

CUMMINS INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 19. LEASES (Continued)

penalty. For each of these leases we have the option to purchase the equipment at the end of the lease term for one dollar. The equipment under these leases is capitalized and amortized over its estimated useful life. As of December 31, 2007 and 2006, we had outstanding capital leases under this program of \$58 million and \$69 million, respectively. Future lease payments, including repurchase obligations, under each lease are included in the table above.

Sale and Leaseback Transactions

In 2001, we entered into a sale-leaseback agreement whereby we sold and leased back certain heavy-duty engine manufacturing equipment from a grantor trust wholly-owned by a financial institution. The lease was classified as an operating lease with a lease term of 11.5 years, expiring June 28, 2013, and includes an early buyout purchase option on January 14, 2009. The early buyout option can be exercised for approximately \$35 million, or 28 percent of the equipment's fair market value at the inception of the lease. If we do not exercise the option, we are obligated to purchase insurance that insures the equipment's residual value. At the end of the lease term, we are obligated to pay the difference, if any, between the equipment's guaranteed residual value and its fair market value.

The lease agreement includes certain default provisions requiring us to make timely rent payments, maintain, service, repair and insure the equipment, procure residual value insurance and maintain minimum debt ratings for our long-term senior unsecured debt obligations.

In December 2003, the grantor trust which acts as the lessor in the sale and leaseback transaction described above was consolidated due to the adoption of FIN 46R. A description of the entity consolidated and the impact of adopting FIN 46R are described in Note 3. As a result of the consolidation, the manufacturing equipment and the trust's obligations under its non-recourse debt arrangement are included in our *Consolidated Balance Sheets* as property, plant and equipment and long-term debt, respectively. The non-recourse debt arrangement is more fully discussed in Note 10. In addition, our *Consolidated Statements of Earnings* includes interest expense on the lessor's debt obligations and depreciation expense on the manufacturing equipment rather than rent expense under the lease agreement. The amount of interest expense in 2007, 2006 and 2005 was \$4 million, \$5 million and \$6 million, respectively. The amount of depreciation expense in 2007, 2006 and 2005 was \$12 million, \$17 million and \$14 million, respectively.

NOTE 20. SALES OF ACCOUNTS RECEIVABLE

In January 2004, we entered into a three-year facility agreement with a financial institution to sell a designated pool of trade receivables to Cummins Trade Receivables, LLC (CTR), a wholly-owned special purpose subsidiary. In July 2007, we amended the agreement to extend the facility until July 2010, and raised the purchase limitation from \$200 million to \$400 million. The agreement also provides us with an option to increase the purchase limitation up to \$500 million upon approval. As necessary, CTR may transfer a direct interest in its receivables, without recourse, to the financial institution. To maintain a balance in the designated pools of receivables sold, we sell new receivables to CTR as existing receivables are collected. Receivables sold to CTR in which an interest is not transferred to the financial institution are included in "Receivables, net" on our *Consolidated Balance Sheets*. The maximum interest in sold receivables that can be outstanding at any point in time is limited to the lesser of \$400 million or the amount of eligible receivables held by CTR. There are no provisions in this agreement that require us to maintain a minimum investment credit rating; however, the terms of the agreement contain the same financial covenants as our revolving credit facility (See Note 10). As of December 31, 2007 and 2006, there were no amounts outstanding under this program.

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NOTE 20. SALES OF ACCOUNTS RECEIVABLE (Continued)

No accounts receivable sold to CTR were written off during 2007, 2006 or 2005. The sold receivables servicing portfolio, which is included in receivables and the proceeds from the sale of receivables and other related cash flows are as follows:

	As of and for the years ended December 31,		
	2007	2006	2005
	Millions		
Sold receivables servicing portfolio	\$ 759	\$ 719	\$ 605
Proceeds outstanding from receivable sales	—	—	—
Receivables sold to special purpose subsidiary	6,615	6,368	5,706
Collections reinvested in special purpose subsidiary	6,575	6,254	5,517
Servicing fees and interest	1	1	1

NOTE 21. OPERATING SEGMENTS

SFAS No. 131, “Disclosures about Segments of an Enterprise and Related Information,” set standards for reporting information regarding operating segments in financial statements. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision-maker, or decision making group, in deciding how to allocate resources and in assessing performance. Cummins chief operating decision-maker (CODM) is the Chief Executive Officer.

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

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

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