OSHKOSH CORP
Form 10-Q
January 31, 2019
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended December 31, 2018
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission file number: 1-31371
Oshkosh Corporation
(Exact name of registrant as specified in its charter)

Wisconsin	39-0520270
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
P.O. Box 2566 Oshkosh, Wisconsin	54903-2566
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code: (920) 235-9151
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ý Yes o No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ý Yes o No
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 ý	Accelerated filer o
Non-accelerated filer o	Smaller reporting company o
	Emerging growth Company o

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. o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). o Yes ý No
As of January 23, 2019, 70,046,674 shares of the registrant’s Common Stock were outstanding.

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FOR THE QUARTER ENDED DECEMBER 31, 2018

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PART I - FINANCIAL INFORMATION
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ITEM 1. FINANCIAL STATEMENTS
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OSHKOSH CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In millions, except per share amounts; unaudited)

	Three Months Ended December 31,	
		As adjusted
	2018	2017
Net sales	$1,803.4	$1,586.3
Cost of sales	1,475.1	1,343.3
Gross income	328.3	243.0
Operating expenses:		
Selling, general and administrative	158.6	157.9
Amortization of purchased intangibles	9.2	10.6
Total operating expenses	167.8	168.5
Operating income	160.5	74.5
Other income (expense):		
Interest expense	(13.7)	(15.4)
Interest income	2.2	1.7
Miscellaneous, net	(1.2)	(0.2)
Income before income taxes and earnings of unconsolidated affiliates	147.8	60.6
Provision for income taxes	39.7	4.7
Income before earnings of unconsolidated affiliates	108.1	55.9
Equity in earnings of unconsolidated affiliates	0.9	0.5
Net income	$109.0	$56.4
Earnings per share:		
Basic	$1.53	$0.75
Diluted	1.51	0.74
Cash dividends declared per share on Common Stock	$0.27	$0.24

The accompanying notes are an integral part of these financial statements

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OSHKOSH CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In millions; unaudited)

	Three Months Ended December 31,	
	2018	2017
Net income	$109.0	$56.4
Other comprehensive income (loss), net of tax:		
Employee pension and postretirement benefits	—	0.5
Currency translation adjustments	(8.8)	2.1
Total other comprehensive income (loss), net of tax	(8.8)	2.6
Comprehensive income	$100.2	$59.0

The accompanying notes are an integral part of these financial statements
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OSHKOSH CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(In millions, except share and per share amounts; unaudited)

	December 31, 2018	September 30, 2018
Assets		
Current assets:		
Cash and cash equivalents	$159.9	$ 454.6
Receivables, net	1,072.1	1,521.6
Unbilled receivables, net	342.9	—
Inventories, net	1,291.6	1,227.7
Other current assets	77.7	66.0
Total current assets	2,944.2	3,269.9
Property, plant and equipment, net	487.1	481.1
Goodwill	1,005.2	1,007.9
Purchased intangible assets, net	460.0	469.4
Other long-term assets	133.6	65.9
Total assets	$5,030.1	$ 5,294.2
Liabilities and Shareholders’ Equity		
Current liabilities:		
Revolving credit facilities and current maturities of long-term debt	$—	$ —
Accounts payable	608.4	776.9
Customer advances	425.2	444.9
Payroll-related obligations	119.8	192.5
Other current liabilities	324.8	275.8
Total current liabilities	1,478.2	1,690.1
Long-term debt, less current maturities	818.3	818.0
Other long-term liabilities	322.4	272.6
Commitments and contingencies		
Shareholders’ equity:		
Preferred Stock ($0.01 par value; 2,000,000 shares authorized; none issued and outstanding)	—	—
Common Stock ($0.01 par value; 300,000,000 shares authorized; 75,101,465 shares issued)	0.7	0.7
Additional paid-in capital	797.6	814.8
Retained earnings	2,090.8	2,007.9
Accumulated other comprehensive loss	(124.7)	(106.8)
Common Stock in treasury, at cost (5,075,430 and 2,730,707 shares, respectively)	(353.2)	(203.1)
Total shareholders’ equity	2,411.2	2,513.5
Total liabilities and shareholders’ equity	$5,030.1	$ 5,294.2

The accompanying notes are an integral part of these financial statements

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OSHKOSH CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(In millions, except per share amounts; unaudited)

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Common Stock in Treasury, at Cost	Total
Balance at September 30, 2017	$ 0.9	$ 802.2	$ 2,399.8	$ (125.0)	$ (770.5)	$ 2,307.4
Net income	—	—	56.4	—	—	56.4
Employee pension and postretirement benefits, net of tax of $0.2	—	—	—	0.5	—	0.5
Currency translation adjustments	—	—	—	2.1	—	2.1
Cash dividends ($0.24 per share)	—	—	(18.0)	—	—	(18.0)
Repurchases of Common Stock	—	—	—	—	(63.7)	(63.7)
Exercise of stock options	—	(1.8)	—	—	10.4	8.6
Stock-based compensation expense	—	7.5	—	—	—	7.5
Payment of stock-based restricted and performance shares	—	(8.6)	—	—	8.6	—
Shares tendered for taxes on stock-based compensation	—	—	—	—	(7.4)	(7.4)
Balance at December 31, 2017	$ 0.9	$ 799.3	$ 2,438.2	$ (122.4)	$ (822.6)	$ 2,293.4

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Common Stock in Treasury, at Cost	Total
Balance at September 30, 2018	$ 0.7	$ 814.8	$ 2,007.9	$ (106.8)	$ (203.1)	$ 2,513.5
Effect of adopting new Accounting Standard Updates (ASU):						
Revenue recognition (ASU 2014-09)	—	—	(60.4)	—	—	(60.4)
Tax accounting for intra-entity asset transfers (ASU 2016-16)	—	—	44.5	—	—	44.5
Tax impact of U.S. tax reform on Accumulated Other Comprehensive Income (ASU 2018-02)	—	—	9.1	(9.1)	—	—
Balance at October 1, 2018	0.7	814.8	2,001.1	(115.9)	(203.1)	2,497.6
Net income	—	—	109.0	—	—	109.0
Currency translation adjustments	—	—	—	(8.8)	—	(8.8)
Cash dividends ($0.27 per share)	—	—	(19.3)	—	—	(19.3)
Repurchases of Common Stock	—	—	—	—	(170.0)	(170.0)
Exercise of stock options	—	(1.8)	—	—	3.5	1.7
Stock-based compensation expense	—	7.9	—	—	—	7.9
Payment of stock-based restricted and performance shares	—	(23.3)	—	—	23.3	—
Shares tendered for taxes on stock-based compensation	—	—	—	—	(6.9)	(6.9)
Balance at December 31, 2018	$ 0.7	$ 797.6	$ 2,090.8	$ (124.7)	$ (353.2)	$ 2,411.2

The accompanying notes are an integral part of these financial statements

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OSHKOSH CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions; unaudited)

	Three Months Ended December 31,	
	2018	2017
Operating activities:		
Net income	$109.0	$56.4
Depreciation and amortization	28.7	31.4
Stock-based compensation expense	7.9	7.5
Deferred income taxes	(1.0)	(27.8)
Gain on sale of assets	(0.8)	(0.6)
Foreign currency transaction gains	(0.2)	(0.8)
Other non-cash adjustments	(0.9)	0.9
Changes in operating assets and liabilities	(228.6)	(37.8)
Net cash provided (used) by operating activities	(85.9)	29.2
Investing activities:		
Additions to property, plant and equipment	(13.2)	(18.7)
Additions to equipment held for rental	(5.9)	(1.2)
Proceeds from sale of equipment held for rental	2.3	2.5
Other investing activities	1.7	(0.8)
Net cash used by investing activities	(15.1)	(18.2)
Financing activities:		
Proceeds from issuance of debt (original maturities greater than three months)	—	6.5
Repayments of debt (original maturities greater than three months)	—	(5.0)
Repurchases of Common Stock	(176.9)	(71.1)
Dividends paid	(19.3)	(18.0)
Proceeds from exercise of stock options	1.7	8.6
Net cash used by financing activities	(194.5)	(79.0)
Effect of exchange rate changes on cash	0.8	0.1
Decrease in cash and cash equivalents	(294.7)	(67.9)
Cash and cash equivalents at beginning of period	454.6	447.0
Cash and cash equivalents at end of period	$159.9	$379.1
Supplemental disclosures:		
Cash paid for interest	$13.4	$6.8
Cash paid for income taxes	5.6	0.8

The accompanying notes are an integral part of these financial statements

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OSHKOSH CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Basis of Presentation

In the opinion of management, the accompanying unaudited Condensed Consolidated Financial Statements contain all adjustments (which include normal recurring adjustments, unless otherwise noted) necessary to present fairly the financial position, results of operations and cash flows for the periods presented. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States (U.S. GAAP) have been condensed or omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. These Condensed Consolidated Financial Statements should be read in conjunction with the audited financial statements and notes thereto included in the Annual Report on Form 10-K of Oshkosh Corporation for the year ended September 30, 2018. The interim results are not necessarily indicative of results for the full year. “Oshkosh” refers to Oshkosh Corporation not including its subsidiaries and “the Company” refers to Oshkosh Corporation and its subsidiaries. Certain reclassifications have been made to the fiscal 2018 financial statements to conform to the fiscal 2019 presentation.

2. New Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued new revenue recognition guidance (Accounting Standard Codification (ASC) 606) to provide a single, comprehensive revenue recognition model for all contracts with customers, Accounting Standard Update (ASU) 2014-09, Revenue from Contracts with Customers (Topic 606). This guidance requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard supersedes all existing U.S. GAAP guidance on revenue recognition and is expected to require the use of more judgment and result in additional disclosures.

The Company adopted the new guidance on October 1, 2018 following the modified retrospective method of transition. The Company applied the new guidance to contracts that were not completed at the date of initial adoption, resulting in a reduction of retained earnings by $60.4 million, after-tax, at that date. For contracts that were modified prior to October 1, 2018, the Company considered the aggregate impact of all modifications that occurred prior to the effective date of the standard for purposes of identifying performance obligations, determining transaction price and allocating transaction price to performance obligations. Prior period comparative information was not recast to reflect the impact of the new guidance and therefore continues to be reported under the accounting guidance in effect during those periods.

Under the new guidance, the majority of the Company’s contracts with the U.S. government will follow an over time model using the cost-to-cost method to measure performance. Previously the Company had recognized revenue from these contracts on the percentage of completion method using either the cost-to-cost or the units-complete method. In addition, the new guidance changes the definition of a contract, resulting in the Company no longer considering unexercised government options in the measurement of completion and profitability. The new guidance is expected to result in additional volatility in the Company’s earnings based upon the date of receipt of contract orders.

In the fire & emergency segment, the point in time at which “control transfers” to the customer differs from when the Company no longer maintains “risk of loss”, which under the new guidance delays the point in time at which the

Company will recognize revenue on contracts for which the end user, rather than the Company's dealer, is the Company's customer. In the commercial segment, the Company builds certain units on chassis owned by the end customer. Revenue related to these arrangements moves from a point in time revenue recognition model to an over time model that will be measured using the cost-to-cost method of percentage-of-completion as the Company is enhancing a customer asset. In addition, under the new guidance, the Company defers revenue, including the estimated profit, for service warranties instead of recording a liability for estimated costs.

See Note 3 of the Notes to Condensed Consolidated Financial Statements for additional information regarding the Company's revenue recognition method under the new revenue guidance.

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OSHKOSH CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The cumulative effect of initially applying the new revenue recognition guidance to the Company's Consolidated Financial Statements as of October 1, 2018 was as follows (in millions):

	Balance as of September 30, 2018	Cumulative Impact from Adopting New Revenue Standard	Balance as of October 1, 2018
Assets			
Receivables, net	$ 1,521.6	$ (248.9)	$ 1,272.7
Unbilled receivables, net	—	309.7	309.7
Inventories, net	1,227.7	(75.9)	1,151.8
Other current assets	66.0	0.3	66.3
Total current assets	3,269.9	(14.8)	3,255.1
Other long-term assets	65.9	18.7	84.6
Total assets	5,294.2	3.9	5,298.1
Liabilities and Shareholders' Equity			
Customer advances	$ 444.9	$ 27.2	$ 472.1
Other current liabilities	275.8	6.4	282.2
Total current liabilities	1,690.1	33.6	1,723.7
Other long-term liabilities	272.6	30.7	303.3
Retained earnings	2,007.9	(60.4)	1,947.5
Total shareholders' equity	2,513.5	(60.4)	2,453.1
Total liabilities and shareholders' equity	5,294.2	3.9	5,298.1

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OSHKOSH CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The impact from adopting the new revenue recognition guidance on the Company's Condensed Consolidated Financial Statements as of and for the three-month period ended December 31, 2018 was as follows (in millions):

	Three Months Ended December 31, 2018		
	As Reported	Previous Accounting Guidance	Impact of New Revenue Recognition Standard
Condensed Consolidated Statement of Income			
Net sales	$1,803.4	$ 1,765.3	$ 38.1
Cost of sales	1,475.1	1,462.2	12.9
Gross income	$328.3	$ 303.1	$ 25.2
Operating income	$160.5	$ 135.3	$ 25.2
Income before income taxes and earnings of unconsolidated affiliates	$147.8	$ 122.6	$ 25.2
Provision for income taxes	39.7	33.7	6.0
Income before earnings of unconsolidated affiliates	108.1	88.9	19.2
Equity in earnings of unconsolidated affiliates	0.9	0.9	—
Net income	$109.0	$ 89.8	$ 19.2
Earnings per share:			
Basic	$1.53	$ 1.26	$ 0.27
Diluted	1.51	1.25	0.26

	December 31, 2018		
	As Reported	Previous Accounting Guidance	Impact of New Revenue Recognition Standard
Condensed Consolidated Balance Sheet			
Assets			
Receivables, net	$1,072.1	$ 1,349.2	$ (277.1)
Unbilled receivables, net	342.9	—	342.9
Inventories, net	1,291.6	1,356.5	(64.9)
Other current assets	77.7	77.6	0.1
Total current assets	2,944.2	2,943.1	1.1
Other long-term assets	133.6	120.9	12.7
Total assets	5,030.1	5,016.3	13.8
Liabilities and Shareholders' Equity			
Customer advances	$425.2	$ 416.5	$ 8.7
Other current liabilities	324.8	311.5	13.3

Total current liabilities	1,478.2	1,456.2	22.0	
Other long-term liabilities	322.4	289.4	33.0	
Retained earnings	2,090.8	2,132.0	(41.2	)
Total shareholders’ equity	2,411.2	2,452.4	(41.2	)
Total liabilities and shareholders’ equity	5,030.1	5,016.3	13.8	

In October 2016, the FASB issued ASU 2016-16, Income Taxes (Topic 740), Intra-Entity Transfers of Assets Other Than Inventory. The standard requires that an entity recognize the income tax consequences of an intra-entity transfer of an asset when the transfer occurs as opposed to when the asset is transferred to an outside party. The standard does not apply to intra-entity transfers of inventory. The Company adopted ASU 2016-16 on October 1, 2018 following the modified retrospective approach through a cumulative effect adjustment, which resulted in an increase to retained earnings of $44.5 million.

In March 2017, the 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 standard requires that an entity report the service cost component of net periodic pension and postretirement cost in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The remaining components of net benefit costs are required to be presented in the income statement separately from the service component and outside a subtotal of income from operations. The amendment further allows only the service cost component of net periodic pension and postretirement costs to be eligible for capitalization, when applicable. The Company adopted ASU 2017-07 on October 1, 2018. The impact of this standard was a reclassification of $0.7 million of other components of net periodic pension cost to “Miscellaneous, net” on the Condensed Consolidated Statement of Income for the three months ended December 31, 2017. The Company utilized a practical expedient included in the ASU which allowed the Company to use amounts previously disclosed in its Employee Benefit Plans footnote for the prior period as the estimation basis for applying the required retrospective presentation requirements.

In February 2018, the FASB issued ASU 2018-02, Income Statement—Reporting Comprehensive Income (Topic 220), Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The standard allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the U.S. Tax Cuts and Jobs Act (the “Tax Reform Act”), thereby eliminating the resulting stranded tax effect. The Company adopted ASU 2018-02 on October 1, 2018. The Company increased retained earnings by $9.1 million upon adoption of ASU 2018-02 to eliminate the tax effects stranded in accumulated other comprehensive income resulting from the Tax Reform Act.

Standards not yet adopted

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), and has since issued amendments to this standard, which requires lessees to reflect most leases on their balance sheet as lease liabilities with corresponding right-of-use assets, while leaving presentation of lease expense in the statement of income largely unchanged. The standard also eliminates the real-estate specific provisions that exist under current U.S. GAAP and modifies the classification criteria and accounting lessors must apply to sales-type and direct financing leases. The Company will be required to adopt ASU 2016-02 and related amendments to the standard as of October 1, 2019. The Company is currently evaluating the impact of ASU 2016-02 on the Company’s consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments. The standard requires a change in the measurement approach for credit losses on financial assets measured on an amortized cost basis from an incurred loss method to an expected loss method, thereby eliminating the requirement that a credit loss be considered probable to impact the valuation of a financial asset measured on an amortized cost basis. The standard requires the measurement of expected credit losses to be based on relevant information about past events, including historical experience, current conditions, and a reasonable and supportable forecast that affects the collectability of the related financial asset. The Company will be required to

adopt ASU 2016-13 as of October 1, 2020. Early adoption is permitted. The Company is currently evaluating the impact of ASU 2016-13 on the Company's consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350), Simplifying the Test for Goodwill Impairment. The standard simplifies the measurement of goodwill impairment by eliminating the requirement that an entity compute the implied fair value of goodwill based on the fair values of its assets and liabilities to measure impairment. Instead, goodwill impairment will be measured as the difference between the fair value of the reporting unit and the carrying value of the reporting unit. The standard also clarifies the treatment of the income tax effect of tax deductible goodwill when measuring goodwill impairment loss. The Company will be required to adopt ASU 2017-04 as of October 1, 2020. Early adoption is permitted. The Company is currently evaluating the impact of ASU 2017-04 on the Company's consolidated financial statements.

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3. Revenue Recognition

Revenue is recognized when control of the goods or services promised under the contract are transferred to the customer either at a point in time (e.g. upon delivery) or over time (e.g., as the Company performs under the contract) in an amount that reflects the consideration to which the Company expects to be entitled in exchange for the goods or services. The Company accounts for a contract when it has approval and commitment from both parties, the rights and payment terms of the parties are identified, the contract has commercial substance and collectability of consideration is probable. If collectability is not probable, the sale is deferred until collection becomes probable or payment is received.

Contracts are reviewed to determine whether there is one or multiple performance obligations. A performance obligation is a promise to transfer a distinct good or service to a customer and represents the unit of accounting for revenue recognition. For contracts with multiple performance obligations, the expected consideration (e.g., the transaction price) is allocated to each performance obligation identified in the contract based on the relative standalone selling price of each performance obligation, which are determinable based on observable stand alone selling prices or are estimated using an expected cost plus a margin approach. Revenue is then recognized for the transaction price allocated to the performance obligation when control of the promised goods or services underlying the performance obligation is transferred. When the amount of consideration allocated to a performance obligation through this process differs from the invoiced amount, it results in a contract asset or liability. The identification of performance obligations within a contract requires significant judgment.

The following is a description of the primary activities from which the Company generates revenue.

Access equipment, Fire & emergency and Commercial segments revenue

The Company derives revenue in the access equipment, fire & emergency and commercial segments (non-defense segments) through the sale of machinery, vehicles and related aftermarket parts and services. Customers include distributors and end-users. Contracts with customers generally exist upon the approval of a quote and/or purchase order by the Company and customer. Each contract is also assessed at inception to determine whether it is necessary to combine the contract with other contracts.

The Company’s non-defense segments offer various customer incentives within contracts, such as sales and marketing rebates, volume discounts and interest subsidies, some of which are variable and therefore must be estimated by the Company. Transaction prices may also be impacted by rights of return, primarily within the aftermarket parts business, which requires the Company to record a liability and asset representing its rights and obligations in the event a return occurs. The estimated return liability is based on historical experience rates.

Revenue for performance obligations consisting of machinery, vehicle and after-market parts (together “product”) is recognized when the customer obtains control of the product, which typically occurs at a point in time, based on the shipping terms within the contract. In the commercial segment, concrete mixer and refuse products are sold both on Company owned chassis and customer owned chassis. When performing work on a customer owned chassis, revenue is recognized over time based on the cost-to-cost method, as the Company is enhancing a customer owned asset.

All non-defense segments offer aftermarket services related to their respective products such as repair, refurbishment and maintenance (together “services”). The Company generally recognizes revenue on service performance obligations over time using the method that results in the most faithful depiction of transfer of control to the customer.
Non-defense segments also offer extended warranty coverage as an option on most products. The Company considers extended warranties to be service-type warranties and therefore a performance obligation. Service-type warranties differ from the Company’s standard, or assurance-type warranties, as they are generally separately priced and negotiated as part of the contract and/or provide additional coverage beyond what the customer or customer group that purchases the product would receive under an assurance-type warranty. The Company has concluded that its extended warranties are stand-ready obligations to perform and therefore recognizes revenue ratably over the coverage period.
The Company also provides a standard warranty on its products and services at no additional cost to its customers in most instances. See Note 13 of the Notes to Condensed Consolidated Financial Statements for further discussion on product assurance warranties.

Defense segment revenue

The majority of the Company's defense segment net sales are derived through long-term contracts with the U.S. government to design, develop, manufacture or modify defense products. These contracts, which also include those under the U.S. Government-sponsored Foreign Military Sales (FMS) program, accounted for approximately 90% of defense segment revenue in fiscal 2018. Contracts with defense segment customers are generally fixed-price or cost-reimbursement type contracts. Under fixed-price contracts, the price paid to the Company is generally not adjusted to reflect the Company's actual costs except for costs incurred as a result of contract modifications. Certain fixed-price contracts include an incentive component under which the price paid to the Company is subject to adjustment based on the actual costs incurred. Under cost-reimbursement contracts the price paid to the Company is determined based on the allowable costs incurred to perform plus a fee. The fee component of cost-reimbursement contracts can be fixed based on negotiations at contract inception or can vary based on performance against target costs established at the time of contract inception. The Company will also design, develop, manufacture or modify defense products for international customers through Direct Commercial Sale contracts. The defense segment supports its products through the sale of aftermarket parts and services. Aftermarket contracts can range from long-term supply agreements to ad hoc purchase orders for replacement parts.

The Company evaluates the promised goods and services within defense segment contracts at inception to identify performance obligations. The goods and services in defense segment contracts are typically not distinct from one another as they are generally customized, have complex inter-relationships and the Company is responsible for overall management of the contract. As a result, defense segment contracts are typically accounted for as a single performance obligation. The defense segment provides standard warranties for its products for periods that typically range from one to two years. These assurance-type warranties typically cannot be purchased separately and do not meet the criteria to be considered a performance obligation. See Note 13 of the Notes to Condensed Consolidated Financial Statements for further discussion on product assurance warranties.

The Company determines the transaction price for each contract at inception based on the consideration that it expects to receive for the goods and services promised under the contract. This determination is made based on the Company's current rights, excluding the impact of any subsequent contract modifications (including unexercised options) until they become legally enforceable. Contract modifications frequently occur within the defense segment. The Company evaluates each modification to identify changes that impact price or scope of its contracts, which are then assessed to determine if the modification should be accounted for as an adjustment to an existing contract or as a separate contract. Contract modifications within the defense segment are generally accounted for as a cumulative effect adjustment to existing contracts as they are not distinct from the goods and services within the existing contract.

For defense segment contracts that include a variable component of the sale price, the Company estimates variable consideration. Variable consideration is included within the contract's transaction price to the extent it is probable that a significant reversal of revenue will not occur. The Company evaluates its estimates of variable consideration on an ongoing basis and any adjustments are accounted for as changes in estimates in the period identified. Common forms of variable consideration within defense segment contracts include cost reimbursement contracts that contain incentives, customer reimbursement rights and regulatory or customer negotiated penalties tied to contract performance.

The Company recognizes revenue on defense segment contracts as performance obligations are satisfied and control of the underlying goods and services is transferred to the customer. In making this evaluation, the defense segment

considers contract terms, payment terms and whether there is an alternative future use for the good or service. Through this process the Company has concluded that substantially all of the defense segment's performance obligations, including a majority of performance obligations for aftermarket goods and services, transfer to the customer continuously during the contract term and therefore revenue is recognized over time. For U.S. government and FMS contracts, this determination is supported by the inclusion of clauses within contracts that allow the customer to terminate a contract at its convenience. When the clause is present, the Company is entitled to compensation for the work performed through the date of notification at a price that reflects actual costs plus a reasonable margin in exchange for transferring its work in process to the customer. For contracts that do not contain termination for convenience provisions, the Company is generally able to support the continuous transfer of control determination as a result of the customized nature of its goods and services and contractual rights.

The defense segment recognizes revenue on its performance obligations that are satisfied over time by measuring progress using the cost-to-cost method of percentage-of-completion because it best depicts the transfer of control to the customer. Under the cost-to-cost method of percentage-of-completion, the defense segment measures progress based on the ratio of costs incurred to date to total estimated costs for the performance obligation. The Company recognizes changes in estimated sales or costs and

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the resulting profit or loss on a cumulative basis. Cumulative estimate-at completion (EAC) adjustments represent the cumulative effect of the changes on prior periods. If a loss is expected on a performance obligation, the complete estimated loss is recorded in the period in which the loss is identified. For contracts with only aftermarket parts performance obligations, revenue is recognized at the time the parts are physically committed to the order or based on shipping terms depending on whether the contracts contain a termination for convenience clause. For performance obligations consisting solely of services, revenue is recognized by either using the cost-to-cost method of percentage-of-completion method or as the Company has the right to bill the customer in instances that billing rights approximates timing of transfer of control to the customer.

There is significant judgment involved in estimating sales and costs within the defense segment. Each contract is evaluated at contract inception to identify risks and estimate revenue and costs. In performing this evaluation, the defense segment considers risks of contract performance such as technical requirements, schedule, duration and key contract dependencies. These considerations are then factored into the Company’s estimated revenue and costs. Preliminary contract estimates are subject to change throughout the duration of the contract as additional information becomes available that impacts risks and estimated revenue and costs. In addition, as contract modifications (e.g. new orders) are received, the additional units are factored into the overall contract estimate of costs and transaction price. Contract adjustments in the defense segment increased net sales, operating income, net income and diluted earnings per share during the three months ended December 31, 2018 by $31.6 million, $30.3 million, $23.2 million and $0.32 per share, respectively.

Disaggregation of Revenue

The table below presents consolidated net sales disaggregated by segment and timing of revenue recognition (in millions):

	Three Months Ended December 31, 2018					
	Access equipment	Defense	Fire & emergency	Commercial	Corporate and Intersegment Eliminations	Total
Point in time	$807.8	$0.3	$ 290.9	$ 121.2	$ (4.9)	$1,215.3
Over time	18.7	463.8	4.6	101.0	—	588.1
	$826.5	$464.1	$ 295.5	$ 222.2	$ (4.9)	$1,803.4

See Note 19 of the Notes to Condensed Consolidated Financial Statements for further disaggregated sales information.

Contract Assets and Contract Liabilities

The Company is generally entitled to bill its customers upon satisfaction of its performance obligations, with the exception of its long-term contracts in the defense segment which typically allow for billing upon acceptance of the finished good, advance payments from customers primarily within the fire & emergency segment and extended warranties that are usually billed in advance of the warranty coverage period. Customer payment is usually received shortly after billing and payment terms generally do not exceed one year. With the exception of the fire & emergency segment, the Company’s contracts typically do not contain a significant financing component. In the fire & emergency segment, customers earn interest on customer advances at a rate determined in a separate financing transaction

between the fire & emergency segment and the customer at contract inception. Interest due on customer advances of $3.6 million and $4.6 million was recorded in “Interest expense” in the Condensed Consolidated Statements of Income for the three months ended December 31, 2018 and 2017, respectively.

The timing of billing does not always match the timing of revenue recognition. In instances where a customer pays consideration in advance or when the Company is entitled to bill a customer in advance of recognizing the related revenue, the Company records a contract liability within “Customer advances”, “Other current liabilities” or “Other long-term liabilities” in the Condensed Consolidated Balance Sheet. Total contract liabilities were $549.0 million as of December 31, 2018, of which $425.2 million, $74.9 million and $48.9 million was included in “Customer advances”, “Other current liabilities” and “Other long-term liabilities”, respectively. The Company reduces contract liabilities when revenue is recognized. The Company recognized $236.0 million of revenue that was recorded as a contract liability as of the beginning of the period during the three months ended December 31, 2018.

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In instances where the Company recognizes revenue prior to having an unconditional right to payment, the Company records a contract asset within "Unbilled receivables, net" in the Condensed Consolidated Balance Sheet. The Company reduces contract assets when the Company has an unconditional right to payment. The Company periodically assesses its contract assets for impairment.

Contract assets and liabilities are determined on a net basis for each contract. The Company did not record any impairment losses on contracts from customers during the three-month period ended December 31, 2018. See Note 8 of the Notes to Condensed Consolidated Financial Statements for additional information on the Company's receivable balances.

The Company offers a variety of service-type warranties, including optionally priced extended warranty programs. Revenue related to service warranties is deferred until after the expiration of the standard warranty period. The revenue is then recognized in income over the term of the extended warranty period in proportion to the costs that are expected to be incurred. Changes in the Company's service-type warranties were as follows (in millions):

	Three Months Ended December 31,	
	2018	2017
Balance at beginning of period	$30.7	$30.8
Adoption of ASC 606	35.7	