Canada in 2018 are expected to be 235,000 to 265,000 units compared to 218,400 in 2017. In Europe, the 2018 truck industry registrations for over 16-tonne vehicles are expected to be 290,000 to 320,000 units compared to 306,100 in 2017. In South America, heavy-duty truck industry sales were 68,700 units in 2017 and in 2018 are estimated to be in a range of 65,000 to 75,000 units.

Parts Outlook

In 2018, PACCAR Parts sales are expected to grow 5-8% compared to 2017 sales.

Financial Services Outlook

Based on the truck market outlook, average earning assets in 2018 are expected to increase 2-4% compared to 2017. Current good levels of freight tonnage, freight rates and fleet utilization are contributing to customers' profitability and cash flow. If current freight transportation conditions decline due to weaker economic conditions, then past due accounts, truck repossessions and credit losses would likely increase from the current low levels and new business volume would likely decline.

Capital Spending and R&D Outlook

Capital investments in 2018 are expected to be \$425 to \$475 million, and R&D is expected to be \$280 to \$310 million. The Company is investing in new truck models, integrated powertrain, enhanced aerodynamic truck designs, advanced driver assistance and truck connectivity technologies, and expanded manufacturing and parts distribution facilities.

See the Forward-Looking Statements section of Management's Discussion and Analysis for factors that may affect these outlooks.

RESULTS OF OPERATIONS:

(\$ in millions, except per share amounts)				
Year Ended December 31,	2017	2016	2015	
Net sales and revenues:				
Truck	\$14,774.8	\$12,767.3	\$14,782.5	
Parts	3,327.0	3,005.7	3,060.1	
Other	85.7	73.6	100.2	
Truck, Parts and Other	18,187.5	15,846.6	17,942.8	
Financial Services	1,268.9	1,186.7	1,172.3	
	\$19,456.4	\$17,033.3	\$19,115.1	
Income (loss) before income taxes:				
Truck	\$1,296.9	\$1,125.8	\$1,440.3	
Parts	614.2	543.8	555.6	
Other*	(37.1)	(873.3)	(43.2)	
Truck, Parts and Other	1,874.0	796.3	1,952.7	
Financial Services	264.0	306.5	362.6	
Investment income	35.3	27.6	21.8	
Income taxes**	(498.1)	(608.7)	(733.1)	
Net Income	\$1,675.2	\$521.7	\$1,604.0	
Diluted earnings per share	\$4.75	\$1.48	\$4.51	
After-tax return on revenues	8.6 %	3.1 %	8.4 %	%
Adjusted after-tax return on revenues (non-GAAP)***	7.7 %	8.0 %	%	%

* In 2016, Other includes the EC charge of \$833.0 million.

** In 2017, Income Taxes include a one-time benefit of \$173.4 million from the Tax Act.

*** See Reconciliation of GAAP to non-GAAP Financial Measures on page 33.

The following provides an analysis of the results of operations for the Company's three reportable segments - Truck, Parts and Financial Services. Where possible, the Company has quantified the impact of factors identified in the following discussion and analysis. In cases where it is not possible to quantify the impact of factors, the Company lists them in estimated order of importance. Factors for which the Company is unable to specifically quantify the impact include market demand, fuel prices, freight tonnage and economic conditions affecting the Company's results of operations.

2017 Compared to 2016:

Truck

The Company's Truck segment accounted for 76% of revenue in 2017 compared to 75% in 2016.

The Company's new truck deliveries are summarized below:

Year Ended December 31,	2017	2016	% CHANGE
-------------------------	------	------	-------------

Edgar Filing: PACCAR INC - Form 10-K

U.S. and Canada	84,200	71,500	18
Europe	57,100	53,000	8
Mexico, South America, Australia and other	17,600	16,400	7
Total units	158,900	140,900	13

In 2017, industry retail sales in the heavy-duty market in the U.S. and Canada increased to 218,400 units from 215,700 units in 2016. The Company's heavy-duty truck retail market share increased to 30.7% in 2017 from 28.5% in 2016. The medium-duty market was 81,300 units in 2017 compared to 85,600 units in 2016. The Company's medium-duty market share was 17.1% in 2017 compared to 16.2% in 2016.

The over 16 tonne truck market in Europe in 2017 increased to 306,100 units from 302,500 units in 2016, and DAF's market share decreased to 15.3% in 2017 from 15.5% in 2016. The 6 to 16 tonne market in 2017 decreased to 52,600 units from 52,900 units in 2016. DAF market share in the 6 to 16-tonne market in 2017 increased to 10.5% from 10.1% in 2016.

The Company's worldwide truck net sales and revenues are summarized below:

(\$ in millions)

Year Ended December 31,	2017	2016	% CHANGE
Truck net sales and revenues:			
U.S. and Canada	\$8,775.2	\$7,363.5	19
Europe	4,254.9	3,863.0	10
Mexico, South America, Australia and other	1,744.7	1,540.8	13
	\$14,774.8	\$12,767.3	16
Truck income before income taxes	\$1,296.9	\$1,125.8	15
Pre-tax return on revenues	8.8	% 8.8	%

The Company's worldwide truck net sales and revenues increased to \$14.77 billion in 2017 from \$12.77 billion in 2016, primarily reflecting higher truck deliveries in the U.S. and Canada, Europe and Australia. Truck segment income before income taxes in 2017 reflects higher truck deliveries, while pre-tax return on revenues were unchanged at the higher volumes due to a lower gross margin percentage.

The major factors for the changes in net sales and revenues, cost of sales and revenues and gross margin between 2017 and 2016 for the Truck segment are as follows:

(\$ in millions)	NET SALES AND REVENUES	COST OF SALES AND REVENUES	GROSS MARGIN
2016	\$ 12,767.3	\$ 11,256.8	\$ 1,510.5
Increase (decrease)			
Truck delivery volume	1,841.9	1,559.7	282.2
Average truck sales prices	121.6		121.6
Average per truck material, labor and other direct costs		100.5	(100.5)
Factory overhead and other indirect costs		81.6	(81.6)
Operating leases	(28.1)	(25.2)	(2.9)
Currency translation	72.1	104.1	(32.0)
Total increase	2,007.5	1,820.7	186.8
2017	\$ 14,774.8	\$ 13,077.5	\$ 1,697.3

Truck delivery volume, which resulted in higher sales and cost of sales, primarily reflects higher truck deliveries in the U.S. and Canada (\$1,309.0 million sales and \$1,104.3 million cost of sales) and Europe (\$370.4 million sales and

\$312.2 million cost of sales).

▲ Average truck sales prices increased sales by \$121.6 million, primarily due to higher price realization in Europe (\$66.7 million) and the U.S. and Canada (\$66.2 million), partially offset by lower price realization in Mexico (\$12.5 million).

▲ Average cost per truck increased cost of sales by \$100.5 million, reflecting higher material costs.

▲ Factory overhead and other indirect costs increased \$81.6 million, primarily due to higher salaries and related expenses (\$38.9 million), higher maintenance costs (\$27.8 million) as well as higher depreciation expense (\$12.7 million).

○ Operating lease revenues decreased by \$28.1 million and cost of sales decreased by \$25.2 million, reflecting higher revenues deferred and lower revenues recognized.

◻ The currency translation effect on sales primarily reflects an increase in the value of the euro relative to the U.S. dollar, partially offset by a weaker British pound. The currency effect on cost of sales primarily reflects the stronger euro relative to the U.S. dollar.

◻ Truck gross margins decreased to 11.5% in 2017 from 11.8% in 2016 primarily due to the factors noted above.

16

Truck selling, general and administrative expenses (SG&A) for 2017 increased to \$206.5 million from \$202.5 million in 2016. The increase was primarily due to higher professional fees and salaries and related expenses, partially offset by lower sales and marketing expenses. As a percentage of sales, Truck SG&A decreased to 1.4% in 2017 from 1.6% in 2016 due to higher net sales.

Parts

The Company's Parts segment accounted for 17% of revenues in 2017 compared to 18% in 2016.

(\$ in millions)			
Year Ended December 31,	2017	2016	% CHANGE
Parts net sales and revenues:			
U.S. and Canada	\$2,175.0	\$1,932.7	13
Europe	801.0	761.8	5
Mexico, South America, Australia and other	351.0	311.2	13
	\$3,327.0	\$3,005.7	11
Parts income before income taxes	\$614.2	\$543.8	13
Pre-tax return on revenues	18.5	% 18.1	%

The Company's worldwide parts net sales and revenues increased to a record \$3.33 billion in 2017 from \$3.01 billion in 2016, due to higher aftermarket demand and successful marketing programs in all markets. The increase in Parts segment income before income taxes and pre-tax return on revenues in 2017 was primarily due to higher sales volume.

The major factors for the changes in net sales, cost of sales and gross margin between 2017 and 2016 for the Parts segment are as follows:

(\$ in millions)	NET SALES	COST OF SALES	GROSS MARGIN
2016	\$3,005.7	\$2,195.7	\$ 810.0
Increase (decrease)			
Aftermarket parts volume	270.0	183.6	86.4
Average aftermarket parts sales prices	45.9		45.9
Average aftermarket parts direct costs		37.5	(37.5)
Warehouse and other indirect costs		17.1	(17.1)
Currency translation	5.4	10.3	(4.9)
Total increase	321.3	248.5	72.8
2017	\$3,327.0	\$2,444.2	\$ 882.8

- ◆ Aftermarket parts sales volume increased by \$270.0 million and related cost of sales increased by \$183.6 million due to higher demand in all markets.
 - ◆ Average aftermarket parts sales prices increased sales by \$45.9 million, reflecting higher price realization in the U.S. and Canada and Europe.
 - ◆ Average aftermarket parts direct costs increased \$37.5 million due to higher material costs.
 - ◆ Warehouse and other indirect costs increased \$17.1 million, primarily due to higher salaries and related expenses to support the higher sales volume.
 - ◆ The currency translation effect on sales primarily reflects an increase in the value of the euro relative to the U.S. dollar, partially offset by a weaker British pound. The currency effect on cost of sales primarily reflects the stronger euro relative to the U.S. dollar.
 - ◆ Parts gross margins in 2017 decreased to 26.5% from 26.9% in 2016 due to the factors noted above.
- Parts SG&A expense for 2017 was \$195.0 million compared to \$191.7 million in 2016 primarily due to higher salaries and related expenses. As a percentage of sales, Parts SG&A was 5.9% in 2017, down from 6.4% in 2016, due to higher net sales.

Financial Services

The Company's Financial Services segment accounted for 7% of revenues in 2017 and 2016.

(\$ in millions)			
Year Ended December 31,	2017	2016	% CHANGE
New loan and lease volume:			
U.S. and Canada	\$2,450.7	\$2,474.9	(1)
Europe	1,107.7	1,104.8	
Mexico, Australia and other	769.7	643.7	20
	\$4,328.1	\$4,223.4	2
New loan and lease volume by product:			
Loans and finance leases	\$3,330.2	\$3,016.4	10
Equipment on operating lease	997.9	1,207.0	(17)
	\$4,328.1	\$4,223.4	2
New loan and lease unit volume:			
Loans and finance leases	33,500	31,000	8
Equipment on operating lease	9,700	12,000	(19)
	43,200	43,000	
Average earning assets:			
U.S. and Canada	\$7,351.9	\$7,454.0	(1)
Europe	2,937.7	2,673.2	10
Mexico, Australia and other	1,613.0	1,465.5	10
	\$11,902.6	\$11,592.7	3
Average earning assets by product:			
Loans and finance leases	\$7,407.5	\$7,287.2	2
Dealer wholesale financing	1,601.2	1,643.4	(3)
Equipment on lease and other	2,893.9	2,662.1	9
	\$11,902.6	\$11,592.7	3
Revenues:			
U.S. and Canada	\$734.0	\$690.3	6
Europe	306.8	287.1	7
Mexico, Australia and other	228.1	209.3	9
	\$1,268.9	\$1,186.7	7
Revenues by product:			
Loans and finance leases	\$375.2	\$369.9	1
Dealer wholesale financing	55.9	56.3	(1)
Equipment on lease and other	837.8	760.5	10
	\$1,268.9	\$1,186.7	7
Income before income taxes	\$264.0	\$306.5	(14)

New loan and lease volume was \$4.33 billion in 2017 compared to \$4.22 billion in 2016, primarily due to higher truck deliveries in 2017. PFS finance market share on new PACCAR truck sales was 24.9% in 2017 compared to 26.7% in 2016.

PFS revenues increased to \$1.27 billion in 2017 from \$1.19 billion in 2016. The increase was primarily due to higher average operating lease earning assets, and higher used truck sales, partially offset by unfavorable effects of currency translation, which decreased PFS revenues by \$.6 million in 2017.

PFS income before income taxes decreased to \$264.0 million in 2017 from \$306.5 million in 2016, primarily due to lower results on returned lease assets, higher borrowing rates, a higher provision for losses on receivables, and the effects of translating weaker foreign currencies to the U.S. dollar, partially offset by higher average earning asset balances. The currency exchange impact decreased PFS income before income taxes by \$1.2 million in 2017.

Included in Financial Services “Other Assets” on the Company’s Consolidated Balance Sheets are used trucks held for sale, net of impairments, of \$221.7 million at December 31, 2017 and \$267.2 million at December 31, 2016. These trucks are primarily units returned from matured operating leases in the ordinary course of business, and also includes trucks acquired from repossessions or through acquisitions of used trucks in trades related to new truck sales.

The Company recognized losses on used trucks, excluding repossessions, of \$45.1 million in 2017 compared to \$16.4 million in 2016, including losses on multiple unit transactions of \$29.2 million in 2017 compared to \$6.8 million in 2016. Used truck losses related to repossessions, which are recognized as credit losses, were \$5.1 million and \$3.4 million in 2017 and 2016, respectively.

The major factors for the changes in interest and fees, interest and other borrowing expenses and finance margin between 2017 and 2016 are outlined below:

	INTEREST AND OTHER		
	INTEREST AND FEES	BORROWING EXPENSES	FINANCE MARGIN
(\$ in millions)			
2016	\$ 426.2	\$ 127.2	\$ 299.0
Increase (decrease)			
Average finance receivables	2.3		2.3
Average debt balances		2.4	(2.4)
Yields	5.3		5.3
Borrowing rates		21.0	(21.0)
Currency translation	(2.7)	(1.0)	(1.7)
Total increase (decrease)	4.9	22.4	(17.5)
2017	\$ 431.1	\$ 149.6	\$ 281.5

▲Average finance receivables increased \$89.1 million (excluding foreign exchange effects) in 2017 as a result of retail portfolio new business volume exceeding collections.

▲Average debt balances increased \$130.6 million (excluding foreign exchange effects) in 2017. The higher average debt balances reflect funding for a higher average earning assets portfolio, which includes loans, finance leases, wholesale and equipment on operating lease.

♣Higher portfolio yields (4.81% in 2017 compared to 4.77% in 2016) increased interest and fees by \$5.3 million. The higher portfolio yields reflect higher lending volumes in North America which have higher market rates than Europe.

♣Higher borrowing rates (1.7% in 2017 compared to 1.5% in 2016) were primarily due to higher debt market rates in North America, partially offset by lower debt market rates in Europe.

♣The currency translation effects reflect a decline in the value of foreign currencies relative to the U.S. dollar, primarily the Mexican peso and the British pound, partially offset by a strengthening euro.

The following table summarizes operating lease, rental and other revenues and depreciation and other expenses:

Edgar Filing: PACCAR INC - Form 10-K

(\$ in millions)

Year Ended December 31,	2017	2016
Operating lease and rental revenues	\$784.6	\$720.5
Used truck sales and other	53.2	40.0
Operating lease, rental and other revenues	\$837.8	\$760.5
Depreciation of operating lease equipment	\$587.4	\$509.1
Vehicle operating expenses	99.6	92.1
Cost of used truck sales and other	40.5	34.0
Depreciation and other expenses	\$727.5	\$635.2

The major factors for the changes in operating lease, rental and other revenues, depreciation and other expenses and lease margin between 2017 and 2016 are outlined below:

(\$ in millions)	OPERATING LEASE, RENTAL AND OTHER REVENUES			DEPRECIATION AND OTHER EXPENSES		LEASE MARGIN
2016	\$	760.5		\$	635.2	\$ 125.3
Increase (decrease)						
Used truck sales		9.7			8.5	1.2
Results on returned lease assets					31.0	(31.0)
Average operating lease assets		56.5			47.9	8.6
Revenue and cost per asset		5.5			5.1	.4
Currency translation and other		5.6			(.2)	5.8
Total increase (decrease)		77.3			92.3	(15.0)
2017	\$	837.8		\$	727.5	\$ 110.3

▲ A higher volume of used truck sales increased operating lease, rental and other revenues by \$9.7 million and increased depreciation and other expenses by \$8.5 million.

✶ Results on returned lease assets increased depreciation and other expenses by \$31.0 million, primarily due to higher losses on sales of returned lease units.

▲ Average operating lease assets increased \$223.8 million (excluding foreign exchange effects), which increased revenues by \$56.5 million and related depreciation and other expenses by \$47.9 million.

✶ Revenue per asset increased \$5.5 million primarily due to higher rental income. Cost per asset increased \$5.1 million due to higher depreciation expense, partially offset by lower vehicle operating expenses.

✶ The currency translation effects reflect an increase in the value of foreign currencies, relative to the U.S. dollar, primarily the euro, partially offset by a weakening of the British pound.

The following table summarizes the provision for losses on receivables and net charge-offs:

(\$ in millions)	2017 PROVISION FOR LOSSES NET		2016 PROVISION FOR LOSSES NET	
	RECEIVABLES	CHARGE- OFFS	RECEIVABLES	CHARGE- OFFS
U.S. and Canada	\$ 13.7	\$ 14.5	\$ 14.0	\$ 14.7
Europe	1.4	1.4	.4	1.2
Mexico, Australia and other	7.2	5.5	4.0	3.3
	\$ 22.3	\$ 21.4	\$ 18.4	\$ 19.2

The provision for losses on receivables was \$22.3 million in 2017, an increase of \$3.9 million compared to 2016, reflecting higher portfolio balances in Mexico, Australia and other and Europe.

The Company modifies loans and finance leases as a normal part of its Financial Services operations. The Company may modify loans and finance leases for commercial reasons or for credit reasons. Modifications for commercial reasons are changes to contract terms for customers that are not considered to be in financial difficulty. Insignificant delays are modifications extending terms up to three months for customers experiencing some short-term financial stress, but not considered to be in financial difficulty. Modifications for credit reasons are changes to contract terms for customers considered to be in financial difficulty. The Company's modifications typically result in granting more time to pay the contractual amounts owed and charging a fee and interest for the term of the modification. When considering whether to modify customer accounts for credit reasons, the Company evaluates the creditworthiness of the customers and modifies those accounts that the Company considers likely to perform under the modified terms. When the Company modifies loans and finance leases for credit reasons and grants a concession, the modifications are classified as troubled debt restructurings (TDR).

The post-modification balance of accounts modified during the years ended December 31, 2017 and 2016 are summarized below:

	2017		2016	
	RECORDED OF TOTAL		RECORDED OF TOTAL	
(\$ in millions)	INVESTMENT PORTFOLIO*		INVESTMENT PORTFOLIO*	
Commercial	\$ 189.7	2.4 %	\$ 236.2	3.2 %
Insignificant delay	78.9	1.0 %	90.3	1.3 %
Credit - no concession	58.2	.8 %	51.9	.7 %
Credit - TDR	20.5	.3 %	31.6	.4 %
	\$ 347.3	4.5 %	\$ 410.0	5.6 %

*Recorded investment immediately after modification as a percentage of the year-end retail portfolio balance. In 2017, total modification activity decreased compared to 2016, reflecting lower volumes of refinancing for commercial reasons, primarily in the U.S. The decrease in modifications for insignificant delay reflects fewer fleet customers requesting payment relief for up to three months. Credit - TDR modifications decreased to \$20.5 million in 2017 from \$31.6 million in 2016 mainly due to the contract modifications for two fleet customers in 2016.

The following table summarizes the Company's 30+ days past due accounts:

At December 31,	2017	2016
Percentage of retail loan and lease accounts 30+ days past due:		
U.S. and Canada	.4 %	.3 %
Europe	.3 %	.5 %
Mexico, Australia and other	1.5 %	1.8 %
Worldwide	.5 %	.5 %

Accounts 30+ days past due were .5% at December 31, 2017 and December 31, 2016, reflecting lower past dues in Europe as well as Mexico, Australia and other, offset by an increase in the U.S. and Canada. The Company continues to focus on maintaining low past due balances.

When the Company modifies a 30+ days past due account, the customer is then generally considered current under the revised contractual terms. The Company modified \$.6 million and \$2.6 million of accounts worldwide during the fourth quarter of 2017 and the fourth quarter of 2016, respectively, which were 30+ days past due and became current at the time of modification. Had these accounts not been modified and continued to not make payments, the pro forma percentage of retail loan and lease accounts 30+ days past due would have been as follows:

At December 31,	2017	2016
Pro forma percentage of retail loan and lease accounts 30+ days past due:		
U.S. and Canada	.4 %	.3 %

Europe	.3	%	.5	%
Mexico, Australia and other	1.5	%	2.0	%
Worldwide	.5	%	.6	%

Modifications of accounts in prior quarters that were more than 30 days past due at the time of modification are included in past dues if they were not performing under the modified terms at December 31, 2017 and 2016. The effect on the allowance for credit losses from such modifications was not significant at December 31, 2017 and 2016.

The Company's 2017 and 2016 annualized pre-tax return on average earning assets for Financial Services was 2.2% and 2.6%, respectively. The decrease was due primarily to higher losses on used trucks in 2017.

Other

Other includes the winch business as well as sales, income and expenses not attributable to a reportable segment, including the EC charge and a portion of corporate expense. Other sales represent less than 1% of consolidated net sales and revenues for 2017 and 2016. Other SG&A was \$48.1 million in 2017 and \$46.6 million in 2016. The increase in other SG&A was primarily due to higher labor related costs.

Other income (loss) before tax was a loss of \$37.1 million in 2017 compared to a loss of \$873.3 million in 2016, which included the impact of the \$833.0 million EC charge.

Investment income increased to \$35.3 million in 2017 from \$27.6 million in 2016, primarily due to higher average U.S. portfolio balances and higher yields on U.S. investments due to higher market interest rates.

Income Taxes

In 2017, the effective tax rate was 22.9% compared to 53.8% in 2016. The lower rate is due to the 2017 one-time impact from the change in U.S. tax law as explained below, and the unfavorable 2016 impact of the one-time non-deductible expense of \$833.0 million for the EC charge.

On December 22, 2017, the U.S. enacted new federal income tax legislation, the Tax Cuts and Jobs Act (“the Tax Act”). The Tax Act lowered the U.S. statutory income tax rate from 35% to 21%, imposed a one-time transition tax on the Company’s foreign earnings, which previously, had been deferred from U.S. income tax and created a modified territorial system. As a result, the Company recorded a provisional amount of \$304.0 million of deferred tax benefits, due to the re-measurement of net deferred tax liabilities at the new lower statutory tax rate. In addition, the Company recorded a provisional amount of \$130.6 million of tax expense on the Company’s foreign earnings, which previously had been deferred from U.S. income tax. These provisional amounts may change in 2018, as new information becomes available, as the Tax Act continues to be interpreted and as new technical guidance is issued. Based on the Company’s current operations, the Company does not expect its future foreign earnings will be subject to significant U.S. federal income tax as a result of the new modified territorial system. The Company’s effective tax rate for 2018 is estimated at 23% to 25%, reflecting the reduced federal tax rate of 21% and other provisions of the Act.

(\$ in millions)				
Year Ended December 31,	2017		2016	
Domestic income before taxes	\$1,347.8		\$1,190.7	
Foreign income (loss) before taxes	825.5		(60.3)	
Total income before taxes	\$2,173.3		\$1,130.4	
Domestic pre-tax return on revenues	12.8	%	12.8	%
Foreign pre-tax return on revenues	9.2	%	(.8)	%
Total pre-tax return on revenues	11.2	%	6.6	%

In 2017, the improvement in domestic income before taxes was due to higher truck deliveries and improved aftermarket demand. Foreign income (loss) before taxes improved due to stronger truck and aftermarket demand as well as the 2016 impact of the \$833.0 million EC charge.

2016 Compared to 2015:

Truck

The Company’s Truck segment accounted for 75% of revenue in 2016 compared to 77% in 2015.

The Company’s new truck deliveries are summarized below:

Year Ended December 31,	2016	2015	% CHANGE
U.S. and Canada	71,500	91,300	(22)
Europe	53,000	47,400	12
Mexico, South America, Australia and other	16,400	16,000	3
Total units	140,900	154,700	(9)

In 2016, industry retail sales in the heavy-duty market in the U.S. and Canada decreased to 215,700 units from 278,400 units in 2015. The Company's heavy-duty truck retail market share increased to 28.5% in 2016 from 27.4% in 2015. The medium-duty market was 85,600 units in 2016 compared to 80,200 units in 2015. The Company's medium-duty market share was 16.2% in 2016 compared to 17.0% in 2015.

The over 16 tonne truck market in Europe in 2016 increased to 302,500 units from 269,100 units in 2015, and DAF's market share increased to 15.5% in 2016 from 14.6% in 2015. The 6 to 16 tonne market in 2016 increased to 52,900 units from 49,000 units in 2015. DAF market share in the 6 to 16-tonne market in 2016 increased to 10.1% from 9.0% in 2015.

The Company's worldwide truck net sales and revenues are summarized below:

(\$ in millions)			
Year Ended December 31,	2016	2015	% CHANGE
Truck net sales and revenues:			
U.S. and Canada	\$7,363.5	\$9,774.3	(25)
Europe	3,863.0	3,472.1	11
Mexico, South America, Australia and other	1,540.8	1,536.1	
	\$12,767.3	\$14,782.5	(14)
Truck income before income taxes	\$1,125.8	\$1,440.3	(22)
Pre-tax return on revenues	8.8	% 9.7	%

The Company's worldwide truck net sales and revenues decreased to \$12.77 billion in 2016 from \$14.78 billion in 2015, primarily due to lower truck deliveries in the U.S. and Canada, partially offset by higher truck deliveries in Europe. Truck segment income before income taxes and pre-tax return on revenues decreased in 2016, reflecting the lower truck unit deliveries and lower margins.

The major factors for the changes in net sales and revenues, cost of sales and revenues and gross margin between 2016 and 2015 for the Truck segment are as follows:

(\$ in millions)	NET SALES AND REVENUES	COST OF SALES AND REVENUES	GROSS MARGIN
2015	\$ 14,782.5	\$ 12,978.3	\$ 1,804.2
(Decrease) increase			
Truck delivery volume	(1,815.9)	(1,581.2)	(234.7)
Average truck sales prices	(147.8)		(147.8)
Average per truck material, labor and other direct costs		(110.5)	110.5
Factory overhead and other indirect costs		(35.6)	35.6
Operating leases	88.7	87.4	1.3
Currency translation	(140.2)	(81.6)	(58.6)
Total decrease	(2,015.2)	(1,721.5)	(293.7)
2016	\$ 12,767.3	\$ 11,256.8	\$ 1,510.5

Truck delivery volume reflects lower truck deliveries in the U.S. and Canada, which resulted in lower sales (\$2,276.0 million) and cost of sales (\$1,954.1 million), partially offset by higher truck deliveries in Europe which resulted in higher sales (\$413.3 million) and cost of sales (\$320.5 million).

Average truck sales prices decreased sales by \$147.8 million, primarily due to lower price realization in the U.S. and Canada (\$108.9 million) and Europe (\$26.3 million).

Average cost per truck decreased cost of sales by \$110.5 million, primarily due to lower material costs.

Factory overhead and other indirect costs decreased \$35.6 million, primarily due to lower salaries and related expense (\$24.7 million) and lower maintenance costs (\$18.3 million), partially offset by higher depreciation expense (\$8.3 million).

Operating lease revenues increased by \$88.7 million and cost of sales increased by \$87.4 million due to higher average asset balances.

The currency translation effect on sales and cost of sales reflects a decline in the value of foreign currencies relative to the U.S. dollar, primarily the British pound and the Canadian dollar.

Truck gross margins decreased to 11.8% in 2016 from 12.2% in 2015 due to the factors noted above.

Truck selling, general and administrative expenses (SG&A) for 2016 increased to \$202.5 million from \$192.6 million in 2015. The increase was primarily due to higher salaries and related expenses. As a percentage of sales, Truck SG&A increased to 1.6% in 2016 compared to 1.3% in 2015, reflecting the lower sales volume.

Parts

The Company's Parts segment accounted for 18% of revenues in 2016 compared to 16% in 2015.

(\$ in millions) Year Ended December 31,	2016	2015	% CHANGE
Parts net sales and revenues:			
U.S. and Canada	\$1,932.7	\$1,969.4	(2)
Europe	761.8	773.9	(2)
Mexico, South America, Australia and other	311.2	316.8	(2)
	\$3,005.7	\$3,060.1	(2)
Parts income before income taxes	\$543.8	\$555.6	(2)
Pre-tax return on revenues	18.1	% 18.2	%

The Company's worldwide parts net sales and revenues decreased to \$3.01 billion in 2016 from \$3.06 billion in 2015, primarily due to lower aftermarket demand in North America and the effect of translating weaker foreign currencies into the U.S. dollar. The decrease in Parts segment income before income taxes and pre-tax return on revenues in 2016 was primarily due to lower sales volume and margins in North America and the effect of translating weaker foreign currencies into the U.S. dollar.

The major factors for the changes in net sales, cost of sales and gross margin between 2016 and 2015 for the Parts segment are as follows:

(\$ in millions)	NET SALES	COST OF SALES	GROSS MARGIN
2015	\$3,060.1	\$2,232.4	\$ 827.7
(Decrease) increase			
Aftermarket parts volume	(43.0)	(28.9)	(14.1)
Average aftermarket parts sales prices	22.5		22.5
Average aftermarket parts direct costs		(4.1)	4.1
Warehouse and other indirect costs		8.5	(8.5)
Currency translation	(33.9)	(12.2)	(21.7)
Total decrease	(54.4)	(36.7)	(17.7)
2016	\$3,005.7	\$2,195.7	\$ 810.0

▲Aftermarket parts sales volume decreased by \$43.0 million and related cost of sales decreased by \$28.9 million, primarily due to lower market demand in North America.

▲Average aftermarket parts sales prices increased sales by \$22.5 million reflecting higher price realization in Europe.

▲Average aftermarket parts direct costs decreased \$4.1 million due to lower material costs.

▲Warehouse and other indirect costs increased \$8.5 million primarily due to start-up costs and higher depreciation expense for the new parts distribution center in Renton, Washington, and higher maintenance expense.

The currency translation effect on sales and cost of sales reflects a decline in the value of foreign currencies relative to the U.S. dollar, primarily the British pound.

Parts gross margins decreased to 26.9% in 2016 from 27.0% in 2015 due to the factors noted above.

Parts SG&A expense for 2016 was \$191.7 million compared to \$194.7 million in 2015. As a percentage of sales, Parts SG&A was 6.4% in 2016 and 2015, reflecting lower sales offset by ongoing cost control.

Financial Services

The Company's Financial Services segment accounted for 7% of revenues in 2016 compared to 6% in 2015.

(\$ in millions)			
Year Ended December 31,	2016	2015	% CHANGE
New loan and lease volume:			
U.S. and Canada	\$2,474.9	\$2,758.7	(10)
Europe	1,104.8	1,039.0	6
Mexico, Australia and other	643.7	639.5	1
	\$4,223.4	\$4,437.2	(5)
New loan and lease volume by product:			
Loans and finance leases	\$3,016.4	\$3,383.0	(11)
Equipment on operating lease	1,207.0	1,054.2	14
	\$4,223.4	\$4,437.2	(5)
New loan and lease unit volume:			
Loans and finance leases	31,000	33,300	(7)
Equipment on operating lease	12,000	10,700	12
	43,000	44,000	(2)
Average earning assets:			
U.S. and Canada	\$7,454.0	\$7,458.3	
Europe	2,673.2	2,512.9	6
Mexico, Australia and other	1,465.5	1,536.1	(5)
	\$11,592.7	\$11,507.3	1
Average earning assets by product:			
Loans and finance leases	\$7,287.2	\$7,239.9	1
Dealer wholesale financing	1,643.4	1,775.2	(7)
Equipment on lease and other	2,662.1	2,492.2	7
	\$11,592.7	\$11,507.3	1
Revenues:			
U.S. and Canada	\$690.3	\$675.5	2
Europe	287.1	278.6	3
Mexico, Australia and other	209.3	218.2	(4)
	\$1,186.7	\$1,172.3	1
Revenues by product:			
Loans and finance leases	\$369.9	\$384.7	(4)
Dealer wholesale financing	56.3	59.1	(5)
Equipment on lease and other	760.5	728.5	4
	\$1,186.7	\$1,172.3	1
Income before income taxes	\$306.5	\$362.6	(15)

New loan and lease volume was \$4.22 billion in 2016 compared to \$4.44 billion in 2015, primarily due to lower truck deliveries in the U.S. and Canada. PFS finance market share on new PACCAR truck sales was 26.7% in 2016 compared to 25.9% in 2015.

PFS revenues increased to \$1.19 billion in 2016 from \$1.17 billion in 2015. The increase was primarily due to higher average earning asset balances, partially offset by the effects of translating weaker foreign currencies to the U.S. dollar. The effects of currency translation lowered PFS revenues by \$27.1 million for 2016.

PFS income before income taxes decreased to \$306.5 million in 2016 from \$362.6 million in 2015, primarily due to lower results on returned lease assets, higher borrowing rates, the effects of translating weaker foreign currencies to the U.S. dollar and a higher provision for losses on receivables, partially offset by higher average earning asset balances. The effects of currency translation lowered PFS income before income taxes by \$9.7 million for 2016.

The major factors for the changes in interest and fees, interest and other borrowing expenses and finance margin between 2016 and 2015 are outlined below:

	INTEREST AND OTHER		
	INTEREST AND FEES	BORROWING EXPENSES	FINANCE MARGIN
(\$ in millions)			
2015	\$ 443.8	\$ 118.0	\$ 325.8
(Decrease) increase			
Average finance receivables	(2.2)		(2.2)
Average debt balances		(.2)	.2
Yields	(1.0)		(1.0)
Borrowing rates		13.7	(13.7)
Currency translation	(14.4)	(4.3)	(10.1)
Total (decrease) increase	(17.6)	9.2	(26.8)
2016	\$ 426.2	\$ 127.2	\$ 299.0

▲Average finance receivables decreased \$43.9 million (excluding foreign exchange effects) in 2016 as a result of lower dealer wholesale financing, partially offset by loans and finance leases and retail portfolio volume exceeding collections.

▲Average debt balances decreased \$9.0 million (excluding foreign exchange effects) in 2016. The lower average debt balances reflect lower funding requirements as the higher average earning asset portfolio (which includes loans, finance leases, wholesale and equipment on operating lease) was funded with retained equity.

▲Lower portfolio yields (4.91% in 2016 compared to 4.92% in 2015) decreased interest and fees by \$1.0 million. The lower portfolio yields reflect higher lending volumes in Europe at lower relative market rates.

▲Higher borrowing rates (1.5% in 2016 compared to 1.4% in 2015) were primarily due to higher debt market rates in North America, partially offset by lower debt market rates in Europe.

▲The currency translation effects reflect a decline in the value of foreign currencies relative to the U.S. dollar.

The following table summarizes operating lease, rental and other revenues and depreciation and other expenses:

(\$ in millions)	2016	2015
Year Ended December 31,		
Operating lease and rental revenues	\$720.5	\$691.6
Used truck sales and other	40.0	36.9
Operating lease, rental and other revenues	\$760.5	\$728.5
Depreciation of operating lease equipment	\$509.1	\$466.6
Vehicle operating expenses	92.1	90.7
Cost of used truck sales and other	34.0	26.4
Depreciation and other expenses	\$635.2	\$583.7

The major factors for the changes in operating lease, rental and other revenues, depreciation and other expenses and lease margin between 2016 and 2015 are outlined below:

(\$ in millions)	OPERATING LEASE, RENTAL AND OTHER REVENUES		DEPRECIATION AND OTHER EXPENSES	LEASE MARGIN
2015	\$ 728.5		\$ 583.7	\$ 144.8
Increase (decrease)				
Used truck sales	3.2		5.2	(2.0)
Results on returned lease assets			19.2	(19.2)
Average operating lease assets	29.2		24.0	5.2
Revenue and cost per asset	11.8		12.5	(.7)
Currency translation and other	(12.2)		(9.4)	(2.8)
Total increase (decrease)	32.0		51.5	(19.5)
2016	\$ 760.5		\$ 635.2	\$ 125.3

▲ higher volume of used truck sales increased operating lease, rental and other revenues by \$3.2 million. Depreciation and other expenses increased by \$5.2 million due to higher volume and impairments of used trucks reflecting lower used truck prices.

✱ Results on returned lease assets increased depreciation and other expenses by \$19.2 million, primarily due to gains on sales of returned lease units in 2015 versus losses in 2016.

▲ Average operating lease assets increased \$178.3 million in 2016 (excluding foreign exchange effects), which increased revenues by \$29.2 million and related depreciation and other expenses by \$24.0 million.

✱ Revenue per asset increased \$11.8 million, primarily due to higher rental rates in Europe, partially offset by lower rental utilization and fuel surcharge revenue. Cost per asset increased \$12.5 million, primarily due to higher depreciation expense in Europe.

✱ The currency translation effects reflect a decline in the value of foreign currencies relative to the U.S. dollar, primarily the Mexican peso and British pound.

The following table summarizes the provision for losses on receivables and net charge-offs:

(\$ in millions)	2016 PROVISION FOR LOSSES ON RECEIVABLES		2015 PROVISION FOR LOSSES ON RECEIVABLES	
	CHARGE	-OFFS	CHARGE	-OFFS
U.S. and Canada	\$ 14.0	\$ 14.7	\$ 7.7	\$ 4.6
Europe	.4	1.2	1.9	3.9
Mexico, Australia and other	4.0	3.3	2.8	4.6
	\$ 18.4	\$ 19.2	\$ 12.4	\$ 13.1

The provision for losses on receivables was \$18.4 million in 2016, an increase of \$6.0 million compared to 2015, reflecting higher losses in the oil and gas sector in the U.S. and Canada, partially offset by improved portfolio performance in Europe.

The Company modifies loans and finance leases as a normal part of its Financial Services operations. The Company may modify loans and finance leases for commercial reasons or for credit reasons. Modifications for commercial reasons are changes to contract terms for customers that are not considered to be in financial difficulty. Insignificant delays are modifications extending terms up to three months for customers experiencing some short-term financial stress, but not considered to be in financial difficulty. Modifications for credit reasons are changes to contract terms for customers considered to be in financial difficulty. The Company's modifications typically result in granting more time to pay the contractual amounts owed and charging a fee and interest for the term of the modification. When considering whether to modify customer accounts for credit reasons, the Company evaluates the creditworthiness of the customers and modifies those accounts that the Company considers likely to perform under the modified terms. When the Company modifies loans and finance leases for credit reasons and grants a concession, the modifications are classified as troubled debt restructurings (TDR).

The post-modification balance of accounts modified during the years ended December 31, 2016 and 2015 are summarized below:

	2016		2015	
	RECORDED OF TOTAL		RECORDED OF TOTAL	
(\$ in millions)	INVESTMENT PORTFOLIO*		INVESTMENT PORTFOLIO*	
Commercial	\$ 236.2	3.2 %	\$ 166.8	2.3 %
Insignificant delay	90.3	1.3 %	70.0	1.0 %
Credit - no concession	51.9	.7 %	36.6	.5 %
Credit - TDR	31.6	.4 %	44.4	.5 %
	\$ 410.0	5.6 %	\$ 317.8	4.3 %

*Recorded investment immediately after modification as a percentage of the year-end retail portfolio balance.

In 2016, total modification activity increased compared to 2015, primarily reflecting higher volume of refinancings for commercial reasons, including a contract modification for one large customer in the U.S. The increase in modifications for insignificant delay reflects more fleet customers requesting payment relief for up to three months. Credit - no concession modifications increased primarily due to extensions granted to one customer in Australia.

The following table summarizes the Company's 30+ days past due accounts:

At December 31,	2016	2015
Percentage of retail loan and lease accounts 30+ days past due:		
U.S. and Canada	.3 %	.3 %
Europe	.5 %	.7 %
Mexico, Australia and other	1.8 %	1.3 %
Worldwide	.5 %	.5 %

Accounts 30+ days past due were .5% at December 31, 2016 and 2015, reflecting lower past dues in Europe offset by higher past dues in Mexico. The Company continues to focus on maintaining low past due balances.

When the Company modifies a 30+ days past due account, the customer is then generally considered current under the revised contractual terms. The Company modified \$2.6 million of accounts worldwide during the fourth quarter of 2016 and the fourth quarter of 2015 which were 30+ days past due and became current at the time of modification. Had these accounts not been modified and continued to not make payments, the pro forma percentage of retail loan and lease accounts 30+ days past due would have been as follows:

At December 31,	2016	2015
Pro forma percentage of retail loan and lease accounts 30+ days past due:		

Edgar Filing: PACCAR INC - Form 10-K

U.S. and Canada	.3	%	.3	%
Europe	.5	%	.7	%
Mexico, Australia and other	2.0	%	1.6	%
Worldwide	.6	%	.6	%

Modifications of accounts in prior quarters that were more than 30 days past due at the time of modification are included in past dues if they were not performing under the modified terms at December 31, 2016 and 2015. The effect on the allowance for credit losses from such modifications was not significant at December 31, 2016 and 2015.

The Company's 2016 and 2015 annualized pre-tax return on average earning assets for Financial Services was 2.6% and 3.2%, respectively.

Other

Other includes the winch business as well as sales, income and expenses not attributable to a reportable segment, including the EC charge and a portion of corporate expense. Other sales represent less than 1% of consolidated net sales and revenues for 2016 and 2015. Other SG&A was \$46.6 million in 2016 and \$58.7 million in 2015. The decrease in SG&A was primarily due to lower salaries and related expenses and lower professional fees. Other income (loss) before tax was a loss of \$873.3 million in 2016 compared to a loss of \$43.2 million in 2015. The higher loss in 2016 was primarily due to the EC charge and lower pre-tax results from the winch business, which has been affected by lower oilfield related sales, partially offset by lower SG&A expense.

Investment income increased to \$27.6 million in 2016 from \$21.8 million in 2015, primarily due to higher yields on investments due to higher market interest rates and higher realized gains.

Income Taxes

In 2016, the effective tax rate increased to 53.8% from 31.4% in 2015, and substantially all of the difference in tax rates was due to the non-deductible expense of \$833.0 million for the EC charge in 2016.

(\$ in millions)			
Year Ended December 31,	2016	2015	
Domestic income before taxes	\$1,190.7	\$1,581.6	
Foreign (loss) income before taxes	(60.3)	755.5	
Total income before taxes	\$1,130.4	\$2,337.1	
Domestic pre-tax return on revenues	12.8 %	13.7 %	
Foreign pre-tax return on revenues	(.8)%	9.9 %	
Total pre-tax return on revenues	6.6 %	12.2 %	

In 2016, the decline in income before income taxes and return on revenues for domestic operations was primarily due to lower revenues from truck operations. In 2016, the EC charge of \$833.0 million resulted in a loss before income taxes and a negative return on revenues for foreign operations. Excluding the EC charge, foreign operations income before income taxes and return on revenues increased primarily due to higher revenues from European truck operations as a result of improved truck volumes and margins in Europe.

LIQUIDITY AND CAPITAL RESOURCES:

(\$ in millions)			
At December 31,	2017	2016	2015
Cash and cash equivalents	\$2,364.7	\$1,915.7	\$2,016.4
Marketable debt securities	1,367.1	1,140.9	1,448.1
	\$3,731.8	\$3,056.6	\$3,464.5

The Company's total cash and marketable debt securities at December 31, 2017 increased \$675.2 million from the balances at December 31, 2016, mainly due to an increase in cash and cash equivalents.

The change in cash and cash equivalents is summarized below:

(\$ in millions) Year Ended December 31,	2017	2016	2015
Operating activities:			
Net income	\$1,675.2	\$521.7	\$1,604.0
Net income items not affecting cash	999.5	1,072.7	910.9
Pension contributions	(70.6)	(185.7)	(62.9)
Changes in operating assets and liabilities, net	111.7	892.1	104.0
Net cash provided by operating activities	2,715.8	2,300.8	2,556.0
Net cash used in investing activities	(1,964.6)	(1,564.3)	(1,974.9)
Net cash used in financing activities	(393.8)	(823.5)	(196.5)
Effect of exchange rate changes on cash	91.6	(13.7)	(105.8)
Net increase (decrease) in cash and cash equivalents	449.0	(100.7)	278.8
Cash and cash equivalents at beginning of the year	1,915.7	2,016.4	1,737.6
Cash and cash equivalents at end of the year	\$2,364.7	\$1,915.7	\$2,016.4

2017 Compared to 2016:

Operating activities: Cash provided by operations increased by \$415.0 million to \$2.72 billion in 2017. Higher operating cash flows reflect higher net income of \$1.68 billion in 2017, compared to net income of \$521.7 million in 2016, which includes payment of the \$833.0 million EC charge. In addition, there were higher cash inflows of \$342.2 million from accounts payable and accrued expenses as purchases of goods and services exceeded payments. The higher cash inflows were offset by wholesale receivables on new trucks of \$673.6 million as originations exceeded cash receipts in 2017 (\$272.0 million) compared to cash receipts exceeding originations in 2016 (\$401.6 million). Additionally, there was a higher cash usage of \$214.0 million from inventory due to \$149.9 million in net inventory purchases in 2017 versus \$64.1 million in net inventory reductions in 2016. Finally, there was a higher cash outflow for payment of income taxes of \$160.0 million.

Investing activities: Cash used in investing activities increased by \$400.3 million to \$1.96 billion in 2017 from \$1.56 billion in 2016. Higher net cash used in investing activities reflects \$463.7 million in marketable debt securities as there was \$190.8 million in net purchases of marketable debt securities in 2017 compared to \$272.9 million in net proceeds from sales of marketable debt securities in 2016. In addition, there were higher net originations of retail loans and direct financing leases of \$87.0 million in 2017 compared to 2016. The outflows were partially offset by lower cash used in the acquisitions of equipment for operating leases of \$166.5 million.

Financing activities: Cash used in financing activities was \$393.8 million in 2017 compared to cash used in financing activities of \$823.5 million in 2016. The Company paid \$558.3 million in dividends in 2017 compared to \$829.3 million in 2016; the decrease of \$271.0 million was primarily due to a lower special dividend paid in January 2017 than the special dividend paid in January 2016. In 2016, the Company repurchased 1.4 million shares of common stock for \$70.5 million, while there were no stock repurchases in 2017. In 2017, the Company issued \$1.67 billion of term debt, increased its outstanding commercial paper and short-term bank loans by \$352.1 million and repaid term debt of \$1.90 billion. In 2016, the Company issued \$1.99 billion of term debt, repaid term debt of \$1.63 billion and reduced its outstanding commercial paper and short-term bank loans by \$322.8 million. This resulted in cash provided by borrowing activities of \$125.2 million in 2017, \$78.3 million higher than the cash provided by borrowing activities of \$46.9 million in 2016.

2016 Compared to 2015:

Operating activities: Cash provided by operations decreased by \$255.2 million to \$2.30 billion in 2016. Lower operating cash flows reflect lower net income of \$521.7 million in 2016, which includes payment of the \$833.0 million EC charge, and higher pension contributions of \$122.8 million. This was partially offset by \$675.0 million from Financial Services segment wholesale receivables, whereby cash receipts exceeded originations in 2016 (\$401.6 million) compared to originations exceeding cash receipts in 2015 (\$273.4 million). In addition, there was a lower cash outflow for payment of income taxes of \$281.4 million.

Investing activities: Cash used in investing activities decreased by \$410.6 million to \$1.56 billion in 2016 from \$1.97 billion in 2015. Lower net cash used in investing activities reflects \$567.2 million from marketable debt securities as there was \$272.9 million in net proceeds from sales of marketable debt securities in 2016 versus \$294.3 million in net purchases of marketable debt securities in 2015 and higher net originations of retail loans and direct financing leases of \$100.7 million. This was partially offset by higher cash used in the acquisitions of equipment for operating leases of \$151.2 million and higher payments for property, plant and equipment of \$88.5 million.

Financing activities: Cash used in financing activities was \$823.5 million in 2016 compared to cash used in financing activities of \$196.5 million in 2015. The Company paid \$829.3 million in dividends in 2016 compared to \$680.5 million in 2015; the increase of \$148.8 million was primarily due to an increase for the 2015 special dividend paid in January 2016. In 2016, the Company issued \$1.99 billion of term debt, repaid term debt of \$1.63 billion and reduced its outstanding commercial paper and short-term bank loans by \$322.8 million. In 2015, the Company issued \$1.99 billion of term debt, increased its outstanding commercial paper and short-term bank loans by \$250.7 million and repaid term debt of \$1.58 billion. This resulted in cash provided by borrowing activities of \$46.9 million in 2016, \$616.9 million lower than the cash provided by borrowing activities of \$663.8 million in 2015. The Company repurchased 1.4 million shares of common stock for \$70.5 million in 2016 compared to 3.8 million shares for \$201.6 million in 2015, a decline of \$131.1 million.

Credit Lines and Other:

The Company has line of credit arrangements of \$3.52 billion, of which \$3.31 billion were unused at December 31, 2017. Included in these arrangements are \$3.0 billion of syndicated bank facilities, of which \$1.0 billion expires in June 2018, \$1.0 billion expires in June 2021 and \$1.0 billion expires in June 2022. The Company intends to replace these credit facilities on or before expiration with facilities of similar amounts and duration. These credit facilities are maintained primarily to provide backup liquidity for commercial paper borrowings and maturing medium-term notes. There were no borrowings under the syndicated bank facilities for the year ended December 31, 2017.

On September 23, 2015, PACCAR's Board of Directors approved the repurchase of up to \$300.0 million of the Company's common stock, and as of December 31, 2017, \$206.7 million of shares have been repurchased pursuant to the 2015 authorization.

At December 31, 2017 and December 31, 2016, the Company had cash and cash equivalents and marketable debt securities of \$1.84 billion and \$1.33 billion, respectively, which are reinvested in foreign subsidiaries. The Company periodically repatriates foreign earnings. Dividends paid by foreign subsidiaries to the U.S. parent were nil, \$.33 billion and \$.24 billion in 2017, 2016 and 2015, respectively. The Company believes that its U.S. cash and cash equivalents and marketable debt securities, future operating cash flow and access to the capital markets, along with periodic repatriation of foreign earnings, will be sufficient to meet U.S. liquidity requirements.

Truck, Parts and Other

The Company provides funding for working capital, capital expenditures, R&D, dividends, stock repurchases and other business initiatives and commitments primarily from cash provided by operations. Management expects this method of funding to continue in the future.

Investments for property, plant and equipment in 2017 increased to \$425.7 million from \$394.6 million in 2016, reflecting additional investments in the Company's manufacturing facilities, new product development and enhanced aftermarket support. Over the past decade, the Company's combined investments in worldwide capital projects and R&D totaled \$6.11 billion, and have significantly increased the operating capacity and efficiency of its facilities and enhanced the quality and operating efficiency of the Company's premium products.

Capital investments in 2018 are expected to be \$425 to \$475 million, and R&D is expected to be \$280 to \$310 million. The Company is investing in PACCAR's new truck models, integrated powertrains, enhanced aerodynamic truck designs, advanced driver assistance and truck connectivity technologies, and expanded manufacturing and parts distribution facilities.

The Company conducts business in certain countries which have been experiencing or may experience significant financial stress, fiscal or political strain and are subject to the corresponding potential for default. The Company routinely monitors its financial exposure to global financial conditions, global counterparties and operating environments. As of December 31, 2017, the Company's exposures in such countries were insignificant.

Financial Services

The Company funds its financial services activities primarily from collections on existing finance receivables and borrowings in the capital markets. The primary sources of borrowings in the capital markets are commercial paper and medium-term notes issued in the public markets and, to a lesser extent, bank loans. An additional source of funds is loans from other PACCAR companies.

The Company issues commercial paper for a portion of its funding in its Financial Services segment. Some of this commercial paper is converted to fixed interest rate debt through the use of interest-rate swaps, which are used to manage interest-rate risk.

In November 2015, the Company's U.S. finance subsidiary, PACCAR Financial Corp. (PFC), filed a shelf registration under the Securities Act of 1933. The total amount of medium-term notes outstanding for PFC as of December 31, 2017 was \$4.45 billion. The registration expires in November 2018 and does not limit the principal amount of debt securities that may be issued during that period. PFC intends to renew the registration in 2018.

As of December 31, 2017, the Company's European finance subsidiary, PACCAR Financial Europe, had €1.34 billion available for issuance under a €2.50 billion medium-term note program listed on the Professional Securities Market of the London Stock Exchange. This program replaced an expiring program in the second quarter of 2017 and is renewable annually through the filing of new listing particulars.

In April 2016, PACCAR Financial Mexico registered a 10.00 billion peso medium-term note and commercial paper program with the Comision Nacional Bancaria y de Valores. The registration expires in April 2021 and limits the amount of commercial paper (up to one year) to 5.00 billion pesos. At December 31, 2017, 6.25 billion pesos were available for issuance.

In the event of a future significant disruption in the financial markets, the Company may not be able to issue replacement commercial paper. As a result, the Company is exposed to liquidity risk from the shorter maturity of short-term borrowings paid to lenders compared to the longer timing of receivable collections from customers. The Company believes its cash balances and investments, collections on existing finance receivables, syndicated bank lines and current investment-grade credit ratings of A+/A1 will continue to provide it with sufficient resources and access to capital markets at competitive interest rates and therefore contribute to the Company maintaining its liquidity and financial stability. A decrease in these credit ratings could negatively impact the Company's ability to access capital markets at competitive interest rates and the Company's ability to maintain liquidity and financial stability. PACCAR believes its Financial Services companies will be able to continue funding receivables, servicing debt and paying dividends through internally generated funds, access to public and private debt markets and lines of credit.

Commitments

The following summarizes the Company's contractual cash commitments at December 31, 2017:

	MATURITY				TOTAL
	WITHIN 1 YEAR	1-3 YEARS	3-5 YEARS	MORE THAN 5 YEARS	
(\$ in millions)					
Borrowings*	\$4,475.7	\$3,498.3	\$926.3		\$8,900.3
Purchase obligations	186.5	133.5	122.8		442.8
Interest on debt**	98.2	109.3	18.6		226.1
Operating leases	23.0	24.9	10.9	\$ 2.6	61.4
Other obligations	58.8	9.2	1.2	6.6	75.8
	\$4,842.2	\$3,775.2	\$1,079.8	\$ 9.2	\$9,706.4

*Commercial paper included in borrowings is at par value.

**Interest on floating-rate debt is based on the applicable market rates at December 31, 2017.

Total cash commitments for borrowings and interest on term debt are \$9.13 billion and were related to the Financial Services segment. As described in Note I of the consolidated financial statements, borrowings consist primarily of term notes and commercial paper issued by the Financial Services segment. The Company expects to fund its maturing Financial Services debt obligations principally from funds provided by collections from customers on loans and lease contracts, as well as from the proceeds of commercial paper and medium-term note borrowings. Purchase obligations are the Company's contractual commitments to acquire future production inventory and capital equipment. Other obligations include deferred cash compensation.

The Company's other commitments include the following at December 31, 2017:

	COMMITMENT EXPIRATION				TOTAL
	WITHIN 1 YEAR	1-3 YEARS	3-5 YEARS	MORE THAN 5 YEARS	
(\$ in millions)					
Loan and lease commitments	\$928.6				\$928.6
Residual value guarantees	287.8	\$479.4	\$134.0	\$8.6	909.8
Letters of credit	11.7	.5	.1	3.0	15.3
	\$1,228.1	\$479.9	\$134.1	\$11.6	\$1,853.7

Loan and lease commitments are for funding new retail loan and lease contracts. Residual value guarantees represent the Company's commitment to acquire trucks at a guaranteed value if the customer decides to return the truck at a specified date in the future.

RECONCILIATION OF GAAP TO NON-GAAP FINANCIAL MEASURES:

This Form 10-K includes "adjusted net income (non-GAAP)" and "adjusted net income per diluted share (non-GAAP)", which are financial measures that are not in accordance with U.S. generally accepted accounting principles ("GAAP"), since they exclude the one-time tax benefit from the Tax Cuts and Jobs Act ("the Tax Act") in 2017 and the non-recurring European Commission charge in 2016. These measures differ from the most directly comparable measures calculated in accordance with GAAP and may not be comparable to similarly titled non-GAAP financial measures used by other companies. In addition, the Form 10-K includes the financial ratios noted below calculated based on non-GAAP measures.

Management utilizes these non-GAAP measures to evaluate the Company's performance and believes these measures allow investors and management to evaluate operating trends by excluding significant non-recurring items that are not representative of underlying operating trends.

Reconciliations from the most directly comparable GAAP measures of: adjusted net income (non-GAAP) and adjusted net income per diluted share (non-GAAP) are as follows:

(\$ in millions, except per share amounts) Year Ended December 31,	2017	2016		
Net income	\$1,675.2	\$521.7		
One-time tax benefit from the Tax Act	(173.4)			
Non-recurring European Commission charge		833.0		
Adjusted net income (non-GAAP)	\$1,501.8	\$1,354.7		
Per diluted share:				
Net income	4.75	\$1.48		
One-time tax benefit from the Tax Act	(.49)			
Non-recurring European Commission charge		2.37		
Adjusted net income (non-GAAP)	\$4.26	\$3.85		
After-tax return on revenues	8.6	%	3.1	%
One-time tax benefit from the Tax Act	(.9)%		
Non-recurring European Commission charge			4.9	%
After-tax adjusted return on revenues (non-GAAP) *	7.7	%	8.0	%
After-tax return on beginning equity	24.7	%	7.5	%
One-time tax benefit from the Tax Act	(2.5)%		
Non-recurring European Commission charge			12.0	%
After-tax adjusted return on beginning equity (non-GAAP) *	22.2	%	19.5	%

* Calculated using adjusted net income.

	Three Months Ended
(\$ in millions, except per share amounts)	December 31, 2017
Net income	\$ 589.2
One-time tax benefit from the Tax Act	(173.4)
Adjusted net income (non-GAAP)	\$ 415.8

Per diluted share:	
Net income	\$ 1.67
One-time tax benefit from the Tax Act	(.49)
Adjusted net income (non-GAAP)	\$ 1.18

Shares used in diluted share calculations:	
GAAP	353.2
Non-GAAP	353.2

	Three Months Ended	Three Months Ended
(\$ in millions, except per share amounts)	March 31, 2016	June 30, 2016
Net (loss) income	\$(594.6)	\$481.3
Non-recurring European Commission charge	942.6	(109.6)
Adjusted net income (non-GAAP)	\$348.0	\$371.7

Per diluted share:		
Net (loss) income	\$(1.69)	\$1.37
Non-recurring European Commission charge	2.68	(.31)
Adjusted net income (non-GAAP)	\$.99	\$1.06

Shares used in diluted share calculations:		
GAAP	351.3	351.6
Non-GAAP	351.9	351.6

IMPACT OF ENVIRONMENTAL MATTERS:

The Company, its competitors and industry in general are subject to various domestic and foreign requirements relating to the environment. The Company believes its policies, practices and procedures are designed to prevent unreasonable risk of environmental damage and that its handling, use and disposal of hazardous or toxic substances have been in accordance with environmental laws and regulations in effect at the time such use and disposal occurred.

The Company is involved in various stages of investigations and cleanup actions in different countries related to environmental matters. In certain of these matters, the Company has been designated as a “potentially responsible party” by domestic and foreign environmental agencies. The Company has accrued the estimated costs to investigate and complete cleanup actions where it is probable that the Company will incur such costs in the future. Expenditures

related to environmental activities in the years ended December 31, 2017, 2016 and 2015 were \$1.9 million, \$2.2 million and \$2.0 million, respectively. Management expects that these matters will not have a significant effect on the Company's consolidated cash flow, liquidity or financial condition.

CRITICAL ACCOUNTING POLICIES:

The Company's significant accounting policies are disclosed in Note A of the consolidated financial statements. In the preparation of the Company's financial statements, in accordance with U.S. generally accepted accounting principles, management uses estimates and makes judgments and assumptions that affect asset and liability values and the amounts reported as income and expense during the periods presented. The following are accounting policies which, in the opinion of management, are particularly sensitive and which, if actual results are different from estimates used by management, may have a material impact on the financial statements.

Operating Leases

Trucks sold pursuant to agreements accounted for as operating leases are disclosed in Note E of the consolidated financial statements. In determining its estimate of the residual value of such vehicles, the Company considers the length of the lease term, the truck model, the expected usage of the truck and anticipated market demand. Operating lease terms generally range from three to five years. The resulting residual values on operating leases generally range between 30% and 60% of original equipment cost. If the sales price of the trucks at the end of the term of the agreement differs from the Company's estimated residual value, a gain or loss will result.

Future market conditions, changes in government regulations and other factors outside the Company's control could impact the ultimate sales price of trucks returned under these contracts. Residual values are reviewed regularly and adjusted if market conditions warrant. A decrease in the estimated equipment residual values would increase annual depreciation expense over the remaining lease term.

During 2017, market values on equipment returning upon operating lease maturity decreased, resulting in an increase in depreciation expense of \$41.2 million. During 2016, market values on equipment returning upon operating lease maturity decreased, resulting in an increase in depreciation expense of \$9.6 million. During 2015, market values on equipment returning upon operating lease maturity were generally higher than the residual values on the equipment, resulting in a reduction in depreciation expense of \$5.8 million.

At December 31, 2017, the aggregate residual value of equipment on operating leases in the Financial Services segment and residual value guarantee on trucks accounted for as operating leases in the Truck segment was \$2.73 billion. A 10% decrease in used truck values worldwide, if expected to persist over the remaining maturities of the Company's operating leases, would reduce residual value estimates and result in the Company recording an average of approximately \$78.1 million of additional depreciation per year.

Allowance for Credit Losses

The allowance for credit losses related to the Company's loans and finance leases is disclosed in Note D of the consolidated financial statements. The Company has developed a systematic methodology for determining the allowance for credit losses for its two portfolio segments, retail and wholesale. The retail segment consists of retail loans and direct and sales-type finance leases, net of unearned interest. The wholesale segment consists of truck inventory financing loans to dealers that are collateralized by trucks and other collateral. The wholesale segment generally has less risk than the retail segment. Wholesale receivables generally are shorter in duration than retail receivables, and the Company requires periodic reporting of the wholesale dealer's financial condition, conducts periodic audits of the trucks being financed and in many cases, obtains guarantees or other security such as dealership assets. In determining the allowance for credit losses, retail loans and finance leases are evaluated together since they relate to a similar customer base, their contractual terms require regular payment of principal and interest, generally over three to five years, and they are secured by the same type of collateral. The allowance for credit losses consists of both specific and general reserves.

The Company individually evaluates certain finance receivables for impairment. Finance receivables that are evaluated individually for impairment consist of all wholesale accounts and certain large retail accounts with past due balances or otherwise determined to be at a higher risk of loss. A finance receivable is impaired if it is considered probable the Company will be unable to collect all contractual interest and principal payments as scheduled. In addition, all retail loans and leases which have been classified as TDRs and all customer accounts over 90 days past due are considered impaired. Generally, impaired accounts are on non-accrual status. Impaired accounts classified as TDRs which have been performing for 90 consecutive days are placed on accrual status if it is deemed probable that the Company will collect all principal and interest payments.

Impaired receivables are generally considered collateral dependent. Large balance retail and all wholesale impaired receivables are individually evaluated to determine the appropriate reserve for losses. The determination of reserves for large balance impaired receivables considers the fair value of the associated collateral. When the underlying collateral fair value exceeds the Company's recorded investment, no reserve is recorded. Small balance impaired receivables with similar risk characteristics are evaluated as a separate pool to determine the appropriate reserve for losses using the historical loss information discussed below.

The Company evaluates finance receivables that are not individually impaired on a collective basis and determines the general allowance for credit losses for both retail and wholesale receivables based on historical loss information, using past due account data and current market conditions. Information used includes assumptions regarding the likelihood of collecting current and past due accounts, repossession rates, the recovery rate on the underlying collateral based on used truck values and other pledged collateral or recourse. The Company has developed a range of loss estimates for each of its country portfolios based on historical experience, taking into account loss frequency and severity in both strong and weak truck market conditions. A projection is made of the range of estimated credit losses inherent in the portfolio from which an amount is determined as probable based on current market conditions and other factors impacting the creditworthiness of the Company's borrowers and their ability to repay. After determining the appropriate level of the allowance for credit losses, a provision for losses on finance receivables is charged to income as necessary to reflect management's estimate of incurred credit losses, net of recoveries, inherent in the portfolio.

The adequacy of the allowance is evaluated quarterly based on the most recent past due account information and current market conditions. As accounts become past due, the likelihood that they will not be fully collected increases. The Company's experience indicates the probability of not fully collecting past due accounts ranges between 30% and 80%. Over the past three years, the Company's year-end 30+ days past due accounts were 0.5% of loan and lease receivables. Historically, a 100 basis point increase in the 30+ days past due percentage has resulted in an increase in credit losses of 8 to 38 basis points of receivables. At December 31, 2017, 30+ days past dues were 0.5%. If past dues were 100 basis points higher or 1.5% as of December 31, 2017, the Company's estimate of credit losses would likely have increased by a range of \$6 to \$30 million depending on the extent of the past dues, the estimated value of the collateral as compared to amounts owed and general economic factors.

Product Warranty

Product warranty is disclosed in Note H of the consolidated financial statements. The expenses related to product warranty are estimated and recorded at the time products are sold based on historical and current data and reasonable expectations for the future regarding the frequency and cost of warranty claims, net of recoveries. Management takes actions to minimize warranty costs through quality-improvement programs; however, actual claim costs incurred could materially differ from the estimated amounts and require adjustments to the reserve. Historically those adjustments have not been material. Over the past three years, warranty expense as a percentage of Truck, Parts and Other net sales and revenues has ranged between 1.3% and 1.4%. If the 2017 warranty expense had been .2% higher as a percentage of net sales and revenues in 2017, warranty expense would have increased by approximately \$36 million.

Income Taxes

Income taxes are disclosed in Note M of the consolidated financial statements. The Company calculates income tax expense on pre-tax income based on current tax law. Deferred tax assets and liabilities are recorded for future tax consequences on temporary differences between recorded amounts in the financial statements and their respective tax basis. The determination of income tax expense requires management estimates and judgement regarding the future outcomes of tax law issues included in tax returns and jurisdictional mix of earnings. The Company updates its assumptions on all of these factors each quarter as well as new information on tax laws and differences between estimated taxes and actual returns when filed. If the Company's assessment of these matters changes, the effect is accounted for in earnings in the period the change is made.

FORWARD-LOOKING STATEMENTS:

This report contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include statements relating to future results of operations or financial position and

any other statement that does not relate to any historical or current fact. Such statements are based on currently available operating, financial and other information and are subject to risks and uncertainties that may affect actual results. Risks and uncertainties include, but are not limited to: a significant decline in industry sales; competitive pressures; reduced market share; reduced availability of or higher prices for fuel; increased safety, emissions, or other regulations resulting in higher costs and/or sales restrictions; currency or commodity price fluctuations; lower used truck prices; insufficient or under-utilization of manufacturing capacity; supplier interruptions; insufficient liquidity in the capital markets; fluctuations in interest rates; changes in the levels of the Financial Services segment new business volume due to unit fluctuations in new PACCAR truck sales or reduced market shares; changes affecting the profitability of truck owners and operators; price changes impacting truck sales prices and residual values; insufficient supplier capacity or access to raw materials; labor disruptions; shortages of commercial truck drivers; increased warranty costs; litigation, including EC-related claims; or legislative and governmental regulations. A more detailed description of these and other risks is included under the heading Part 1, Item 1A, "Risk Factors" in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Currencies are presented in millions for the market risks and derivative instruments sections below.

Interest-Rate Risks - See Note O for a description of the Company's hedging programs and exposure to interest rate fluctuations. The Company measures its interest-rate risk by estimating the amount by which the fair value of interest-rate sensitive assets and liabilities, including derivative financial instruments, would change assuming an immediate 100 basis point increase across the yield curve as shown in the following table:

Fair Value Gains (Losses)	2017	2016
CONSOLIDATED:		
Assets		
Cash equivalents and marketable debt securities	\$(21.0)	\$(20.0)
FINANCIAL SERVICES:		
Assets		
Fixed rate loans	(69.7)	(68.3)
Liabilities		
Fixed rate term debt	99.1	95.0
Interest-rate swaps	15.0	4.8
Total	\$23.4	\$11.5

Currency Risks - The Company enters into foreign currency exchange contracts to hedge its exposure to exchange rate fluctuations of foreign currencies, particularly the Canadian dollar, the euro, the British pound, the Australian dollar, the Brazilian real and the Mexican peso (see Note O for additional information concerning these hedges). Based on the Company's sensitivity analysis, the potential loss in fair value for such financial instruments from a 10% unfavorable change in quoted foreign currency exchange rates would be a loss of \$55.7 related to contracts outstanding at December 31, 2017, compared to a loss of \$31.5 at December 31, 2016. These amounts would be largely offset by changes in the values of the underlying hedged exposures.

ITEM 8. FINANCIAL STATEMENTS AND
SUPPLEMENTARY DATA.
CONSOLIDATED STATEMENTS OF INCOME

Year Ended December 31,	2017	2016	2015
	(millions, except per share data)		
TRUCK, PARTS AND OTHER:			
Net sales and revenues	\$18,187.5	\$15,846.6	\$17,942.8
Cost of sales and revenues	15,593.7	13,517.7	15,292.1
Research and development	264.7	247.2	239.8
Selling, general and administrative	449.5	440.8	445.9
European Commission charge		833.0	
Interest and other expense, net	5.6	11.6	12.3
	16,313.5	15,050.3	15,990.1
Truck, Parts and Other Income Before Income Taxes	1,874.0	796.3	1,952.7
FINANCIAL SERVICES:			
Interest and fees	431.1	426.2	443.8
Operating lease, rental and other revenues	837.8	760.5	728.5
Revenues	1,268.9	1,186.7	1,172.3
Interest and other borrowing expenses	149.6	127.2	118.0
Depreciation and other expenses	727.5	635.2	583.7
Selling, general and administrative	105.5	99.4	95.6
Provision for losses on receivables	22.3	18.4	12.4
	1,004.9	880.2	809.7
Financial Services Income Before Income Taxes	264.0	306.5	362.6
Investment income	35.3	27.6	21.8
Total Income Before Income Taxes	2,173.3	1,130.4	2,337.1
Income taxes	498.1	608.7	733.1
Net Income	\$1,675.2	\$521.7	\$1,604.0
Net Income Per Share			
Basic	\$4.76	\$1.49	\$4.52
Diluted	\$4.75	\$1.48	\$4.51
Weighted Average Number of Common Shares Outstanding			
Basic	351.9	351.1	354.6
Diluted	352.9	351.8	355.6

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Year Ended December 31,	2017	2016	2015
	(millions)		
Net income	\$1,675.2	\$521.7	\$1,604.0
Other comprehensive income (loss):			
Unrealized (losses) gains on derivative contracts			
Net (loss) gain arising during the period	(125.5)	(6.5)	38.7
Tax effect	33.9	6.7	(10.8)
Reclassification adjustment	133.4	10.8	(29.3)
Tax effect	(36.3)	(8.9)	8.5
	5.5	2.1	7.1
Unrealized (losses) gains on marketable debt securities			
Net holding loss	(1.5)	(.1)	(2.3)
Tax effect	.4	.4	.6
Reclassification adjustment	(.6)	(3.7)	(2.1)
Tax effect	.2	1.0	.6
	(1.5)	(2.4)	(3.2)
Pension plans			
Net gain (loss) arising during the period	37.1	(50.3)	17.7
Tax effect	(16.7)	7.7	(2.6)
Reclassification adjustment	26.6	28.9	42.4
Tax effect	(8.5)	(10.0)	(14.8)
	38.5	(23.7)	42.7
Foreign currency translation gain (loss)	292.0	(87.1)	(483.8)
Net other comprehensive income (loss)	334.5	(111.1)	(437.2)
Comprehensive Income	\$2,009.7	\$410.6	\$1,166.8

See notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

December 31,	2017	2016
	(millions)	
ASSETS		
TRUCK, PARTS AND OTHER:		
Current Assets		
Cash and cash equivalents	\$2,254.8	\$1,781.7
Trade and other receivables, net	1,127.9	862.2
Marketable debt securities	1,367.1	1,140.9
Inventories, net	928.4	727.8
Other current assets	404.4	225.6
Total Truck, Parts and Other Current Assets	6,082.6	4,738.2
Equipment on operating leases, net	1,265.7	1,013.9
Property, plant and equipment, net	2,464.4	2,260.0
Other noncurrent assets, net	425.2	432.0
Total Truck, Parts and Other Assets	10,237.9	8,444.1
FINANCIAL SERVICES:		
Cash and cash equivalents	109.9	134.0
Finance and other receivables, net	9,697.1	8,837.4
Equipment on operating leases, net	2,876.3	2,623.9
Other assets	519.0	599.5
Total Financial Services Assets	13,202.3	12,194.8
	\$23,440.2	\$20,638.9

CONSOLIDATED BALANCE SHEETS

December 31,	2017	2016
	(millions)	
LIABILITIES AND STOCKHOLDERS' EQUITY		
TRUCK, PARTS AND OTHER:		
Current Liabilities		
Accounts payable, accrued expenses and other	\$2,569.5	\$2,034.1
Dividend payable	422.1	210.4
Total Truck, Parts and Other Current Liabilities	2,991.6	2,244.5
Residual value guarantees and deferred revenues	1,339.0	1,072.6
Other liabilities	939.8	739.1
Total Truck, Parts and Other Liabilities	5,270.4	4,056.2
FINANCIAL SERVICES:		
Accounts payable, accrued expenses and other	466.2	395.0
Commercial paper and bank loans	2,933.9	2,447.5
Term notes	5,945.5	6,027.7
Deferred taxes and other liabilities	773.7	934.9
Total Financial Services Liabilities	10,119.3	9,805.1
STOCKHOLDERS' EQUITY:		
Preferred stock, no par value - authorized 1.0 million shares, none issued		
Common stock, \$1 par value - authorized 1.2 billion shares;		
issued 351.8 million and 350.7 million shares	351.8	350.7
Additional paid-in capital	123.2	70.1
Retained earnings	8,369.1	7,484.9
Accumulated other comprehensive loss	(793.6)	(1,128.1)
Total Stockholders' Equity	8,050.5	6,777.6
	\$23,440.2	\$20,638.9

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Year Ended December 31,	2017	2016	2015
	(millions)		
OPERATING ACTIVITIES:			
Net Income	\$1,675.2	\$521.7	\$1,604.0
Adjustments to reconcile net income to cash provided by operations:			
Depreciation and amortization:			
Property, plant and equipment	321.4	302.4	292.2
Equipment on operating leases and other	786.1	690.7	614.9
Provision for losses on financial services receivables	22.3	18.4	12.4
Deferred taxes	(173.9)	30.9	(55.2)
Other, net	43.6	30.3	46.6
Pension contributions	(70.6)	(185.7)	(62.9)
Change in operating assets and liabilities:			
(Increase) decrease in assets other than cash and cash equivalents:			
Receivables:			
Trade and other receivables	(207.2)	(61.8)	105.3
Wholesale receivables on new trucks	(272.0)	401.6	(273.4)
Sales-type finance leases and dealer direct loans on new trucks	71.9	116.1	(6.6)
Inventories	(149.9)	64.1	64.3
Other assets, net	131.4	41.0	(125.1)
Increase (decrease) in liabilities:			
Accounts payable and accrued expenses	333.6	(8.6)	(162.6)
Residual value guarantees and deferred revenues	166.3	155.9	242.0
Other liabilities, net	37.6	183.8	260.1
Net Cash Provided by Operating Activities	2,715.8	2,300.8	2,556.0
INVESTING ACTIVITIES:			
Originations of retail loans and direct financing leases	(3,116.8)	(2,825.9)	(3,064.5)
Collections on retail loans and direct financing leases	2,713.7	2,509.8	2,681.9
Net decrease (increase) in wholesale receivables on used equipment	5.2	9.5	(24.7)
Purchases of marketable debt securities	(970.3)	(1,031.9)	(1,329.8)
Proceeds from sales and maturities of marketable debt securities	779.5	1,304.8	1,035.5
Payments for property, plant and equipment	(423.4)	(375.2)	(286.7)
Acquisitions of equipment for operating leases	(1,423.2)	(1,589.7)	(1,438.5)
Proceeds from asset disposals	470.7	433.8	448.8
Other, net		.5	3.1
Net Cash Used in Investing Activities	(1,964.6)	(1,564.3)	(1,974.9)
FINANCING ACTIVITIES:			
Payments of cash dividends	(558.3)	(829.3)	(680.5)
Purchases of treasury stock		(70.5)	(201.6)
Proceeds from stock compensation transactions	39.3	29.4	21.8
Net increase (decrease) in commercial paper and short-term bank loans	352.1	(322.8)	250.7
Proceeds from term debt	1,670.2	1,994.8	1,993.2
Payments on term debt	(1,897.1)	(1,625.1)	(1,580.1)

Edgar Filing: PACCAR INC - Form 10-K

Net Cash Used in Financing Activities	(393.8)	(823.5)	(196.5)
Effect of exchange rate changes on cash	91.6	(13.7)	(105.8)
Net Increase (Decrease) in Cash and Cash Equivalents	449.0	(100.7)	278.8
Cash and cash equivalents at beginning of year	1,915.7	2,016.4	1,737.6
Cash and cash equivalents at end of year	\$2,364.7	\$1,915.7	\$2,016.4

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

December 31,	2017	2016	2015
	(millions, except per share data)		
COMMON STOCK, \$1 PAR VALUE:			
Balance at beginning of year	\$350.7	\$351.3	\$355.2
Treasury stock retirement		(1.4)	(4.6)
Stock compensation	1.1	.8	.7
Balance at end of year	351.8	350.7	351.3
ADDITIONAL PAID-IN CAPITAL:			
Balance at beginning of year	70.1	69.3	156.7
Treasury stock retirement		(43.4)	(128.5)
Stock compensation and tax benefit	53.1	44.2	41.1
Balance at end of year	123.2	70.1	69.3
TREASURY STOCK, AT COST:			
Balance at beginning of year			(42.7)
Purchases, shares: 2017 - nil; 2016 - 1.38; 2015 - 3.85		(70.5)	(201.6)
Retirements		70.5	244.3
Balance at end of year			
RETAINED EARNINGS:			
Balance at beginning of year	7,484.9	7,536.8	6,863.8
Net income	1,675.2	521.7	1,604.0
Cash dividends declared on common stock,			
per share: 2017 - \$2.19; 2016 - \$1.56; 2015 - \$2.32	(771.1)	(547.9)	(819.8)
Treasury stock retirement		(25.7)	(111.2)
Cumulative effect of change in accounting principle	(19.9)		
Balance at end of year	8,369.1	7,484.9	7,536.8
ACCUMULATED OTHER COMPREHENSIVE LOSS:			
Balance at beginning of year	(1,128.1)	(1,017.0)	(579.8)
Other comprehensive income (loss)	334.5	(111.1)	(437.2)
Balance at end of year	(793.6)	(1,128.1)	(1,017.0)
Total Stockholders' Equity	\$8,050.5	\$6,777.6	\$6,940.4

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

A. SIGNIFICANT ACCOUNTING POLICIES

Description of Operations: PACCAR Inc (the Company or PACCAR) is a multinational company operating in three principal segments: (1) the Truck segment includes the design and manufacture of high-quality, light-, medium- and heavy-duty commercial trucks; (2) the Parts segment includes the distribution of aftermarket parts for trucks and related commercial vehicles; and (3) the Financial Services segment (PFS) includes finance and leasing products and services provided to customers and dealers. PACCAR's finance and leasing activities are principally related to PACCAR products and associated equipment. PACCAR's sales and revenues are derived primarily from North America and Europe. The Company also operates in Australia and Brasil and sells trucks and parts to customers in Asia, Africa, Middle East and South America.

Principles of Consolidation: The consolidated financial statements include the accounts of the Company and its wholly owned domestic and foreign subsidiaries. All significant intercompany accounts and transactions are eliminated in consolidation.

Use of Estimates: The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Revenue Recognition:

Truck, Parts and Other: Substantially all sales and revenues of trucks and related aftermarket parts are recorded by the Company when products are shipped to dealers or customers, except for certain truck shipments that are subject to a residual value guarantee to the customer. Revenues related to these shipments are generally recognized on a straight-line basis over the guarantee period (see Note E). At the time certain truck and parts sales to a dealer are recognized, the Company records an estimate of any future sales incentive costs related to such sales. The estimate is based on historical data and announced incentive programs. In the Truck and Parts segments, the Company grants extended payment terms on selected receivables. Interest is charged for the period beyond standard payment terms. Interest income is recorded as earned.

Financial Services: Interest income from finance and other receivables is recognized using the interest method. Certain loan origination costs are deferred and amortized to interest income over the expected life of the contracts, generally 36 to 60 months, using the straight-line method which approximates the interest method. For operating leases, rental revenue is recognized on a straight-line basis over the lease term. Rental revenues for the years ended December 31, 2017, 2016 and 2015 were \$760.9, \$698.9 and \$668.6, respectively. Depreciation and related leased unit operating expenses were \$665.7, \$581.7 and \$536.2 for the years ended December 31, 2017, 2016 and 2015, respectively.

Recognition of interest income and rental revenue is suspended (put on non-accrual status) when the receivable becomes more than 90 days past the contractual due date or earlier if some other event causes the Company to determine that collection is not probable. Accordingly, no finance receivables more than 90 days past due were accruing interest at December 31, 2017 or December 31, 2016. Recognition is resumed if the receivable becomes current by the payment of all amounts due under the terms of the existing contract and collection of remaining amounts is considered probable (if not contractually modified) or if the customer makes scheduled payments for three

months and collection of remaining amounts is considered probable (if contractually modified). Payments received while the finance receivable is on non-accrual status are applied to interest and principal in accordance with the contractual terms.

Cash and Cash Equivalents: Cash equivalents consist of liquid investments with a maturity at date of purchase of 90 days or less.

Marketable Debt Securities: The Company's investments in marketable debt securities are classified as available-for-sale. These investments are stated at fair value with any unrealized gains or losses, net of tax, included as a component of accumulated other comprehensive income (loss) (AOCI).

The Company utilizes third-party pricing services for all of its marketable debt security valuations. The Company reviews the pricing methodology used by the third party pricing services, including the manner employed to collect market information. On a quarterly basis, the Company also performs review and validation procedures on the pricing information received from the third party providers. These procedures help ensure that the fair value information used by the Company is determined in accordance with applicable accounting guidance.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The Company evaluates its investment in marketable debt securities at the end of each reporting period to determine if a decline in fair value is other-than-temporary. Realized losses are recognized upon management's determination that a decline in fair value is other-than-temporary. The determination of other-than-temporary impairment is a subjective process, requiring the use of judgments and assumptions regarding the amount and timing of recovery. The Company reviews and evaluates its investments at least quarterly to identify investments that have indications of other-than-temporary impairments. It is reasonably possible that a change in estimate could occur in the near term relating to other-than-temporary impairment. Accordingly, the Company considers several factors when evaluating debt securities for other-than-temporary impairment, including whether the decline in fair value of the security is due to increased default risk for the specific issuer or market interest rate risk.

In assessing default risk, the Company considers the collectability of principal and interest payments by monitoring changes to issuers' credit ratings, specific credit events associated with individual issuers as well as the credit ratings of any financial guarantor, and the extent and duration to which amortized cost exceeds fair value.

In assessing market interest rate risk, including benchmark interest rates and credit spreads, the Company considers its intent for selling the securities and whether it is more likely than not the Company will be able to hold these securities until the recovery of any unrealized losses.

Receivables:

Trade and Other Receivables: The Company's trade and other receivables are recorded at cost, net of allowances. At December 31, 2017 and 2016, respectively, trade and other receivables include trade receivables from dealers and customers of \$962.0 and \$734.6 and other receivables of \$165.9 and \$127.6 relating primarily to value added tax receivables and supplier allowances and rebates.

Finance and Other Receivables:

Loans – Loans represent fixed or floating-rate loans to customers collateralized by the vehicles purchased and are recorded at amortized cost.

Finance leases – Finance leases are retail direct financing leases and sales-type finance leases, which lease equipment to retail customers and dealers. These leases are reported as the sum of minimum lease payments receivable and estimated residual value of the property subject to the contracts, reduced by unearned interest which is shown separately.

Dealer wholesale financing – Dealer wholesale financing is floating-rate wholesale loans to PACCAR dealers for new and used trucks and are recorded at amortized cost. The loans are collateralized by the trucks being financed.

Operating lease receivables and other – Operating lease receivables and other include monthly rentals due on operating leases, unamortized loan and lease origination costs, interest on loans and other amounts due within one year in the normal course of business.

Allowance for Credit Losses:

Truck, Parts and Other: The Company historically has not experienced significant losses or past due amounts on trade and other receivables in its Truck, Parts and Other businesses. Accounts are considered past due once the unpaid balance is over 30 days outstanding based on contractual payment terms. Accounts are charged-off against the allowance for credit losses when, in the judgment of management, they are considered uncollectible. The allowance for credit losses for Truck, Parts and Other was \$1.5 and \$1.7 for the years ended December 31, 2017 and 2016, respectively. Net charge-offs were \$.1, \$.1 and \$.3 for the years ended December 31, 2017, 2016 and 2015, respectively.

Financial Services: The Company continuously monitors the payment performance of its finance receivables. For large retail finance customers and dealers with wholesale financing, the Company regularly reviews their financial statements and makes site visits and phone contact as appropriate. If the Company becomes aware of circumstances that could cause those customers or dealers to face financial difficulty, whether or not they are past due, the customers are placed on a watch list.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The Company modifies loans and finance leases in the normal course of its Financial Services operations. The Company may modify loans and finance leases for commercial reasons or for credit reasons. Modifications for commercial reasons are changes to contract terms for customers that are not considered to be in financial difficulty. Insignificant delays are modifications extending terms up to three months for customers experiencing some short-term financial stress, but not considered to be in financial difficulty. Modifications for credit reasons are changes to contract terms for customers considered to be in financial difficulty. The Company's modifications typically result in granting more time to pay the contractual amounts owed and charging a fee and interest for the term of the modification.

When considering whether to modify customer accounts for credit reasons, the Company evaluates the creditworthiness of the customers and modifies those accounts that the Company considers likely to perform under the modified terms. When the Company modifies loans and finance leases for credit reasons and grants a concession, the modifications are classified as troubled debt restructurings (TDR). The Company does not typically grant credit modifications for customers that do not meet minimum underwriting standards since the Company normally repossesses the financed equipment in these circumstances. When such modifications do occur, they are considered TDRs.

On average, modifications extended contractual terms by approximately five months in 2017 and four months in 2016 and did not have a significant effect on the weighted average term or interest rate of the total portfolio at December 31, 2017 and 2016.

The Company has developed a systematic methodology for determining the allowance for credit losses for its two portfolio segments, retail and wholesale. The retail segment consists of retail loans and direct and sales-type finance leases, net of unearned interest. The wholesale segment consists of truck inventory financing loans to dealers that are collateralized by trucks and other collateral. The wholesale segment generally has less risk than the retail segment. Wholesale receivables generally are shorter in duration than retail receivables, and the Company requires periodic reporting of the wholesale dealer's financial condition, conducts periodic audits of the trucks being financed and in many cases, obtains guarantees or other security such as dealership assets. In determining the allowance for credit losses, retail loans and finance leases are evaluated together since they relate to a similar customer base, their contractual terms require regular payment of principal and interest, generally over three to five years, and they are secured by the same type of collateral. The allowance for credit losses consists of both specific and general reserves.

The Company individually evaluates certain finance receivables for impairment. Finance receivables that are evaluated individually for impairment consist of all wholesale accounts and certain large retail accounts with past due balances or otherwise determined to be at a higher risk of loss. A finance receivable is impaired if it is considered probable the Company will be unable to collect all contractual interest and principal payments as scheduled. In addition, all retail loans and leases which have been classified as TDRs and all customer accounts over 90 days past due are considered impaired. Generally, impaired accounts are on non-accrual status. Impaired accounts classified as TDRs which have been performing for 90 consecutive days are placed on accrual status if it is deemed probable that the Company will collect all principal and interest payments.

Impaired receivables are generally considered collateral dependent. Large balance retail and all wholesale impaired receivables are individually evaluated to determine the appropriate reserve for losses. The determination of reserves

for large balance impaired receivables considers the fair value of the associated collateral. When the underlying collateral fair value exceeds the Company's recorded investment, no reserve is recorded. Small balance impaired receivables with similar risk characteristics are evaluated as a separate pool to determine the appropriate reserve for losses using the historical loss information discussed below.

The Company evaluates finance receivables that are not individually impaired on a collective basis and determines the general allowance for credit losses for both retail and wholesale receivables based on historical loss information, using past due account data and current market conditions. Information used includes assumptions regarding the likelihood of collecting current and past due accounts, repossession rates, the recovery rate on the underlying collateral based on used truck values and other pledged collateral or recourse. The Company has developed a range of loss estimates for each of its country portfolios based on historical experience, taking into account loss frequency and severity in both strong and weak truck market conditions. A projection is made of the range of estimated credit losses inherent in the portfolio from which an amount is determined as probable based on current market conditions and other factors impacting the creditworthiness of the Company's borrowers and their ability to repay. After determining the appropriate level of the allowance for credit losses, a provision for losses on finance receivables is charged to income as necessary to reflect management's estimate of incurred credit losses, net of recoveries, inherent in the portfolio.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

In determining the fair value of the collateral, the Company uses a pricing matrix and categorizes the fair value as Level 2 in the hierarchy of fair value measurement. The pricing matrix is reviewed quarterly and updated as appropriate. The pricing matrix considers the make, model and year of the equipment as well as recent sales prices of comparable equipment sold individually, which is the lowest unit of account, through wholesale channels to the Company's dealers (principal market). The fair value of the collateral also considers the overall condition of the equipment.

Accounts are charged-off against the allowance for credit losses when, in the judgment of management, they are considered uncollectible, which generally occurs upon repossession of the collateral. Typically the timing between the repossession and charge-off is not significant. In cases where repossession is delayed (e.g., for legal proceedings), the Company records a partial charge-off. The charge-off is determined by comparing the fair value of the collateral, less cost to sell, to the recorded investment.

Inventories: Inventories are stated at the lower of cost or market. Cost of inventories in the U.S. is determined principally by the last in, first-out (LIFO) method. Cost of all other inventories is determined principally by the first-in, first-out (FIFO) method. Cost of sales and revenues include shipping and handling costs incurred to deliver products to dealers and customers.

Equipment on Operating Leases: The Company's Financial Services segment leases equipment under operating leases to its customers. In addition, in the Truck segment, equipment sold to customers in Europe subject to a residual value guarantee (RVG) by the Company is generally accounted for as an operating lease. Equipment is recorded at cost and is depreciated on the straight-line basis to the lower of the estimated residual value or guarantee value. Lease and guarantee periods generally range from two to five years. Estimated useful lives of the equipment range from four to nine years. The Company reviews residual values of equipment on operating leases periodically to determine that recorded amounts are appropriate.

Property, Plant and Equipment: Property, plant and equipment are stated at cost. Depreciation is computed principally by the straight-line method based on the estimated useful lives of the various classes of assets. Certain production tooling is amortized on a unit of production basis.

Long-lived Assets and Goodwill: The Company evaluates the carrying value of property, plant and equipment when events and circumstances warrant a review. Goodwill is tested for impairment at least on an annual basis. There were no significant impairment charges for the three years ended December 31, 2017. Goodwill was \$117.4 and \$103.0 at December 31, 2017 and 2016, respectively. The increase in value was mostly due to currency translation.

Product Support Liabilities: Product support liabilities include estimated future payments related to product warranties and deferred revenues on optional extended warranties and repair and maintenance (R&M) contracts. The Company generally offers one year warranties covering most of its vehicles and related aftermarket parts. For vehicles equipped with engines manufactured by PACCAR, the Company generally offers two year warranties on the engine. Specific terms and conditions vary depending on the product and the country of sale. Optional extended warranty and R&M contracts can be purchased for periods which generally range up to five years. Warranty expenses and reserves are estimated and recorded at the time products or contracts are sold based on historical data regarding the source, frequency and cost of claims, net of any recoveries. The Company periodically assesses the adequacy of

its recorded liabilities and adjusts them as appropriate to reflect actual experience. Revenue from extended warranty and R&M contracts is deferred and recognized to income generally on a straight-line basis over the contract period. Warranty and R&M costs on these contracts are recognized as incurred.

Derivative Financial Instruments: As part of its risk management strategy, the Company enters into derivative contracts to hedge against interest rates and foreign currency risk. Certain derivative instruments designated as either cash flow hedges or fair value hedges are subject to hedge accounting. Derivative instruments that are not subject to hedge accounting are held as economic hedges. The Company's policies prohibit the use of derivatives for speculation or trading. At the inception of each hedge relationship, the Company documents its risk management objectives, procedures and accounting treatment. All of the Company's interest-rate and certain foreign-exchange contracts are transacted under International Swaps and Derivatives Association (ISDA) master agreements. Each agreement permits the net settlement of amounts owed in the event of default and certain other termination events. For derivative financial instruments, the Company has elected not to offset derivative positions in the balance sheet with the same counterparty under the same agreements and is not required to post or receive collateral. Exposure limits and minimum credit ratings are used to minimize the risks of counterparty default. The Company's maximum exposure to potential default of its swap counterparties is limited to the asset position of its swap portfolio. The asset position of the Company's swap portfolio is \$53.3 at December 31, 2017.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The Company uses regression analysis to assess effectiveness of interest-rate contracts on a quarterly basis. For foreign-exchange contracts, the Company performs quarterly assessments to ensure that critical terms continue to match. All components of the derivative instrument's gain or loss are included in the assessment of hedge effectiveness. Gains or losses on the ineffective portion of cash flow hedges are recognized in current earnings. Hedge accounting is discontinued prospectively when the Company determines that a derivative financial instrument has ceased to be a highly effective hedge.

Foreign Currency Translation: For most of the Company's foreign subsidiaries, the local currency is the functional currency. All assets and liabilities are translated at year-end exchange rates and all income statement amounts are translated at the weighted average rates for the period. Translation adjustments are recorded in AOCI. The Company uses the U.S. dollar as the functional currency for all but one of its Mexican subsidiaries, which uses the local currency. For the U.S. functional currency entities in Mexico, inventories, cost of sales, property, plant and equipment and depreciation are remeasured at historical rates and resulting adjustments are included in net income.

Earnings per Share: Basic earnings per common share are computed by dividing earnings by the weighted average number of common shares outstanding, plus the effect of any participating securities. Diluted earnings per common share are computed assuming that all potentially dilutive securities are converted into common shares under the treasury stock method.

New Accounting Pronouncements: In February 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2018-02 Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The amendment requires a reclassification from accumulated other comprehensive income (AOCI) to retained earnings the difference between the historical corporate income tax rate and the newly enacted income tax rate resulting from the Tax Act. This ASU is effective for annual periods beginning after December 15, 2018, and interim periods within those annual periods. Early adoption is permitted. Upon adoption, the Company estimates Retained earnings will increase and AOCI will decrease approximately \$40 million with no impact to Stockholders' Equity. The Company expects to early adopt this ASU in 2018.

In March 2017, FASB issued ASU 2017-07 Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The amendment disaggregates the service cost component from non-service cost components of pension expense and prescribes where to present the various components of pension cost on the income statement. This ASU also allows only the service cost component to be eligible for capitalization, when applicable (e.g. as a cost of manufactured inventory or self-constructed assets). The Company will adopt this ASU in January 2018 and accordingly will apply the income statement presentation of service and non-service components of pension expense retrospectively and the capitalization of service cost prospectively. Non-service components of pension expense (see Note L) are currently reported in Cost of sales and revenues and Selling, general and administrative expenses. Upon adoption of this ASU these costs will be reported in Truck, Parts and Other: Interest and other expenses, net.

In October 2016, the FASB issued ASU 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory. The amendment in this ASU requires recognition of income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. Currently the recognition of current and deferred

income taxes for an intra-entity asset transfer is recognized when the asset has been sold to an outside party. This ASU is effective for annual reporting periods beginning after December 15, 2017 and interim periods within those annual periods, and early adoption is permitted. This amendment should be applied on a modified retrospective basis with a cumulative effect adjustment to retained earnings as of the beginning of the period of adoption. The Company adopted this ASU on January 1, 2017. The effect of the adoption reduced prepaid income taxes and retained earnings by \$19.9. Because the corresponding deferred tax asset is not realizable, the Company recorded an offsetting valuation allowance.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The amendment in this ASU requires entities having financial assets measured at amortized cost to estimate credit reserves under an expected credit loss model rather than the current incurred loss model. Under this new model, expected credit losses will be based on relevant information about past events, including historical experience, current conditions and reasonable and supportable forecasts that affect collectability. The ASU is effective for annual periods beginning after December 15, 2019 and interim periods within those annual periods. Early adoption is permitted, but not earlier than annual and interim periods beginning after December 15, 2018. This amendment should be applied on a modified retrospective basis with a cumulative effect adjustment to retained earnings as of the beginning of the period of adoption. The Company is currently evaluating the impact on its consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) which amends the existing accounting standards for leases. Under the new lease standard, lessees will recognize a right-of-use asset and a lease liability for virtually all leases (other than short-term leases). Lessor accounting is largely unchanged. The ASU is effective for annual periods beginning after December 15, 2018 and interim periods within those annual periods. Early adoption is permitted. This ASU requires leases to be recognized and measured at the beginning of the earliest period presented using a modified retrospective approach. The Company is currently evaluating the impact on its consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This ASU amends the existing accounting standards for revenue recognition. Under the new revenue recognition model, a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The FASB has subsequently issued several related ASUs to clarify the implementation guidance in ASU 2014-09. This standard may be applied retrospectively to each prior period presented or modified retrospectively with a cumulative effect recognized as of the date of initial application. The Company will adopt this ASU on a modified retrospective basis on January 1, 2018.

The most significant effect of the standard relates to trucks sold in Europe that are subject to a residual value guarantee (RVG) and are currently accounted for as an operating lease in the Truck, Parts and Other section of the Company's Consolidated Balance Sheets (see Note E). Under the new standard, revenues will be recognized immediately for certain of these RVG contracts that allow customers the option to return their truck and for which there is no economic incentive to do so. The Company expects the overall effects on revenues to not be significant, as the increase in revenues from immediate recognition will largely be offset by reduced amortization of RVG revenue that had been deferred under the prior standard. Upon adoption of the new standard, total RVG assets will decrease by approximately \$497 million and the related liability will decrease by approximately \$520 million. The cumulative effect adjustment will increase Retained earnings by approximately \$17 million, net of tax. Also as required by the new standard, the Company will recognize an asset for the value of expected returned aftermarket parts which had previously been netted with the related liabilities. The new standard also requires new and expanded footnote disclosures.

In addition to ASU 2016-16 disclosed above, the Company adopted the following standards effective January 1, 2017, none of which had a material impact on the Company's consolidated financial statements.

STANDARD DESCRIPTION

2017-04 * Intangibles –
Goodwill and
Other (Topic
350):
Simplifying the
Test for
Goodwill

2016-09 **	Impairment. Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting.
2015-11 **	Inventory (Topic 330): Simplifying the Measurement of Inventory.

*The Company early adopted in 2017.

**The Company adopted on the effective date of January 1, 2017.

The FASB also issued the following standards, which are not expected to have a material impact on the Company's consolidated financial statements.

STANDARD	DESCRIPTION	EFFECTIVE DATE
2016-01 *	Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities.	January 1, 2018
2016-15 *	Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments.	January 1, 2018
2017-12 **	Derivative and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities.	January 1, 2019

*The Company will adopt on the effective date.

**The Company expects to early adopt on January 1, 2018.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

B. INVESTMENTS IN MARKETABLE DEBT SECURITIES

Marketable debt securities consisted of the following at December 31:

2017	AMORTIZED COST	UNREALIZED GAINS	UNREALIZED LOSSES	FAIR VALUE
U.S. tax-exempt securities	\$ 537.9		\$ 2.4	\$535.5
U.S. corporate securities	89.7	\$.2	.2	89.7
U.S. government and agency securities	48.9		.2	48.7
Non-U.S. corporate securities	459.4	1.3	1.4	459.3
Non-U.S. government securities	91.5	.3	.1	91.7
Other debt securities	142.8	.1	.7	142.2
	\$ 1,370.2	\$ 1.9	\$ 5.0	\$1,367.1

2016	AMORTIZED COST	UNREALIZED GAINS	UNREALIZED LOSSES	FAIR VALUE
U.S. tax-exempt securities	\$ 597.9	\$.2	\$ 3.1	\$595.0
U.S. corporate securities	47.6	.2		47.8
U.S. government and agency securities	16.0			16.0
Non-U.S. corporate securities	306.9	1.5	.4	308.0
Non-U.S. government securities	97.6	.6		98.2
Other debt securities	75.9	.2	.2	75.9
	\$ 1,141.9	\$ 2.7	\$ 3.7	\$1,140.9

The cost of marketable debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Amortization, accretion, interest and dividend income and realized gains and losses are included in investment income. The cost of securities sold is based on the specific identification method. Gross realized gains were \$1.4, \$4.4 and \$2.6, and gross realized losses were \$.5, \$.1 and \$.8 for the years ended December 31, 2017, 2016 and 2015, respectively.

Marketable debt securities with continuous unrealized losses and their related fair values were as follows:

At December 31, 2017		2016	
LESS	TWELVE	LESS	TWELVE
THAN		THAN	
	MONTHS		MONTHS
TWELVE	OR	TWELVE	OR GREATER

Edgar Filing: PACCAR INC - Form 10-K

	MONTHS	GREATER	MONTHS
Fair value	\$908.5	\$ 18.4	\$615.5
Unrealized losses	4.8	.2	3.7

For the investment securities in gross unrealized loss positions identified above, the Company does not intend to sell the investment securities. It is more likely than not that the Company will not be required to sell the investment securities before recovery of the unrealized losses, and the Company expects that the contractual principal and interest will be received on the investment securities. As a result, the Company recognized no other-than-temporary impairments during the periods presented.

Contractual maturities on marketable debt securities at December 31, 2017 were as follows:

Maturities:	AMORTIZED COST	FAIR VALUE
Within one year	\$ 413.7	\$413.3
One to five years	939.6	936.9
More than ten years	16.9	16.9
	\$ 1,370.2	\$1,367.1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

C. INVENTORIES

Inventories include the following:

At December 31,	2017	2016
Finished products	\$515.7	\$452.3
Work in process and raw materials	586.2	444.7
	1,101.9	897.0
Less LIFO reserve	(173.5)	(169.2)
	\$928.4	\$727.8

Inventories valued using the LIFO method comprised 47% and 49% of consolidated inventories before deducting the LIFO reserve at December 31, 2017 and 2016, respectively.

D. FINANCE AND OTHER RECEIVABLES

Finance and other receivables include the following:

At December 31,	2017	2016
Loans	\$4,147.8	\$3,948.6
Direct financing leases	3,211.7	2,798.0
Sales-type finance leases	781.1	867.3
Dealer wholesale financing	1,880.6	1,528.5
Operating lease receivables and other	161.1	150.9
Unearned interest: Finance leases	(368.0)	(344.7)
	\$9,814.3	\$8,948.6
Less allowance for losses:		
Loans and leases	(101.9)	(97.1)
Dealer wholesale financing	(6.0)	(5.5)
Operating lease receivables and other	(9.3)	(8.6)
	\$9,697.1	\$8,837.4

The net activity of sales-type finance leases, dealer direct loans and dealer wholesale financing on new trucks is shown in the operating section of the Consolidated Statements of Cash Flows since those receivables finance the sale of Company inventory.

Annual minimum payments due on finance receivables are as follows:

Edgar Filing: PACCAR INC - Form 10-K

Beginning January 1, 2018	FINANCE	
	LOANS	LEASES
2018	\$1,351.5	\$ 1,226.7
2019	1,088.1	959.6
2020	857.2	716.6
2021	542.0	440.6
2022	242.9	217.8
Thereafter	66.1	90.6
	\$4,147.8	\$ 3,651.9

Estimated residual values included with finance leases amounted to \$340.9 in 2017 and \$239.1 in 2016. Experience indicates substantially all of dealer wholesale financing will be repaid within one year. In addition, repayment experience indicates that some loans, leases and other finance receivables will be paid prior to contract maturity, while others may be extended or modified.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

For the following credit quality disclosures, finance receivables are classified into two portfolio segments, wholesale and retail. The retail portfolio is further segmented into dealer retail and customer retail. The dealer wholesale segment consists of truck inventory financing to PACCAR dealers. The dealer retail segment consists of loans and leases to participating dealers and franchises that use the proceeds to fund customers' acquisition of commercial vehicles and related equipment. The customer retail segment consists of loans and leases directly to customers for the acquisition of commercial vehicles and related equipment. Customer retail receivables are further segregated between fleet and owner/operator classes. The fleet class consists of customer retail accounts operating more than five trucks. All other customer retail accounts are considered owner/operator. These two classes have similar measurement attributes, risk characteristics and common methods to monitor and assess credit risk.

Allowance for Credit Losses: The allowance for credit losses is summarized as follows:

	2017				
	DEALER WHOLESALE		CUSTOMER RETAIL	OTHER*	TOTAL
Balance at January 1	\$ 5.5	\$ 9.6	\$ 87.5	\$ 8.6	\$ 111.2
Provision for losses		(.3)	21.1	1.5	22.3
Charge-offs			(24.8)	(1.9)	(26.7)
Recoveries			5.0	.3	5.3
Currency translation and other	.5	.1	3.7	.8	5.1
Balance at December 31	\$ 6.0	\$ 9.4	\$ 92.5	\$ 9.3	\$ 117.2

	2016				
	DEALER WHOLESALE		CUSTOMER RETAIL	OTHER*	TOTAL
Balance at January 1	\$ 7.3	\$ 10.3	\$ 88.9	\$ 8.3	\$ 114.8
Provision for losses	(1.7)	(.7)	18.6	2.2	18.4
Charge-offs			(22.9)	(2.1)	(25.0)
Recoveries			5.5	.3	5.8
Currency translation and other	(.1)		(2.6)	(.1)	(2.8)
Balance at December 31	\$ 5.5	\$ 9.6	\$ 87.5	\$ 8.6	\$ 111.2

	2015				
	DEALER WHOLESALE		CUSTOMER RETAIL	OTHER*	TOTAL
Balance at January 1	\$ 9.0	\$ 11.9	\$ 93.6	\$ 7.5	\$ 122.0
Provision for losses	(.8)	(1.4)	11.6	3.0	12.4
Charge-offs	(.3)		(13.6)	(3.2)	(17.1)
Recoveries			3.5	.5	4.0

Edgar Filing: PACCAR INC - Form 10-K

Currency translation and other	(.6)	(.2)	(6.2)	.5	(6.5)
Balance at December 31	\$7.3	\$ 10.3	\$ 88.9	\$ 8.3	\$ 114.8

*Operating lease and other trade receivables.

52

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

Information regarding finance receivables evaluated and determined individually and collectively is as follows:

At December 31, 2017	DEALER WHOLESALE	RETAIL	CUSTOMER RETAIL	TOTAL
Recorded investment for impaired finance				
receivables evaluated individually	\$.1	\$ 4.0	\$ 50.8	\$ 54.9
Allowance for impaired finance receivables				
determined individually	.1		6.6	6.7
Recorded investment for finance receivables				
evaluated collectively	1,880.5	1,354.7	6,363.1	9,598.3
Allowance for finance receivables determined				
collectively	5.9	9.4	85.9	101.2
At December 31, 2016	DEALER WHOLESALE	RETAIL	CUSTOMER RETAIL	TOTAL
Recorded investment for impaired finance				
receivables evaluated individually	\$.1		\$ 57.3	\$ 57.4
Allowance for impaired finance receivables				
determined individually	.1		4.9	5.0
Recorded investment for finance receivables				
evaluated collectively	1,528.4	\$ 1,406.0	5,805.9	8,740.3
Allowance for finance receivables determined				
collectively	5.4	9.6	82.6	97.6

The recorded investment for finance receivables that are on non-accrual status is as follows:

At December 31,	2017	2016
Dealer:		
Wholesale	\$.1	\$.1

Customer retail:		
Fleet	44.4	49.5
Owner/operator	6.0	6.9
	\$50.5	\$56.5

Impaired Loans: Impaired loans are summarized below. The impaired loans with specific reserve represent the unpaid principal balance. The recorded investment of impaired loans as of December 31, 2017 and December 31, 2016 was not significantly different than the unpaid principal balance.

At December 31, 2017	DEALER		CUSTOMER RETAIL		TOTAL
	WHOLESALE	RETAIL	FLEET	OWNER/ OPERATOR	
Impaired loans with a specific reserve	\$.1		\$ 18.8	\$ 1.0	\$ 19.9
Associated allowance	(.1)		(3.0)	(.2)	(3.3)
			\$ 15.8	\$.8	\$ 16.6
Impaired loans with no specific reserve	\$ 3.9		13.1	.2	17.2
Net carrying amount of impaired loans	\$ 3.9		\$ 28.9	\$ 1.0	\$ 33.8
Average recorded investment	\$.1	\$ 4.0	\$ 31.3	\$ 1.8	\$ 37.2

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

	DEALER	CUSTOMER RETAIL	OWNER/ FLEET OPERATOR	TOTAL
At December 31, 2016				
Impaired loans with a specific reserve	\$.1	\$ 18.9	\$ 1.8	\$ 20.8
Associated allowance	(.1)	(2.8)	(.3)	(3.2)
		\$ 16.1	\$ 1.5	\$ 17.6
Impaired loans with no specific reserve		10.8	.2	11.0
Net carrying amount of impaired loans		\$ 26.9	\$ 1.7	\$ 28.6
Average recorded investment	\$ 2.8	\$ 28.0	\$ 2.4	\$ 33.2

During the period the loans above were considered impaired, interest income recognized on a cash basis was as follows:

	2017	2016	2015
Interest income recognized:			
Customer retail - fleet	\$ 1.6	\$ 1.1	\$ 1.4
Customer retail - owner/operator	.1	.4	.4
	\$ 1.7	\$ 1.5	\$ 1.8

Credit Quality: The Company's customers are principally concentrated in the transportation industry in North America, Europe and Australia. The Company's portfolio assets are diversified over a large number of customers and dealers with no single customer or dealer balances representing over 5% of the total portfolio assets. The Company retains as collateral a security interest in the related equipment.

At the inception of each contract, the Company considers the credit risk based on a variety of credit quality factors including prior payment experience, customer financial information, credit-rating agency ratings, loan-to-value ratios and other internal metrics. On an ongoing basis, the Company monitors credit quality based on past due status and collection experience as there is a meaningful correlation between the past due status of customers and the risk of loss.

The Company has three credit quality indicators: performing, watch and at-risk. Performing accounts pay in accordance with the contractual terms and are not considered high-risk. Watch accounts include accounts 31 to 90 days past due and large accounts that are performing but are considered to be high risk. Watch accounts are not impaired. At-risk accounts are accounts that are impaired, including TDRs, accounts over 90 days past due and other accounts on non-accrual status. The tables below summarize the Company's finance receivables by credit quality indicator and portfolio class.

At December 31, 2017	DEALER		CUSTOMER RETAIL		TOTAL
	WHOLESALE	RETAIL	FLEET	OWNER/ OPERATOR	
Performing	\$1,874.5	\$1,354.7	\$5,290.3	\$ 1,005.2	\$9,524.7
Watch	6.0		62.9	4.7	73.6
At-risk	.1	4.0	44.7	6.1	54.9
	\$1,880.6	\$1,358.7	\$5,397.9	\$ 1,016.0	\$9,653.2

At December 31, 2016	DEALER		CUSTOMER RETAIL		TOTAL
	WHOLESALE	RETAIL	FLEET	OWNER/ OPERATOR	
Performing	\$1,519.3	\$1,406.0	\$4,863.4	\$ 922.1	\$8,710.8
Watch	9.1		14.9	5.5	29.5
At-risk	.1		50.4	6.9	57.4
	\$1,528.5	\$1,406.0	\$4,928.7	\$ 934.5	\$8,797.7

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The tables below summarize the Company's finance receivables by aging category. In determining past due status, the Company considers the entire contractual account balance past due when any installment is over 30 days past due. Substantially all customer accounts that were greater than 30 days past due prior to credit modification became current upon modification for aging purposes.

At December 31, 2017	DEALER		CUSTOMER RETAIL		TOTAL
	WHOLESALE	RETAIL	FLEET	OWNER/ OPERATOR	
Current and up to 30 days past due	\$ 1,880.5	\$ 1,358.7	\$ 5,365.7	\$ 1,007.4	\$ 9,612.3
31 – 60 days past due			14.7	4.0	18.7
Greater than 60 days past due	.1		17.5	4.6	22.2
	\$ 1,880.6	\$ 1,358.7	\$ 5,397.9	\$ 1,016.0	\$ 9,653.2

At December 31, 2016	DEALER		CUSTOMER RETAIL		TOTAL
	WHOLESALE	RETAIL	FLEET	OWNER/ OPERATOR	
Current and up to 30 days past due	\$ 1,528.4	\$ 1,406.0	\$ 4,898.4	\$ 926.4	\$ 8,759.2
31 – 60 days past due			12.6	3.9	16.5
Greater than 60 days past due	.1		17.7	4.2	22.0
	\$ 1,528.5	\$ 1,406.0	\$ 4,928.7	\$ 934.5	\$ 8,797.7

Troubled Debt Restructurings: The balance of TDRs was \$37.9 and \$43.1 at December 31, 2017 and December 31, 2016, respectively. At modification date, the pre-modification and post-modification recorded investment balances for finance receivables modified during the period by portfolio class are as follows:

	2017		2016	
	RECORDED INVESTMENT PRE-MODIFICATION	RECORDED INVESTMENT POST-MODIFICATION	RECORDED INVESTMENT PRE-MODIFICATION	RECORDED INVESTMENT POST-MODIFICATION
Fleet	\$ 19.9	\$ 19.9	\$ 27.2	\$ 27.2
Owner/operator	.6	.6	4.4	4.4
	\$ 20.5	\$ 20.5	\$ 31.6	\$ 31.6

The effect on the allowance for credit losses from such modifications was not significant at December 31, 2017 and 2016.

TDRs modified during the previous twelve months that subsequently defaulted (i.e., became more than 30 days past due) in the year ended by portfolio class are as follows:

	2017	2016
Fleet	\$4.7	\$.3
Owner/operator	.2	.4
	\$4.9	\$.7

There were \$1.4 and \$4.8 of finance receivables modified as TDRs during the previous twelve months that subsequently defaulted and were charged off for the year ended December 31, 2017 and 2016, respectively.

Repossessions: When the Company determines a customer is not likely to meet its contractual commitments, the Company repossesses the vehicles which serve as collateral for the loans, finance leases and equipment under operating leases. The Company records the vehicles as used truck inventory included in Financial Services Other assets on the Consolidated Balance Sheets. The balance of repossessed inventory at December 31, 2017 and 2016 was \$13.1 and \$25.4, respectively. Proceeds from the sales of repossessed assets were \$58.3, \$51.7 and \$48.0 for the years ended December 31, 2017, 2016 and 2015, respectively. These amounts are included in Proceeds from asset disposals in the Consolidated Statements of Cash Flows. Write-downs of repossessed equipment on operating leases are recorded as impairments and included in Financial Services Depreciation and other expenses on the Consolidated Statements of Income.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

E. EQUIPMENT ON OPERATING LEASES

A summary of equipment on operating leases for Truck, Parts and Other and for the Financial Services segment is as follows:

At December 31,	TRUCK, PARTS AND OTHER		FINANCIAL SERVICES	
	2017	2016	2017	2016
Equipment on operating leases	\$1,615.5	\$1,282.3	\$4,066.3	\$3,640.6
Less allowance for depreciation	(349.8)	(268.4)	(1,190.0)	(1,016.7)
	\$1,265.7	\$1,013.9	\$2,876.3	\$2,623.9

Annual minimum lease payments due on Financial Services operating leases beginning January 1, 2018 are \$628.5, \$433.2, \$267.1, \$138.2, \$49.4 and \$9.6 thereafter.

When the equipment is sold subject to an RVG, the full sales price is received from the customer. A liability is established for the residual value obligation with the remainder of the proceeds recorded as deferred lease revenue. These amounts are summarized below:

At December 31,	TRUCK, PARTS AND OTHER	
	2017	2016
Residual value guarantees	\$909.8	\$699.2
Deferred lease revenues	429.2	373.4
	\$1,339.0	\$1,072.6

The deferred lease revenue is amortized on a straight-line basis over the RVG contract period. At December 31, 2017, the annual amortization of deferred revenues beginning January 1, 2018 is \$188.9, \$123.8, \$69.5, \$42.3, \$4.5 and \$.2 thereafter. Annual maturities of the RVGs beginning January 1, 2018 are \$287.8, \$269.9, \$209.5, \$79.8, \$54.2 and \$8.6 thereafter.

F. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment include the following:

Edgar Filing: PACCAR INC - Form 10-K

At December 31,	USEFUL LIVES	2017	2016
Land		\$263.3	\$221.2
Buildings and improvements	10 - 40 years	1,315.1	1,134.1
Machinery, equipment and production tooling	3 - 12 years	3,782.1	3,285.2
Construction in progress		253.8	352.8
		5,614.3	4,993.3
Less allowance for depreciation		(3,149.9)	(2,733.3)
		\$2,464.4	\$2,260.0

G. ACCOUNTS PAYABLE, ACCRUED EXPENSES AND OTHER

Accounts payable, accrued expenses and other include the following:

At December 31,	2017	2016
Truck, Parts and Other:		
Accounts payable	\$1,154.7	\$938.6
Product support liabilities	372.1	344.2
Accrued expenses	401.4	233.1
Accrued capital expenditures	120.1	111.2
Salaries and wages	238.9	194.8
Other	282.3	212.2
	\$2,569.5	\$2,034.1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

H. PRODUCT SUPPORT LIABILITIES

Changes in product support liabilities are summarized as follows:

WARRANTY RESERVES	2017	2016	2015
Balance at January 1	\$282.1	\$346.2	\$310.8
Cost accruals	242.1	211.9	294.8
Payments	(236.8)	(255.7)	(228.8)
Change in estimates for pre-existing warranties	(2.0)	(7.3)	(21.3)
Currency translation	13.4	(13.0)	(9.3)
Balance at December 31	\$298.8	\$282.1	\$346.2

DEFERRED REVENUES ON EXTENDED WARRANTIES AND R&M

CONTRACTS	2017	2016	2015
Balance at January 1	\$573.5	\$524.8	\$462.0
Deferred revenues	371.8	347.6	333.0
Revenues recognized	(328.2)	(274.3)	(248.4)
Currency translation	36.8	(24.6)	(21.8)
Balance at December 31	\$653.9	\$573.5	\$524.8

Product support liabilities are included in the accompanying Consolidated Balance Sheets as follows:

	WARRANTY RESERVES		DEFERRED REVENUES	
At December 31,	2017	2016	2017	2016
Truck, Parts and Other:				
Accounts payable, accrued expenses and other	\$176.0	\$181.4	\$196.1	\$162.8
Other liabilities	122.8	100.7	441.0	395.7
Financial Services:				
Deferred taxes and other liabilities			16.8	15.0
	\$298.8	\$282.1	\$653.9	\$573.5

I. BORROWINGS AND CREDIT ARRANGEMENTS

Financial Services borrowings include the following:

Edgar Filing: PACCAR INC - Form 10-K

	2017		2016	
	EFFECTIVE		EFFECTIVE	
At December 31,	RATE BORROWINGS		RATE BORROWINGS	
Commercial paper	1.3%	\$ 2,723.7	.7%	\$ 2,242.5
Bank loans	6.9%	210.2	5.5%	205.0
		2,933.9		2,447.5
Term notes	1.7%	5,945.5	1.5%	6,027.7
	1.7%	\$ 8,879.4	1.4%	\$ 8,475.2

Commercial paper and term notes borrowings were \$8,669.2 and \$8,270.2 at December 31, 2017 and 2016, respectively. Unamortized debt issuance costs, unamortized discounts and the net effect of fair value hedges were \$(20.9) and \$(19.3) at December 31, 2017 and 2016, respectively. The effective rate is the weighted average rate as of December 31, 2017 and 2016 and includes the effects of interest-rate contracts.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The annual maturities of the Financial Services borrowings are as follows:

	COMMERCIAL PAPER	BANK LOANS	TERM NOTES	TOTAL
Beginning January 1, 2018	\$ 2,725.5	\$ 57.1	\$ 1,693.1	\$ 4,475.7
2018		27.8	1,785.4	1,813.2
2019		74.8	1,610.3	1,685.1
2020		50.5	575.8	626.3
2021			300.0	300.0
2022	\$ 2,725.5	\$ 210.2	\$ 5,964.6	\$ 8,900.3

Interest paid on borrowings was \$127.4, \$108.2, and \$101.3 in 2017, 2016 and 2015, respectively. For the years ended December 31, 2017, 2016 and 2015, the Company capitalized interest on borrowings of nil for all periods presented, in Truck, Parts and Other.

The primary sources of borrowings in the capital markets are commercial paper and medium-term notes issued in the public markets, and to a lesser extent, bank loans. The medium-term notes are issued by PACCAR Financial Corp. (PFC), PACCAR Financial Europe and PACCAR Financial Mexico.

In November 2015, the Company's U.S. finance subsidiary, PFC, filed a shelf registration under the Securities Act of 1933. The total amount of medium-term notes outstanding for PFC as of December 31, 2017 was \$4,450.0. The registration expires in November 2018 and does not limit the principal amount of debt securities that may be issued during that period. PFC intends to renew the registration in 2018.

As of December 31, 2017, the Company's European finance subsidiary, PACCAR Financial Europe, had €1,343.6 available for issuance under a €2,500.0 medium-term note program listed on the Professional Securities Market of the London Stock Exchange. This program replaced an expiring program in the second quarter of 2017 and is renewable annually through the filing of new listing particulars.

In April 2016, PACCAR Financial Mexico registered a 10,000.0 peso medium-term note and commercial paper program with the Comision Nacional Bancaria y de Valores. The registration expires in April 2021 and limits the amount of commercial paper (up to one year) to 5,000.0 pesos. At December 31, 2017, 6,250.0 pesos remained available for issuance.

The Company has line of credit arrangements of \$3,520.0, of which \$3,306.8 were unused at December 31, 2017. Included in these arrangements are \$3,000.0 of syndicated bank facilities, of which \$1,000.0 expires in June 2018, \$1,000.0 expires in June 2021 and \$1,000.0 expires in June 2022. The Company intends to replace these credit facilities on or before expiration with facilities of similar amounts and duration. These credit facilities are maintained primarily to provide backup liquidity for commercial paper borrowings and maturing medium-term notes. There were no borrowings under the syndicated bank facilities for the year ended December 31, 2017.

J. LEASES

The Company leases certain facilities and computer equipment under operating leases. Leases expire at various dates through the year 2026. At January 1, 2018, annual minimum rent payments under non-cancelable operating leases having initial or remaining terms in excess of one year are \$23.0, \$14.6, \$10.3, \$6.5, \$4.4 and \$2.6 thereafter. For the years ended December 31, 2017, 2016 and 2015, total rental expenses under all leases amounted to \$30.1, \$28.8 and \$30.5, respectively.

K. COMMITMENTS AND CONTINGENCIES

At December 31, 2017, PACCAR had standby letters of credit and surety bonds totaling \$26.3, from third party financial institutions, in the normal course of business, which guarantee various insurance, financing and other activities. At December 31, 2017, PACCAR's financial services companies, in the normal course of business, had outstanding commitments to fund new loan and lease transactions amounting to \$928.6. The commitments generally expire in 90 days. The Company had other commitments, primarily to purchase production inventory, equipment and energy amounting to \$243.9, \$71.6, \$69.1, \$62.3, \$60.5 and nil for 2018, 2019, 2020, 2021, 2022 and beyond, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The Company is involved in various stages of investigations and cleanup actions in different countries related to environmental matters. In certain of these matters, the Company has been designated as a “potentially responsible party” by domestic and foreign environmental agencies. The Company has an undiscounted accrual to provide for the estimated costs to investigate and complete cleanup actions where it is probable that the Company will incur such costs in the future. Expenditures related to environmental activities for the years ended December 31, 2017, 2016 and 2015 were \$1.9, \$2.2 and \$2.0, respectively.

While the timing and amount of the ultimate costs associated with future environmental cleanup cannot be determined, management expects that these matters will not have a significant effect on the Company's consolidated financial position.

In the first half of 2016, the Company recorded a charge of €752.7 (\$833.0) in connection with an investigation by the European Commission (EC) of all major European truck manufacturers, including DAF Trucks N.V., its subsidiary DAF Trucks Deutschland GmbH (collectively, “DAF”) and the Company as their parent. On July 19, 2016, the EC reached a settlement with DAF and the Company under which the EC imposed a fine of €752.7 (\$833.0) for infringement of European Union competition rules. DAF paid the fine in August 2016. Following the EC settlement, claims and lawsuits have been filed against the Company, DAF and certain DAF subsidiaries and other truck manufacturers. Others may bring EC related claims and lawsuits against the Company or its subsidiaries. While the Company believes it has meritorious defenses, such claims and lawsuits will likely take a significant period of time to resolve, and it is not possible to estimate a range of potential loss. An adverse outcome of such proceedings could have a material impact on the Company's results of operations.

PACCAR is also a defendant in various other legal proceedings and, in addition, there are various other contingent liabilities arising in the normal course of business. After consultation with legal counsel, management does not anticipate that disposition of these various other proceedings and contingent liabilities will have a material effect on the consolidated financial statements.

L. EMPLOYEE BENEFITS

Severance Costs: The Company incurred severance expense in 2017, 2016 and 2015 of \$.8, \$2.0 and \$3.3, respectively.

Defined Benefit Pension Plans: The Company has several defined benefit pension plans, which cover a majority of its employees. The Company evaluates its actuarial assumptions on an annual basis and considers changes based upon market conditions and other factors.

The expected return on plan assets is determined by using a market-related value of assets, which is calculated based on an average of the previous five years of asset gains and losses.

Generally, accumulated unrecognized actuarial gains and losses are amortized using the 10% corridor approach. The corridor is defined as the greater of either 10% of the projected benefit obligation or the market-related value of plan assets. The amortization amount is the excess beyond the corridor divided by the average remaining estimated service life of participants on a straight-line basis.

The Company funds its pensions in accordance with applicable employee benefit and tax laws. The Company contributed \$70.6 to its pension plans in 2017 and \$185.7 in 2016. The Company expects to contribute in the range of \$70.0 to \$100.0 to its pension plans in 2018, of which \$21.2 is estimated to satisfy minimum funding requirements. Annual benefits expected to be paid beginning January 1, 2018 are \$84.4, \$87.1, \$94.0, \$99.9, \$106.2 and for the five years thereafter, a total of \$609.7.

Plan assets are invested in global equity and debt securities through professional investment managers with the objective to achieve targeted risk adjusted returns and maintain liquidity sufficient to fund current benefit payments. Typically, each defined benefit plan has an investment policy that includes a target for asset mix, including maximum and minimum ranges for allocation percentages by investment category. The actual allocation of assets may vary at times based upon rebalancing policies and other factors. The Company periodically assesses the target asset mix by evaluating external sources of information regarding the long-term historical return, volatilities and expected future returns for each investment category. In addition, the long-term rates of return assumptions for pension accounting are reviewed annually to ensure they are appropriate. Target asset mix and forecast long-term returns by asset category are considered in determining the assumed long-term rates of return, although historical returns realized are given some consideration.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The fair value of mutual funds, common stocks and U.S. treasuries is determined using the market approach and is based on the quoted prices in active markets. These securities are categorized as Level 1. The fair value of debt securities is determined using the market approach and is based on the quoted market prices of the securities or other observable inputs. These securities are categorized as Level 2.

The fair value of commingled trust funds is determined using the market approach and is based on the unadjusted net asset value (NAV) per unit as determined by the sponsor of the fund based on the fair values of underlying investments. These assets are collective investment trusts, and substantially all of these investments have no redemption restrictions or unfunded commitments. Securities measured at NAV per unit as a practical expedient are not classified in the fair value hierarchy.

The following information details the allocation of plan assets by investment type. See Note P for definitions of fair value levels.

At December 31, 2017	FAIR VALUE HIERARCHY			MEASURED		
	TARGET	LEVEL	LEVEL	TOTAL	AT NAV	TOTAL
		1	2			
Equities:						
U.S. equities					\$ 768.5	\$768.5
Global equities					866.8	866.8
Total equities	50 - 70%				1,635.3	1,635.3
Fixed income:						
U.S. fixed income		\$223.3	\$238.2	\$461.5	\$ 416.0	\$877.5
Non-U.S. fixed income			27.4	27.4	299.4	326.8
Total fixed income	30 - 50%	223.3	265.6	488.9	715.4	1,204.3
Cash and other		9.2	70.1	79.3	.7	80.0
Total plan assets		\$232.5	\$335.7	\$568.2	\$ 2,351.4	\$2,919.6

At December 31, 2016	FAIR VALUE HIERARCHY			MEASURED		
	TARGET	LEVEL	LEVEL	TOTAL	AT NAV	TOTAL
		1	2			
Equities:						
U.S. equities					\$ 690.8	\$690.8
Global equities					746.1	746.1
Total equities	50 - 70%				1,436.9	1,436.9

Edgar Filing: PACCAR INC - Form 10-K

Fixed income:						
U.S. fixed income		\$195.7	\$196.9	\$392.6	\$317.8	\$710.4
Non-U.S. fixed income			19.6	19.6	254.5	274.1
Total fixed income	30 - 50%	195.7	216.5	412.2	572.3	984.5
Cash and other		8.8	60.0	68.8	3.9	72.7
Total plan assets		\$204.5	\$276.5	\$481.0	\$2,013.1	\$2,494.1

The following additional data relates to all pension plans of the Company:

At December 31,	2017	2016
Weighted average assumptions:		
Discount rate	3.3 %	3.7 %
Rate of increase in future compensation levels	3.9 %	3.9 %
Assumed long-term rate of return on plan assets	6.4 %	6.4 %

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The components of the change in projected benefit obligation and change in plan assets are as follows:

	2017	2016
Change in projected benefit obligation:		
Benefit obligation at January 1	\$2,505.6	\$2,306.0
Service cost	92.9	88.6
Interest cost	81.1	94.3
Benefits paid	(82.6)	(80.2)
Actuarial loss	154.7	186.4
Currency translation and other	68.6	(90.6)
Participant contributions	.4	1.1
Projected benefit obligation at December 31	\$2,820.7	\$2,505.6
Change in plan assets:		
Fair value of plan assets at January 1	\$2,494.1	\$2,219.0
Employer contributions	70.6	185.7
Actual return on plan assets	369.8	254.5
Benefits paid	(82.6)	(80.2)
Currency translation and other	67.3	(86.0)
Participant contributions	.4	1.1
Fair value of plan assets at December 31	\$2,919.6	\$2,494.1
Funded status at December 31	\$98.9	\$(11.5)

	2017	2016
Amounts recorded on balance sheet:		
Other noncurrent assets	\$228.9	\$107.2
Other liabilities	130.0	118.7
Accumulated other comprehensive loss:		
Actuarial loss	372.9	410.6
Prior service cost	2.6	3.4
Net initial transition amount	.1	.1

Of the December 31, 2017 amounts in accumulated other comprehensive loss, \$30.4 of unrecognized actuarial loss and \$1.3 of unrecognized prior service cost are expected to be amortized into net pension expense in 2018.

The accumulated benefit obligation for all pension plans of the Company was \$2,492.4 and \$2,215.3 at December 31, 2017 and 2016, respectively.

Information for all plans with an accumulated benefit obligation in excess of plan assets is as follows:

At December 31,	2017	2016
Projected benefit obligation	\$142.5	\$110.2
Accumulated benefit obligation	124.0	100.4
Fair value of plan assets	23.5	9.3

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

The components of pension expense are as follows:

Year Ended December 31,	2017	2016	2015
Service cost	\$92.9	\$88.6	\$91.3
Interest on projected benefit obligation	81.1	94.3	92.2
Expected return on assets	(159.7)	(141.7)	(140.8)
Amortization of prior service costs	1.2	1.2	1.3
Recognized actuarial loss	25.4	27.7	41.1
Curtailment gain			(.1)
Net pension expense	\$40.9	\$70.1	\$85.0

On January 1, 2017, the Company changed the method used to estimate service cost and interest cost components of pension expense from a single weighted-average method, which is a single discount rate determined at the pension plans measurement date, to an individual spot rate approach, which applies specific spot rates along the yield curve to the relevant projected cash flows. This approach is a more precise measurement of net periodic benefit costs and does not impact the benefit obligation. The Company considers this a change in estimate inseparable from a change in accounting principle and is being accounted for prospectively. This change lowered net pension expense by approximately \$15.0 in 2017.

Multi-employer Plans: The Company participates in multi-employer plans in the U.S. and Europe. These are typically under collective bargaining agreements and cover its union-represented employees. The Company's participation in the following multi-employer plans for the years ended December 31 are as follows:

PENSION PLAN	EIN	PENSION PLAN NUMBER	COMPANY CONTRIBUTIONS		
			2017	2016	2015
Metal and Electrical Engineering Industry Pension Fund		135668	\$25.0	\$23.1	\$23.0
Western Metal Industry Pension Plan	91-6033499	001	1.4	1.5	2.1
Other plans			.8	.7	.9
			\$27.2	\$25.3	\$26.0

The Company contributions shown in the table above approximates the multi-employer pension expense for each of the years ended December 31, 2017, 2016 and 2015, respectively.

Metal and Electrical Engineering Industry Pension Fund is a multi-employer union plan incorporating all DAF employees in the Netherlands and is covered by a collective bargaining agreement that will expire May 31, 2018. The Company's contributions were less than 5% of the total contributions to the plan for the last two reporting periods

ending December 2017. The plan is required by law (the Netherlands Pension Act) to have a coverage ratio in excess of 104.3%. Because the coverage ratio of the plan was 101.5% at December 31, 2017, a funding improvement plan effective through 2026 is in place. The funding improvement plan includes a reduction in pension benefits and delays in future benefit increases.

The Western Metal Industry Pension Plan is located in the U.S. and is covered by a collective bargaining agreement that will expire on November 1, 2020. In accordance with the U.S. Pension Protection Act of 2006, the plan was certified as critical (red) status as of December 31, 2017, and a funding improvement plan was implemented requiring additional contributions through 2022 as long as the plan remains in critical status. Contributions by the Company were 7% and 8% of the total contributions to the plan for the years ended December 31, 2017 and 2016, respectively.

Other plans are principally located in the U.S. For the last two reporting periods, none were under funding improvement plans and Company contributions to these plans are less than 5% of each plan's total contributions.

There were no significant changes for the multi-employer plans in the periods presented that affected comparability between periods.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

Defined Contribution Plans: The Company maintains several defined contribution benefit plans whereby it contributes designated amounts on behalf of participant employees. The largest plan is for U.S. salaried employees where the Company matches a percentage of employee contributions up to an annual limit. The match was 5% of eligible pay in 2017, 2016 and 2015. Other plans are located in Australia, Brasil, Canada, the Netherlands, Belgium and Germany. Expenses for these plans were \$37.9, \$34.1 and \$36.1 in 2017, 2016 and 2015, respectively.

M. INCOME TAXES

The Company's tax rate is based on income and statutory tax rates in the various jurisdictions in which the Company operates. Tax law requires certain items to be included in the Company's tax returns at different times than the items reflected in the Company's financial statements. As a result, the Company's annual tax rate reflected in its financial statements is different than that reported in its tax returns. Some of these differences are permanent, such as expenses that are not deductible in the Company's tax return, and some differences reverse over time, such as depreciation expense. These temporary differences create deferred tax assets and liabilities. The Company establishes valuation allowances for its deferred tax assets if, based on the available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The components of the Company's income before income taxes include the following:

Year Ended December 31,	2017	2016	2015
Domestic	\$1,347.8	\$1,190.7	\$1,581.6
Foreign	825.5	(60.3)	755.5
	\$2,173.3	\$1,130.4	\$2,337.1

The components of the Company's provision for income taxes include the following:

Year Ended December 31,	2017	2016	2015
Current provision:			
Federal	\$397.7	\$322.9	\$521.8
State	63.8	41.7	61.1
Foreign	210.5	213.2	205.4
	672.0	577.8	788.3
Deferred provision (benefit):			
Federal	(173.8)	31.5	(57.8)
State	2.3	4.8	5.3
Foreign	(2.4)	(5.4)	(2.7)
	(173.9)	30.9	(55.2)
	\$498.1	\$608.7	\$733.1

Edgar Filing: PACCAR INC - Form 10-K

Tax benefits recognized for net operating loss carryforwards were \$4.3, \$1.2 and \$.6 for the years ended 2017, 2016 and 2015, respectively.

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

	2017	2016	2015
Statutory rate	35.0 %	35.0%	35.0%
Effect of:			
Rate change on deferred taxes	(14.0)		
Transition tax	6.0		
Non-deductible EC charge		25.8	
State	1.8	2.9	2.1
Federal domestic production deduction	(1.1)	(2.6)	(1.8)
Tax on foreign earnings	(4.0)	(7.4)	(2.7)
Other, net	(.8)	.1	(1.2)
	22.9 %	53.8%	31.4%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

On December 22, 2017, the U.S. enacted new federal income tax legislation, the Tax Cuts and Jobs Act (“the Tax Act”). The Act lowered the U.S. statutory income tax rate from 35% to 21%, imposed a one-time transition tax on the Company’s foreign earnings, which previously had been deferred from U.S. income tax and created a modified territorial system. As a result, the Company recorded a provisional amount of \$304.0 of deferred tax benefits, due to the re-measurement of net deferred tax liabilities at the new lower statutory tax rate. In addition, the Company recorded a provisional amount of \$130.6 of tax expense on the Company’s foreign earnings, which previously had been deferred from U.S. income tax. These provisional amounts may change in 2018, as new information becomes available, as the Tax Act continues to be interpreted and as new technical guidance is issued. The Company will finalize certain tax positions upon filing its 2017 U.S. income tax returns. The Company will then conclude whether the associated provisional amounts require further adjustment. Based on the Company’s current operations, the Company does not expect its future foreign earnings will be subject to significant U.S. federal income tax as a result of the new modified territorial system.

As noted above, as of December 31, 2017, the Company has provided a U.S. transition tax of \$130.6 on all of the Company’s foreign earnings. Included in domestic taxable income for 2016 and 2015 are \$180.4 and \$249.7 of foreign earnings, respectively, which are not indefinitely reinvested, for which domestic taxes of \$7.1 and \$12.2, respectively, were provided to account for the difference between the domestic and foreign tax rate on those earnings.

At December 31, 2017, the Company had net operating loss carryforwards of \$399.4, of which \$271.3 related to foreign subsidiaries and \$128.1 related to states in the U.S. The related deferred tax asset was \$94.6, for which a \$78.3 valuation allowance has been provided. The carryforward periods range from three years to indefinite, subject to certain limitations under applicable laws. The future tax benefits of net operating loss carryforwards are evaluated on a regular basis, including a review of historical and projected operating results.

The tax effects of temporary differences representing deferred tax assets and liabilities are as follows:

At December 31,	2017	2016
Assets:		
Accrued expenses	\$ 183.9	\$ 239.2
Net operating loss and tax credit carryforwards	102.1	84.4
Postretirement benefit plans		11.7
Allowance for losses on receivables	35.6	41.2
Goodwill and intangibles	34.4	1.3
Other	89.2	105.1
	445.2	482.9
Valuation allowance	(118.6)	(64.5)
	326.6	418.4
Liabilities:		
Financial Services leasing depreciation	(608.2)	(808.7)

Edgar Filing: PACCAR INC - Form 10-K

Depreciation and amortization	(165.1)	(246.1)
Postretirement benefit plans	(39.5)	
Other	(28.8)	(35.3)
	(841.6)	(1,090.1)
Net deferred tax liability	\$(515.0)	\$(671.7)

The balance sheets classification of the Company's deferred tax assets and liabilities are as follows:

At December 31,	2017	2016
Truck, Parts and Other:		
Other noncurrent assets, net	\$71.0	\$119.5
Other liabilities	(1.9)	(6.3)
Financial Services:		
Other assets	45.2	74.6
Deferred taxes and other liabilities	(629.3)	(859.5)
Net deferred tax liability	\$(515.0)	\$(671.7)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017, 2016 and 2015 (currencies in millions, except per share data)

Cash paid for income taxes was \$661.4, \$499.4 and \$879.7 in 2017, 2016 and 2015, respectively.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

	2017	2016	2015
Balance at January 1	\$17.3	\$19.1	\$12.0
Additions for tax positions related to the current year	5.6	3.9	10.3
Additions for tax positions related to prior years			
Reductions for tax positions related to prior years		(.3)	(2.0)
Reductions related to settlements		(5.4)	
Lapse of statute of limitations			(1.2)
Balance at December 31	\$22.9	\$17.3	\$19.1

The Company had \$22.9, \$17.3 and \$19.1 of unrecognized tax benefits, of which \$16.8, \$13.9 and \$9.9 would impact the effective tax rate, if recognized, as of December 31, 2017, 2016 and 2015, respectively.

The Company recognized \$.2, \$1.9 and \$1.9 of income related to interest in 2017, 2016 and 2015, respectively. Accrued interest expense and penalties were \$1.1, \$.9 and \$2.8 as of December 31, 2017, 2016 and 2015, respectively. Interest and penalties are classified as income taxes in the Consolidated Statements of Income.

The Company believes it is reasonably possible that approximately \$1.8 of unrecognized tax benefits, resulting primarily from intercompany transactions, will be resolved within the next twelve months from Competent Authority negotiations between tax authorities of two jurisdictions. The Company does not expect the net impact of these negotiations to be material to its effective tax rate. As of December 31, 2017, the United States Internal Revenue Service has completed examinations of the Company's tax returns for all years through 2012, with the exception of 2009 which remains subject to examination. The Company's tax returns for other major jurisdictions remain subject to examination for the years ranging from 2008 through 2017.

N. STOCKHOLDERS' EQUITY

Accumulated Other Comprehensive Income (Loss): The components of AOCI and the changes in AOCI, net of tax, included in the Consolidated Balance Sheets and the Consolidated Statements of Stockholders' Equity, consisted of the following:

DERIVATIVE	MARKETABLE	PENSION	FOREIGN	TOTAL
------------	------------	---------	---------	-------

Edgar Filing: PACCAR INC - Form 10-K

	CONTRACTS	DEBT	PLANS	CURRENCY	
	SECURITIES			TRANSLATION	
Balance at January 1, 2017	\$ (4.3)	\$ (.3)	\$ (414.1)	\$ (709.4)	\$ (1,128.1)
Recorded into AOCI	(91.6)	(1.1)	20.4	292.0	219.7
Reclassified out of AOCI	97.1	(.4)	18.1		114.8
Net other comprehensive income (loss)	5.5	(1.5)	38.5		