GENESEE & WYOMING INC
Form 10-Q
November 06, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2018

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ________ to ________

Commission File Number 001-31456

GENESEE & WYOMING INC.
(Exact name of registrant as specified in its charter)

Delaware	06-0984624
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

20 West Avenue, Darien, Connecticut 06820
(Address of principal executive offices)(Zip Code)
(203) 202-8900
(Registrant's telephone number, including area code)

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. x Yes o No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). x 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	x	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 Exchange Act). o Yes x No

Shares of common stock outstanding as of the close of business on November 1, 2018:

Class	Number of Shares Outstanding
Class A Common Stock	58,390,843
Class B Common Stock	541,138

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Unless the context otherwise requires, when used in this Quarterly Report on Form 10-Q, the terms "Genesee & Wyoming," "G&W," the "Company," "we," "our" and "us" refer to Genesee & Wyoming Inc. and its subsidiaries. All references to currency amounts included in this Quarterly Report on Form 10-Q, including the financial statements, are in United States dollars unless specifically noted otherwise. The term carload represents physical railcars and the estimated railcar equivalents of commodities transported by metric ton or other measure, as well as intermodal units. From time to time, we may use our website as a channel of distribution of material company information. Financial and other material information regarding the Company is routinely posted on and accessible at www.gwrr.com/investors. In addition, you may automatically receive email alerts and other information about us by enrolling your email address in the "Email Alerts" section of www.gwrr.com/investors. The information contained on or connected to our Internet website is not deemed to be incorporated by reference in this Quarterly Report or filed with the Securities and Exchange Commission.

Forward-Looking Statements

This report and other documents referred to in this report contain forward-looking statements regarding future events and the future performance of Genesee & Wyoming Inc. that are based on current expectations, estimates and projections about our industry, our business and our performance, management's beliefs and assumptions made by management. Words such as "anticipates," "intends," "plans," "believes," "could," "should," "seeks," "expects," "will," "estimates," "trends," "outlook," variations of these words and similar expressions are intended to identify these forward-looking statements. These statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to forecast, including the following: risks related to the operation of our railroads; severe weather conditions and other natural occurrences, which could result in shutdowns, derailments, railroad network and port congestion or other substantial disruption of operations; customer demand and changes in our operations or loss of important customers; exposure to the credit risk of customers and counterparties; changes in commodity prices; consummation and integration of acquisitions; implementation of restructuring plans; economic, political and industry conditions, including employee strikes or work stoppages; retention and contract continuation; our ability to attract and retain skilled workers; legislative and regulatory developments, including changes in environmental and other laws and regulations to which we or our customers are subject; increased competition in relevant markets; funding needs and financing sources, including our ability to obtain government funding for capital projects; international complexities of operations, currency fluctuations, finance, tax and decentralized management; challenges of managing rapid growth, including retention and development of senior leadership; unpredictability of fuel costs; susceptibility to and outcome of various legal claims, lawsuits and arbitrations; increase in, or volatility associated with, expenses related to estimated claims, self-insured retention amounts and insurance coverage, collectability and limits; consummation of new business opportunities; decrease in revenues and/or increase in costs and expenses; susceptibility to the risks of doing business in foreign countries; uncertainties arising from a referendum in which voters in the United Kingdom (U.K.) approved an exit from the European Union (E.U.), commonly referred to as Brexit; our ability to integrate acquired businesses successfully or to realize the expected synergies associated with acquisitions; risks associated with our substantial indebtedness; failure to maintain satisfactory working relationships with partners in Australia; failure to maintain an effective system of internal control over financial reporting as well as disclosure controls and procedures and other risks including, but not limited to, those set forth in Part II Item 1A of this Quarterly Report on Form 10-Q, if any, and those noted in our 2017 Annual Report on Form 10-K under "Risk Factors." Therefore, actual results may differ materially from those expressed or forecasted in any such forward-looking statements. Forward-looking statements speak only as of the date of this report or as of the date they were made. We do not undertake, and expressly disclaim, any duty to publicly update any forward-looking statement, whether as a result of new information, future events, or otherwise, except as required by law.

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PART I - FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS.
GENESEE & WYOMING INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
AS OF SEPTEMBER 30, 2018 and DECEMBER 31, 2017 (Unaudited)
(dollars in thousands, except per share and share amounts)

	September 30, 2018	December 31, 2017
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 74,067	$ 80,472
Accounts receivable, net	441,105	416,705
Materials and supplies	52,517	57,750
Prepaid expenses and other	54,292	34,606
Total current assets	621,981	589,533
PROPERTY AND EQUIPMENT, net	4,613,295	4,656,921
GOODWILL	1,128,580	1,165,587
INTANGIBLE ASSETS, net	1,466,137	1,567,038
DEFERRED INCOME TAX ASSETS, net	3,883	3,343
OTHER ASSETS	70,122	52,475
Total assets	$ 7,903,998	$ 8,034,897
LIABILITIES AND EQUITY		
CURRENT LIABILITIES:		
Current portion of long-term debt	$ 25,138	$ 27,853
Accounts payable	271,539	253,993
Accrued expenses	171,011	185,935
Total current liabilities	467,688	467,781
LONG-TERM DEBT, less current portion	2,300,556	2,303,442
DEFERRED INCOME TAX LIABILITIES, net	866,821	873,194
DEFERRED ITEMS - grants from outside parties	323,370	321,592
OTHER LONG-TERM LIABILITIES	162,993	172,796
COMMITMENTS AND CONTINGENCIES		
EQUITY:		
Class A Common Stock, $0.01 par value, one vote per share; 180,000,000 shares authorized at September 30, 2018 and December 31, 2017; 75,199,229 and 74,808,305 shares issued and 58,737,895 and 61,946,078 shares outstanding (net of 16,461,334 and 12,862,227 shares in treasury) on September 30, 2018 and December 31, 2017, respectively	752	748
Class B Common Stock, $0.01 par value, ten votes per share; 30,000,000 shares authorized at September 30, 2018 and December 31, 2017; 541,138 and 701,138 shares issued and outstanding on September 30, 2018 and December 31, 2017, respectively	5	7
Additional paid-in capital	1,779,168	1,757,332
Retained earnings	2,426,690	2,234,864
Accumulated other comprehensive loss	(135,076)	(105,534)
Treasury stock, at cost	(510,245)	(236,951)
Total Genesee & Wyoming Inc. stockholders' equity	3,561,294	3,650,466
Noncontrolling interest	221,276	245,626
Total equity	3,782,570	3,896,092
Total liabilities and equity	$ 7,903,998	$ 8,034,897

The accompanying notes are an integral part of these consolidated financial statements.

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GENESEE & WYOMING INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2018 and 2017 (Unaudited)
(in thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
OPERATING REVENUES	$603,304	$576,927	$1,772,955	$1,636,468
OPERATING EXPENSES:				
Labor and benefits	175,853	169,576	539,407	500,936
Equipment rents	35,325	33,291	104,214	100,399
Purchased services	53,717	68,562	178,864	176,358
Depreciation and amortization	65,392	64,222	197,127	186,509
Diesel fuel used in train operations	45,713	34,535	137,487	105,718
Electricity used in train operations	2,742	765	7,020	6,072
Casualties and insurance	9,912	10,624	32,862	33,346
Materials	32,744	30,664	97,589	77,861
Trackage rights	22,838	22,632	67,119	66,652
Net gain on sale and impairment of assets	(642)	(315)	(2,501)	(1,096)
Restructuring costs	3,286	2,628	12,931	8,744
Other expenses, net	28,604	29,901	82,978	89,494
Total operating expenses	475,484	467,085	1,455,097	1,350,993
OPERATING INCOME	127,820	109,842	317,858	285,475
Interest income	417	463	1,499	1,271
Interest expense	(26,429)	(28,281)	(80,605)	(80,431)
Other income/(loss), net	1,515	1,868	(237)	4,519
Income before income taxes	103,323	83,892	238,515	210,834
Provision for income taxes	(31,013)	(30,507)	(41,569)	(82,032)
Net income	$72,310	$53,385	$196,946	$128,802
Less: Net income attributable to noncontrolling interest	2,720	3,145	8,090	6,317
Net income attributable to Genesee & Wyoming Inc.	$69,590	$50,240	$188,856	$122,485
Basic earnings per common share attributable to Genesee & Wyoming Inc. common stockholders:	$1.18	$0.82	$3.13	$1.99
Weighted average shares – Basic	59,168	61,629	60,343	61,518
Diluted earnings per common share attributable to Genesee & Wyoming Inc. common stockholders:	$1.16	$0.80	$3.08	$1.96
Weighted average shares – Diluted	60,131	62,477	61,255	62,399

The accompanying notes are an integral part of these consolidated financial statements.

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GENESEE & WYOMING INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2018 and 2017 (Unaudited)
(dollars in thousands)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
NET INCOME	$72,310	$53,385	$196,946	$128,802
OTHER COMPREHENSIVE INCOME/(LOSS):				
Foreign currency translation adjustment	(9,501)	32,902	(59,042)	100,054
Net unrealized gain on qualifying cash flow hedges, net of tax (provision) of ($1,583), ($303), ($4,612) and ($567), respectively	5,153	736	14,756	638
Changes in pension and other postretirement benefits, net of tax (provision)/benefit of ($14), ($20), ($42) and $887, respectively	43	38	129	(2,149)
Other comprehensive (loss)/income	(4,305)	33,676	(44,157)	98,543
COMPREHENSIVE INCOME	$68,005	$87,061	$152,789	$227,345
Less: Comprehensive (loss)/income attributable to noncontrolling interest	(2,179)	8,500	(9,495)	24,663
COMPREHENSIVE INCOME ATTRIBUTABLE TO GENESEE & WYOMING INC.	$70,184	$78,561	$162,284	$202,682

The accompanying notes are an integral part of these consolidated financial statements.

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GENESEE & WYOMING INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2018 and 2017 (Unaudited)
(dollars in thousands)

	G&W Stockholders							
	Class A Common Stock	Class B Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Treasury Stock	Non-controlling Interest	Total Equity
BALANCE, December 31, 2016	$742	$ 8	$1,709,615	$1,685,813	$(197,316)	$(232,348)	$220,607	$3,187,121
Net income	—	—	—	122,485	—	—	6,317	128,802
Other comprehensive income	—	—	—	—	80,197	—	18,346	98,543
Conversion of 45,000 shares Class B Common Stock to Class A Common Stock	1	(1)	—	—	—	—	—	—
Value of stock issued for stock-based compensation - 296,580 shares Class A Common Stock	2	—	8,001	—	—	—	—	8,003
Settlement of deferred stock awards - 17,661 shares	—	—	738	—	—	—	—	738
Compensation cost related to stock-based compensation	—	—	13,309	—	—	—	—	13,309
Value of treasury stock repurchased - 44,114 shares	—	—	—	—	—	(3,275)	—	(3,275)
Other	—	—	444	—	—	—	(6)	438
BALANCE, September 30, 2017	$745	$ 7	$1,732,107	$1,808,298	$(117,119)	$(235,623)	$245,264	$3,433,679

	G&W Stockholders							
	Class A Common Stock	Class B Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Non-controlling Interest	Total Equity
BALANCE, December 31, 2017	$748	$ 7	$1,757,332	$2,234,864	$(105,534)	$(236,951)	$245,626	$3,896,092
Net income	—	—	—	188,856	—	—	8,090	196,946
Other comprehensive loss	—	—	—	—	(26,572)	—	(17,585)	(44,157)
Conversion of 160,000 shares Class B Common Stock to	2	(2)	—	—	—	—	—	—

Class A Common Stock								
Value of stock issued for stock-based compensation - 209,357 shares Class A Common Stock	2	—	7,812	—	—	—	—	7,814
Settlement of deferred stock awards - 21,567 shares	—	—	995	—	—	—	—	995
Compensation cost related to stock-based compensation	—	—	13,029	—	—	—	—	13,029
Value of treasury stock repurchased - 3,599,107 shares	—	—	—	—	—	(273,294)	—	(273,294)
Distribution to noncontrolling interest	—	—	—	—	—	—	(14,898)	(14,898)
Amounts reclassified from accumulated other comprehensive loss to retained earnings related to the United States Tax Cuts and Jobs Act	—	—	—	2,970	(2,970)	—	—	—
Other	—	—	—	—	—	—	43	43
BALANCE, September 30, 2018	$752	$ 5	$1,779,168	$2,426,690	$(135,076)	$(510,245)	$ 221,276	$3,782,570

The accompanying notes are an integral part of these consolidated financial statements.

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GENESEE & WYOMING INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2018 and 2017 (Unaudited)
(dollars in thousands)

	Nine Months Ended September 30,	
	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$196,946	$128,802
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	197,127	186,509
Stock-based compensation	13,029	13,354
Deferred income taxes	7,978	51,231
Net gain on sale and impairment of assets	(2,501)	(1,096)
Changes in assets and liabilities which provided/(used) cash, net of effect of acquisitions:		
Accounts receivable, net	(50,143)	(18,020)
Materials and supplies	3,133	8,998
Prepaid expenses and other	(11,663)	14,257
Accounts payable and accrued expenses	33,818	(41,529)
Other assets and liabilities, net	9,750	7,883
Net cash provided by operating activities	397,474	350,389
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(194,132)	(149,105)
Grant proceeds from outside parties	16,696	15,998
Net cash paid for acquisitions, net of cash acquired	—	(107,586)
Proceeds from sale of business	7,927	—
Proceeds from sale of investment	—	2,100
Insurance proceeds for replacement of assets	2,780	1,406
Proceeds from disposition of property and equipment	3,710	4,238
Other investing activities	(2,921)	—
Net cash used in investing activities	(165,940)	(232,949)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Principal payments on revolving line-of-credit, long-term debt and capital lease obligations	(766,713)	(498,925)
Proceeds from revolving line-of-credit and long-term borrowings	821,666	418,735
Debt amendment/issuance costs	(5,318)	—
Common share repurchases	(270,488)	—
Distribution to noncontrolling interest	(14,898)	—
Installment payments on Freightliner deferred consideration	(6,255)	—
Other financing related activities, net	5,006	4,728
Net cash used in financing activities	(237,000)	(75,462)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(939)	5,980
(DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS	(6,405)	47,958
CASH AND CASH EQUIVALENTS, beginning of period	80,472	32,319
CASH AND CASH EQUIVALENTS, end of period	$74,067	$80,277

The accompanying notes are an integral part of these consolidated financial statements.

1. PRINCIPLES OF CONSOLIDATION AND BASIS OF PRESENTATION:

The interim consolidated financial statements presented herein include the accounts of Genesee & Wyoming Inc. and its subsidiaries. All significant intercompany transactions and accounts have been eliminated in consolidation. These interim consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and are unaudited. They do not contain all disclosures which would be required in a full set of financial statements prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). In the opinion of management, the unaudited financial statements for the three and nine months ended September 30, 2018 and 2017 are presented on a basis consistent with the audited financial statements and contain all adjustments, consisting only of normal recurring adjustments, necessary to provide a fair statement of the results for the interim periods presented. The results of operations for interim periods are not necessarily indicative of results of operations for the full year. The consolidated balance sheet data for 2017 was derived from the audited financial statements in the Company's 2017 Annual Report on Form 10-K, but does not include all disclosures required by U.S. GAAP.

The results of operations of the foreign entities are maintained in the local currency of the respective subsidiary and translated into United States dollars at the applicable exchange rates for inclusion in the consolidated financial statements. As a result, any appreciation or depreciation of these currencies against the United States dollar will impact the Company's results of operations.

The interim consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2017 included in the Company's 2017 Annual Report on Form 10-K.

Certain reclassifications and adjustments have been made to prior period balances to conform to the current year presentation as noted below.

On January 1, 2018, the Company adopted ASU 2017-07, Compensation-Retirement Benefits (Topic 715), Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. Prior to the adoption of ASU 2017-07, the Company presented net pension costs within operating income on the same line item as other compensation costs arising from services rendered by the applicable employees. ASU 2017-07 requires that net pension costs, other than service cost, be presented outside of operating income. The Company applied these changes retrospectively to its consolidated statement of operations which resulted in a $1.6 million and $4.8 million decrease in operating income and a corresponding change in other income/(loss), net for the three and nine months ended September 30, 2017, respectively. The adjustments had no impact on net income.

On January 1, 2018, the Company adopted ASU 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220), Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The current standard, ASC Topic 740, requires deferred tax liabilities to be adjusted for the effect of a change in tax laws or rates with the effect included in income from operations in the reporting period of the enactment date. The Tax Cuts and Jobs Act of 2017 (the TCJA) enacted by the Unites States federal government resulted in tax effects of items recorded within accumulated other comprehensive income (AOCI) or accumulated other comprehensive loss (AOCL), as the case may be, to be "stranded," as those items no longer reflect the appropriate tax rate. This amendment allows the reclassification from AOCI/AOCL to retained earnings for the stranded tax effects resulting from the new income tax rates. The Company applied the amendments as of January 1, 2018 by reclassifying $3.0 million from AOCL to retained earnings, eliminating the stranded tax effects in AOCL resulting from the TCJA. This reclassification reduced AOCL and increased retained earnings by $3.0 million. It is the Company's policy to release income tax effects from AOCI/AOCL using the item-by-item approach.

On January 1, 2018, the Company adopted ASU 2014-09, Revenue from Contracts with Customers, which supersedes previous revenue guidance. The standard requires that the Company recognize revenue when it transfers the promised goods or services to customers in an amount that reflects the consideration the Company expects to receive in exchange for those goods or services. The Company adopted ASU 2014-09 and all related amendments using the modified retrospective approach. Under the standard, the Company continues to recognize freight revenue

proportionally as a shipment moves from origin to destination. The adoption did not affect the Company's financial condition, results of operations or liquidity. Disclosures related to the nature, amount and timing of revenue and cash flows resulting from contracts with customers are included in Note 4, Revenue.

On December 1, 2016, a subsidiary of the Company completed the acquisition of Glencore Rail (NSW) Pty Limited (GRail) and concurrently issued a 48.9% stake in G&W Australia Holdings LP (GWAHLP) (collectively, the Australia Partnership), which is the holding entity for all of the Company’s Australian businesses, including GRail, to a consortium of funds and clients managed by Macquarie Infrastructure and Real Assets (MIRA), a large infrastructure investment firm. The Company, through wholly-owned subsidiaries, also made incremental investments and retained a 51.1% ownership in GWAHLP. The investments made by both the Company and MIRA consisted of equity and debt financing of GWAHLP in similar proportions. As MIRA's investments were made at the contemporaneous fair value of GWAHLP as of December 1, 2016, accounting for MIRA's noncontrolling interest in the Company's consolidated financial statements required adjustments to reflect a proportional interest in the net book value of GWAHLP. During the three months ended March 31, 2018, the Company determined that there was an error in its December 1, 2016 calculation of the noncontrolling interest for MIRA's 48.9% equity interest, which resulted in the following adjustment within the total equity section of the Company's consolidated balance sheet: a decrease in noncontrolling interest of $71.9 million, an increase in additional paid-in capital of $57.9 million and a decrease in AOCL of $14.0 million. This revision has been reflected in the Company's consolidated balance sheet as of December 31, 2017 as well as the December 31, 2016 equity balances as disclosed in the Company's consolidated statements of changes in equity. There was no effect on any other section of the Company's balance sheet. This revision had no impact on the Company's consolidated statements of operations, comprehensive income or cash flows for the three and nine months ended September 30, 2018 and 2017. The Company does not consider this revision material to any previously issued consolidated financial statements.

When comparing the Company's results of operations from one reporting period to another, it is important to consider that the Company has historically experienced fluctuations in revenues and expenses due to acquisitions, changing economic conditions, fluctuations in commodity prices, competitive forces, changes in foreign currency exchange rates, rail network issues and congestion, the ability to attract and retain skilled workers, one-time freight moves, fuel price fluctuations, customer plant expansions and shutdowns, sales of property and equipment, derailments and weather-related conditions, such as hurricanes, cyclones, tornadoes, high winds, droughts, heavy snowfall, unseasonably hot or cold weather, freezing and flooding, among other factors. In periods when these events occur, the Company's results of operations are not easily comparable from one period to another. Finally, certain of the Company's railroads have commodity shipments that are sensitive to general economic conditions, global commodity prices and foreign exchange rates, such as steel products, iron ore, paper products, lumber and forest products and agricultural products, as well as product specific market conditions, such as the availability of lower priced alternative sources of power generation (coal) and energy commodity price differentials (crude oil and natural gas liquids) or congestion at ports (intermodal). Other shipments are relatively less affected by economic conditions and are more closely affected by other factors, such as winter weather (salt) and seasonal rainfall (agricultural products). As a result of these and other factors, the Company's results of operations in any reporting period may not be directly comparable to the Company's results of operations in other reporting periods.

2. CHANGES IN OPERATIONS:

North American Operations

Heart of Georgia Railroad, Inc.: On May 31, 2017, the Company completed the acquisition of all the outstanding shares of Atlantic Western Transportation, Inc., the parent company of Heart of Georgia Railroad, Inc. (HOG), for $5.6 million in cash and contingent consideration valued at $5.7 million. The contingent consideration is payable to the sellers upon satisfaction of certain conditions, which the Company expects to be paid in 2021. The results of operations from HOG have been included in the Company's consolidated statements of operations since the acquisition date.

HOG was founded in 1999 and operates 219 miles of track that runs across the State of Georgia. The track is leased from the Georgia Department of Transportation. It connects with the Company’s Georgia Southwestern Railroad at Americus, Georgia, and with the Company’s Georgia Central Railway at Vidalia, Georgia. HOG serves an inland intermodal terminal at Cordele, Georgia, providing five days per week, direct rail service via the Georgia Central

Railway to the Port of Savannah for auto, agricultural products and other merchandise customers. HOG has Class I railroad connections with CSX Corp. at Cordele and with Norfolk Southern at Americus and Helena, Georgia. HOG transports approximately 7,000 annual carloads of agricultural products, feed, fertilizer, and lumber and forest products.

Australian Operations

Arrium Limited: On April 7, 2016, Genesee & Wyoming Australia's (GWA) customer, Arrium Limited (Arrium) announced it had entered into voluntary administration. As a result, during the first quarter of 2016, the Company recorded a $13.0 million non-cash charge related to the impairment of GWA's idle rolling-stock maintenance facility and an allowance for doubtful accounts charge of $8.1 million. Also, as a result of the voluntary administration, all payments to GWA associated with the rail haulage agreement for Arrium's Southern Iron mine ceased.

On August 31, 2017, Arrium was sold to GFG Alliance. The steel making business was rebranded as Liberty OneSteel, and the mining business was rebranded as SIMEC Mining (SIMEC). Although the Southern Iron mine is still mothballed, GWA continues to provide services and receive payments under the rail haulage agreement for SIMEC's Middleback Range operations. Pursuant to that rail haulage agreement, GWA serves several iron ore mines in the Middleback Range and the Whyalla steelworks operations.

In December 2017, the Company recovered $0.9 million of cash in relation to the Company's previous agreements with Arrium. During the three and nine months ended September 30, 2018, the Company recorded $0.9 million and $7.3 million, respectively, of gains on settlement from additional cash recoveries of pre-petition claims associated with Arrium, which were recognized as offsets to other expenses, net in the Company’s consolidated statement of operations.

U.K./European Operations

Continental Europe Intermodal Business: In 2017, the Company ceased all "open" train services from the port of Rotterdam, closed its Continental Europe intermodal business, ERS Railways B.V. (ERS), offices in Rotterdam and Frankfurt, and the ERS customer services function in Warsaw. The Company recorded restructuring charges of $0.7 million and $5.2 million for the three and nine months ended September 30, 2017, respectively, primarily related to severance costs and costs associated with surplus locomotive and railcar leases at ERS.

On June 5, 2018, the Company finalized the sale of ERS for gross cash proceeds of €11.2 million (or $13.1 million at the exchange rate on June 5, 2018) or €6.8 million (or $7.9 million at the exchange rate on June 5, 2018) net of €4.4 million (or $5.2 million at the exchange rate on June 5, 2018) of cash on hand that transferred to the buyer. The sale resulted in a net loss of $1.4 million recognized in the Company’s consolidated statement of operations for the nine months ended September 30, 2018 within other income/(loss), net.

Pentalver Transport Limited: On May 3, 2017, the Company's subsidiary, GWI UK Acquisition Company Limited, purchased for cash all of the issued share capital of Pentalver Transport Limited (Pentalver) from a subsidiary of APM Terminals (a subsidiary of AP Møller-Maersk A/S) for £97.8 million (or $126.2 million at the exchange rate on May 3, 2017) or £77.5 million (or $100.1 million at the exchange rate on May 3, 2017) net of £20.2 million (or $26.1 million at the exchange rate on May 3, 2017) of cash received in connection with the sale. The Company funded the acquisition with borrowings under the Company's Second Amended and Restated Senior Secured Syndicated Credit Facility Agreement.

Headquartered in Southampton, U.K., Pentalver operates off-dock container terminals (most under long-term leases) strategically placed at each of the three major seaports of Felixstowe, Southampton and London Gateway, as well as an inland terminal located at Cannock, in the Midlands, near many of the nation’s largest distribution centers. In addition to providing storage for loaded and empty containers on over 100 acres of land, Pentalver also operates a trucking haulage service with more than 150 trucks, primarily providing daily service between the seaports of Felixstowe and Southampton and its inland terminal at Cannock. Pentalver also provides services related to container customization, maintenance and repair (including refrigerated containers) and is one of the largest sellers of new and used containers in the U.K.

Pentalver’s operations are complementary to those of the Company's Freightliner Group Limited (Freightliner) subsidiary, which is the largest rail maritime intermodal operator in the U.K. The logistics of maritime container transportation in the U.K. are highly competitive, whether by road, rail or short-sea, with a premium placed on timely, efficient and safe service. The results of operations from Pentalver have been included in the Company's consolidated statements of operations since the May 3, 2017 acquisition date.

The Company accounted for the acquisition as a business combination using the acquisition method of accounting under U.S. GAAP. The acquired assets and liabilities of Pentalver were recorded at their acquisition-date fair values and were consolidated with those of the Company as of the acquisition date. The foreign exchange rate used to translate the balance sheet to United States dollars was $1.29 for one British pound.

The acquisition date fair values were assigned to the acquired net assets as follows (amounts in thousands):

	GBP	USD
Cash and cash equivalents	£20,224	$26,117
Accounts receivable	16,849	21,759
Materials and supplies	13,360	17,253
Prepaid expenses and other	3,238	4,182
Property and equipment	20,649	26,666
Goodwill	8,592	11,096
Intangible assets	42,000	54,239
Total assets	124,912	161,312
Accounts payable and accrued expenses	21,341	27,560
Deferred income tax liabilities, net	5,220	6,741
Deferred items-grants from outside parties	601	776
Net assets	£97,750	$126,235

The $54.2 million of intangible assets relate to amortizable operational rights with contractual terms spanning up to 50 years and a weighted average amortization period of 33 years. The $11.1 million of goodwill will not be deductible for tax purposes.

3. EARNINGS PER COMMON SHARE:

The following table sets forth the computation of basic and diluted earnings per common share for the three and nine months ended September 30, 2018 and 2017 (in thousands, except per share amounts):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Numerators:				
Net income attributable to Genesee & Wyoming Inc.	$69,590	$50,240	$188,856	$122,485
Denominators:				
Weighted average Class A common shares outstanding – Basic	59,168	61,629	60,343	61,518
Weighted average Class B common shares outstanding	664	723	679	743
Dilutive effect of employee stock-based awards	299	125	233	138
Weighted average shares – Diluted	60,131	62,477	61,255	62,399
Earnings per common share attributable to Genesee & Wyoming Inc. common stockholders:				
Basic earnings per common share	$1.18	$0.82	$3.13	$1.99
Diluted earnings per common share	$1.16	$0.80	$3.08	$1.96

The following total number of shares of Class A Common Stock issuable under the assumed exercise of stock-based awards computed based on the treasury stock method were excluded from the calculation of diluted earnings per common share, as the effect of including these shares would have been antidilutive (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Antidilutive shares	704	1,245	1,045	1,302

Share Repurchase

In September of 2015, the Company's Board of Directors authorized the repurchase of up to $300 million of the Company's Class A Common Stock (the Repurchase Program), subject to certain limitations under the Company's credit facility. The table below presents information regarding shares repurchased by the Company under the Repurchase Program during the three and nine months ended September 30, 2018 (in thousands, except for per share amounts):

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018
Class A Common Stock repurchased	894	3,560
Average price paid per share of Class A Common Stock repurchased	$ 87.46	$ 75.99
Shares excluded from weighted-average basic shares outstanding	301	1,707

Repurchased shares are recorded in treasury stock, at cost, which includes any applicable commissions and fees. As of September 30, 2018, the remaining amount authorized for repurchase under the Repurchase Program was $29.5 million. In October 2018, the Company completed the $300 million Repurchase Program, and the Company's Board of Directors authorized a new $500 million repurchase plan of Class A Common Stock, subject to certain limitations under the Company's credit facility. See Note 6, Long-Term Debt, for additional information regarding the Company's credit facility.

4. REVENUE:

The Company classifies its operating revenues into the following three categories: freight, freight-related and all other. Revenue is recognized when obligations under the terms of a contract with a customer are satisfied. Revenue is measured as the amount of consideration the Company expects to receive in exchange for providing services. Certain of the countries in which the Company operates have a tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer. The Company records these taxes on a net basis.

The Company generates freight revenues from the haulage of freight by rail based on a per car, per container or per ton basis. Freight revenues are recognized over time as shipments move from origin to destination as the customer simultaneously receives and consumes the benefit. Related expenses are recognized as incurred.

The Company generates freight-related revenues from port terminal railroad operations and industrial switching (where the Company operates trains on a contract basis in facilities it does not own), as well as demurrage, storage, car hire, trucking haulage services, track access rights, transloading, crewing services, traction service (or hook and pull service that requires the Company to provide locomotives and drivers to move a customer's train between specified origin and destination points), and other ancillary revenues related to the movement of freight. Freight-related revenues are recognized as services are performed or as contractual obligations are fulfilled.

The Company generates all other revenues from third-party railcar and locomotive repairs, container sales, property rentals and other ancillary revenues not directly related to the movement of freight. All other revenues are recognized as services are performed or as contractual obligations are fulfilled.

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. The Company’s contracts may have a single performance obligation or multiple performance obligations. Contracts with multiple obligations are evaluated to define the specific performance obligations to the customer. The Company typically allocates the standalone selling price adjusted for any applicable variable consideration to each performance obligation to determine the transaction price.

For interline traffic, one railroad typically invoices a customer on behalf of all railroads participating in the route. The invoicing railroad then pays the other railroads their portion of the total amount invoiced on a monthly basis. When the Company is the invoicing railroad, it is exposed to customer credit risk for the total amount invoiced and is

required to pay the other railroads participating in the route even if the Company is not paid by the customer. The Company records revenue related to interline traffic that involves the services of another party or railroad on a net basis. The portion of the gross amount billed to customers that is remitted by the Company to another party is not reflected as revenue.

The timing of revenue recognition, billings and cash collections result in trade accounts receivable, contract assets and contract liabilities. The Company’s contract assets and liabilities are typically short-term in nature, with terms settled within a 12-month period. The Company had no material contract assets or contract liabilities recorded on the consolidated balance sheet as of September 30, 2018.

Disaggregation of Revenue

The Company disaggregates its operating revenues into the following three categories: freight revenues, freight-related revenues and all other revenues. The Company further disaggregates its freight revenues into 14 commodity groups. Refer to Note 15, Segment Information, for the disaggregation of the Company's operating revenues by reportable segment for the three and nine months ended September 30, 2018 and 2017.

5. ACCOUNTS RECEIVABLE:

Accounts receivable consisted of the following as of September 30, 2018 and December 31, 2017 (dollars in thousands):

	September 30, 2018	December 31, 2017
Accounts receivable – trade	$ 423,880	$ 401,723
Accounts receivable – grants from outside parties	14,610	17,734
Accounts receivable – insurance and other third-party claims	12,186	10,753
Total accounts receivable	450,676	430,210
Less: Allowance for doubtful accounts	(9,571)	(13,505)
Accounts receivable, net	$ 441,105	$ 416,705

Grants from Outside Parties

The Company periodically receives grants for the upgrade and construction of rail lines and the upgrade of locomotives from federal, provincial, state and local agencies in the United States and provinces in Canada in which the Company operates. These grants typically reimburse the Company for 50% to 100% of the actual cost of specific projects. In total, the Company received grant proceeds of $16.7 million and $16.0 million for the nine months ended September 30, 2018 and 2017, respectively, from such grant programs. The proceeds were presented as cash inflows from investing activities within each of the applicable periods.

None of the Company's grants represent a future liability of the Company unless the Company abandons the rehabilitated or new track structure within a specified period of time or fails to maintain the upgraded or new track to certain standards, fails to make certain minimum capital improvements or ceases use of the locomotives within the specified geographic area and time period, or fails to comply with other grant provisions in each case, as set forth in the applicable grant agreement. As the Company intends to comply with the requirements of these agreements, the Company has recorded additions to track property and locomotives and has deferred the amount of the grants. The amortization of deferred grants is a non-cash offset to depreciation expense over the useful lives of the related assets. The following table sets forth the offset to depreciation expense from the amortization of deferred grants recorded by the Company during the three and nine months ended September 30, 2018 and 2017 (dollars in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Amortization of deferred grants	$3,173	$2,978	$8,776	$9,287

Insurance and Third-Party Claims

Accounts receivable from insurance and other third-party claims as of September 30, 2018 included $6.4 million from the Company's U.K./European Operations and $5.8 million from the Company's North American Operations. The balance from the Company's U.K./European Operations resulted primarily from the Company's anticipated insurance recoveries associated with a personal injury that occurred in the U.K. in 2016. The balance from the Company's North American Operations resulted predominately from the Company's anticipated insurance recoveries associated with a bridge washout in Canada in January 2018. The Company received proceeds from insurance totaling $2.8 million and $1.4 million for the nine months ended September 30, 2018 and 2017, respectively.

Accounts receivable from insurance and other third-party claims at December 31, 2017 included $5.9 million from the Company's North American Operations, $4.3 million from the Company's U.K./European Operations and $0.6 million from the Company's Australian Operations. The balance from the Company's North American Operations resulted predominately from the Company's anticipated insurance recoveries associated with a 2015 trestle fire in the United States and derailments in Canada. The balance from the Company's U.K./European Operations resulted primarily from the Company's anticipated insurance recoveries associated with an ERS rail-related collision in Germany in 2014 that occurred prior to the Company's acquisition of Freightliner. This receivable and the associated claim liability were removed from the Company's consolidated balance sheet with the sale of ERS in June 2018. See Note 2, Changes in Operations, for additional information regarding the sale of ERS.

6. LONG-TERM DEBT:

Credit Agreement Amendment

On June 5, 2018, the Company entered into Amendment No. 3 (the Amendment) to the Credit Agreement, the Third Amended and Restated Senior Secured Syndicated Credit Facility Agreement (the Amended Credit Agreement). At closing, the credit facilities under the Amended Credit Agreement were comprised of a $1,423.0 million United States term loan, a £272.9 million (or $365.2 million at the exchange rate on June 5, 2018) U.K. term loan and a $625.0 million revolving credit facility. The revolving credit facility includes borrowing capacity for letters of credit and swingline loans. The Amendment also extended the maturity date of the Company's credit facilities to June 5, 2023.

In connection with entering into the Amendment, the Company wrote-off $2.2 million of unamortized deferred financing fees and capitalized an additional $5.3 million of new fees. Deferred financing costs are amortized as additional interest expense over the terms of the related debt using the effective-interest method for the term loan debt and the straight-line method for the revolving credit facility.

At the Company's election, at the time of entering into a specific borrowing, interest on that borrowing is calculated under a "LIBOR" or "Base Rate." LIBOR is the London Interbank Offered Rate. The applicable borrowing spread for the LIBOR Rate loans ranges from 1.00% to 2.00% depending on the Company's total leverage ratio. The applicable spread for the Base Rate loans ranges from 0.00% to 1.00% depending on the Company's total leverage ratio.

In addition to paying interest on any outstanding borrowing under the Amended Credit Agreement, the Company is required to pay a commitment fee related to the unutilized portion of the commitments under the revolving credit facility. The commitment fee ranges from 0.20% to 0.30% depending on the Company's total leverage ratio as defined in the Amended Credit Agreement.

Since entering into the Amendment, the Company has made prepayments of $120.0 million on its United States term loan and £25.0 million (or $32.8 million at the exchange rate at the time the payments were made) on its U.K. term loan, which were applied towards its future quarterly installments. As of September 30, 2018, the Company had the following amounts of term loans outstanding under the Amended Credit Agreement (amounts in thousands, except percentages):

	Local Currency	United States Dollar Equivalent	Interest Rate
United States dollar	$1,303,000	$1,303,000	3.74 %
British pound	£247,932	$323,353	2.22 %

The United States dollar-denominated and British pound-denominated term loans will amortize in quarterly installments, with the remaining principal balance payable upon maturity, as set forth below (amounts in thousands):

Quarterly Payment Date	Principal Amount of Each Quarterly Installment

United States dollar:	March 31, 2020	$4,513
	June 30, 2020 through March 31, 2023	$17,788
	Maturity date - June 5, 2023	$1,085,031
British pound:	June 30, 2020	£2,293
	September 30, 2020 through March 31, 2023	£3,412
	Maturity date - June 5, 2023	£208,111

The Company's availability to draw from the unused borrowing capacity is subject to covenant limitations as discussed below. As of September 30, 2018, the Company had the following unused borrowing capacity under its revolving credit facility (amounts in thousands):

	September 30, 2018
Total available borrowing capacity	$ 625,000
Outstanding revolving loans	$ 6,304
Outstanding letter of credit guarantees	$ 2,086
Unused borrowing capacity	$ 616,610

As of September 30, 2018, the Company had the following outstanding revolving loans under its revolving credit facility (amounts in thousands, except percentages):

	Local Currency	United States Dollar Equivalent	Interest Rate
United States dollar (swingline loan)	$ 5,000	$ 5,000	5.75 %
British pound (swingline loan)	£ 1,000	$ 1,304	2.20 %

Under the Amended Credit Agreement, the Company is required to comply with specified maximum senior secured leverage ratios. The maximum senior secured leverage ratio is set at 4.25 to 1.00 through June 30, 2019, and then, except as described below, decreases to 4.00 to 1.00 for all periods thereafter, subject, if applicable, to netting of certain cash and cash equivalents of the Company. Following acquisitions by the Company in excess of $500 million, subject to certain limitations, the senior secured leverage ratio will be set at a level of 4.50 to 1.00 for the four fiscal quarters immediately following the date of such applicable acquisition.

In addition, the Amended Credit Agreement contains a maximum total leverage ratio and a minimum interest coverage ratio. The maximum total leverage ratio is 4.50 to 1.00 and the minimum interest coverage ratio is 3.50 to 1.00 for the term of the Amended Credit Agreement.

The Amendment permits the Company to repurchase an unlimited amount of shares of the Company's Class A Common Stock if the Company's total leverage ratio after giving effect to such repurchases on a pro forma basis would be less than 3.25 to 1.00, subject to certain other restrictions and limitations. If the Company's total leverage ratio after giving effect to such repurchases on a pro forma basis would exceed 3.25 to 1.00, the Company may, subject to certain limitations, repurchase shares of the Company's Class A Common Stock with a value of up to the sum of $500 million and the amount remaining under the Company's current share repurchase program, which was $29.5 million as of September 30, 2018, if the Company maintains at least $100 million of liquidity. See Note 3, Earnings Per Common Share, for additional information regarding the Company's common share repurchases.

As of September 30, 2018, the Company was in compliance with the covenants under the Amended Credit Agreement.

7. U.K. OPERATIONS OPTIMIZATION:

In 2018, the Company reorganized its U.K. business into three service platforms: Rail (Intermodal and Heavy Haul), Road (former Freightliner and Pentalver road operations) and Terminals (former Freightliner and Pentalver terminals), with a single combined commercial organization responsible for selling all three services. The Company also announced a program to restructure and further optimize its operations in the U.K. that began in May 2018 and is intended to be completed by early 2019. The program includes the rationalization of the locomotive and railcar fleet, management restructuring (following the U.K. consultative process), and technology investments to upgrade systems to enhance productivity and service quality. Restructuring and related expenses associated with the optimization are expected to be approximately $52 million (assuming the adjustment described in footnote (a) below does not occur and an exchange rate of $1.30 for one British pound) and are comprised of the following, including the current estimate of the timing of the related charges, which is subject to change (dollars in thousands):

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018	Estimated Total Restructuring and Related Costs
Rationalization of locomotive and railcar fleet[(a)]	$ 379	$ 6,317	$ 28,000
Management restructuring[(b)]	1,610	3,739	10,000
Productivity and automation investments	1,502	2,790	14,000
Total	$ 3,491	$ 12,846	$ 52,000

(a) The emergence of new commercial opportunities may result in less restructuring and related expense.
(b) Subject to requisite U.K. consultative process.

Restructuring and related activity for the U.K. Operations Optimization program for the nine months ended September 30, 2018 was as follows (dollars in thousands):

	Rationalization of Locomotive and Railcar Fleet	Management Restructuring	Productivity and Automation Investments	Total
Restructuring and related liability as of December 31, 2017	$ —	$ —	$ —	$—
Restructuring and related costs incurred	6,317	3,739	2,790	12,846
Cash payments	(797)	(2,405)	(2,567)	(5,769)
Non-cash settlements	(897)	—	(223)	(1,120)
Restructuring and related liability as of September 30, 2018	$ 4,623	$ 1,334	$ —	$5,957

8. DERIVATIVE FINANCIAL INSTRUMENTS:

On January 1, 2018, the Company adopted ASU 2017-12, Derivatives and Hedging (Topic 815), Targeted Improvements to Accounting for Hedging Activities, which expands and refines hedge accounting for both nonfinancial and financial risk components and aligns the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements. The amendment also includes certain improvements to ease the application of current guidance related to the assessment of hedge effectiveness. The adoption of this guidance amended the Company's accounting for cross-currency swaps whereby interest expense accruals previously presented in an interest expense line item are presented as a gain/loss on currency conversion within other income/(loss), net in the non-operating section of the consolidated statement of operations. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

The Company actively monitors its exposure to interest rate and foreign currency exchange rate risks and uses derivative financial instruments to manage the impact of these risks. The Company uses derivatives only for purposes of managing risk associated with underlying exposures. The Company does not trade or use derivative instruments with the objective of earning financial gains on the interest rate or exchange rate fluctuations alone, nor does the

Company use derivative instruments where it does not have underlying exposures. Complex instruments involving leverage or multipliers are not used. The Company manages its hedging position and monitors the credit ratings of counterparties and does not anticipate losses due to counterparty nonperformance. Management believes its use of derivative instruments to manage risk is in the Company's best interest. However, the Company's use of derivative financial instruments may result in short-term gains or losses and increased earnings volatility. The Company's instruments are recorded in the consolidated balance sheets at fair value in prepaid expenses and other, other assets, accrued expenses or other long-term liabilities.

The Company may designate derivatives as a hedge of a forecasted transaction or a hedge of the variability of the cash flows to be received or paid in the future related to a recognized asset or liability (cash flow hedge). The portion of the changes in the fair value of the derivative used as a cash flow hedge that is offset by changes in the expected cash flows related to a recognized asset or liability is recorded in other comprehensive income/(loss). As the hedged item is realized, the gain or loss included in accumulated other comprehensive income/(loss) is reported in the consolidated statements of operations on the same line item as the hedged item.

The Company matches the hedge instrument to the underlying hedged item (assets, liabilities, firm commitments or forecasted transactions). At inception of the hedge and at least quarterly thereafter, the Company assesses whether the derivatives used to hedge transactions are highly effective in offsetting changes in either the fair value or cash flows of the hedged item. When it is determined that a derivative ceases to be a highly effective hedge, the Company discontinues hedge accounting, and any gains or losses on the derivative instrument thereafter are recognized in earnings during the period in which it no longer qualifies for hedge accounting.

From time to time, the Company may enter into certain derivative instruments that may not be designated as hedges for accounting purposes. For example, to mitigate currency exposures related to intercompany debt, cross-currency swap contracts may be entered into for periods consistent with the underlying debt. The Company believes such instruments are closely correlated with the underlying exposure, thus reducing the associated risk. The gains or losses from the changes in the fair value of derivative instruments not accounted for using hedge accounting are recognized in current period earnings within other income/(loss), net. Derivative instruments entered into in conjunction with contemplated acquisitions also do not qualify as hedges for accounting purposes.

Interest Rate Risk Management

The Company uses interest rate swap agreements to manage its exposure to the changes in interest rates on the Company's variable rate debt. These swap agreements are recorded in the consolidated balance sheets at fair value. Changes in the fair value of the swap agreements are recorded in net income or other comprehensive income/(loss), based on whether the agreements are designated as part of a hedge transaction and whether the agreements are effective in offsetting the change in the value of the future interest payments attributable to the underlying portion of the Company's variable rate debt. Interest payments accrued each reporting period for these interest rate swaps are recognized in interest expense. The Company formally documents its hedge relationships, including identifying the hedge instruments and hedged items, as well as its risk management objectives and strategies for entering into the hedge transaction.

The following table summarizes the terms of the Company's outstanding interest rate swap agreements entered into to manage the Company's exposure to changes in interest rates on its variable rate debt (amounts in thousands):

		Notional Amount			
Effective Date	Expiration Date	Date	Amount	Pay Fixed Rate	Receive Variable Rate
12/1/2016	12/1/2021	12/1/2021	A$372,600	2.44%	AUD-BBR
12/1/2016	12/1/2021	12/1/2021	A$110,746	2.44%	AUD-BBR
12/1/2016	12/1/2021	12/1/2021	A$34,155	2.44%	AUD-BBR
8/31/2018	8/31/2021	8/31/2021	$ 100,000	2.70%	1-month LIBOR
8/31/2018	8/31/2021	8/31/2021	$ 100,000	2.71%	1-month LIBOR
8/31/2018	8/31/2048	8/31/2048	$ 100,000	2.84%	1-month LIBOR
8/31/2018	8/31/2048	8/31/2048	$ 100,000	2.87%	1-month LIBOR
8/31/2018	8/31/2048	8/31/2048	$ 100,000	2.84%	1-month LIBOR

During the three months ended September 30, 2018, the Company entered into multiple 30-year interest rate swap agreements to manage the exposure to changes in interest rates on the Company's variable rate debt. The swaps have a mandatory termination feature on August 31, 2023. These 30-year swaps qualify for hedge accounting. In addition, it remains probable that the Company will either issue $300.0 million of fixed-rate debt or have $300.0 million of variable-rate debt under the Company's commercial banking lines throughout the term of the outstanding swap agreements. The Company expects to amortize any gains or losses on the settlements over the life of the respective

swap.

The following table summarizes the Company's interest rate swap agreements that were settled during the nine months ended September 30, 2018 (dollars in thousands):

Effective Date	Settlement Date	Notional Amount Date	Amount	Pay Fixed Rate	Receive Variable Rate
9/30/2016	8/15/2018	9/30/2026	$100,000	2.76%	1-month LIBOR
9/30/2016	8/15/2018	9/30/2026	$100,000	2.74%	1-month LIBOR
9/30/2016	8/15/2018	9/30/2026	$100,000	2.73%	1-month LIBOR

The fair values of the Company's interest rate swap agreements were estimated based on Level 2 inputs. During the three and nine months ended September 30, 2018, $0.5 million and $1.2 million, respectively, of existing net losses were realized and recorded as interest expense in the consolidated statements of operations. During the three and nine months ended September 30, 2017, $0.6 million and $1.5 million, respectively, of existing net losses were realized and recorded as interest expense in the consolidated statements of operations. Based on the Company's fair value assumptions as of September 30, 2018, it expects to realize $0.2 million of existing net losses that are reported in AOCL into earnings within the next 12 months. See Note 13, Accumulated Other Comprehensive Loss, for additional information regarding the Company's cash flow hedges.

Foreign Currency Exchange Rate Risk

As of September 30, 2018, the Company's foreign subsidiaries had $1.0 billion of third-party debt, including capital leases, denominated in the local currencies in which the Company's foreign subsidiaries operate, including the Australian dollar, the British pound, the Canadian dollar and the Euro. The debt service obligations associated with this foreign currency debt are generally funded directly from those foreign operations. As a result, foreign currency risk related to this portion of the Company's debt service payments is limited. However, in the event the foreign currency debt service is not paid by the Company's foreign subsidiaries and is paid by its United States subsidiaries, the Company may face exchange rate risk if the Australian dollar, the British pound, the Canadian dollar or the Euro were to appreciate relative to the United States dollar and require higher United States dollar equivalent cash.

The Company is also exposed to foreign currency exchange rate risk, including non-functional currency intercompany debt, typically associated with acquisitions and any timing difference between announcement and closing of an acquisition of a foreign business. To mitigate currency exposures of non-United States dollar-denominated acquisitions, the Company may enter into foreign currency forward purchase contracts. To mitigate currency exposures related to non-functional currency denominated intercompany debt, cross-currency swaps or foreign currency forward contracts may be entered into for periods consistent with the underlying debt. To mitigate currency exposures related to significant asset purchases in non-functional denominated currencies, foreign currency forward contracts may be entered into for periods consistent with the anticipated future outflow of cash. In determining the fair value of the derivative contract, the significant inputs to valuation models are quoted market prices of similar instruments in active markets. However, cross-currency swap contracts and foreign currency forward contracts used to mitigate exposures on foreign currency intercompany debt may not qualify for hedge accounting. In cases where the cross-currency swap contracts and foreign currency forward contracts do not qualify for hedge accounting, the Company believes that such instruments are closely correlated with the underlying exposure, thus reducing the associated risk. The gains or losses from changes in the fair value of derivative instruments that do not qualify for hedge accounting are recognized in current period earnings within other income/(loss), net.

The following table summarizes the Company's outstanding foreign currency forward contracts associated with assets to be purchased by GWA in United States dollars within the next six months (dollars in thousands):

Effective date	Settlement Date	Notional Amount	Exchange Rate (AUD to USD)
5/2/2018	11/5/2018	$4,315	0.75
5/2/2018	12/21/2018	$5,753	0.75

The following table summarizes the Company's foreign currency forward contract that was settled during the nine months ended September 30, 2018 (dollars in thousands):

Effective date	Settlement Date	Notional Amount

			Exchange Rate (AUD to USD)
4/18/2018	7/5/2018	$5,379	0.78

The fair values of the Company's foreign currency forward contracts were estimated based on Level 2 inputs, as further described in Note 9, Fair Value of Financial Instruments. During the three and nine months ended September 30, 2018, $0.4 million of net gains were recorded as other income/(loss), net in the consolidated statements of operations. Based on the Company's fair value assumptions as of September 30, 2018, it expects to realize $0.4 million of existing net gains that are reported in AOCL into earnings within the next 12 months. See Note 13, Accumulated Other Comprehensive Loss, for additional information regarding the Company's cash flow hedges.

On March 25, 2015, the Company closed on the Freightliner acquisition and paid cash consideration of £492.1 million (or $733.0 million at the exchange rate on March 25, 2015). The Company financed the acquisition through a combination of available cash and borrowings under the Company's Credit Agreement. A portion of the funds were transferred from the United States to the U.K. through an intercompany loan with a notional amount of £120.0 million (or $181.0 million at the exchange rate on the effective date of the loan) and accrued interest as of September 30, 2018 of £28.1 million (or $36.7 million at the exchange rate on September 30, 2018), each of which are expected to remain until maturity of the loan. To mitigate the foreign currency exchange rate risk related to this non-functional currency intercompany loan and the related interest, the Company entered into British pound forward contracts, which are accounted for as cash flow hedges.

The fair values of the Company's British pound forward contracts were estimated based on Level 2 inputs. During the three and nine months ended September 30, 2018, $0.2 million and $0.5 million, respectively, of net gains were recorded as interest income in the consolidated statements of operations. During the three and nine months ended September 30, 2017, $0.1 million and $0.4 million, respectively, of net gains were recorded as interest income in the consolidated statements of operations. Based on the Company's fair value assumptions as of September 30, 2018, it expects to realize $0.8 million of existing net gains that are reported in AOCL into earnings within the next 12 months. See Note 13, Accumulated Other Comprehensive Loss, for additional information regarding the Company's cash flow hedges.

The following table summarizes the Company's outstanding British pound forward contracts (British pounds in thousands):

Effective Date	Settlement Date	Notional Amount	Exchange Rate (GBP to USD)
3/25/2015	3/31/2020	£60,000	1.51
3/25/2015	3/31/2020	£60,000	1.50
6/30/2015	3/31/2020	£2,035	1.57
9/30/2015	3/31/2020	£1,846	1.51
12/31/2015	3/31/2020	£1,873	1.48
3/31/2016	3/31/2020	£1,881	1.45
6/30/2016	3/31/2020	£1,909	1.35
9/30/2016	3/31/2020	£1,959	1.33
12/30/2016	3/31/2020	£1,989	1.28
3/31/2017	3/31/2020	£1,975	1.30
6/30/2017	3/31/2020	£2,026	1.34
10/2/2017	3/31/2020	£2,079	1.36
12/29/2017	3/31/2020	£2,111	1.39
3/29/2018	3/31/2020	£2,096	1.44
6/29/2018	3/31/2020	£2,151	1.36
9/28/2018	3/31/2020	£2,207	1.34

On December 1, 2016, GWAHLP and the Company's subsidiary, GWI Holding B.V. (GWBV), entered into an A$248.9 million non-recourse subordinated partner loan agreement (GRail Intercompany Loan), which is eliminated in consolidation. GWAHLP used the proceeds from this loan to fund a portion of the acquisition of GRail. To mitigate the foreign currency exchange rate risk related to the non-functional currency intercompany loan, the Company

entered into two Euro/Australian dollar floating-to-floating cross-currency swap agreements (the Swaps) on December 22, 2016, which effectively convert the A$248.9 million intercompany loan receivable in the Netherlands into a €171.7 million loan receivable. These agreements do not qualify as hedges for accounting purposes and, accordingly, mark-to-market changes in the fair value of the Swaps relative to the underlying GRail Intercompany Loan will be recorded over the life of the agreements, which expire on June 30, 2019.

The first swap requires the Company to pay Australian dollar BBR plus 4.50% based on a notional amount of A$123.9 million and allows the Company to receive EURIBOR plus 2.68% based on a notional amount of €85.5 million on a semi-annual basis. BBR is the Bankers Buyers Rate and EURIBOR is the Euro Interbank Offered Rate, which the Company believes are generally considered equivalents to LIBOR. The second swap requires the Company to pay Australian dollar BBR plus 4.50% based on a notional amount of A$125.0 million and allows the Company to receive EURIBOR plus 2.90% based on a notional amount of €86.3 million on a semi-annual basis. The Swaps require semi-annual net settlement payments. During the three and nine months ended September 30, 2018, $2.4 million and $4.9 million of net expense, respectively, was realized within other income/(loss), net in the consolidated statement of operations as a result of the mark-to-market impact of the GRail Intercompany Loan compared to the mark-to-market of the Swaps.

During the three and nine months ended September 30, 2017, $0.8 million and $4.5 million, respectively, of net expense was realized within other income/(loss), net in the consolidated statements of operations as a result of the mark-to-market impact of the GRail Intercompany Loan compared to the mark-to-market of the Swaps. Over the life of the Swaps, the Company expects the cumulative impact of net gains and losses from the mark-to-market of the GRail Intercompany Loan and Swaps to be approximately zero.

The following table summarizes the fair value of the Company's derivative instruments recorded in the consolidated balance sheets as of September 30, 2018 and December 31, 2017 (dollars in thousands):

	Balance Sheet Location	Fair Value September 30, 2018	Fair Value December 31, 2017
Asset Derivatives:			
Derivatives designated as hedges:			
Interest rate swap agreements	Prepaid expenses and other	$527	$ —
Foreign currency forward contracts	Prepaid expenses and other	383	—
Interest rate swap agreements	Other assets	6,596	—
British pound forward contracts	Other assets	20,803	13,657
Total derivatives designated as hedges		$28,309	$ 13,657
Derivatives not designated as hedges:			
Cross-currency swap contract	Prepaid expenses and other	$16,648	$ 5,775
Cross-currency swap contract	Other assets	—	2,887
Total derivatives not designated as hedges		$16,648	$ 8,662
Liability Derivatives:			
Derivatives designated as hedges:			
Interest rate swap agreements	Accrued expenses	$755	$ 1,972
Interest rate swap agreements	Other long-term liabilities	1,706	12,410
British pound forward contracts	Other long-term liabilities	246	829
Total derivatives designated as hedges		$2,707	$ 15,211

The following table shows the effect of the Company's derivative instruments designated as cash flow hedges for the three and nine months ended September 30, 2018 and 2017 in other comprehensive income (OCI) (dollars in thousands):

	Total Cash Flow Hedge OCI Activity, Net of Tax			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Derivatives Designated as Cash Flow Hedges:				
Effective portion of net changes in fair value recognized in OCI, net of tax:				
Interest rate swap agreements	$4,816	$388	$14,396	$(1,382)
Foreign currency forward contracts	(13)	—	275	—
British pound forward contracts, net [(a)]	350	348	85	2,020
	$5,153	$736	$14,756	$638

(a) The three and nine months ended September 30, 2018 represented a net gain of $2.0 million and $5.5 million, respectively, for the mark-to-market of the British pound forward contracts, offset by a net loss of $1.7 million and $5.4 million, respectively, for the mark-to-market of the U.K. intercompany loan. The three and nine months ended September 30, 2017 represented a net gain of $3.2 million and $8.6 million, respectively, for the mark-to-market of the U.K. intercompany loan, offset by a net loss of $2.8 million and $6.6 million, respectively, for the mark-to-market of the British pound forward contracts.

The following table shows the effect of the Company's derivative instruments not designated as hedges for the three and nine months ended September 30, 2018 and 2017 in the consolidated statements of operations (dollars in thousands):

	Location of Amount Recognized in Earnings	Amount Recognized in Earnings			
		Three Months Ended September 30,		Nine Months Ended September 30,	
		2018	2017	2018	2017
Derivative Instruments Not Designated as Hedges:					
Cross-currency swap agreements	Interest expense	$—	$(1,887)	$—	$(1,887)
Cross-currency swap agreements, net [(a)]	Other income/(loss), net	(2,410)	(842)	(4,900)	(4,510)
		$(2,410)	$(2,729)	$(4,900)	$(6,397)

(a) The three months ended September 30, 2018 represented a net gain of $0.6 million for the mark-to-market of the Swaps, offset by a net loss of $3.0 million for the mark-to-market of the GRail Intercompany Loan. The nine months ended September 30, 2018 represented a net gain of $3.2 million for the mark-to-market of the Swaps, partially offset by a net loss of $8.1 million for the mark-to-market of the GRail Intercompany Loan. The three and nine months ended September 30, 2017 represented a net gain of $1.7 million and $2.0 million, respectively, for the mark-to-market of the Swaps, offset by a net loss of $2.5 million and $6.5 million, respectively, for the mark-to-market of the GRail Intercompany Loan.

9. FAIR VALUE OF FINANCIAL INSTRUMENTS:

The Company applies the following three-level hierarchy of valuation inputs for measuring fair value:

- Level 1 - Quoted prices for identical assets or liabilities in active markets that the Company has the ability to access at the measurement date.
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Level 2 - Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; and model-derived valuations in which all significant inputs are observable market data.

- Level 3 - Valuations derived from valuation techniques in which one or more significant inputs are unobservable.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments held by the Company:

Financial Instruments Carried at Fair Value: Derivative instruments are recorded on the consolidated balance sheets as either assets or liabilities measured at fair value. During the reporting period, the Company's derivative financial instruments consisted of interest rate swap agreements, foreign currency forward contracts and cross-currency swap agreements. The Company estimated the fair value of its interest rate swap agreements based on Level 2 valuation inputs, including fixed interest rates, LIBOR and BBR implied forward interest rates and the remaining time to maturity. The Company estimated the fair value of its British pound forward contracts based on Level 2 valuation inputs, including LIBOR implied forward interest rates, British pound LIBOR implied forward interest rates and the remaining time to maturity. The Company estimated the fair value of its foreign currency forward contracts based on Level 2 valuation inputs, including BBR implied forward interest rates and the remaining time to maturity. The Company estimated the fair value of its cross-currency swap agreements based on Level 2 valuation inputs, including EURIBOR implied forward interest rates, BBR implied forward interest rates and the remaining time to maturity.

The Company's recurring fair value measurements using significant unobservable inputs (Level 3) relate to the Company's deferred consideration from the HOG acquisition in 2017. The fair values of the deferred consideration liabilities were estimated by discounting, to present value, contingent payments expected to be made.

Financial Instruments Carried at Historical Cost: Since the Company's long-term debt is not actively traded, fair value was estimated using a discounted cash flow analysis based on Level 2 valuation inputs, including borrowing rates the Company believes are currently available to it for loans with similar terms and maturities.

The following table presents the Company's financial instruments carried at fair value using Level 2 inputs as of September 30, 2018 and December 31, 2017 (dollars in thousands):

	September 30, 2018	December 31, 2017
Financial instruments carried at fair value using Level 2 inputs:		
Financial assets carried at fair value:		
Interest rate swap agreements	$ 7,123	$ —
Foreign currency forward contracts	383	—
British pound forward contracts	20,803	13,657
Cross-currency swap contracts	16,648	8,662
Total financial assets carried at fair value	$ 44,957	$ 22,319
Financial liabilities carried at fair value:		
Interest rate swap agreements	$ 2,461	$ 14,382
British pound forward contracts	246	829
Total financial liabilities carried at fair value	$ 2,707	$ 15,211

The following table presents the Company's financial instrument carried at fair value using Level 3 inputs as of September 30, 2018 and December 31, 2017 (dollars in thousands):

	September 30, 2018	December 31, 2017
Financial instrument carried at fair value using Level 3 inputs:		
Financial liabilities carried at fair value:		
Accrued deferred consideration – HOG	$ 6,368	$ 5,974

At the date of acquisition of HOG in 2017, the contingent liability represented the fair value of the deferred consideration payable to the sellers upon satisfaction of certain conditions, which the Company expects to be paid in 2021. See Note 2, Changes in Operations, for additional information regarding HOG.

As of September 30, 2017, the Company also had a $37.2 million deferred consideration liability associated with the 2015 acquisition of Freightliner. At the date of acquisition of Freightliner, the contingent liability represented the aggregate fair value of the shares transferred to the Company by certain former management shareholders of Freightliner (Management Shareholders) in exchange for the right to receive cash consideration for the representative economic interest of approximately 6% in Freightliner in the future (deferred consideration).

The Company's contingent liabilities have been adjusted each period since the acquisition dates to represent the fair value of the deferred consideration as of each balance sheet date. To do so, the Company recalculated the estimated fair value of the Freightliner deferred consideration in each reporting period by using a contractual formula designed to estimate the economic value of the Management Shareholders' retained interest in a manner consistent with that used to derive the Freightliner acquisition price per share on the acquisition date. The Company bought out the Freightliner deferred consideration in November 2017. In addition, the Company recalculates the HOG's deferred consideration based on the contractual formula as defined in the stock purchase agreement. These calculations effectively represent the present value of the expected payment to be made upon settlement of the deferred consideration. Accordingly, such recalculations reflect both the impact of the time value of money and the impact of changes in the expected future performance of the acquired business, as applicable. The Company expects to recognize future changes in HOG's contingent liability for the estimated fair value of the deferred consideration through other expenses within the Company's consolidated statement of operations. This future change in the estimated fair value of the deferred consideration is not expected to be deductible for tax purposes.

The following table presents the amounts recognized, through other expenses, net within the Company's consolidated statements of operations during the three and nine months ended September 30, 2018 and 2017, as a result of the change in the estimated fair value of the deferred consideration, which primarily represented the time value of money (dollars in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Freightliner	$—	$859	$—	$2,405
HOG	$137			